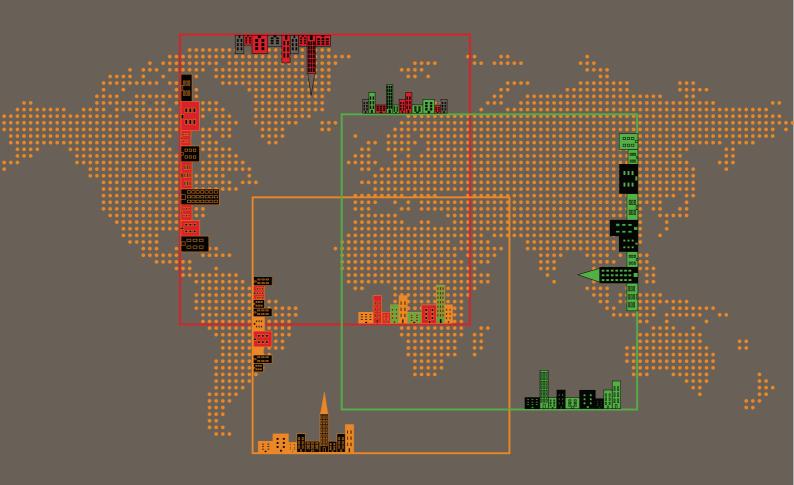


# **ECONOMIC** and other benefits of the **ENTREPRENEURS' COOPERATIVE** as a specific form of **ENTERPRISE** cluster

Nicole Göler von Ravensburg



#### **ILO COOP**

The International Labour Organization (ILO) is the sole agency of the United Nations that has a specific mandate for cooperative development. Accordingly, the ILO has a programme devoted to cooperatives and the 2002 Promotion of Cooperatives Recommendation (No. 193) represents the unique international standard dedicated to this purpose.

Based on this Recommendation, the work of the ILO Cooperative Programme (EMP/COOP) supports cooperative policy and law reform, capacity building for cooperative stakeholders, promoting cooperatives and their impacts on employment and increasing public awareness through advocacy and sensitization to cooperative values and principles.

A cooperative is a particular type of enterprise defined to be "an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise". By definition, cooperatives have a distinct and particular status when compared to other types of enterprise. What makes cooperatives distinct is their overarching objective to meet their members' common economic, social and cultural interests. According to their values and principles, cooperatives can be distinguished by their democratic and egalitarian organizational functioning based on the "one member, one vote" rule, as well as by a fair surplus allotment mode.

Cooperatives are enterprises which can be found in both industrialised and developing countries. Ac cording to the International Cooperative Alliance (ICA), cooperatives represent 1 billion individuals and provide at least 100 million jobs worldwide; that is 20 per cent more than multinational companies. Furthermore, it is estimated that the livelihood of nearly 3 billion people, has been made secure by cooperative enterprises. In terms of turnover, the world's 300 largest cooperatives organizations produced an income of US\$ 1.6 trillion during the 2009-10 financial period.



Cooperative Facility for Africa (COOPAFRICA) is a regional technical cooperation programme of the International Labour Organization (ILO) in support of cooperative development. It promotes favourable policy and legal environments, strong vertical structures (such as cooperative unions and federations) and improved cooperative governance, efficiency and performance. The programme covers nine countries in East and Southern Africa (Botswana, Ethiopia, Kenya, Lesotho, Rwanda, Swaziland, Tanzania mainland and Isles, Uganda and Zambia) from the ILO Office in Tanzania with technical support from the ILO Cooperative

Programme (EMP/COOP) in Geneva. It was launched in October 2007 with core funding from the UK Department for International Development (DFID). COOPAFRICA is a partnership initiative involving a range of international and national organizations.



COPAC is a committee made up of the United Nations, the Food Agriculture Organization, International Labour Organization, and the International Cooperative Alliance. Members work together on equal terms to promote and coordinate sustainable cooperative development by promoting and raising awareness on cooperatives, holding policy dialogues and advocating policies that enable cooperative success, working together on technical cooperation activities and sharing knowledge and information.



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## **Foreword**

On a worldwide scale small industrial producers and service providers, professionals and local public enterprises create more employment than large international firms. They also offer employment opportunities to the most vulnerable in society, including women, youth and the poor. However, globalization and liberalization of markets, new financing patterns, increasing customer expectations and the revolution in information technology have, for some time now, put them under considerable pressure.

So called "global players" find it easier than ever to participate local markets for provision of private and public goods. They use decentralized holding structures, develop systems with which to address customers individually, and redirect risk to their medium sized suppliers. In doing so, large companies successfully emulate comparative advantages that were unique to micro, small and medium size enterprises and other local providers. At the same time international corporations try to extend their advantages of scale through developing strategic alliances and negotiating mergers and acquisitions. Small producers and service providers face increasing cost competition and pressures on their profit margins, as well as ever shorter product life cycles. This results in growing demands for and expenditure on research and development. The most promising answer to this lies in sustainable diversification and/or differentiation. In other words, by significantly improving their entrepreneurial concept.

To achieve this, SMEs, professionals and public enterprises alike have to improve their core competences through continual efforts at innovation and by systematically identifying and exploiting their potential for cooperation. Both strategic approaches must be looked at together. The way in which enterprises cooperate and develop clusters

ought to reconcile the external factors forcing enterprises to cooperate and focus on the potential benefits for the individual enterprise.

Experience shows that in many instances where entrepreneurs' cooperatives have been established, they have supported the development of SMEs and informal sector businesses, created sustainable employment and improved the social standing of the members and their families. Entrepreneurs' cooperatives have thus supported the implementation of the ILO's Job Creation in Small and Medium-Sized Enterprises Recommendation, 1998 (No. 183). For women's groups as well as women and youth entrepreneurs, Entrepreneurs' cooperatives offer a means of helping to sustain and develop their business activities, while enhancing their voice and status within their communities. Entrepreneurs' cooperatives thus support the efforts of the ILO in its decent work mandate, and most importantly support the ILO's mandate for cooperative development outlined in the Promotion of Cooperatives Recommendation, 2002 (No. 193). Entrepreneurs' cooperatives are also an expression of the ILO's Freedom of Association and Protection of the Right to Organise Convention, 1948 (No. 87), which entails the right of employers and workers to freely establish organizations of their own choosing, in order to promote protection of their occupational and industrial interests.

Yet, the model of the entrepreneurs' cooperative has not spread equally throughout the world. Entrepreneurs' cooperatives have proven to be highly effective over the course of nearly 150 years in several Western European countries, with professionals and public bodies there and in North America increasingly making use of them in recent times. However, to date, entrepreneurs' cooperatives have hardly diffused into Eastern European, African, Asian or Latin American markets.

It was for these reasons that EMP/COOP, the Cooperative Programme of the International Labour Office, commissioned a comprehensive academic study on entrepreneurs' cooperatives. This book documents examples of economically viable entrepreneurs' cooperatives around

the world that provide stabilization, or even increases in income and employment, to a great number of households, in order to learn how the model could be rendered useful elsewhere. At the same time, the study constitutes the ILO's contribution to the work of the interagency Committee for the Promotion and Advancement of Cooperatives (COPAC).

This book contains the results of this study. It describes how entrepreneurs' cooperatives are frequently started and goes on to characterize the nature of their organization. It outlines their economic, social and other benefits and, drawing on theoretical and international empirical research, analyzes the reasons for their being used to such varying degrees in different parts of the world. The comparative approach shows that this is partly due to legal and/or administrative barriers, which in many instances prevent juridical entities from joining a primary cooperative. Further, the model was and still is unknown, even where it has been possible for legal entities to use it. This is largely attributable to the misconceptions that people have of primary cooperatives, which discourages them from forming such associations. Therefore, an in depth examination of how supportive legal and policy frameworks could be fashioned, and what promotional measures can be introduced.

The task entrusted to the author was not an easy one, as data was not readily available. There is a virtual void of descriptions of entrepreneurs' cooperatives in some parts of the world, while there are many formal and informal SME-organizations that show distinctive cooperative features. Whether this is a direct result of deterring cooperative policies or mere lack of knowledge, this data deficiency is likely to be one of the reasons why there is so little awareness of the potential of this form of business cluster. This is despite indications that collective socio-economic undertakings play an important role in the economy.

We are convinced that this study will significantly contribute to cooperative development and enterprise development throughout the world. It gives considerable insights into the workings and application of the entrepreneurs' cooperative model. Systematically applied, its recommendations form a sound basis for the development of enabling legal and policy frameworks in any country. The International Labour Office and COPAC are grateful to the author for having taken up this challenge and having produced a wealth of information, as well as the ingredients for action.

We would also like to thank Michael Henriques, the former Director of the Job Creation and Enterprise Development Department for his encouragement and for making the necessary funds available.

We thank Cooperative Facility for Africa, a regional technical cooperation programme of the ILO and its team, composed of Philippe Vanhuynegem, Elizabeth Mwakalinga, Eva Majurin and Emma Allen, tirelessly read and reread the draft, as did Maria-Elena Chavez Hertig, Coordinator of COPAC. We wish to thank all of them for their valuable contributions. Finally, the EMP/COOP team participated in the various phases of the elaboration of the study. We are grateful to them as well.

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### List of abbreviations

AC Acceded Country

ACME Association of European Cooperative and Mutual

Insurers

BA Business Association

BMO Business Membership Organi-zation CBA Cooperative Business Association

C.C.A.C.E. Co-ordinating Committee of European Cooperative

Associations

DC Developing Country

DGRV Deutscher Genossenschafts- und Raiffeisenverband

e.g. exempli gratia

EC Commission of the European Communities

EC Entrepreneurs' Cooperative

ed. Editor eds. Editors etc. et cetera

EU European Union

GEBC Groupement Européen des Banques Coopératives

i.e. id est

IC Industrialized Country

ICA International Co-operative Alliance

IFAD The International Fund for Agricultural Development

ILO International Labour Office

Ltd. Limited

MTO Mutual Trading Organization NGO Non-Government Organization

NPO Non-Profit Organization

p. Pagepp. Pages

PRSP Poverty Reduction Strategy Paper

R&D Research and Development

SHO Self-Help Organization TC Countries in Transition

USDA United States Department of Agriculture

WTO World Trade Organization

## **Acknowledgements**

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## Notes on the author

The author is a professor at Frankfurt University of Applied Sciences, specializing in cooperative research in national, European and development contexts. Her PhD concentrated on the integration of cooperatives into main stream economics in South Africa, dealing with all aspects of cooperative development. This included legal and policy framework, institutional arrangements for promotion, tax and management issues and the need to accommodate varied business aims and norms. She has spent many years consulting in cooperative development in Africa.

## **Executive Summary**

Entrepreneurs' cooperatives have helped small and mediumsized enterprises (SMEs) in many countries to become and remain competitive. Although this form of business clustering is not wide spread, there are signs that its development and entrepreneurship effects are gradually being considered.

This study analyses the set up and the economic, social and employment benefits of entrepreneurs' cooperatives as well as the reasons why their use has not spread spread. Based on theoretical and empirical research, as well as the documentation of 69 Internet appearances by entrepreneurs' cooperatives from all over the world, the study indicates those features which allow for replication of the model elsewhere and concludes with a number of recommendations.

While the importance of various international efforts with regard to general cooperative policy and law is being reaffirmed, five key issues seem of particular relevance to entrepreneurs' cooperatives:

- Concrete group and organizational norms can be fashioned much more flexibly and effectively for the organization's aim where modern economic policies and organizational law are either not of major importance (in informal economy for local production) or not obstructive (for formal organizations involved in local and international trade).
- Entrepreneurs' cooperatives neither need a special level of protection nor do they need any more promotion than that which other business networks, professional clusters or public service delivery syndicates can obtain.
- Entrepreneurs' cooperatives are best served by competing promotion agencies as well as market-driven environments,

- which offer room for experimentation with different organizational structures, norms and learning processes.
- International policy and legal advice efforts can help national policy and law makers to design institutional paths conducive to more entrepreneurs' cooperatives being set up.
- Where SME and informal sector promotion is to entail entrepreneurs' cooperative promotion, a national cooperative dialogue is needed to tap the resources which already exist. Such promotion should include the fashioning of an appropriate image, education and training for promoters and entrepreneurs' cooperative leaders, access to finance and capacity building for entrepreneurs' cooperatives as well as a modern concept on which to base the role of entrepreneurs' cooperative's federations and up-to-date statistics.

Through its tripartite structure (governments, employers and workers), its international partners as well as networking with national cooperative federations, unions and colleges, the ILO can play a significant role in improving the understanding of, general climate for and the support available to entrepreneurs' cooperatives. A first step in this regard could be the development of a consistent classification of entrepreneurs' cooperatives and the identification of those types with the highest employment potential.

Where the promotion of the informal economy or SMEs includes special promotion efforts for entrepreneurs' cooperatives, national or local partnerships between the ILO and its constituents are suggested. Also that carefully selected authorities and business membership organizations such as chambers of commerce, trade, crafts and industries be considered. Any assistance, however, must be based on an accurate recognition of the ability of cooperatives and their members to become sustainable. The author suggests a roster with

#### xviii Executive Summary

which start-up consultancies of any provenience can analyse the respective circumstances of entrepreneurs' cooperatives and discuss the findings with the prospective members.

The ILO and its constituents should concentrate on working with SME promotion agencies, national cooperative federations and northern cooperative movements, which also aim at creating self-sustaining cooperative systems. Joint promotion programmes thereby ought to respect that the different promotional tasks, such as trade (inputs and sales for member entrepreneurs' cooperatives), production services (packaging, marketing, technical services etc.) and consulting might need different organizational answers.

The author further believes that the core elements of any entrepreneurs' cooperative promotion strategy must be the selection and training of promotion personnel, the development of basic routines for strategic planning and adequate monitoring and evaluation within the entrepreneurs' cooperatives assisted. Also, inclusion of public relation measures that facilitate a later "roll-out" would be important.

## Chapter 1

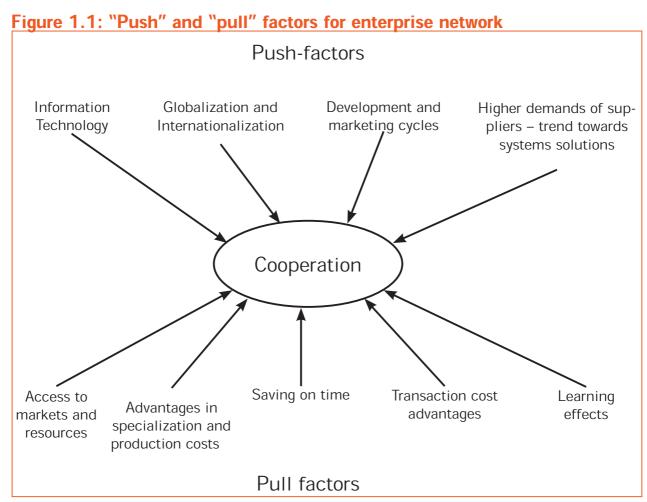
## Cooperation among enterprises – Survival strategy and competitive edge

Small and medium-sized enterprises (SMEs), the world over, are facing particular challenges resulting from globalization, increasing customer expectations and the revolution in information technology. Due to reduced trade barriers, lower transaction costs, and increasing similarity of lifestyles around the world, so called "global players" find it easier than ever to infiltrate local markets. In order to minimize the disadvantages of large size (such as lack of flexibility and the comparatively high cost of coordination) and to reduce complexity, they use decentralized holding structures, develop systems with which to address customers individually, and redirect risk to their medium-sized suppliers. In doing so, large companies successfully emulate what used to be comparative advantages unique to SMEs (Grothus, 2000, p. 19). At the same time they try to extend their advantages of scale, such as the effects of experiential learning curves and networking and global purchasing strategies (global sourcing) by means of strategic alliances and mega mergers (Krüger and Danner, 2000, p. 92).

In the last decade of the 20<sup>th</sup> century, large organizations often underwent restructuring which led to demands for high value systems solutions and extraordinary quality from their small and medium-sized subcontractors and suppliers. At the same time technological

#### Entrepreneurs' cooperatives ENTERPRISE CLUSTERS

developments meant a growing use of automation leading to a need for higher capital intensity even in medium-sized firms (Frank, 1994, p. 104). Growing expenditure on research and development, shorter product life cycles, and increasing cost competition are stark realities faced by small and medium-sized enterprises. SMEs can only answer these pressures on their profit margins by sustainable diversification and/or differentiation. To do this they have to improve their core competencies through continual efforts at innovation and by systematically identifying and exploiting potential for cooperation (Pinkwart, 2001, p. 191). These strategic approaches must be looked at together. This is especially true for research and development, the costs and risks of which can be born more easily by large enterprises (Mugler, 1998, p. 47).



Source: Based on Dörsam and Icks, 1997, p. 35

Against this background *Dörsam and Icks* (1997, p. 33) see the way in which enterprises cooperate, e.g. the form enterprise clusters take, as a reconciler between external factors forcing enterprises to cooperate ("push" factors) and potential benefits at the level of the individual enterprise ("pull" factors).

Table 1.1: Direct aims of cooperation between SMEs

Figure 2 2 2 2 2 2 2 2 2 2 2 2 2 2 2 2 2 2 2		
Efficiency goals	Quality goals	
<ul> <li>economies of scale and scope (incl. sharing of resources, facilities and risks);</li> <li>access to new (domestic and foreign) product markets (including participation in larger public tenders);</li> <li>easier access to finance;</li> <li>fixed costs can be lowered by:         <ul> <li>vertical and/or horizontal integration of product chains;</li> <li>sharing research and development (R &amp; D);</li> <li>use of standardized components; and</li> <li>use of common logistics and marketing;</li> </ul> </li> <li>enlargement of markets through common marketing and distribution;</li> <li>more diversified clients and markets;</li> <li>more stable relationships with buyers and producers;</li> <li>risk-sharing through joint funding and/or operations;</li> <li>management-training, development;</li> <li>shortening of development cycles; and</li> <li>use of purchasing advantages.</li> </ul>	<ul> <li>new materials, processes and products can be created by combining complementary R &amp; D capabilities;</li> <li>systems solutions through product combination;</li> <li>improvement in customer proximity;</li> <li>acceleration of knowledge transfer and technology upgrading; and</li> <li>enhanced skills, standards and capacity.</li> </ul>	

Cooperation between SMEs is one way for them to build or gain power in the market and to become part of a larger system without losing their own legal or economic independence (Commission of the

## Entrepreneurs' cooperatives ENTERPRISE CLUSTERS

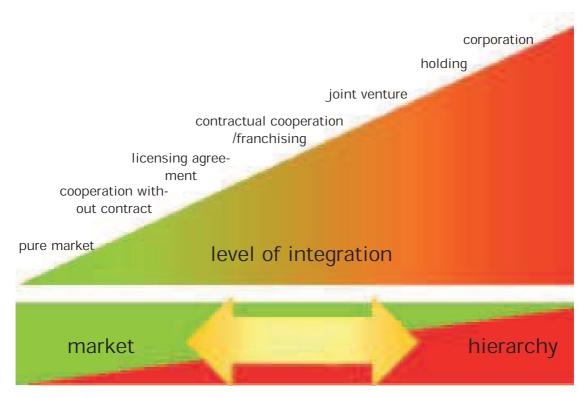
European Communities (EC), 2004, p.5; Mandewirth, 1997, p.1). Using cooperative strategies, enterprises can reduce the scope of production in ways conducive to making the most of their individual core competences, concentrating on those areas which contribute most to the overall enterprise. Using partners whose specified inputs cost less or are of better quality than one's own production has always been the single most important factor for cooperation (cooperation in purchasing). This has not changed and works best where partners can use differing economies of scale, and of cost control, as well as obtaining differing experiential and learning curves in their specialized fields. Table 1 gives a view of the quantitative and qualitative aims, which can be addressed by cooperation between SMEs (EC, 2004, p. 5; Göler von Ravensburg; Pinkwart; Schmidt, 2003, p. 4; Jenkins et al., 2007, p.6).

To cooperate in an enterprise cluster, SMEs can choose from a wide range of governance types, which form a continuum between market coordination and hierarchical integration (see diagram 2).

Different forms of cooperations can express themselves in different organizational forms. The most frequently used three forms (Abel, 1992, p. 94) are:

- the more decentralized form of cooperation where partners act largely independently and only share resources for one or two processes;
- the leadership firm type cooperation, where certain functions are fulfilled by only one of the cooperating partners; and
- cooperative outsourcing into a joint venture (Bullinger; Ohlhausen; Hoffmann, 1997, p. 46) forming a business entity quite separate from cooperating partners.

Figure 1.2: Level of integration



Source: Based on Fieten, Friedrich and Lagemann, 1997, p. 219

Where it is sensible to form a joint venture, the choice of legal form is of prime importance. Careful thought should be given to this question in order to make a joint venture sustainable, and to create and nurture the trust amongst partners so essential to successful cooperation. In principle all available legal forms can be used for joint ventures depending on national legislation, the desired image of the legal form to users, administrative ease and international acceptability (where international trade is sought).

For the rest of this publication we will concentrate on the entrepreneurs' cooperative as one organizational form particularly suited to certain kinds of cooperation between SMEs, and which is legally well defined in many countries. In order to do so, we begin with the search for a working definition which describes the phenomenon across borders and legal systems.

We then discuss the benefits of forming entrepreneurs' cooperatives from empirical and theoretical perspectives in chapter three. Chapter four focuses on the employment effects of entrepreneurs' cooperatives and how they can be used to support improvements in quality of life.

Chapter five considers the operational practices and problems of entrepreneurs' cooperatives, offering empirical and theoretical perspectives. Chapter six discusses the challenges to the establishment of entrepreneurs' cooperatives and what is needed to promote them. Chapter seven links in with this discussion by focusing on the legal and policy framework for promoting good practice. The final chapter conculdes by giving insights into the possible promotional avenues for entrepreneurs' cooperatives. Illustratives examples are provided throughout the text.

## Chapter 2

## Approaching a definition

### 2.1 Definition by membership

Farmers, tradesmen, and craftsmen have cooperated in joint ventures, adopting the cooperative form, for some time, thereby gaining advantages associated with size without losing their individual entrepreneurial freedom. Approximately 150 years ago entrepreneurs' cooperatives among SMEs began to develop, probably first in Germany. They were then copied rapidly in other European countries across a range of business sectors (Zerche; Schmale; Blome-Drees, 1998, p. 26-27). Their founding and development were encouraged simultaneously by various promoters with sometimes similar, sometimes differing ideas. For example, in Germany Schultze-Delitzsch was one of the known cooperative promoters and is considered the "father" of German cooperative law. Schulttze-Delitzsch always arqued that what small enterprises and independent trades people needed most, besides access to finance, was cooperation in order to purchase inputs in bulk and save on input costs (Dülfer, 1994, p. 788; Göler von Ravensburg, 2007, p. 58; Fehl, 2007 p. 99).

Today, purchasing and marketing cooperatives (the oldest type of entrepreneurs' eooperative) make up 33 per cent of all newly founded

#### **Example 2.1: Texmoda, Finland**

Texmoda is Finland's largest specialized chain of businesses operating in women's and men's wear. The Texmoda Fashion Group cooperative incorporates 42 members. The cooperative develops fashion lines and business concepts for its member retailers. One key part of this cooperation is to produce individual product ranges for the retailers. This enables members of the cooperative to reduce design costs, while having a common inventory also reduces distribution costs.

Source: http://www.moda.fi (14. Oct. 2008)

cooperatives in Germany (see Alscher and Priller, 2007, p. 7), while according to *Schwettmann* (2006 p. 6), over 50 per cent of all small businesses in Germany are members of entrepreneurs' cooperatives.

In the course of this historic process entrepreneurs' cooperatives given differing, sometimes more descriptive names different European countries and economic sectors. In Germany, "Gewerbliche Genossenschaften" example, (commercial cooperatives), "Einkaufsgenossenschaften" (purchasing cooperatives) or "Vermarktungsgenossenschaften" (marketing cooperatives) all represent entrepreneurs' cooperatives in the trades and industrial sectors. In France, the distinction seems to be between cooperatives of shopkeepers, handicraft businesses or independent professionals. In Belgium, cooperatives of independent retailers have a different name, while in Italy and in Great Britain the term "cooperative consortia" is much in use (Cooperatives UK, 2006, p. 1). They are all entrepreneurs' cooperatives in the true sense (Couture, 2003, p. 1), even if not called SO.

A cooperative (also co-operative or co-op) is defined by the International Co-operative Alliance's Statement on the Cooperative Identity as:

"...an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically controlled enterprise".<sup>1</sup>

The term 'persons' thereby encompasses both individuals well as legal or judicial entities, such as companies, associations or even (primary) cooperatives.

In principle this means that cooperatives can be created by individuals, such as consumer and worker cooperatives. Entrepreneurs' cooperatives, however, are formed by groups of entrepreneurs, independently owned businesses, tradesmen, professionals, or by municipalities and other public bodies (Birchall, 2001; Parnell, 2001; Bhuyan, 1996).

From the early 1970s onwards this type of cooperative became increasingly interesting in parts of the USA and Canada, especially in rural areas, where entrepreneurs' cooperatives were founded to maintain vulnerable privately owned and public sector infrastructure (Couture, 2003, p. 1; Young et al., 2001, p. 13; Doherty, 1997, p. 2; British Columbia Cooperative Association, 2007, p. 3).<sup>2</sup> Here they were named "Shared Services Cooperatives" (SSCs).

In 1995, on behalf of the United States Department of Agriculture (USDA), *Crooks, Spatz and Warmann* (1995, p. 5) defined shared services cooperatives to be:

"...a group of private businesses or public entities that join to form an organization which provides one or more services to enhance or increase the competitiveness of members' operations."

<sup>1</sup> See also http://www.ica.coop/coop/principles.html (14. Oct. 2008).

<sup>2</sup> See also http://www.ncba.coop/abcoop.cfm (14. Oct. 2008) and http://www.nreca.coop/AboutUs/Overview.htm (14. Oct. 2008),

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In that report the term "cooperative" is defined as an organization legally incorporated as a cooperative or non-profit corporation that operates on a cooperative basis (member-owned, member-controlled, and member-service oriented).

#### **Example 2.2: Rural Wisconsin Health Cooperative (RWHC)**

The Rural Wisconsin Health Cooperative is owned and operated by 32 rural, acute, general medical-surgical hospitals. It is a strong and innovative cooperative, which develops and manages a variety of health products and services for member hospitals. It also assists members to offer high quality and effective health care and to partner with others to make their communities healthier. It also generates additional revenue by providing services to non-members.

**Source:** http://www.Rwhc.com (14. Oct. 2008)

This definition, entailing membership of public entities, is the result of a particular need in North America (Bhuyan, 1996, p. 5-6). Here, entrepreneurs' cooperatives are frequently viewed as vehicles to introduce, improve, or sustain essential infrastructure (e.g. electricity supply), social services (British Columbia Cooperative Association, 2007, p. 3) and socio-economically important services (e.g. a community shop, a school or day care) in remote rural areas (Bhuyan, 1996, p. 5-6; Doherty, 1997, p. 1). It is here, that apart from business and municipal members, entrepreneurs' cooperatives often include consumers and self-employed persons (individuals) (Doherty, 1997, p. 2). It is also here that municipalities first used the cooperative form in

Many rural areas in the United States are supplied with electricity by cooperatives, which in turn are largely affiliated to the National Rural Cooperative Association. This is a secondary cooperative and as explained above represents an entrepreneurs' cooperative – http://www.nreca.coop/AboutUs/OurMembers.htm (14. Oct. 2008).

which to operate.4

In the USA, since 1995, two significant alterations in the dominant view have occurred. In 1997 the same authors altered their definition somewhat by excluding any reference to the legal status of cooperatives and included the sentence:

"In simplest terms, the shared-services cooperative provides services in response to the specific needs of its member-owners. This makes the cooperative an extension of each member's own operation" (Crooks, Spatz and Warmann, 1997, p. iii).

In 2008 the USDA website published a definition of SSCs dating from 1998, which suggests that they are a mere purchasing cooperative:

"A shared-services cooperative is an organization whose members are businesses or public entities that jointly acquire goods and/or services at a specified quality for the best available price."

The latest ILO publication on this type of cooperative, by Marie-France Couture (2003, p. 2), calls them "*Cooperative Business Associations (CBAs)*" and uses the following definition, likewise attributing it to the USDA:

"Purchasing or shared services cooperatives (CBAs) are cooperatives whose members are other businesses or public entities which join together to increase the performance and competitiveness of their organizations. Members of these cooperatives have found that, by pooling their purchasing power to acquire goods and services, they can lower their operating costs. Like all cooperatives, the purchasing or

One SSC founded early on by municipalities was the Western Areas Cities and Counties Cooperative (Trechter et al., 1998).

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shared services cooperative exists to meet its members' needs, and almost any service can be provided by these cooperatives for their members".5

This definition is very useful in that it clarifies membership (businesses and public entities). However, it narrows the range of services to purchasing, whereas the theory explored at the beginning of this paper,

#### **Example 2.3: Lesotho-Coop, Lesotho**

Lesotho-Coop is an Entrepreneurs' Cooperative owned by many small groups producing grass baskets in the mountains of Lesotho. The joint purchasing and supply of raw materials provided by the cooperative reduces the material and transportation costs. The collection of the finished baskets further reduces the overall production costs.

**Source:** http://www.podi-mohair.de/Projekte/Lesotho-Coop/leotho-coop.html (22. Feb. 2008)

and the examples given, show that the range of services which members want from their entrepreneurs' cooperative can be much broader. This definition also ignores the more recent trend towards entrepreneurs' cooperatives for professionals and SME rendering services. Although largely limited to industrialized countries, these new trends warrant closer study - if for no other reason than the fact that new employment created in the tertiary sector far outweighs employment created in the primary and secondary sectors.

Lately, the European Union has begun to differentiate between consumer, employee, and so-called *Client (producer) cooperatives*. Client cooperatives are where producers of certain products or services own the cooperative for the purposes of marketing, adding value to products and services, or jointly purchasing raw materials or means of

<sup>5</sup> United States Department of Agriculture (USDA) (1998) This definition is also used by the National Cooperative Business Association.

production (EC, 2001, p. 7).

The biggest obstacle to a definition on the basis of membership remains the difference between workers and independent trades persons, especially as far the informal economy<sup>6</sup> is concerned. For this study, we assume that no employment contracts exist between members and entrepreneurs' cooperatives where as they do between workers and a typical workers' cooperative. Members of an entrepreneurs' cooperative have a different contractual relationship with their cooperative, which concentrates on the exchange of supplies, services or produce for marketing. Payments from entrepreneurs' cooperatives to members is based on units of these services rendered, rather than on working hours.

### 2.2 Definition by benefits and activities

For the purpose of defining entrepreneurs' cooperatives for this study, the preferred definition an entrepreneur's cooperative is the one given by M.-F. Couture in 2003. However, it is necessary to extend the discussion of the benefits and activities of entrepreneurs' cooperatives,

#### **Example 2.4: Valley Bakers Cooperative Association, USA**

The Valley Bakers Cooperative Association is a bakery and foodservice wholesale distribution company, which was founded in 1949 in order to bring together member purchasing power, storage and distribution of products in the most economical way. It enables members to reduce costs of ingredients through volume purchasing, creates efficient distribution services, reduces time salesmen spend with customers, and time spent servicing multiple supplier accounts.

Source: http://www.valleybakers.com (14. Oct. 2008)

A typical example of how differentiation becomes confounded again can be seen in *Parnell* (2001, p. 45-46).

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in order to understand fully the most recent trends in cooperating over a wide range of economic environments before arriving at a revised working definition.

By cooperating through entrepreneurs' cooperatives, members might (Commission of the European Communities, 2004, p. 5; Göler von Ravensburg; Pinkwart; Schmidt, 2003, p. 4; Couture, 2003, p. 7; Bhuyan, 1996, p. 5):

- pool and share resources (machinery, equipment, buildings,
   I.T. facilities as well as knowledge);
- use economies of scale in buying raw materials and commodities;<sup>7</sup>
- enlarge their markets or improve individual market access through joint strategic planning, market analysis, marketing and logistics channels and systems (e.g. publicity and promotion, brand creation and market intelligence);
- share research and development facilities;
- shorten development cycles;
- use standardized methods or components;
- improve accounting, management and general human resources (e.g. through education, training and development);
- outsource accounting services, tax and legal advice;
- increase scope for economies of space (e.g. for common product storage and warehousing);
- create common insurance covers, credit facilities; and/or;

See for example *ILO*: http://www.ilo.org/dyn/empent/empent.portal?p\_docid=CREATION& p\_prog=C&p\_subprog=MS (6. Sep. 2007). For an impression on the various basic systems used by entrepreneurs' cooperatives in bulk buying and distribution to members see *Couture* (2003 p. 7-8).

provide other (economic) benefits for members.

Empirical research shows that various types of SMEs, professionals and trades people cooperate in such functions. In 1996 *Bhuyan* (1996, p. 7) lists a fairly short list of restaurants and food outlets, independent hardware stores, pharmacies and retail outlets, electric cooperatives, beauty salons and direct mailing contractors which do so. In 1997 *Doherty* (p. 2) adds handicraft producers; *Couture* (2003, p. 4-6) adds a comprehensive list of craft traders of various kinds, hotels, travel services and independent professionals such as doctors, lawyers and management consultants. *Crow* (2006) draws attention to another possible field for Entrepreners' Cooperatives, namely publishing.

This wide spectrum of interest in using common activities and benefits has led to entrepreneurs' cooperatives being called "Common Facility Cooperatives" (International Labour Office, 1961, p. 135), "Common Service Cooperatives" (International Labour Office, 1961, p. 138), "Cooperative Business Associations" (Couture, 2003, p. 1) or "Shared Services Cooperatives" in previous ILO publications (2003).8

#### 2.3 Types of joint consortia

Entrepreneurs' cooperatives differ in a number of ways from other systems of collective business, such as joint ventures, holding companies, trade associations or from franchising systems.

Small and medium-sized enterprises frequently have the need to cooperate with other enterprises, even with those who may be competitors. Such cooperation can take on various forms:

#### 2.3.1 Trade Association/Business Association

For the purpose of this study, trade associations and business associations are seen to be synonymous. Business associations are

<sup>8</sup> See http://www.rurdev.usda.gov/RBS/pub/cir49.pdf (14. Oct. 2008)

non-profit organizations in which members are competing companies or individuals from the same business sectors. Members are usually engaged in a common business pursuit, even if they be competitors. Usually any applicant meeting the standards of the association must be accepted as a member. Anti-trust law frequently prohibits a Business Association from denying an otherwise qualified applicant membership. For example, if the applicant is in close geographical proximity to an existing member.

As well as offering members opportunities to meet to discuss common problems, local Business Associations frequently offer lobbying services, and by representing their members' collective interests - sometimes bordering on political representation or controlling local competition - can fulfill a (quasi-) public function. They often maintain educational programmes and offer technical and legal advice, as well as market intelligence (Nadvi, 1999, p. 2). Sometimes they distribute marketing materials designed to be imprinted by each member.

Few Business Associations, however, offer much direct help in the major areas of business, such as those associated with purchasing, production or marketing. Often the purpose of Business Associations is not perceived to be in the provison of common economies of scale or scope, but rather in providing a local forum for joint action. Even in the few instances where elective group purchasing plans are offered, they bear no credit risk in transactions. Instead, they provide selected vendors with access to the large body of members, but the vendor must assure the credit worthiness of each purchaser.

To sustain its operations, a Business Association generally receives a joining fee and/or a yearly subscription from its members, and may also collect rebates or commissions from such chosen suppliers. Relatively low membership fees are imposed, so most Business Associations have neither the ability to offer a national marketing capacity nor access to expensive technologies, nor cost-effective purchasing programmes. With limited financial resources, Business Associations do not have

the management structures for major projects, such as national sales and marketing.

Doner and Schneider (1998, p. 11 as quoted by Nadvi, 1999, p. 2) detail ways by which Business Associations may contribute to economic performance by supporting members with a range of "market-complementing" and "market-enhancing" functions. These include:

- Horizontal and vertical coordination amongst producers as well as using upstream and downstream linkages, so long as both are within anti-trust and competition law;
- The setting and enforcement of product standards; and
- The provision of information and technical training.

*Nadvi* (1999, p. 20), who researched the development effects of Business Associations in four industrial clusters in India, Mexico, Brazil and Pakistan, found no significant improvements in the delivery of producer services associated with raising skills, labour training or technical upgrading. the findings of the research however indicate:

"the function that Business Associations can play in providing a catalyst for action, in collectively articulating cluster wide interests, and in promoting programmes of upgrading. It also shows clearly how collective goals can be thwarted by the actions and particular interests of key leading actors."

The findings indicate that internal differentiation within the cluster is of great importance for its effectiveness in rendering services that serve all members.

### 2.3.2 Franchising

By definition, a franchise is a form of business cooperation in which

a company with a successful product or service (the franchisor) enters into continuous contractual relationships with other businesses (franchisees) in order to extend its turnover and profitability. This contract (often called licensing as well) usually includes well-defined and comprehensive purchasing, marketing and organizational methods with clearly defined responsibilities and controls between franchisor and franchisee (Collrepp, 2004, p. 69). By paying a fee franchisees obtain the right to operate under the franchisor's trade name, use the same method of doing business, use trademarks, signage, products, software and business systems. The business agrees a common approach to delivering a product or service with the franchisor's guidance.

Franchises may be established on a territorial basis without violating antitrust laws and usually, the franchisee owns the non-real estate assets of a franchise. The franchise fee is generally substantial and the franchise contract consists of a variety of contractual matters, such as licensing and agency agreements, know-how contracts, representational clauses and contracts of service. Not adhering to any of the franchise terms often means violating the whole agreement. Frequently the franchisee cannot make independent business decisions, such as the purchase of any inputs or the opening hours of business, and very often the agreement negates substantially individual freedom of disposition.

Such franchise "chains" exist in many sectors and for many products and services, including accounting, further education, employment agencies, senior citizens care, restaurants and travel services. National franchising associations exist in at least 48 countries. 10

Being a franchisee has certain advantages over going it alone, particularly for business start-ups.<sup>11</sup> A tried and tested entrepreneurial concept can

<sup>9</sup> http://www.franchisehandbook.com/directory/view.asp?search=cat&cat= 107 (9. Aug. 2007).

<sup>10</sup> http://www.franchisehandbook.com/associations/ (14. Oct. 2008).

<sup>11</sup> http://www.entrepreneur.com/encyclopedia/term/82150.html (14.

be followed without needing much creativity, and know-how is readily available. The trademark, the product and its image already exist in the market. Often franchising has a competitive advantage by exploiting a new business idea or product, presenting a new solution to an old problem or creating a special marketing concept. The investment risk is comparatively low, there is guidance, economies of scale can be achieved, and training, consulting and guidance are provided. Sometimes low interest loans are available and in some countries start-ups within franchise systems do attract public loan subsidies (Collrepp, 2004, p. 72).

However not all franchise systems are equally reputable or reliable and the individual franchisee still carries a significant amount of risk (Collrepp, 2004, p. 69). The economic success of the venture is heavily dependent on the quality of the franchise system. The fees are usually very high and can be an economic burden. At the same time, the entrepreneur is restricted; individual wishes seldom can be accommodated, and when the contract expires the enterprise usually must be closed.

On a side-note: It appears that several franchise chains have formed entrepreneurs' cooperatives in order to save on supplies. *Bhuyan* (1996, p. 7) quotes the National Cooperative Bank (of the USA) when stating that in one case such a purchasing cooperative has helped thousands of Kentucky Fried Chicken franchises to save about \$ 1,000 per month.

### 2.3.3 Joint Venture<sup>13</sup>

A joint venture is an entity formed between two or more parties to undertake one or more economic activities together. The parties agree

Oct. 2008) and http://www.thebfa.org/whatis.asp (14. Oct. 2008).

See also http://sbinfocanada.about.com/od/startup/g/franchise.htm (14. Oct. 2008).

<sup>13</sup> http://www.law.cornell.edu/wex/index.php/Joint\_venture (14. Oct. 2008).

to create a new entity by contributing equity, and they then share in the revenues, expenses, and control of the enterprise. The venture can be for one specific project only, or a continuing business relationship, such as the Sony Ericsson joint venture. This is in contrast to a strategic alliance, which involves no equity stake from the participants, and is a much less rigid arrangement.

A joint venture may exist in the short or long term, involve any type of business and the "persons" involved can be individuals, groups of individuals, companies, or corporations. Joint ventures are widely used by companies to enter foreign markets, by forming ties with domestic companies and pooling technologies and business practices in the venture. The domestic companies already have the relationships, the necessary legal entity as well as being entrenched in the domestic market. These joint ventures may last for a long time.

Non-Profit Organizations may also form joint ventures. For example, a child welfare organization in the USA initiated a joint venture to develop and service client-tracking software for five welfare organizations whose representatives sit on the joint venture corporation's board. This enabled them to provide the community with a much-needed resource.

The phrase "joint venture" generally refers to the *purpose* of and not to the type of entity. Therefore, a joint venture may be incorporated as a shareholding company, limited liability company, partnership, cooperative or other legal structure, depending on national company law and on other considerations such as tax and tort liability. In order to be incorporated as a cooperative, the prime purpose of promoting the members interests must be acceptable in national law. Some countries' cooperative laws make provision for so-called 'cooperative joint stock companies', which are hybrids of cooperative and shareholding companies (Luther, 1994, p. 511-517).

### 2.3.4 Holding Company

A holding company is a company, which owns enough voting stock in another to control management and operations by influencing or electing its board of directors. <sup>14</sup> It is thus often called a parent company. The arrangement makes venturing outside a company's core business possible and, under certain conditions, allows benefits from tax consolidation, the sharing of operating losses, and ease of divestiture. The legal definition of a holding company varies with the legal system. For example, share holding requirements may be of a majority (80 per cent) or the entire (100 per cent), while elsewhere "holding" entails as little as five per cent of the voting shares of the subsidiary. Holding companies can, in theory, assume different legal forms, but in practice are usually organized as mutuals, shareholding companies or companies with limited liability. The regulations on this differ widely internationally.

## 2.4 The cooperative type of joint venture

Cooperatives in general may operate in many sectors including agriculture, banking, housing, wholesaling, retailing, production and so on. They may have producers, tenants, traders or consumers as members. As a form of enterprise, a cooperative differs from a mutual in that its enterprise goes beyond raising common funds.

An entrepreneurs' cooperative is a cooperative with some similarity to a trade or business association, but a significant difference between the two is that the members of a business association has no equity in the association. Typically cooperative members do own equity, in that each owns a portion of the enterprise. This may entail a qualification criteria associated with membership, which is another difference with the business association, which has to serve all businesses of a certain kind within a locality.

<sup>14</sup> http://www.legal-explanations.com/definitions/holding-company.htm (14. Oct. 2008).

Cooperatives of all kinds, including entrepreneurs' cooperatives, are governed by democratic principles, such as "one member, one vote". The direction of decision making is principally "bottom up", and governance is ideally by members who make up the general assembly and elect the board of directors (and maybe a supervisory board as well). The members exonerate these boards and decide on the use of surpluses accrued, and they alone can change the constitution of their joint venture. In contrast, governance and decision making in most share-holding enterprises, franchise systems and joint ventures is "top down".

Entrepreneurs' cooperatives (like all cooperatives) have certain structural differences from other investor-owned enterprises:

- return of profits is restricted and normally proportional to the use made of the cooperative's services;
- accumulation of asset value is not reflected in the value of shares;
- shares cannot be exchanged on stock markets;
- freedom of entrance and exit to the cooperative is guaranteed;
- nominal capital is variable; and
- in liquidating operations to principle of non-distribution applies.

In relation to investor-owned companies, these specific characteristics of cooperative enterprises result in distinct advantages and disadvantages.

### 2.4.1 The definition an of entrepreneurs' cooperative

An entrepreneurs' cooperative is a special form of cooperative. It differs from consumer and producer cooperatives in that its members are predominantly (formalized and/or informal) enterprises, SMEs, self-employed persons and professionals, sometimes municipalities or other public bodies. Members have businesses producing for and/or trading in markets, or are supplying paying customers with services. Members can be legal entities or individuals. Membership is taken for the sake of obtaining services, which are of key importance to members' businesses. Members expect benefits to income and economic well being, not primarily for consumer, social or cultural reasons.

For the purpose of this study, the emphasis will be on cooperatives in the legal sense (registered under national law), also known as incorporated cooperatives.<sup>16</sup>

Although mutual saving by and lending to members can be an important economic service for members, credit cooperatives are excluded from the investigation, as the financial markets differ from markets for other services and goods.

Similarly, for the purposes of this study, agricultural cooperatives and new generation cooperatives are considered to be separate issues. Although there are many parallels between agricultural producers and business people in cooperatives (See for example Wöhlken, 1994, p.

Public bodies, trade unions or self-help-groups, for example, follow other commendable aims like infrastructure delivery, lobbying activities or mutual support. However, they do not usually enter competitive markets in the same way as businesses and professionals. Entrepreneurs' cooperatives however, pursue their aim to support their members by running a common enterprise or joint venture, which in turn, competes in certain markets.

In some regions of the world it is difficult to incorporate, yet possible to act as an entrepreneurs' cooperative. From time to time the book may refer to cooperatives "in the economic sense" (See *Engelhardt*, 1994, p. 103).

11-15), agricultural economics have many characteristics unique to the primary sector, and these warrant separate treatment. Moverover, as agricultural cooperatives are so prolific internationally, they have been much better researched than entrepreneurs' cooperatives.

## 2.4.2 Types of entrepreneurs' cooperatives

In Europe entrepreneurs' cooperatives can be and are (as in Germany) sometimes classified again in sub-groups according to their membership (See for example Schädel, 2007, p. 169). There are cooperatives whose members are exclusively producing entrepreneurs, businesses and industries, and again there is a group of entrepreneurs' cooperatives whose members are in retail and wholesale trade. More recently, Entrepreneurs' cooperatives founded in Europe, USA and Australia unite professionals, or represent joint ventures of municipalities or other public institutions (e.g. schools and hospitals) (See for example Bhuyan, 1996, p. 4-11). There are also second tier entrepreneurs' cooperatives, which provide primary cooperatives in trade, commerce and agriculture with common services.

A classification of entrepreneurs' cooperatives according to their activities in serving their member economies makes little sense. Entrepreneurs' cooperatives continually take on new challenges and many entrepreneurs' cooperatives combine several of these functions (see Appendix 2 and 3).

Entrepreneurs' cooperatives at the primary level can be non-profit organizations (NPOs) or for profit organizations (POs). They may also organize cooperatively at a secondary level, and cooperatives can be members of these entrepreneurs' cooperatives. However, these secondary cooperatives are usually NGOs, in that they pay back all surpluses one way or another to their member organizations.<sup>17</sup>

http://www.asianphilanthropy.org/countries/philippines/definition (22. Feb. 2008).

# Chapter 3

## Benefits of forming entrepreneurs' cooperatives

Prior to industrialization, entrepreneurs' cooperatives served their members mainly by helping to manage the incalculable risks of transport (Kaufmannsgilden = traditional cooperations of traders, traders guilds), of markets (tradesmen's guilds) and of prospecting (mining unions) (Kluge, 2007, p. 30).

In contemporary **industrialized countries**, independent traders, entrepreneurs and professionals maintain cooperative joint ventures in order to improve their economic effectiveness, efficiency and quality (Göler von Ravensburg, Pinkwart & Schmidt, 2003, p. 4). They also do this to ensure survival (Couture, 2002, p. 1) in a time of ever increasing concentration and competition (Commission of the European Communities, 2001, p. 9). They cooperate mainly to achieve lower fixed costs and to increase sales and turnover. They also cooperate in order to improve marketing by diversifying methods and by concentrating on their own core competences.

Demand has also risen in developing countries for entrepreneurs' cooperatives, as a result of pressures associated with market liberalization and the rolling back of the state (Couture, 2003). Information technology and global business relationships have

### **Example 3.1: When independent retailers cooperate**

In Europe some groups of independent retailers have managed to survive competition by forming purchasing groups, symbol groups or cooperatives. They have become some of the largest organizations in their retail sectors.

Of the top 20 European retailers by group turnover, seven are defined as cooperatives or symbol groups. At the national level, such groups now hold leading positions in several EU Member States (notably, France, Germany, Denmark, Sweden, Finland, Italy, Spain and Greece). Also, at the individual retail sector level, these groups hold significant positions across a range of countries (e.g. Spar in groceries, Euronics in electrical goods, and Intersport in sports goods) or across a range of sectors within the same country (e.g. Kesko under various arrangements in grocery, hardware and agricultural supplies, clothing, footwear, sports goods, general electronics, computers, optical goods, and cars).

**Source**: Authors's own analysis.

introduced the concepts of enterprise clusters and cooperative methods into business communities. The national consultations¹ leading up to the Extraordinary Summit on Employment and Poverty Alleviation held in Burkina Faso in 2004, for example, listed employment and poverty alleviation among Africa's priorities. One of ways that this was to be achieved was through applying the cooperative concept to new areas, such as cooperatives for small businesses (ILO, 2003, p. 11). According to the ILO Report on its Regional Conference on Employment Creation through Cooperatives and Small Enterprises in Bangkok in 2001 (ILO, 2001b), the interest in entrepreneurs' cooperatives is also very pronounced in Asia. Yet, little literature specific to this type of cooperative exists.

As summed up in an ILO report titled "Working out of poverty. Views from Africa" (ILO, 2003).

Table 3.1: Top 20 European Retailers, 2004

Rank	Company	Home market	European turnover (€ bn)	No. of European countries	% sales in Europe	Enterprise Type
1	Carrefour	France	62.8	13	86	Public
2	Metro	Germany	55.3	24	98	Public
3	Tesco	UK	45.7	8	91	Public
4	Rewe	Germany	40.8	13	100	Со-ор
5	Edeke	Germany	32.9	5	100	Со-ор
6	Lidl & Schwarz	Germany	32.6	19	100	Private
7	Intermarché	France	32.0	8	100	Со-ор
8	Aldi	Germany	31.2	10	87	Private
9	Auchan	France	28.7	8	95	Private
10	Lecierc	France	24.1	6	100	Со-ор
11	Spar International	Netherlands	23.5	21	86	Symbol
12	Wal-Mart	US	23.3	2	10	Public
13	Sainsbury	UK	22.0	1	100	Public
14	Casino	France	19.4	3	84	Public
15	Morrison/ Safeway	UK	18.1	1	100	Public
16	Tengelmann	Germany	16.9	12	63	Private
17	Ahold	Netherlands	13.9	10	27	Public
18	EI Corte	Switzerland	13.2	3	100	Со-ор
19	Inglés	Spain	12.4	2	100	Private
20	Systéme U	France	12.1	1	100	Со-ор

Notes: Data are as at year end 2004 – based on IGD Research. "Ownership" is defined by ACNielson and may not necessarily accord with how groups perceive their own ownership form.

**Source**: ACNielson, The Retail Pocket Book, 2006 Edition (World Advertising Research Centre Ltd)

Much research, theoretical as well as empirical, has been carried out on the general effects of cooperation on SMEs. The general economic and non-economic effects of cooperatives have been almost as well researched theoretically, and the empirical research is particularly good on agricultural and credit cooperatives. In comparison, the listed direct effects of entrepreneurs' cooperatives provided in Chapter 2 could be supported by further empirical research. In particular, one question is wide open: How do entrepreneurs' cooperatives compare with non-cooperative joint ventures in satisfying the aims of their members? Little research is available on the social and more indirect effects of entrepreneurs' cooperatives, including their quantitative and qualitative effects on employment and the benefits to local communities or national economies.

That said, it is worth examining what research is available. The focus must be on any likeness the development of entrepreneurs' cooperatives might show irrespective of where they occur and especially their capacity to create benefits for their members and their environment. Therefore this chapter will discuss the research that is specific to entrepreneurs' cooperatives. Research on cooperatives in general will be brought in where the argument applies specifically to entrepreneurs' cooperatives. The economic benefits of entrepreneurs' cooperatives will be dealt with thereafter, and social and indirect effects in a third section. Employment effects will be examined in Chapter 4.

### 3.1 The current state of research

Regardless of the methodologies, existing studies suggest a variety of definitions for entrepreneurs' cooperatives. The main differences – as seen in the previous discussion - lie with the questions of membership and designation. An accepted definition still applies from when Couture wrote her analysis in 2003. Thus, this becomes our suggested working definition for the purpose of this study (see the end of Chapter 2).

There are various methodologies that can be applied to analyze and

draw lessons from established entrepreneurs' cooperatives, especially their economic and other benefits. Most of these have a *hermeneutic* nature, e.g. examinations/discussions/interpolations of the effects that entrepreneurs' cooperatives have had during their long history in Europe and elsewhere. There are also a number of theoretical based approaches (neoclassical, institutional, and evolutionary economics). Last but not least a few empirical studies exist.

### 3.1.1 Empirical literature

Currently empirical research into the question of entrepreneurs' cooperative benefits largely results from several studies. These include studies from the International Labour Organization, the Commission of the European Communities and the National Cooperative Business Association in the United States, which are discussed hereunder.

Couture (2003) discusses the benefits of cooperative business associations (CBAs) using four examples from Europe, Japan and North America and three from developing countries (Kenya, India and Senegal). The paper argues that some lessons learned from entrepreneurs' cooperatives in industrialized countries may be applicable for developing countries. Couture (2003, p. 8) identifies the conditions which hamper development of entrepreneurs' cooperatives and discusses a strategy, based on establishing pilot projects to promote them.

The examples selected from industrialized countries range from an entrepreneurs' cooperative of community owned health-care organizations and self-employed physicians (VHA Health Care Cooperative in the USA), to entrepreneurs' cooperatives of wall and ceiling materials distributors (AMAROK Cooperative, USA), to independent opticians (Cooperative Optic, France) and shipbuilding companies (Chuzoko Shipbuilders Cooperative, Japan). Examples chosen from developing countries include an entrepreneurs' cooperative of independent handloom-weavers in India (Anjuman

Textiles Handloom Weavers' Cooperative Society Ltd., founded in 1984), an entrepreneurs' cooperative of self-employed craft workers in Kenya (Akamba Handicraft Industry Cooperative Society Ltd., founded in 1963)<sup>2</sup> and an entrepreneurs' cooperative of 17 different building trades in Senegal (Coopérative des Ouvriers de Bâtiment). The three case studies are analyzed in terms of organizational structure, business relationships, services offered, sources of finance, and the economic and social benefits gained by members and local communities. Conclusions are drawn about their sustainability using a SWOT approach.

Couture (2003, p. 44) concludes from these case studies that entrepreneurs' cooperatives can help entrepreneurs and SMEs in both developed and developing countries to be more competitive and innovative. The findings also indicate that entrepreneurs' cooperatives can be profitable and can achieve greater economies of scale, allowing members access to goods and services at prices that they could not achieve individually. Some entrepreneurs' cooperatives were able to provide access to new markets, such as Fair-Trade export markets. All these benefits contributed to creating jobs and sustaining growth.

There are two notable studies from the European Commission, namely:

- Commission of the European Communities. 2001. Cooperatives in Enterprise Europe, Consultation Paper, Brussels.
- Commission of the European Communities. 2004.
   On the promotion of cooperative societies in Europe.
   Communication from the Commission to the Council and the European Parliament, the European Economic and

Although the cooperative makes workspace available to the craft-workers these remain independent in that they do not have an employment contract with the cooperative (thus it is not a workers' cooperative). On the contrary, they frequently employ their own staff (Couture, 2003, p. 23).

Social Committee and the Committee of Regions, Brussels.

Although not based on their own empirical research, these two documents of the European Commission are worth including under "empirical research". Neither would have been written but for extensive consultations between the EU, the ILO, cooperative associations represented at EU-level, representatives from relevant Member States and national cooperative federations, unions and associations. Indirectly, both the consultation paper and the resulting communication of the European Commission are thus empirically based.

The European Commission (2004, p. 5) views that cooperatives may be provide a means for building or increasing the economic power of SMEs in the market. The European Commission recognises that entrepreneurs' cooperatives have potential to provide economies of scale, access to markets, increase in purchasing power, broaden marketing efforts and support innovative through training and research. They state that:

"Cooperatives offer an appropriate vehicle for enterprises to undertake joint activities and share risks, whilst retaining their independence. Cooperatives also enable vertical integration of product chains. This can be beneficial for small enterprises that are in a weak position in the supply chain and wish to gain for themselves the revenue from added value of their products or services."

At the same time it is recognised that the concept of entrepreneurs' cooperatives is not well socialized. However, in the context of economic liberalization and consumers' demand for quality at competitive prices, cooperating can be a means of providing the high quality specialized products and services sustainably. In particular the European Commission identifies a niche for cooperatives in the services sector:

"Service enterprises must provide increasingly high

quality and tailored services to their users. A co-operative structure can allow to the users of its services, since they are at the same time its members, the power to influence the business that serves them, ensuring that it responds directly to their needs. Co-operatives are often able to provide services to groups that would otherwise not be able to access them because their supply is not attractive to profit driven companies. This is the case of the "proximity services" such as health and welfare, sectors where co-operatives are growing most rapidly (2004, p. 5)."

Furthermore the European Commission believes that cooperating increases the critical mass of SMEs, which provides opportunity for accessing public contracts. It also acknowledges the positive effects of cooperatives and their investment in education and training, referring to cooperatives as:

"... schools of entrepreneurship and management for those who might not otherwise have access to positions of responsibility." (2004, p. 5)

Beyond these direct effects, the European Commission (2001, p. 24) also sees that entrepreneurs' cooperatives have indirect benefits, contributing to the development of the European Community.

"The co-operative formula may be particularly suited as a vehicle for achieving diverse community objectives. It may:

- Correct market failures and enable the efficient organization of markets by enabling those who are in a weaker market position to combine their purchasing or selling power;
- Unite small enterprising activities into bigger marketable and more efficient units whilst allowing

them to retain their autonomy;

- Give market power to lay people or small enterprises where homogenous products or services are needed;
- Enable those who have little capital to influence economic decision making;
- Enable citizens to affect or determine services they need;
- Take a longer-term view being based on maximizing stakeholder benefits rather than shareholder value. Members are less likely to "vote with their feet" than shareholders who seek maximum returns in global financial markets. For similar reasons a co-operative will be less likely to withdraw from a particular region or sector because its capital could be more profitably employed elsewhere. Co-operatives can therefore provide a cushion from structural change;
- Provide a school of management, particularly to people who might not otherwise have access to positions of responsibility;
- Integrate large sections of the population to economic activity;
- Benefit local markets and service local needs with close contact to citizens. Raising economic activity in the regions and sectors where co-operatives are active;
- Provide stability. Because the purpose of a co-operative is to benefit its members, rather than to provide a return on capital, they can often survive and succeed in circumstances where investor-owned businesses would be deemed unviable;
- Generate trust and create and maintain social capital due to democratic governance and economic

# Entrepreneurs' cooperatives ENTERPRISE CLUSTERS participation."

Last but not least, the European Commission (2001, p. 24-30) places a great deal of hope on cooperatives for the creation of employment and social security. All these effects can be expected not only inside the European Union, but in differing degrees throughout the world, depending on economic, legal and administrative environments.

Another study to be mentioned is from the National Cooperative Business Association in the United States. The National Cooperative Business Association published information about the benefits of entrepreneurs' cooperatives (which are referred to as shared services cooperatives and equate to purchasing cooperatives). Although the exact methodology is unclear, their statements are based on observance of membership, and thus could be considered to be part of the empirical<sup>3</sup> body of research on entrepreneurs' cooperatives. For instance,

"Belonging to a purchasing or shared services cooperative can be the key to prosperity and even survival for many small businesses ... Members of these cooperatives have found that they can adapt quickly to changing economic conditions rather than become victims of them. Through these cooperatives, businesses and public entities have found they can reduce costs, respond better to competition, and improve overall performance.

Members also receive these economic benefits while maintaining the independence of their business. A cooperative is one way for individual store owners – the backbone of Main Street – to prosper and effectively meet the challenge of chain stores.

For example, Strategic Alliance Alert: Joint Ventures and Partnerships reported in 1994 that Food Service

<sup>3</sup> http://www.ncba.coop/abcoop\_purch\_bene.cfm (7. Oct. 2002).

Purchasing Cooperative saved its members \$1,000 per month per store.

Cooperative benefits come not only from initial savings through group purchasing power, but also from sharing the earnings of the cooperative based on the patronage or use of the co-op."

Finally an empirical study that might be interesting as it is explicitly geared at entrepreneurs' cooperatives was completed by Göler von Ravensburg, Pinkwart and Schmidt in 2003. This study was conducted at the Institute for Cooperative Research at the Philipps-University in Marburg, Germany, in cooperation with the Department for Small and Medium-sized Enterprises of the Faculty for Business Administration at the University of Siegen, Germany. It concerns an empirical research project on the criteria for the initiation of entrepreneurs' cooperatives.

This piece of work centres exclusively on entrepreneurs' cooperatives, which makes it highly relevant to our study. In it, new German entrepreneurs' cooperatives were asked their reasons for using or not using the legal form of a cooperative. Supplementing these questions were the views sought of SME joint ventures, which had chosen a different legal form, and the views of consultants advising their clients in their choices.

The research methodology included a survey of literature, discussions with experts (based on the "delphi-inquiry" method used to select the relevant hypotheses to be tested), the development of a questionnaire, pilot testing in the Rheinland-Pfalz, a national survey and the analysis of the replies. Several group were included in the study, namely:

- new cooperatives among SMEs (established between 1992 and 2000);
- SMEs which showed initial interest in using the form of

- a registered cooperative, but which subsequently did not apply for registration (hereafter called "drop-outs");
- associations and joint ventures not using another legal form or not formalizing at all (hereafter called "noncooperatives"); and
- experts from various consulting professions such as tax advisors, chartered accountants, lawyers and consultants of chambers of commerce (hereafter called "consultants").

The results of the survey were examined to consider why the cooperative form isn't chosen more frequently by cooperating SMEs. The most relevant results of this study can be summarized as follows:

- The German registered cooperative is seen to have some advantages for cooperation among SMEs: Easy entry and exit for members, limited liability, take-over protection, and no minimum capital required;
- Nearly half of all SME-cooperatives operate supraregionally;
- 3. New cooperatives do not allot voting rights in proportion to capital contributions;
- 4. That a departing member does not receive a part of the cooperative gains in asset value and no one is free to trade cooperative shares seems of little importance to cooperative founders;
- 5. The issue of candidates for office having to be a member is seen differently depending on the size of the membership, and small cooperatives want only one board, preferably small, while larger cooperatives prefer to have both a board of directors and a supervisory board;
- 6. The minimum number of seven members to start a cooperative does not seem an obstacle to the choice of this form;

- 7. Pre-registration audit by the federations can be made attractive to starting cooperatives;
- 8. Legal and business consultants who influence the choice of legal form know far too little about the inherent advantages of the cooperative form, and especially about the protection from take-over which it offers;
- 9. Most respondents regard cooperatives mainly as organizations for agriculture and banking, whilst some do recognize housing cooperatives;
- 10. There is great scope for new cooperative endeavours among professionals, in trade, and in social services.

Empirical research on entrepreneurs' cooperatives is uncommon. Other than those quoted above, the authors can only identify case studies on individual cooperatives and of those there are only a few which concentrate on true entrepreneurs' cooperatives. They include those by O. lakouvidou et al. (1997) on women's agro-tourism cooperatives in Greece and those by C. Kazoora on the Shoe Shiners Cooperatives in Uganda (Couture et al., 2002, chapter 9) and the seven presented by Couture (2003, chapters 2-6)<sup>4</sup>.

### 3.1.2 Economic theory

To find a theoretical base for what has been postulated above we have to look to both the work of business academics as well as to economic theory (neoclassics and new institutional economics). However, a theoretical foundation can only be provided for some of what makes entrepreneurs' cooperatives work.

The Internet survey has been conducted in order to replenish this study with an up-to-date impression of the scope and activities of entrepreneurs' cooperatives worldwide. The results of this survey have been summarized and can be found in the tables of Appendix 2 and Appendix 3

It is within the business sector that business academic arguments help clarify our main questions. Value chain arguments based on Porter (2000) can bring some insights into existing cooperative potentials. In essence, he comes to the conclusion that enterprises aiming to generate competitive advantages by cooperating will only create a joint venture if their value chains can be adjusted to benefit both parties or divided between them (Porter, 2000, p. 65). This would happen only for those purposes which carry significant shares of overall costs and where joint operations either produce cost savings because of scale, create benefits from mutual learning or improve the use of capacity (Porter, 2000, p. 421-423).

Cooperatives thus have a definite potential to help smaller firms to retain or gain market shares vis-à-vis large (even multi-national) companies. At the same time, in direct competition, cooperative value chains have to compensate for the additional costs of complexity inherent in any cooperative arrangement.

Discussions based on neoclassical theory mostly point to improvements in access to markets and economies of scale. Those based on new institutional economics frequently centre on the special aptitude of cooperatives to lower transactional and coordination costs, thereby creating trust (social capital), as well as making use of flexible rules and participative governance structures (Theurl, 2004).

According to New Institutional Economics (NIE) the particular ability of cooperatives to lower transaction costs is responsible for real benefits which they can achieve.

Economic theory (rather than business theory) suggests that cooperatives are particularly able to (Göler von Ravensburg, 1998, p. 192):

 concentrate on the socio-economic needs of the members and their economic integration;

- achieve economies of scale;
- break the power of local monopolies;
- show a particularly high level of flexibility and adaptability to changing market situations;
- promote local knowledge and understanding of democratic processes;
- build up their resources thus make themselves truly autonomous, able to survive independent of external support and able to compete in the relevant markets;
- avoid the development of a "recipient mentality" on the part of members;
- instil a high level of identification in the group for the organization's aims;
- inspire innovation, diversification and specialization in their members' enterprises;
- lower enhance accurate information at lower costs, abolish asymmetric information<sup>5</sup>, decrease financial risk and make complementary investments<sup>6</sup> attractive, thus
- In the language of New Institutional Economics 'asymmetric information' describes inter alia the information advantage professional management in a commercial cooperative or the one politically integrated leaders of autochthonous groups might have over ordinary rank and file members.
- The main characteristics of such investments are that neither the individuals nor the organizations investments are profitable without the others. Thus their realization depends on a high degree of certainty of the other party's continued interest in a particular field of business. For example members or clients of a service organization may undertake such investments only if the service organization gives them certain services, supplies, access to a specific market or offers to buy the resultant product from them. In return the organization may make such investments only if it can rely on agreed levels and quality of supply and/or demand on the part of its suppliers/members.

- significantly limiting transaction costs for both, members and organization; and
- establish self-financed federal systems (e.g. regional cooperatives or national unions) for consulting, training, marketing and political representation.

New Institutional Economics (NIE) explains most of these comparative advantages over non-cooperative business organizations by describing the particular hybrid organizational form of cooperatives: Their specific combination of hierarchical agency forces with democratic decision making and market forces (Bonus, 1994, p. 472). Röpke, Bonus and other academic proponents of NIE attribute the lower transaction costs of cooperatives particularly to their ability to overcome asymmetric systems of information, to limit production and market related risks for their members and to effect mutually dependent (rather than one-sided) investments (Bonus, 1994).

Two attributes which were frequently considered to be among the most important advantages of cooperatives seem to be less important when entrepreneurs' cooperatives operate in highly developed contexts. We refer to their ability to achieve economies of scale and to break the power of monopolies (Göler von Ravensburg, 1999, p. 5-6). Bonus (1994, p. 474 and 1987, p. 11) explains that wherever economies of scale matter most, purchasing inputs from large firms usually proves more lucrative now than internal production. Also monopolies that cooperatives were able to break in the past were usually local, whereas now they are regional or national monopolies, which represents a much bigger challenge.

However, Bonus's focus was limited to industrialized economies. If read in conjunction with the value chain perspective it suggests merely that savings from lower costs must outweigh additional organizational costs before cooperatives can actually profit from economies of scale. In areas of the world where no relevant SME supply exists, where few services are available or where the costs of such would be prohibitive,

lowering costs may still be achieved quite easily.

Also, it is probably safe to assume that entrepreneurs' cooperatives (especially SMEs and those with credit functions) can derive many cost advantages from their ability to obtain information on customers who are also their members (Bonus, 1994, p. 474). Schreiter (1994, p. 332) calls the knowledge gained (and distributed) by primary cooperatives "co-ordinative knowledge" and explains:

"The establishment of a co-operative enterprise introduces an additional layer of mutual knowledge including a further level of specialization in between members and their contractual partners."

This can be applied analogously to all types of cooperatives. Knowledge remains accessible in a decentralized manner, yet it is still available for coordination. The specific trade off between common and individual knowledge of potential competitors<sup>7</sup>, that is to say the "economization of knowledge and learning", lies at the root of many comparative advantages of cooperatives vis-à-vis capital driven firms and official intermediaries, e.g. state agencies or more conventional NPOs.

However apart from pointing to potentials of cooperatives, economic theory also argues two specific dangers (Schreiter, 1994, p. 133):

- external environments may produce higher organizational costs for members compared with other forms of cooperation; and
- the cooperative form of organizing can result in somewhat lethargic markets.

In order to correctly apply arguments from economic theory to practical

Quite often all members of a cooperative produce the same goods or exercise the same demand.

situations it is important not to limit the analysis to internal factors, but to look also at different (economic and legal) environments, which may influence some elements of costs. This is particularly true of external factors which significantly influence the development of governance structures and internal economic relationships, ultimately resulting in differing balances of organizational costs and production cost savings, thus producing significantly motivated or de-motivated members.

In turn this means that general statements on the benefits and comparative advantages of cooperative organizations must be regarded with considerable suspicion. It is highly likely that business academics using a value chain approach can identify a specific sector and document cooperative potential. At the same time an economist's analysis of the likely effects of framework conditions is also needed. This would include business economics analysis of a sector or branch, together with an assessment of the organizational costs of cooperation. Then a decision can be reached on whether cooperative action in this sector might be viable or if existing cooperatives will be threatened.

To summarize, economic theory holds several general truths:

- 1. It is important that any entrepreneurs' cooperative is efficient in its operations as well as in its relationships with the members (Göler von Ravensburg, 1998);
- 2. Entrepreneurs' cooperatives must be competitive with non-cooperative joint ventures in the same sector. This entails the achievement of certain economies of scale and/ or scope (market test)<sup>8</sup>;
- With regard to the efficiency of relationships with members, contractual and coordinative costs (as components of overall transaction costs) will depend primarily on the size of the organization, the familiarity among members and on conflict resolution systems rather than on being incorporated as a cooperative;

<sup>8</sup> For this and what is called SHO-Test see *Röpke* (1992, p. 41).

- 4. Social functions (e.g. education, job security, provision for old age or consumer loans in crisis situations) can only be integrated successfully into economically active cooperatives, where this is either not done by other institutions (e.g. specialist organizations, neighbourhood or family systems), where these alternative institutions cannot/can no longer fulfil these at least as well (SHO-Test) (Göler von Ravensburg, 1998, p. 363), or where external resources can be accessed in ways other than through markets (e.g. volunteer work, subsidies, sponsorships);
- 5. Entrepreneurs' cooperatives need to be of a certain size in order to survive and to serve their members well during difficult economic times. It is then that trade-offs have to be made between differing members' interests, reduced business successes and the operating requirements of the entrepreneurs' cooperative (Schreiter, 1994, p. 132). Financial reserves are frequently necessary to mediate during these times;
- 6. Members businesses will vary in turnover and number of employees. Craftsmen, sole traders or professionals will also have different interests depending on age, gender or other professional or social criteria. This usually results in the aims and objectives of an entrepreneurs' cooperative being more complex than those of an organization steered top down, which might result higher coordination costs that need to be kept at bay with the help of adequate organizational structures. These structures are as important to long-term operational success as the competitive situation that the entrepreneurs' cooperative faces is;
- 7. In cooperatives, economic and organizational/institutional developments are closely interlinked. Any assessment or prediction of their overall development presupposes an integrated analysis of both (Schreiter, 1994, p. 135);
- 8. Any entrepreneurs' cooperative which intends to enter

certain markets, develop new ones, maintain or enlarge current market share as well as satisfying its members needs to (Göler von Ravensburg, 1998):

- continuously assess and utilise its changing comparative advantages as they occur;
- innovate in respect of its internal and external dealings;
- minimize transaction costs by engendering, developing and maintaining trust (e.g. good communication, reducing informational asymmetries and uncertainties, and shaping mutual dependencies); and
- o construct and use a good management of change.
- 9. Good management of change for entrepreneurs' cooperatives entails continuous monitoring and selection of (Schreiter, 1994, p. 126):
  - the range of products/services offered;
  - o the technologies and concepts used;
  - o the structural elements governing member, customer and supplier relationships.

The choice of products/services, technologies and concepts depends by and large on the rules governing purchasing and sellingmarkets. The selection of structural elements however, largely depends on the code of conduct and patterns ruling how members trade and interact with each other, and on the respective civil law and external institutions; and

10. The promotional activities of registered cooperatives, cooperative associations and cooperative federations influence on the decision to start an entrepreneurs' cooperative.

For a given joint venture the economics and socially relevant advantages of cooperatives compared with non-cooperative organizations can only be assessed when the economies of a particular sector, and the regional or national institutional framework (e.g. legal and tax conditions) are

known. To do this and remain universally valid is impossible.

#### 3.2 Economic benefits – lessons learned

As we have shown, entrepreneurs' cooperatives can produce positive economic effects for enterprises, for the individual member businesses as well as for the cooperative itself. For the purpose of this study economic effects which go beyond these are seen as macro-economic and are dealt with later in this chapter.

### 3.2.1 Modus operandi

We think it worthwhile recalling the modus operandi of most entrepreneurs' cooperatives, before looking in more detail at the benefits attributed to them. Entrepreneurs' cooperatives frequently offer one or more of the following services to their members<sup>9</sup>:

- supplies of raw materials or commodities (food and nonfood products);
- plant and machinery supplies;
- purchase of machinery and equipment shared among members;
- storage of products;
- marketing and distribution;
- publicity and promotion;
- creation of brand names;
- setting of and certifying quality standards;
- information about products, production and the sector;
- staff education, training and development;

Based upon *Couture* (2003, p. 7) and our own Internet survey of 69 entrepreneurs' cooperatives – see Appendix 2.

- insurance services;
- accountancy, management;
- legal and tax services;
- investment;
- advising members (tax and legal advice, management advice, etc.);
- market analysis and strategic planning;
- occasionally access to business and household finance;
- risk cover; and
- dividends.

Table 3.2: Services in comparison: statistic

	Cooperatives rendering such services in				
Services	Developing countries (percentage)	Industrialized countries (percentage)			
Supplies	14.29 %	23.53 %			
Purchasing	8.57 %	52.94 %			
Creating brand names	0,00 %	11,43 %			
Setting quality standards	28.57 %	17.65 %			
Information about products	11.43 %	20.59 %			
Accountancy	5.71 %	26.47 %			
Marketing	57,14 %	38.24 %			
Education and training	34.29 %	26.47 %			
Promotion	74.29 %	17.65 %			
Legal and tax services	5.71 %	29.41 %			

Entrepreneurs' cooperatives mark up costs of purchased products or services in order to cover operating expenses. Any surpluses achieved are then returned to members in the form of a redistribution of profits according to either the patronage<sup>10</sup> of the member with the entrepreneurs' cooperative or as dividends on capital invested by the member. In many cases entrepreneurs' cooperatives prefer the non-profit status and/or mainly distribute surplus on the basis of patronage.

Most entrepreneurs' cooperatives in their early years offer a limited number of business services for members, with some beginning by offering just one service (Crooks, Spatz and Warmann, 1995, p. 5). This could be called an "outsourcing" effort, which entails that certain processes being delegated to the entrepreneurs' cooperative, with the cooperative operation being wholly owned and steered by the interests of members. As these interests change the cooperative business ventures should follow suit, with members also sharing the gains and risks involved (also see Chapter 5).

As they mature, many entrepreneurs' cooperatives diversify and create intricate structures of ownership and governance or even form financial networks within a greater "symbol group". An example of this is the Conad System<sup>11</sup> described by Prof. *Dobson* in his 2006 report for UGAL.

Like trade associations, cooperatives can delineate membership according to certain professional or business criteria, yet they cannot exclude members on the basis of geography or create exclusive territories. Some entrepreneurs' cooperatives limit their marketing and

<sup>&</sup>quot;According to patronage" means according to the value of products a member delivered to, purchased from or the value of services he bought from or rendered through the entrepreneurs' cooperative.

The choice of Conad as an illustration is based simply on the recognition that it shows the kind of relationships, ownership issues, behavioural and contractual aspects that apply generally to other independent retailer groups. There are many equally useful examples of independent retailer groups that could illustrate the same points. See further details relating to Conad and discussion on the effects and implications of present competition law for the organization (ANCD/ Conad, 2004).

advertising efforts to a given region. However, as we will outline at a later stage, international fair trade often uses the cooperative as a vehicle. Apart from economies of scale, cutting out middle men and pooling of risks (thus lowering transaction costs), cooperative marketing seems able to build more trust into the relationships between producers and consumers.

### 3.2.2 Potential benefits to member enterprises<sup>12</sup>

In general, conditions faced by SMEs, crafts persons, traders and professionals differ not only from one economic sector to another but also with the level of infrastructure, legal, political and economic development of their home countries.

Entrepreneurs' cooperatives are started only by the users of the services if they can be fairly sure that they will generate benefits to their individual businesses. Thus they need to be convinced that the prevailing (positive) market and legal frameworks will remain and allow them to use a certain level of entrepreneurial skill. Based current research we can conclude that entrepreneurs' cooperatives can generate the following direct economic and socio-economic benefits at local and regional levels<sup>13</sup>:

- diversification of production or increased volumes of production leading to improved labour and capital productivity;
- 2. higher incomes and better employment conditions if not more employment (see Chapter 4 for detail);
- 3. improved company growth;
- 4. better access to and mobilization of local resources;
- Please also see Appendix 1: Benefits in hermeneutic literature (pp. 168 ff.).
- See section on "3.1 Current state of research" (pp. 21 ff.) in connection with *Göler von Ravensburg* (2007b, p. 779) and the sources given there.

- 5. diffusion of innovation;
- 6. improvement in use of human resources, transfer of knowhow (especially to smaller enterprises), production of better quality wares with increased value added potential (costs of market research, screening of contractual partners, negotiation and contract supervision are reduced);
- 7. increased efficiency and savings on transaction costs resulting in better credit worthiness and new investment possibilities;
- 8. better risk management;
- 9. possibility to invest in infrastructure development of material as well as immaterial kind<sup>14</sup>; and
- 10. more democracy in local business structures, allocation and distribution of resources.

This goes hand in hand with the summary of the interpretive literature as well as with Porter's model on value chain management<sup>15</sup>. In value chain terms entrepreneurs' cooperatives are joint ventures where individual enterprises cooperate in one or more parts of their value (creation) chain. Such a value chain is pictured in Figure 3.1

Each enterprise is an accumulation of functions (primary and support activities) through which its products are designed, produced, distributed, delivered, transported or supported. All these activities are depicted in Figure 3.1. The value chain of an enterprise and its way of operating in each stage mirror its history, strategy, methods of implementing this strategy and the basic economic rules of the operations themselves (Porter, 2000, p. 67).

By cooperating small entrepreneurs, for example, may be able to obtain training and information, which they would otherwise not be able to access.

<sup>15</sup> See Figure 4: A model of a value chain on p. 35

Figure 3.1: A model of a value chain

		M			
Support		a r			
Support		Techno	logv developme	nt	î
	Procurement				
	Inbound logistics	Operations	Inbound logistics	Marketing and sales	Services g r a

Primary activities

Source: Porter, 2000, p. 66

## **Example 3.2: Interpretation of an Internet-survey**

An Internet survey of the websites of 69 cooperatives in 32 countries indicated that entrepreneurs' cooperatives in developing countries most frequently provide members with assistance in the promotion of products. About 74 per cent provide this service. Marketing services (57 per cent) and education and training services (34 per cent) also rank high.

Entrepreneurs' cooperatives in industrialized countries, by contrast, provide mostly purchasing services (40 per cent), marketing (29 per cent) and different kinds of legal, tax, and accounting services (22 per cent). A comparison of the most frequently provided services can be seen in Table 3.2. Most cooperatives in the survey provide multiple services for their members this explains why the total of services exceeds 100 per cent of all cooperatives.

**Source**: Author's own data

Cooperation mostly takes place in the primary activities. Value gains for members can be achieved by lowering production costs or by helping to assure a standardized quality where this plays an important economic role for them.

Entrepreneurs' cooperatives targeting joint purchasing of inputs or cooperating on output logistics can utilize volume leverage for obtaining both lower prices from suppliers and lower transport costs (Grosskopf, 1994, p. 861; See Figure 3.1). The same principles apply to common storage transport facilities, joint production and marketing activities. Value gains can be achieved by using production capacities fully or more evenly or, by common investments, enlarging them thus indirectly leading to larger volumes, higher quality or more diversified production. These, in due time, may offer possibilities for wider cooperation in marketing and sales and open options to enter new markets, increase market share or improve market penetration. Common customer services 5) might become affordable regardless of fluctuations in demand.

It is relatively easy to measure costs and leverage effects in these fields at the levels of both the entrepreneurs' cooperative and among members, and so devise governance patterns which distribute costs and benefits in a transparent and just manner.

The value gains from cooperation in secondary activities (See Figure 3.1) are more difficult to determine than gains from cooperation in primary activities. Whilst cooperatives created for common purchasing, joint use of infrastructure<sup>16</sup> or for provision of services might find it possible to calculate the exact benefits and costs for each member, it can often be difficult. Especially for those intent on common development of technology or those sharing personnel. In these areas governance systems have to be more complicated with well thought

<sup>16</sup> Cooperatives adding value to primary (agricultural) frequently attracting, pooling and using non-agricultural capital, also see *Doherty* (1997).

### **Example 3.3 The Conad System**

Formed in 1962, Conad's original role was as a national-level purchasing group to operate on behalf of associated retailers in Italy. Over the years, the Conad distribution system (consisting of three vertical levels: a national centre; cooperatives; associated outlets) changed to become a system of distribution companies responding to the consumer, through organizing the common supply and purchasing of foodstuffs and other consumer goods, as well as any other service required to eliminate all forms of intermediation and improve members' business activities to the consumers' benefit.

The present Conad system is made up of retail companies, grouped under eight separate regional cooperative companies. Each cooperative works from a distribution centre supplying its own associates as a wholesaler, as well as granting the use of the CONAD brand. The cooperatives also manage their own outlets, through a controlling company, either exclusively or jointly with their associates. In addition, they are owners of sales outlets that they do not manage but which they rent to companies of associated businesspeople (i.e. independent retailers). Overall, there are some 2,900 branded retail outlets divided into four channels (Conad supermarkets, Margherita local stores, Leclerc/Conad hypermarkets, and Discount stores), plus supply to unaffiliated food stores. Conad retailer turnover amounted to €7bn in 2004, giving the group a market share of around 9.4 per cent (and thereby the number two position behind Coop Italia) in the Italian retail grocery trade.

The cooperatives authorize the use of the logo brand products to those retailers who accept a series of special obligations (e.g. to take an appropriate private label assortment, respect the promotional campaigns, etc.). Purchasing loyalty is maintained through a system of discounts on the prices of goods. In some cases, there are minimum purchasing requirements (to ensure efficiency in order and delivery sizes). Retail price setting is left to members, but there is a system of suggested prices between the cooperatives and the members.

As well as their wholesaling and store management and ownership roles, the regional cooperatives also carry out all the basic transport and logistical support, through distribution centre companies. The cooperatives are, in turn, associates of CONAD Central, together with smaller companies and consortia, usually controlled exclusively or jointly with the same cooperatives. The central CONAD consortium, on behalf of the associates, is the central negotiator for the supply contracts with the producers. The national consortium also carries out other services, including quality controls, conditions and negotiating the contracts for purchasing the private label products, the setting up of certain initiatives for promoting a particular product for the retailers of associated cooperatives, and national advertising campaigns under the CONAD logo.

The agreement between the enterprises and their cooperative is, however, much more involved than the mere re-sale of goods, and is similar to a franchising agreement where the retailer is the affiliate and the cooperative is the coordinating body. The cooperative provides its brand, logo, know-how and assistance in distributing products that it sells and delivers to its affiliate. Moreover, through other associated companies, it provides other services to its members, for example, technical, financial (leasing, etc.), human resource management, computer services and training, and legal and administrative services.

In summary, the CONAD system is made up of horizontal and vertical agreements aimed at providing its various member companies, that are legally distinct, a uniformity of strategic guidelines, of sales policies and a shared external image and favourable supply terms to allow retail members to compete effectively in the market and serve consumers well.

out rules for transparency, accounting procedures, distribution and sanctioning.

No matter what their activities and related savings on production costs or increases in revenue, entrepreneurs' cooperatives undoubtedly also generate transaction cost advantages by building trust and interdependencies within their membership. In other words, building "internal social capital" (Commission of the European Communities, 2001, p. 9). Information costs can be lowered (Grosskopf, 1994, p. 861) and in that way an "... additional layer of knowledge and learning..." will have been introduced between member businesses and the markets (Schreiter, 1994, p. 332). Although knowledge remains with the members, thus decentralized, it is still accessible to all and available for coordination. The special trade-off between common and individual knowledge of potential competitors frequently lies at the root of many comparative advantages of cooperatives versus other business organizations and public bodies.

Cooperative social capital, which in general is usually instrumental in achieving a heightened flexibility and adaptability to changing market situations (Crooks, Spatz and Warmann, 1995, p. 4), can substitute partly for complex governance and costly reporting and sanctioning mechanisms. It also has a significant role in inspiring innovation, diversification and specialization in members' enterprises, something particularly interesting to many SMEs in industrialized countries (Göler von Ravensburg, Pinkwart and Schmidt, 2003, p. 30). It may also be responsible for the success of many entrepreneurs' cooperatives for professionals and those in service industries<sup>17</sup>. Its economic effectiveness may be much enhanced by supporting management development among members, by creating

The development of entrepreneurs' cooperatives of professionals and SME rendering services is relatively recent, even in industrialized countries. Thus there is virtually no research on the specifically cooperative economics in these fields. Also there is virtually no research as yet on the effects (positive and negative) of integration of enterprises in developing countries into global value chains by means of whatever organizational form of cooperation (also see Morrison; Pietrobelli; Rabellotti, 2006, esp. p. 19).

common training and research capacities and programmes. Sometimes cooperative social capital may be harvested for vertical integration of product chains. If information is shared both ways between members and their cooperative enterprise and if the levels of mutual trust are high enough, interdependent investments become possible and productive for the common good.

### **Example 3.4: VINZ Co-operative, New Zealand**

"The VINZ Co-operative is a Transport Services Delivery Agent (TSDA) of Land Transport New Zealand (Land Transport NZ). Our services include Vehicle Certification (used vehicles); ... Motor Registration and re-licensing. Our partners operate as "one stop shops" for Entry Certification.

Ownership of a co-operative generally comprises people or organisations with a common interest. Members share the economic benefits of the operation by way of reduced costs and returns on shareholder investments."

Source: http://www.vinz.co.nz/about.html (14 Oct. 2008)

In developing countries and countries in transition however, the greatest achievement of entrepreneurs' cooperatives might be that they concentrate on the socio-economic needs of the members, their economic integration, and thus frequently pave the way for them to move into a monetary market, into a non-local market or even into exporting for the first time. Entrepreneurs' cooperatives create options which did not exist before. Examining the activities and functions by which they do this, using value chain analysis, may provide insights into specific potentials not yet explored.

In Summary: Members and enterprises can benefit from cooperation

through economies of scale in production, leveraging in buying and selling, economies of scope for diversification and lengthening the value chain, creating significant transaction cost savings and informational advantages. However, a combination of value chain analysis and new institutional economic analysis helps to clarify that production cost savings alone are not sufficient to justify cooperation in entrepreneurs' cooperatives. Only if the production costs can be lowered to such an extent that they outweigh increased coordination costs and if framework conditions do not impose artificially high organizational costs, any specific kind of entrepreneurs' cooperative will be successful. To quantify coordination, organizational and production costs objectively and to react accordingly is especially important in cooperatives since members can choose to vote with their feet (i.e. leave the cooperative), if their individual value gain is impaired or not improved.

Table 3.3: Cost reduction in developing and industrialized countries

Cost reduction in fields	Percentages of cooperatives in developing countries	Percentages of cooperatives in industrialized countries
Transport	14.29 %	11.76 %
Input	11.43 %	20.59 %
Distribution	11.43 %	11.76 %
Purchasing	2.86 %	55.88 %

These figures show the percentage of cooperatives which claim to achieve cost reduction for their members in four categories.

### 3.3 Social and other benefits most frequently cited<sup>18</sup>

Systematically assessing the social and other indirect effects which entrepreneurs' cooperatives might have is rather difficult<sup>19</sup>. Firstly that

Please also see Appendix 1: Benefits in hermeneutic literature (p. 168).

<sup>19</sup> Consult Göler von Ravensburg (2007, p. 40-42) for historical explanations as to why that is so for cooperatives in developing countries.

entrepreneurs' cooperatives exist in a certain locality or branch may or may not be related to specified social improvements. Secondly, entrepreneurs' cooperatives are started by members for their common good and if third parties experience social and other benefits, these parties are not obliged to publish their experiences. Thirdly, where entrepreneurs' cooperatives are promoted with the intention of producing social and other effects for the community at large, the circle of beneficiaries is often so vaguely defined that evaluation of the effects is hampered by uncertainty. To some extent the creation of employment is an exception to this, so this will be dealt with separately (see Chapter 4).

It is of no surprise, therefore, that we cannot find one reliable empirical study on social and other effects of entrepreneurs' cooperatives. There are some interpretive and even a few theoretical papers, which comment on the social and other benefits created by cooperatives in general, by SME cooperation of various kinds and even by entrepreneurs' cooperatives. Some of the interpretive literature on cooperatives tends to stress their special democratic features and their deduction is that cooperatives automatically have certain social and other effects. By contrast, other interpretive literature, particularly that addressing SME cooperation, and some more theoretically based papers on cooperatives, seem more inclined to view these effects produced by cooperatives

### Example 3.5: ArchiTeam, Australia

ArchiTeam is a cooperative established as a support network for architects in small practices. It provides a range of services including professional development, monthly bulletins and an insurance package, as well as providing information to the public about architectural services. It also identifies among its members the architect whose professional abilities enable him or her to satisfy best the requirements of clients in any particular project.

Source: http://www.architeam.net.au (14 Oct. 2008)

simply as side effects of their main endeavours. Economists call them 'positive external effects' and believe that they only occur if entrepreneurs' cooperatives are economically successful. Economists do not deny, however, that these external effects can be enhanced if members and concerned role players outside the entrepreneurs' cooperatives have a specific interest in promoting such benefits (Göler von Ravensburg, 1998, p. 26-27).

We now look at examples of literature from approaches concentrating on both industrialized and developing countries.

#### 3.3.1 In industrialized and transition countries

Writing for the US Department of Agriculture, Jenkins *et al.* (2007, p. 6) list an impressive number of social and other benefits which they see arising from SME cooperation regardless of the legal form adopted: These benefits include:

- stimulation of economic activity and enhanced local economic development;
- increased production and employment;
- long-term increase in local or regional competitiveness;
- additional local purchasing power;
- access to more affordable, reliable, or better quality products and services;
- increased possibility for large-scale companies to participate in local business and community development;
- balance of payment benefits when products are exported and/or substituted for imports; and
- development of local business service providers catering to SMEs.

It is relatively straight forward to relate this list directly to the

## **Example 3.6: Seminole Electric Cooperative, Inc., USA**

Seminole Electric is a generation and transmission cooperative. It was incorporated in 1948 to give a group of Florida electric distribution cooperatives buying clout, by aggregating their demand. Today Seminole helps its member systems lower their wholesale costs by the providing a flexible mix of owned generation and purchased power contracts. More than 1.6 million (18.8 million in Florida) individuals and businesses rely on Seminole's Member Systems. It is one of the most important electric suppliers in Florida and the second largest electric cooperative in the USA.

Seminole's values statement includes a commitment to "improve the quality of life in our communities". Community service is an important aspect of that commitment.

**Source:** http://www.seminole-electric.com (14. Oct. 2008)

economic activity of entrepreneurs' cooperatives. Similarly (but a little less stringently) appear the social and other benefits espoused for entrepreneurs' cooperatives in the USA by Bhuyan (1996, p. 3-5) (who also speaks of "quality of life") and Crooks, Spatz and Warmann (1995, p.3) (talk of opportunities to meet to discuss problems and topics of mutual concern). Crow (2006, p. 3) highlights the professional ethos, alternatives for the consumer and new ways to fund and govern publishers for federations, unions and employers' associations. He relates less to social and more to sector benefits. Doherty (1997, p.1) underlines the points that women can gain business experience in entrepreneurs' cooperatives, and communities gain access to services not provided otherwise because of major overhead costs or withdrawal by the state. The British Columbia Cooperative Association (2007, p. 2) in Canada adds "transparency and accountability" as well as "strengthening ties and loyalty to local communities" and emphasizes the potential for creating employment.

The stance taken by the European Commission in its Consultation Paper of 2001 on "Co-operatives in Enterprise Europe" is closely related to macroeconomic facets, if perhaps in a little broader sense than that of Jenkins listed above. Although the publication does not address entrepreneurs' cooperatives alone, particular attention is given to entrepreneurs' cooperatives in that the EU hopes for correction of market failures, more market power for SMEs, more stability for particular regions or sectors or at least some cushioning from structural change as well as the maintenance of social capital due to democratic governance and economic participation (European Commission, 2001, p. 24).

Furthermore there is also the expectation that cooperatives will contribute their share to the balanced development of the economies and societies of the accession countries in three ways (European Commission, 2001, p. 26-27), namely:

- first by acting as important vehicles in modernising these economies, bringing the benefits of the market to a wider range of citizens;
- second to be an effective and appropriate way of providing for the spectrum of unmet need generated during the period of transition;
- third by providing "schools of entrepreneurship" for many citizens who would not otherwise have the opportunity to gain management experience.

On a more socially related note the Consultation paper is convinced, that:

"Cooperative enterprises tend to be very sensitive to their social responsibilities. Their first responsibility is naturally towards their members, but their decentralized and democratic nature means that they are firmly rooted in local and regional communities. Their decisions are therefore more likely to take into account these interests than in a company where returns on capital are the primary concern." (EC, 2001, p. 7)

In 2004 the European Commission adds to this: "Such strong local roots can be an effective counter to the desertification of rural areas and assist the development of poorer regions and localities." By this, the European Commission finally makes it quite clear that it sees cooperatives (and with it entrepreneurs' cooperatives) as ideal engines for sustainable local and regional development.

### 3.3.2 In developing countries

Münkner (2000b) is not alone when he believes that cooperatives in general seem to be returning to the development agenda. Commodity cooperatives have developed wide international trading links<sup>20</sup> and many micro-credit schemes work cooperatively. In the last few years entrepreneurs' cooperatives have been "rediscovered" particularly in some Latin American countries as an element of the social economy. In such countries the social economy is favoured by governments in order to compensate for real or feared losses of economic and social self-determination in the wake of globalization (See for example Sibal, 2000; Lebovitz, 2006; Schwettmann, 2006). Even so, where no state supported social economy exists, the discussion of the relevance of cooperatives to poverty has new impetus (See for example DGRV, 2006; Imoisili, 2001). The relevance for entrepreneurs' cooperatives, as we have seen, can be important because they occur all over the world and their constituency and membership is all-embracing.

In general, the literature coming from or relating to developing countries tends to have wider and more diverse expectations for social and other benefits that can be achieved through cooperatives. But not always<sup>21</sup>

<sup>20</sup> http://intergroup.com/ (15. Nov. 2007).

<sup>21</sup> We do not know however, whether the new popularity cooperatives

does it state explicitly on which reasons it postulates such effects. Many previous authors, papers and case studies, formal and informal, have helped Parnell, Couture, Birchall and various ILO authors to form views on the social and other benefits which can be expected of (cooperatives and) entrepreneurs' cooperatives in developing countries. Most empirical and hermeneutic literature, however, does not permit a strict differentiation between the developmental effects of cooperatives in general and those of entrepreneurs' cooperatives in particular. We indicate when statements relate to, or have natural implications for entrepreneurs' cooperatives in particular, but arguments are mostly geared towards cooperatives in general.

According to Parnell (2001) entrepreneurs' cooperatives have a role to play even in crisis resolution and socio-economic recovery. He lists a number of positive effects that they can have on crisis-ridden communities (Parnell, 2001, p. 30-31) by their capacity for advocacy,

### **Example 3.7: Prainha do Canto Verde, Brazil**

"Prainha do Canto Verde" is a cooperative, promoted by ASHOKA in Fortaleza, Brazil, which organizes Eco-Tourism and Fair Trade for several village communities under its leadership. The cooperative also comprises a Fishing Cooperative for direct sale without intermediaries.

**Source:** http://www.todo-contest.org/preistraeger/prainha01.html (14. Oct. 2008)

and with them entrepreneurs' cooperatives have been gaining in some countries in recent years can be attributed to this – See for example *Lebovitz* (2006, p. 2): Apparently in Venezuela the number of cooperatives increased from under 800 when Chavez was first elected in 1998 to almost 84,000 by August 2005. Also *Sibal* (2000): the number of cooperative in the Philippines raised 7.5 fold from 1975 to 1993.

reduction of vulnerability and the facilitation of change. He is also convinced that entrepreneurs' cooperatives in particular can:

- be deployed to re-establish economic activity in areas which have been ravaged by war or catastrophe;
- form a defence against the flight of capital at a time of financial downturns, providing and supporting local employment and SMEs;
- assist to resettle returning refugees and reintegrate excombatants into tradesmen and artisans cooperatives; and
- help protect natural resources and prevent environmental degradation.

Parnell (2001, p. 36-37) repeats that he sees entrepreneurs' cooperatives among other cooperatives as "developing locally owned enterprises as a defence against the flight of capital in the case of financial downturns."

### Couture (2003, p. 43) stresses:

- access to government financial support for housing, health, education and welfare needs;
- access to information;
- pooling of expertise and collaboration, training and education; and
- access to other associations, social recognition and new social relations/networking.

She thus concerns herself more with the secondary effects that entrepreneurs' cooperatives can have in local communities than with their effects on economic sectors.

Report V(1) by ILO (2000, pp. 45-47) concentrates on:

- the alleviation of poverty;
- the mitigation of hardship resulting from transition from centrally planned to market economies and related structural adjustments;
- the provision of an effective base for differing disadvantaged groups to organise themselves for social and economic benefit;
- the re-integration of marginalized groups, the provision of services previously offered by the state; and
- possible contributions to environmental conservation.

Interestingly enough, ILO Report (V) 1 also gives cooperatives (and with it entrepreneurs' cooperatives) a role in social peace keeping (ILO, 2000, p. 61):

"By defending the interests of their members, cooperatives defend at the same time the interests of certain groups of the population (...). They demonstrate to the general public that economic activities need not necessarily be directed to maximize profit and shareholder value, but can also be need-oriented, improving the quality or reducing the price of goods and services."

It even calls them "... schools of democracy .... practice participation in and democratic control of goal-setting and decision-making processes" (p. 62). In 2003 the ILO specified the way that cooperatives (and by implication entrepreneurs' cooperatives ) can aid poverty alleviation (ILO, 2003, p. 10):

"... combat poverty in three ways: they empower people by enabling the poorest segments of the population to take action; they create job opportunities for those who have skills but no capital; and they provide protection by organizing mutual help in communities." ... "Several

countries reported that cooperatives were an effective approach to poverty reduction in the agricultural sector and the informal economy..."

Based on a Shoe Shiners Cooperative in Uganda, Birchall (2003) points out the following development effects for entrepreneurs' cooperatives:

- poverty reduction;
- the promotion of women;
- the prevention of rural-urban migration, rural diversification;
- improved use and control of local resources;
- capacity building; and
- their special potential to open markets including export markets (Birchall, 2004, p. 46).

He also shows in a case study another economic inequality that needs to be taken into account (Birchall, 2003, p. 40), namely the gender issue and especially that between men and women in the same household.

Birchall (2003, p. 4) believes that all cooperatives produce social and other effects as they are

"... open to new members, do not require people to invest large amounts of capital, and tend to share economic results equitably, they have an automatic tendency to benefit the poor".

We support Birchall (2003, p. 4) fully when he points out:

"However, this potential may not always be realized, either because members lose sight of the needs of other potential members, or because those concerned with poverty reduction see cooperatives as tools rather than as autonomous organizations."

### **Example 3.8: Modis International, Rwanda**

The members of Modis International are groups of artisans, cooperatives and women's associations producing handicraft products. This is their main source of income and provides them with the most basic necessities – food, clothing, shelter and education.

Modis International began by collaborating with two women's cooperatives developing marketable products for them. Today it is working closely with 15 associations and cooperatives comprising nearly 1,000 women and young people who depend on this sector for their livelihood. Some groups and cooperatives of Modis International were organised by orphans of the genocide of 1994. Another one was begun by widows who came together to make a sustainable living as well as for companionship and solace. Nine years later this association alone has grown to more than 600 members and their activities now include embroidery, tailoring, basketry etc.

**Source:** http://www.modishandicrafts.com (22.Feb. 2008)

In this context Birchall expresses his astonishment that neither the World Bank nor the International Monetary Fund fully seem to recognize the positive developmental effects of cooperatives<sup>22</sup>. This may be for several reasons, including:

- the relative scarcity of internationally comparable empirical research<sup>23</sup>;
- the difficulties in understanding the available research;

According to *Birchall* (2004, p. 49) only Poverty Reduction Strategy Papers (PRSP) refers to an entrepreneurs' cooperative, namely the SEWA women's organization.

Up to now, the development effects of cooperatives can best be recognized in direct relation to the local and regional level.

- the ideological arguments which have long obscured the discussion; and
- in many countries cooperatives are out of favour with governments and thus get no official recognition.

The last two points are not easily changed and it can only be hoped that in the not too distant future trade unions, women's groups and direct representatives of the poor will be involved more than they are now in the drafting of national poverty reduction strategy papers (PRSP) (Birchall, 2004, p. 50). But even then the development and especially the propoor potential of cooperatives and entrepreneurs' cooperatives will not easily be realized or harnessed. For one, the design of participation processes is still at the discretion of governments, which need to be encouraged to reach out to traditionally marginalized groups. There also needs to be more well-based research to argue the case for all the benefits of entrepreneurs' cooperative activity. What would be a systematic approach to determine the developmental potential of entrepreneurs' cooperatives under these circumstances?

Often the development contributions of cooperatives are categorized as political, social and economic contributions. But these are artificial distinctions, not easily maintained, nor helpful in the design of, or the justification for, realistic development and promotion policies. Rösner (2001, p. 439) points to mistakes in promotion of cooperatives which happened because of attempts to attain either political, economic or social change. However, if the purpose in analyzing the cooperative potential is to contribute to the development of adequate external promotion efforts, and developmentally efficient entrepreneurs' cooperatives, the categorization into governance-, structural and procedural policy effects, used by Rösner in his instructive article in 2001 does not help much either. We believe that the categories of micro- and macro-effects first introduced by Hanel (1992, p. 104-110) and implicitly followed in the above are more helpful with regard to policy development.

### Example 3.9: Machakos, Kenya

Machakos district cooperative was established in 1964 originally to market coffee for producers in the Machakos area. It has since been expanded and now represents a variety of "cooperatives" which produce agricultural and handicraft products made from local materials such as sisal, soapstone and especially wood. The Machakos cooperative also backs some environmental projects. In 2000 a tree nursery was started which plants, grows and then provides seedlings to wood carvers working in the cooperative. In this way it makes a substantial contribution to reforestation and thus to the preservation of water supply to the area.

Source: http://www.mdcultd.org (22. Feb. 2008)

The following concentrates on those "external" effects which entrepreneurs' cooperatives are generally expected to have and which are positive for development. Other opinions are possible, just as entrepreneurs' cooperatives can, under certain circumstances, also provoke unwanted consequences, such as when they monopolize a market to such an extent that competitors are hindered from entering<sup>24</sup>. However, this is an issue of anti-trust controls rather than a theme in the design of development policy. We deal with it at a later stage when promotional strategies are discussed.

From an economist's point of view, two sets of expectations of cooperatives are worth examining: their socio-political and socio-economic potentials.

The expectations of cooperatives to contribute positively to the sociopolitical development of a region or nation usually centre on their

Evolutionary economics, however, suggest that innovation produces continuously new balances and imbalances in markets which in turn render lasting prohibitions to market entry improbable (Fehl, 1997, p. 98; 1996/2004 p. 320).

assisting (Hanel, 1992, p. 107):

- in the acceleration of social change;
- socially weaker population groups;
- democratization by providing a platform for participation;
   and
- to bridge dual economic structures, e.g. between formal and informal, modern and traditional.

### **Example 3.10: Yuri Enga Enterprises, Ghana**

Yuri Enga is a cooperative of the shea butter producers and basket weavers in Ghana. The cooperative has 1,200 members, most of them women. The region is very poor, the unemployment rate is very high and it is almost impossible to find a job. Eighty per cent of women in the region must not only keep the house but also earn the family's living. Most of the families are living from subsistence agriculture. Basket weaving and production of shea butter in the cooperative created jobs and therefore generated earnings for the women and their families. Money earned in the cooperative is mostly used for health care, education and other essential purchases.

**Source:** http://www.yuri-enga.com/index.htm (14. Oct. 2008)

Cooperatives can fulfil these expectations only if they are operationally efficient and satisfy their members' needs, which in turn is possible only if they do not face framework conditions which go against true self-help (Kötter, 1994, p. 796).

The same applies to the generally expected effects of macro-economic development (Hanel, 1992, p. 107):

increases in (regional but also national) gross product;

- growth of exports or substitution of imports;
- a slow but gradual change in the minds of small farmers and entrepreneurs so that they learn to appreciate and use resources more productively and profitably, access new resources and – given there is proper division of labour and specialization – can move from traditional work patterns to market integrated production, therefore overcoming preindustrial dualisms in economic and social structures;
- the development of an entrepreneurial middle class;
- an improvement of economic and technical infrastructure

## **Example 3.11: Encouraging inclusive development**

"Poverty reduction strategies that assume that economic power and opportunity stops at the household unit ignore the real power differential between men and women. Most farmer cooperatives are owned and controlled by men. Whether the economic benefits that flow from cooperation reach the rest of the household is an empirical question. In cases where the women of the household do not have access to paid work outside the home and they do not have an independent income, it is necessary to foster women's cooperatives. This might be as a first stage in farm organization where there is none, or it might be in parallel to farmer cooperatives that already exist. Another strategy might be to try to open up existing cooperatives to women's influence. In Japan, the formation of han groups at a more local level than the formal cooperative, but linked to it, shows that this is possible. However, in Japan it is also the case that changes in landholding patterns mean that more women are achieving the status of 'farmer' independently of men".

**Source**: Birchall, J. (2004, p. 40)

(Rösner, 2001, p. 442) because cooperatives seek to:

- bring members closer to markets and empower them economically;
- widen markets for their members;
- o serve as market substitutes for their members or help create new markets (Hanisch, 2006, p. 306-309);
- decouple interlinked markets (e.g. between credit and marketing of produce); and
- o support the market power of members (Eschenburg, 1984, p. 317-331).
- secondary structural effects such as getting beyond subsistence production, better supplies for consumers and the adoption of technological improvements;
- improvements in social infrastructure:
  - by way of improving the professional and social integration of minorities through education and training (e.g. in "environmentally friendly tourism"); and
  - o by way of complementing patchy or non-existent systems of public welfare and risk reduction through cooperative services (Rösner, 2001, p. 443).
- the creation of public services where or when the established public sector cannot (or will no longer) finance them, and private firms do not provide them. Cooperatives can fill the gap while increasing (local) levels of trust and aiding market transparency (Eisen, 2004, p. 2);
- implementation of environmental and quality standards in food production by transferring "cooperative knowledge" to agricultural and entrepreneurial members. These standards have become a central bottleneck in national marketing through supermarket retail chains as well as with export (Wollni and Zeller, 2007); and

• the increase of business assets (both material and immaterial) by integrating members with weaker potential for income growth and asset endowment into regional, formal and informal financial markets<sup>25</sup>. In the long run this action serves to stabilize positive income and purchasing power (Hartmann, 2004; Göler von Ravensburg, 1998, p. 186; Koch, 1986, p. 15).

Cooperatives can produce such development only if their business environment is structurally conducive and development minded (See for example Hanel, 1981, p. 108 and p. 148; Baldus et al., 1981, p. 4; Münkner; Baltes; Gamm, 1992, p. 27; Koch, 1986, p. 83). In the first instance, economic development should be seen as a process started and maintained by private organizations and companies and not by governments or foreign donors (Paul and Dias, 1982, p. 9; Röpke, 1992, p. 23). This in turn means that the focus needs to be:

- 1. on the micro-economic (direct) concerns of cooperatives; and
- 2. on the relevant policy and legal frameworks.

That is why Röpke's (1994, p. 256) scepticism with regard to cooperative promotion needs to be taken seriously.

For instance, the ILO's Promicro programme in El Salvador has promoted associations of small-scale operators along with micro-finance institutions.

## Chapter 4

## **Employment effects**

The ability of cooperatives to create high quality sustainable jobs and improve employment conditions is increasingly being recognized (See for example Commission of the European Communities, 2001, p. 24-26; 2004, p. 15; Bhuyan, 1996, p. 5-7; British Columbia Cooperative Association, 2007; Couture, 2003, p. 43; International Labour Office, 2000, p. 45; 2003, p. 10). However, as with the development effects of entrepreneurs' cooperatives, there is little empirical research on their direct and indirect effects on employment. A scan of entrepreneurs' cooperatives on the internet revealed that very few claim that they produce jobs or increase opportunities for employment among members' enterprises as a result of the cooperative's activities<sup>1</sup>.

Yet the potential is surely there. For example, Couture (2003, p.43) documents that entrepreneurs' cooperatives contribute to:

"... job creation and maintaining employment, and thus to social and economic well-being in their region. Given stiff competition and liberalization, the survival of SMEs is precarious and hence a lot of jobs are constantly at

Only 10 of the 69 entrepreneurs' cooperatives identified claim that they generate employment effects, see **Appendix 3** (p. 179).

risk. Joining an cooperative may mean survival for an SME and consequently the jobs may be spared. Similarly, an SME that increases its volume of trade by joining a CBA may generate employment. In public services, where members are, for instance, health or education services, the same tendency towards job creation can be found.

The level of employment in a population directly affects the community's economic and social development. Having an income means that the standard of living improves, and the region's economy is boosted."

### **Example 4.1: Akamba Handicraft Industry Cooperative Society**

By economically empowering 2,902 entrepreneurs, who in turn employ approximately 3,000 people, the AHICS in Kenya plays a key role in promoting the economic vibrancy of its community. Besides making a direct contribution to creating some 5,000 jobs, it indirectly helps several entrepreneurs who have set up small businesses such as bars, restaurants, clothes sellers around the cooperative to meet members' needs. Therefore, the AHICS is not merely a tool for development that serves its members, but it also serves the wider local community.

**Source:** Couture, 2003, p. 43

The *Commission of the European Communities* (2004, p. 15) sees cooperatives as member-based organizations, which are rooted in local communities, and gives them credit for maintaining local jobs and local services in the context of economic globalization.

In the context of the social economy, Schwettman (2006, p. 5) points

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"According to the overall economy of 36 countries studied by the John Hopkins Comparative Nonprofit Sector Project<sup>2</sup>, "the non-profit sector outpaced the overall growth of employment ... by nearly 2.5 to 1. " Fair-trade certified coffee is the fastest growing segment of the speciality coffee market and makes up about 2 per cent of the world market. In 2003, 18.5 million pounds of green coffee were fair-trade certified with a value of USD \$208 million in retail sales. This represented a 90 per cent increase in one year (Develtere and Pollet, 2005). Between 1990 and 2004, employment in European cooperatives rose from 2.2 million to 5.4 million. Employment in the Italian social cooperatives is growing by 10 per cent per year<sup>3</sup>. The French Entrepreneur Cooperatives have increased their market share from 10 per cent in the 1960s to 25 per cent in 2005. A study carried out in eight European countries between 1995 and 1998 showed that employment in associations had been growing in all but one of country, while employment in foundations grew between 2 per cent and 13 per cent in each of the eight countries."

Frequently however, the quantitative employment effect of entrepreneurs' cooperatives cannot be extracted from the records. The EU for example, by including cooperatives together with the wider social economy in the mainstream European Employment Strategy and the Guidelines for the National Action Plans (NAP) for employment, asks their Member States to report on social economy initiatives under the Entrepreneurship pillar 22. This makes separation of SME cooperatives impossible.

<sup>2</sup> http://www.jhu.edu/cnp/compdata.html (22. Feb. 2008).

<sup>3</sup> See article on "cooperatives" in www.wikipedia.org.

For this reason the discussion of employment effects is limited to a qualitative one. This chapter therefore considers entrepreneurs' cooperatives potential to:

- increase or maintain employment;
- provide decent work.
- provide representation in the informal economy.

### 4.1 Entrepreneurs' cooperatives and employment creation

On its website<sup>4</sup>, the ILO summarizes cooperatives' potential to create or maintain jobs to be the result of increased economies of scale and scope, increased bargaining power of the members, active member participation and provision of benefits such as representation of interest, organizational stability, innovation and legal protection.

Current research on the direct effects of entrepreneurs' cooperatives on member businesses<sup>5</sup> suggests that entrepreneurs' cooperatives have a special potential to boost the self-employment opportunities of their members and a tendency to favour labour-intensive production processes. They can stabilize businesses and turnover of independent trades people or professionals because they contribute to some risk sharing between members. Risk sharing and innovation gained from cooperation helps to maintain and increase the number of jobs available. It also stabilizes employers' potential to pay decent wages and fulfil additional responsibilities towards their employees, such as provision of social security.

The most promising areas where entrepreneurs' cooperatives could provide entry points for increasing both the quality and quantity of employment include organizing enterprises in the informal economy into entrepreneurs' cooperatives.

<sup>4</sup> See http://www.ilo.org/coop

<sup>5</sup> See chapter "Current state of research" (p. 21).

## **Example 4.2: Poverty and insecurity in Africa**

"Three hundred million Africans alone live in extreme poverty. This tragic waste of human potential is caused by unemployment, underemployment and low productivity in existing jobs, particularly in agriculture and in the urban informal economy – the main source of employment in most African economies. Africa has the world's highest rates of open unemployment and youth unemployment. Women's unemployment in all categories is significantly higher than the national average. In most sub-Saharan African countries, wage employment occupies only between 6 per cent (landlocked countries in West and Central Africa) and 25 per cent (southern Africa) of the active population. In other words, 75 to 94 per cent of the active population is either unemployed or ekes out a living in the rural or informal economy where they work in precarious economic activities, without any social protection - often in an unsafe working environment. The fact of the matter is that African women and men are obliged to do any work they can get, no matter how insecure, no matter how badly paid, to be able to feed their families."

**Source**: ILO, 2003, p. 1

## 4.2 Organizing the informal economy

Not only in Africa, but in large parts of the world, employment creation, both in the formal and informal parts of the economy, is one of the best ways to help people and nations to develop. To organize business, people in the informal economy cooperatively represents an indirect approach to employment creation, as it creates job opportunities for those who have some skills but little capital.

On its website, the ILO emphasizes that the cooperative form of organization enables independent entrepreneurs and workers in the informal economy to carry out joint economic activities at reduced costs. The 2003 Africa Conference on "Working out of poverty" argued, in this context:

"Many participants underlined that most economic (nonfarm) activities in Africa were carried out by small and micro-enterprises in the formal or the informal economy. However, the low level of productivity and income, and the precarious nature of some of these businesses, generally resulted in unstable employment relationships and in poor living standards. In order to improve the situation, the participants felt it was necessary to:

- establish policies and a regulatory and legislative environment that would stimulate enterprise growth and development, thus encouraging enterprises to start-up, grow and create jobs;
- nvest domestic savings in enterprise and job creation;
- facilitate access to product markets, capital, training and information;
- provide education, training and efficient business development services as indispensable ingredients for successful entrepreneurship."

As pointed out in Chapter 3, all these functions can be performed by entrepreneurs' cooperatives. Schwettmann (2001, p. 16) is convinced that:

"In addition to creating employment, cooperatives and group-based enterprises have the potential to broaden the social dialogue, because they constitute representative organizations that cater for the interests of both unprotected workers and informal economy employers. In fact, such

# cooperative enterprises build a bridge between the informal economy and the formal economy."

In some developing countries trade unions have supported the formation and development of entrepreneurs' cooperatives in the informal economy (Birchall, 2001, p. 6-8; ILO, 2001b, p. 5). At an international level, the trade unions associated with the ILO backed the revision of the Promotion of Cooperatives Recommendation (No.127) in 2003. This provides an important demonstration of solidarity, which paves the way for greater collaboration between the two movements.

The endorsement of the ICA Board in April 1999, of the ILO Declaration on the Fundamental Principles and Rights at Work was another important statement of intent and could contribute significantly to the continued dialogue between the movements. Furthermore, the World Confederation of Labour (WCL) suggests that its affiliates develop a two-pronged strategy to support increases in the quality and quantity of employment in the informal economy, namely support formation of 1) trade union structures and 2) cooperatives. The role of cooperatives in the informal economy would be to increase capacity through economies of scale and increase sustainability through sharing of risk. Improving the economic viability of enterprises should go together with improving employment quality (Birchall, 2001, p. 24).

Trade union and cooperative spheres of activity cannot always be separated so clearly. When looking at trade union support for cooperative activities in the informal economy, the most persistent and successful strategies so far have been associated with the organization of women, either in a sub-sector such as home working or in the sector as a whole.

In 2001 the ILO drew attention to one more important point:

"Despite the importance of informal economy enterprises in many countries, they effectively have no voice in employers' organizations, although it is in the interests

of everybody, not least the formal sector enterprises, that productivity and purchasing power increase in the informal economy so that it can contribute more to the national economy and deepen the market" (ILO, 2001, p. 69).

### **Example 4.3: Assetamorwa**

In Kigali, the capital of Rwanda, the costs of entering the private transport industry are prohibitive. For many the only option is to lease motorbikes from local entrepreneurs at exorbitant rates, which does not even allow the entrepreneurs to reach the one-dollar-a-day poverty line.

Assetamorwa is one response to this situation. It is a cooperative of motorcyclists in Kigali, which has more than 2,500 members. The cooperative runs a common garage and repairs motorcycles. It has a common fund of money, which enables it to purchase new motorcycles or to give consumer credit to the members. For a group of people who were previously unorganized and working in the informal economy, Assetamorwa is a considerable achievement.

Each of the motorcycle taxi drivers is an individual trader, but they support each other and negotiate together with the authorities. In return the cooperative helps the authorities to organize and keep city traffic in order. Establishing the cooperative has also given members a better chance to protect themselves against crime on the dangerous streets of Kigali.

**Source**: http://www.rwandagateway.org/article.php3?id\_article=2769 (14. Oct. 2008)

Entrepreneurs' cooperatives need to be considered in the context of the global challenge of reducing the "decent work" gap.

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## 4.3 entrepreneurs' cooperatives and decent work

Two things threaten people's access to decent work. Firstly, economic growth does not always create new jobs. Secondly, employment opportunities may not reach the poor if they do not have the skills needed or are prevented by more powerful groups from entering the formal labour market. Yet, employment with decent remuneration is a good way to leave poverty behind (Birchall, 2003, p. 26).

How can decent working conditions be established and maintained in a world where the poor have no common voice? In a world where labour intensive production is in decline and where companies can locate or relocate production more or less freely, investing and withdrawing investments in ever shorter time spans? The goal of "decent work" stands for economic growth with social equity as proclaimed by the ILO and all its constituents, with the backing of the UN. The question is how can synergies for decent work be created in today's globalized world and which institutions can help to create these synergies?

Schwettmann (2001, p. 16) believes that:

"because of their democratic, voluntary and community-based nature, cooperatives and similar SMEs lay much emphasis on the quality of employment, and on satisfactory conditions of work. They have thus the potential to contribute to the achievement of the decent work objective upon which the ILO is based".

Birchall (2001, p. 39) supports him in this, and points to the possibility for cooperatives to play a role in strengthening social dialogue and the attainment of "decent work" goals because cooperatives are acceptable negotiating partners to unions, employers' organizations and governments. He repeats this in 2003 (2003, p. 29) with regard to one of the ILO's pillars of decent work, namely the strengthening of social dialogue. He explains that governments see cooperatives as

### **Example 4.4: Unions cooperating**

There have been many cases where unions, cooperatives and associations have worked together to open up access to markets and provide skills training. For example:

Cote d'Ivoire: In 1990 a National Union of Informal Sector Women (SYNAFSI) was created with help from the national trade union centre DIGNITE. The initiative provided access to training and equipment as a first step to supporting the establishment of buyers' and sellers' cooperatives for women.

**South Africa**: The National Union of Mine Workers is unionizing small-scale miners and sponsors an agency to assist retrenched miners. Similarly, the South African Self-Employed Women's Union (SEWU) provides a wide variety of services to meet the specific needs of women workers.

**Benin**: The cement workers union, SYNTRACIB, works with a women's association to provide training on income generating skills and access to markets through organizing women in 33 villages into cooperatives.

Source: Birchall, 2001, p. 26

non-threatening and essential building blocks of civil society (which is increasingly the case, as proven by a number of new legislative and policy initiatives), that employers see them as entrepreneurial business models (encouraging the development of markets in a number of ways) and that for the trade unions their attraction lies in the formal employment they create (with employees maybe becoming members of unions).

In the same publication (p. 27) Birchall also explains how he sees cooperatives contributing to the other three strategic objectives linked with the "decent work" concept. This being in the promotion of rights

at work and increases in employment and income, leading to greater social security. Although he refers to different types of entrepreneurs' cooperatives he believes that all of them strengthen the employees' human and working rights. Also that in creating alternative or increased incomes, they contribute to the abolition of child labour and bonded labour, increase labour and total business productivity and tackle adverse terms of trade. They do this by lowering the cost of inputs or improving the marketing possibilities of small craft persons, traders and professionals (Birchall, 2003, p. 28).

Birchall (2003) argues that entrepreneurs' cooperatives have the greatest potential to raise skills, open markets and improve working conditions in the informal sector. With regard to social protection,

### **Example 4.5: Innovation from cooperation**

"Save the Children has set up a project in the Philippines, an Alliance of Home-based Retazo workers in Metro Manila. It has two basic strategies: group-lending of microfinance and a women's micro-enterprise network. What is most interesting about it is that, instead of just responding to the needs of their members, they have gone out and researched their market situation. They have organized the bulk purchase of the raw materials needed (clothing remnants from the garment industry), at a saving of 15 per cent to their members and have tapped into new, more regular and secure markets among large companies. By analysing the markets first, designing a set of interventions that are sensitive to women's needs and can be expanded rapidly, they have provided real economic benefits to their members. With a membership of 25,000 workers in Manila and 50,000 nationwide, they are aiming to develop into a strong national institution to represent low-income women micro-entrepreneurs."

**Source**: Birchall, 2001, p. 26-27

Birchall (2003, p. 24) quotes Patel 2002 and points out that microcredit enterprises and cooperatives have proved to be effective in delivering publicly funded health and social insurance to very poor people:

"They are particularly effective in offering contributory insurance schemes in the informal economy, where they are the only organizations that can be trusted and have the organizational capacity to collect contributions and pay benefits."

## Chapter 5

## **Operational practices and problems**

The brief for this study includes an analysis of the practices and problems of setting up and operating entrepreneurs' cooperatives as means of development. Considering that the conditions faced by SMEs, craft persons, traders and professionals differ not only from one economic sector to another, but also with the legal, political and economic context, any conclusions arrived at in this chapter must be somewhat general. Still, knowing the huge development contribution entrepreneurs' cooperatives have made in Europe over the last 150 years, it is appropriate to identify both the "good practices" and the limits of cooperative entreprises.

An example of where gaps in the value chain of production and marketing have been addressed by cooperative action comes from Namibia. The producers wanted to increase the stability and sustainability of their position in the market. They did this by cooperating, which enabled them to add vaule to their primary products. Subequently, they have been able to offer their market a high quality product in a consistent and stable manner. What has worked there might be copied in other regions.

### Example 5.1: Namibia – women's marula oil cooperative

"In Namibia, following many years of struggle to achieve independence, which involved armed conflict, many communities suffer from the lack of income earning opportunities. In the North Namibian women's marula oil cooperative nearly 1,000 women belonging to nine community groups are extracting marula oil from the kernels of the marula plant. The oil is sold to a company that sells it on the world market as a beauty product. The overall goal of the project is to support the establishment and development of a secondary-type cooperative in the north of Namibia and to create a professional and sustainable marketing system of the members' production (and eventually processing) of marula oil."

**Source:** Parnell, 2001, p. 27

This case study illustrates that people start to cooperate if they can be fairly sure that the joint effort will generate benefits for their individual businesses. They also need to feel confident in the overall condition of the economy and legal framework. Support for development of entrepreneurial knowledge through external assistance can also helpt to biuld cooperation.

In developing countries, entrepreneurs' cooperatives might well be started with the assistance of "promoters" coming from government or non-government agencies. Usually the promoting agencies hope or expect that the new entrepreneurs' cooperatives will benefit their members in both the economic and social sense. Enhancing cooperative membership within markets - be it a local, national, or export market - can trigger an increase in productivity. Especially if accompanied by training in entrepreneurial and social competencies. Successful entrepreneurs' cooperatives in developed and developing countries necessarily support both.

Human resource development is necessary in most developing countries

before self-organizing and entrepreneurial management works. Ideally lobbying and negotiating skills, not only at the primary level but also at other levels of (vertical) integration, need to be developed. This will allow entrepreneurs' cooperatives to gain stature with external partners and may over time lead to gains in certain political and social aims (such as better social security or access to improved infrastructure).

## Example 5.2: Education and cooperation go hand in hand

"The main reason for cooperative failures was still the lack of education and training. This was revealed in more than 80 studies, which assessed the growth and development of cooperatives .... in the Philippines. Lack of education and training correlates with the following causes of cooperative failure:

- 1. Lack of capital;
- 2. Inadequate volume of business;
- 3. Lack of loyal membership support;
- 4. Vested interest and corruption among leaders;
- 5. Weak leadership and mismanagement; and
- 6. Lack of government support."

Source: Sibal, J.V., 2000

In order to be clear about the key features, practices and problems faced by entrepreneurs' cooperatives in developing countries, one needs to consider theoretical and empirical factors. This can help to provide an explanation of the critical internal factors that are necessary for effective development of cooperatives. Here it is necessary to differentiate the process of setting up cooperatives from sustainably operating them.

### 5.1 Theoretical perspectives on critical internal factors

Improving one's own business and income is usually the most important single motivator for members to cooperate.¹ Members (or potential members) mostly expect that the cooperative will supply them with services and goods in an effective and efficient manner (Hanel, 1992, p. 58),² at more favourable conditions and/or better quality than they could produce themselves or obtain from other sources (markets, public institutions or development projects).³ At any one time, the cooperative can only do so if (Hanel, 1989; 1992b):

- it is successful in the market by being operationally efficient (Bottomley, 1989, p. 45);
- it is member-efficient, in that it provides member-promotion (See for example Dülfer, 1979, p. 189; Boettcher, 1980, p. 48), enables members to participate in formulation of intent, decision-making and control of the organization (Hanel, 1992, p. 61);
- members accept that the relationship between their contributions and benefits is fair; and
- "free-riding" effects are avoided, in that no member can receive the same benefits as others without taking on the same responsibilities or producing the same contributions.

Over a period of time, members expect that their cooperative organization will:

See i.e. *Draheim, G.* (1955, p. 21); *Hanel, A.* (1981, p. 152); *Zörcher, J.* (1996, p. 80). For a discussion of other than economic motivations see *Brentano, D. v.* (1980). For an extensive discussion of possible motives to join or found a cooperative see *Chukwu, S. C.* (1990, p. 9-11).

<sup>2</sup> Effective in this context means the services and performances wanted; efficient means their competitive provision in time.

For details concerning individual considerations see *Röpke* (1992, p. 41) and *Röpke* (1992b, p. 23)

- push through innovations;
- change the institutional and normative patterns of the environment (property rights in the wider sense, including rights to act in a particular way);<sup>4</sup> or
- bring them closer to their aims, particularly when environmental conditions change to their disadvantage (Eisenstadt, 1968, p. 416).

The latter expectations point particularly to the role played by the individuals' property rights (in the more narrow sense), contractual rights, rights of access to productive factors, education and training, political participation and social security (Kötter, 1994, p. 797). While these rights are usually the rights of the individual, the status of these rights can influence the sociological and the psychological of the cooperative.

## 5.1.1 Organizing into a cooperative

It was primarily *Schreiter* (1994, p. 331) who showed convincingly that people's choice for organizing into a cooperative is significantly influenced by the way in which knowledge is distributed between the organization and the members' enterprises (See also Göler von Ravensburg, 1998). However, although cooperative organizations can usually use specific (member-owned) knowledge and distribute it effectively, restrictions on coordination can often not be overcome without the help of (external) promoters. Using such promoters can help to make sure that all this knowledge becomes available as a public good (Röpke, 1994, p. 257; Schreiter, 1994, p. 332; Göler von Ravensburg, 1998).

These cooperative promoters or "cooperative entrepreneurs" as *Röpke* (1994, p. 257) calls them, must be available in the first phase of the establishment of a cooperative self-help organization (SHO). It is

<sup>4</sup> For a definition see *Göler von Ravensburg* (1998, p. 275)

they who discover the transaction cost advantages (or other advantages which pertain to different, not yet sufficiently researched reasons) of the cooperative form, compared to other organizational forms. In order to do this they must be allowed to experiment freely and without too many bureaucratic or regulatory limitations.

In addition, they must be able and willing to invest in the initial needs of the organization, which relate to the undertaking of feasibility studies and communicating with prospective members. It is unlikely that they will be rewarded and they will face uncertainties about the success of their work. When the cooperative is up and running they may still have to share the results of their ideas with the other members. Sometimes future generations of members will benefit from his/her activity and often it will produce external effects, from which neither the promoter nor the cooperative will benefit directly. In addition, a cooperative promoter must overcome a belief that in society - if there are winners there MUST be losers - a belief which is prevalent at least in Africa (Göler von Ravensburg, 1998, p. 342; Bakhit, 1997, p. 238). If promoter-members attempt to keep some of the benefits accruing from their ideas and endeavours for themselves, it may generate an unequal distribution of surplus, risk a decline in member motivation as well as being seen to be corrupt.

Internal promoters with the necessary complex motivational disposition are rare to find, which is why we often talk of the "cooperative incentive failure". this is similar to the infant industry protection argument. This phenomenon is the main reason that justifies the provision of external promotion activities.

However, even if there are able and willing promoters, the founding of cooperative SHOs might be ill-fated. For example, if members cannot see the advantages of cooperating or they do not trust each other or the promoters. The first is dependent on the sector and production systems within which the cooperative is to operate. By interpreting the activities and production systems of the prospective members based on the

"theory of the efficient boundaries of a firm" (Göler von Ravensburg, 1998, p. 292), sector-specific potentials can be predicted somewhat reliably. The other two criteria are interlinked and are as much of an obstacle because the promoters are incapable of shattering them. To create the initial trust might prove more difficult for outsiders than for locals, but it can just as well work the other way around.

#### 5.1.2 The development of cooperatives

The lack of founding members or promoters does not represent the only obstacle to successful cooperative development. In the long run any cooperative might deviate from its member-orientation, losing support as it goes. This can happen because membership becomes more heterogeneous, professional management is effectively undermining member control<sup>5</sup> or non-members might obtain the same conditions as members (free-rider effects). Cooperatives can outgrow the formal structure, which members have given themselves at the beginning or their internal rules might turn out to be ineffective. In the course of time the incentive-contribution-relationship for the individual might change so that it is no longer attractive. Further, the cooperative enterprise might struggle to survive because of a lack of sufficient capital or capable management.

Any cooperative must maintain sufficient levels of member loyalty, solidarity and participation if it does not want to be paralysed. It is thus important that members are included in all ongoing processes of identification, definition and evaluation of organizational objectives. They also need to build capacity and main responsibility in driving appropriate change processes. In other words **members must determine** the direction of **organizational development** (i.e. Koch, 1986).

This being a general problem in all types of companies and organizations, cooperatives as hybrid organizations face a particular set of limitations with regard to the right balance between self-determination and the necessity for hierarchical leadership structures (see for example Hettlage, 1987, p. 285).

This could also help to alleviate another risk factor faced, especially by rural cooperatives in developing countries. Here, leaders are frequently elected according to their economic or political status (Koch, 1986, p. 63), which can, under certain circumstances, cause the set of organizational objectives to move away from the members' original objectives. If feedback mechanisms and effective sanctions for undemocratic behaviour or lack of accountability are missing, the promotional activity of the cooperative can, in extreme cases, even worsen inequality rather than eliminate it (Hettlage, 1987, p.298; Koch, 1986, p. 61).

Last but not least cooperatives must successfully establish their credentials in the outside world, creating as much external trust capital as possible. This is necessary to maintain low transaction costs. In a liberal economy, cooperatives cannot expect to be treated equally to other company forms by their commercial suppliers or clients unless they have put their name to the test.

#### 5.1.3 The need for structural formalization

Entrepreneurs' Cooperatives have a unique position when it comes to social and employment effects. Many of them have a relative advantage of mobilizing local resources and reduced transaction costs. Comparative analysis with non-cooperative joint ventures - such as trade associations, franchises and holding companies - shows that all cooperative principles are interlinked and their complete implementation is a precondition for maximum development effects (Göler von Ravensburg, 1998). This will commonly be achieved only in very few cooperatives and not all cooperatives that do achieve this are registered.

That said, the general term 'Entrepreneurs' Cooperative' encompasses all cooperatives, whether registered or not, which maintain cooperative principles (Hanel, 1992, p. 42). Registration as a cooperative, however, can serve the purpose of an external, independent institution assuring

that members are not being misled or exploited by management and protecting third parties, particularly in case of bankruptcy.<sup>6</sup> Meanwhile, autochthonous cooperatives, pre-cooperatives, SHOs as well as marketing, purchasing and protective associations of the informal economy (Hanel, 1992, p. 22) are a frequent phenomenon during the transformation from subsistence to market economies (Kirsch; Armbruster; Kochendörfer-Lucius, 1984, p. 13). They all show differing degrees of structural formalization.

The formal structure encompasses a set of cooperative organizational norms (e.g. democratic management, voluntary membership, rules for the equitable distribution of surplus or for the use of common assets etc.). These rules as well as their implementation – if need be through sanctions – are a precondition for optimizing the overall long term developmental impact of entrepreneurs' cooperatives, be they registered or not (Münkner; Baltes; Gamm, 1992, p. 10; Kötter, 1994, p. 799; Hanel, 1992b, p. 24). Regardless of whether such rules have been written down in statutes, a constitution or set of bylaws, are based on general law or are implemented by measures of social control, they must:

- be adhered to by all members;
- be known to everybody and be appropriate for the current membership;
- affect all members in the same way;

In practice, however, non-registered cooperative SHOs have been made illegal in many countries, and have been excluded from (official) marketing channels in others. In some African countries individual farmers were forced to market their produce through registered cooperatives, while elsewhere any resident of a particular locality was automatically made a member of a cooperative. These scenarios, of course, do not reflect the cooperative principles of autonomy and voluntary membership. As such they are not - in the truest sense - cooperatives and in many cases such cooperatives have failed to facilitate development. Cooperatives that have been able to maintain cooperative principles have been major proponents of rural development.

- allow for democratic decision-making and control processes; and
- offences against the rules must be sanctioned.

Even if the norms are cooperative in content, should any of the above conditions not be fulfilled, the cooperative will lack typically cooperative features and thus have lower or fewer effects on development. This last point should not be overlooked because it is of great importance for the maintenance of efficient member control, for organizational development and administration, for the possibility to replace directors in a democratic way and for the structured equality of members.

## 5.2 Empirical perspective

What we can learn from an empirical look at the practices and problems of setting up entrepreneurs' cooperatives and operating them? We need to first look at the preconditions necessary for their start-up and then at those determining their development.

## 5.2.1 The formation of entrepreneurs' cooperatives

When choosing governance structures for cooperating, prospective members have various options. But in order to organize themselves cooperatively it is not necessary for them to choose the legal form of an incorporated cooperative. However, empirically the suggestion is that their initiation influences the choice of governance structures, the source of initial capital, the management capacity available as well as the business aims (See for example Couture, 2003).

Whilst foundering members **in industrialized countries** are either relatively well informed, or can easily obtain advice during the establishment of a joint venture, this may not be the case for countries in transition from a centrally planned or socialist economy to a more liberal, market oriented system. In developing countries, and especially in rural areas, entrepreneurs have great difficulties accessing information due to their

lack of network across sectors and markets. This is made worse where sparse population and low levels of information technology contribute to poor development of infrastructures. But even so, there are external agents initiating the establishment of entrepreneurs' cooperatives.

The tendency is for most entrepreneurs' cooperative that start-up in Central Europe, Australia, New Zealand and North America to be initiated by SMEs, trades people or professionals themselves. Cooperative federations, with their public relations efforts, might have been instrumental in a certain number of joint venture starts, but by and large, cooperative federations in these countries only have direct contact with cooperators when they have already decided to work cooperatively. The original decision to form a cooperative is thus made by cooperators either entirely without external influence or with the influence of tax-, law- or business advisers who are independent of the cooperative system. The degree to which these professions are familiar with the organizational and legal specifics of the cooperative form varies greatly in Europe. In some countries, such as Germany, the relevant professionals to whom aspirant cooperative ventures turn first, either have insufficient knowledge about cooperative law or believe the form itself to be inferior to other corporate forms and thus do not advise in its favour (Göler von Ravensburg; Pinkwart; Schmidt, 2003, p. 81).

Conversely, in Eastern Europe, Asia, Africa and Latin America cooperative federations and other non-governmental organizations (NGOs) are major promoters of cooperative ventures (Hanel, 1992; ILO, 2000). In some countries, the state also is involved in the promotion of cooperatives.

In general one or more of the following criteria may entice entrepreneurs' cooperative foundering members to choose the cooperative form (EC, 2001, p. 13):

 joint interests of a larger stakeholder group helps to create business innovations;

#### Example 5.3: Inti Wasi Adaiwa, Peru

"Inti Wasi" – which means "house of the sun" – is a cooperative association of "right commerce" tradesmen located in Peru. It is an association of tradesmen who guarantee customers that their production obeys the principles of "right commerce", meaning:

- rejection of child labour
- respect for human rights
- respect for the environment

This project has obtained the support of PROMPEX (Promotion of the Medium and Small Company for Export) - an institution of the Peruvian Government –giving it the optimal qualification for the export of handicraft products.

**Source:** http://www.adaiwa.com/car/index.php?act=view Doc&docId=1 (14. Oct. 2008)

- member interests provide wider scope for temporary adaptation to economic or other difficulties;
- a temporary lack of nominal capital does not automatically provoke insolvency;
- democratic decision making leads to more sustainable outcomes;
- limited access to external capital may strengthen selfcapitalization;
- non-distribution of reserves assists capital formation; and
- in general, sustainable enterprise development is possible despite external pressures.

For any entrepreneurs' cooperative, the dominant motives of members might differ. Therefore the governance and the strategic and operational management of any entrepreneurs' cooperative must cater for the mixture of motives within the member group. This suggests that any promoter need to have a very good appreciation of the members' economic and wider expectations, as well as the economics of the sector in which members wish to continue operating. This constitutes a good argument for aiming for the widest participation in the processes of making by-laws and developing a business plan.

## 5.2.2 Internal conditions for successful development

Couture's study (2003, p. 55) of the need for certain internal conditions to be met before entrepreneurs' cooperatives can operate properly seems very convincing. What is emphasizes at various points in her work is that SMEs need sufficient entrepreneurial skills, marketable products and investment capacity. Couture also highlights that in some countries it is the lack of entrepreneurial support for them that obstructs entrepreneurs' cooperative ideas. She further points out that members' commitment is a prerequisite for sustainable success and that cooperative management is particularly complex. Accordingly, the greatest care must be taken in:

- the choice of elected leaders and (professional) managers (with a clear understanding of their respective roles and responsibilities);
- in professional financial management;
- management of human resources (members and personnel);
- sound strategic planning;
- management of services; and
- training and education efforts.

For example, a singular problem affecting a purchasing cooperative (also called a supply cooperative) is that it may incur particular management risks by holding considerable assets in the form of inventory and by providing credit to buyers. The members of the cooperative risk the loss of invested capital if the venture proves unsuccessful.

# Participation Properties Entrepreneurs' cooperatives ENTERPRISE CLUSTERS

The benefits and the limits of sustained cooperative development have been empirically researched and discussed by the European Commission (2001, p. 13-14). The report lists the following "disadvantages and dilemmas" of the cooperative pattern:

- "Membership orientation can cause difficulties in diversifying products and services to take advantage of new opportunities where such opportunities may have no relation to the interests of the members. The allocation of capital to its most efficient usage is therefore less effective through co-operatives than via stock markets;
- Limited access to external equity capital through available capital markets can lead to dependence on loan capital where members own capital is insufficient. Restricted voting rights (normally one person – one vote) can be a disadvantage in attracting risk capital without commensurate voting power;
- Democratic governance can lead to a slow decision making process;
- A large membership base can result in failure to keep abreast of members' needs and interests;
- In cases where members invest modestly this can lead to modest member interest and activity to develop the enterprise;
- The easy exit and entry to co-operatives can potentially cause problems to the stability of the enterprise due to exit of active members (for example on retirement of a professional – alteration by authors) and other development factors;
- Lack of understanding of the particular nature of cooperative management in traditional enterprise support and advice services; and
- Access to public procurement, whilst public authorities

# sometimes consider cooperatives as non-profit organisations and therefore ineligible as bidders."

It seems that some of the dangers seen in Europe are not relevant to the developing world and vice versa. While the greatest danger to entrepreneurs' cooperatives in Europe might be that with time the capital accumulated in the reserves outgrows members' contributions considerably (thereby weakening their influence on management), finding sufficient capital of their own in order to become competitive might be one of the greatest challenges to entrepreneurs' cooperatives in the developing world.

For entrepreneurs' cooperatives to contribute to development, or in other words to produce external effects which alleviate poverty and protect self-employment (if not create employment), they need to fulfil the following:

- sustain competitiveness by continuously giving efficient and appropriate services, supplying adequate goods and creating the necessary marketing channels regardless of the composition of the membership (Hanel, 1992, p. 114-115);
- remain fully managed by members and utilize the social capital acquired to help disperse innovations among members;
- use part of the economic surplus achieved in the cooperative core-enterprise to finance members' educational and social aims, whilst at the same time safeguarding the decision making process so that it remains lively, participative and productive; and
- discuss (re)distribution of surplus according to criteria (arrived at by participation) in order to protect and reinforce member-driven decision making processes. Normally, members will accept that some share of the cooperative's reserves and surplus should go towards increasing the

productivity of the poorer members because this increases their own access to more of the same resources (Münkner; Baltes; Gamm, 1992, p. 2).

In general those cooperatives which make the most of their comparative advantages in development terms include the following in their portfolios (Hanel, 1992, p. 114-115; Münkner; Baltes; Gamm, 1992, p. 34):

- information, education, training and consulting (e.g. improving the entrepreneurial competencies of their members);
- support for their members in the exercise of their political, economic and modern legal rights (including the use of their full credit worthiness, access to markets and developing markets);
- creating access to training and institutions on modern law as well as in creating new markets;
- support in entrepreneurial activities;
- processing and marketing of primary products; and
- collective production and supply of local services, such as education, training, health services, drinking and irrigation water.

The extent of the impact of cooperatives on poverty, however, will depend on its membership and whether or not poverty relief forms an integral and intentional part of the organization's objectives and on the availability of necessary skills (Marburg Consult, 1989, p. 85; Göler von Ravensburg, 1996, p. 68).

Other working hypotheses based on both empirical and theoretical research conducted in the late nineties in Marburg (Germany) relate to the influence that cooperative activities frequently have on property rights in the informal economy. For example, often poverty is a result

of ownership of property rights that obstruct more efficient use of local resources. At the same time, ill defined boundaries or environments, material or immaterial (e.g. political) changes to to context, changing relationships, changes in group composition or their basic beliefs and objectives can cause people to accept new organizations and the way they work. Apart from the general advantage all organised groups have in protecting their claims by acting in large numbers (Hanel, 1981, p. 143), cooperatives stand a chance of dealing with problems arising from ill-defined or disadvantageous property rights by forming effective and efficient second and/or third level federations. This is common practice in cooperative movements and enables them to exert greater influence locally as well as at regional or even national level (Göler von Ravensburg, 1998, p. 330).

It is the most effective way cooperatives can protect their autonomy visà-vis the state. Furthermore, such federations can exercise additional negotiating or bargaining power and help the primary organizations. This can be in the form of increasing profit from processes of adding value (by the pooling of members produce and resources), purchasing and marketing and by offering the necessary new information inputs (Göler von Ravensburg, 1998). The prime interest of these federations must, however, remain with the primary organizations and their members.

## 5.2.3 Value-chain integration and management

Value chain management is an indispensable part of cooperative management. Ideas to support this and take advantage of the way the system works for entrepreneurs' cooperatives in developing countries include (Hax and Candea, 1987):

See also *Eisenstadt, S.N.* (1968, p. 418) Development towards political democracy inevitably leads to demands for more economic democracy (Hettlage, 1987, p. 408; Adam, 1994, p. 41-42), while the reverse is not always applicable (for example, some Asian countries or Chile during the Pinochet era).

- the use of a model to generate an optimal number of leastcost solutions at the macro level, taking into account the most important cost components; and
- the use of simulation models to evaluate the solutions.

Business economic theory on Global Value Chains has been undertaken in order to investigate how different patterns of governance may enhance or hinder the upgrading of different types of firms. *Morrison Pietrobelli and Rabellotti* (2006) for example analyzed how governance structures can be used as strategies to augment per-unit value of products (product upgrading), to increase the efficiency of production processes, to implement new functions in the chain (e.g. the transition from simple assembling to design activities, or "functional upgrading") or to enter new sectors (i.e. inter-sectoral upgrading). They suggest that:

"technological change is the result of purposeful investments undertaken by firms, and therefore transfer and diffusion of knowledge and technology are effective insofar as they also include elements of capability building." (Morrison, Pietrobelli and Rabellotti, 2006, p. 4).

Apart from the composition of membership, the "collective efficiency", as *Jenkins et al.* (2007, p. 1) call it with reference to *Schmitz*, depends primarily on member participation in the setting of objectives, and monitoring and control processes. This forms an integral and intentional part of the organization's objectives and depends heavily on the availability of the necessary management competences.

This is true for entrepreneurs' cooperatives in the industrialized world as is evident in the results of the empirical study conducted by *Göler von Ravensburg, Pinkwart and Schmidt* in 2003 on entrepreneurs' cooperatives start-ups in Germany. In that study the first question examined was whether the choice of a particular legal form can be attributed to differences in the manner of cooperation. It became clear

that horizontal cooperation among SMEs prevails in Germany (68 per cent) while vertical and complementary cooperation accounts for the remainder (32 per cent). The registered cooperative is not used only for geographically limited cooperation, because on the contrary, nearly half of all new German SME-cooperatives operate nationwide. Cooperative startups are most common in the service sector (68 per cent) and they focus their activities mainly on common purchasing, exchange and/or common use of resources and know-how, administrative services and the saving of time.

In the developing world, cooperative membership might differ not only in income and ownership of assets but also in levels of education. The issue of internal differences within SME cooperations is of great importance for their effectiveness in rendering services that serve all members equally.

Couture (2003, p. 7-8) describes three empirical types of cooperative purchasing methods. It is safe to assume that in most cases either a simple purchasing club or a licensing agreement is a sufficient basis for a group of fairly homogenous members. Unless an entrepreneurs' cooperative takes some of its own risk, the cooperative legal form is likely to be too expensive an arrangement as it creates organizational costs which are too high for the members. Yet, the question is, under what circumstances will the third type, called by Couture "retail and wholesale buying", take on such risks? Would it be worth forming and registering in the legal form of a cooperative?

Obviously the similarity of member enterprises in any given joint venture, or the diversity of their expectations of services from it, determine how complex its supply chain coordination and integration systems need to be. This will also influence the level of formality needed and the style and scope of management will be appropriate.

In developing countries entrepreneurs' cooperatives might develop

several coordination and integration pathways<sup>8</sup>. This in turn influences the management competencies needed, not only for integration within the cooperative but also for integration upstream with suppliers and/or downstream with distributors and customers. Heterogeneous members might need different services as well as links with upstream and downstream partners. Common purchasing or marketing activities will benefit some more than others. Some might benefit more from internal supply relationships, whilst others need access to more capital or training from outside. From the start the cooperative might have to develop various coordinating and integrating systems. Perhaps it ought to aim for joint development of the services to be delivered. Also for a mutual exchange and integrated system of information transfer (with cross coordination on several levels in member and non-member companies, which could result in a larger network), long term contractual arrangements and different levels of process integration (Skjoett-Larsen, 2000).

Since integration reduces the individual entrepreneurs' freedom of action to some degree and might even lead to lock-in situations, members will only accept it if the cooperative's governance allows them to participate fairly in strategic management. Possibilities for important active participation, as well as mechanisms for a fair sharing of risks and benefits, need to be safeguarded.

An integrated supply chain provides one with enormous advantage: It reduces the so called "bullwhip-effect" (Lee et al., 1997) where a small change or minor decision on one level of the network may result in large fluctuations, large overstocking, and/or increased lead times on other levels. As the process becomes more integrated, the complexity of decisions ensuring the internal economics of the supply chain also

<sup>8</sup> Coordination and integration mean different things to different authors, but basically they all agree that they mean collaborative working and this implies joint planning and controlling.

A 'lock-in' is a term from New Institutional Economic theory. It signifies a situation where an economic subject has invested or faces the need to make an investment which it knows it will not be (fully) recoverable unless a certain business relationship lasts for a considerable time.

increases. The need for sophisticated tools and information systems for decision making increases proportionally to the degree with which the concept of process integration is embraced by entrepreneurs' cooperatives and their member enterprises. It is important to ensure that decision makers remain able to evaluate possible alternatives and their impact on the whole supply chain.

## 5.2.4 Entrepreneurs' cooperatives and poverty

Poverty is such a dominant development problem that a short section on the potential of entrepreneurs' cooperatives to alleviate is justified. Empirically studied entrepreneurs' cooperatives should provide effective poverty relief by the more efficient use or enhancing of common human and material resources for productive purposes. Traditional user groups, neighbourhood societies, women's associations, informal savings clubs and working brigades do this to some extent. They can pool risks and opportunities and make possible some specialization even under subsistence conditions. However it usually needs modern cooperative organization for affording access to institutions of modern law, the creation or widening of markets and/or the development of modern public infrastructure (education, water delivery, roads, health services etc.) (Münkner; Baltes; Gamm, 1992; Hanel, 1992, p. 114-115).

Informal cooperatives might be better at keeping the cost of organization to a minimum, thus attracting more poor members, but are usually inferior vehicles for the development of external relations, sustainability, reliability and width of effect (Marburg Consult, 1989). Even formalized purchasing or marketing cooperatives in trades, crafts and agriculture have not always effectively contributed to development. Where their turnover remained low (resulting from small numbers of members who were poor and whose enterprises were weak) (Marburg Consult, 1989, p. 13; Hyden, 1982, p. 92), they frequently lacked market power and the financial capacity for competing successfully with well-capitalized companies (Deutsche Stiftung für Internationale

Entwicklung (DSE), 1988, p. 96).

Medium-sized formal cooperatives are believed to have the largest potential for the creation of increased income opportunities for all members. In general, cooperatives which have both wealthier and poorer members are thought able to extend important benefits to the poorer members, such as improved market position, access to production finance, leadership and economies of scale and scope (Hanel, 1992, p. 116; Münkner; Baltes; Gamm, 1992, p. 27). However many do not use this potential as they tend to concentrate on the needs of their wealthier members whose turnover and business volume with the cooperative tends to be higher. Thus, the more wealthy members often have more de facto influence on the services rendered and frequently benefiting more from higher patronage, reimbursements or bonuses. In theory, these factors can be balanced by charging the wealthier with more than an equal share of the administrative costs. But this is unlikely to be the adopted business philosophy unless poorer members are well represented on the governing bodies, which may tend to drive wealthier members away.

The alternative is to separate various functions and to create a nexus between the use of these and reimbursements or bonus payments.<sup>10</sup> Another is to support entrepreneurial innovation by individual businesses (especially in planning, diversifications, specialization, labour intensive production processes and education and training). These are all measures, which also tend to promote the interests of poorer members.

The question of gender plays a major role in alleviation of poverty. As increasing numbers of women are affected by globalization (United Nations, 1995, p. 7; Heintz, 2006). Women experience problems with obtaining equal membership in an agricultural or entrepreneurs' cooperatives (Göler von Ravensburg and Jacobsen, 1999). They may also experience de facto exclusion from important information,

<sup>10</sup> Especially in regard to marketing and credit functions (Platteau, 1990, p. 5).

decisions or material benefits (Walter, 1996, p. 116). At the same time they are frequently the preferred borrowers and members of credit cooperatives, because they are more reliable even when they are not disposing of the loan themselves (IFAD, 2004; Göler von Ravensburg and Jacobsen, 1999).

Several studies have discussed at length whether or not it is better for women or the poor to form their own cooperatives or to become members of existing groups (See for example Birchall, 2003, p. 66). The contribution that any entrepreneurs' cooperative can make to the alleviation of poverty will depend on whether this aim has a significant position in its hierarchy of objectives and if the necessary management competencies exist (Göler von Ravensburg, 1996, p. 68). In order to integrate women and poorer members on equal terms, there has to be strategic management geared towards this. This is something which is missing in many development projects. However, there may be a new focus on this with the advent of poverty reduction strategy papers (Birchall, 2003, p. 17). Careful evaluation by promoters and members of entrepreneurs' cooperatives of the possibilities they might have to promote women or poorer members, and offering the respective training and education opportunities, is possibly the best to be hoped for (Marburg Consult, 1989, p. 85).

# Chapter 6

# Challenges to the establishment of entrepreneurs' cooperatives

Around the world entrepreneur-type cooperatives are less common than agricultural or savings and credit cooperatives. To our knowledge this has yet to be comprehensively studied and reasons given. The other question that has been studied by a number of authors in the past is: What are the key interactions between cooperatives and the political, economic and social environments? However, the interactions between (institutional) environment and cooperatives are so complex that to date most studies are of an interpretive nature. Neither empirical nor theoretical research has as yet provided an all encompassing conceptual explanation and it is possible it never will.

For the purposes of this chapter it is no longer practical or helpful to differentiate between a theoretical and an empirical approach. It is rather more instructive to summarize using all approaches together. In focussing the discussion on entrepreneurs' cooperatives we need also to allow for many paths common to both the development of cooperative typologies, as well as the environments created, in order to promote and regulate cooperatives.

Based on New Institutional Economics, Evolutionary Economic Theory and Cooperative Economic Theory we can be fairly certain that the

economic and social success of entrepreneurs' cooperatives are particularly influenced by (Hanel, 1981, p. 137):

- the historical institution building process;
- 2. general constitutional, political and economic frameworks:
- 3. economic development strategies;
- 4. regional and sector policy systems (e.g. the sector specific terms of trade);
- 5. promotional programmes for small and medium scale entrepreneurs;
- 6. certain civil law regulations (e.g. regarding access to resources and credit-worthiness);
- 7. cooperative policy and law; and
- 8. activities for the promotion of cooperatives and entrepreneurs' cooperatives.

## 6.1 Entrepreneurs' cooperatives in cooperative history

Cooperative history began in Europe and spread to developing countries through colonial administration.

#### 6.1.1 In the Industrialized World

Entrepreneurs' Cooperatives in Europe have evolved through time with various types being dominant in different countries. The entrepreneurs' cooperative of craft persons and traders have different roots.

In the traditional economies of Europe most produce was sold locally, with producers also acting as traders of their own produce. Throughout the Middle Ages craft persons were organized in guilds (Kluge, 2007, p. 16), with membership being neither voluntary nor free. Guilds dominated not only decisions on what and how to produce, but also on the private lives of their members. They were also more than economic

organizations as they exercised military, religious, legal, social and local government functions. However, they lost most of their influence during industrialization.

The advent of long distance trade meant that another associative form was needed in order to provide insurance, risk sharing transport networks (e.g. rafting goods along rivers and making available animal drawn conveyances at certain points along the road). This trade was so profitable that it could provide many other needs (such as credit) within the individual trading firm, and so common marketing or purchasing by various firms very seldom developed.

During the later stages of European industrialization trades people came under considerable economic pressure, but at the same time new business opportunities opened for them. The effects were very different in different economies, but in all sectors the craft people who fared best in the process of structural change were those which organized common purchasing and marketing organizations. In this context is the work of the well-known German cooperative promoter *Hermann Schulze-Delitzsch* (Neumann, 1994). Using his ideas, craft people working as cooperatives created economies of scale similar to those of industrial enterprises, without losing their autonomy.

The step from early cooperative merchants' organizations to modern entrepreneurs' cooperatives took place only in the 19<sup>th</sup> century and was probably best promoted in France and Italy. Several governments supported the self-organization of workers and small business people with what they saw as adequate legal and institutional frameworks (Fehl, 2007; Göler von Ravensburg, 2007; 1998).

As a modern phenomenon, cooperative retail organizations and service agencies for their members are largely limited to Europe, North America and Australia. Today in Europe and North America

<sup>1</sup> The "Hansa" was such an organization trading very successfully for nearly three centuries throughout Northern and Central Europe.

there are entrepreneurs' cooperatives in nearly every retail sector, in service sectors such as travel and hotels, as well as among self-employed trades people in all sectors. Wholesalers in various fields have chosen this legal form, as have transport firms (especially in the navigation of inland waters), taxi owners and commercial forwarders.<sup>2</sup> The professions are well represented (particularly lawyers, dentists, doctors, tax consultants, engineers, management consultants and court bailiffs) and derive benefit from using the cooperative legal form.

## 6.1.2 In the Developing World

Countries in Latin America became independent from Spain or Portugal much earlier than those which were colonies in Asia and Africa. It was in the former that the first cooperatives were seen early in the 19<sup>th</sup> century. The introduction of cooperatives into so-called developing countries can be traced back to the 1900s in the British and French colonial administrations.<sup>3</sup> According to *Eschenburg* (1985, p. 197) the promotion of cooperatives was meant:

There are more than 300 entrepreneurs' cooperatives in Germany 2 whose members are independent trade or handicraft enterprises. The most famous of them are REWE, Edeka, Intersport and Vedes. The fact that many entrepreneurs' cooperatives are market leaders in their branches is often not widely known. In total 200,000 member enterprises operating in 45 different branches generate a yearly turnover of 122.5 billion Euro. The number of entrepreneurs' cooperatives by itself is proof of their great importance to the national economy. There isn't any branch where the entrepreneurs' cooperatives would not be operating and they have achieved large market shares in many central business areas. E.g. entrepreneurs' cooperatives in the building trades have reached a market share of 76 per cent, entrepreneurs' cooperatives in furniture retailing a market share of 60.6 per cent and entrepreneurs' cooperatives in food retailing 52 per cent. See http://www.zgv-online. de/ZGV\_intern/Erfolgsgeschichte \_Kooperationen/E3037.print. Feb. 2008)

The earliest cooperative act outside of Europe was the "British-Indian Cooperative Act" in 1903.

"on the one hand to support the general economic exchange between colonies and mother countries, and on the other hand to alleviate social problems and support the social and economic integration in the colonies."

Their promotion concentrated on agricultural and credit cooperatives in order to encourage marketable primary production in developing countries. Industrialized production and value-adding activities were seen to be the prerogative of the now industrialized countries, which might also explain why entrepreneurs' cooperatives were not an issue in developing countries for some time. The role of cooperatives was redefined as developing countries gained their independence from the 1950s onwards (Münkner, 1989, p. 198). Here, the discourse largely followed the one in Europe, centring on the controversy about whether cooperatives were to serve the revolutionary conquest of capitalism or to represent a reforming supplement to a market-oriented way of production. Again entrepreneurs' cooperatives were hardly considered. The production or workers' cooperative became the favourite cooperative form in the urban areas and various kinds of farmers' cooperatives were dominant in the countryside.

In both "ideologies" cooperatives were regarded as transitory organizations and given roles as engines of economic and social change (Rösner, 2001, p. 439). By the end of the Cold War era it was obvious that state-led cooperative systems could not provide Africa, Asia or Latin America with sustainable development. But the hope that the cooperative model could help to overcome dualistic economic structures (formal-informal, rural-urban, local-international etc.) did not disappear altogether. Meanwhile the interaction between cooperatives and their environments have increasingly been brought into focus. Recently the development effectiveness and efficiency of entrepreneurs' cooperatives, as one form of cooperative largely unknown in developing countries, has entered the cooperative development agenda.

#### 6.2 Normative environment

Progress in promoting entrepreneurs' cooperatives and other cooperatives has been made possible in recent years by macro-level changes, legal reforms and technical and financial support. Despite comprehensive legal and institutional reforms in some countries, the cooperative approach as a whole still suffers from the legacies of the past when governments used cooperatives to control people, markets and products. Moreover, many countries have yet to realize the full benefits of horizontal and vertical integration, especially for professionals, SMEs, local government service providers and the informal economy. As a special supplementary report by the Director General of the ILO (2003, p. 11) states, more needs to be done in regard to:

- establishing a conducive legislative, regulatory and institutional framework;
- organizational and managerial tools to foster ownership, accountability and effective participation;
- the integration of different types of cooperatives into national cooperative movements; and
- the application of the cooperative concept "...to new areas, such as shared service cooperatives for small businesses".

We now look in some detail at what results if and where the normative environmental conditions are not conducive to entrepreneurs' cooperative development.

## 6.2.1 Overarching macro conditions

Cooperatives are self-help organizations (SHOs). entrepreneurs' cooperatives are SHOs of SMEs, other entrepreneurs and professionals. Without certain constitutional, political and economic rights their members can neither become active in their own right nor assemble and associate as members of a cooperative association. For both to

materialize, members need to be guaranteed the following (Henry, 2005, p. 8; Göler von Ravensburg, 1998):

- civil liberties (basic democratic and human rights, judicial independence and authority over all public acts, nondiscretional and non-discriminatory exercise of judicial and administrative power, free choice of trade, craft, profession, personal property and inheritance rights etc.);
- contractual freedom and the right to associate;
- autonomy of organization, of business planning and in management;
- a reasonably liberal, market related policy environment, including non-discriminate rules on local and regional administration;
- the legal freedom to compete as well as free entry into competitive markets;
- equal treatment in regard to taxation, incentives for and fiscal handling of innovation, trade and production;
- clear and generally applicable rules on accountancy, banking, consumer protection, social security, transports and marketing; and
- a minimum level of infrastructure.

These needs apply to the individual member enterprise as well as to the cooperative. In addition, the cooperative needs to be treated nondiscriminatorily with regard to all aspects of commercial, financial, taxation and international trading law.

In reality it is rare to find any country or sector where all these conditions are fully met. National and sector differences are responsible, at least in part, for entrepreneurs' cooperatives having developed different patterns of formalization and sector clustering and differing degrees of success. At the same time the fact that entrepreneurs' cooperatives

have been started and are operating successfully in many countries obviously means that not all conditions need to be met at the same time. However, whatever the normative environment that entrepreneurs' cooperatives face, its trace may be seen.

## 6.2.2 Economic and development policies

The introduction to ILO Report V (I) describes the need for Recommendation No. 127 in regard to the incumbent political, economic and social changes taking place around the world. These changes have affected not just cooperatives, but all business organizations and economic sectors to a greater or lesser extent. Economic boundaries, which existed during the Cold War era, have largely disappeared. Whilst the largest international trade volumes are still concentrated in Europe, North America and South and East Asia, Latin American and African states are nevertheless also faced with the need to adjust to WTO agreements and globalized trade patterns.

Structural adjustment programmes (SAP) have led to more liberalization and privatization. Virtually all sectors of production regard themselves as under pressure to adhere to international product and production standards and investments are increasingly influenced by global financial markets. Currently the protection of certain industries is becoming the exception rather than the rule. Customs regulations, import and export subsidies or duties, competition policies and antitrust laws are subject to regional economic integration. Countries which used to rely on primary produce and natural resources for their foreign currency earnings are facing worsening terms of trade. Africa South of the Sahara is especially hard hit. Under these circumstances the leeway for the design of economic policies is significantly reduced.

At the same time the immanent scarcity of certain natural resources and a number of internationally shared ecological problems obviously present a challenge to identify best practices in international coordination and governance (See for example Radermacher, 2006, p. 2). Other

impediments to development in the productive and (increasingly) in the service sectors result from the HIV/AIDS pandemic. The economically active population is very badly affected in some countries, with the resulting shortage of manpower and technical and professional staff being especially detrimental to any further economic development (DIE ZEIT, 26th July 2007). Other natural disasters aggravate the situation. The international spread of bird flu, for example, caused the established poultry industry in South East Asia to suffer severe losses. This together with the lack of infrastructure to facilitate transport and communication which persists in some regions, this renders remaining public development strategies less effective, with some even doubting that economic development can be influenced by policies at all.

However the State has an important role to play in providing the political, legal and administrative framework and certain public goods necessary for the development of private organizations. However, less than favourable local and national public policy environments hamper potential members of entrepreneurs' cooperatives as well as the entrepreneurs' cooperatives themselves in their business development. Property rights systems, competition law, business licensing fees and procedures, tax structures, and regulatory compliance requirements are only some examples of policy areas which can obscure market relationships, favouring certain business sizes, certain sectors or certain individuals over others.

In any case, injustices in all the policy areas mentioned above can impose disproportionately high costs on craft persons, SMEs and professionals, and, in so doing, limit their growth and capacity to form entrepreneurs' cooperatives. These barriers may even keep SMEs in the informal economy, where they may be unable to enter certain types

<sup>&</sup>quot;Over the past two months, more than 100 million birds have either died of the disease or been culled in Asia. This figure is greater than the total number of poultry affected, over years, in the world's previous five largest outbreaks combined." http://www.who.int/csr/don/2004\_03\_02/en/index.html (17. Nov. 2007).

## **Example 6.1: Unfair competition policy**

In Europe competition policy and law has created a scenario which is currently seen as unfair by the European Cooperative Federation of entrepreneurs' cooperatives (UGAL)...

"Specifically, national and EU competition policy and law currently restrict the behaviour and relations between members within cooperative and other groups of independent retailers in ways that are fundamentally discriminatory compared to the freedom enjoyed by wholly integrated retailers. Independent retailer groups are, for example, limited in the control they can exercise over retail prices and promotions, store-level stocking/range decisions, and purchasing requirements of members, thereby affecting group efficiency and the consistency of retail image/offer presented to consumers. They are also subject to stringent market share thresholds, resulting in further restrictions on their behaviour and greater legal uncertainty over their agreements as they grow in size. These restrictions do not apply to fully integrated retailer groups that have been, with few exceptions, freely allowed to grow and increasingly dominate markets, often at the expense of independent retailers."

Source: Dobson, P. 2006, p. iii

of legal contract or seek legal redress if or when contracts are broken.

#### 6.2.3 Critical external factors

Economic policies and large areas of legal systems in place have been less favourable for all types of cooperatives in developing countries compared to conditions entrepreneurs' cooperatives face in industrialized countries. Despite much of this having changed dramatically in recent years, with liberalization and democratization having made much progress in many parts of the world, the struggle for change has been and still is a long one and not everyone (particularly in the rural areas) has yet fully understood their new rights.

Certain culturally-tied social norms and traditional (local) property rights have persisted in developing countries and these at times can conflict with economic opportunities resulting from modern changes in political and legal systems. This may not always be obvious nor may modern law be the preferred solution at local level. Sometimes it is simply the whole social environment, which is not conducive for entrepreneurs' cooperatives. It may not always allow, let alone encourage, the formation, participation and maintenance of a group and even entrepreneurial behaviour.<sup>5</sup>

## 6.2.4 Development policy

In development policy today, the Millennium Development Goals (MDGs) and Poverty Reduction Strategy Papers (PRSPs) are of prominence. That cooperatives in general, and with them entrepreneurs' cooperatives, are currently being underestimated in their development effects has been said before (see Chapter 3.1, Section "social and other benefits"). At an international level, the ICA and the ILO are trying to overcome this and to some degree their efforts are showing initial progress.

The ILO, particularly its Policy Integration Department and the Cooperative Programme, has been encouraging the participation of cooperatives in the process of drafting national PRPSs, by building their capacities (Birchall, 2004, p. 53). In Africa, several sub-regional and national workshops have been organized by the Cooperative Programme, the Policy Integration Department and the ICA. Their aim

This implies especially the possibility to take autonomous entrepreneurial decisions and to choose ones profession freely.

has been to familiarize cooperative managers and leaders with the design, implementation and monitoring of the country PRSPs, and to enable them to participate in such processes. They have also aimed to sensitize policy-makers to the role of cooperatives in reducing poverty and promoting decent working conditions.

Country PRSPs and related reports describe several approaches relating to cooperatives. In 2004 there were a number of reports which made no mention of cooperatives at all. There were reports that mentioned cooperatives but only as part of a listing of organizations, making reference largely to rural and/or farmer cooperatives and microfinance institutions. Thirdly, there were reports that really did discuss the cooperative contribution, usually in the context of changing policies and financing arrangements towards existing cooperatives as well as the formation of cooperative unions, a cooperative bank or rural credit cooperatives. Occasionally mention was made of a "revival of the 'cooperative movement'", as in Madagascar, where at the time new regulations were being drafted for credit cooperatives. Cooperatives are now seen as part of the wider renaissance of the private sector. Mostly, however, only agricultural cooperatives are mentioned in the national PRSPs, while entrepreneurs' cooperatives largely remain without a trace.

This is understandable because agricultural policy is one of the most important parts of most PRSPs and agricultural cooperatives are by far the most frequent. However, even their importance can vary widely from country to country and their effectiveness in poverty reduction must sometimes be doubted. This is especially where farmers see them as state agencies and find many ways to escape participation within the structure, rather than increasing their engagement. entrepreneurs' cooperatives, on the other hand, have a great potential for poverty reduction in the informal economy, and are not yet tarnished with a bad reputation.

## **Example 6.2: Challenges to cooperating**

In Uganda the cooperative movement was strong in the post-colonial period, with the government offering them a monopoly status in agricultural marketing. However, as political interference and insecurity started to trickle in the 1970s, members' involvement in the management of cooperatives eroded. The cooperative movement remains weak today, and though it is showing signs of revival, it still has a long way to go before it can champion development...

"In Uganda, despite the lack of mention of cooperatives, they have had an input into the plan for modification of agriculture, and have been invited by the government to participate at numerous levels of policy deliberation, including on the Social Development Sector review of the PRSP. However, the Uganda Cooperative Alliance has not yet seized the opportunity provided. The movement is weak after the collapse of many secondary societies during the early 1990s owing to the effects of structural adjustment. It faces an unfavourable legal framework, insufficient access to finance, weak linkage to government structures dealing with cooperatives, and isolation due to the previous bad experience with state-guided cooperatives (International Labour Office/International Cooperative Alliance, 2003a)."

Source: Birchall, 2004 p. 53

## 6.2.5 Parallel regimes in public and private law

In many developing countries a dualism of parallel legal systems does persist: One or more traditional political and legal systems have been overlaid by a modern political and legal system. This causes a certain degree of divergence between de lege and de facto rights for the individual, general legal uncertainties, intricate social power

positions, risks to overall economic planning and enormous social risks. Marginalized groups in rural or semi-urban areas and the informal economy are particularly vulnerable. They can no longer rely on the traditional social system nor have they gained access to a modern one. The resulting uncertainty influences their economic behaviour much more than is usually recognized in the discussion about adequate framework conditions for cooperatives (Kötter, 1994, p. 798).

Where modern legal norms do not interfere with traditional social structures, they are frequently ignored by traditional societies and indigenous cooperatives alike (e.g. in common bond production units as known in Bali, Indonesia). Such cooperatives are usually dominated by interpersonal and internal relationships and their development path is an autopoietic one. However, as soon as they make contact with strangers and supra-local organizations (e.g. in order to market their produce), modern social institutions and norms applicable in larger markets and the rule of modern law begin to impinge on them (Kirsch; Armbruster; Kochendörfer-Lucius, 1984, p. 172).

Instead of changing easily in the direction of "modern" organizations (with all the demands for new knowledge and capacities this brings), they decide that they should survive in their previous form. This is either because they can use existing influences over inefficient bureaucracies to compensate for any disadvantage the refusal to change might cause them, or because they can undermine unfavourable political or bureaucratic decisions by using their comparative advantage of knowledge. In both cases this influences their competitors and results in the deforming of the market mechanisms. Particularly affected are land, financial and agricultural produce markets.

## 6.2.6 Traditional challenges

Another problem which might be even more serious, especially for rural and informal entrepreneurs' cooperatives in developing countries

<sup>6</sup> This could be claimed as 'political rent-seeking'.

(but also in countries in transition), relates to the lingering effects of discrimination against women from historic private and family law. Many rural entrepreneurs' cooperatives for example are almost exclusively made up of women. Yet, there are still a number of countries where all married women are subject to their husbands' will, their legal status being that of minors or even less (Birchall, 2004, p. 20; Zimmermann, 1983, p. 86; Singh, 1990, p. 89). In many areas women traditionally have had no rights to contract and were unable to lay a charge in traditional courts. Customary marriages have a doubtful legal standing in modern law and women frequently have no right in customary law to inherit land use rights. They are dependent on other relatives if they are widowed (Göler von Ravensburg, 1998).

Even under modern law it still takes courage for most women to ask their husbands for permission to open a bank account or a shop. Not many will do this without their husband's expressed approval (Zimmermann, 1983, p. 87). Most modern family and property law holds more promise for women, but even so it does not always allow women to inherit their deceased husband's assets (Birchall, 2004, p. 20). Modern law does not always quickly become known at the level of local society and even if it does, will women find the courage (and the resources) to claim their rights in a modern court of law?

As a result, many primary entrepreneurs' cooperatives still battle with out-dated mental patterns. Although they are frequently headed by men (even though the majority of members are women), the inferior status women have in many traditional societies and legal systems means they lack self confidence when it comes to facing up to external (male dominated) institutions such as local government, business partners etc. There are many examples of conditions created by internal (local) behaviours and social organization persisting even when and where the more modern environment seems to render them outmoded (Eisenstadt, 1968). They can be extremely obstructive to real self-help and participation, or cause severe internal conflict between those

For example in Southern Africa (Schapera, 1966/1970, p. 205).

members preferring "proven" ways and others more flexible, to the point where the cooperative business might not survive.

Paradoxically there are also examples where maintaining traditional social customs (such as reserving certain public roles for men or seniors) is accepted by a majority of those affected. They can also results in organizations being successful in business terms, at least in the short term. In developing countries even profit-oriented enterprises with "modern" organizational structures might maintain systems of decision making and rights of disposal that follow different, more personality-dependent patterns (Lomnitz, 1988). Around 35 years ago Mühlmann (1986) called this phenomenon 'hierarchical ontology'. He described it as the tendency of societies to avoid changing hierarchies by voluntarily re-introducing the same criteria for the previous pattern of leadership (e.g. by electing old councillors after tribal government was replaced with democratically elected councils).

With more recent insights from New Institutional Economics and, in particular, with the help of contract theory we now know that the existence of 'sunk costs', 'moral hazard problems' and 'lock-in situations' is largely responsible for such phenomena.<sup>8</sup> It is to be hoped that these explanations for what appear rigidly status-driven organizational hierarchies may, in time, provide us with better ideas on how to monitor organizational structures and norms. Also, more importantly, how to draw to their members' attention the risks resulting from dominance of power, so that the democratic nature of cooperatives does not become dilluted.

## 6.2.7 Risk adversity of traditional societies

Starting entrepreneurs' cooperatives from below – just as starting any other enterprise – is an experiment which can succeed or fail. Foundering members are bound to weigh the risks before they start. In the course of the development of an entrepreneurs' cooperative its

<sup>8</sup> For details see *Göler von Ravensburg* (1998, ch. IV.2.2.1.4).

wider social acceptance will determine whether or not it attracts more members and enlarges its business. In this respect, *North* (1990, p. 42) believes that:

"... culture defines the way individuals process and utilize information and hence may affect the way informal constraints get specified. Conventions are culture specific, as indeed are norms."

North also points out the positive role cooperation plays in the reduction of transaction costs and in particular innovation and information costs. Other economists researching the role of organizational culture for the development of organizations and their structures draw conclusions which are less positive. Hettlage for example is adamant that there is more to successful long term cooperation than just contractual agreements (Bakhit, 1997, p. 327). At least people need to have sufficient personal freedom to experiment at all.

Bakhit indirectly criticizes North's view firstly by pointing to the subsistence related motivations, which characterize many rural and informal economy businesses and cooperatives. According to him this leaves very little room for experiments, at least not for failures. Bakhit (1997) secondly refers to a number of other obstacles to effective participation and business development, which must be attributed to culturally determined value systems and traditional law, such as:

- a different perception of time;
- the socialization of the individual; and
- social tendencies towards:
  - (a) the minimizing of risk;
  - (b) zero-sum mentality;9 and

This relates to that belief that no-one can benefit unless someone else loses, which is still fairly common in many African societies (Bakhit, 1997, p. 238).

(c) social levelling ('equalization') by way of minimizing personal and trans-generational capital accumulation.

With regard to the start-up of entrepreneurs' cooperatives *Bakhit* (1997) sees these factors as equally important to the lack of promoters. He attests that especially African societies have relatively weak capacities for extra-familiar trust and generally believes that this is why comparatively few supra-local cooperative organizational structures have developed from below.

All these factors must be kept in mind when searching for reasons why entrepreneurs' cooperatives have not developed significantly better in developing countries.

#### **Example 6.3: Summit on Employment and Poverty Alleviation**

National Consultations leading up to the Extraordinary Summit on Employment and Poverty Alleviation held in Burkina Faso in 2004, as summed up in an ILO Report titled "Working out of poverty. Views from Africa" conclude:

"Many participants underlined that most economic (non-farm) activities in Africa were carried out by small and micro-enterprises in the formal or the informal economy. However, the low level of productivity and income, and the precarious nature of some of these businesses, generally resulted in unstable employment relationships and in poor living standards."

**Source**: ILO, 2003, pp 10-11

#### 6.2.8 Legal personna and development impact

There is much discussion among international economists, economic planners and politicians about the role of the informal economy in the national economies of developing countries. Some praise the potential for employment and wealth creation, while others fear that this 'shadow economy' might create more welfare losses than gains. Among the arguments, the latter put forward are the concerns that resources are being wasted in the informal economy due to low productivity, that labour law is circumvented and that neither consumers nor employees are sufficiently protected.

The variety of ways in which group owned enterprises and economically active SHOs formalize themselves structurally or legally in different countries is both a reflection of past and present legal systems as well as ethno-sociological or socio-cultural circumstances. In many African countries, for example, cooperative SHOs have found it difficult to become part of the legal cooperative sector for a variety of reasons not the least of which being a reluctance to become agents of the state<sup>10</sup> or that they prefer to limit their membership to family members (Hettlage, 1994; Kötter, 1994).

To answer one of the most important questions posed in this paper, that is whether or not there is a difference in the effects on development produced by legally formalized entrepreneurs' cooperatives as distinct from those entrepreneurs' cooperatives which are not, we examine what can be deduced from empirical data.

This evidence suggests that indigenous family groups, user groups, women's clubs, workers' associations and savings and credit associations show the most immediate impact on local poverty (Münkner; Baltes; Gamm, 1992, p. 2). This might be because many

<sup>10</sup> Concerning the various forms of self-help organizations see *Münkner, Baltes and Gamm, (*1992, p. 12, Diagram 1).

informal primary self-help organizations (SHOs)<sup>11</sup> have a reasonably homogenous membership of (or at least including) significant numbers of largely poor members. Also that the group tends to concentrate on the more efficient use and/or growth of the common resources necessary for production.

On the other hand the permanence and scope of their effects remain limited and their reliability as partners for official development aid programmes must often be doubted (Marburg Consult, 1989).<sup>12</sup> The lack of legal standing hampers their capacity for external relations, the financing of growth, standing surety for their members and the formation of supra-local federations. This matters little so long as they produce for only a local market. Observation shows that almost as soon as they produce more, or try to sell different products that cannot be absorbed locally, they either seek formalization or vanish. Another reason for formalizing occurs when members expect economic conditions in the mainstream economy to be better for them than remaining in the informal economy. Also when they wish to gain access to external resources such as credit or because they want to influence legal and other framework conditions they consider relevant to them (Kirsch; Armbruster; Kochendörfer-Lucius, 1984, p. 10).

Somewhat analogous to agricultural cooperatives' formalization should be advantageous for entrepreneurs' cooperatives attempting to achieve higher levels of capitalization and modern operational patterns. At least in theory, formalization should also provide better opportunities for improving incomes of both wealthier and poorer members, and develop a greater scope for protection, financing, leadership and economic scale (Hanel, 1992, p. 116). Yet in practice, the dangers of conflict within a heterogeneous membership (Hanel, 1992; Münkner, 1976, p. 2) must be recognized, in particular the risk that the better off benefit relatively

By this we mean SHOs not formalized into legal entities in the sense of organizational law

See also Chapter 5 above (p. 65) as well as the section on "The need for a certain degree of structural formalization" (p. 69).

more from bonus payments than the poorer (Münkner, 1976, p. 111).

The challenge for entrepreneurs' cooperatives with a heterogeneous membership lies in creating the right mix between incentives for larger member businesses and the economic advancement of less well off members (Marburg Consult, 1989, p. 13; Hyden, 1982, p. 92). In order to realize their (theoretical) special potential for development so-called multi-purpose cooperatives, offering a wide range of services, need particularly talented strategic management. This is significantly different from the strategic management a largely profit oriented company usually develops. Above all, any entrepreneurs' cooperative attempting to offer a wide range of services as well as achieve the creation of equal opportunities and fight effectively against poverty might just over extend itself and its members.

#### 6.2.9 Summary normative environment

In summary, it seems that the normative environment for entrepreneurs' cooperatives is decisive to ascertain if there is a potential for formal entrepreneurs' cooperatives in various business sectors, for independent craft people as well as for professionals. Depending on national legal frameworks, political and administrative demands as well as social standing, this can mean variable effort and variable costs. If informal cooperation is more appealing in many areas of the world, 13 this could be because the necessary steps and procedures to establish and run a formal entrepreneurs' cooperative will only be considered worthwhile where integration into modern and supra-regional markets is intended.

## 6.3 Promotion for small and medium-sized enterprises

Couture (2003, p. 55) is to be supported in her belief that:

"For CBAs (cooperative business associations) to emerge

This is not just relevant in developing countries but also for industrialized countries; for the USA (Bhuyan, 1996, p. 8).

and flourish, the economic environment must first foster the establishment and survival of SMEs and independent producers sufficiently for them to make a livelihood from their enterprise and be financially involved in their CBA."

Indeed SMEs are still facing less than advantageous conditions in many parts of the world. SMEs are frequently limited in scope and to local markets, which in turn are dominated by the informal economy with its low prices (due to self-exploitation), as well as evasion of tax and social security payments. Moreover, strategies to help formalize the informal economy frequently fail because the local purchasing capacity is not sufficient to carry the additional product cost resulting from adherence to higher product and work standards, licensing and taxation.

Often, therefore, promotional strategies for SMEs include marketing and other efforts. The driving forces behind such strategies are either government agencies or – and increasingly so – international business organizations. Development not-for-profit organization, while frequently active on the input side (the keyword here is micro-credit) are less frequently found in marketing or international trade. Fair trade organizations could be said to be an exception.

Surprisingly, there is not a lot of recognition at international level for the role entrepreneurs' cooperatives could play for SMEs, and in the informal economy, not even by the cooperative movement itself. For example, Birchall (2001, p. 30) notes that:

"For many cooperative movements, the economy presents itself more as a split between urban and rural, large and small enterprises, exporting and producing for local consumption, and so on. The informal sector is seen as part of this wider economy. There is, however, an equivalent duality between official, registered cooperatives that are mainly in the rural areas focusing on the needs of farmers and a kind of informal cooperative sector that includes

unregistered "pre-cooperatives" or informal cooperatives. As with the concept of informal sector, there is some recognition that it is in these informal cooperatives that the future dynamic will be found for the growth of genuine member-owned and controlled cooperatives."

*Birchall* also offers a valid explanation why cooperative movements in developing countries are not as involved in SME promotion as they could be:

"At the national level, in developing countries there is a preoccupation with the survival of the "formal" cooperative sector in the face of structural adjustment programmes, the gradual withdrawal of state involvement and the restructuring of cooperative federations to cope with the loss of government funding. The main priority is to ensure the commercial survival of large agricultural cooperatives in the global market. Like the trade unions, the cooperative federations are short of the skills and resources they need to work in the informal sector."

This said, it is interesting to note that NGOs frequently use inherently cooperative style institutionalization for the implementation of (micro-) lending and other SME promotion programmes. Some such programmes cooperate with the regional offices of the ICA. Virtually none cooperate with national cooperative federations, as these - apart from being preoccupied with their own survival - are frequently seen as instruments of governments, rather than as autonomous bodies governed from the primary cooperatives below. Beyond this, however, lies great potential if informal economy (pre-) cooperatives and established cooperatives were to cooperate more closely.

SME promotion with regard to the development of entrepreneurs' cooperatives is not just an issue in developing countries, however. Not all cooperative movements in Europe seem to be particularly well

positioned in the promotion of SMEs (Göler von Ravensburg; Pinkwart; Schmidt, 2003, p. 81), as not all of them have traditionally catered for entrepreneurs' cooperatives. While Italy and France have a history of entrepreneurs' cooperative promotion, entrepreneurs' cooperatives in Germany, Great Britain and the Scandinavian countries have always been fewer than other types of cooperatives. It seems almost as though the development paths begun in the 19<sup>th</sup> century concentrated on two or three types of cooperatives in each country, and then the favoured types remained the same in the 20<sup>th</sup> century. Acknowledging that promotional efforts on the part of cooperative federations represent investments by the associated cooperatives into new cooperatives, is in some degree is self-explanatory.

Other reasons can be found in the image and start-up costs attached to cooperatives. A study by the Marburg University Institute for Cooperative Science showed that a majority of entrepreneurs, as well as small and medium-sized firms in Germany do not consider using the cooperative form for their inter-company cooperation, instead preferring to use other legal constructs (Göler von Ravensburg; Schmidt; Ullrich, 2003, p. 34-46). The reasons are complex, but it became obvious that neither the official bodies supporting start-ups in production or service sectors, nor the private sector legal consultants, advise in favour of the cooperative. This is perhaps because they do not fully appreciate how a cooperative works, believing it to be a form for the agricultural and credit sectors only. They are also weary that they might lose their clients, as German cooperative law prescribes a membership of all cooperatives in regional federations, thereby to some degree monopolizing the possible consulting businesses (legal as well as business consulting are parts of the portfolio of German cooperative federations).

## 6.4 Cooperative policy and law

The challenges in formulating cooperative policy and law today are different to the ones pertaining in the seventies and early eighties of

the 20th century. At that time governmental strategies for the promotion of cooperatives often remained part of larger (agricultural) development plans. The greater their role was within these, the stronger the tendency to make cooperatives an official instrument (Eschenburg, 1985b, p. 225 and sources given there). Promotion strategies therefore regularly based themselves on strong, direct government promotion and control during the start-up phase, with a planned phasing out of support forecast for a later stage.

Strategies of this kind have proven a failure in most countries (Koch, 1986; Shah, 1999, p. 56). Huge, unwieldy public cooperative promotion agencies have developed instead, bureaucracy increased and unwanted side effects such as corruption, nepotism and misuse of power have occurred. Cooperatives tended to become organizations for the wealthy, while the gap between rich and poor grew larger instead of smaller. Functionaries, bureaucrats, governments and political parties took control, while large parts of the target population were either not reached or were apathetic. Attempts to include informal cooperatives by way of allowing one or other pre-cooperative set-ups or to (at least) tolerate indigenous cooperatives did not change the picture fundamentally (Eschenburg, 1985b, p. 228-230). In the nineties it became obvious that new ways needed to be found.

In 1999 the General Assembly of the United Nations adopted guidelines to help governments create legislative and policy environments conducive to the establishment of autonomous cooperatives (Pollet and Develtere, 2004, p. 21). This official recognition of the need to liberalize the relationship between cooperatives and the state and to deregulate cooperative sectors was the result of a lengthy consultation process between national governments, cooperative movements, the ICA and the ILO. Consequently a number of governments began to devise strategies for their disengagement from the cooperative sector (Couture, 2003, p. 56).

In 2002, the ILO Recommendation on the Promotion of Cooperatives

(No. 193) was endorsed. With it, all constituents recognized the importance of cooperatives in job creation, mobilization of resources, generation of investment and their contribution to the economy. Modern cooperative policies directed at harnessing such effects therefore tend to see cooperatives as just one business organization among others.

Subsequently over 60 countries have codified the new, restricted role for government in regard to cooperatives in a new cooperative law or are in the process of doing so (Birchall, 2004). Some go so far as to limit themselves to the prescription of minimum standards for the internal governance and external supervision, while others take a more active promotional stance. Some seem to want to cover every type of cooperative and every eventuality, while others leave a lot of discretionary freedom to the members.

Perhaps the most remarkable evolution over the years has been that, in the course of ICA, ILO, FAO and eventually COPAC endeavours, the basics of an international cooperative law have emerged. *Hagen Henry* (2005, p. iii) explains the historical process which led there in his foreword to the second, revised edition of the ILO Document "Guidelines for Cooperative Legislation". There is now in the public domain a set of international legal instruments which pre-shapes national cooperative laws. COPAC, whose members engage in cooperative policy and legislative advice, is committed to recognize the legal nature of these international instruments and advises its members to do so as well.

However, the message has not been heard everywhere. Sometimes the cooperative law is published in the official national language, but the primary addressees might neither be able to read nor understand the legal terminology (Henry, 2005, p. 16). The promulgation of cooperative laws in vernacular languages, the use of an accessible style or the adoption of a law that can be understood as far as possible (without having to resort to other texts) are still not common. Law makers are frequently reluctant to use language which would be inconsistent with that of other legal texts, apprehensive of harming the cohesion of the

entire legal system.

Some countries find it very difficult to abstain from direct interference in the cooperative sector, because too many jobs depend on it.<sup>14</sup> In others, the new definitions of cooperative values and principles inherent in the international declarations have either not yet been included in government policy or legislation or they have not filtered down to cooperative members or the general public (Pollet and Develtere, 2004, p. 22). Much remains to be done in respect of the business and the membership rights of women (Birchall, 2004, p. 20).<sup>15</sup> In many countries the wide spectrum of activities (other than agriculture and credit) which cooperatives can potentially be involved in has not yet been fully accommodated in policy or law.

More liberal cooperative policies can only become effective if they are complemented with adequate policies governing (at least) competition, taxation, labour markets and the states' endeavours in SME promotion. In reality, however, too many prospective member businesses, professionals or individuals are prevented from forming a cooperative, or getting it legally registered as such, by less than liberal legislation in these areas.

Local licensing and the hurdle of paying taxes are likely to be among the chief hindrances. Other barriers stem from the practicalities of the type of business SMEs and informal (vocational) traders are in. For example there is an ongoing dispute in some European countries about whether cooperatives can be organizations in the so-called "common interest". In many countries organizations which are recognized to work for the common good can apply for tax privileges. <sup>16</sup> Social sector

This applies, for example, to the agricultural cooperative sector in Egypt (*Göler von Ravensburg*, 2007b, p. 772).

See also the paragraph on "Obstacles resulting from mental patterns and ill-defined private and property law" above (p. 88).

This is equally true for developing countries (see Country Information Brazil http://www.usig.org/countryinfo/brazil.asp) as it is for Industrialized Countries.

organizations, which have to compete with other service providers such as non-profit organizations and charities, may think twice about adopting this legal form unless they have some clarity in advance.

#### **Example 6.4: Criteria influencing cooperative formation**

A survey was conducted with potential entrepreneurs cooperators in Germany about the respective criteria influencing their decision about adopting the cooperative legal form. The survey showed that all respondents, regardless of their connections with cooperatives, confirmed the advantages of the cooperative option. That there was no participation in the gain in asset value for the departing member seemed to be of little importance to cooperating SMEs. Free trading of shares was considered only moderately important by non-cooperatives and consultants, whilst new cooperatives and drop-outs argued strongly against the possibility.

Under current German Cooperative law, both the board of directors and the supervisory committee must be elected from the ranks of members. This rule is held by many to be a disadvantage of the cooperative form. Among new cooperatives and drop-outs, slightly more than half were in favour of an administrative board exclusively composed of members. But they were willing to include non-members in the supervisory committee. About half of the "non-cooperatives" and consultants reported that the rule to elect the office-bearers from among the members was unattractive.

The minimum number of founding members (7 until 2006, now 3) required to register the legal form of a cooperative could be perceived as a hindrance. Nevertheless, only seven per cent of new cooperatives and only eight per cent of drop-outs found this minimum too high. However, more than half of the non-cooperatives starting with fewer than seven founder members.

Source: Göler von Ravensburg, Pinkwart and Schmidt, 2003

Another barrier exists when entrepreneurs' cooperatives need or want to enter public tenders. Even where they have to be treated without discrimination vis-à-vis other firms, small, local cooperatives with SME members frequently find that public authorities formulate the tender-projects in such large volumes that they cannot realistically enter for them.

Entrepreneurs' Cooperatives are often limited by categorization in cooperative law to executing a single business function, e.g. purchasing of products (supply cooperative), services (services cooperative) or marketing (marketing cooperative), or the act does not foresee corporate members, only individuals. Some European countries' cooperative policy and law do not always offer ideal conditions for entrepreneurs' cooperatives in relation to aspects of governance. For example regulations may state that only members may be elected to administrative and supervisory boards. Of real relevance is the cost and compulsory nature of federation membership and federation audits, together with the inherent structural disadvantages of cooperatives in comparison with their closest competitors, and what actions policy designers and legislators can or will take to mitigate these.

## 6.4.1 Compulsory audit and image

The formal pre-registration audit, which is compulsory for German registered cooperatives, is frequently considered to be expensive and tedious. However with hindsight, about half of all registered cooperatives and drop-outs surveyed by *Göler von Ravensburg, Pinkwart and Schmidt* recognised the pre-registration audit to be reasonable if not outright helpful for all main establishment decisions. Among the questioned non-cooperatives, around 70 per cent considered an audit of the business concept prior to start-up to be unimportant. Within the group of drop-outs, those who continued cooperating in another legal form generally held a more negative opinion of the pre-registration audit than did those drop-outs who ended their cooperation as a result of the audit. The study also discovered that only a small portion of all

SMEs in Germany were aware of the cooperative as a form of organizing inter-company cooperation. This is much more surprising because Germany is one of the few countries where a tradition of entrepreneurs' cooperatives has existed for 150 years.

#### **Example 6.5: Cooperative image constraints**

The relevance of a positive image of a legal form has been explicitly confirmed in the "delphi-inquiry" of that study. The choice of organizational structure for inter-company cooperations depends particularly on whether or not a legal form is perceived to be up-to-date. More than 80 per cent of the questioned cooperatives consider that this is so for their legal form, but nearly 70 per cent of the questioned non-cooperatives see this to be more or less out-of-date. Cooperatives are mainly associated with agriculture and credit, so enterprises and professionals in other sectors (or with needs other than credit) were not aware that the cooperative form might apply to their own businesses. Consultants stated with a large majority that they were less familiar with the cooperative form than with the limited liability company or other legal forms.

Source: Göler von Ravensburg, Pinkwart and Schmidt, 2003, pp. 38-39

### 6.4.2 Policy measures to offset disadvantages

In its 2001 communication on the issue of cooperatives in Europe, the European Commission (p. 13) lists the following main disadvantages of the cooperative "formula":

 "Membership orientation can cause difficulties in diversifying products and services to take advantage of new opportunities where such opportunities may have no relation to the interests of the members. The allocation of

- capital to its most efficient usage is therefore less effective through cooperatives than via stock markets;
- Limited access to external equity capital through available capital markets can lead to dependence on loan capital where members own capital is insufficient. Restricted voting rights (normally one person - one vote) can be a disadvantage in attracting risk capital without commensurate voting power;
- Democratic governance can lead to a slow decision making process;
- A large membership base can result in failure to keep abreast of members' needs and interests; in cases where members invest modestly this can lead to modest member interest and activity to develop the enterprise;
- The easy exit and entry to cooperatives can potentially cause problems to the stability of the enterprise due to exit of active members (for example on retirement of a farmer in an agricultural cooperative) and other development factors;
- Lack of understanding of the particular nature of cooperative management in traditional enterprise support and advice services; and
- Access to public procurement, whilst public authorities sometimes consider cooperatives as non-profit organizations and therefore ineligible as bidders."

Entrepreneurs' cooperatives are most likely to be affected by these disadvantages. For example, those active in trade are usually in fierce competition with integrated retail chains<sup>17</sup> and those non-cooperative wholesalers which trade on a worldwide scale (Dobson and CRA)

Frequently integrated retail chains have brought wholesale functions into their businesses, thus profiting from both horizontal and vertical integration (Dobson and CRA International, 2006, p. 21).

International, 2006, p. 14). For them the first two arguments are particularly relevant.

Smaller entrepreneurs' cooperatives, with producing SMEs as members, frequently find themselves competing with public and not-for-profit service providers, particularly in the social and educational fields (Göler von Ravensburg, 2006, p. 113-115). They are affected by difficulties in accessing capital as well as public procurement and by comparatively slow decision making.

In recent years all European countries have undertaken legislative efforts not only to help reduce the restrictions for cooperatives in the founding process, but also in reaching financial markets. Such reforms have included (EC, 2001, p. 17)<sup>18</sup>:

- reducing the minimum number of persons required to create a cooperative;
- the possibility of giving some members more than one vote;
- broadening the limits on activities and on trading with non-members;
- the possibility of issuing specific bonds, representing risk or debt capital;
- allowing third parties to participate in share capital; and
- permitting the transformation of cooperatives into jointstock companies.

It can be argued that some of these developments run contrary to the cooperative principles, but in the European Union they have been considered desirable in order to satisfy the needs of growing cooperatives in a modern economy. Today entrepreneurs' cooperatives in developing countries are facing both the same structural disadvantages and the

The Table in Appendix 1 (pp. 151) to this Consultation Paper gives an overview of the legislation governing cooperatives in the Member States particularly identifying where such provisions exist.

same competitive situation, so they might be able to profit from similar legal provisions.

## 6.5 Cooperative unions and (con-) federations

This description, which can be found on the homepage of the *British Columbia Cooperative Association* (see below), is fairly representative of a modern mission statement for a cooperative federation.

Unfortunately not all federations and cooperative unions are equally open to new cooperative ventures, such as entrepreneurs' cooperatives. Most existing federations are of well-established "traditional" cooperatives, such as agricultural cooperatives. In many countries entrepreneurs' cooperatives have no such traditions, so cooperatives

#### **Example 6.6: British Columbia Cooperative**

#### Mission

To build a cooperative economy that promotes social and economic justice and advances the well-being of British Columbians and their communities.

#### **Vision**

BCCA is the voice of the BC coop movement and strives to build a cooperative economy that unites and mobilizes cooperatives as a leading force for progressive economic, social, and environmental change.

Through our work, we will advance a vision of society that is caring, creative, and humane. We will realize our vision while embracing the international cooperative principles, and by creating a workplace that inspires staff through our core values of mutual respect, trust, cooperation, and excellence.

**Source**: http://bcca.coop/

in non-traditional fields cannot always obtain support from the existing federations. Without strong vertical and horizontal cooperative integration, however, we agree with *Birchall* (2004, p. 47) when (based on *Putnam*) he argues:

"Cooperatives can also be isolated, and may like other local groups be high in 'bonding social capital' but not be able to find the 'bridging social capital' that will link them to others."

In addition there are further problems faced by federations and their members, which hamper their effectiveness in creating economies of scope and scale for the primary cooperatives (including entrepreneurs' cooperatives) who are their members.

In some developing countries and countries in transition governments still have a tendency to control federations and unions and to staff them with their own personnel (Kötter, 1994, p. 800; ILO, 2000, p. 90-92). In other countries, federations have become so powerful that they not only suppress the interests of competing groups, but also infiltrate government structures of their own volition and use the functions there for their own gain. Where programmes of de-officialization<sup>19</sup> have begun, most federations are encouraged to concentrate on those core issues that they best understand. The promotion of entrepreneurs' cooperatives usually does not fall within this and such de-officialization processes often take some time to show positive results for the primary cooperatives, which are already members of the federation. In all of these cases no impetus to support entrepreneurs' cooperatives can be expected.

It also appears that existing cooperative federations and syndicate

This represents a comprehensive management of change process in which a federation (for whichever reasons is highly influenced by the state) is "privatized" to its "members", the primary cooperatives, who from then on take responsibility themselves for the secondary and tertiary level organizations.

structures are not always well prepared to keep abreast of the increasing speed at which structural change towards an industrial and service economy occurs (Schwettmann, 1998; Kirk, 2003, p. 437; Fehl, 2003; ICA et al., 1999). This might be a significant reason why many opportunities to offer lucrative services that the state is abandoning in the course of SAPs are not taken up by entrepreneurs' cooperatives, as they are in North America and Europe. Instead other legal forms are chosen to offer such services (Birchall, 2001).

Entrepreneurs' Cooperatives aren't always well represented in approaches to political decision makers. Sometimes their numbers and turnover do not warrant the establishment of special unions, associations or federations at a regional or national level.

Wide disparities between cooperatives at different levels exist in most developing countries, with the primary cooperatives being weaker than the secondary federations, and with the apex level federations being the strongest. There is still a significant level of government interference at that level of the cooperative movements in most countries, and clear national policies aiming to clarify the nature of cooperative federations are overdue.

#### 6.6 Administrative barriers

Apart from ineffective federations and flaws in national policy and law regarding SMEs and entrepreneurs' cooperatives, there are also problems relating to administrative structures and processes. Many cooperative administrations relate too little with federations, and have become too large and unwieldy or do not know entrepreneurs' cooperatives well enough to be able to promote them properly. Other problems stem from a lack of adequate data on entrepreneurs' cooperatives.

## **Example 6.7: Entrepreneurs' cooperatives in Europe**

Most European countries have national level unions of retailers or wholesalers in the food and non-food sectors. At the European Commission level they are represented by UGAL (the Union of Groups of Independent Retailers of Europe). UGAL represents 31 groups and associations in Europe, gathering together more than 325,000 independent retailers with a retail turnover of more than 473 billion euro and employment upwards of 3,586,000.

This body, with a further seven sectoral associations (ACME, CECODHAS, CECOP, COGECA, EUROCOOP, GEBC, UEPS and UGA) forms the Co-ordinating Committee of European Cooperative Associations (C.C.A.C.E.). This in turn coordinates the representation of common interests of all kinds of cooperatives and includes amongst its members certain national, multi-sectoral cooperative associations. The European Commission has frequent contact with the individual sectoral associations and the C.C.A.C.E. on cooperative issues.

The International Cooperative Alliance (ICA), based in Geneva, adopted a regional structure in 1994 and now has a vice president and director for Europe. In the past ICA Europe has not been particularly active with respect to EU issues, although the level of such contact and activity is increasing, particularly in relation to enlargement. The role of the ICA as a "guardian" of the cooperative principles, rather than as a sectoral interest group, makes it an important interlocutor for the Commission.

**Source**: Author's own analysis

#### 6.6.1 Administrative structures and federations

The problems described by the European Commission are fairly

symptomatic and by no means limited to the European Union, where cooperative policy has to a degree become a unified effort. They are as relevant to cooperative development in all other countries, whether industrialized, threshold and developing countries and for all types of cooperatives, entrepreneurs' cooperatives included.

Something else can be deduced from this statement: The character of

#### **Example 6.8: The EU consultation paper on cooperatives**

"The very diversity of cooperative enterprises, and their inherent double nature as both enterprises and associations of members, has led to the adoption of diverse ways by Member State authorities to deal with their regulation and development in a co-ordinated way. This is reflected in the variety of ministries that have responsibility for the cooperative sector in different Member States. In recent years several European governments have made efforts to increase the coherence of their administrative structures in this respect....

..... Nevertheless, cooperative organisations complain about a frequent lack of knowledge, or, more seriously, a misunderstanding of the cooperative form within the public authorities with which they deal. This can lead to a lack of sensitivity to the specific character and needs of cooperative enterprises in the context of more general policies. There is also much concern that there is no reflex to consult cooperative organisations regarding regulatory initiatives that may This lack of understanding may also lead to lost opportunities for the promotion of cooperative models where they might be advantageous, for example in considering how to provide services previously provided by the public sector."

**Source**: EC, 2001, p. 30

cooperatives is perceived differently in different European countries. This is mirrored in the decision reached about which ministry or authority is to represent the interests of the whole cooperative sector (see also Henry, 2005, p. 15). The EU emphasizes the representation through a Ministry for Social Economy, while many national cooperative movements see themselves firmly rooted in the private sector and especially in the business sectors. They tend then to find other channels for representation.

In many developing countries cooperative matters are dealt with by ministries or departments of agriculture, since agricultural cooperatives are the dominant cooperative form. Of course, these authorities neither have the imperative to promote cooperatives in non-agricultural production, among small business people, in the urban informal economy or among professionals. Nor do they have the knowledge to assess business prospects in all sectors and branches or to advise applicants accordingly. As a result, good applications are turned down for these reasons.

In other countries the responsibility for cooperatives is spread over several ministries or administrations, such as a ministry for economic affairs or a health authority. This necessitates cross-departmental communications including questions relating to changes in the Cooperative Act, to cooperative regulations and statutes, to discussions about promotional efforts and the legitimate nature of cooperative endeavours. These questions may bring with them the need for feedback mechanisms among all administrative units dealing with cooperatives.

Many countries have a registration office, so where responsibilities and powers are diversified, this might be the office to which all communication has to come. At the same time there is a danger that a registrar might be partial to that cooperative sector which best fits to a particular ministry's brief.

Lastly, but perhaps most importantly, many cooperative administrations in developing countries have developed into large, unwieldy bureaucracies

with insufficiently qualified staff. Due to lack of budgets or de-officialization induced downsizing, the personnel often have little motivated. Often there is no cooperation between authorities and the respective cooperative federations. Instead there is great fear that cooperation with federations makes the administration even more obsolete, costing even more jobs. There can even be apprehension about unwanted lobbying, private sector interventions in one's core business, and there may be bribery. That is both understandable and regrettable, because it negates the potential which federations can have to advise both the applicant cooperative as well as the registrar on particular sector economies. Of course, cooperation between administration and federations needs to be properly governed and controlled.

#### 6.6.2 Lack of data

Accurate statistical data is an essential tool in understanding the nature of a sector and in developing suitable policy. As the EC states (EC, 2001, p. 30):

"Accurate data and efficient consultation, both between public authorities and with representative organisations, are fundamental to developing appropriate policies and programmes for cooperatives."

To date statistical information regarding entrepreneurs' cooperatives is very scarce. Whatever has been collected is based on either business registry data or survey data.

Business registry data tends to underestimate the importance of cooperatives (Commission of the European Communities, 2001, p. 31). In most countries a large number of cooperatives remain invisible in such data, because they operate in a legal form different from that of a registered cooperative. Business registry data can have the methodological advantage, however, of making possible a breakdown of activities according to their sector of activity. Survey data, on the

other hand, is normally collected via representative organizations<sup>20</sup> and as such is only as good as the quality of responses to questionnaires.

Depending on the system "double counting" can occur, particularly where one cooperative is a member of more than one federation. Survey data may include many activities that are not strictly undertaken by cooperatives. For example many cooperatives have non-cooperative subsidiaries with significant turnover. Frequently, data relating to the member companies of a secondary cooperative might be included in the turnover or employment figures for the primary cooperative itself.

The patchiness of data resulting from either source makes it impossible to have an accurate understanding of the importance of entrepreneurs' cooperatives even in Europe, let alone in countries less well endowed with statistical and academic competences. This lack of regular data makes it impossible to have a dynamic view of the development of entrepreneurs' cooperatives over time.

### 6.7 Active promotion of cooperatives

According to *Pollet and Develtere* (2004, p. 22) there is a great deal of renewed international interest in the promotion of cooperatives. Within the general movement towards more involvement of civil society in development, several donor countries have expressed their positive attitude towards cooperatives in that respect.

Regardless of the source of promotion, several critical points need scrutiny when active promotion of cooperatives is being considered (Göler von Ravensburg, 1999, p. 157):

 local economic potentials and indigenous structural limitations are not always sufficiently well known;

In the EU for example a major study was financed by the European Commission in 1997 and undertaken by the International Cooperative Alliance.

- legal formalization of local self-help efforts can lead to estrangement;
- much training and education is necessary to enhance competencies;
- sustainability can be achieved only if secondary, federation structures are developed alongside the primary entrepreneurs' cooperatives; and
- Entrepreneurs' Cooperatives should not become dependent on (just one) external partner(s).

What happened to many cooperatives which were offered extensive support in the past could happen again. Officialization of cooperatives mostly resulted from excessive financial and administrative support by the public sector (Hanel, 1992b, p. 28). Only because private sector support did not reach the same level, are there few cooperatives that depend on such sources. entrepreneurs' cooperatives were hardly affected in developing countries only because few of them existed. Actively promoting them means risking similar negative effects. Much depends on the people involved in the promotion of entrepreneurs' cooperatives (Hanel, 1992).

Advisors to, or promoters of, entrepreneurs' cooperatives should be able to help make sensible and locally appropriate decisions on the need for, and the way towards structure, level and content of formalized cooperation. The demands on such promoters in terms of skills, knowledge and attitudes are fairly high (Shah, 1999, p. 49). They must have knowledge of the relevant sector economics and production processes, have good communication skills, be good mediators and have leadership qualities. At the same time they must accept that democratic rules govern the cooperative as soon as it is established. Their attention must be focussed on educational rather than administrative matters. To remain motivated they must have a great deal of identification with cooperative principles and aims. They are expected to invest their time and creativity into start-ups, whilst

at the same time needing to divorce their personal expectations of success from their expectations for the cooperative. Most importantly, they must accept that cooperative endeavours are driven "from below". It is the members' prerogative to set the goals, decide on strategy and vote for their leadership.

Promoters can be members of the entrepreneurs' cooperative (internal promoters) or external promoters, employed by not-for profits or cooperative federations for the purpose.<sup>21</sup> In either case, they will neither profit from the endeavour (any more than fellow members or colleagues), nor will they be granted a great deal of external acclaim. They work to become dispensable, something which many state employed promoters have not found easy (Shah, 1999, p. 190).

#### 6.8 Attitudes of business communities

The attitude of the business community towards cooperatives is important in two respects. Cooperatives among SMEs, craft people and professionals will only be started if the image of the cooperative form is reasonably positive or founder members will opt for other legal forms. Furthermore, the continued development of an entrepreneurs' cooperative is much influenced by its competitiveness with companies organized in a different legal way and its positive relations with suppliers and purchasers.

Members often remained in state controlled (agricultural) cooperatives in developing countries because membership was compulsory, especially in agriculture. Or they remained because the cooperative had the status of a monopoly whilst other cooperatives provided its members with guaranteed prices, tax privileges, or with subsidies and other support measures, making members dependent on them.

When states had to withdraw support for cooperatives because of a lack of

See Chapter 5, especially the sections on starting new cooperative SHOs and on critical internal factors.

funds, frequently only the privatized, competitive cooperatives survived. Yet, the business community in many developing countries often still associate tight state controls, state interventions, bureaucracy mismanagement, lack of reliability and corruption with the word "cooperative" (Pollet and Develtere, 2004). Small business people and professionals frequently do not want to be members of such organizations or trade with them for these reasons. Sometimes they also consider cooperatives to be "poor men's clubs", never to develop into viable businesses. In other cases, when they have succeeded in using economies of scale, cooperatives are accused of being "ordinary business undertakings". The business communities' attitude is varied and frequently less than objective.

However, the policy changes outlined above, as well as the increased efforts of some northern cooperatives and cooperative development agencies, are beginning to have initial effects on the cooperative image (Pollet and Develtere, 2004).<sup>22</sup> For example, a number of international corporations currently maintain business links with cooperative organizations in developing countries (See for example Jenkins et al., 2007, p. 49). Such cooperation presents opportunities and challenges for business. But inequalities in market power between the partners in these negotiations can result in a loss of much of the entrepreneurial freedom of disposition. However, if the cooperative negotiates well for its members, and the normative environment is conducive, excellent opportunities are presented to maximize the organization's benefits for having organized cooperatively in the first place.

See as well "Appendix 4: Fair Trade Organizations which work with Cooperatives or entrepreneurs' cooperatives".

## Chapter 7

# Legal and policy framework for good practice

Efforts geared towards increasing the self-help capacities of entrepreneurs, professionals, SMEs and even larger firms in developing countries are seen to reduce the possibility of "leakage" of development funds, as funds go directly to citizens rather than via government agencies (EC, 2001, p. 29). When using a cooperative approach they are frequently based on the creation of favourable legal frameworks and on the availability of cooperative advisors (Münkner, 2000, p. 14-15). Such approaches are most promising in a normative environment - upholding basic human rights, maintaining legal certainty, and allowing markets to function as widely as possible. They also limit the role of the state to services which neither business nor civil society organizations render in sufficient quality or quantity.

In industrialized countries today, entrepreneurs' cooperatives thrive in competitive markets. Although they do not seek to maximize profits on capital, they have achieved significant market shares in areas where capitalised companies are very strong. This includes areas such as insurance, food retail, pharmacy and fair trade. They are growing quickly in the sectors of health care and services to business and education (EC, 2004, p. 3).

Legal and other barriers to the establishment of entrepreneurs' cooperatives still exist around the world. National Consultations leading the Extraordinary Summit on Employment and Poverty Alleviation held in Burkina Faso in 2004, as summed up in an ILO Report titled "Working out of poverty. Views from Africa", state as reform a priority (ILO, 2003, p. 10-11):

"Several countries reported that cooperatives were an effective approach to poverty reduction in the agricultural sector and the informal economy, while acknowledging that support was needed to:

- establish a conducive legislative, regulatory and institutional framework;
- develop organizational and managerial tools to foster ownership, accountability and effective participation; and
- integrate different types of cooperatives into national cooperative movements."

With respect to the promotion of SMEs, the same report also states:

"In order to improve the situation, the participants felt it was necessary to:

- establish policies and a regulatory and legislative environment that would stimulate enterprise growth and development, thus encouraging enterprises to start-up, grow and create jobs;
- invest domestic savings in enterprise and job creation;
- facilitate access to product markets, capital, training and information; and
- provide education, training and efficient business development services as indispensable ingredients for successful entrepreneurship."

Apart from the interest shown in entrepreneurs' cooperatives, the report is only one of many signs of the willingness to let go of political and legal provisions, which for so long have hampered the development of cooperatives in many developing countries. This appraisal is supported by various annual reports of the International Cooperative Alliance, especially the 2001 report. Within these are the reports of the Regional Representatives for Africa, Asia and the Pacific (ICA, 2001, p. 9-12), as well as by Mr. *Michael Henriques'* (Director, Job Creation and Enterprise Development) in the opening statement to the Regional Conference on Employment Creation through Cooperatives and Small Enterprises in Bangkok in 2001 (ILO, 2001b, p. 1-2).

With this drive in mind, this chapter discusses what constitutes policy and law that is favourable to entrepreneurs' cooperatives (in developing countries). That these modern cooperative frameworks should no longer offer special promotion to cooperatives, but concentrate on non-discrimination (positive or negative) of the legal form, has repeatedly been stated throughout this book.

We want to start by establishing what main governance issues are special or different for entrepreneurs' cooperatives, relating back to what was said in Chapters 5 and 6. We then highlight various international efforts at policy and legal advice, which hold positive repercussions for entrepreneurs' cooperatives and deduce what currently characterizes good entrepreneurs' cooperative promotion. Thirdly we conclude that what needs to be done at national levels in order to create favourable policy environments that are conducive to cooperative legislation in transitional countries and developing countries. Also to look at the roles cooperative federations and networks can play as well as point to a smaller issue, which nevertheless is important for the image entrepreneurs' cooperatives can display worldwide (namely data collection and analysis).

## 7.1 Governance requirements of entrepreneurs' cooperatives

Organization of common business (working to a robust business and marketing plan and appointing a secretary or board to deal with the legal requirements of running it) is as necessary for an entrepreneurs' cooperative as for any other business. However, there are a number of issues that affect them particularly. Even though it may adopt any legal form, which can be adapted to the definition described in Chapter 2, and even though specific legislation is neither necessary nor a guarantee that its cooperative nature is maintained, entrepreneurs' cooperatives show some peculiarities. These will have to be considered when fashioning adequate internal governance patterns (e.g. statutes, by-laws or articles of association).

#### 7.1.1 Internal financial relationships

A high level of trust and personal honesty between members is an essential pre-requisite for the effective functioning of this type of cooperative. This cannot be created without a minimum of legal requirements and macro-economic stability. The financing of entrepreneurs' cooperatives is usually carried out, in the first instance, by members providing funds in the form of buying shares, paying membership fees or in the form of loan capital. These are signs of the members' commitment to the venture and may be needed if loans from a financial institution are required.

How monies are raised from members may depend on the legal form chosen and this affects how such monies are shown on the balance sheet. For many entrepreneurs' cooperatives this is a straightforward issue. But for some, especially those with extensive assets, it will be complex.

Another way of increasing capital in the course of the life of an entrepreneurs' cooperative is the build up of reserves. Statutes can regulate this, yet national legislation might also regulate minimum

levels of surplus allocation to the reserves.

There can be a variety of payments made to the entrepreneurs' cooperative by members. There could be an annual payment, a commission may be levied on goods sold or a percentage of the value of produce handled or services obtained. These will vary according to the industrial sector and the wishes of members.

Members decide whether the cooperative takes ownership of the goods or produce before it sells them on, or simply sells them as an agent on the members' behalf. The latter might be preferable to minimise risk and liability in the case of faulty goods. The first kind (the full business entrepreneurs' cooperative) provides more clarity with regard to members' status as self-employed or independent businesses. In both cases membership agreements should include stipulations on quality control and procedures for dealing with faulty goods (see below).

Accrued surpluses will be used to pay dividends or refunds on the members' trade with the cooperative during the previous year, but each cooperative will need to develop its own policy on retention of surpluses. Few entrepreneurs' cooperatives will, in practice, build up large surpluses or reserves, and income will be passed on to members through the sale of the product or service at the time, or be reinvested in central services or marketing. Nevertheless a policy for retention of surpluses and a robust system for dealing with dividends, where they occur, needs to be formulated. In the case of mutual trading status the word "bonus" or "return of charges" usually more conform with tax law.

### 7.1.2 Internal business relationship

Members want to receive fair treatment by systems and staff. There must not be preferential treatment of any member in the sale of their goods, services or in marketing or promotion. Systems for the smooth and fair treatment of members need to be established because high

levels of trust will make the business more efficient.

The entrepreneurs' cooperative will be answerable for the responsible employment of staff, such as administrators, finance officers, cleaners and so forth. This may require a dedicated personnel function undertaken by one member. There may also be payment made to the secretary or manager of the entrepreneurs' cooperative for work done.

In any entrepreneurs' cooperative there may be some tension between the independence of the sole trader or SME member who wants to make an impact or have his/her voice heard and the need for a collective approach. These tensions are lessened if there are clear formal agreements in place for decision-making with transparency and good communication the key mechanisms. The methods may be determined by the nature of the business; quarterly meetings, regular reports, business update bulletins, email or telephone.

Developing a strong cooperative brand requires the option to reject members' products or services considered to be of sub-standard quality. Quality control by peers is often cited as an important benefit of membership of a cooperative and tends to raise the overall quality of all members' products. This is provided systems are in place to ensure that the process causes no conflict and there are clear terms of engagement including a process for appeal and redress, ideally including ways of dealing with customer complaints.

The right of members to sell outside the cooperative also needs to be clearly defined. In such circumstances the pricing of items must be laid down to avoid undermining the viability of the cooperative - should customers learn that they can get a better prices by buying directly from the producer or contracting directly with a member. A cooperative may decide to develop policies on the commitment of supply of goods or services meeting the required standards from its members, but these need to be legally enforceable.

#### 7.1.3 Rules for dissolution and discontinuation

A formally agreed method of redistribution of all assets and reserves owned by the cooperative, as a business entity, is necessary to meet the eventuality of dissolution of the cooperative or if members choose to leave. A common approach in both cases is that all investment by members is given back at par, with possible surpluses having been redistributed periodically (according to the extent of trade) and with any losses being offset against members' share holding. Reserves tend to be appropriated according to legal or statutory provisions.

In entrepreneurs' cooperatives the payback periods to members leaving can vary from two to 10 years. Shorter periods might burden the cooperative's cash flow, longer ones increase the need for record keeping and mean extra administration. Depending on national legislation, entrepreneurs' cooperatives on dissolution may choose to grant assets to a charity, a good cause or to another cooperative.

#### 7.1.4 The need to adopt statutes

Fundamental to the good working of the entrepreneurs' cooperative and maintaining the commitment of its members are a mission statement, clear objectives and agreements to which members will adhere. These will need to be reviewed regularly. Good systems for communication and transparent decision-making will help to maintain the ethos of the business and the satisfaction of its members. The salient points agreed should form the basis of a set of statutes.

#### 7.1.5 Labour law and employment status

An agency-type entrepreneurs' cooperative provides its self-employed members with central services, so they usually want to retain as much as possible of the profits made from each piece of work. If members pay a regular membership fee or if they give back a percentage of their earnings to the cooperative, they clearly signal that they are

self-employed. Where or when the cooperative invoices third parties, receives money and then reimburses the member, it is more difficult to argue for self-employed status, especially if the member's business is very small and all but relies on the entrepreneurs' cooperative as its prime customer. Indeed if a self-employed individual receives the bulk of his or her income from the cooperative, the responsible tax authorities (e.g. the Office of Inland Revenue) may rule that he/she is an employee and should pay income or wage tax on the income from the entrepreneurs' cooperative.

Often the tax authorities are also responsible for making decisions on the status of a sole trader member of an entrepreneurs' cooperative. Money flow, the economic dependency of the member on the entrepreneurs' cooperative and issues, such as holiday pay received from the cooperative, seem to be decisive factors. However, there are no hard and fast rules, and decisions about employment status may vary according to the tax office concerned.

#### 7.1.6 Mutual trading status

If a cooperative can persuade the tax authorities that it is a mutual trading organization (MTO) for the common good or non-profit organization (NPO), it might become exempt from paying company tax, corporation tax or other taxes on profits earned from business with its members. To qualify for such a special tax status, the entrepreneurs' cooperative must often have the following characteristics:

- there must be a complete identity of status between those who contribute to a surplus and those who are entitled to the return of that surplus (for MTO status);
- surpluses must be returned to contributors in their capacity as contributors. In practice what this means is that only service-users may be members (not employees or others) (for MTO status);
- surpluses must either be returnable to the members (not

given for charitable purposes or otherwise), and assets must be returnable to members (so common ownership or 'philanthropic distribution' clauses are out) (applies for MTO status); and

 surpluses must not be distributed to members (applies in most countries for NPO).

None of these hurdles are insurmountable, but all need to be understood and discussed by the founding members. Decisions reached need to be enshrined in the governing documents of the business (the statutes) and in the general approach to business. They may need reviewing at intervals and members should be encouraged to sign up to them on starting or joining the cooperative.

## 7.2 International policy and legal advice

As we have said, efforts to actively promote entrepreneurs' cooperatives depend primarily on the recognition of the role they can play for SMEs, professionals and the informal economy. The local economic development climate and the general image of cooperatives influence promotional success. Sometimes these factors are more important than the administrative ease and costs of starting-up. How well entrepreneurs' cooperatives develop largely depends on two factors: How they are treated in competition and tax law and on the availability of cooperative entrepreneurship and management skills.

Regardless of whether cooperation is in formal or informal entrepreneurs' cooperatives, in most countries it is unlikely that promotional efforts will come from existing cooperative federations and unions. Instead, most entrepreneurs' cooperative promotion in transitional countries and developing countries is currently undertaken by capitalized companies (as private enterprise linkages), by development NGOs and by cooperative syndicates from the northern hemisphere (Pollet and

<sup>1</sup> See Chapter 6 "Cooperative unions and (con-) federations" (p. 100).

Develtere, 2004; Jenkins et al., 2007; Wahl et al., 2007; Meyer-Antz, 1996). All these external promotional efforts have to rely on national legislation and public policy.

### 7.2.1 Tripartite agreements on cooperatives

In Bangkok in 2001, Asian governments and employers and workers organizations presented their views on how they promote (shared service) cooperatives (ILO, 2001b, p. 8-11). They offered the following conclusions about favourable legal and policy environments for cooperatives (ILO, 2001b, p. 12-13):

- "37. Cooperative law and related legislation:
- a) It is important that the cooperative law should be simple and can be understood by the members. It should respect the autonomy of cooperatives and move towards selfregulation.
- b) Government's role should be primarily as a catalyst/facilitator and not controller or intruder.
- c) Outsourcing may create opportunities for workers' cooperatives but this should not be used against the interest of trade unions.
- 38. Institutional and administrative environment:
- a) Restrictions on organizing trade unions, cooperatives
   must be removed because it contravenes freedom of association.
- b) Coop organizing must meet all tripartite interests by bringing mutual benefits to them, being sensitive to their needs, and publicizing good practices for replication/adaptation."

The report on the Tenth African Tripartite Meeting in Addis Ababa in 2003 states that (ILO, 2003, p. 10):

"Several countries reported that cooperatives were an

effective approach to poverty reduction in the agricultural sector and the informal economy, while acknowledging that support was needed to:

- establish a conducive legislative, regulatory and institutional framework;
- develop organizational and managerial tools to foster ownership, accountability and effective participation;
- integrate different types of cooperatives into national cooperative movements; and
- apply the cooperative concepts to new areas, such as shared service cooperatives for small businesses."

This indicates a search for improved policies and legal frameworks for the cooperative sector.

### 7.2.2 International measures to promote cooperatives

In the USA 'the Support for Overseas Cooperative Development Act' was passed in 2000. With this act Congress clarified that "it is in the mutual economic interest of the United States and peoples in developing and transitional countries to promote cooperatives and credit unions" (Pollet and Develtere, 2004, p. 22). The act requires the United States Agency for International Development (USAID) to promote all types of cooperatives and identifies five key areas in which to do this (Pollet and Develtere, 2004, p. 22):

- "new cooperative solutions to help rebuild HIV/AIDS devastated communities in East Africa;
- seek better understanding and methods to adapt Western cooperative approaches to emerging market economies;
- target assistance to local cooperatives through their stages of development to achieve greater scale and impact;
- strengthen networks of cooperatives to solve multiple

economic and social challenges and advance specialized cooperatives in agriculture, financial systems, community owned infrastructure and community services; and

 develop new analytic tools on the strength and weakness of cooperatives to promote them with multilateral institutions, such as the UN and World Bank."

The Act also defines two kinds of 'Cooperative Development Organization', namely cooperatives from the northern hemisphere or organizations with an "organic link" to the US cooperative movement engaged in development activities that focus upon the promotion of cooperatives south of the equator.

Several development policies of European countries mention cooperative development in the course of sustainable socio-economic development. Frequently development agencies see cooperatives in the South as an element of the social economy or as linkages for fair trade or environmental issues.

# 7.2.3 International cooperative legislation

Over the past few years the beginnings of an international cooperative law have been developed. *Henry* (2005, p. iii) summarizes the process which led there in the Foreword to the ILO Document "Guidelines for Cooperative Legislation". He then goes on to explain the essential character of these guidelines.

The main intention of these Guidelines is to bring cooperative laws in line with the universally recognized cooperative values and principles. This, it is thought, will ease cross border cooperation between cooperatives and their federations and thus be an adequate answer to the need for regional and international economic integration. Importantly, the Guidelines provide only a checklist and leave space for the particularities socio-economic and legal conditions, so that legislators can adapt the concepts to the local context.

The Guidelines can help national cooperative movements to safeguard their individualities by providing a universally accepted profile which differentiates cooperatives from stake-holding companies. This is precisely in order to demonstrate that cooperatives can indeed be an alternative organizational form, which is capable of depicting specific cultural traits specificities. This argument is even more convincing when one considers the lengthy and tedious detours some countries had to take before coming to terms with the character of cooperatives.

However, it is also important to ask to what degree can legal texts actually influence the success of business practices? Furthermore, where are the sanctioning mechanisms which will tie national governments to adhere to such guidelines? How can it be assured that good cooperative law isn't contradicted or rendered useless by more general legislation, such as tax law or competition law? How can people who live under traditional law (or face such dire economic straights that they have only a subsistence level economy access) help in cooperative conflicts, when all institutions foreseen by this guideline represent the "modern" world of markets and money and less by subsistence exchange?

These complex questions can be answered in two ways. Of course modern laws must be harmonized in order to avoid unintended contradictions. Any development law faces severe limits; the impulse to create entrepreneurs' cooperatives will not grow from a new cooperative act, but new entrepreneurs' cooperatives might find success easier if adequate cooperative law and well thought out policies level the playing field between them and other business organizations (thus serving as models).

### 7.2.4 Cooperative legislation in the European Union

Cooperatives are explicitly recognised in the European Union as one type of 'companies or firms' under the Treaty of Rome (Article 48) (EC 2001, p. 17). Within all Member States of the EU (EC, 2001, Appendix 1), cooperatives have a legal framework within which they

can operate (although there is not always a specific cooperative law or even an explicit mention of entrepreneurs' cooperatives). This protects the interests of members and third parties.<sup>2</sup>

Recently acceded countries (ACs) also frequently have long cooperative traditions. However, cooperative enterprises clearly being a market economy phenomenon have experienced problems in those countries that were subject to socialist planning, through an erroneous identification with state collectives and the planning system.

Thus, there are two main issues related to cooperatives in the enlargement process of the EU (EC, 2001, p. 26):

- cooperative enterprises will need to adjust to the competitive context markets; and
- state authorities in ACs may need assistance in developing appropriate regulations for cooperatives, and in the adoption of any potential acquis communautaire in respect of the European Cooperative Statute.

With respect to the former, the most effective means of assisting cooperatives in ACs is to modernise their management, enhance the quality of their financial structures, develop intermediary structures, and encourage their contacts with similar enterprises that thrive within the market.<sup>3</sup> With respect to the latter, public officials from (then) Candidate Countries participated in the group of other public officials established as a follow-up to the recommendations of the Commissions Consultation Paper. They were thus involved in discussions leading to the European Commissions' Communication of 2004 (EC, 2004).

<sup>2</sup> For more detail see Commission of the European Communities (EC) (2001, p. 17-24).

This was the method employed by the Commission co-financed SCOPE project (Phare Business Support Programme) for workers cooperatives in ACs and candidate countries respectively.

Accession issues to one side, European cooperatives have the right to expect equal and fair treatment in the market place. However it still remains difficult to ensure that they are indeed treated equally and fairly compared with other forms of enterprise. This, as we have seen, is particularly important to entrepreneurs' cooperatives as they work in open competition with the vertical and horizontal networks of other forms of economic activity.

Under certain circumstances the EU allows special concessions to cooperatives<sup>4</sup> in order to address the potential disadvantages of the form (mainly related to capitalization and decision making). Two approaches are seen possible in the EU:

- a more flexible regulatory regime can be applied, for instance, by allowing access to traditional equity capital, or voting rights related to share-ownership; and
- a stricter regulatory environment can be applied with particular advantages or derogations being justified in return for respecting these rules.

The choice of approach differs significantly between member states. In all cases the approach is nuanced (but in reality a combination of both exists), and dilemmas created by both approaches are evident. The first approach dilutes the cooperative identity and may ultimately call into question the need for a different legal form. The second approach can lead to accusations of unfair advantages, or worse still, use of the cooperative form purely as a means of avoiding tax. Any such advantages or derogations must be a measured response to the

<sup>4 &</sup>quot;The role of Member States in relation to cooperatives should be to provide a supportive policy and legal framework consistent with the nature and function of cooperatives and which is guided by the cooperative values and principles." The proposition of the Committee on the Promotion of Cooperatives on the 89th ILO International Labour Conference (5-21 June 2001); report by the national cooperative organizations of the Committee, September 2001, p. 66. as quoted by *Commission of the European Communities (EC)* (2001 p. 17.)

restrictions implicit in the cooperative form. In those countries where no specific cooperative legal form exists, the possibilities of the second approach are limited.

When thinking of the special needs for entrepreneurs' cooperatives, it is also worthwhile knowing that the European Charter for Small Enterprises<sup>5</sup> calls on member states and the Commission to "achieve a regulatory, administrative and fiscal framework conducive to entrepreneurial activity". This implies that company legislation should be enabling rather than restrictive. However in the case of entrepreneurs' cooperatives the degree of flexibility must not threaten their nature as member-driven enterprises. Cooperative legislation in the EU tries to assure this in one of three different ways:

- (1) with one national, general law;
- (2) with several cooperative laws, divided according to the sector and social purpose of the cooperative; or
- (3) with no national cooperative law, but by assessing the cooperative nature of a company from its articles of association (statutes or rules).

In EU countries that have one general law on cooperatives there is wide freedom to establish cooperatives and for cooperatives to undertake whatever actions they believe to be in their members' interests. However, in these countries there tend to be no specific benefits or allowances made to cooperatives.

In EU countries where cooperative legislation is divided by sector or purpose, there are frequently special benefits or allowances according to the social purpose of the cooperative. It has been argued, however, that this type of legislation hampers the economic development of the country and that it is not in the long-term interest of either cooperatives

European Charter for Small Enterprises, adopted by the General Affairs Council, 13 June 2000 and welcomed by Feira European Council, 19/20 June 2000 – see *European Commission(EC)* (2001, p. 18.)

or their members.6

In 2001, 10 of the (then 15) member states gave cooperatives (or at least some types of cooperatives) special advantages, mostly in tax law. Some countries also have specific regulations governing the creation or distribution of reserves on winding up. These tend to be countries where cooperatives (and with them entrepreneurs' cooperatives) have a status that is very different from that of other economic entities. While this might be advantageous for those entrepreneurs' cooperatives which depend on public tenders, it might not be at all satisfactory for other entrepreneurs' cooperatives facing full commercial competition, because financial institutions frequently do not regard them as being equal to other companies.

What is highly relevant is that even in the EU there are restrictions regarding the economic sectors in which cooperatives can function (EC, 2001, p. 20). In some cases these may run contrary to European rules on the freedom of establishment. For example, there are cases of cooperatives being excluded from the production and distribution of electric power and the distribution of petrol sectors. This is important, as cooperative models have improved the efficiency of markets and provided protection from monopoly pricing in other countries, thereby securing fair prices for consumers. The European Commission is likely to scrutinize the justification for these restrictions on cooperative's activities very soon.

## 7.3 National cooperative dialogue

When joining an entrepreneurs' cooperative members must be sure

<sup>6</sup> Commission of the European Communities (EC) (2001) p. 19 and source given in footnote 18.

Higher council for co-operation (2000) (Inter-ministerial task force for social innovation and for the social economy, France): Cooperative movements in the European Union. DIES/30 January 2001 as quoted by Commission of the European Communities (EC) (2001, p. 19).

that they are not inadvertently integrated into state administrative structures, such as marketing boards. Members should not be at risk of losing property or contractual rights or be taxed less favourably than before. They will want to retain entrepreneurial freedom of disposition, while at the same time increasing their economic power and planning certainty.

A factual and wide spread understanding of the benefits which entrepreneurs' cooperatives hold for both members and the general public is likely to have more influence on their attraction to potential founders than detailed legal provisions (Göler von Ravensburg; Pinkwart; Schmidt, 2003). On the other hand, the definition of an entrepreneurs' cooperative has to be legal, and this is the basis for equal treatment in terms of taxation and competition law.

By their very nature as enterprises, entrepreneurs' cooperatives need entrepreneurial and managerial resources. The ability to attract good personnel and advice, as well as to access education and training for entrepreneurs' cooperative staff and members has proven to be important prerequisites for entrepreneurs' cooperative development in many countries. These factors also depend on the question of image.

Most national dialogue on cooperative policy and law (as has happened or is happening now in many countries) does cover de-officialization, taxation and competition law, so in this study we shall not repeat the recommendations but refer to the ILO report V (1) of 2001, especially Chapter II, Sections 2 and 3.

For the above reasons such dialogues should include certain topics which are of particular importance to entrepreneurs' cooperatives. The results of dialogue, of course, might necessitate both adaptations to cooperative law or steps to institutionalize certain promotional programmes or projects.<sup>8</sup>

<sup>8</sup> See Chapter 8 hereafter.

### 7.3.1 Ensuring an accurate understanding

Promoting a wider dissemination of the concept of entrepreneurs' cooperatives as formal enterprise networks or clusters reveals the need to explain the areas in which they have a strong role to play (Wahl et al., 2007, p. 5; Göler von Ravensburg; Pinkwart; Schmidt, 2003, p. 85-88):

- entrepreneurs' cooperatives may be a means for building or increasing economic power of small and medium-sized enterprises (SMEs) in the market. The cooperative is a form of company, which allows SMEs to acquire some advantages of size, such as economies of scale and scope, access to markets (including participation in larger public tenders), purchasing power, marketing power, management-development, training and research capacity. entrepreneurs' cooperatives offer an appropriate vehicle for professionals, SMEs and public entities to undertake joint activities and share risks, whilst retaining their independence, including free disposition over their property rights and resources (horizontal integration).
- Entrepreneurs' cooperatives also enable vertical integration of product chains. This can be beneficial for certain professionals and SMEs that are in a weak position in the supply chain, as it can help them to add value to their products and/or services. However most professionals and non-cooperative enterprises remain unaware that the cooperative form might be an appropriate vehicle for such common activities.
- Entrepreneurs' cooperatives are a means for providing high quality services. This becomes increasingly important as economies develop or enterprises want to export. Services represent 70 per cent of output and 69 per cent of jobs in the EU. More than 75 per cent of all new businesses created in Europe are in the services sectors. So, these

must provide increasingly high quality and tailored services to their customers who, in a cooperative, are at the same time its members, and have the power to ensure the responsiveness of the serves that are provided. This means that formal democracy in this way also makes possible a kind of "material" democracy.

- Entrepreneurs' cooperatives are often able to provide services to groups that would otherwise not be able to access them because the supply is not attractive to profit driven companies. This is the case with "proximity services", such as health and welfare, the sectors where cooperatives are growing most rapidly (Göler von Ravensburg, 2006). Similarly entrepreneurs' cooperatives can also help to ensure services increasingly needed by SMEs, such as research and development or marketing become available.
- Entrepreneurs' cooperatives assist in building a knowledge-based society because members, as users, have a real influence over management decisions and thus the participatory management structure of cooperative enterprises fosters development of knowledge and skills. In this sense entrepreneurs' cooperatives act as schools of entrepreneurship and management for those who might not otherwise have access to positions of responsibility.

In order to ensure that entrepreneurs' cooperatives continue to make these important contributions to economic dynamics and growth it will be important for national authorities, as well as interested organizations at every level, to develop or intensify their efforts in fostering a better understanding of the sector.

## 7.3.2 Cooperative policy design

The ILO report "Promotion of cooperatives" (Report V (1), 2000) explains very well what an ideal cooperative policy should be. For this

study we will assume that this report forms the basis of all modern cooperative policy design and add what we find particularly important for the promotion of entrepreneurs' cooperatives, particularly with regard to SMEs' ability to incorporate, grow, and form linkages with larger firms.

All cooperatives really need from the government is an **indirect promotion policy**. This should concentrate on devising a reliable and liberal cooperative law, which maintains equitable taxation of, and competition between, all organizational forms by reducing all restrictions on economic sectors. Also, governments should motivate cooperative entrepreneurship, guarantee a high level of autonomy for cooperatives and their federations and assure that cooperative managers remain accountable to their members (Röpke, 1992, p. 70). In addition to any official promotion of entrepreneurs' cooperatives, there should be support for cooperative apex organizations in the drafting of the related legal framework and negotiating the design of economic policies, strategies and measures (Münkner and Shah, 1993, p. 57).

## 7.3.3 Education and training

Curricula for the management training of cluster organizations of SMEs, professionals and other "actors" in local development tend to be based on the requirements of the predominant business model, i.e. the limited companies. It is therefore hardly surprising that young entrepreneurs rarely consider the "cooperative option", even when it might be the most appropriate for their needs, skills and ambitions.

Several examples exist, however, of specific models for cooperative management training<sup>9</sup> (including distance learning) and there are even dedicated university courses for cooperative entrepreneurs. Unfortunately, most such initiatives remain isolated geographically, but these could be usefully networked across the globe. Many more

<sup>9</sup> See International Labour Office "Training Methodology for Cooperative Management" in http://www.ilo.org/coop (22. Feb. 2008).

### **Example 7.1: Strengthening the environment for business linkages**

"South Africa's National Business Initiative (NBI), founded in 1995, is a coalition of over 140 local and multi-national companies. The organization is an alliance of forward-thinking South African and overseas companies that are committed to realizing the vision of a thriving South African society, with a market economy that functions for the benefit of all. NBI aims to promote and facilitate the formation of business linkages through a number of actions to strengthen the enabling environment, including:

**Development of guidelines and good practice:** A number of large firms have adopted and implemented innovative approaches in the development of strong commercial linkages with SMEs in their value chains. Guidelines on good practice and case studies are being developed and successful initiatives marketed and promoted for a multiplier-effect.

**Policy and regulatory advocacy:** NBI and its partners have performed substantial research on the policy and regulatory environment for small business development and linkages with large firms in South Africa. Given that SMEs generally lack a platform for influencing the government and large enterprises, NBI plays a direct advocacy role in the promotion of policies and improved business practices conducive to linkages formation.

**Support for intermediaries:** NBI has found that intermediary organizations can play instrumental roles in facilitating linkages between SMEs and large firms, and is evaluating strategies for building the capacity of such organizations to play their roles effectively."

Source: Jenkins et al., 2007, p. 10

States, national educational institutes and stakeholders' organizations could develop awareness of the cooperative form via the curricula of business study courses at secondary and university levels and promote the development of relevant management skills. Apart from issues relevant to entrepreneurs' cooperative managers, such education and training should also be directed to the staff and leaders of (con-) federations and syndicates.

### 7.3.4 Business support services

The particular nature of entrepreneurs' cooperatives also calls for tailored business support services. Such counselling can be an invaluable accompaniment to, and condition of, loan financing. The networking of agencies offering specialised services to entrepreneurs' cooperatives should be intensified in order to enable beneficial exchanges of experience. However, where demand for these services is not sufficient to justify specialised agencies, a referral system may be more appropriate. Governments, employers federations, chambers of commerce, workers and other stakeholders all need to be aware of the need to examine and ensure the provision of support and advisory services to entrepreneurs' cooperatives, where and when the need arises. For the special purposes of export and international marketing, international agencies or cooperative organizations from the North should be approached.

#### 7.3.5 Access to finance

Entrepreneurs' Cooperatives frequently have no access (or only limited access) to equity markets and are therefore dependent on their own capital or credit financing. This is mainly due to the general lack of knowledge about the characteristics of cooperatives and their enterprises by credit institutions and the regulatory authorities. In our view the ILO's constituents could play an important role by facilitating exchanges of experience amongst cooperative organizations and national administrations on good innovative practices in financing

entrepreneurs' cooperatives. However, this can only achieve positive results in a given country if the national rules governing financial markets adhere to common international standards. In addition it is important to examine how best accounting procedures, and other relevant reporting rules, are able to take into consideration the structure of the capital and valuation of assets of cooperatives.

As far as public financing is concerned, national governments need to ensure that enterprise-financing initiatives are also accessible and appropriate for entrepreneurs' cooperatives. In view of the specific needs of cooperatives, it might well be worthwhile to examine the pertinence of forging formal links between entrepreneurs' cooperatives and the cooperative banking system.

### 7.3.6 Capacity building

Evaluations of more direct promotion strategies for cooperative SHOs and, in particular, of the centrally designed and managed strategies regularly show them to have failed (Göler von Ravensburg, 1998, p. 151). This makes it seem likely that the success rate of cooperative SHOs, and thus the sum of their long term contributions to social and economic development, depends very largely on the vitality of as many promotional agencies as possible competing to sell their services to cooperative SHOs (Röpke, 1994, p. 258). Consequently the state's role in such a strategy would simply be to control whether the members of any entrepreneurs' cooperative are indeed being promoted and to create advantageous conditions for a system of decentralized and competing promotion agencies and entrepreneurs' cooperatives.

Government capacity building needs particular attention, as agencies' efficiency in matters like business licensing, taxation, and regulatory enforcement can be critical to small business success. Linked to this is a third strategy for strengthening the enabling environment, that is, strengthening the linkages to public policy processes. Large firms are starting to explore channels for dialogue on the kinds of policies,

programmes, and regulations that affect entrepreneurs' cooperatives (Jenkins et al., 2007, p. 10).

A more active promotional approach should begin with the training of cooperative promoters for primary entrepreneurs' cooperatives (Röpke, 1994, p. 257). The skills, knowledge and qualities demanded of such promoters and office bearers results from both the cooperative model and the (frequently) low educational attainment of members. The right education and training as well as career options should be created after careful assessment of local, regional and national needs and potentials. Consideration should be given to formal entrepreneurs' cooperatives and also indigenous and other informal entrepreneurs' cooperatives, so that they can adapt to changing social and market environments.

Such training and consulting services should ideally be delivered by cooperative federations and other private sector organizations. Apart from being closer to the market, such approaches are also usually more cost effective, particularly where they can be designed as on-the-job-training, job rotation or job enlargement. The state might subsidize promotional efforts at the same rate if it subsidizes other service organizations in the small business sector. An increase in competition between promotional agencies, and thus the number of promotional approaches offered (by the process of trial and error), might be the best way to improve the quality of promotion.

# 7.3.7 Development promotion through cooperatives

Should the state (or any development NGO) want to go beyond this in an attempt selectively to promote entrepreneurs' cooperatives (e.g. for the alleviation of poverty and/or democratization of parts of society), 10

<sup>10</sup> See <a href="http://www.usaid.gov/sl/news/2006/060815\_diamond/index.">http://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a> <a href="http://www.usaid.gov/sl/news/2006/060815\_diamond/index.">http://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a> <a href="http://www.usaid.gov/sl/news/2006/060815\_diamond/index.">http://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a> <a href="http://www.usaid.gov/sl/news/2006/060815\_diamond/index.">http://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a> <a href="https://www.usaid.gov/sl/news/2006/060815\_diamond/index.">https://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a> <a href="https://www.usaid.gov/sl/news/2006/060815\_diamond/index.">https://www.usaid.gov/sl/news/2006/060815\_diamond/index.</a>

it should look particularly at the labour market conditions for (and consequences of) cooperative activity. Whilst producing cooperatives (workers as members) usually show a significant danger of instability, the (indirect) promotion of entrepreneurs' cooperatives with both poorer and wealthier members seems to create automatic secondary employment effects. This is because the members' enterprises increase may increase their activity and share of the market with the aid of their cooperative. Thus, strategies for increasing the productivity of the work force in the informal economy through strengthening self-help capabilities might also form a valuable part of poverty-oriented entrepreneurs' cooperative strategies.

Such strategies must also focus on legal reforms that would have an impact on the distribution of opportunities, working conditions and access to resources (e.g. by land reforms, improved infrastructure and educational policies). The further liberalization of financial and labour markets, together with the abolition of privileges for big industrial, agricultural, trade and banking enterprises, might be necessary (Hanel, 1992, p. 117).

What must be kept in mind is that direct material support for entrepreneurs' cooperatives with poor members may create a danger of officialization, of bureaucracy and of the paralysis of self-help forces. Such support may be counter-productive in the long run when public resources or the contributions of development or welfare organizations become scarce. In short, state promotion of entrepreneurs' cooperatives should be independent of their legal form, but relate to the sector they work in, at best favouring systems of labour-intensive production

#### 7.4 Federations and networks

It is really only in Europe and North America that entrepreneurs' cooperatives are well represented at the national and international levels through their national or sector federations. It is very necessary that cooperative federations in transitional countries and developing

countries should be represented in the policy dialogue and law making processes, but there have been some problems regarding federations in transitional countries and developing countries becoming effective in the promotion of entrepreneurs' cooperatives.<sup>11</sup>

It is a truism that cooperative development agencies (both Northern cooperative movements as well as other NPOs) became very disillusioned with supporting federations in the transitional countries and developing countries (Pollet and Develtere, 2004, p. 53). But, although many federations are to be blamed for conceiving themselves as "governing bodies" for the cooperative sector (Kirk, 2003), others simply were not given the chance to perform properly (Kötter, 1994, p. 800; ILO, 2000).

Whatever the case, empirical evidence, as well as modern governance theory, supports the demand for national law and cooperative policy to give cooperative syndicates, networks and (con-) federations the necessary freedom to exist. This includes the right to levy membership fees and to provide certain services to the member cooperatives whilst, at the same time, to circumscribe their rights and duties towards their members, the state and the general public.

Above all, governments must relinquish all control of federations and cooperative networks and instead enshrine the principle of subsidiarity in legislation for all levels of the cooperative movement. This is necessary to ensure that the governance of federations is the sole prerogative of member cooperatives and that bottom up processes will prevail within all cooperatives. At the same time cooperative federations must not be allowed to steer government structures either.

Whether cooperative federations, other promotion agencies or even an office of the registrar are responsible for (pre-registration and regular) the audit of cooperatives (and entrepreneurs' cooperatives), it is more important that audits are performed professionally, competently,

<sup>11</sup> See Chapter 6 "Cooperative unions and (con-) federations" (p. 100).

objectively, regularly and on time by the performing agency. The results should be conveyed comprehensibly to the cooperatives concerned and discussed with the supervisory committee (if any exists) or the general assembly, so that there is an opportunity to learn from the exercise.

The number of tiers in a cooperative system should be decided upon by the cooperatives themselves, keeping in mind their cost/benefit relationship. *Henry* (2005, p. 53) rightly draws attention to certain requirements (with regard to horizontal and vertical integration) which need to be governed by cooperative law (including entrepreneurs' cooperatives):

"The state should refrain from any intervention, except monitoring these organizations' compliance with their obligation to support and represent their members. Especially, cooperatives should not be forced to integrate on the lines of administrative subdivisions or on the lines of activities if they freely choose otherwise. Consequently the cooperative law must define the legal form of the different levels of this cooperative pyramid and specify the activities, which each level should exercise. The rights and obligations of the higher-level cooperative organizations include:

- representation of the members at national, regional and international level;
- promotion, education and training;
- advice, financial, insurance and economic services (marketing, supplies, exports, imports, etc.);
- development of inter-cooperative relations;
- research and development;
- arbitration;
- control and audit; and finally

### dissemination of the cooperative law."

Cooperative law should also ensure that cooperative unions, syndicates and (con-) federations should be allowed if not encouraged to take part in what is commonly known as 'movement to movement' support.

Currently cooperative federations in many industrialised countries maintain specific development units to assist cooperatives in developing countries (Pollet and Develtere, 2004; Parnell, 2001, p. 51). These include the Rabobank Foundation (the development arm of the cooperative bank of the Netherlands), Canadian Cooperative Association (CCA), KF Project Centre (Sweden), German Cooperative and Raiffeisen Federation, Credit Mutuel (France), Legacoop (Italy) and Central Union of Agricultural Cooperatives from Japan. They have had to adapt their development strategy as partners in transitional countries and developing countries have become more vocal and independent (Pollet and Develtere, 2004, p. 55). Susequently such cooperative movements tend to invest more in collaboration. In the future it will be important that South-South links become stronger, so that the required expertise can be exchanged more adequately. In this way promotional personnel can become aware of best practices as well as common errors and be deployed more quickly within crisis response programmes.12

## 7.5 Data collection and analysis

In order to improve our understanding of entrepreneurs' cooperatives it would be beneficial to improve data collection and analysis, ideally to satisfy the important need to adopt comparable categories for entrepreneurs' cooperative statistics worldwide. One system that might be worth considering is a business registry for statistical purposes, which was introduced in 2001 in the EU by EUROSTAT and the national statistical institutes of Member States (EC, 2001, p. 33).

<sup>12</sup> See examples given by *Parnell* (2001, p. 52.)

In the longer term the following would also be necessary:

- (1) agreement of common definitions and indicators with national statistical institutes and cooperative research bodies;
- (2) studies of business register data to be undertaken by national statistical offices and coordinated by a statistical bureau with similar capacities as those of EUROSTAT;
- (3) survey data to be collected by contractors (probably the apex organizations of cooperatives in the individual states or academic organizations);
- (4) collation and comparison of data at nation state level to identify and explain differences between business register and survey data; and
- (5) collation of data at international level and publication.

This process should take place every five to ten years, with progressive integration of more and more countries. If necessary, data could be compiled on the basis of satellite accounts to the national accounts, something which has been tried in a few EU Member States (for example in Spain and Belgium). The results of these exercises, and the methods used, might form the basis of a useful exchange of experience between government officials, promoting bodies and national statistical bodies.

# 7.6 Summary

What has been shown is that firm group and organizational norms can be fashioned much more flexibly and effectively for the organization's aims where modern economic policies and commercial laws are not obstructive. entrepreneurs' cooperatives neither need a special level of protection nor special promotion beyond that which other business networks, professional clusters or public service delivery bodies are offered. entrepreneurs' cooperatives develop best in market-driven environments that are characterized by competition.

International policy and legal advice can help national policy and law makers to design institutional paths to enable more entrepreneurs' cooperatives to become established. National cooperative dialogue is needed to tap into the existing resources in order effectively to promote entrepreneurs' cooperatives.

Elements of a national approach to the promotion of entrepreneurs' cooperatives should include the fashioning of an appropriate legal and policy environment, a positive image, the promotion of SMEs, education and training for promoters and entrepreneurs' cooperative leaders, access to finance and capacity building for entrepreneurs' cooperatives as well as a modern concept on which to base the role of entrepreneurs' cooperative-federations.

# **Chapter 8**

# The promotion of cooperatives

Before starting a discussion of possible promotional measures, one issue must be raised. Entrepreneur cooperatives in sum have greater diversity than any other category of cooperatives. They differ widely in membership, aims, financial base and activities. This makes them subject to varied legal and economic frameworks. The resources allocated to this study, its broad brief and the intention to address a wide audience only allow for the discussion of promotional measures that are appropriate to all types and circumstances. There will have to be a degree of abstraction regarding the applicability of more specific measures to entrepreneurs' cooperatives of professionals, trades people, small and medium-sized businesses, single entrepreneurs as well as (local) government owned businesses. Sectoral variation should also be considered.

To arrive at more detailed and specific recommendations that apply to all countries or regions is an almost impossible task. So it is suggested that the results of this study be used to define a classification for entrepreneurs' cooperatives, and this provide the essential basis for further regionally or nationally conducted empirical research. This would include research into the motivation of founders, truly relevant employment-, growth- and social effects, and the comparative

advantages of entrepreneurs' cooperatives over other forms in a given national or sectoral context together with the preconditions best suited for this type of cooperative. One example of an empirical study yielding specific indications for promotional measures is the Marburg Study on the criteria for German small and medium-sized enterprises choosing the legal form of a cooperative (Göler von Ravensburg; Pinkwart; Schmidt, 2003). This study provides examples of entrepreneurs' cooperatives in various regions and sectors, giving thorough discussion of theoretically and empirically proven potentials of this type of cooperative. It provides a good starting point for a classification. That it does not recommend a classification of its own is a recognition that any classification essentially represents a "political" decision and that it (and with its initiators) will, to a certain extent, be setting an agenda for the future.

This said, it is the author's conviction that the ILO's tripartite structure (governments, employers and workers), its international partners as well as the sum of national cooperative federations, unions and colleges with which the ILO is networking, can all play significant roles in improving the understanding of, framework conditions for and the support available to entrepreneurs' cooperatives. When and where cooperatives are voluntary and autonomous, it seems sensible to highlight again those areas where progress for all cooperatives will benefit entrepreneurs' cooperatives. Also it is important to focus on the justification for such promotion, before specifying possible and positive promotional measures specific for entrepreneurs' cooperatives.

### 8.1 Possible promotional avenues

In Europe, and where cooperatives are seen as private sector services, promotion is usually limited to that given to all businesses, for example (ILO, 2000):

 programmes for starting new enterprises (start-up or venture capital, subsidized feasibility studies);

- export promotion facilities;
- access to a suitable legal framework;
- services to promote enterprises in special branches of business (e.g. alternative energy sources);
- public information systems (e.g. on markets and prices) and services provided by semi-public institutions, such as chambers of commerce, industry, trades bodies; and
- public education, training facilities and research results.

The ILO Report V (1) allows for more direct cooperative support services to be provided by governments in exceptional cases or for special purposes. These could include (ILO, 2000, p. 90):

- audit services parallel with cooperative audit systems (the state does so in Cyprus and Italy); and
- restructuring of cooperatives by means of amalgamation (Japan).

Where such promotion is not offered, cooperatives can decide whether to buy the services they need, to organize their own support services (for example through their federations) or use special daughter organizations of the federations. Such services could include:

- central book-keeping and electronic data processing for primary entrepreneurs' cooperatives at the regional level, audit services with specially trained auditors;
- cooperative training centres mainly for vocational and technical staff training;
- central services within an integrated cooperative system;
   and
- cooperative research centres or institutes, sometimes in partnership with government.

Wherever entrepreneurs' cooperatives are seen to be a useful development tool (e.g. as a bridge for SMEs to enter markets, thus compensating for disadvantages they might have compared to large shareholding companies) or where a certain infrastructure is to be maintained by entrepreneurs' cooperatives because (local) government is not able to do so, a variety of more direct support services can be offered. For example:

- special research grants;
- access to advice from business promoters or incubators;
- access to soft loans and grants;
- access to public contracts; and
- opportunities for movement to movement assistance or partnerships.

However, as explained in the section on cooperative policy and law in Chapter 6, any over-promotion or exaggerated interventions by government agencies or private sector agencies (whether non-profit or for profit is immaterial) can do harm to cooperatives.

# 8.2 Why promotion can be justifiable

However tacit or indirect, any promotion of entrepreneurs' cooperatives among marginalized or impoverished population groups may represent a redistribution policy (Kötter, 1994, p. 796). Some well-known economists and policy planners insist, however, that such can both alleviate poverty and contribute towards the liberalization of local economic systems. That is if entrepreneurs' cooperatives have autonomy, this may counteract any hand-out mentality and preserve or even enhance their comparative development advantages over both private companies and bureaucracies (Göler von Ravensburg, 1998).

These three provisos must be safeguarded if entrepreneurs' cooperatives are to be self-sustaining, dynamic and flexible in terms of adjusting

to changing environments. As new ways of organizing activities, new processes and new products are all innovations, one could sum up by equating their large comparative advantage with the innovative potential they have, and justify their promotion this way.

In *developing countries*, but also in *countries in transition*, individual entrepreneurs usually face major obstacles to being innovative. Inadequate financial resources and unfavourable regimes of social obligations and property rights do not permit them to "do things differently". Both tend to diminish what initial motivation and acceptance of risk might have been there. In addition, relatively low or inappropriate competency and skill levels hinder their performance and imperfect markets prevent them from achieving a just reward for their efforts.

Entrepreneurs' cooperatives can be of assistance in overcoming these obstacles to innovation. The most important assistance they can render lies in forming secondary and tertiary bodies representing the interests of their member entrepreneurs and workers towards policy makers. They can lobby for better legal, market and financing conditions for SMEs, whether lay groups or professionals. By further pooling resources and using their local information advantage, they can provide members with the initial capital needed and can be back-stopping agents by helping them to access information on markets and prices (for both products and inputs), on technologies and on optimal factor combinations. They can create employment in areas where the state is rolling back needed services. Finally and very importantly, they can shelter the individual from social pressure within the village or town, by taking on part of the risk of innovation themselves, thus demonstrating solidarity. In fact entrepreneurs' cooperatives are already part of all these processes.<sup>1</sup>

In some cases entrepreneurs' cooperatives play a mitigating role between the forces of liberalization, globalization and technological progress.

<sup>1</sup> See the profiles of entrepreneurs' cooperatives collected in Appendix 2 and 3.

### **Example 8.1: Oaxacan State Coffee Producers Network, Mexico**

"In 1989, a structural adjustment programme and subsequent budget cuts caused the Mexican government largely to abandon its coffee sector. The inception of the Oaxacan State Coffee Producers Network (CEPCO) followed soon after, uniting a diverse organization of small-scale coffee producers in many distinct regions of Oaxaca. CEPCO was formed with the objective of collectively confronting the coffee crisis that threatened the basic needs of farmers and their communities. In 1993, the first of CEPCO's member organizations became Fair Trade certified by Fairtrade Labelling Organizations International (FLO).

CEPCO is currently undertaking a major initiative to promote its organic coffee. With the help of academic institutions and environmental NGOs, CEPCO is participating in the Mexican Civil Council for Sustainable Coffee, enhancing the long-term environmental sustainability of their members' land."

**Source:** http://transfairusa.org/pdfs/profiles/Cepco-Mex.PDF http://www.cepco.com.mx/index2.htm

They can reduce marginalization and improve social protection. Their information networks and the international cooperative trade (Pollet and Develtere, 2004, pp. 21-32) can help to equalize world-wide supply and demand (particularly of consumer and producer cooperatives), by beginning to form a counterweight to huge international conglomerates.

For example, fair trade organizations help to reduce disparities between nations by creating opportunities for disadvantaged producers to deliver products that don't undermine labour market standards or environmental conditions. Their contribution is growing, and consumer trends (demands for guaranteed quality standards for produce, consumer interest in environmentally friendly and socially conscious produced and traded products) suggest that this movement will

continue to get much stronger.

This globalization of cooperative trade and information has a real advantage at the local level. The basic distinctions of cooperative business continue to be:

- income creation through employment and self-employment opportunities, even in remote areas;
- improved working conditions
- a minimum of social security for all involved in the production process;
- ecologically conscious ways of production;
- dissemination of technological progress through innovation;
- training and education; and
- the inclusion of disadvantaged or marginalized groups.

User-members will increasingly be prepared to uphold these opportunities, even if that might mean foregoing some interest in capital invested. Entrepreneurs' cooperatives which are truly driven by their members' interests and still achieve the management capacities necessary will be in an excellent position to utilise all those areas of business which larger companies cannot do because of high transaction costs or lack of appreciation of the market.

# 8.3 Identifying the relevant role players

Alongside the ILO, other international organizations are dealing with cooperative promotion. Among this is the ICA, with whom the ILO has a Memorandum of Understanding and shared interest in promoting cooperatives, including entrepreneurs' cooperatives. Both organizations place special emphasis on:<sup>2</sup>

<sup>2</sup> http://www.ilo.org/dyn/empent/empent.Portal?p\_prog=C&p\_lang=EN (22. Feb. 2008) as well as http://www.ica. coop/ica/index.html (12.

- raising the awareness of and knowledge about cooperatives;
- providing policy advice to ILO Member States and ICA affiliated member organizations (e.g. unions, federations etc.);
- organizing international and regional conferences and meetings;
- technical cooperation activities including cooperative legislation, human resource development, strategic planning, poverty alleviation and local economic development; and
- networking and promoting the exchange of experience and movement-to-movement assistance.

Within the process of institution building, the ILO and ICA have helped governments and their administrations in many developing and transitional countries. For example, by financing experts to advise on the design of cooperative policy and law. In some countries this has resulted in much progress in terms of moving from government to member control and even new cooperative legislation.<sup>3</sup>

Unfortunately national cooperative dialogue has taken a long time in other countries and in some cases ended with a minimum consent which was not practical for registrars and cooperatives alike (See for example Göler von Ravensburg, 1998, p. 504; Abdel-Seed Mohamed, 2004, pp. 49-55). This shows that it is not always easy to align the interests of cooperatives, national governments, employers and workers' organizations, cooperative federations and international standards into workable compromises.

The movement to movement support has grown a great deal during the

Nov. 2007) and the report on common activities of the ILO and ICA since the MoU was signed in 2004 on http://www.ilo.org/dyn/empent/docs/F655694416/MoU%20activities%2007.pdf (12. Nov.2007).

3 *USCDC* (2007) pp. 32-35.

last decade. In the fair trade movement many successful marketing deals have been struck between farmers' cooperatives and handicraft and art entrepreneurs' cooperatives developing countries with fair trade chains, welfare organizations and even supermarkets in the North.<sup>4</sup> Although the fair trade movement began in the agricultural sector, particularly with tea and coffee, non-agricultural producers are also beginning to use international cooperative marketing channels.<sup>5</sup>

It is much more difficult to generalize on who could be the relevant partners for entrepreneurs' cooperatives rendering services to SMEs, professionals and public institutions trading at the local level. In many countries one might expect the sectoral entrepreneurs' cooperatives unions and federations to be prime partners. Other likely promotion partners would be chambers of commerce and industry, chambers of trade and vocational crafts, and national and regional associations of local governments. Public and private national, regional and local level economic promotion agencies, as well as social welfare and health organizations and authorities have also, on occasion, acted as promoting agencies. In short, all of those organizations and agencies could be relevant partners in the promotion of entrepreneurs' cooperatives if they believe that problems they are facing can be solved, or at least alleviated, by so doing.

# 8.4 Measures to promote entrepreneurs' cooperatives

Entrepreneurs' cooperatives are a relatively young and unknown kind of cooperative, which can mobilize different groups of SMEs, professionals and even public institutions. They offer a great deal of potential for trade with consumer and agricultural cooperatives, they can raise their members' levels of turnover in a relatively short time span (Wahl et al.; 2007, p. 37), can lower the risk of self-employment, ensure employment or even widen it. But despite all this, local entrepreneurs' cooperative

<sup>4</sup> See *USCDC* (2007) pp. 33 ff., and Appendix 4: Fair Trade Organizations which work with cooperatives.

<sup>5</sup> See "Appendix 2: Economic benefits of practice examples".

models that could serve as a nuclei for copying by other branches or target groups are still lacking in most parts of the world. This might have been the reason for *Couture* (2003, pp. 62-70) to suggest to the ILO that it should start pilot projects in this field. An alternative would be to cooperate with SME promotion agencies already running projects on the ground. Of course such an approach pre-supposes clear advantages for all partners concerned.

Regardless of which avenue of promotion is followed, the end aim must be to demonstrate the benefits of entrepreneurs' cooperatives to political decision makers, SME promoters, local governments, professional associations, chambers of commerce, chambers of trade and industries and users alike. The process of establishment and development of entrepreneurs' cooperative in certain sectors will make it a great deal easier to see what the interests of all parties concerned would be, how a national or regional policy to further them should be fashioned and who are the best role players for any part of a promotional effort.

The responsibility of those wanting to see entrepreneurs' cooperative adopt the cooperative legal form will rest primarily with two aspects:

- lobbying for and assisting governments and other major role players to fashion a favourable general climate; and
- initiating and popularising best practices.

### 8.4.1 Improving the general climate

A first step would be that national cooperative legislation gives legal personae the same cooperative membership rights as natural personae. Next, the ILO and all its constituents should continue to pursue their efforts to:

 assist all relevant public and private national bodies to develop modern cooperative policy, whilst including entrepreneurs' cooperative representatives in the setting of clear promotional aims, design of strategies and continued development of law. For the sake of all types of cooperatives, but especially for entrepreneurs' cooperatives, attention should be given to the greatest possible ease of administration (e.g. time and cost for registration and audit etc.);

- support restructuring activities by national governments for cooperative promotion agencies, encouraging them to accommodate entrepreneurs' cooperatives and thus arrive at a truly autonomous cooperative movement;
- sustain or possibly enlarge educational and training activities for the promotional personnel of selected cooperative federations, cooperative authorities and (public or private) cooperative promotion agencies, selection being based on the effectiveness of past promotional efforts; and
- systematically encourage contacts between cooperative movements in the South and the North for more movement to movement trade, the sharing of experience and for mutual learning.

The content of education and training programmes needs to include all topics relevant to entrepreneurs' cooperatives. Since they can provide a wide range of services and their members usually come from a diversity of branches, staff intent on promoting this cooperative model need to be particularly familiar with these branches. This might mean that in some cases it will be more effective to educate SME promoters, or staff of business chambers about the cooperative system, than to try and train all-round cooperative promoters in the different economies in which entrepreneurs' cooperatives can operate. It might also be very useful to devise and deliver systems for business advisors, from non-cooperative agencies and cooperative promoters to work together on the (pre-)registration audit.

Furthermore, the ILO and all its constituents could do a great deal for the promotion of entrepreneurs' cooperatives if they also:

- initiated research into typical organizational patterns, activities and markets which characterize entrepreneurs' cooperatives worldwide;
- included entrepreneurs' cooperatives issues into their portfolio of publications;
- actively and systematically approached SME promotion agencies, local governments, professional associations as well as health and welfare organizations in order to convey the benefits and characteristics of entrepreneurs' cooperatives;
- helped design campaigns for the promotion of image to which private and public sector promotion agencies could add their national, regional or local traits; and
- help national cooperative authorities and federations to build relationships with advisors to whom entrepreneurs wishing to cooperate turn in the first instance (e.g. tax or business consultants).

The best promotional progress, however, will result from the awareness of local and regional entrepreneurs' cooperative successes and the reliable and widespread publication of best practices. It is thus important that SME promoters, local governments and professional associations are shown how to identify and popularize the potentials of entrepreneurs' cooperatives in their vicinity and how to react to requests for consultation on cooperative issues.

### 8.4.2 Promoting best practices

The potential for entrepreneurs' cooperative activities is far greater in most areas of the world than has been discovered up to now. In the following section we concentrate on a few ideas of how to initiate and

popularize entrepreneurs' cooperatives whilst keeping in mind that in liberal economies SMEs, trades people, professionals, local governments and NPOs are free to make their own decisions. This includes why, how and with whom to cooperate. No agency or promoter has the right to do more than offer advice on a range of alternatives. They cannot know, nor should pretend to know, if another form of cooperation would be better for the members.

The circumstances of SMEs, professionals and public organizations as well as entrepreneurs' cooperatives are very diverse in different countries, so recommendations need to be general. At the same time local federations, all constituents of the ILO, as well as the ILO itself should be encouraged to initiate national dialogues on the promotion of entrepreneurs' cooperatives. This need not take a long time if it is well focussed on identifying certain parameters. These include motivating other promotion agencies and potential entrepreneurs' cooperative members, screening the national economy for sectors and business models suited to cooperative action and identifying the right national or local partners for a promotion project. Once the decision has been taken to enter a promotion project, it must be planned strategically in order to maximize chance of success and facilitate a later "roll-out".

We have already answered the questions as to who cooperates in entrepreneurs' cooperatives are and what motivates cooperators, These are "invariables" to any promotional strategy. The circumstances under which members set-up and maintain entrepreneurs' cooperatives could be seen as the variables in a promotional strategy. These can, within limits, be used or influenced by promoters in their promotion strategies.

## 8.4.3 Other determinants of cooperation

Three primary conditions determine whether any offer of promotion is a) made by a promotion agency and b) accepted voluntarily by potential members:

- 1. Both potential promoters and potential members are aware of a problem of economies of scale or scope (autonomous identification and definition of the problem) and perceive it as urgent enough to cause an impulse for action (urgency to solve a problem);
- 2. Both are willing to do something about the problem (willingness to solve the problem); and
- 3. Both believe that they can solve the problem by cooperating in a cooperative (if given adequate external assistance).

The economic and the social value systems of a society have decisive (secondary) influences on the perception of the urgency of the problem. The social value and the political systems also influence the willingness to solve the problem. The economic potential of members, their endowment with (natural) resources and their creativity are the secondary determinants influencing members' as well as promoters' ability to solve the problem. In this way it becomes apparent that promotional interventions can only be effective if they address promoters' and members' economic potential.

There are good reasons to be wary of the risks of promotional efforts based on material supports, particularly if this assistance is given regardless of the ability of cooperatives and their members to ever pay. It is suggested that promotional strategies are based largely on information, education, training and networking. For such strategies to have a reasonable chance of success it is important that promotional agencies carefully screen groups, clusters or networks of SMEs, professionals or public institutions to assess their potential to respond well to such assistance.

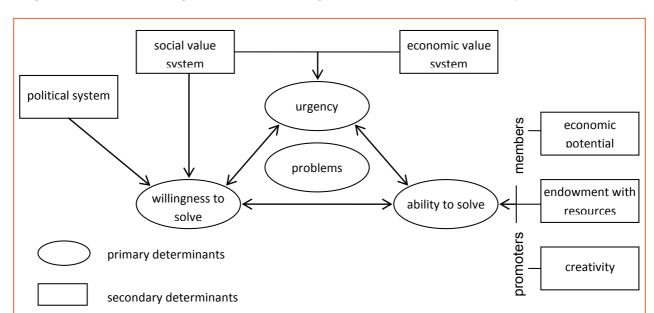


Figure 8.1: Primary and secondary determinants of cooperation

## 8.4.4 Screening for suitability

Compared to their total number, only a relatively small proportion of SMEs, professionals or local government bodies work together for common purchasing or marketing activities. Under these circumstances the thought of promotional agencies carefully screening applicants for the likely success of them sharing services cooperatively might sound a little strange. Not all such groups will be economically successful (Wahl et al., 2007, p. 5) or indeed should attempt to use the legal form of a cooperative. Some groups are small enough to make use of simpler contractual alternatives (see for example Wahl et al., 2007 or Bhuyan, 1996, p. 8). Others might have to reconsider the economic potential of their idea and some ideas represent one off exchanges which do not lend themselves to continued business. All these and many other ideas and groups would be badly served with a cooperative structure.

On the other hand, we know that several positive key factors increase the likelihood of a shared services idea and a group of potential members being really well served by the cooperative form.

As far as the business ideas are concerned, the entrepreneurs' cooperative joint venture is best suited for:

- horizontal cooperations<sup>6</sup> in such branches which in any national economy has reached a significant level of concentration without being entirely dominated by one or a limited number of firms. Under such competitive conditions, entrepreneurs' cooperatives might save their members production costs, help to access knowledge, create economies of scale and scope or to safeguard their economic future;
- vertical cooperations<sup>7</sup> in branches where concentration of firms has increased to such a degree that there is again room for small flexible firms. The individual members' motivation to cooperate usually lies in the wish to compensate for their shortcomings by outsourcing certain functions or specializing within a close network of partners;
- cooperations which aim at developing new products or services, uplifting their quality standards, implementing larger projects than they could cope with individually or productively using surplus capacities; and
- cooperations which are intended to last.

The entrepreneurs' cooperative in turn has proven to best serve those (prospective) members, who:

have a clear and common business objective;

Horizontal cooperation includes the sharing or exchange of machinery, implements, knowledge and other production resources, the common purchase of inputs or marketing of produce and services, the sharing of book keeping or research and development facilities, information systems and other administrative functions.

<sup>7</sup> Several SMEs with different but complementary core businesses cooperate in order to attract larger orders or new customers, to create new quality standards or improve plant or capacity utilization.

- want to retain their entrepreneurial autonomy;
- are prepared for a degree of transparency between themselves (for example regarding business benchmarks);
- have worked together for a while in an informal cooperation;
- have a positive image of the cooperative form;
- see a need to protect innovations (shares in cooperatives are not freely tradable);
- wish to limit their liability;
- want to keep to a minimum the capital required to start a formal joint venture;
- are looking actively to participate in the strategic management of the cooperative business regardless of the relative size of their financial commitment;
- place a premium on a business culture characterized by synergies, transparency, democracy and trust; and
- believe in a transparent business plan with which to start in the common business and the benefit of regular external controls of what has been achieved.

None of these criteria will apply to all groups. However, it is important to find out whether a particular business idea fits the most important of these conditions early in the start-up of consultancy. It would be desirable if the criteria above were also tested on occasions in entrepreneurs' cooperatives that have existed for some time. This would help identify any possibly detrimental changes.

Two sets of circumstances are worth examining a little more deeply; one because it presents a borderline scenario for ascertaining whether or not the entrepreneurs' cooperative form is advisable, and two because it demands special care for the design of organizational norms beyond those usually laid down in the basic statutes:

- 1. Vertical cooperation in entrepreneurs' cooperatives is likely to become more complex than horizontal cooperation. In reality the number of cooperating partners in a vertical cooperation tends to be smaller, which in turn makes informal cooperation or other company forms appear more attractive. If the number of members is large, however, a cooperative form still has significant advantages over informal cooperation and competes successfully with other organizational forms. The contractual arrangements necessary to make vertical integration work might even be easier to fashion in a capital driven company. This is because the entrepreneurs' cooperative might be able to maintain the levels of social capital created in the (informal) precursor more easily.
- 2. Entrepreneurs' cooperatives can serve a single purpose as well as multiple purpose. While it is at times satisfactory to concentrate on sharing one function (e.g. common data processing), a complex shared service (e.g. common marketing frequently), has immediate repercussions for other business functions (e.g. quality control or packaging). Sometimes the successful rendering of one shared service encourages members to share other services. Multipurpose entrepreneurs' cooperatives are well advised to work out service contracts with their members which specify very clearly the responsibilities of member businesses as well as the cooperative business.

## 8.4.5 Cooperating with SME promotion agencies

The empirical evidence, analysis and conclusions provided by *Nadvi, Bhuyan, Couture, Pollet & Develtere, Wahl et al.* suggest several things:

1. The relatively strict distinction made in Central Europe between bodies which represent and regulate SMEs and bodies responsible for increasing their economic efficiency, may be less suited to the conditions faced by SMEs and even professionals in developing countries. There, business associations, sector units and business membership organizations, cooperative business associations and

- entrepreneurs' cooperatives alike usually have to fulfil political, economic and as well social functions;
- 2. Opportunities as well as economic necessities for sustainable cooperation are seldom discovered by SMEs, professionals or public entities themselves;
- 3. Harnessing the economic opportunities of cooperation makes a degree of formalization absolutely essential;
- 4. Potential members of all these organizations need external knowhow in order to fashion sustainable group norms, set attainable objectives and install transparent monitoring and evaluation procedures. All these in turn are indispensable for sustainable cooperation;
- 5. External assistance must not be offered free of charge, as it could make the primary joint ventures dependent;
- 6. Institutionalization of secondary if not tertiary member-based organizations is necessary for (the sharing of) services, which can only be rendered at cost if demand can be combined from several primary organizations.

All this describes the typical scenario for the development of a twoor three-tier cooperative system. However, while historically very few agencies existed to promote cooperation among SMEs, when those few federations developed in Europe, this led to a many agencies that were active in developinng countries promoting SMEs. Cooperative federations also exist in many developing countries, although their interest in entrepreneurs' cooperatives differs widely.

Most modern SME promotion agencies are directed at creating selfsustaining systems. They usually agree that the economies of most production and service sectors today are so specific that it is difficult for just one unit to render high quality business services, lobbying, training, consulting and book keeping for a multitude of business sectors. These organizations might be the best bridging agents for the

ILO, its national constituents, national cooperative federations and Northern cooperative movements alike. Through them, cooperative potentials can be discovered and harnessed, whilst cooperative and business consulting can complement each other.

The selection of countries, sectors and partners, however, needs a great deal of care. It is recommended that the ILO and its constituents only promote entrepreneurs' cooperative in countries where the legal and policy environments are conducive. They should select partners which have shown full appreciation of the importance for self-sustaining institutionalization. This scrutiny should apply to both national cooperative federations as well as SME promotion agencies.

Furthermore the aims of national or local partner organizations should be complementary to those of the ILO. It might be possible for certain activities in training and education to be conducted jointly by a federation or SME promotion agency and a secondary cooperative. There should be a clear delineation of responsibilities with regard to trade (inputs and sales for member entrepreneurs' cooperative), production services (packaging, marketing, technical services etc.) and consulting. The earlier should be strictly the business of a secondary (member-controlled) entrepreneurs' cooperative. All functions rendered by either promotion agencies or (second tier) entrepreneurs' cooperatives should be monitored and reported separately to their respective members.

In countries where the cooperative climate is favourable for entrepreneurs' cooperatives, but either no suitable SME promotion agency can be identified or cooperation with a SME promotion agency is impossible, consideration should be given to helping a national cooperative federation to develop both systems – a group based SME promotion and a secondary entrepreneurs' cooperative level.8 *Wahl et al* (2007) have shown very convincingly how this can be done. They

<sup>8</sup> The federation in turn might find that it can win chambers of commerce, trades, industries or crafts for partners for the group based promotion system.

developed a manual called the 'Manual for Business Membership Organizations' (BMOs), which is based on 10 years of experience in Latin America and elsewhere. Although their experience is based on cooperation between chambers of commerce in both the North and the South, the approach could be adapted to cover a cooperative approach.

The manual refers to "Sector Units" and this concept corresponds to pre-cooperative types of entrepreneurs' organizations. This form of cooperation might start with a simpler mode of formalization, e.g. with a memorandum of understanding or with by-laws instead of full statutes (Wahl et al., 2007, p. 31). With time, the Sector Units can develop into registered primary entrepreneurs' cooperatives. The BMOs, which in their concept are the original promoters of group-based entrepreneurial activity, might like to "outsource" certain trading and production related functions to (secondary) entrepreneurs' cooperatives once the number of sector units is large enough. This would then automatically result in a healthy separation of business and lobbying functions.

Whether the ILO should encourage national cooperative federations to compete with BMOs already representing Sector Units should be decided on a case by case basis. In some cases this could result in fruitless conflicts between a cooperative federation and a BMO, with both seeing only the potential for income to be that coming from members. In other cases BMOs might welcome such an approach by a cooperative federation, because Sector Units and even "fully grown" entrepreneurs' cooperative can be members of both at the same time. This shows that it might also be important for cooperative federations to adopt a fairly open and non-competitive approach to the representation of entrepreneurs' cooperatives.

In this context one detail might also deserve attention: Whilst in

<sup>9</sup> Wahl et al. (2007) use the term "Business Membership Organizations" (BMO) as a bracket for all kinds of membership based business organizations including chambers, CBAs, ECs, coop federations etc.

many countries cooperative legislation foresees only natural personae as members, the statutes governing chambers of commerce, trades, industries or associations of vocational crafts might allow only for the admission of registered firms (Wahl et al., 2007, p. 32). Such BMOs might need to amend their statutes if, as promotion agencies, they also want to admit informal businesses and self-employed professionals. For the same reason they might also want to adapt their scales of membership fees.

## 8.4.6 Strategy Design

The core elements of the strategy suggested above must be the selection and training of promotion personnel, the development of basic routines for strategic planning, adequate monitoring and evaluation in entrepreneurs' cooperatives and public relation measures which facilitate a later "rollout".

## Selection and training of promotion personnel

Apart from the selection of the sectors in which to establish entrepreneurs' cooperatives, the choice and training of facilitators for them are the most important factors for success. In *Wahl*'s methodology they are called group consultants (Wahl et al., 2007). They help the group to identify common problems, prioritize them and develop a joint action plan. This operates as a link with other advisory agents outside the cooperative. For example, if the group identifies a need to prepare business plans, its consultant will refer to a specialized consultant and monitor their work with the members of the entrepreneurs' cooperative. Usually, the facilitator is employed by a BMO, which as we have seen can also be a cooperative federation or an organization started for this purpose.

With some adaptations covering cooperative principles, legislation, administration etc., the details given here as to his or her profile, training needs and the selection process can also be a good base for the selection and training of entrepreneurs' cooperative facilitators.

## Strategic planning, monitoring and evaluation

Entrepreneurs' cooperatives need a very clear definition of their objectives. The facilitator should guide the group through the process of deciding on these and help to concentrate on objectives which can realistically be achieved, starting with the most promising. Indicators and outputs that will help to achieve this objective should be recorded. This strategic plan can be developed into a real business plan, possibly with the help of external expertise. It also serves as the basis for a regular (annual) participative evaluation of achievements, for the redefinition of objectives and the adaptation of action plans by members. The instrument must be designed and used in a way that minimizes the time that entrepreneurs and other members have to spend on it. Monitoring processes should be based on the needs indicated by this strategic plan.

#### Public relations measures

Any promotion of entrepreneurs' cooperatives must be considered in the light of the potentials for replication and sustainability. Both will be significantly enhanced if the entrepreneurs' cooperative is popularized by making successes visible. This must not be done too early or else the number of visitors, phone calls or invitations to speak might surpass capacity or interfere with work. On the other hand, entrepreneurs' cooperatives need to advertise their success for their own sake. They can attract new suppliers through organizing suppliers' days and obtain discounts if their logo is recognizable. Arranging exhibitions or participating in fairs can pave the way for new customers. Breakfasts and round tables with federation representatives and legislators might help to promote their macro-economic standing and legal environment. The higher the public visibility and the higher the connectedness of the business interest between the members of the entrepreneurs' cooperative, the easier it will be to mobilize them to participate.

#### **Formalization**

Entrepreneurs' cooperative do not necessarily have to be registered as cooperatives, as they can operate without a certain degree of formalization. Their organizational norms must be such that trade in the common name becomes possible, which is a matter of trust with members retaining full control.

The minimum formal requirements for entrepreneurs' cooperatives should be a code of conduct to which members agree. This should include specifications for the resolution of internal conflicts, their duties and rights, the election of leadership, as well as other relevant issues. While some would have this written down in a "Memorandum of Understanding" (Wahl et al., 2007, p. 31), entrepreneurs' cooperatives may also draw up statutes or by-laws which signal higher degrees of formality. Entrepreneurs' cooperatives that want to be registered need to draw up statutes. These must adhere to the relevant national law and any regulations by the registrar or federation.

All entrepreneurs' cooperatives should also have a registry of members providing conventional data such as names, contact addresses, information on the type of product or service marketed by the members, the number of their employees, suppliers, clients, etc. Such a database can serve various purposes when performing the day-to-day tasks in the entrepreneurs' cooperative and the promotional agency.

## 8.5 Summary

The ILO's tripartite structure (governments, employers and workers), its international partners as well as the sum of national cooperative federations, unions and colleges with which it is networking, can play a significant role in improving both the general climate for entrepreneurs' cooperatives. This chapter has aruged this case and points out that the ILO and its constituents have already contributed to cooperatives in general being seen as voluntary and autonomous organizations in many

countries, while also providing support to assist framework conditions to be fashioned accordingly.

A case can be made for special promotion efforts for entrepreneurs' cooperatives, based on national or local partnerships between the ILO and its constituents on the one side, and carefully selected authorities and chambers of commerce, trades, crafts and industries on the other. The ultimate promotional success will result from local and regional entrepreneurs' cooperatives successes and reliable and widespread publication of them. So it seems important that SME promoters, local governments and professional associations are shown how to identify and popularize potential initiatives in their vicinity.

There are good reasons to be wary of the risks of promotional efforts based on material supports, particularly if this assistance is given regardless of the ability of cooperatives and their members to pay. To explore the locally relevant positive key factors which increase the likelihood of a shared services idea, and a group of potential members being well served by the cooperative form, must form the core of any promotion strategy.

SME promotion agencies may also be good bridging agents for the ILO, its national constituents, national cooperative federations and Northern cooperative movements alike. Through them, cooperative potentials can be discovered and harnessed. This is provided that they aim at creating self-sustaining systems and their objectives are complementary to those of the ILO.

It might be possible that certain activities in training and education could be conducted jointly by a federation or SME promotion agency and a secondary cooperative. But there should be a clear distinction of responsibilities with regard to trade (inputs and sales for member), production services (packaging, marketing, technical services etc.) and consulting. These tasks should be strictly the business of a secondary (member-controlled) entrepreneurs' cooperative and the functions

rendered by the promotion agency and the (second tier) entrepreneurs' cooperatives respectively should be monitored and reported separately to the members.

The authors further believe that the core elements of any entrepreneurs' cooperative promotion strategy must be the selection and training of promotion personnel, the development of basic routines for strategic planning and adequate monitoring and evaluation in the entrepreneurs' cooperatives assisted. Also included must be public relation measures which facilitate a later "roll-out".

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# Appendix 1: Benefits in hermeneutic literature<sup>1</sup>

Authors and main addressees	Economic benefits	efits	
Bhuyan, S. (1996)	savings through lower administrative costs, quantity purchasing discounts, sharing fixed	"provide services that are absent or inadequate in rural communities" p. 3	"i.e. through strategic alliances, these communities may be able to create jobs,
addresses himself to SMEs but also to public planners, municipalities and other public institutions such as	costs, and assured levels of business with vendors and suppliers" p. 3, p. 4 (with ref. to	"maintain or improve the quality of life in	(p. 5)
hospitals and schools; only those parts are featured here which are of relevance to SMEs and individual	Crooks et al 1995)	rural communities" (p. 5)	"the Western Area Cities/Counties Cooperative (WACCO) Then extended its
ousinesses as well as professionals	"given that SSCs can provide services at reduced costs to members"	"i.e. through strategic alliances, these communities may be able to create jobs,	functions to provide employee training" (p. 5).
At the same time in developing countries many of the		attract new businesses and services, and	
services provided by municipalities in industrialized countries are not available either and it might well	<ul> <li>p. 5:(1) overcoming high individual fixed costs across the group, (2) increase</li> </ul>	strengthen their local economies (p. 5)	private businesses are also forming SSCS to provide health care or health insurance to
be worth considering rendering security services, fire protection, garbage removal or water and sewer	bargaining power for marketing or purchasing supplies or acquiring services, (3) reduce		their employees." (p. 7)
services or supplies to schools and hospitals through	redundant resources of the group members		
une cumpean confirmatify (see p. o and o). Among SME entrepreneurs' cooperatives he emphasizes	by consolidating operations (4) reduce his and uncertainty by spreading risk among		
fast food franchise chains and hardware stores, independent pharmacies and retail food outlets.	members, (5) improve market coordination or efficiencies. (6) improve quality of product		
-	or service by setting group standards or		
	negotiating premium prices for quality, (7) penetrate new markets otherwise inaccessible		
	by individuals, (8) improve access to		
	information and share costs of securing		
	information, and (9) overcome isolation from markets or sources of needed services."		
	"Public entitiesjoint purchase of expensive		
	but underused equipment and various supplies and services through SSCs to increase their		
	negotiating and bargaining power." (p. 5)		
	"to purchase supplies, train employees or other activities to share and reduce costs" (p. 7)		

Based on Internet self-representation of 69 entrepreneurs' cooperatives chosen at random from all continents.

		(700 (general) coops in British Columbia employ 13.000 people
Poverty reduction through selective integration into the wider economy, and the building up of a defensive structure against poverty at household, group, and village level.  Promotion of women in economic terms and of their role in society; prevention of rural urban migration through income generation and rural diversification; participation;  use of local resources; sustainable development; enhancing local control over factors of production; capacity-building, improvement in literacy and health.	"Gooperatives have a contribution to make both on the supply and demand sides. They open up markets by organizing supply of inputs and marketing of outputs At several times in the history of cooperatives, international cooperative trading organizations have been created that have significantly improved the export potential of producer cooperatives, and the importing activity of consumer cooperatives."  ((p. 46) (ref. to Verhagen 1985)  "However, it is a fair assumption that where people are individually powerless they have to group together in strong local organizations of one kind or another, which will have cooperative characteristics." (p. 46)	transparency and accountability; strengthening of and loyalty to communities (surplus reinvested locally)
(supplementary) income generation especially for rural women; diversification of income sources for rural households Job creation; defending ones interests against government authorities build up of bargaining power and claim-making power; widening of options for income-generating activities,	balancing the advantages of size and scope by forming horizontal and vertical cooperative networks (p. 47) risk sharing, absorption and insurance(p. 48)	assurance of supply;  Protection from take-over and closure by outside decision makers;  Higher survival rate than private businesses
Birchall, J. (2003) esp. case studies on a) Women's Agro-tourism Cooperatives in Greece pp. 37-40 and b) on the Uganda Shoe-shiners Industrial Cooperative Society pp. 51-53 (this is an entrepreneurs' cooperative which also has credit functions and in some ways resembles a worker cooperative)	Birchall, J. (2004)  Addresses the contributions cooperatives can make to the attainment of the Millennium Development Goals (MDGs)	British Columbia Cooperative Association (2007) addresses the public at large. It makes only implicit mention of entrepreneurs' cooperatives (in regard to social service providers organising cooperatively)

Dito 2004 p. 15:	Coops in general "can therefore effectively integrate excluded groups into work and	society, giving them also entrepreneurial experience and management responsibility." And " can create jobsin this way they add	to the flexibility of labour markets."												
Dito 2001:	services to groups that would otherwise not be able to access them;	correction of market failures and increased market efficient organization of markets (through collective purchasing or selling power);	market power to lay people or small enterprises where homogenous products or services are needed;	enable citizens to affect or determine services they need;	longer-term view being based on maximising stakeholder benefits rather than shareholder value; less likelihood of coops withdrawing from a particular region or sector because its	capital could be more prolitably employed elsewhere (coops as cushion from structural change);	provide a school of management;	integrate large sections of the population to economic activity;	provide stability;	Generate and maintain social capital due to democratic governance and economic participation	Dito 2004, p. 15:	"Such strong local roots can	be an effective counter to the desertification of rural areas and assist the development	of poorer regions and localities."	
building or increasing economic power of SMFs in the market: scale economies; access	to markets (including participation in larger public tenders), purchasing power; traiteting power; traiteting powers and propose and propo	power, management development, daming and research capacity; sharing of risks; vertical integration of product chains; members gain revenue from added value to their produce or service; achieving high quality; possibility to	or services to clien influence the busi ning the necessary services to bid for p	or entrepreneurship and management for those who might not otherwise have access to positions of responsibility;											
Commission of the European Communities (2001) mainly on 24-30 & Commission of	the European Communities (2004) mainly p. 5	Both papers concern themselves with cooperatives in general. We have selected those arguments, which can safely be assumed to be benefits for entrepreneurs'	cooperatives as well.												

can save money, spread risk, and enables the participating businesses to pool their resources, provide mutual support and learning and strengthen their business sector, while maintaining their business independence (p. 1)	<ul> <li>Producing volume and/or continuity of supply, Critical mass and economies of scale. (b. 5)</li> <li>Sharing risks and development costs. Consortium members can pool resources for jointly exploring markets, for example, or developing feasibility studies on new opportunities. The ability to invest in shared facilities and equipment. (b. 5)</li> <li>Control over standards, quality and ways of working. Crucial decisions, such as methods of marketing, hours and conditions are put in the hands of those most affected. It also enables the members to be free of potential exploitation by a third party. It ensures that the balance of power is in the hands of those delivering the work. Peer pressure means that quality is often raised and a better service is given to the customer or client.</li> <li>Mutual support. Sole traders, lone professionals or craftspeople are often isolated. It enables joint working, the sharing of ideas, work and concerns. Co-operative consortia are particularly valuable for traders or businesses that are geographically isolated.</li> <li>Promoting a particular ethical approach to business. Cooperative consortia are ideal for those wanting to work in a democratic way with other like-minded traders or businesses (pp. 5-6)</li> </ul>	
Cooperatives UK (2006): Trading for Mutual Benefit. A GUIDE TO Co-operative Consortia addresses itself to potential entrepreneurs' cooperative founders		

Job creation and maintaining employment (p. 43)	
access to Government financial support for housing, health, education and welfare needs; access to information (trends, markets); Pooling expertise and collaborating; training and education; access to other associations; social recognition; new social relations/ networking;  Social and economic well-being in the region (p. 43)	and discuss problems and topics of mutual concern;
access to product markets: improved sales revenues; savings on input-purchases (incl. bonuses); access to rare raw materials; access to services (lease of equipment etc.); access to Government financial support; entrepreneurial promotion (through assistance with accounting, promotion services); improved returns on capital (dividends, attractive investment); access to working capital; risk absorption (emergency loans);	Member control over the price and quality of services and products they wish to buy; constant, supportive access to products and services; access to specific or scarce materials or services; innovative ideas from members for members; flexibility in the types and magnitudes of services: "As members' needs change over time, cooperatives can respond by adjusting their services. The ability to respond to change depends upon the purpose and objective of the organization." (1995, p. 4)  Responding to changed government policies (e.g. in provision of special school education or garbage disposal);  Sharing of information;
addresses herself to ILO, its constituents and cooperative organizations and focuses on the potential of entrepreneurs' cooperatives for developing countries. Four case studies in industrialized countries and 3 case studies in developing countries (largely deduced from Summary Table 6.3 p. 39 with slight modifications in categorization)	Crooks, A. C., Spatz, K. J., Warmann M. (1995), esp. p. 4; Crooks, A. C., Spatz, K. J., Warmann M. (1997) pp. 2-3; both publications are specific to entrepreneurs' cooperatives

p. 2: " a scalable publishing model that aligns with the ethos of learned societies while providing a financial framework capable of sustaining society publishing programs." p. 3: " provide societies with an alternative to publishing through commercial channelsa framework that makes a transition to new funding and access models more practically feasible."	Business experience for women (p. 1); communities gain access to services otherwise not provided because of major overheads (costs for empty wards and classrooms) or where the state withdrew
assuring the existence of small publishing houses  (p. 3: "slow the exodus of society publishers to commercial outsourcing"  " expand the capacity of societies to meet the growing demand for new journals and scholarly communications channels, rather than ceding that expansion to for-profit publishers.")  p. 15-18: improved bargaining power & reduced publishing costs via scale economies; increased Society Publisher market presence & circulation; specialized business management services; ability to manage & mitigate risk; stabilized or improved financial performance while retaining current business models at the level of member enterprises; framework for longtern structural changes in access & funding	models; access to capital; maintaining society relevance amidst changing scholarly communications practices: Additional income for women (p. 1); common advertising;
Crow, R. (2006); Researches the options entrepreneurs' cooperatives offer for society publishers to overcome structural disadvantages, which threaten their very existence (esp. pp. 15-18)	Doherty, M. (1997) draws mainly on examples from the (handi-) craft and restaurant sector in the rural USA. With our working definition the other coops he lists as "SSCCs", namely those providing child care and other community services (incl. provision of groceries) as well as housing coops among the elderly, would rather be consumer coops.

Empowerment of the poor through collective action;	
Information for Development Programme   opportunities for job creation, income   Empowerment of the poor through collective (2006), p. 10	
Information for Development Programme (2006), p. 10	On coops in general but mention is made of entrepreneurs' cooperatives as an application of the cooperative concept to a new area (p. 11)

p. 45:	generation of employment opportunities, particularly in rural areas; ustments; see for different anise themselves fift; alized groups; usly offered by realth care and cooperatives of froms of energy reatives active in ling, soft tourism find, soft tourism ened-oriented, cing the price of decision-making decision-making	
pp. 45-47:	alleviation of poverty:  mitigation of hardship resulting from transition from centrally planned to market economies and structural adjustments;  provision of an effective base for different disadvantaged groups to organise themselves for social and economic benefit;  re-integration of marginalized groups; provision of services previously offered by the state (particularly in health care and the care for elderly people): contribution to environmental conservation (cooperatives developing and producing new forms of energy generation and supply, cooperatives active in waste management and recycling, soft tourism etc.).  p. 61:  "By defending the interests of their members, coops defend at the same time the interests of certain groups of the population (). They demonstrate to the general public that economic activities need not necessarily be directed to maximize profit and shareholder value, but can also be need-oriented, improving the quality or reducing the price of goods and services."  p. 62: " are schools of democracy practice participation in and democratic control of goal-setting and decision-making processes."	
p. 32:	The greatest direct economic impact of cooperatives at the micro-level surely lies in the additional income they create for their members. They achieve this by: securing higher prices for their products (marketing cooperatives); by lowering input costs -thus either enabling members to use higher input levels, achieve higher production levels and/or have larger profit margins (supply cooperatives); introducing innovations, offering insurance () and credit at a more favourable overall cost  pp. 32-33:  Most successful cooperatives promote their members by improving:  - the productivity of their subsistence activities or in their own enterprises;  - their market position as producers,;  - their access to material and non-material resources;  - the predictability of incomes, production levels and prices;  - the ducation and training:  - their know-how, formal or informal knowledge, standards of information or education and training:  - the predicted is superior in quality to alternative providers;	
International Labour Office (2000): Report V (1)	Addresses all cooperatives; we have included those elements which are particularly relevant to entrepreneurs' cooperatives	

р. 10:	"Cooperatives empower the poor through collective action;"	
p. 10:	"combat poverty in three ways: they empower people by enabling the poorest segments of the population to take action; they create job opportunities for those who have skills but no capital; and they provide protection by organizing mutual help in communities." "Several countries reported that cooperatives were an effective approach to poverty reduction in the agricultural sector and the informal economy"	mentions Pharmacists' cooperatives as one type of cooperative which can assist in improving the health of communities (p. 32) and attributes the potential of "assisting to resettle returning refugees" and "reintegrating ex-combatants" to tradesmen and artisans coops (p. 36) unfortunately without giving an example.  Also, he sees entrepreneurs' cooperatives among other coops as "developing locally owned enterprises as a defence against the flight of capital in the case of financial downturns." (p. 37).
p. 10:	" also create opportunities for job creation, income generation and sustainable livelihoods."	Although he lists  "Business marketing and service cooperatives (Shared services)***  Craftsmen and artisans cooperatives  Eco-tourism /farm tourism cooperatives  Market operator cooperatives  Taxi and transport operators' cooperatives" (p. 32)  as having the potential to support SMEs and entrepreneurs in their endeavours to cope with crisis situations, he makes no mention of specific economic benefits of entrepreneurs' cooperatives in crisis situations
International Labour Office (2003):	Coops in general are seen as one way of several to create pro-employment development; we only report those benefits, which can be credited to entrepreneurs' cooperatives, too.	Parnell, E (2001):

p. 12:	<ol> <li>Access to quality supplies and services at reasonable costs</li> <li>Increased clout in the marketplace</li> <li>Share in the earnings</li> <li>Political action</li> </ol>	9. Local economy enhanced and protected
Young, M. M. (2002)	Addresses small water supply systems; its account of benefits of entrepreneurs' cooperatives is based on the United States Rural Business-Cooperative Service Publications	

Appendix 2: Economic benefits of practice example

-						
	Examples	Dividends	Financing, Credit	Insurance	Information about products and production	Marketing
Africa						
1.	Machakos District Co-op Ltd. (Kenya)		consumer			
2.	Mango True Mirage (Kenya)		consumer		×	×
3.	Akamba Handicrafts Industry Cooperative (Kenya)	×	consumer			×
4	Kalangu Project (Ghana)					×
5.	The Kilimanjaro Native Cooperative Union (Tanzania)		production credit		X	×
9.	Yuri Enga Enterprises (Ghana)		production and consumer		×	×
7.	Lesotho Co-operative Handicrafts (Lesotho)					
×.	Kavokiva(Cooperative Agricole Kavokiva de Daloa) (Cote D)		consumer			
9.	Assetamorwa (Rwanda)		production and consumer			×
10.	Modis International (Rwanda)					×
11.	Alternative Trade Network (Nigeria)					×
12.	Kagera Cooperative Union (Tanzania)					×
North America	erica					
13.	NEMEON (USA)	×	discounts and rebates		×	
14.	IMARK (USA)	×	discounts and rebates			
15.	Valley Bakers Cooperative Association (USA)	×	discounts			
16.	Rural Wisconsin Health Cooperative (USA)				×	
17.	National Cable Television Cooperative (USA)					
18.	Quality Bakers of America Cooperative (USA)					
19.	Starnet Commercial Flooring Cooperative (USA)				×	×

Appendix 2: Economic benefits of practice example (continued)

2.0.         Adventure BC Travel Cooperative (Canada)         X           2.1.         Federated Cooperative (Canada)         4           2.2.         Climate Cooperative Limited (Canada)         4           2.3.         To Climate Cooperative (Lixt)         7           2.4.         Sinch Red Cooperative (Lixt)         7           2.5.         Seniore (Lixt)         7           2.6.         Seniore (Lixt)         7           2.7.         Favorable (Canada)         7           2.8.         Ringford (Canada)         7           2.9.         Eurorics 6C (Germany)         7           2.9.         Eurorics 6C (Germany)         7           3.0.         Obschiedree-Enhand Ost 6C (Germany)         7           3.1.         Corp. Lamine Goody (Financy)         7           3.2.         John Loss Perversibi (LiVC)         7           3.1.         Corp. Lamine Goody (Financy)         7           3.2.         John Loss Perversibi (LiVC)         7           3.3.         Intrace (Merineracion)         7           3.4.         Norwallan agricultural purchashing and marketing Co-Op         7           3.5.         Accurling Boying Co-operative Link (Australia)         7           3.5. </th <th></th> <th>Examples</th> <th>Dividends</th> <th>Financing, Credit</th> <th>Insurance</th> <th>Information about products and production</th> <th>Marketing</th>		Examples	Dividends	Financing, Credit	Insurance	Information about products and production	Marketing
1. Federated Co-operative Limited (Coractal)         A Scounts and rebates         A Scounts and rebates         X           2. Truck/alue Company (USA)         4 Shop Ree (LISA)         X         A Scounts and rebates         X         X           3. Truck/alue Company (USA)         5 Seminole (USA)         X         X         X         X           4. Shop Ree (ISA)         7. Tearnoofe (USA)         X         X         X         X           5. Seminole (USA)         7. Tearnoofe (USA)         X         X         X         X           6. Associated Independent Stores (USA)         X         X         X         X         X           7. Tearnoofe (USA)         X         X         X         X         X         X           8. Enronics of Germany)         X         X         Accounts increasing and marketing Co-Op         X         Accounts increasing and marketing Co-Op         X         Accounts and rebates           9. Innee (Nebrelations)         X         Accounts and rebates         X         Accounts increasing and marketing Co-Op         X         Accounts increasing	20.	Adventure BC Travel Cooperative (Canada)					×
2. Climate Care (Cenade)         discounts and rebates         X         X           3. True Value Cempany (USA)         A SnopRite (USA)         X         X           5. Seminole (USA)         X         X         X         X           6. Sendinole (USA)         X         X         X         X         X           6. Sendinole (USA)         X         X         X         X         X         X           6. Associated Independent Stores (UK)         X         X         X         X         X         X         X           7. Texmode Fashen Goup (Finand)         X <td< td=""><td>21.</td><td>Federated Co-operative Limited (Canada)</td><td></td><td></td><td></td><td></td><td>×</td></td<>	21.	Federated Co-operative Limited (Canada)					×
3. True Value Company (USA)         discounts and rebates         X           4. SnopRite (USA)         Propertie (USA)         X         Propertie (USA)           5. Seminote (USA)         Propertie (	22.	Climate Care (Canada)					×
4. SnopRite (USA)         Seminole (USA)         Monosgian agricultural purchasing and marketing Co-Operative Limited (Australia)         X         Monosgian agricultural purchasing and marketing Co-Operative Society Lid. (Australia)         X         Moscounts           4. Acan Repair Crosperative Lid. (Australia)         X         discounts and rebates         X         X           5. Adama Buying Co-opertive Limited (Australia)         X         discounts and rebates         X         X           6. Acan Repair Crosperative Lid. (Australia)         X         discounts and rebates         X         X           7. Captricon Society Lid. (Australia)         X         discounts and rebates         X         X           8. Acan Repair Crosperative Limited (Australia)         X         discounts and rebates         X         X           9. Acan Repair Crosperative Lid. (Australia)         X         discounts         X         X           9. Acan Repair Crosperative Lid. (Australia)         X         discounts         X         X           9. Acan Repair Crosperative Lid. (Australia)         X         discounts         X         X           9. Acan Repair Crosperative Lid. (Australia)         X         discounts         X         X           9. Acan Repair Crosperative Society Lid. (Australia)         X         discounts         X	23.	True Value Company (USA)		discounts and rebates		X	×
5. Seminole (USA),         Cerp control (USA)         Cerp control (USA)         Cerp control (Finitard)         Cerp control (Finitard)         Cerp control (Finitard)         Cerp control (Finitard)         X         Cerp control (Finitard)         X         Cerp control (Finitard)         X         Cerp control (Germany)         X         Cerp control (Germa	24.	ShopRite (USA)					
6. Associated Independent Stores (UK)         Associated Independent Stores (UK)         X         X           7. Texmoda Fashion Graup (Finland)         X         business insurance         X           9. Euronics eG (Germany)         X         business insurance         X           10. Dachdecker-Einkauf Ost eG (Germany)         X         X         X           2. John Lews Partnership (UK)         X         discounts and rebates         X           3. Intres (Netherlands)         X         discounts and rebates         X           4. Norwegian agricultural purchasing and marketing Co-Op         discounts and rebates         X           5. Acuna Buying Co-opertive Limited (Australia)         X         discounts           6. ArchiTeam Co-operative Lid. (Australia)         X         discounts           6. ArchiTeam Co-operative Society Ltd. (Australia)         X         discounts           7. Captriconn Society Ltd. (Australia)         X         discounts           8. The Hairdessers' Cooperative Society Ltd.         X         discounts           9. Interflora New Zealand         X         discounts	25.	Seminole (USA)					
6. Associated Independent Stores (UK)         Associated Independent Stores (UK)         X         <							
Associated Independent Stores (UK)         Associated Independent Stores (UK)         Associated Independent Stores (UK)         X         Associated Independent Stores (UK)         X         Dusiness insurance         X         Associated I	Europe						×
Euronics G (Germany)         X         business insurance         X         business insurance         X         business insurance         X         business insurance         X         Cerp-Loraline Group (France)         X         Cerp-Loraline Group (France)         X         discounts and rebates         X	26.	Associated Independent Stores (UK)					
Euronics eG (Germany)         X         business insurance         Cerp Common           Leuronics eG (Germany)         X         business insurance         Cerp Common           Dachdecker Einkauf Ost eG (Germany)         X         discounts and rebates         X           Donn Lews Partnership (UK)         X         discounts and rebates         X           Intres (Netherlands)         X         discounts and rebates         X           Norwegian agricultural purchasing and marketing Co-Op         Aiscounts and rebates         X           Acuma Buying Co-opertive Limited (Australia)         X         discounts           Acuma Buying Co-operative Ltd. (Australia)         X         discounts           ArchiTean Co-operative Ltd. (Australia)         X         discounts, production           Capricom Society Ltd. (Australia)         X         discounts, production           The Hairdressers' Cooperative Society Ltd.         X         discounts, production           The Hairdressers' Cooperative Society Ltd.         X         discounts, production           The Hairdressers' Cooperative Society Ltd.         X         discounts, production	27.	Texmoda Fashion Group (Finland)				X	×
Euronics eC (Germany)         X         business insurance         business insurance         Cerp-Loraline Group (France)         X         business insurance         X         Cerp-Loraline Group (France)         X         discounts and rebates         X         <	28.	Ringfoto Gruppe (Germany)					
Cerp-Lorraine Group (France)         X         discounts and rebates         X         Moveedian (Prance)         Moveedian (Prance)         X	29.	Euronics eG (Germany)			business insurance		
. Gerp-Lorraine Group (France)         X         discounts and rebates         X         discounts and rebates         X         Activitient (Mx)         Activitient (Mx)         X         Activitient (Mx)         Act	30.	Dachdecker-Einkauf Ost eG (Germany)	×				×
John Lews Partnership (UK)         X         discounts and rebates         X         discounts and rebates         X <t< td=""><td>31.</td><td>Cerp-Lorraine Group (France)</td><td>×</td><td></td><td></td><td></td><td></td></t<>	31.	Cerp-Lorraine Group (France)	×				
. Intres (Netherlands)         X         discounts and rebates         X           . Norwegian agricultural purchasing and marketing Co-Op         Accounts and rebates         Accounts         Accounts <td>32.</td> <td>John Lews Partnership (UK)</td> <td>X</td> <td></td> <td></td> <td></td> <td></td>	32.	John Lews Partnership (UK)	X				
. Norwegian agricultural purchasing and marketing Co-Op  Acuma Buying Co-opertive Limited (Australia)  ArchiTeam Co-operative Ltd. (Australia)  Capricom Society Ltd. (Australia)  The Hairdressers' Cooperative Society Ltd.  Interflora New Zealand  X  discounts  credit  X  discounts  Adiscounts  redit  X  Interflora New Zealand  X	33.	Intres (Netherlands)	×	discounts and rebates		X	×
Acuma Buying Co-opertive Limited (Australia)  ArchiTeam Co-operative Ltd. (Australia)  Capricorn Society Ltd. (Australia)  The Hairdressers' Cooperative Society Ltd.  Interflora New Zealand  X  discounts  credit  X  Interflora New Zealand  X	34.	Norwegian agricultural purchasing and marketing Co-Op		discounts and rebates			
Acuma Buying Co-opertive Limited (Australia) discounts  ArchiTeam Co-operative Ltd. (Australia) X discounts  Capricorn Society Ltd. (Australia) X discounts, production credit  The Hairdressers' Cooperative Society Ltd. X  Interflora New Zealand  X							
Acuma Buying Co-opertive Limited (Australia)       X       discounts         ArchiTeam Co-operative Ltd. (Australia)       X       discounts, production         Capricorn Society Ltd. (Australia)       X       discounts, production         The Hairdressers' Cooperative Society Ltd.       X       x         Interflora New Zealand       X       X	Australia						
ArchiTeam Co-operative Ltd. (Australia)       X       discounts, production         Capricorn Society Ltd. (Australia)       X       discounts, production         The Hairdressers' Cooperative Society Ltd.       X       x         Interflora New Zealand       X       X	35.	Acuma Buying Co-opertive Limited (Australia)		discounts			
Capricorn Society Ltd. (Australia)  The Hairdressers' Cooperative Society Ltd.  Interflora New Zealand  X discounts, production  Credit  X X	36.	ArchiTeam Co-operative Ltd. (Australia)	×	discounts			
The Hairdressers' Cooperative Society Ltd. Interflora New Zealand	37.	Capricorn Society Ltd. (Australia)	×	discounts, production credit	business insurance		
Interflora New Zealand	38.	The Hairdressers' Cooperative Society Ltd.	×				
	39.	Interflora New Zealand	×				

Appendix 2: Economic benefits of practice example (continued)

-	•		•	•		
	Examples	Dividends	Financing, Credit	Insurance	Information about products and production	Marketing
40.	Motor Trade association (New Zealand)		discounts	business and personal		
41.	Plumbing World Ltd. (New Zealand)	×				×
42.	VINZ (Vehicle Inspection New Zealand)	×			×	×
43.	Foodstuffs (New Zealand)		discounts and rebates		×	×
South America	arica					
44.	Artesanos de Villa Carlos Paz (Argentina)					
45.	Belize Fishermen Cooperative Association (BFCA)					
46.	Toledo Ecotourism Association (Belize)					
47.	A.A.A.Sociation de artes Andinos					×
48.	Q'Antati (Bolivia)				×	×
49.	Asociacion Artesanal Boliviana (Bolivia)					×
50.	Prainha do Canto Verde (Brazil)					×
51.	Corporacion Red de Artesanas (Colombia)					×
52.	FEPP-Camari (Ecuador)					×
53.	"Masapan" (Ecuador)		banking services			×
54.	SATI -The treasures of the Incan Artisanal Society (Ecuador)					
55.	Asociasion Culinaria de Mexico, A.C. (Mexico)					×
56.	CEPCO (Mexico)		production and consumer	business and personal		×
57.	Union Majomut (Mexico)		production			×
58.	Cooperative de Taxi de Agosto (Nicaragua)			business		
59.	Inti Wasi Adaiwa (Peru)					×
.09	Asociacion de Artesanos del Estado Merida (Venezuela)					×

Appendix 2: Economic benefits of practice example (continued)

	Examples	Dividends	Dividends Financing, Credit Insurance	Insurance	Information about products and production	Marketing
Asia						
61.	61. HLHC Holy Land Handicraft Cooperative (Israel)					×
62.	Sunbula (Israel)					×
63.	TCP Travel Cooperative of the Philippines	×				
64.	EMA (India)		production and consumer		×	×
.59	Mahila SEWA Cooperative Bank (India)		banking services			
.99	Asha Handicrafts (India)					
.79	Sewa Bharat - All India federation of Self Employment Women (India)		production	personal	×	×
.89	Saigon Co-op (Vietnam)					
.69	Seikatsu Club Consumer's Coop Union (Japan)				×	

Appendix 3<sup>2</sup>: Social benefits of practice example

-		-			
		Examples	Reducing of cost	Training	Advice, Services
Africa	à				
	-:	Machakos District Co-op Ltd. (Kenya)	transport costs (I)		
	2.	Mango True Mirage (Kenya)			×
	33	Akamba Handicrafts Industry Cooperative (Kenya)	input and transport costs (I)	×	×
	4.	Kalangu Project (Ghana)	input costs	×	
	5.	The Kilimanjaro Native Cooperative Union (Tanzania)	input and transport costs (L)	×	
	9.	Yuri Enga Enterprises (Ghana)	transport costs (L)	×	×
	7.	Lesotho Co-operative Handicrafts (Lesotho)	input and transport costs(L)		×
	×.	Kavokiva(Cooperative Agricole Kavokiva de Daloa) (Cote D'Ivoire)	transport costs(L)		
	9.	Assetamorwa (Rwanda)	input costs	×	
	10.	Modis International (Rwanda)		×	
	11.	Alternative Trade Network (Nigeria)			
	12.	Kagera Cooperative Union (Tanzania)	transport costs(L)	×	×
Nort	North America	rica			
	13.	NEMEON (USA)	purchasing costs		
	14.	IMARK (USA)	purchasing costs		
	15.	Valley Bakers Cooperative Association (USA)	input and distribution costs		
	16.	Rural Wisconsin Health Cooperative (USA)	input costs		
	17.	National Cable Television Cooperative (USA)	input costs		
	18.	Quality Bakers of America Cooperative (USA)	distributions costs		
7		3ased on Internet self-representation	Based on Internet self-representation of 69 entrepreneurs' cooperatives chosen at random from all continents.	ın at random from	all continents.

Based on Internet self-representation of 69 entrepreneurs' cooperatives chosen at random from all continents.

19.	arnet	input costs	×	
Appendix	3: Social benefits of practice	example (continued)		
	Examples	Reducing of cost	Training	Advice, Services
20.	Adventure BC Travel Cooperative (Canada)	input costs	×	
21.	Federated Co-operative Limited (Canada)	purchasing costs	×	×
22.	Climate Care (Canada)	input costs	×	
23.	True Value Company (USA)	purchasing costs	×	
24.	ShopRite (USA)	purchasing and transport costs (L)	×	×
25.	Seminole (USA)	purchasing costs		
Europe				
26.	Associated Independent Stores (UK)	purchasing costs	×	
27.	Texmoda Fashion Group (Finland)	input costs		
28.	Ringfoto Gruppe (Germany)	purchasing costs		
29.	Euronics eG (Germany)	purchasing costs	×	×
30.	Dachdecker-Einkauf Ost eG (Germany)	purchasing costs	×	
31.	Cerp-Lorraine Group (France)	purchasing costs		
32.	John Lews Partnership (UK)	purchasing costs		
33.	Intres (Netherlands)	purchasing and transport costs (L)		×
34.	Norwegian agricultural purchasing and marketing Co-op	purchasing and transport costs (L)		×
Australia				
35.	Acuma Buying Co-opertive Limited (Australia)	purchasing costs		
36.	ArchiTeam Co-operative Ltd. (Australia)	×		×
37.	Capricorn Society Ltd. (Australia)	purchasing costs		×
38.	The Hairdressers' Cooperative Society Ltd.	purchasing costs	×	×
39.	Interflora New Zealand	distribution costs		

Appendix 3: Social benefits of practice example (continued)

•				
	Examples	Reducing of cost	Training	Advice, Services
40.	Motor Trade association (New Zealand)	purchasing costs		×
41.	Plumbing World Ltd. (New Zealand)	×		
42. 43.	VINZ (Vehicle Inspection New Zealand)	purchasing and transport costs (L)		×
44.	Foodstuffs (New Zeeland)	distribution and transport costs (L)	×	×
South America	erica			
45.	Artesanos de Villa Carlos Paz (Argentina)	distribution costs		
46.	Belize Fishermen Cooperative Association (BFCA)			
47.	Toledo Ecotourism Association (Belize)			
48.	A.A.A.Asociation de artes Andinos		×	×
49.	Q'Antati (Bolivia)		×	×
50.	Asociacion Artesanal Boliviana (Bolivia)			×
51.	Prainha do Canto Verde (Brazil)			×
52.	Corporacion Red de Artesans (Colombia)			
53.	FEPP-Camari (Ecuador)		×	×
54.				×
55.	SATI -The treasures of the Incan Artisanal Society (Ecuador)	distribution costs		
56.			×	×
57.	CEPCO (Mexico)			×
58.	Union Majomut (Mexico)			
59.	Cooperative de Taxi de Agosto (Nicaragua)	input costs		
.09				
61.	Asociacion de Artesanos del Estado Merida (Venezuela)			

Appendix 3: Social benefits of practice example (continued)

	Examples	Reducing of cost	Training	Advice, Services
Asia				
62.	HLHC Holy Land Handicraft Cooperative (Israel)			
63.	Sunbula (Israel)		×	X
.64.	TCP Travel Cooperative of the Philippines	distribution costs	×	X
.65.	EMA (India)	input costs		X
.99	Mahila SEWA Cooperative Bank (India)		×	×
.67.	Asha Handicrafts (India)			
.89	Sewa Bharat - All India federation of Self Employment Women (India)		×	X
.69	Saigon Co-op (Vietnam)	purchasing and distribution costs	×	×
70.	Seikatsu Club Consumer's Coop Union (Japan)	purchasing costs		X

## **ECONOMIC** and other benefits of the **ENTREPRENEUR COOPERATIVE** as a specific form of **ENTERPRISE** cluster

Nicole Göler von Ravensburg

Entrepreneurs' cooperatives have helped small and medium sized enterprises in many countries to become and remain competitive. Although this form of business clustering has not been widely adopted so far, there are indications that this form of enterprise cluster offers several strategic benefits. In order to support the uptake of entrepreneurs' cooperatives this study analyses the economic, social and employment benefits of this form of enterprise cluster and outlines a number of strategic recommendations for the promotion of entrepreneurs' cooperatives.

ILO Country Office for the United Republic of Tanzania, Kenya, Rwanda and Uganda Coop<sup>AFRICA</sup>
Kazi House, Maktaba Street
P.O. BOX 9212
Dar es Salaam
United Republic of Tanzania
Tel: +255.22.2196700
Fax: +255.22.2122597

E-mail: coopafrica@ilo.org www.ilo.org/coopafrica

International Labour Office Cooperative Programme (EMP/COOP) 4, route des Morillons 1211 Geneva 22 Switzerland

Tel: +41.22.7997021 Fax: +41.22.7996570 E-mail: coop@ilo.org www.ilo.org/coop

Committee for the Promotion and Advancement of Cooperatives (COPAC) 150 route de Ferney, PO Box 2100 1211 Geneva 2 Switzerland

Tel: + 41 22 798 8825 Fax: +41 22 798 4122 E-mail: copac@copac.coop

www.copac.coop

