
Developing Cooperative Strategy to Create and Improve Member Value

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Today's Game Plan

- Evaluate a strategic decision-making framework for cooperatives
- Discuss alternative types of cooperative strategies used to increase member value
- Consider specific examples of strategic choices and their implications



Warm-up

USDA estimated that the total number of agricultural (farmer) cooperatives in the U.S. in 2009, including marketing, supply and service cooperatives was:

- A. 238
- B. 2,389
- C. 23,894
- D. 238,942

Warm-up

	2009
Number of cooperatives	2,389

Type	Number
Marketing:	1,169
Supply:	970
Service:	250

**Correct
Answer:
B**

Source: USDA Cooperative Programs 2011

Warm-up

USDA estimated that the total number of agricultural (farmer) cooperative memberships in the U.S. in 2009, including marketing, supply and service cooperatives was **(in thousands)**:

- A. 224
- B. 2,248
- C. 22,484
- D. 224,842

Warm-up

			2009
Number of cooperatives			2,389
Memberships (millions)			2.2
Gross business volume (billion \$)			170.2
Net business volume (billion \$)			147.7
Net income before taxes (billion \$)			4.4
Total assets (billion \$)			61.2
Net worth (billion \$)			23.8
Full-time employees (thousand)			122.6
Part-time and seasonal employees (thousand)			57.8

**Correct
Answer:
B**

Type	Number	Memberships (000)
Marketing:	1,169	753.0
Supply:	970	1,390.2
Service:	250	104.7
Total	2,389	2,247.9

Source: USDA Cooperative Programs 2011

Warm-up

The **total number** of agricultural (farmer) cooperatives in the **Northeast U.S.*** in 2009, including marketing, supply and service cooperatives was:

- A. 61
- B. 103
- C. 162
- D. 225
- E. 458

*Includes ME, VT, MA, CT, NY, PA, NJ, MD, DE (NH & RI not rep. < 3)

Warm-up

The **total number** of agricultural (farmer) cooperatives in the **Northeast U.S.*** in 2009, including marketing, supply and service cooperatives was:

- A. 61
 - B. 103
 - C. 162**
 - D. 225
 - E. 458
- | | | | | | |
|----|----|----|----|----|----|
| ME | 22 | VT | 3 | MA | 8 |
| CT | 5 | NY | 55 | PA | 39 |
| NJ | 12 | MD | 15 | DE | 3 |

Source: USDA Cooperative Programs 2011

Warm-up

The state with the **highest number** of agricultural (farmer) cooperatives in 2009, including marketing, supply and service cooperatives was:

- A. Minnesota
- B. Texas
- C. North Dakota
- D. California
- E. Iowa

Warm-up

The state with the **highest number** of agricultural (farmer) cooperatives in 2009, including marketing, supply and service cooperatives was:

- A. Minnesota 213**
- B. Texas 198
- C. North Dakota 168
- D. California 127
- E. Iowa 109
- F. Illinois 127
- G. Wisconsin 116

Source: USDA Cooperative Programs 2011

Warm-up

The state with the **highest gross business volume** for agricultural (farmer) cooperatives in 2009, including marketing, supply and service cooperatives was:

- A. Minnesota
- B. Texas
- C. North Dakota
- D. California
- E. Iowa

Warm-up

The state with the highest gross business volume for agricultural (farmer) cooperatives in 2009, including marketing, supply and service cooperatives was:

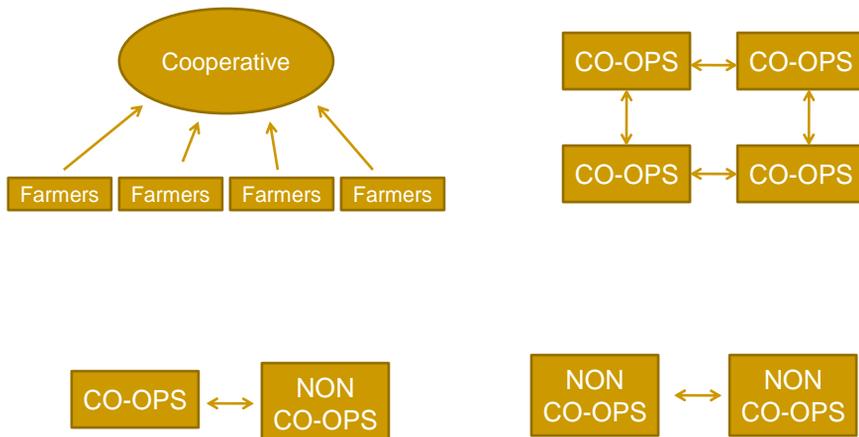
- A. Minnesota \$17.6 billion (2nd)
- B. Texas \$5.0 billion (12th)
- C. North Dakota \$6.4 billion (9th)
- D. California \$10.0 billion (4th)
- E. Iowa \$18.1 billion (1st)**
- F. Illinois \$12.7 billion (3rd)
- G. Wisconsin \$9.4 billion (5th)
- H. New York \$2.7 billion (18th)
- I. Pennsylvania \$2.0 billion (20th)

Source: USDA Cooperative Programs 2011

Defining Cooperative Strategy

- Definition: “Cooperative Strategy is the attempt by organizations to realize their objectives through cooperation with other organizations, rather than in competition with them.” (Child & Faulkner 1998)
 - *Strategic* decisions – making decisions in light of information on the expected actions and responses of others
 - Recognize *individual incentives* in making cooperation possible, e.g., receive *positive differential returns* over other options
 - Closely linked to attaining the *goals desired by cooperative* – maximizing value to its members

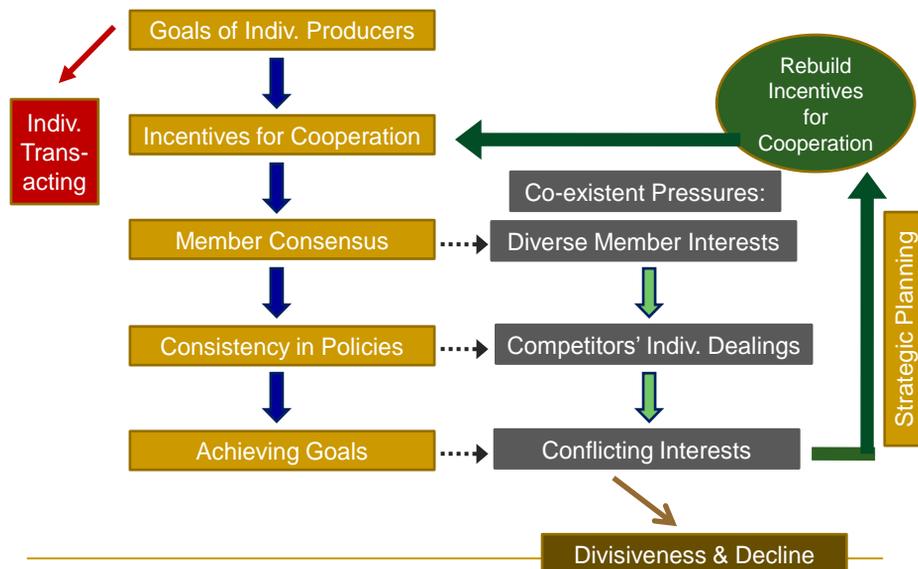
Forms of Cooperative Strategy



Defining Cooperative Strategy

- Advantages/Incentives of cooperative strategies?
 - Pooling of competencies and resources, information exchange
 - Combining different perspectives & experience in making decisions
 - Can build new values and innovative ideas
 - Reduce risk exposure; e.g., pooling, diversification, market integration
 - Easier access to or securing member markets
 - Market power effects
 - Transaction cost economies
- Obstacles to cooperative strategies?
 - Constrained focus (+ or -)
 - Incomplete or inaccurate information
 - Balancing cooperative goals and member incentives
 - Business as usual trap, ability or ease of change
 - **Diverse member interests and needs**

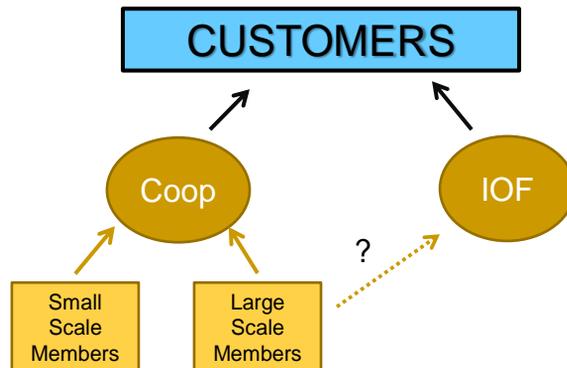
Strategic Framework with Diverse Member Interests



Source: Reynolds 1997

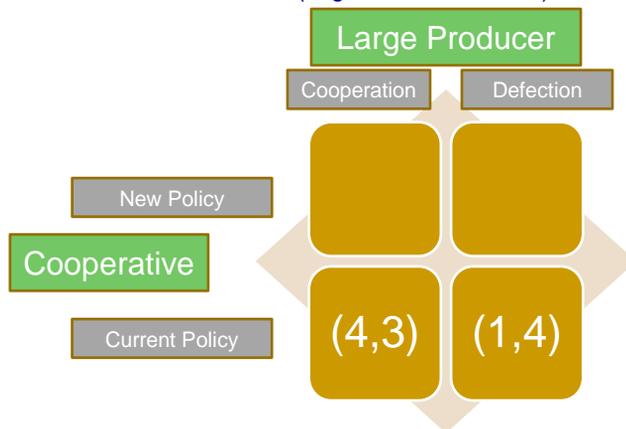
Strategy Examples - Attracting Large Producers

- Hypothetical cooperative that operates more efficiently when it receives patronage from large members
- A competitor offers individualized deals to bid large members away from the cooperative.
- You are members of the BOD that must decide whether to accept various policies (strategies) proposed by management



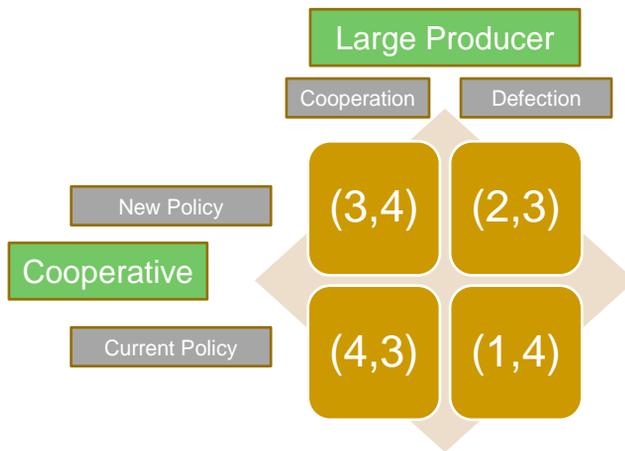
Setting the Stage

- Initially, by being a larger coop, it receives a total payment of \$7, distributed to members based on patronage implies SP receive \$4 and LP receive \$3.
- LP have the opportunity to defect (leave), since by acting individually, they could receive a payment of \$4
- The resulting lower volume in the coop reduce efficiencies and lower member returns to \$1 (large scale economies)



Policy Proposal I

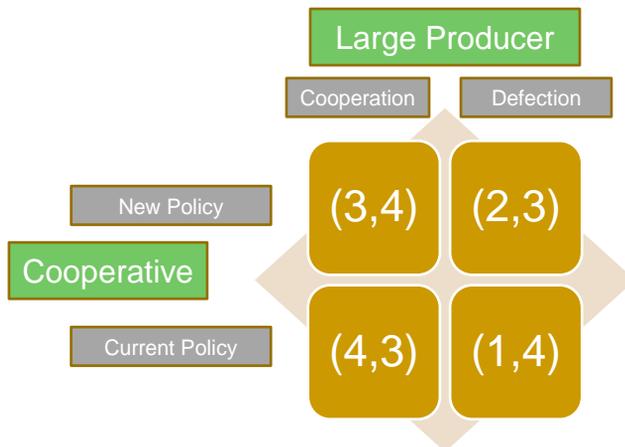
- Establish differential pricing in proportion to product volume delivered.
- Large producers will be penalized if they leave the coop by expropriating a portion of their equity (or retained for an extended period of time).
- With the expected outcomes of the alternative scenarios below (and known by both), how should you vote and what will the large producer do (optimally)?



Policy Vote and Outcome

How would you vote and how will the large producers respond?

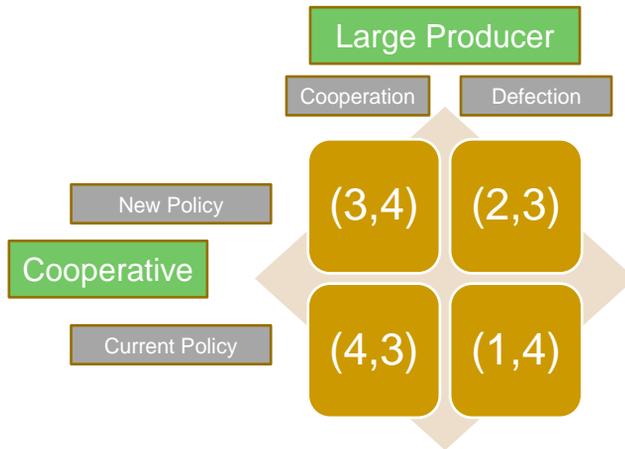
- Coop rejects new policy, LP defects
- Coop rejects new policy, LP cooperates
- Coop accepts new policy, LP cooperates
- Coop accepts new policy, LP defects.



Policy Vote and Outcome

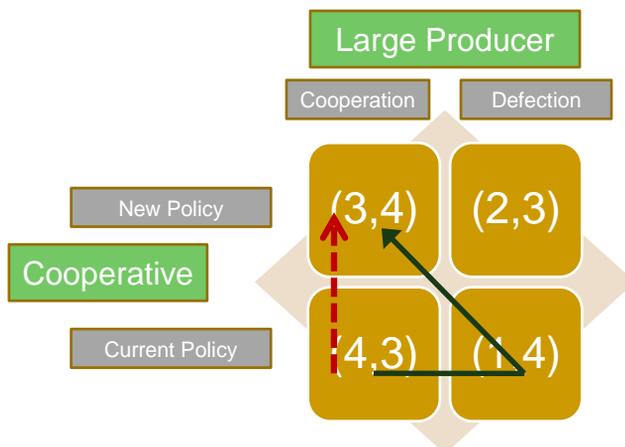
How would you vote and how will the large producers respond?

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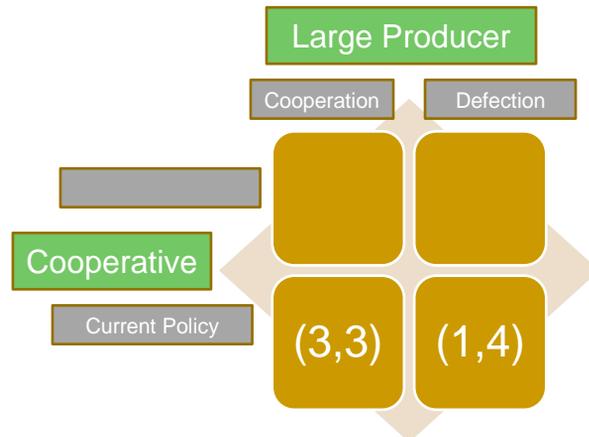
Policy Result

- The equilibrium solution is the upper-left cell (option C).
- Smaller producers are willing to transfer a portion of their value to large producers and large producers rejoin the co-op in this sequential game.
- Can also think about the defection choice under new policy, as if the LP hasn't left yet.



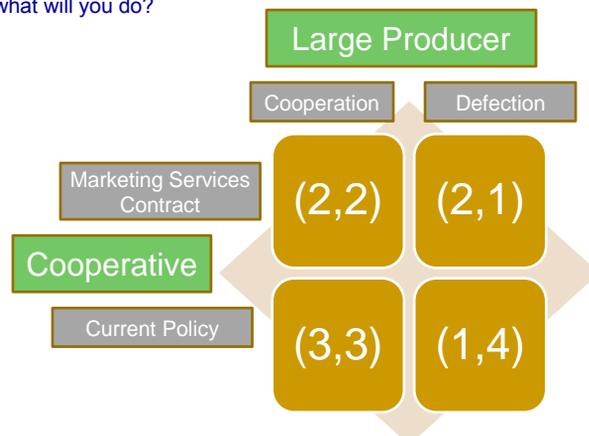
Example 2 – Changing Market Conditions

- Overall market conditions have worsened and there is less opportunity to use the policy as before; in this case, the co-op receives a lower payment of \$6 that now is allocated evenly to small and large producers at \$3 each.
- The large producer still has the opportunity to defect and get a higher payoff of \$4, but now this payoff depends on the continued existence of the coop (yardstick effect)
- Given that further benefits of scale economies have disappeared, the co-op is considering reducing scope of it's operations.



Policy Proposal II

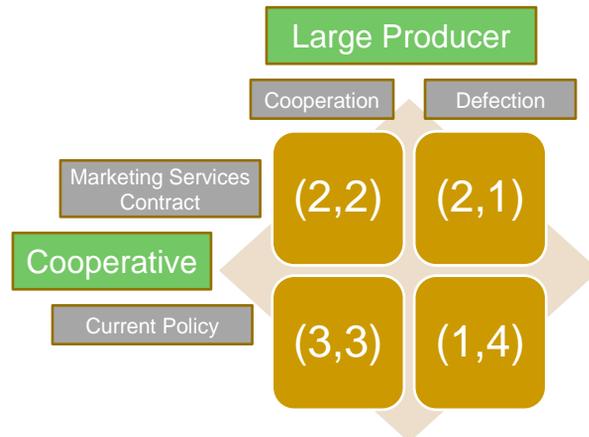
- Reduce the scope of operations by terminating independent marketing program and contract with our former competitor for marketing services.
- Coop will still provide storage, product assembly, and will negotiate the marketing services contract.
- The expected payments are estimated to be (2,2) with LP and (2,1) without.
- The existence of the option is under discussion and known by all.
- Now what will you do?



Policy Vote and Outcome?

What will the players do now?

- A. Coop approves proposal, LP cooperates
- B. Coop approves proposal, LP defects
- C. Coop rejects proposal, LP cooperates
- D. Coop rejects proposal, LP defects

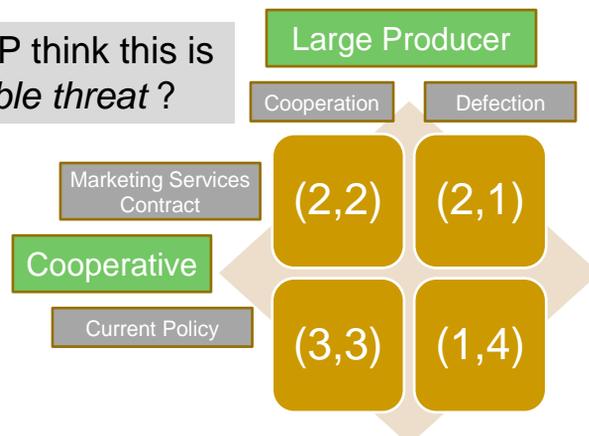


Policy Results – What will the players do now?

What will the players do now? It Depends! 😊

- A. Coop approves proposal, LP cooperates ... perhaps
- B. Coop approves proposal, LP defects
- C. Coop rejects proposal, LP cooperates ... perhaps
- D. Coop rejects proposal, LP defects

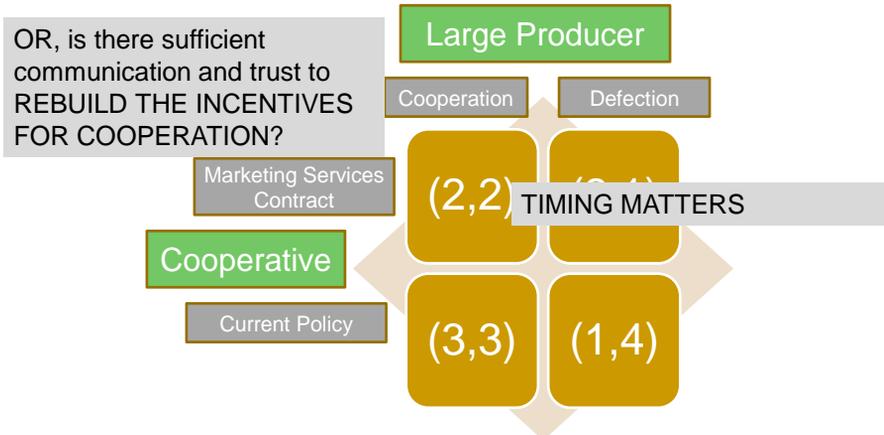
Does LP think this is a *credible threat*?



Policy Results – What will the players do now?

What will the players do now? **It Depends!** 😊

- A. Coop approves proposal, LP cooperates ... perhaps
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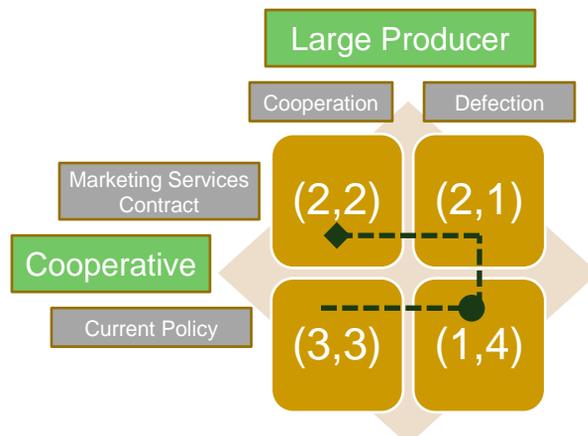


Policy Results

Case 1: If LP thinks the threat is not credible...

- LP will defect
- But if policy subsequently implemented, LP is much worse by staying defected
- LP switches to cooperation (Answer A)

Trust
Communication
Timing

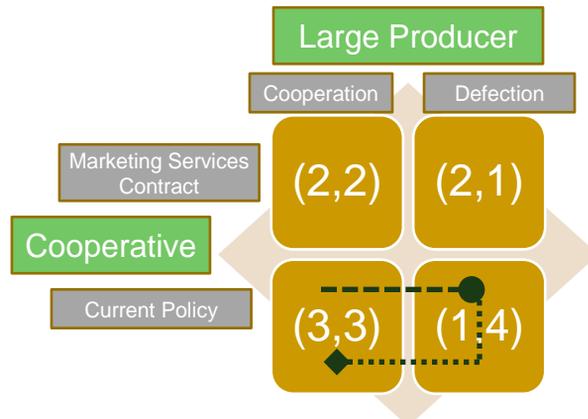


Policy Results

Case 2: If LP thinks the threat is credible...

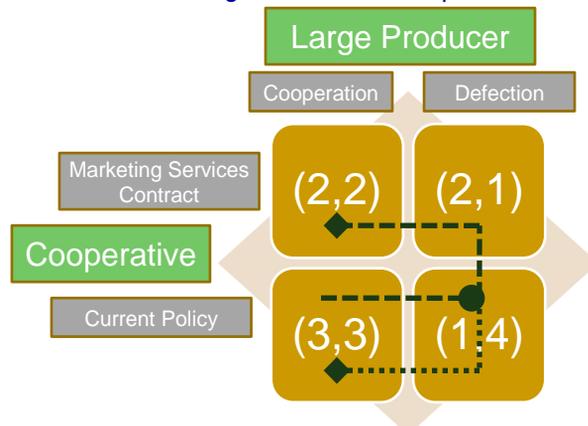
- **Opportunity to achieve the original outcome!**
- Answer C (but, in essence, w/o the BOD actually acting on the proposal)
- It is not the LP's preferred selection at the start, before the threat was perceived as credible, but it's better than the alternative

Trust
Communication
Timing



Policy Results

- Evaluating strategic options can be complicated as you need to consider your own and others (inter-dependent) choices, as well as impacts to overall market structures (e.g., yardstick effect)
- Even simple examples can show alternative solutions
- **Process and communication** of alternative strategies to members vital to rebuilding incentives for cooperation.



Conclusions

- Most cooperatives follow a rich mix of strategies that happen simultaneously and address multiple goals.
 - Most situations are more subtle and generally unfold as a gradual process of adjustment.
 - Our examples assume complete information that is adequately communicated, including the consequences of various actions. Lack of this can lead to lower-value joint outcomes.
 - There are many cooperative strategy examples we can think of that look to strike the balance between the needs of the members and the cooperative; e.g., building cooperative liquidity versus paying patronage, short run versus long run effects, etc.
 - Hopefully today's discussion wetted your appetite to learn (and do) more!
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