



PROMOTING THE UNDERSTANDING OF COOPERATIVES **FOR A BETTER WORLD**



Euricse's contribution
to the International
Year of Cooperatives

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For a better world

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Foreword

This report summarizes the main findings of the conference ‘Promoting the Understanding of Cooperatives for a Better World’, which was co-organized by Euricse and the International Co-operative Alliance (ICA) on 15 and 16 March 2012 in Venice, Italy. The report draws mainly, but not exclusively, on the papers and presentations delivered by the invited speakers.

The authors are extremely grateful to the invited speakers for their outstanding contributions. Special thanks also to the chairs, discussants, and rapporteurs for their valuable work and stimulating insights.

1

Realizing cooperative potential

Cooperative enterprises are influential institutions. In both industrialized and developing countries, cooperatives contribute to socio-economic development, support employment growth, and sustain a more balanced redistribution of wealth. Moreover, a widening set of innovative activities are based on cooperative efforts, especially in the provision of new services such as open-source software and general-interest services that improve the quality of life for entire communities.

The role and importance of cooperatives is increasingly apparent in the wake of the global financial and economic crisis. In most countries, cooperatives have responded more effectively to the crisis than investor-owned

firms¹. The resilience of cooperatives has increasingly been acknowledged, and policy and opinion makers are eager to understand how cooperatives can play a role in tackling the dramatic consequences of the global crisis and reforming the system that has contributed to generating it. The attention recently paid to cooperatives and related organizations by social networks, the media, and international organizations highlights this growing awareness.

However, in spite of their importance, cooperatives have not yet received the attention they deserve. The basic reason for this neglect has been a widespread conformism in interpreting the functioning of the economy, despite the increasingly inability of convention-

¹ In this report, the terms *investor-owned* and *for-profit* are used interchangeably to refer to enterprises that are owned by investors and specifically aim to maximize profits; both terms include family businesses. The term *for-profit* refers to the goal of the organization; the term *investor-owned* refers to ownership rights.

al economic theory to explain major events affecting contemporary societies. Since the mid-1970s, and especially following the collapse of the Socialist regimes, an increasingly strong wind of ‘market fundamentalism’ has blown from New York and Washington, deeply influencing the approach to economic policy around the world (Ferri, 2012).

The vision promoted by this wind is that the best way to trigger human progress is through an allocation mechanism of self-regulated markets populated by rational agents. Furthermore, the investor-owned enterprise is taken to be the ideal form for organizing the production of all goods and services, and efficiency is measured exclusively by the ability to create value for the enterprise’s shareholders - i.e., by maximizing profits (Ferri, 2012).

The main implications of this approach have been the adoption of privatization policies that aim to create more space for markets and the underestimation of entrepreneurial forms that differ from the for-profit ideal type. Consequently, cooperatives have been viewed as accidents, exceptions, or transitional organizations that were expected to disappear as a result of market completion. Few observers regard cooperatives as a distinctive type of institutional arrangement that populates the economic system alongside investor-owned firms (Grillo, 2012).

The predominance of this restrictive interpretation has weakened the interest of policy makers and researchers in cooperatives. Analyses have not been proportional to the importance of the cooperative sector, and those studies that have been conducted are rather

limited compared with the extensive research conducted on for-profit firms and markets.

In addition, most of these studies are based on inconsistent hypotheses. The specific features of cooperatives that distinguish them from family businesses and investor-owned firms have not been sufficiently analysed nor explained. A comprehensive theoretical framework that can account for the upsurge of cooperatives has not been elaborated. This lack of theorization has prevented the development of appropriate indicators to measure the social impact of cooperative enterprises. Moreover, the uncritical application of indicators designed to assess the efficiency of for-profit enterprises has consolidated the image of cooperatives as archaic or eccentric entrepreneurial forms that survive thanks to outdated traditions, special legal protection, and/or state intervention (Ferri, 2012).

The scarce interest in cooperatives and the widespread existence of *de facto* cooperatively managed enterprises that are not designated as cooperatives have prevented an accurate assessment of the size and impact of these institutions. Cooperatives are defined in various ways in different contexts or not defined at all. In countries where cooperatives are not recognized by law, people tend to establish collective enterprises but not to call them cooperatives, as sometimes occurs when farmers associate to market their products or communities inadequately served by commercial banks establish informal credit unions. Moreover, international statistical standards adopted by most national statistical offices do not collect data on the ownership

forms of enterprises. As a consequence, the available statistics on cooperatives are unsatisfactory: comprehensive data exist for only a few countries and are not sufficiently reliable.

Taken together, these deficiencies attenuate the visibility of cooperatives and limit the scope, performance, and success of cooperative enterprises. A lack of public understanding about the role and impact of cooperatives on well-being means that cooperatives are not widely recognized as an important form of entrepreneurial activity. Moreover, education about cooperatives is either limited or lacking in most public and private educational programmes. Consequently, cooperatives are often unable to find trained personnel and end up copying the management practices, organizational strategies, and impact-assessment methodologies of investor-owned firms.

There is a clear need to overcome the contradiction that exists between the reality and the recognition of cooperatives. This need has been accentuated by the ongoing crisis, the origins of which can be traced to unexamined beliefs about the role of competitive versus cooperative behaviours and the conviction that markets alone can ensure growth and welfare. These beliefs have in turn led to inadequate regulation of financial markets, deep and increasing inequalities in income and wealth distribution, misuses of non-renewable resources, and the predominance of short-term and irresponsible consumption models that threaten the environment.

Most observers agree that this crisis cannot be tackled by conventional policy measures, which will at best attenuate some of its dra-

matic consequences. New paradigms and institutional arrangements are essential. Given their ability to effectively combine economic, social, and ecological goals, cooperatives have the potential to address and alleviate the crisis, which suggests that possible paths to exit the crisis are available, but they have not yet been fully exploited. There is a dramatic need not only for improved models for explaining cooperative enterprises and their functioning, but also for innovative interpretations of the working of economic systems and the institutions that govern them.

Against this background, the Euricse Conference offered a multidisciplinary reflection on how diverse cooperative forms can contribute to shaping a sustainable economy and a fairer society. The conference stimulated discussion about the rationale, role, and size of cooperatives in various economic sectors. Existing theories were critically analysed and confronted with empirical evidence. Thus, the conference provided the conditions for the construction of new empirical knowledge and the elaboration of theoretical frameworks that can further our understanding of the potential of cooperative enterprises. The main findings are summarized in the following sections.

Section 2 highlights the lessons learned from history and the importance of cooperatives in terms of their socio-economic contribution and social value generated. Section 3 identifies the main obstacles preventing the full exploitation of the competitive advantages of cooperatives, including the existence of inadequate legal frameworks, ineffective

market regulations and policies, and poorly developed managerial practices. Section 4 examines the theoretical developments that can help explain the nature and rationale of cooperative enterprises, taking into account both the limitations of conventional interpretations and recent theoretical innovations. Section 5 analyzes the trends and challenges for cooperatives, while Section 6 summarizes three sets of recommendations that address the research community, public authorities, cooperative movements, and international donors.

2

The importance of cooperatives

From various perspectives, the contributors to the conference provided new data and information that highlight the importance of cooperatives both historically and in the contemporary conjuncture.

2.1

Lessons from history

Cooperatives have existed for around two hundred years. While operating in all fields of economic activity, cooperatives have greater longevity than for-profit firms. The cooperative model has continually adapted to changing conditions, and innovative forms of cooperation have emerged to address new economic and social concerns.

Cooperatives have developed in countries characterized by profoundly diverse political conditions, degrees of economic development, cultural characteristics,

and historical backgrounds. Consumer cooperatives, agricultural cooperatives, mutual-aid societies, credit unions, credit cooperatives, and worker cooperatives have been set up almost everywhere. Some specific types of cooperatives have registered an extraordinary growth in particular countries: for example, credit cooperatives in Germany, housing cooperatives in the United Kingdom and Sweden, and worker cooperatives in France and Italy. At the end of the 19th century, cooperatives performed an important role as economic and social institutions in Central and Eastern Europe. Interesting examples of self-reliance initiatives occurred in the Czech Republic, Bulgaria, Serbia, and Poland before the socialist takeovers (Borzaga et al., 2008). Similarly, cooperatives have played a key role in developing countries, even though they are often not institutionalized nor even acknowledged by law (Münkner, 2012).

When they first emerged, cooperatives were usually spontaneous defensive reactions to the harsh conditions engendered by the industrial revolution or rural poverty. Over the years, cooperatives have provided an ever-increasing share of income and employment in many countries and regions. Cooperative development is an ongoing process. New types of cooperatives—for instance, social and community cooperatives—have emerged to provide services that are characterized by an unsatisfactory supply, including social, educational, and work integration services to local communities and disadvantaged people. Furthermore, new cooperatives have emerged to help communities better exploit local resources (Hagedorn, 2012).

The main reason for the success and longevity of cooperatives is that they are not motivated to maximize the rate of profit for investors, but rather to address the needs of communities. Cooperatives should be regarded as collective problem solvers. Historically, cooperatives have prospered when they have specific advantages over investor-owned enterprises and satisfy needs that are otherwise unmet. User and consumer cooperatives have been established to minimize intermediation costs and retail prices; producer, especially agricultural, cooperatives to increase the weak market power of producers; worker cooperatives to provide members opportunities to self-manage their businesses. Mutual aid societies have been set up by workers and communities to provide common insurance and assistance. By satisfying the needs of their members,

cooperatives have contributed to improving the quality of life of large –and often disadvantaged–segments of society. Many public welfare policies have been established thanks to pioneering invention and experimentation by cooperatives. Key welfare institutions were originally developed by mutual aid and cooperative societies. Starting at the beginning of the 20th century, however, most social and health services in Europe were taken on by government authorities as part of the process of constructing welfare states. Consequently, these services were removed from cooperative and mutual control, and started to be publicly funded and provided by law to all citizens. This trend did not turn out to be unidirectional, however, since by the end of the 20th century new cooperatives were playing an increasingly important role in delivering services in many European countries.

Historical evidence shows that cooperatives not only survive crises better than other types of enterprises, but also more successfully address the effects of crises. The history of British consumer cooperatives during the 19th century is one of sustained growth that was only marginally checked by the impact of periodic recessions (Birchall, 2012). During the Great Depression of the 1930s, electricity and telecommunication cooperatives helped transform the rural economy of the USA. During the 1960s, a cooperative movement was created in New York to house 27,000 families (Birchall and Hammond Ketilson, 2009). During the radical restructuring of the 1970s, worker cooperatives in Europe grew

in number and demonstrated a lower failure rate than for-profit firms. The current crisis has provided further evidence of the strengths and resiliency of cooperatives.

2.2

The size of the cooperative sector

To understand the cooperative movement, a realistic estimation of the overall size of the cooperative sector is needed.

From the evidence available, it is clear that cooperatives play a significant economic role. Just to mention a few data, the United Nations estimated in 1994 that the livelihood of nearly 3 billion people—or half the world's population—was made more secure by cooperative enterprises (ICA, 2012). Worldwide, there are three times as many member owners of cooperatives as there are individual shareholders in investor-owned enterprises, and in the fast-growing BRIC countries there are four times as many cooperative members as direct shareholders (Mayo, 2012). The combined membership of cooperatives is between 800 million (ICA, 2012) and 1 billion people (Worldwatch Institute, 2012). According to the ICA, cooperatives are active in all countries and their importance is especially significant in poor communities.

As contributions to the Euricse conference documented, cooperatives are prominent in several sectors. In Europe, agricultural cooperatives have an aggregate market share of about 60 per cent in the processing and marketing of agricultural commodities and an estimated 50 per cent share in the supply of

inputs. In the USA, cooperatives have a market share of about 28 per cent in the processing and marketing of agricultural products, and a 26 per cent in the supply of inputs (Valentinov et al., 2012).

Worldwide, there are around 53,000 credit cooperatives and credit unions. In Europe, there are some 4,200 credit cooperative banks with 63,000 branches. These cooperative banks have 50 million members (about 10 per cent of the continent's population), 181 million clients, 780,000 employees, €5.65 billion of assets, and an average market share of about 20 per cent (V. Zamagni, 2012).

In the European retail sector, 3,200 consumer cooperatives employ 400,000 people and have 29 million members, 36,000 points of sale, and €73 billion of turnover.

As for utilities, the presence of cooperatives is quite important in the USA, where almost 1,000 electricity cooperatives control 40 per cent of the national electricity distribution lines, covering 75 per cent of country's territory and serving 37 million members and their households (V. Zamagni, 2012). Cooperatives play a major role in managing water supplies in Argentina and in Bolivia, where one large urban water cooperative serves around 700,000 customers (Mori, 2012).

Workers have organized cooperatives in a wide range of industries. In Italy, there are more than 25,000 worker cooperatives (Pérotin, 2012). In Spain, around 14,000 new cooperatives were established between 1998 and 2008, of which 75 per cent were worker cooperatives (Díaz-Foncea, 2012). The sectoral distribution of these cooperatives

tends to vary from one country to another: in France, many worker cooperatives exist in manufacturing and construction and a smaller number in services; conversely, in Uruguay a lower proportion are located in manufacturing and a higher proportion in transport and services, when compared to investor-owned enterprises (Pérotin, 2012).

According to the International Cooperative and Mutual Insurance Federation, 25 per cent of the world insurance market in 2008 was cooperative including 44 per cent in Germany, 39 per cent in France, 38 per cent in Japan, and 30 per cent in both the USA and Canada (V. Zamagni, 2012).

Social cooperatives, which are especially widespread in some European countries and in Canada, are a new form of cooperative that explicitly aims to enhance collective benefits. As a type, the social cooperative is positioned between the traditional cooperative and the non-profit organization, and it generally combines the involvement of a plurality of stakeholders (cooperative members) with the pursuit of general-interest goals. In Italy, where this type of cooperative is the most developed, social cooperatives over the last two decades have become key players in the welfare system. Since they were first created, social cooperatives in Italy have registered an average annual growth rate ranging from 10 to 20 per cent. In 2008, there were 13,938 social cooperatives, employing approximately 350,000 workers, utilizing 35,000 volunteers, and serving 4.5 million users (Andreaus et al., 2012).

In contrast to the conventional wisdom, recent research demonstrates that

cooperatives exist in a wide range of industries. Furthermore, in some countries they are larger than other enterprises and may even be better capitalized. Recent empirical studies show that employment levels in cooperatives appear more stable than in investor-owned firms: conventional firms tend to adjust employment levels, while worker cooperatives adjust pay, thus safeguarding employment (Pérotin, 2012).

To sum up, the contribution of cooperatives to income and employment is important overall, albeit not homogeneous. Despite the crisis and a demutualization process that has led many cooperatives to be transformed into investor-owned firms over the last two decades, cooperatives are not in contraction.

2.3

The economic impact of cooperatives

As highlighted by several presenters at the Euricse Conference, the assessment of the economic impact of cooperatives must be broadened beyond narrowly quantitative parameters. To better understand the role of cooperatives, particular attention needs to be paid to the contribution that these institutions provide to the overall functioning of economic systems.

Cooperatives contribute in at least five ways. First, they play a far from marginal role in reducing market failures, thereby improving the functioning of the economic system and the well-being of large groups of people (Hansmann, 1996). This contribution stems from the distinctive ownership and

governance rules of cooperatives. The coexistence of a plurality of enterprises that have diverse ownership structures and pursue different goals contributes to improving market competitiveness, which in turn provides more choices to consumers, helps prevent the formation of monopolies, lowers retail prices, provides opportunities for innovation, and limits information asymmetry.

Second, cooperatives play a key role in stabilizing the economy, especially in sectors characterized by considerable uncertainty and price volatility, such as finance and agriculture. Cooperative banks in Europe and credit unions in North America are seen as a stabilising influence on the banking system (Birchall, 2012). As historical evidence from previous recessions demonstrates, the stabilizing role of cooperatives is crucial during times of crises. Moreover, the presence of cooperatives improves the capacity of societies to respond to uncertain changes in the future.

Third, cooperatives contribute to keeping the production of goods and services close to the needs of the people that they serve. Often supplying goods and services that are innovative, cooperatives meet the specific needs of their members rather than respond to the rationale of profit maximization. They also can produce goods and services with low and uncertain, if not negative, profitability that investor-owned enterprises are not interested in providing and public authorities are unable to supply. Services with low or negative profitability include social, health, educational, and other personal and

community services. In cases of negative profitability, cooperatives can achieve the break-even point thanks to the attraction of additional resources—such as voluntary work and donations—or the implementation of price discrimination policies. Evidence from the experience of cooperatives shows that voluntary work and donations are especially important in the start-up phase of all types of cooperatives, regardless of their context of operation.

Fourth, cooperatives tend to adopt a long-term perspective, as they often become productive assets for the communities in which they operate. Cooperatives are generally concerned about the welfare of current and future generations. Consistent with the third ICA principle of members' economic participation, numerous cooperative statutes allocate a portion of cooperative surpluses to a collective and indivisible reserve fund that does not belong to members individually but must be utilized for the benefit of all and future generations. In some countries, the long-term perspective of cooperatives is incorporated into laws that oblige cooperatives to move part of their annual surplus to asset locks, meaning that part of their assets and profits must be used to promote community interests.

Fifth, cooperatives contribute to a fairer distribution of income. Since cooperatives are created to meet the needs of their members and are not conceived to accumulate profits, they tend to redistribute their resources either to workers by increasing wages or employment or to consumers by charging lower prices.

2.4

The social value of cooperatives

Since their establishment, cooperatives have been not only economic institutions, but also social actors that are explicitly committed to addressing problems affecting local communities or groups of stakeholders in need.

The social role of cooperatives is often highlighted, but it is seldom analysed systematically. The social impact of cooperatives is more than an additional feature or an externality: it is an added value that is voluntarily generated and is an integral part of the operation of cooperatives.

Nevertheless, the beneficial social impact generated by cooperatives varies according to the type of cooperative, the context, and the time frame. In addition to regional and sectorial specificities, it should be underlined that cooperatives are often institutional responses to extreme situations of need that threaten the lives of ordinary people and that they form thanks to joint action by a social group sharing a collective identity (Defourny and Nyssens, 2012). The focus of early cooperatives varied according to the main target group involved: in the UK, this was consumers; in France, artisans; and in Germany, farmers, urban artisans, and traders (Münkner, 2012). The social function of cooperatives is reflected in Raiffeisen's idea of a Christianity of action, Schulze-Delitzsch's idea of self-help, the Rochdale Pioneers' idea of an emancipation of the workers, and Victor Huber's idea of active self-education.

Historical evidence demonstrates that compared with investor-owned enterprises, cooperative solutions are more inclusive and more oriented to promoting general-interest goals with a beneficial impact on well-being. Financial cooperatives often aim to overcome financial exclusion; consumer cooperatives guarantee the supply of basic commodities, thus ensuring the survival of entire households; and agricultural cooperatives are the main institutional tool whereby independent farmers respond to the market power held by big retailers and seek to maintain their roles as the producers and protectors of local economies.

Early cooperative initiatives were strongly rooted in a 'collective awareness' that sought to improve the well-being of communities (Defourny and Nyssens, 2012). However, over the years cooperatives have become extremely diversified according to their location and field of operation. In countries where markets are more developed, cooperatives have weakened their social commitment and in some cases evolved into entrepreneurial forms that differ from investor-owned enterprises solely due to their ownership rights, rather than by virtue of their social aims. In some other countries, including many in Latin America, cooperatives have evolved into broader community-oriented enterprises. New types of cooperatives with declared social goals have been established over recent decades, and many of these operate in new fields of activity. Social cooperatives, for instance, are strongly rooted in forms of collective awareness, such

as the need to promote social justice, protect the environment, and support the social and professional integration of disadvantaged individuals. In social cooperatives, collective benefits are not simply induced by economic activity; rather, they are a key feature motivating members to undertake the activity (Defourny and Nyssens, 2012).

The Statement of Cooperative Identity and Principles adopted by the ICA in 1995 includes a seventh principle, ‘concern for community’, that articulates and revitalizes the social dimension of various types of cooperatives (MacPherson, 2012). The incorporation of this principle was designed to counter the tendency of cooperatives to emphasize the economic benefits of membership, which are linked to the distribution of surpluses in proportion to members’ participation, over the social impact. By confirming the connection of cooperatives with their communities, this principle highlights two distinguishing features: cooperatives’ close attention to the social consequences of their activities and their responsibilities to care for the communities in which they operate. In turn, cooperative commitment to the community is expected to generate competitive advantages, as shown by the experience of credit cooperatives, which derive their strength from their local embeddedness and community involvement. Moreover, given cooperatives’ goals and participatory structures, they have a built-in capacity to respond to new community challenges by creating businesses in a wide range of fields (MacPherson, 2012).

The social orientation of cooperatives

generates several beneficial effects. First, thanks to their embeddedness at the local level—which is facilitated by the participation of a plurality of stakeholders, including members, beneficiaries and workers—cooperatives contribute to enhancing social capital and strengthening trust relations within communities. Cooperatives can therefore be regarded as effective tools for developing civic attitudes and, in turn, generating social virtue (Dasgupta, 2012). The positive influence that cooperatives have on social cohesion stems from their ability to institutionalize key rules that ensure the accomplishment of mutually beneficial transactions. Cooperatives are characterized by a mutual affection stemming from the interdependent utilities cooperative members share, and members tend to have a pro-social disposition since they share a common goal that often coincides with the common good. Moreover, since they provide incentives to their members to keep promises, cooperatives can be regarded as institutions that translate into a specific contract the informal agreement of people who pool their resources. Cooperatives can hence be considered an external enforcer of socially oriented behaviours (Dasgupta, 2012).

Second, by protecting incomes and employment, cooperatives help solve problems that would otherwise remain the responsibility of public policies. Cooperatives have demonstrated an ability to create and preserve jobs in deteriorating market conditions better than investor-owned enterprises. Worker buyouts are increasing in some countries as a reaction by employees

who are concerned about losing their jobs. As recent takeovers in several countries have demonstrated, cooperatives can save jobs when a deep crisis occurs (Pérotin, 2012). It is increasingly recognized that unemployment has broader effects than its strictly economic consequences, particularly on health. If worker cooperatives create or preserve jobs for their employees, they also have positive effects on public expenditure and health in their communities. Additionally, when cooperatives complement the public supply of welfare services by providing new services that fill gaps in service delivery, they create new jobs.

Third, cooperatives do not limit themselves to creating employment opportunities; they often privilege disadvantaged workers excluded or at risk of exclusion by the labour market. In some countries, cooperatives explicitly favour workers discriminated against by investor-owned enterprises and provide them with appropriate on-the-job training to help them overcome their disadvantages (Defourny and Nyssens, 2012).

The social benefits generated by cooperatives are seldom taken into consideration by impact analyses that compare the performance of different types of enterprises since these analyses are usually based on narrow efficiency criteria. Most of these comparisons are biased towards investor-owned firms since they do not consider the social aims, intrinsic outcomes, and collective benefits generated by cooperatives. This approach is not only

epistemologically flawed, but also incapable of developing adequate policies (S. Zamagni, 2012).

3

Obstacles to cooperative development

Cooperatives often face severe obstacles that hamper their development. These obstacles are generated by weak legal frameworks, inadequate market regulations and policies, and poorly developed managerial practices adopted by cooperatives.

3.1

Cooperative legislation

While the regulation of for-profit enterprises is relatively uniform across countries, cooperative law varies greatly and in some countries specific legislation is non-existent. These differences are difficult to understand given the strong effort made at the international level to promote a shared conception of the values and principles of cooperatives, as highlighted by the ICA Statement of the Cooperative Identity of 1995,

which was a document officially recognized by the UN in 2001 and the International Labour Organization (ILO) in 2002 (Münkner, 2012). This lack of uniformity has two main implications: first, it undermines or limits the visibility and use of the cooperative ownership form; second, it prevents the internationalization of cooperative businesses and weakens the potential interaction among cooperatives based in different countries.

Cooperative legislation is often restrictive rather than enabling. In some countries, legislation restricts the sectors where cooperatives are allowed to operate and the scope of activities that can be carried out by members. Additional obstacles are generated by setting high minimums on the number of members or assets required to establish new cooperative enterprises. Furthermore, especially in countries where cooperatives are

still classified as non-entrepreneurial entities, there are limitations placed on the scope and form of their business operations.

The low esteem in which cooperatives are generally held has prompted some national legislatures to allow for or to favour cooperative demutualization. This has occurred, for instance, where the law allows the transformation of mutual aid societies and cooperatives into for-profit enterprises, with the consequent risk that transformation choices are induced by opportunistic members or managers who are primarily interested in seizing control of the assets that cooperatives have accumulated.

3.2

Market regulations

Cooperatives can be prevented from fully exploiting their competitive advantages by market regulations. While in some cases market regulations are neutral or even favourable to cooperatives, in others competition rules may limit the development of cooperatives. The Euricse Conference highlighted several examples of market regulations that have had negative effects.

When designed without taking the specificities of cooperatives into account, the regulation of financial markets hinders the development of cooperative enterprises in the credit sector. International accounting standards and international financial rules such as the Basel Accords limit the development and growth of cooperatives when they impose capitalization schemes, liquidity management

systems, and governance mechanisms that fail to take the specificities of the cooperative model into account (Grillo, 2012). A failure to recognize the specific nature of cooperatives can generate disproportionate regulatory costs on cooperative banks and reduce access to credit by small enterprises and households (Ferri, 2012).

Similarly, in the public utilities sector, antitrust authorities may seek to defend users against the market power of providers by imposing rules and constraints that generate additional costs. These rules presuppose the sole existence of investor-owned enterprises. When cooperatives are involved, however, some of these rules and constraints are redundant and generate unnecessary costs since users are already protected by the cooperative ownership form. A similar situation occurs in the general-interest service sector. Cooperatives can be damaged by inequitable processes of contracting out the provision of these services when the system of contracting is based on criteria that do not recognize the intrinsic differences between cooperatives and investor-owned enterprises.

3.3

Support policies

Cooperatives normally benefit from public policies that have been designed to support the start-up and consolidation of business initiatives. Since dedicated measures are sometimes introduced specifically to support cooperatives, there is a widespread conviction that cooperatives are favoured in

comparison to investor-owned enterprises. This is a simplistic conclusion. Indeed, policies supporting cooperatives are often weak, contradictory, or controversial.

In some countries, policies withhold the full status of ‘enterprise’ from cooperatives, thereby denying them the benefits provided to for-profit firms. For example, employment subsidies are sometimes denied to the members or employees of cooperatives. In some other countries, legislation imposes burdensome obligations on cooperatives that do not apply to investor-owned firms. This occurs, for instance, when cooperatives have to comply with locked asset rules, but are not qualified to receive fiscal benefits in the name of competition. Moreover, cooperatives are often not entitled to the incentives and fiscal advantages granted to non-profit organizations even though they pursue the same social and general-interest goals.

3.4

Management and governance practices

Cooperatives face many challenges as they pursue economic performance while seeking to remain faithful to their values and founding principles. Cooperatives must struggle to adopt management and accounting practices that reflect their ethics.

Mainstream managerial practices are often inadequate for managing cooperatives. The lack of educational and training programmes tailored to the needs of cooperatives leads managers to adopt practices and tools inconsistent with the mission of cooperatives.

While cooperatives have grown in number and size in many sectors and proved to be efficient, management has remained an area of weakness (V. Zamagni, 2012). The copying of practices from investor-owned firms disregards the potential of cooperatives to develop alternative models that are more efficient and consistent with the cooperative ownership form.

Weak management has several negative consequences: it encourages cooperatives to mimic the practices of investor-owned enterprises; it hinders cooperatives from exploiting their key advantages, especially those resulting from the strong and active engagement of members; and it stimulates demutualization by opportunistic members and managers.

The lack of consistent management practices occurs especially when cooperatives grow in size and when the heterogeneity of members’ interests increases. In principle, this issue could be managed through innovative governance strategies. However, cooperatives are often trapped between isomorphic tendencies and ideological governance solutions. Thus, experimentation with innovative strategies can be hindered by the passive acceptance of an exclusive governance model of assemblies and boards that are elected on the basis of the principle ‘one head, one vote’ (Hansmann, 2012). At the same time, empirical experience demonstrates that there are various governance strategies by which cooperatives can be managed and ownership costs reduced, even when heterogeneous interests are at play. However,

these innovative strategies have rarely been analyzed in depth and formalized, and hence their adoption has not been extensive.

Presenters at the conference provided examples of these processes. Case studies of Mondragón and cooperative banks in Finland have shown that institutional adaptation is an important factor accounting for success. Thanks to their ability to adjust to changing conditions through the design of innovative governance solutions, both of these cooperative groups have demonstrated their ability to thrive while responding to pressures to sustain democracy (Jones and Kalmi, 2012).

4

Interpreting cooperatives

A new interpretative framework is needed. to overcome the obstacles that have been identified and to strengthen the economic impact and social value of cooperatives. One important aim of the Euricse Conference was to shed light on theoretical developments that can help explain the nature and rationale of cooperative enterprises. The presenters identified both the limitations of conventional interpretations and recent theoretical innovations.

4.1 Limitations of conventional economic theory

While adopting different analytical approaches, all conference presenters agreed on the need to challenge the widespread belief that cooperatives are generally less

efficient than investor-owned enterprises. Several speakers contested the inadequate starting assumptions of conventional theories regarding not only cooperatives, but also larger economic and social systems.

Particular attention was paid to three limitations of existing theories. The first is the assumption that the main condition of efficiency is the specialization of tasks deriving from the division of labour. Economists generally assume that whenever the social division of labour is maximized, the specialization of agents can be strengthened and the maximum level of production allowed by technology will be achieved. This assumption disregards the efficiency gains that can result from cooperation among agents pursuing the same activity rather than specializing in specific tasks.

The second limitation is the assumption

that competitive markets and contracts are the most efficient social institutions for coordinating independent, specialized, and rational agents. An additional embedded assumption is that competitiveness characterizes markets naturally or that it can be achieved through adequate regulation. However, in many cases the market is not—nor can it become—fully competitive, and as a result the market is unable to generate the maximum social welfare. Under such conditions, opportunities for recourse to the market are structurally limited.

The third limitation is the assumption that economic agents are fully rational and self-interested, and thus that they can be characterized by a utility function with one exclusive determinant: the maximization of net income that is generated by their participation in any type of economic activity. This simplification is unable to explain the real behaviour of agents, who are not usually solely motivated by monetary rewards. Moreover, it is unable to explain why transactions take place even when the maximum possible monetary gain is not achieved. There are two important reasons why these transactions may occur. The first is that the decision to take part in an economic activity results from self-interested motivations other than monetary rewards. Such rewards include, for instance, the stabilization of income over time in worker cooperatives and opportunities to sell commodities at fair prices under inter-temporal conditions in agricultural cooperatives. The second reason is that agents are not driven solely by self-interested motivations, but also

by pro-social motivations—such as reciprocity, moral commitments, or process-regarding preferences—that overshadow or are combined with self-interested motivations. A broader view of the nature of individuals has been developed by behavioural economists, who have highlighted the human capacity to cooperate based on ‘strong reciprocity’ (Ben-Ner and Ellman, 2012; S. Zamagni, 2012).

It is not surprising that the conclusions arising from the application of theories that disregard the limitations of the mainstream approach are questionable and inconsistent with the real functioning of cooperatives. For example, consider the ‘perverse supply response’ that is alleged to take place in worker cooperatives—i.e., that cooperatives are expected to reduce employment when prices increase. Recent empirical studies show that cooperatives do not exhibit any perverse supply response to changes in product prices or demand shocks. Rather they show that cooperatives tend to favour the creation and stability of employment more than conventional firms (Pérotin, 2012). A similar condition exists regarding the supposed structural inefficiency of cooperatives due to the expected free-riding behaviour of uncontrolled workers. This interpretation disregards the role of intrinsic motivations, which are often the key factors influencing the decision to join cooperatives.

To sum up, interpretations based on dubious assumptions are not an adequate basis for understanding the rationale of cooperative enterprises.

4.2

New theoretical developments

To understand the rationale of cooperatives, it is necessary to conceive market exchanges as only one possible coordination mechanism generating collective benefits. According to this assumption, which is largely shared by economists, the market's peculiarity is its ability to efficiently manage exchanges when all participating individuals achieve fair benefits by rearranging the distribution of goods or tasks among themselves.

Indeed, alternative mechanisms based on hierarchy or cooperation can also generate collective benefits. According to conventional economic theory, both public agencies and private enterprises relying on a mix of such mechanisms appear to be more efficient social institutions whenever the market fails. Nevertheless, the key step is to recognize that not all enterprises share the same features. Both public agencies and investor-owned enterprises are mainly based on hierarchy. In addition, investor-owned enterprises are largely organized according to contractual relations that replicate the rationale of market exchanges. Indeed, investor-owned enterprises can be regarded as 'privately owned markets' in which interactions among economic agents are based on self-interest and monetary exchanges (Heath, 2006). As a consequence, investor-owned enterprises often tend to fail under the same conditions as markets.

Unlike investor-owned enterprises, cooperatives are mainly based on voluntary cooperation. The possibility of exploiting

the cooperative mechanism allows for the generation of competitive advantages in specific conditions, depending on the type of transactions that take place. Cooperatives have specific advantages especially when coordination cannot be achieved exclusively through economic and self-seeking behaviours. There are indeed several situations in which collective gains can be achieved under the condition that social agents trust each other, adopt cooperative rather than—or in addition to—self-interested behaviours, and activate motivations and behaviours that are other-regarding or based on reciprocity. When inter-temporal agreements generate gains greater than those derived from other arrangements, cooperatives can seize the advantages of scale economies; this situation occurs, for instance, in agricultural cooperatives. When the pooling of risks of large numbers of members occurs, mutuals and insurance cooperatives succeed in achieving more efficient solutions than market exchanges. When efficiency presupposes that agents 'tell the truth', cooperatives can efficiently manage the transmission of information. Finally, when the goods and services produced are characterized by positive externalities that cannot be internalized owing to the impossibility of charging the beneficiaries the full value of the products through the price system, cooperatives have an efficiency advantage.

All these situations are widespread, and consequently a large space of action exists for cooperatives of different types, including cooperatives explicitly pursuing social goals.

This interpretation of the diversification of economic institutions implies that the characteristics distinguishing cooperatives in terms of coordination mechanisms are critical. These characteristics include the indivisibility of cooperatives' economic and non-economic roles, the principles guiding cooperative action, and the statutory constraints under which cooperatives operate. All these characteristics are consistent with the specific coordination problems that confront cooperatives of various types.

This approach to cooperatives has four important implications. The first is the efficiency advantages that characterize cooperatives when compared to market exchanges, investor-owned enterprises, and public institutions. In particular, cooperatives derive specific efficiency advantages from their stronger reliance on motivations other than self-interest. Furthermore, cooperatives are expected to be less subject to free riding compared to other institutions. The additional resource of cooperatives is the members' intrinsic motivations, and efficiency analyses should take this critical factor into account (S. Zamagni, 2012).

The second implication concerns the viability of cooperatives. Cooperatives survive and prosper in fields where mechanisms other than market exchanges apply and non-self-seeking motivations play a key role. This is the case for the credit sector, where organizations based on trust relations contribute to improving the exchange of information. It can also occur in the agricultural sector, where cooperation among farmers allows for the

achievement of important economies of scale in activities that are not subject to the division of labour (Valentinov et al., 2012). Other examples include mutuals, which are effective at pooling risk, and social cooperatives, which are efficient when positive externalities that cannot be internalized are generated.

A third implication concerns the potential of cooperatives. Consistent with the proposed theoretical framework, cooperatives have a lot of potential for development around the world. In developing countries, considerable scope exists for obtaining collective benefits from cooperative mechanisms owing to low levels of income, the underdevelopment of market exchanges, and limited welfare systems. In industrialized countries, there is an increasing and diversified demand for social and community services that are characterized by positive externalities.

A fourth implication involves the limitations of cooperative enterprises. Cooperatives tend to lose their competitive advantages in addressing market failures as soon as markets become more competitive. Nevertheless, the evolution towards competitiveness occurs only in specific markets and under precise conditions; indeed, it involves only those activities where the division of labour can further increase and market failures can be significantly attenuated or eliminated through the evolution of the market itself or by regulation. When markets become more competitive, cooperatives can still play a role provided they adopt marketing or organizational strategies that increase the value added of their products.

To sum up, the decision to create cooperative enterprises of various types, their survival, and their contribution to the economy and society can be explained by the advantages that cooperatives have over for-profit firms. The Euricse Conference clarified two important issues. First, from a variety of perspectives presenters contested the ideas that cooperatives are marginal enterprises and market exchanges and investor-owned firms are inevitably the most efficient social institutions. This belief relies heavily on theories that have many shortcomings. Second, the presenters' findings demonstrated the feasibility of developing a new theoretical strand more consistent with the results of historical and empirical analyses of cooperatives.

Although further theoretical developments are needed, the clarification of these issues has important implications for cooperatives at an operational level.

5

Trends and challenges

The future holds major challenges for cooperatives. The global crisis has not only demonstrated that cooperatives can be more resilient than investor-owned enterprises, but also shed light on the shortcomings of the predominant model of economic organization, which is centred on the action of two types of institutions: for-profit enterprises coordinated by the market and public organizations based on the principle of authority. The crisis has confirmed the inability of for-profit enterprises alone to ensure well-being, especially when exchanges fail to benefit both parties of a transaction. Moreover, it has made explicit the inability of public agencies to confront all the failures of markets and for-profit enterprises on the one hand and to meet the growth and diversification of needs on the other. The crisis has shown that privatization policies based on the reallocation of tasks and roles between

for-profit enterprises and public agencies is not a viable solution. Indeed, the strategy of extensive liberalization and privatization that has been followed by most national governments since the 1980s has led to unsatisfactory outcomes. Such shortcomings have led to a dramatic increase in inequalities, the misuse of non-renewable resources, and the growth of uncertainty and poverty.

The awareness of the limitations of an economic organization that overvalues competitive and self-seeking behaviours is leading to the adoption of social responsibilities and innovative management strategies that emphasize collaboration also by for-profit enterprises. It is not surprising that a growing number of observers consider the expansion of various forms of cooperation as a viable way out of the crisis. Consequently, new spaces for development have emerged

for both traditional and new types of cooperatives.

Traditional cooperatives are expected to play an increasingly significant role in key activities such as providing credit and housing and supporting agriculture and job creation. Cooperative banks and credit unions should continue to develop as they have proven to be less risky than big corporate banks, and they have managed to strengthen trust relations and attract new clients. Agricultural cooperatives will become increasingly important for ensuring the survival of farmers and agricultural production, given increased food needs due to population growth. In addition, agricultural cooperatives can play an important role in ensuring food security, protecting the environment, and promoting a sustainable model of development. With job security decreasing and unemployment rates rapidly increasing, the many existing examples of new worker cooperatives and worker buyouts suggest that a more prominent role can be played by cooperatives in saving jobs and creating employment.

Furthermore, there are several new fields where the potential of cooperatives is far from being fully exploited. These include personal services and, in particular, social, educational and health services. These services are characterized by increasingly diversified demand in situations where, on the one hand, the public supply of these services is limited and decreasing while, on the other, the quality of the private for-profit supply is variable and uncertain. Similar considerations apply to mutuals, which can serve to compensate for

the declining coverage of health and long-term care by public insurance institutions.

Another expanding field is community services, including the management of cultural institutions, water resources, waste disposal, public transportation, and renewable sources of energy. All these activities are characterized by either natural monopolies or low and uncertain profitability. Cooperative enterprises are best suited for providing services under these conditions due to their participatory membership and governance models.

A growing field of activity for cooperatives is institutionalizing networks of small enterprises outside the traditional sectors of agriculture and fishing. Cooperatives can effectively manage common activities, including research and product development, and promote the expansion of markets and increase the productivity and competitiveness of member enterprises.

Presenters at the conference provided several examples of new types of cooperatives and innovative modalities of organizing traditional cooperatives. Nevertheless, it is clear that more effective exchanges of practices would better support mutual learning and stimulate a revival and strengthening of cooperatives around the world.

6

Implications for action

To fully exploit the advantages of cooperatives, several obstacles need to be overcome. The conference presenters emphasized the barriers limiting the development of cooperative enterprises and suggested remedies. Their proposals can be summarized as three sets of recommendations that address the research community, public authorities, cooperative movements, and international donors.

6.1

Introducing adequate regulations and support policies

The first set of recommendations concerns the adoption of both consistent regulations that allow for the exploitation of cooperatives' competitive advantages and support policies that facilitate their start-up, expansion, and

consolidation.

In Europe, cooperatives have developed most rapidly where their expansion has been unhindered by inadequate regulation, their roles are fully recognized, and their operations have not been confined to specific sectors (V. Zamagni, 2012). To develop cooperatives' full potential, cooperative law must recognize the roles of cooperatives and be flexible enough to permit cooperatives to operate in whatever industry they prove useful (Hansmann, 2012). This includes sectors that have been traditionally public, are of public interest, or benefit from public funding. Accordingly, the cooperative principles that have been elaborated by the ICA should be interpreted in a flexible way, supporting the emergence of new forms of cooperation and governance practices.

Cooperatives should be treated according

to their special nature and be guaranteed a level playing field with competitors (Münkner, 2012). Similarly, the regulation of markets should be consistent with the character of cooperative enterprises and designed to maximize collective gains for society. This issue needs to be addressed mainly by public agencies charged with market regulation responsibilities.

Necessary areas of action include helping to start new cooperatives, supporting established cooperatives, and building capacity within the cooperative sector. National policies should ensure that cooperatives have access to business services. In addition, national governments should develop consistent support policies at all levels of government. Given their not-for-profit orientation, cooperatives should be subject to more favourable fiscal treatment than investor-owned enterprises. However, while providing for legitimate tax breaks and special benefits, cooperative legislation should include specific obligations for cooperatives to prevent demutualization, such as asset lock rules. Against this backdrop, cooperative movements can play a key role through umbrella organizations, federations, consortia, and the development of ad hoc cooperative funds supporting the creation of new cooperatives.

Moreover, both national and local governments and the cooperative movement should play a key role in building bridges between the cooperative movements in countries and regions with a well-developed cooperative sector (e.g., the European

Union and North America) and cooperative movements in regions where cooperatives still lack adequate recognition.

6.2

Developing consistent governance and management practices

The second set of recommendations regards the development of a consistent management culture incorporating the values and principles of cooperatives. A stronger awareness by members about the intrinsic features of cooperative enterprises should be encouraged. The widespread practice of altering the management of cooperatives to that of for-profit enterprises should be reversed. To fully exploit the specificities of cooperative enterprises and avoid cooperative enterprises being overtaken by for-profit enterprises in the adoption of cooperative behaviours, management practices more consistent with the values and principles of cooperatives should be adopted. Cooperative movements and universities should endeavour to support new research on management practices and governance models, and seek to develop the managerial skills of cooperative leaders through innovative training and university courses based on recent research findings.

The experience of cooperatives worldwide shows that the most successful cooperatives tend to operate together as a system of enterprises—federations, consortia, or groups—to reap the advantages of scale and provide member cooperatives with

cost-effective technical and management assistance, marketing and purchasing services, training, and project planning. Nevertheless, the tendency of cooperatives to grow in size should be carefully evaluated. In economies increasingly based on knowledge, the most efficient enterprises may indeed be small and organized in networks; in this respect, cooperatives have specific advantages such as their embeddedness in local communities and participatory forms of governance. An effort to strengthen networking practices would help cooperatives achieve economies of scale and take advantage of growth opportunities that single enterprises would not otherwise be able to exploit.

6.3

Promoting the visibility of cooperatives

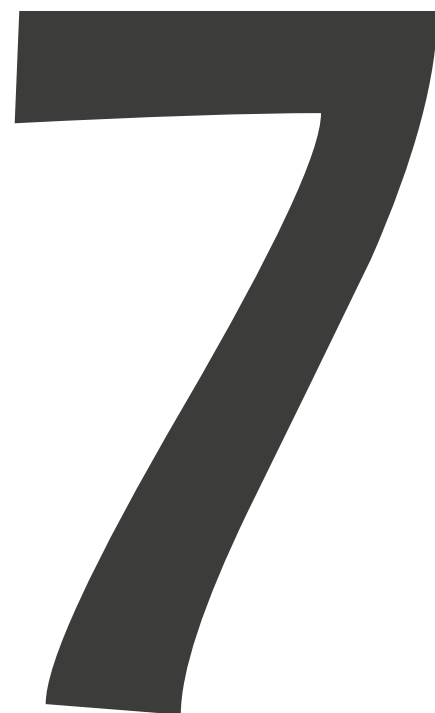
The third set of recommendations involves specific measures and actions for supporting a better understanding of the rationale of cooperatives and increasing their visibility as institutions fulfilling key economic and social roles.

Conference presenters highlighted the considerable scope for new theories that can comprehensively explain the rationale of cooperatives and identify how to better exploit the potential of cooperative action. Researchers should commit themselves to overcoming the fragmentation that has characterized cooperative studies and developing more systematic research that starts with realistic assumptions about both the mechanisms that can be employed by

economic agents and the motivations driving their actions. Updated and homogeneous statistical data should be produced and made available by research institutions and statistical agencies, and new theoretical approaches that can help explain the rationale and competitive advantages of cooperative forms should be developed by universities and research centres.

Drawing on the findings of recent research, measures that enhance the visibility of cooperatives should be promoted by national and international cooperative movements and public authorities. A more effective communication strategy to disseminate research findings should be adopted by both the research community and the cooperative movements at all levels—local, national, and international. Cooperative movements should endeavour to raise awareness by public administrations, policymakers, and communities about the contributions of cooperatives to local economies and welfare systems.

Finally, international donors should support the political recognition of cooperatives especially in those countries that still lack appropriate legal environments for developing and supporting cooperative enterprises.



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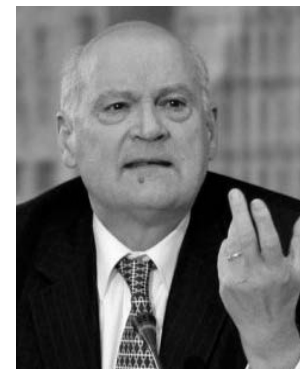
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