



# **Australian Nuffield Farming Scholars Association**

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**Subject:**

**“A General study of Agricultural Co-Operatives”**

**by**

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**THE RON BAILLIEU MEMORIAL SCHOLARSHIP**

**Sponsored by the Australian Nuffield Farming  
Scholars Association**



## THE ASSOCIATION'S MISSION

**The Australian Nuffield Farming Scholars Association promotes excellence in all aspects of Australian agricultural production, distribution and management through the adoption of local and international best practice and the continuous development of a unique network of industry leaders and innovators.**

## **Acknowledgements.**

I would like to thank the Australian Nuffield Farming Scholars Association for the great privilege of being chosen as the Ron Baillieu Memorial Scholar, as well as the opportunity to attend the Wye College course on Advanced Agricultural Management.

To the board of the Mackay Sugar Co-operative Ltd for the additional financial assistance they provided.

I would also like to express my deep gratitude to the directors, senior management, and representatives of the many U.K. and Irish Co-operatives which I interviewed during my Nuffield Scholarship. Invariably they gave freely of their time and experience; without which my scholarship would not have been as productive as it was.

Thankyou to Nuffield Scholars of the U.K. and France for their hospitality and assistance especially Steven Bullock and Simon Weaver. I would also like to express my gratitude to Kate Taggett and Edgar Parnell of the Plunkett Foundation for the assistance they provided.

I wish to thank my brother Henry who looked after my farm so well during my scholarship.

Finally to my wife Stepheny who gave me her support and encouragement as well as a beautiful daughter during my time away.

## **Introduction**

My objective was the study of Agricultural Co-operatives focusing on the areas of development, member relationships, structures, new shareholders, board development and alliances.

## **My Nuffield scholarship was separated into three distinctive parts.**

### **Firstly:**

The Worshipful Company of farmers advanced agricultural management course at Wye College Kent. One Australian or New Zealand Nuffield scholar is chosen annually to attend this course.

The areas covered were

- . Agricultural business planning
- . Management accounting and finance
- . Human resources management
- . The marketing of Agricultural Products
- . Agricultural policy and politics
- . And the Management Environment

Apart from the formal lecture program, a wide variety of after dinner speakers was provided during the three week course. These included Lord Carter (The Government chief whip in the House of Lords), Mr Barry Leathwood (Transport and General Workers Union ), and Professor Norman Coward ( Head of the Agricultural Department of the Midland Bank).

The course was extremely beneficial to me on a number of fronts. One, it increased my knowledge of agricultural management, which it was designed to do. Secondly, it gave me a greater understanding of UK agriculture, which assisted greatly in my latter research of Co-operatives.

### **Secondly:**

The tour organized by the Nuffield scholarship association. The tour was for five weeks. The first two weeks were spent visiting Singapore, Malaysia, Thailand, and Laos. There was no focus on any particular industry, the aim was to expose the participants to as many aspects of Asian agriculture as possible in a two week period.

We visited farms, universities, processing plants, Embassies and Government departments; as well as being introduced to major importers of agricultural commodities.

Following the Asian Leg of the tour was a tour of the UK and Continental Europe; again there was no focus on any particular industry.

One of the highlights for me were the two days spent in Brussels where we received lectures from European community policy makers, farm lobbyists, European and Cairns Group diplomats. It became quickly apparent that the formation and adoption of new policy within this environment could only be achieved under crisis conditions due to the enormous power of the agricultural lobby groups most notably France's.

Another interesting aspect of European agriculture is the prominent position that the farming community has within the national ethos. This combined with strong general public interest in how the rural environment is treated and looks, means a greater propensity to accept the cost of the common agricultural policy. It would seem to me that there is very little likelihood that any substantial changes to CAP outside of those changes needed to cope with the expansion of European community into Eastern Europe are possible.

One other thing that impressed me greatly was how competitive a lot of European Agriculture is; this is especially true in industries, which have little or no assistance from the EC. The UK in particular would have many agricultural industries, which could survive, in the world market.

## **The final part of my scholarship was the study of Co-operatives.**

My study of Co-operatives on my Nuffield Scholarship centered on six areas.

- : Development and history of individual agricultural Co-operatives.
- : Farmer member relationships with their Co-operatives
- : Reviewing different Co-operatives structures principally the difference between Corporate and the traditional Co-operative structure
- : Introduction of new shareholders to the co-operative
- : Board Development
- : Alliance between Co-operatives

Over my Nuffield Scholarship I visited and spoke to the representatives of over 40 Co-operatives and farmer controlled businesses. The bulk of these were in the UK and the Irish republic.

I visited many types of Co-operatives ranging from large diversified operations which may include feed mills, grain storage, livestock trading, plus farm input stores with 8000 members and \$ 250 million + turnover to a specialist seed potato marketing Co-operatives with 10 members and no staff. I tried also to get a cross section over as many agricultural industries as possible to give a greater understanding of the effect different commodities and markets have on the Co-operatives formation and structure. I also visited the Scottish agricultural organisation society Ltd, Ulster Agricultural Organization Society Ltd, Irish Co-operatives Organization Society Ltd, and the Plunkett Foundation. All of these organisations specialise in assisting Co-operatives. The Plunkett Foundation has an excellent library, which also greatly assisted me in my study.

## **1. Development and history of individual co-operatives.**

At each co-operative that I visited I always asked the question "Why was the co-operative originally formed and how has the purpose changed over time."

In reality co-operatives are formed because a group's resources are greater than any single individual. However the stimulus for the formation is often shocks or crises which exposed an individual to his or her fundamental weakness in the face of the market.

The oldest co-operative I visited was Aspatria Farmers Ltd. This is what the UK farmers describe as requisite co-operative. Aspatria Farmers Ltd is a supplier of farm inputs. Aspatria was formed after a group of farmers were dissatisfied with the quality of the fertiliser in 1869 and took the manufacturer to court and lost. However they decided to form a co-operative and get quality inputs at reasonable prices and this is exactly what they are doing in the same area of Cumbria from where they started.

A number of Co-operatives I visited were formed when a processor closed down and they needed to find a new market for their commodities. An interesting feature of a number of these co-operatives, is how they integrated their operations into that of the remaining processors. In the case of one pig marketing co-operative because the co-operative handled the delivery and transport of more than 60% of the processors kill they have reduced their staff and pay the co-operatives for the service. There is also recognition on the part of these co-operatives of the importance of the success of the processors business.

The UK co-operatives scene is not as strong as its continental counter parts. There are a number of explanations, firstly, culture. UK farmers are believed to be more independent. If this is the case it is more due to the fact that they are generally larger farmers than the Europeans. So they can afford independence. Secondly, there has been a long history of statutory marketing boards for many agricultural products, which has provided higher than world markets prices. Thirdly even before the UK joined the EC the British farmer was heavily subsidised dating back to WWII where government policy was to maximise food production, one of the few government policies which achieved its goals. This all has lead to British farmers not being exposed to the full force of the market. Interestingly enough the input side of a farmers business was an area where the growers could do something about. So they formed co-operatives to reduce

costs, through machinery rings, buying groups, and grain storage co-operatives.

The systematic destruction of the marketing boards by the conservative government has created a climate where the individual farmers are suddenly aware of their market weakness. This has stimulated the formation of many marketing co-operatives. The UK dairy industry is a classic case, since 1994 when the milk marketing board was broken up, many co-operatives have been formed. It was extremely interesting for me to see many dairy marketing co-operatives at very early stages of their development and how they are all trying to gain a foothold in the processing sector to secure market share.

Of the co-operatives I visited only a few had moved away from their original purpose, mostly seeking new businesses to help offset the costs of operating the co-operatives original services.

## **2. Farmer member relationship with their Co-operatives.**

The primary focus for me here was how the co-operatives communicated with its members.

Nearly all the co-operatives I saw basically used the same techniques for communication with their members. These included, newsletters, shed meetings, AGM, comprehensive annual reports, extraordinary meetings for special events, and easy access to staff and directors.

Dairy co-operatives however worked at this communication better than others. Mainly due to the need for dairy strict quality control in milk production. As one general manager informed me milk is a dangerous product.

Their field officers maintain close contact with the farmers, rarely using a big stick but trying to work through problems. These field officers are valuable points of contact for the co-operatives to put their case across on other issues.

The dairy co-operatives are acutely aware of other points of contact with growers even though they may not be co-operatives' employees. The milk tanker drivers are the most important of these, they are usually contractors who have daily or bi-daily contact with a large amount of farmers.

One dairy co-operative I spoke to was very careful to make sure that the truck drivers were not spreading rumours or giving out information. I also heard of one instance where a dairy company involved in a merger instructed its drivers to push the merger.

There is one more area of communication, which was used effectively by one Scottish co-operatives. This was the local media. They employed a communications manager who was formerly a journalist. The interesting element for me was that media was used not only to raise general public perception of the co-operatives but as a tool for communicating with members. Playing on the fact that local media has the perception of independence and that a few well-placed stories are a lot more effective than numerous newsletters. The relationship this co-operative had with the local media had been developed over a long

period of time and involved some hospitality being given. I was there on the day of the public release of the annual report, and that evening the managing director was hosting a party for the local media.

The interest farmers have in their co-operatives is directly related to its importance to their farm business. I used the attendance at A.G.M.s to assess farmer interest; this varied from 50% in marketing and processing co-operatives to .5% at some of the larger requisite co-op's. Where there is little owner interest in the co-operative's activities and performance; farmers have only themselves to blame if this performance falters. I also have found some correlation between those co-operatives who have remained focused on their original purpose and the intensity of their farmer shareholders' gaze.

### **3. Reviewing different structures, principally the difference between corporate and co-operative models.**

I found that, in essence there are two types of co-operatives; firstly, those co-operatives whose farmer's lost control of it would cause long term detriment to the farmers' own business; secondly co-operatives which if they didn't exist it would not adversely affect the farmers own operation.

In the first category, many marketing co-operatives, buying groups and processors that represent the only viable outlet for a farmer's produce definitely fulfil this role.

In the second category your large diversified farm input supplier, who may have been formed to compensate for a lack of competition in the market but who are now just another player.

I think it is important to view co-operatives' from this perspective because it has a bearing on whether the co-operatives, structure is relevant. Another area, which seems to influence whether or not a co-operative considers changing to a corporate structure are the amount of assets involved. Often the access to these assets is the principal motivator for structural change. This push for change does not only come from the co-operatives' members, it also often includes senior management. There were a number of occasions on my scholarship where senior managers sighted the creation of a share option scheme as one of the benefits of a corporate structure.

The selection of a corporate or co-operative structure is in some ways irrelevant for those co-operatives, which over time have moved away from direct relevance to their farmer-members' operation. This is not the case for those co-operatives, which are extensions of farming operations, specifically processing and marketing co-ops. Processing co-ops attract a lot more attention in the debate over structural change because of their more tangible assets. To embark on corporatizing of these co-operatives should be done with care.

Firstly, the correct value of the entity; you can not treat the co-operative as a stand alone business. If you do this you are discounting its value, because of the beneficial interactions that exist between its farmer-members and the co-op apart from bonus distribution. These may include tangible benefits, such as access to cheap

byproducts and intangible benefits like the maintenance of control.

Secondly, control; this is probably the most important loss to the farmer in moving from a co-op structure to a company structure. Many structure changes start with company structures which ostensibly protect farmer control of the organisation, using devices such as having controlling stakes still in the hands of the original co-op. These are illusory because the inclusion of dry shareholders immediately changes the focus of the board. From running an entity, which is intent on maximizing the benefits it can provide to its farmer suppliers to one which is focused on the maximizing the value of the company to all its shareholders.

Thirdly, changes to the co-operative structure which move bonus distribution away from payment related to a farmers throughput to payment related to a farmers shareholding. This is extremely important because it takes the co-operative away from being an extension of the farmers business to just another outside investment. The board of such co-operatives thus have the narrower focus of increasing profit per share against looking at the wider area of how the co-operative can contribute to the maximizing the profit of the farmer-members operation

It seems to me that the inherent conflict between the outside investor's singular focus on profit versus a farmer member's focus on access to a processor who for instance is not going to force down the price of his product to maximize company profit is irreconcilable in the longer term.

This conflict leads to the devaluation of the share value if the board attempts to maintain a co-operative style focus in dealing with its producer members. Essentially what is happening are non-dividend transfers to the wet shareholders. If the company wishes to maximize profit there is the temptation to reduce the cost of its biggest input namely the farmer's produce.

If a co-operative is going to turn to a corporate structure it would be better to do this completely rather than be struck in some half way house. This situation only has the effect of selling cheaply a part of the company to the initial dry shareholders.

An indication of the potential consequences of a transfer to a corporate structure can be seen in the experience of the Irish co-operatives turned P.L.C. company. Some of these companies have progressively reduced the co-operatives original share to the point of a non-controlling stake. These companies have also moved a long way from their original business and have embarked on some quite ambitious investments. Some of these companies are very successful and some are not; the correlation between structural change and the creation of large profitable companies is not obvious. There is a greater correlation between talented senior management and success.

The fashionable trend of changing co-operatives into companies in my opinion discounts too heavily the long term benefits to a farmer's operation of maintaining the co-operative structure versus the often one time cash benefit of the structural change.

#### **4. Introduction of new shareholders to the co-operative.**

How this was done often related to whether or not the co-operatives needed new members or what assets the co-operatives held.

For instance, grain storage co-operatives charged a new member so much a tonne of storage capacity. Interestingly enough this was less than the capital cost of building your own equivalent storage, however if you left, you would not get all your original investment back. Marketing co-operatives were more interested in the level of commitment of new members than any financial contribution.

I was often surprised to find co-operatives with quite large assets relative to their membership being very liberal in new membership requirements. This was often associated with co-operatives, which had no thought of any change to a company structure.

A number of processing co-operatives I visited maintained a percentage of non-member suppliers. This in most cases was to counter cyclic demand patterns for their commodity while guaranteeing an outlet for their members.

The way new members are introduced is extremely diverse across the co-operative sector due to the great diversity of individual co-operatives' situations.

#### **5. Board Development.**

Board development is critical to many co-operatives because a majority of the directors will have operated entirely different businesses to the one they are being asked to control. There are two sides to getting the best possible results from a co-operative board.

Firstly, the selection of the board.

Many of the co-operatives in the U.K actively sought board members, both independent and farmer directors. This was caused by a combination of limited interest among farmers to take on these roles and co-operatives rules, which often gave the board some advantages in bringing forward their candidates. This situation has advantages and disadvantages. The advantages are that a potentially good director who may not have popular appeal can be brought forward. However the disadvantages far out weigh this; firstly the bad board could clone itself. Secondly the entire co-operatives membership may not be fairly represented on the board, Thirdly, if it is apparent that a candidate who has board backing has the inside running. This may stop other candidates from putting their name forward.

I saw two instances of co-operatives having second boards that were used as a breeding ground for future directors. This was used in co-operatives, which had large memberships. It is one of the ways of getting over the problem of getting potential candidates for the board becoming sufficiently well known to win a directorship.

The second important element to board development is director training.

Overall I was quite disappointed with the amount of co-operatives that took director training seriously. One of the reasons given for this was that while the board was made up of farmers, these individuals either were on other boards or had significant non-agricultural interests. This was true in a number of co-operatives that I visited. Some co-operatives that I visited believed they could not justify the expense.

In the face of this apathy, a cheese making co-operative offered a complete contrast. It had a small membership to select its farmer directors from, and I think this is one of the reasons why they took directors training so seriously.

This co-operative's director training was systematic and planned. Firstly, all new directors are taken through the business by department heads and given an explanation on the workings of each department, how they relate to the total business, and the problems the managers have.

The basis for this was the recognition that making and marketing of cheese are not the same business as running a dairy farm. Also, new directors are given instruction on their responsibilities and duties.

There is then an ongoing training for all directors carried out to upgrade skills and it is focused on what an individual director needs.

This training is not intended to create directors who can take over management of the concern; it is to provide the depth of understanding of the business necessary to make sound decisions about its future.

One of the weaknesses of many co-operatives is that invariably they have a board where the majority of its members are involved in the same business and that business's only similarity to the co-operatives business is that it provides the raw material for the process.

While overseas I only saw a minority of co-operatives, which took director's training seriously, each of these co-operatives was invariably the best positioned to meet the future.

A footnote, I saw a number of UK co-operatives with executive directors. I think this is a mistake. One of the principal roles of a co-operatives board is the appointment and dismissal of senior management, having them on the board slows the response time when changes need to be made.

#### **6. Alliances between Co-operatives.**

There are two types of alliances I wish to discuss.

Firstly Co-operatives of Co-operatives

These were co-operatives, which provided a service to their member co-operatives. The most notable was United Farmers in Scotland which organized the buying of the member requisite co-operatives. For me it was interesting because the board was made up of senior managers of the co-operatives not directors. It was successful for the reason that the people who make the day to day decisions were on the board.

There were also groups of marketing co-operatives which operated under the same principal. One I visited was United Pig producers which was the amalgamation of three pig marketing co-operatives covering Southern Scotland and Northern England and selling 30,000 plus pigs per weeks.

The important aspect of these alliances was that they had an economic imperative, which drove them. Many times when I was in the UK I would visit a co-operative beside another co-operative which would have been better together but had not joined because of staff worries about redundancies and directors insecurities.

The second type of alliance was a lot less formal. This occurred where large co-operatives assisted smaller co-operatives through the provision of staff, expert advice and resources. Midland Shire farmers, a large requisite co-operative in the center of England was the classic example. I asked the company secretary why they did this? He said it assisted in their profile, it helped co-operatives who were doing business they themselves could not do due to conflict of interests and provided them with an added a pool of potential directors to access which they could more properly assess.

## **Conclusion**

I started my scholarship with some preconceptions about co-operatives, such as, that a co-operative structure was not the best way to meet the challenges of modern agriculture. This completely changed over the period I was away. In many instances co-operatives offer the most effective and equitable way for a group of farmers to create sufficient market power to face the increasingly competitive and demanding conditions under which they have to operate.

My second preconception was that farmer-dominated boards were not that effective. Again I was proved wrong by many of the co-operatives I visited. All of these co-operatives had a focus on board development.

When I look back at what I thought I knew about co-operatives compared to what I learnt is the proof of the value of a Nuffield Farming Scholarship. This coupled with the many other experiences, which go to make up the period away, have made it one of the most valuable times of my life.



**THE AUSTRALIAN NUFFIELD FARMING SCHOLARS ASSOCIATION**

ACKNOWLEDGES WITH THANKS THE RECENT SUPPORT OF THE  
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