

AGRICULTURAL PRODUCER COOPERATIVES

“A DISCUSSION PAPER”

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EXECUTIVE SUMMARY

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“A DISCUSSION PAPER”

“Mutual benefit over self interest equals the survival of values” (Livingstone, 1998).

The purpose of this discussion paper is to review the role of Cooperatives in the development of Canadian and Newfoundland and Labrador Agriculture. It presents a range of cooperative structures that currently exist in Canada and considers how each can be adopted by producers in this province. The value of Agricultural Cooperatives is then discussed in relation to operating margins at the farm level. Critical success factors are identified that will ultimately determine the success of a Marketing Cooperative and include 1) creating a “pull” on product through the cooperative, 2) linking operating efficiency with market demands and 3) adopting an aggressive market orientation. Appendix B outlines a critical path for setting up a successful cooperative.

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INTRODUCTION

Agricultural Producer Cooperatives were initially adopted in Canada during the late 1900's as a means to protect farmers against financial loss brought about by fire. Since then the Cooperative has become a major economic driver within the Canadian Agriculture Sector with a membership base of some 654,047 producers in 1999 (McCagg, 2001). The combined business volume of Agricultural based Cooperatives in 1999 was estimated at \$19.0 billion with some \$7.3 billion in total assets. These organizations have become major players among farm supply dealers, marketing agencies and processing companies, dominating market share in three major commodities, Dairy, Grain/Oilseeds and Poultry at 66%, 49% and 48% of the market respectively (McCagg, 2001).

In 1999 the Cooperative Secretariate for Canada reported that there were 2 Supply Cooperatives and 3 Marketing Cooperatives based in Newfoundland and Labrador. The combined business volume of these Cooperatives was reported at \$5.7 million with total assets valued at \$3.9 million. These cooperatives were, and still are, heavily dependant on processing and marketing supply managed commodities, milk and poultry meat. Recently, however, there has been a growing interest in the cooperative model among the Fruit / Vegetable and Livestock sectors.

Producers within the non-supply managed agricultural sectors are advised that a cooperative's structure and function, like any business structure, must be aligned to fulfill the common goals of its members and add value to the farm. It is recommended that producers become more informed in the structures of cooperatives, their flexibility and their functions before making a decision to commit to adopting a specific model. To be successful the needs of the producer must be clearly defined and the structure of the cooperative must be designed to meet these producer expectations.

BACKGROUND

During the late 19th and 20th centuries the number of commodity buyers in the Canadian market place declined as food industries across North America experienced a period of rapid consolidation. By the mid 1900's marketing opportunities for most farmers became focussed on a few large buyers that together monopolized trading areas throughout the country. These powerful companies usually sought out lower prices in the market and created a downward pressure on commodity prices. Farmers negotiating prices independently had little option but to accept these lower prices, which over time resulted in a decrease in the value of primary agriculture.

As a result of the downward pressure on commodity prices farmers realized that the only way to gain negotiating power in the market was to work together and form producer cooperatives. These cooperatives took on many forms and varied greatly in their strategies. For example, farmers could form marketing cooperatives to gain negotiating power for higher commodity prices or attempt to lower cost of production through joint purchasing of input supplies. Additionally, farmers could opt to invest in processing their own commodities and move further up the value chain to compete with the larger processors for niche markets.

The underlying thread resulting in the evolution of these types of cooperatives was the struggle to regain power in the market place and raise the value of primary agriculture. Through collective action agricultural producers sought to win back negotiating power that it had lost to the large conglomerates. As a result many cooperatives have evolved to play fundamental roles in the development and sustainability of primary agriculture in Canada. They have become an important part of the agriculture landscape in every region of the country and will likely continue to do so well in to the 21st century.

AGRICULTURAL PRODUCER COOPERATIVES

There can be many variations to the agricultural producers cooperative model each playing a critical function in fulfilling its members' needs. Supply cooperatives, for example, make various products available to its members while marketing cooperatives act as a marketing body for farmers to sell their products. Some cooperatives combine both these activities while others provide additional services such as custom harvesting of crops. The cooperative structure and its function is limited only by the needs of its members and the commonality of their goals. Some basic types of agricultural producer's cooperatives, and their functions as they relate to Newfoundland and Labrador primary producers, are outlined in the following discussion.

Supply Cooperatives

Farm supply cooperatives have been an important part of agriculture development in Newfoundland and Labrador since the mid 1900's. For example, the Eastern Farmers Cooperative was established to supply the essential farm operating items such as feed and fertilizer to farmers on the Avalon Peninsula. The principle of this cooperative was that joint purchasing could create economies of scale that could be used to gain bargaining power for lowering prices, which could then be passed on to its patrons, the farmers. Lowering the cost of production provided local farmers with the means to supply their products at a competitive price to the market place.

Other supply cooperatives expanded this model to include the processing of raw materials in to usable forms. They saw an opportunity to gain additional cost savings through secondary processing and moving further up the supply chain. For example, the Feed Mill located in Stephenville was first established as a partnership / supply cooperative to provide a reliable and cost effective source of fresh milled grains to local livestock producers. By performing the milling and mixing of imported

whole feed grains they not only lowered their cost of production but also gained control of the steps in the supply chain that were critical to the success of their operation, for reliable/on-time delivery and quality control.

Production cooperatives

Cooperative Pastures

There are no Production Cooperatives operating in Newfoundland and Labrador however variations to this type of cooperative structure do exist among some producer groups. For example, since the privatization of community pastures beef and sheep producers have organized into Production groups and adopted some cooperative principles. Ownership of the pastures now range from individual producer groups to Regional Economic Development Boards. Farmers wishing to graze their livestock on these pastures pay an annual fee or levy per head of livestock to help cover the maintenance and general upkeep of the pasture. Generally, anyone can utilize these pastures as long as they pay the grazing fees as set down by the controlling board members. The pasture livestock capacity and rotational schedules are determined by the pasture management.

Farm Machinery Cooperatives

Farm Machinery Cooperatives, unlike Cooperative Pastures, are not as common in Newfoundland and Labrador however they can provide farmers with some important benefits. Among this type of cooperative Joint Farm Machinery, Custom Operations, Equipment Rentals and New Technology Adoption Cooperatives provide good opportunities for farmers. Farmers can generate savings by leveraging the capital cost of specialized equipment such as harvesters and chemical sprayers. For example, a production cooperative may purchase a pesticide sprayer, and pay an operator on a fee-for-service basis to conduct all the spraying activities of the cooperative members.

When farm machinery expenses and custom work and machinery rental expenses were compared between Nova Scotia and Newfoundland and Labrador fruit and vegetable farms for 1996, some significant differences were revealed. In particular, farm machinery expenses was among the most significant expense for the farms operating in Newfoundland and Labrador, representing some 17% of the total cost of production. Alternatively, these expenses represented just 11% on similar farms in Nova Scotia. Furthermore, Nova Scotia producers tended to take full advantage of custom work and machinery rentals, which accounted for some 10% of production costs, an expense that represented only 3% of production costs in this province (Appendix A).

With few farm equipment dealers in Newfoundland and Labrador access to custom work and equipment rentals is quite limited. However, it is very likely that the significance of this operating expense may be a key contributor to the higher operating margins (refer to Net Value Added Section) among fruit and vegetable producers in Nova Scotia. In 1996, the operating margin for these farms was 20.5%, while the operating margin for similar farms in Newfoundland and Labrador was just 10.8%.

This type of cooperative farming can have many benefits for supply managed and non-supply managed producers alike. Savings can be realized through shared equipment purchases and lower production costs associated with labour and equipment repairs. Funding programs for new technologies are generally more generous to cooperatives rather than individual farm owners. In this way the capital burden of each member can be reduced further while reducing the risk from individual farm operations wishing to assess new technologies.

New Technologies

Farm Machinery Cooperatives leverage their financial risk among its members so that everyone can either benefit from a good investment or buffer the adverse financial impacts of a poor one. In recent years the Department of Natural Resources has encouraged the cooperative use of new technologies under such programs as the Alternative Feed Program and Cranberry Production Program. The cooperative purchase, maintenance and operation of harvest equipment for Small Feed Grains and Corn Silage, for example, has allowed ruminant livestock farmers to adopt new technologies that may otherwise appear as too risky to try.

The seeding and harvesting equipment acquired for the purposes of research and development can be utilized by a group of partnering farms. This cooperative model is very useful to farmers interested in experimenting with new technologies. For example, a group of vegetable producers could rent or lease a new potato harvester that is suitable for use under stony soil conditions. If the technology is suitable it can be adopted by the industry and potentially have a significant impact to improve the production operations, lowering harvest costs and improving the competitiveness of the industry.

Service Cooperatives

Service cooperatives can also play a significant role in the growth of the agriculture industry. These cooperatives provide services for farms such as seed cleaning and direct marketing, a natural extension to the production cooperative. For example, custom harvesting and handling of vegetables from the field could be done by a farm machinery cooperative, which then delivers the product to a cleaning and sorting facility. Or, slaughtering and packaging services can be provided for animals that were grazed on the cooperatively owned and operated pastures. In this way members can be part of a number of different cooperatives each providing some

benefit to the operation and contributing to the well being and sustainable growth of the industry and rural communities.

Direct Marketing Cooperatives

In recent years many of the newly established producer cooperatives in the fruit and vegetable industry have shown a great deal of interest in direct marketing. This type of cooperative provides market venues in both urban and rural settings to help members sell their products direct to the customer and get the maximum value for their products. During a time of mass consolidation of the retail chains many small farms and those new to the industry are finding fewer opportunities to sell their products through established distribution channels. Consequently, direct marketing is emerging as a viable alternative strategy for marketing local products.

There are many opportunities for farmers direct marketing in Newfoundland and Labrador. For example, the Churchill Square Farmers' Market in St. John's has been in operation for many years selling a variety of products from Cauliflower to Green Peas. There are at least two cooperative farm markets and some 50 independent farm markets operating in both rural and urban settings throughout the province. Studies conducted in both Nova Scotia and Ontario confirm that markets that strive to improve consumer experiences and supply local freshly harvested products will generate a loyal consumer clientele.

Although consumers prefer to purchase local products because of the superior taste and freshness, it is not enough, in itself, to generate loyalty at a Farm Market. One of the most significant challenges to local producers is to satisfy consumer demands for a wide variety of produce to choose from. This means that a market venue created to sell local produce must go beyond the traditional crops such as potatoes, turnips, cabbage, carrots and beets. Farmers must work cooperatively to provide the market with such non-traditional crops as broccoli, cauliflower, onions, tomatoes,

sweet corn, lettuce, and a variety of fruits. These cooperatively run direct marketing venues should also strive to sell other local items such as fresh meats, fresh fish, eggs and some local crafts to reinforce consumer loyalty.

Marketing Cooperatives

Marketing cooperatives provide its members with a wide variety of activities that range from processing to distribution. Belhadji, et al (2000) stated that agricultural marketing cooperatives accounted for more than 82% of the volume of business in Canadian agricultural cooperatives in 1996. These cooperatives are generally large state of the art organizations that play a key role in the sustainability of many agricultural industries such as the Dairy and Poultry industries. Nonetheless, opportunities exist for other commodity groups to benefit from this cooperative model. One such industry that has shown a great deal of interest in adopting this cooperative model in recent years is the vegetable industry.

Traditionally, Newfoundland and Labrador vegetable producers have been able to supply the market with Turnip and Cabbage from August to February. But, with improved storage systems these vegetables can now be stored later in to the Spring and Summer. This provides producers with an opportunity to expand their marketing season and grow their operations. However, investing in farm growth is a critical matter for most farms as it is incremental in nature. And, unless efficiencies are realized quickly profitability may deteriorate and the business could become insolvent. Therefore, for larger farming operations, investing in growth at the farm level is a critical process.

Some of the barriers to real growth at the farm level have been identified during the 1999 Newfoundland and Labrador Vegetable Industry Round Table Sessions in Gander. They included the following:

1. Land Base Development (Clearing & Draining)
2. Land Productivity (Limited technology adoption and research & development to lower cost of production)
3. A clearly identifiable market orientation and promotion (Branding)
4. On-Farm Infrastructure (Improved Storage and Handling Capacity)
5. Industry Communication (Consumer Demands should be communicated back to the producer)
6. Diversification (Traditional and Non-Traditional Crops)

The financial resources and production risks associated with overcoming these barriers, generally, is beyond the scope of the individual farmer operating in this province. However, agricultural producer cooperatives can help address most of them. By working together farmers can leverage their financial and production risks to invest in new technologies and storage infrastructures. They can combine and critically assess market intelligence information to create an identifiable product in the market or expand in to new products. These opportunities, however attractive in principle, come with the harsh reality that farmers must accept a new operating philosophy and become more market oriented managers.

Retailers are highly integrated within the value chain and demand that suppliers of local produce, standardize packaging and product quality. This means that vegetables have to be packaged and graded based on standards agreed upon by both the producers and the buyer. Consistency and reliability of supply is a requirement of most retailers, suggesting that an open exchange of production and purchasing information must be fostered between buyer and producer. Using this information producers can plan in advance for the next growing season while retailers can be assured of a consistent supply of high quality produce that the consumer is looking for.

Buy/Sell Cooperatives

There are two main types of systems that Marketing Cooperatives operate under. The first is the Buy/Sell system and the second is the Pool system. The Buy/Sell system works much like many non-cooperatives where the producer is paid on delivery of the product to the grading, sorting and packaging facility. After the cooperative resells all the product any profits are divided among the members based on the amount of business they have conducted with the cooperative. The buy/sell system tracks each load of produce through the cooperative and the final adjustment payment reflects the price received for each order. Therefore the farmer can expect a different price for each load of product delivered to the cooperative.

This cooperative model may benefit farmers that do not wish to give up traditional markets but have the flexibility to expand markets by selling through the cooperative. However, this model does not provide the cooperative with any control over the amount of product that will be moved through its facility. The marketing flexibility is lost and decision making, on the part of the cooperative, is difficult as the cooperative manager does not know how much product will be available from one year to the next. Therefore this cooperative can not respond with any assurance to buyers in the market place.

Production contracts can greatly improve the buy/sell cooperative model as fixed volumes, or forward cash contracts can be issued to the producers for future delivery of the product. These contracts usually specify the type of product, the amount and often the price the cooperative will pay. Producers can enter into these contracts and plan future production based on the revenue they will require to meet their financial goals. The cooperative can better plan a marketing strategy knowing how much product will be available, as the contract obligates the producer to sell the amount of the contract to the cooperative.

Pool cooperative

In the “Pool” type of cooperative members pool their products to be sold through the cooperative. It does not necessarily mean that all the product is physically mixed in the facility but rather that the price received for the product is “pooled” by the cooperative. All marketing decisions are made by the pool manager and after deducting pool proceeds, the average net price is paid to its members. Depending on the management some pools pay an adjustment for quality while others for transportation. The pool model is a way for producers to spread their expenses among all the members of the cooperative, as well as manage revenue risk.

A producer will usually receive an advanced payment for the produce upon delivery. After the initial expenses are taken into account, progress payments are made on the product. Once all the marketing is complete a final equalization payment is paid, which reflects the remaining proceeds of the pool and any differences in quality of product delivered by individual members of the pool. In this way the average price for the product is delivered to the producers.

The producers in the pool cooperative model share revenue risk among all the members of the cooperative. In the end all producers receive the same price for their products, with adjustments made for quality of product delivered to the pool. This type of cooperative is more effective than the Buy/Sell cooperative (operating without forward contracts) as it has a known volume and quality of product that it must market and therefore can experience some degree of market power.

Marketing Agencies-in-Common (MAC's)

Marketing Agencies-in-Common is a strategic alliance among cooperatives to gain economies of size for marketing like or complementary commodities. These MAC's, as they are referred to, share large costs such as the cost of branding products, especially the high cost of promotions such as television advertisements. Usually member cooperatives maintain operating independence in their various trading areas but produce their products under a common brand name and logo. This type of cooperative can be very effective in creating awareness of products and negotiating promotional activities with large buyers / retailers.

In the fruit and vegetable industry this type of agency can be easily initiated once a critical number of cooperatives have been created. Each member cooperative can identify a trading area to limit the amount of competition between individual cooperatives. Relationships between member cooperatives can then be fostered to help supply product to cooperatives in trading areas that do not have the supply to satisfy demand. An agency such as this one can help local fruit and vegetable producers coordinate the production and movement of produce from one region to the other, and capture significant negotiating power within the market.

New Generation Cooperatives

New Generation Cooperative (NGC) is a term being used more frequently in agriculture. NGC's are very similar to traditional cooperatives in that they maintain democracy through a one member, one vote policy and a board of directors is elected from the membership, to make decisions. What makes NGC's different from other Cooperatives is that instead of simply being a clearinghouse for members' products, the cooperative is invested in "value-added" activity. Farmers participating in the NGC's perceive an opportunity to create value for their businesses.

New Generation Cooperatives also have a fixed or restricted membership. A feasibility study is conducted to determine the amount of produce that can be processed through the processing facility. After this maximum efficiency is determined, membership is decided based on the amount of product that can be accepted. Members purchase delivery rights in the form of shares. Each share represents a two-way contract where the producer guarantees they will deliver a set amount of product and the cooperative agrees to accept that amount for a predetermined price. Quality standards and delivery times are also regulated in the share agreement (Haaf and Stefanson, 2001). These quality standards are very important because often the cooperatives are serving smaller, niche markets that require higher quality products.

The cooperatives own the processing plants they use, ensuring that the profits created from the plant is distributed back to its members. Also, because the cooperative is supported by the equity that members purchased up front, most of the earnings generated are returned to the farmers at the end of the year (Saskatchewan Industry and Resources, 2001). In general, NGC's require a larger investment of cash from each producer to purchase or build the processing facilities.

New Generation Cooperatives are becoming more important to primary producers because of recent changes in Market demands. As in the rest of Canada Newfoundland and Labrador consumers are becoming more discriminating in their food purchase decision. The New Generation Cooperatives are emerging to capitalize on this market trend to capture more value at the farm level. In addition to increased revenue, these cooperatives can generate additional value as the value of their shares or value of each delivery contract rises over time. Farmers retaining these shares have the option to use them as leverage to finance future growth or sell them to other qualified producers and capture its value.

NET VALUE ADDED

According to Statistics Canada the term value added is referred to as the value of product shipments (production) less the cost of materials and supplies, fuel and electricity purchased and used. This Value Added, adjusted for wage and interest expenses, is otherwise referred to as the Operating Margin of the business. The operating margin is one of the most common indicators of profitability of a business and measures the efficient use of capital, labour and management. Using this margin allows for comparisons of profitability and efficiency among cooperatives involved in different areas of the agriculture sector and between cooperatives and non-cooperatives within the agriculture sector as a whole.

In Canada fruit and vegetable cooperatives control a relatively small portion of the market at just 13% of sales. According to the results of a cooperative study conducted by Belhadji et al (2000) the average operating margins for 1986, 1991 and 1996 of these fruit and vegetable cooperatives was approximately 6 - 7% or 6 - 7 cents per dollar of sales. Compared to other Canadian cooperatives only Poultry and Egg cooperatives had higher margins due primarily to the higher degree of value added processing in those industries. Canada fruit and vegetable cooperative primarily provide cleaning, sorting and packaging services to their members.

In order to fully understand the cooperative process it is important to be familiar with the term “marketing levy”. Marketing cooperatives operate on a cost of goods sold margin, which basically means that the Cooperative purchases products from the producer member and subtracts a marketing levy of approximately 30% off the resale value. In other words, if farmers sell to the cooperative at the same price they are currently selling to retailers they will be charged a 30% levy (or tax) on the product to cover the marketing activities at the cooperative such as sorting, grading, packaging and distribution.

The second consideration that must be understood is that although farmers are lowering the net operating income on their farm by selling to the cooperative, their “adjustment payments” or “dividends” should be enough to add value to their operation. For example, an average producer generating \$57,698.00 in revenue selling vegetables directly to the retailer can expect an operating margin of 11% or \$6,346.76. However if the same farmer sold produce through the cooperative the revenue generated would be \$40,388.60 (\$57,698.00 less 30%). Suppose then, that when all the savings from the marketing activities (sorting, grading, packaging and distribution) were added up and all the operating expenses from the farm were paid, the farmer’s operating margin was cut in half. This would leave the farmer with only \$3,173.39 of net operating income ($\$6,346.76 \times 0.5$) by selling directly to the cooperative. However, at the end of the year the Marketing Cooperative realizing an operating margin of 6 - 7%, paid its’ members a dividends of \$3,750.37 (6.5% of \$57,698.00). As a result of doing business with the cooperative the farmer would have realized a total of \$6,923.76 income, or an added value of some \$577.00 or 9% to his operations. In economic terms, this is referred to as the “Net Value Added” to the Farm Operation.

This assessment provides some insight on how Agricultural Producer Cooperatives can add value to a farm operation. It is meant as a general discussion of the impact on operating margins based on industry averages generated from Statistics Canada. The reader is cautioned that a real life scenario can prove to be more or less profitable depending on the success of the Cooperative organization.

CRITICAL SUCCESS FACTORS

Although Agricultural Producer Cooperatives have not played a significant role among primary producers in Newfoundland and Labrador some potential rewards can be realized from adopting this organizational model, as discussed above. These rewards however are dependant on the ability of the Cooperative management to identify and capitalize on the operating factors that are critical to success. The following discussion attempts to describe the “critical success factors” as they relate to Agricultural Marketing Cooperative operating in Newfoundland and Labrador.

Marketing Management

The first, and most important critical success factor for an Agricultural Cooperative operating in Newfoundland and Labrador, is its ability to create a “Pull” on commodities for its members. The “Pull” on commodities can be generated most effectively through forward contract or production contract negotiations with buyers/retailers. Most fruit and vegetable farms operating in Newfoundland and Labrador conduct their business based on the “Push” principle, which refers to the practice of a farmer growing the amount of vegetables that s/he feels can be marketed during the following marketing season. The operator does not determine before hand how much s/he can sell or whether the revenue generated from these sales will be enough to satisfy his/her financial goals.

Alternatively to create a “Pull” through an Agricultural Cooperative farmers must empower the cooperative marketing manager to negotiate production and price contracts with retailers / buyers on behalf of the cooperative members well before the harvest season. These early contract negotiations are critical to the operations of the cooperative as they identify 1) the size, 2) amount, 3) delivery date/time, 4) quality specifications and 5) possible agreed upon price for the product. This

information is then relayed back to the individual member producers, which can plan their production schedules for the next growing season.

The support of the member producers is also critical as the marketing manager can negotiate prices more effectively if s/he has a large quantity of produce and can ensure the buyer that they can supply their needs. By working together as a cooperative, farmers can gain negotiating power with retailers and pass on packaging and quality expectations to its members. If the cooperative manager can reassure the buyer of a consistent quality of product and a sufficient supply forward contracts or production contracts can often be drafted. By conducting these early contract negotiations individual farmers can then plan their planting season and base their production on satisfying their financial needs.

If forward contracting can not be done it is the job of the marketing manager to communicate to its members an estimated sale volume for the following year. The manager will have to actively solicit buyers to purchase the cooperative's products and gain commitment from them. This may involve clarifying product specifications with the buyer, relaying these specifications back to the cooperative members and delivering on them. It may take a number of years to build confidence in the cooperatives ability to deliver these products with consistent quality but, nonetheless, this is considered one of the critical components to a successful marketing cooperative.

Operations Management

Quality specifications and sales forecasts may be critical for managing markets but it is also critical in managing operations. The operations manager of the cooperative must prepare production schedules for the facility based on sales forecast and quality specifications. If the marketing manager can negotiated and forecast sales a year in advance, not only can farmers plan their planting schedules but the

operations manager can schedule sorting and packaging operations and hire the right number of workers to man the plant.

One of the most important management jobs at the cooperative is to create an environment where the facility is working as efficiently as possible to minimize unnecessary costs. By utilizing forward contracts, and forecasting sales the operations manager can effectively plan operations to minimize labour costs. For example, if the manager knows that 10 contracts are required to be filled each week from August to December and that it takes say 12 man hours to prepare one contract (including setup time) then the right number of workers can be hired to prepare these contracts. In this example the facility will only require 3 labourers to prepare the contracts for each week (120 hours / 40 hours per week = 3 labourers).

If the contracts are to be delivered each Tuesday then it is important that the cooperative have at least one day lee-time in case they run in to some operating difficulties. With this system the operations manager can prepare the contracts a week in advance of the delivery date and hold the contracts in inventory for a few days before delivery, while the labourers are preparing the next weeks orders. Forward contracts create efficiency in the cooperative as operations are pro-active rather than responsive to orders. The operations manager can hire the right number of labourers to “fit” the amount of work required and prevent unnecessary expenses.

Inventory management is also a critical factor that must be considered by the operations management. As the produce enters the facility it must be identified and tracked through the sorting and packaging processes. This will not only help the operations manager to deal effectively with product complaints, the manager can also provide rewards to producers for supplying high quality products to the Cooperative. Inventory management should also account for variability in buyer orders. If forward contracts are not negotiated with some buyers their requirements may change from week to week. Effective inventory management will maintain

extra inventory in-stock to deal with these variations rather than change the weekly throughput from the facility.

Key to success in operations management is having a clear understanding of what the market is demanding and what the expectations are of the Cooperative members. Balancing this information is normally done through trial and error but will help the operations manager to prioritize activities and identify what tradeoffs are acceptable in reaching the members' goals. The priorities, that may be affected from tradeoffs between operations management and market uncertainty, need to be clearly understood by the producer/owners. These tradeoffs must be communicated up front by the manager, and can take the form of the following: 1) Costs, 2) Product Quality, 3) Delivery Speed and Reliability, 4) Ability to Cope with Changes in Demand (buyer orders) and 5) Flexibility of Operations.

Cost Reduction is always an important part of agriculture in Newfoundland and Labrador as local producers have little control over commodity prices. Commodity prices here are generally set by producers that have a comparative advantage in the market place. For Newfoundland and Labrador this means that prices for Fruit and Vegetables are generally set by Maritime suppliers as they have a lower cost of production. Thus cost reduction will always be a critical role for the operations manager dealing with commodities.

Product Quality is also a critical issue as the goal of the cooperative is to produce uniform products with consistent quality. These are considered winning attributes among many buyers in the market place. If the cooperative can ensure that buyers receive a product with consistent quality than they are more likely to want to do business. The operations manager must be conscious of quality specifications at all times and continually be measuring these product attributes.

On-time delivery and reliability is an important components of today's highly integrated distribution channels. Most warehouses are attempting to reduce the holding time of produce and operate under three simple rules... 1) keep it clean, 2) keep it cool and 3) keep it moving! These warehouses demand to know when the product will arrive so they can prepare for it in advance and keep it moving through the distribution chain. Working together with these warehouses to coordinate activities will forge good working relationships and build strong relationships. The products will spend the minimal amount of time in the distribution chain and will retain its freshness, which is a very highly desirable attribute among consumers.

Coping with the changing demands in the market place and operations flexibility are two closely related critical points for most Marketing Cooperatives. Today's operations managers are continually adopting to changing consumer tastes, even within the commodity markets. For example traditional produce, such as Turnip and Cabbage, are being substituted for other non-traditional crops such as Broccoli and Green Beans. This is a direct result of changing demographics and an emphasis away from the traditional recipes and toward more convenience meals such as Stir Fry and Salads.

These non-traditional crops require new growing techniques but have a higher value in the marketplace. The flexibility of the Marketing Cooperative to satisfy these changes in demand will greatly improve if the members are encouraged to begin producing these crops early in the product life cycle. This will improve the Cooperatives marketing appeal to buyers and retain the production expertise necessary to quickly increase production if the market so demands.

Operating Philosophy

The operating philosophy is also considered here as a critical factor for success in Marketing Cooperatives. The philosophy that must be adopted by all members is “Market Orientation Management”. Close attention must be given to the needs of the buyers/retailers to foster good working relationships. The information flow must be effective and efficient. Most primary producers within the fruit and vegetable industry have spent a life time building up a good working relationship with retailers and it will require a considerable leap of faith to let the cooperative manager conduct negotiations on their behalf. This is one of the critical factors affecting the success of the cooperative and requires a significant change in the philosophy on the part of the producer members.

This change in operating philosophy from personal negotiations to letting a third party negotiate on their behalf will not happen over night, however, once the benefits of this change in operating philosophy has been seen, changes will occur. To a large degree the success of the cooperative will depend on the empowerment of the management team to negotiate production contracts and encourage member patronage. The critical first years of operations will likely be marked with difficulty as farmers will have to accept that the cooperative has become the primary communications medium with the market.

Alternatively, the first years of operation will also find a reluctance on the part of the buyer to deal with the Cooperative, as they do not have a reliable track record to fall back on. Today, most retailers are comfortable dealing with a small number of producers that can supply them with a consistent quality and volume of produce. However, many buyers have indicated that they would prefer to deal with a marketing organization that represents a large number of producers. This is why patience and endurance is necessary to allow time for the market to adjust to the Cooperatives’ presence. The cooperative manager will have to communicate

effectively with the retailers, providing samples of each members produce to show that they are of consistent quality.

To gain consistency of quality the cooperative manager must also be empowered to provide producers with quality control specifications. If the sorting and packaging operations is conducted at a cooperative facility the manager can control quality. However, if packaging is conducted on individual farms then there will be limited control on quality by the cooperative management. In this case, quality specifications must be inspected on a regular basis and control over membership screening must be strictly adhered to. Each applicant must demonstrate a genuine concern over quality control. This empowerment of the cooperative management is also critical to the success of the cooperative as it will ensure retailers a consistent quality of product to the store. It is also one of the most difficult factors to overcome among producer members.

CONCLUSION

Cooperatives have become very important to the Agriculture Sector in Canada. They have established a strong presence among farm supply and marketing and processing industries generating a combined business value of over \$19.0 billion. They are the dominant players among Dairy, Grain/Oilseed and Poultry commodities and represent some 654,047 producers. Although Newfoundland and Labrador based Cooperatives play a small role in the agriculture sector they are nonetheless growing in importance as primary producers attempt to maintain a competitive position in a continually changing marketplace. Given the present level of adoption of this organizational structure it is likely that Cooperatives will become an increasingly important part of the agriculture landscape in this province.

The structure and function of Agricultural Cooperatives must be aligned to the common goals of its members otherwise it is likely to fail. Therefore, it is important to have a clear understanding of the various options available to primary producers considering a joint investment in the Cooperative Model. There are numerous opportunities for locally based Cooperatives within the Fruit and Vegetable and Livestock industries however a principle factor influencing the success of marketing cooperatives is creating a “pull” on product through the cooperative, linking operating efficiency with market demands and adopting an aggressive market orientation.

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APPENDIX A. A Comparison of Fruit & Vegetable Production Costs, as a percentage of total production costs, for Newfoundland and Labrador and Nova Scotia Farms

| | Newfoundland & Labrador % of Total Costs | Nova Scotia % of Total Costs |
|---|--|---------------------------------|
| <i>Total Operating Revenues</i> | \$57,698 | \$108,925 |
| Expense Item | | |
| Fertilizer & Lime | 13 | 6 |
| Pesticides | 3 | 8 |
| Seed & Plants | 4 | 3 |
| Other Crop Expenses | 4 | 6 |
| Total Crop Expenses | 24 | 23 |
| Small Tool | 1 | <1 |
| Net Fuel Expenses, Machinery, Truck, Auto | 7 | 4 |
| Repairs, Licenses & Insurance | 9 | 6 |
| Total Machinery Expenses | 17 | 11 |
| Salaries | 39 | 33 |
| Rent | 1 | 3 |
| Insurance | 1 | 2 |
| Utilities | 3 | 3 |
| Custom Work & Machine Rental | 3 | 10 |
| Net Interest Expenses | 4 | 6 |
| Net Property Tax | <1 | <1 |
| Building & Fence Repairs | 1 | 1 |
| Miscellaneous | 7 | 7 |
| Total General Expenses | 59 | 65 |
| | 100% | 99% |
| Total Operating Expenses | \$51,462.00 | \$86,581.00 |

*Statistics Canada, 1999.

APPENDIX B. Steps to Starting A Cooperative

Many individuals want to start up a cooperative to address a particular problem within their industry. Once a need is identified, there is a great deal of work that must go into putting the idea into action. The following is a list of steps, adapted from several sources, that outline the process a cooperative can take when starting up. It is recommended that the Newfoundland and Labrador Federation of Cooperatives (www.nlfc.nf.ca) be contacted as an initial step. In addition, the regional Economic Development Officer with the Department of Innovation, Trade and Rural Development can also provide some assistance in the initial stages of starting up a producer's cooperative.

Phase 1: Developing the cooperative business idea

Step 1: Identify the need and assemble a group of interested individuals

Suggesting the cooperative model as a solution to a business problem is only the first step of many. Assembling a solid group of people who want to take action is essential for initial success. Getting the cooperative off the ground involves a great deal of work and this will require committed people with clearly identified goals. An organizing committee must be established and a lawyer, accountant, economic development officer, or financial consultant should be consulted. The organizing committee will also play an essential role in recruiting new members.

Step 2: Conduct a feasibility study

Starting a cooperative may be an excellent idea in theory, but a feasibility study will let interested parties know if it is a viable business option before too much time and money is invested. A study can also identify potential problems that the members can work to correct. It should identify market potential, growth potential, a proper business structure to use and the minimum required number of members for

success. The report should also outline the benefits for potential members such as the price for products, easier access to markets, and discounted costs for farm supplies. Once the feasibility study is complete, the organizing committee will decide whether to proceed.

Phase 2: Coordinating the pre-cooperative activities

Step 3: Hold an organizing meeting

If the feasibility study suggests that the business idea is practical, then the next step is to attract interested parties and set some clear goals for the cooperative. The members will decide the company name, mission and objectives. A temporary board of directors should be selected at this point, which will then become responsible for many of the organizing activities. Members may be asked at this point to invest some money to help finance the rest of the planning process. An application for incorporation should also be submitted to the appropriate agencies.

Step 4: Conduct a viability study

The viability study is similar to the feasibility study, although it will focus primarily on the internal workings of the cooperative. The study should include a projected budget and cash flow. It will also need to evaluate the possible start-up financing options and the human and material resources necessary. The study should answer the question: what are the strategic objectives of the business. A thorough viability study will be useful in preparing the business plan.

Step 5: Prepare a business plan

Preparation of the cooperative's business plan is essential. This will provide a complete description of the cooperative's financial projections, marketing opportunities and all other relevant information. The plan should answer several questions for potential investors and members such as why they should invest in the

proposed business, the seriousness of the business, and the team's ability to launch and develop it successfully. The business plan will be the most important selling tool when trying to attract members. It will also serve as the means by which members of the cooperative evaluate its performance and follow-up on its plans. (coop sect 13)

Step 6: Organize the association

This step involves deciding the structure of the cooperative based on the needs of the members and the objectives of the cooperative. After deciding the structure, the board of directors must be elected and their roles and responsibilities clearly outlined. The bylaws and articles should be established during this time.

Step 7: Organize the enterprise

The board of directors should first decide on the structure of the business. Then the board must develop a one year operational plan, develop an accounting system and design a salary policy. At this point the roles and responsibilities of the staff should be addressed and an Chief Executive Officer must be hired to help with much of the remaining tasks.

The cooperative can now begin to generate the start-up capital. Using the information from the business plan, the board of directors and the CEO can negotiate capital funding from several sources including financial institutions, venture capital corporations and private investments. The cooperative should decide whether it will issue preferred shares to the public and draft appropriate bylaws or target government funding programs. The Cooperative will need to secure medium term loans and a line of credit.

After the financial arrangements have been made, it is time to hire the staff. This will primarily be the responsibility of the chief executive officer. At this point cooperatives should provide education and training for their members, elected

representatives, managers, and employees so that they can contribute more effectively to the cooperatives growth and development.(ICA) This is also a good time to ensure all legal matters are in order including tax and employee numbers, required permits, licences and that incorporation papers are filed.

Step 8: Hold the first annual general meeting

After all the planning and preparation is completed, the cooperative must hold its first annual general meeting. At this meeting the members will adopt the bylaws prepared by the organizing committee. The members will also adopt the business plan, appoint an external auditor and elect the board of directors. After this, the cooperative can begin operations.

These steps are presented as a general guideline to follow when starting a cooperative. Some common organizing pitfalls that should be avoided include a lack of a clearly identified mission, inadequate planning, and failure to use advisors and consultants. (ngc2) Without a clear mission, the coop will never fully realize its potential and will not produce substantial profits for its members.

APPENDIX C. Coop Associations

Newfoundland and Labrador Federation of Cooperatives

www.nlfc.nf.ca

The Canadian Co-operative Association (CCA)

www.coopscanada.coop

Atlantic Co-operator (The)

<http://www.theatlanticco-operator.coop/>

Co-operative Development Foundation of Canada

www.cdfcanada.coop

The International Co-operative Alliance (ICA)

<http://www.ica.coop/ica/ica/ica-intro.html>