Co-operatives: Successful Business Models and Investment Structures

Factors of Success and External Investment

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Executive Summary

This report analyses the traditional cooperative business model in order to understand factors critical to its success and failure. An emphasis is placed on why the model is traditionally seen as unable to attract financing from external sources, often dubbed the "Achilles heel" of cooperative businesses. By synthesising the existing literature and dissecting two successful cooperative case studies, Kibinge and Manduvira in Uganda and Paraguay respectively, the authors find a specific number of aspects that appear crucial to both economic and financial success.

Firstly, the appropriate business model and structure are imperative for allowing cooperative organisations to garner investment. Cooperative principles dictate that (1) active members can only provide cooperative with voting capital, limiting the pool of investment capital, (2) residual claims of cooperative cash flow lack alienability and transferability thus preventing the formation of a cooperative capital market, (3) the property allocation in cooperatives encourages under-investment, fuelling the classic free-rider problem, and (4) cooperative equity capital is not permanent making it a risky foundation for outside loans. Thus internal cooperative structures severely restrict the ability of becoming commercially healthy and hence attractive to external financial entities. Recommended solutions are to allow non-members to provide capital by restricting voting rights to active members in order to accommodate outside capital, whereas the two analysed cooperatives in case studies reassure investors using revolving-funds and innovative collateral options such as export contracts as done by ResponsAbility. Another option, recommended by the authors and featured in one case study, is creating external separate legal entities that function as special-purpose investment vehicles in which the respective cooperative and investor share ownership rights.

Secondly, good governance is key to improving the services delivered by a cooperative as well as attracting external investment. In theory, all members in a traditional cooperative are made privy to details of and part of all decisions pertaining to the business. However, limited educational background paired with a high number of members practically results in enormous organisational inefficiency and alienation rather than belonging. In order to achieve clear

direction of decisions, stability of revenues and sustainable budget management, good leadership needs to be in place to lead all members towards a common objective. Traditionally, cooperative principles require a flat rather than hierarchical leadership structure with board-members directly elected from the membership base. However, their lack of education, experience, and management skills means cooperative organisations can become chaotic, unstructured and slow. Developing or attracting a manager with expertise is therefore of utmost importance, and a solution that the cooperatives featured in this report have opted for. Hereby the manager should enjoy the trust of its membership and include members in the final approval of important decisions. The authors suggest that in cases without the potential to select a manager internally, or where external managers are not an appropriate solution (willingness or ability), cooperatives may choose to have a rotational system more conducive to learning-on-the-job such as the US senate.

Thirdly, transparency is of crucial importance for both internal stability and outside support. Cooperatives need to develop effective and efficient information tools to gather their data regarding operational processes and financial terms. Through the communication of structured and organised information, members and investors understand the objectives and current position of the cooperative organisation resulting in the enhancement of trust. Cooperatives need to pursue internal education and training to develop the regarding organisational skills. Both analysed case studies use modern informational tools and implemented simplified but transparent account overviews in order to institutionalise their operational system. In addition, cooperatives are recommended to apply for certificates of external agencies in order to increase transparency even further, as well as increase publicity and credibility towards buyers and investors. The practical experience of the client and interviewed investors shows that adopting these practices leads to a stronger commitment by cooperative members as well as more possibilities for conventional outside investment.

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1. Introduction

This report was written in order to fill a gap in the analysis of cooperative business models for Christian Aid's market systems research. Agricultural cooperatives offer a natural entrepreneurial solution to the problems of poverty faced by millions in the developing world as they allow even the least literate smallholders to gain market access for their products: enabling cooperatives to successfully function and connect their business to the world market can thus help the most marginalised groups of people in the world. However, compared to traditional business models, cooperatives face detrimental investment constraints due to their organisational structure and cooperative principles, so that many scholars claim that attracting external sources of financing is the "Achilles' heel" of traditional agricultural cooperatives (Sexton & Iskow, 1988). The purpose of this report is to identify the success factors for attracting this financial support for the sustainable development of cooperatives and in doing so, spurring the processes that alleviate poverty. The report critically analyses the aspects that cooperatives should embody in order to be attractive for external investment as well as the necessary business and communication tools needed to stimulate such appeal.

In the first segment, theoretical background is provided in order to explain the principles upon which cooperatives are based, and their consequences for financing options. This part of the research is based on both academic literature and directly held interviews with leading investors in the agricultural cooperative sector. The generated knowledge from interviews with investors should emphasize the requirements upon which financiers put great value during their selection process.

The second section of the report features two separate successful cooperative case studies that the authors have analysed with respect to the theoretical and practical research in part I. The first case study focuses on the Manduvira sugarcane cooperative in Paraguay, which was able to attract $13.6m in external financing to design, construct, and finally operate its own sugar-processing mill in 2014. The second case study centres on the coffee cooperative of Kibinge in the Masaka district of Uganda, which has recently entered talks with several institutional investors like responsibility and Rabobank to increase the scope of their ventures.

The analysis of these two different case studies underlines overlapping factors that appear of crucial importance for agricultural cooperatives to be able to attract external investment, and offer a clear indication of the aspects well-run cooperatives share, namely (1) a business structure conducive to investment without diluting ownership rights, (2) professionalised management structures and a trusting membership base supported by education and inclusion, and (3) an excellent system of information management both internally and externally.

PART I: Theory & Practice

Defining Cooperatives

Cooperatives are business structures which aggregate different, independent, economic units and are run primarily to provide benefits to members through marketing transactions such as input buying and output selling as well as the redistribution of patronage earnings (paid in capital). In return members have a responsibility to provide the cooperative with equity capital (ownership) and exercise member control (governance). By combining independent economic units, cooperatives have the benefit of capturing economies of scale and therefore allow better market access for individual producers involved. These producers make up the membership of a cooperative and through it, become more capable of competing with players in their respective markets, which often operate on a larger scale (Ling, 2013).

Cooperatives differ from 'normal' business models in at least five major ways. Firstly, cooperative's customers are also its owners whereas these are separated in traditional firm models. Hence, ownership and control of the company belongs to its members, while each member remains economically independent and consequently, a rotational board of directors is generally elected for the coordination and management of cooperatives, directly chosen from the membership base (Chaddad & Iliopoulos, 2013; Ferrier, 2004; Ling, 2013).

Secondly, the articles of incorporation fix the price of a cooperative's common stock, which is not traded (nor determined) in an open market. Thirdly, cooperatives have access to a source of capital not available to standard businesses: deferred patronage refunds. Fourthly, cooperative may operate with a single tax on income. Finally, cooperative's objectives are to benefit its member-customers, not just its owners or shareholders.

Hence, a combination of aspects makes it so that cooperatives are more complex from an investment-evaluation perspective. The principles upon which traditional cooperatives are founded create a structure with inherent constraints to both internal and external financing, the focus of the first section of analysis. Furthermore, cooperative principles and purposes (often providing services for the most deprived of farmers) make their organisational aspects a source of concern for traditional investors, the topic of the second part of analysis (Battilani & Schröter, 1950).

2. External Investment and Cooperatives

2.1 Financial Constraints of Traditional Cooperatives

The increasing globalisation of agricultural markets has meant that producers in developing countries are faced with increasing competition from both outside and within. According to Chaddad and Cook (2004), these shifts in the agricultural system has required cooperatives to engage in "offensive" business approaches such as value-added processing, brand name development, and pushing for international market entry. The capital investment for these strategies is substantial but as a consequence of the user-ownership principle, cooperatives are constrained in their ability to acquire risk capital for investment and growth purposes and incur a higher weighted average cost of capital relative to IOFs. These financial barriers need to be understood and analysed in order to achieve effective and sustainable cooperation between farmers (Kalogeras et al., 2013) and to shape an understanding of how cooperatives could become more attractive to external investors.

2.1.1 The Capital Constraint Hypothesis

Chaddad et al. (2004) identify five major constraints cooperatives face inherent to their structure. Firstly, the user-ownership principle imposes a powerful constraint to financing. Since only active members may provide cooperatives with voting equity capital, the potential pool of risk capital is limited by the amount, wealth, and risk-preference of active members. This generally means that cooperatives are restricted to raising capital internally (Barry et al., 2000), which is a problem specifically in developing countries as cooperatives generally operate at the bottom of the supply chain, generating little surplus (Giagnocvo et al., 2011). Furthermore, residual claims on that cooperative's cash flows lack alienability; they are non-transferable and thus prevent the formation of a market in cooperative equity shares (Cook & Iliopoulos, 2000). The idea of the latter is to reduce saleability and thus maintain control over the cooperative in hands of actual farmers.

The cumulative result of these two aspects is that financing risky assets within cooperatives generally happens at a suboptimal level (Fama & Jensen, 1983), whilst the lack of tradability in shares means that public equity markets are non-accessible without changing the organisational form of a cooperatives, potentially undermining the principles it is founded on.

Secondly, cooperative members do not have appropriate incentives to invest; the traditional way of allocating property rights within agricultural cooperatives further undermines incentives for members to invest in the organisation (Cook, 1995; LeVay, 1983; Vitaliano, 1983). Because earnings are allocated according to patronage rather than stock ownership (traditional firm), there is a free-rider problem as members share in the return on cooperative equity capital regardless of whether they invest in the cooperative (Baumer & Knoeber, 1983) meaning it is in every individual's best interest to under-finance the cooperative. For external investors this naturally poses a problem and has instituted a perception that cooperatives are non-profit enterprises with an unreliable ownership structure (Lerman & Parliament, 1993).

This is further linked to the raison-d'être of cooperatives which is firstly to provide services for its members and only secondly as a way to generate profits. This means that rather than trying to generate a profit on capital investment, members aim to keep down costs made by the cooperative so that they can make a larger profit on their individual farm business (Hedges, 1951) and investment is only a secondary consideration after use of services. Essentially, members want the benefits of the cooperative but don't want to accept the corresponding ownership responsibility.

Thirdly, cooperative equity capital is not permanent. The reason is that cooperatives' balance sheets are made up of member funds; therefore all equity capital represents a claim against the cooperative by present and former members on patronage funds. Because these funds can be redeemed at any time, the capital stock of cooperatives can generally not be considered permanent but rather as a "pool of deferred cash dividends that cooperative can temporarily employ"

(Fulton, Lerman, & Parliament, 1990). In other words, limited liability companies have the benefit of capital "lock-in", so they can pursue long-term project, shareholders can get their money back by selling shares (The Economist, 2015). For many lenders, this characteristic of cooperatives is seen as incapable of supporting long or even short term loans with the effect of cooperatives experiencing enormously inflated borrowing costs. Some firms however, such as ResponsAbility, have taken to accepting exports contracts as collateral that lay claims on fixed assets for outstanding loans.

Finally, cooperatives have limited access to external sources of funds. Consequently, traditional agricultural cooperatives are generally seen as unattractive targets for external financiers due to limited collateral and lack of institutional legitimacy.

Hence, in order for a financial structure to suit the cooperative business model it should give assurance of patron ownership and control. This can be done by means of limiting voting privileges to active members and enabling rapid liquidation of funds for non-patron members. There should also be ways of enabling membership for new patrons quickly. Furthermore, the structure should be moulded according to the purpose and scope of the organisation. Risk plays a major role here and can be seen as dependent on the commodity, in so-called pooling cooperatives growers mostly carry the risk as they are paid once commodities are sold whereas in 'purchase-and-sale' marketing cooperatives risk falls on the purchasing association. Collateral for external investment in the first case can be done on the basis of export contract, a method ResponsAbility employs (Bonneux & Jibana, 2015). Finally, it ought to facilitate accumulation and retirement of capital for members, which is difficult when shares cannot be shifted from non-patron shareholders to active patrons. A potential, and often-used solution is the revolving-fund method, which allows active patrons to use accumulated savings in turn.

2.2 Structure-Focussed Solutions

Many cooperatives have transformed into invest-owned firms (IOFs) in order to overcome the identified difficulties cooperatives face in attracting external funds (Giagnocavo, 2012). However in effect members may share profits and eventually control rights with outside investors who are not necessarily patrons of the cooperative and thus have diverging interests. More recently, however, organisational innovations have also emerged within agricultural coops. These differ in the way ownership rights are defined and assigned to economic agents tied to the firm (Chaddad & Cook, 2004). Two types of models have emerged, identified as (1) cooperatives with Capital Seeking equities and (2) investor-share cooperative, which do not restrict ownership to member-patrons and thus are able to acquire outside risk capital, making them of direct interest to this report.

2.2.1 Cooperatives with Capital Seeking Equities

One of the most common ways of allowing the outside acquisition of capital is for cooperatives to establish an external separate legal entity. This can be done by means of establishing a strategic alliance, trust company, or a publicly held subsidiary. These options are ideal ways of circumventing the ownership issues inherently faced within the traditional cooperative structure. In a strategic alliance, a cooperative links with sundry partners in order to acquire permanent equity capital from non-members. These non-traditional financial models allow indirect access to external financial capital in exchange for a share of net margins as well as shared control. Many cooperatives in the developed world have adopted these types of ventures for control over downstream parts of their supply chains, for example Dairy Farmers of America. This solution allows mitigation of managerial risks inherent to cooperatives run by insufficiently trained members, on which more below (Cook & Iliopoulos, 2000).

By establishing a non-operating trust company or joint venture, cooperatives can be enabled to acquire financial capital from external sources. Many times, this will mean investors and the cooperative will each own a part of the novel unit, in which new capital will be invested. This option allows investors claim on their funds by means of direct ownerships, whilst that of the cooperative is not diluted. In many ways, this is a more patient and stable way for cooperatives to finance capital-intensive projects compared to normal debt, which puts heavy pressure on cash-flows, massive costs and penalties of default. Founding a subsidiary, also called the ‘Irish’ model, enables cooperatives to establish a separate public limited company and transfer all existing assets to it. Similarly to trust companies, the separate entity can then be invested in by outside investors without diluting the original ownership structure. This option allows the establishment of downstream processing plants for instance and whilst it allows direct ownership by members in a cooperative, it can be run as a more traditional business (Chaddad & Cook, 2004).

2.2.2 Investor-Share Cooperatives

As opposed to the prior model, the investor-share cooperatives allow acquisition of non-member equity capital by issuing different types of equity shares on top of the existing ownerships rights held by members of a cooperative. Investors shares come in three types: preferred stock, which does not carry voting rights within the cooperatives, nonvoting common stock, essentially a variation on preferred stock where 'A' and 'B' shares are issued, with just the latter being transferable, and finally participation shares, common in France as well as so-called 'Farmer Controlled Businesses' (FCB) in the UK, in which non-members invest in cooperatives without demanding voting rights (Chaddad & Cook, 2004).

2.3 Organisational Constraints

2.3.1 Professional Management

In addition to the structural constraints, a major disadvantage cooperatives face in attracting external investment is their lack of professionalised management. A clear direction, stability of revenues, and budget management are characteristics that are often linked to reliable managers, which in turn can be replaced by shareholders when IOFs perform badly. Not only this, but a confident manager can provide the vision required to motivate members to join any organisation. According to Challenges Worldwide (CWW) CEO Eoghan Mackie an important distinction is that cooperatives are not businesses that can advertise specific job descriptions or have pre-determined roles. Within a business, when individuals do not deliver, they can either get more training or get replaced as their defined function is tied up in a contract of employment.

Cooperative principles require a flat rather than a hierarchical structure and demand that candidates of the board are members of the cooperative (Ling, 2013). Hence, in agricultural cooperatives, farmers are elected into the board and are assigned the responsibility to manage the organisation whilst they are usually inexperienced, uneducated, and hence not suitable for the job. Decisions are theoretically made collectively and hence decision-making processes are very slow whilst regular rotations of the board members prohibits a strong and long-term learning curve of the members elected into the board (Kalogeras et al., 2013; Ferrier, 2004; Obern & Jones, 2007). The lack of management capabilities in terms of experience, knowledge, as well as skills of cooperative managers is a tremendous problem. Moreover, when a cooperative is successfully operating and increasingly expanding, the lack of effective representation on boards on a national level can induce communication and coordination problems (Ferrier, 2004). Such governance issues can make the coordination and management of the organisation chaotic, unstructured, and slow. Comprehensive management capabilities are the basis for the development of innovation capabilities meaning the likelihood of optimised processes, organisational practices, or marketing methods is decreased in cooperatives (Basterretxea & Martinez, 2012; Jensen & Miller, 1947). According to Gaelle Bonnieux from ResponsAbility, the extent of formal management has a strong impact on the rationality of decision-making processes within cooperatives; whilst some non-professional cooperatives are able to adapt to changing circumstances, others are slow to react and not collaborative.

A solution therefore would be to attract externally or develop internally a professional manager. In (rare) cases of openness and willingness to attract competent managers externally, cooperatives struggle to attract capable and proficient managers because of wage limitations, and the fact that small organisations do not have the ability to promote themselves in the marketplace. In addition, external managers often struggle to adapt to the cooperative culture and principles, and hence do not fully respect or understand the required close collaboration with a cooperative's board. Therefore the inclusion of external competent managers can create a degenerative impact on the organisation's democracy-based practices and principles, leading to ill success (Basterretxea &

Martinez, 2012). The NGO CWW offers another solution, which has been very successful in providing cooperative business with the tools they need to become more professionally structured and managed. By analysing organisational deficiencies, the organisation attempts to understand the context in which a cooperative operates and to supplement their existing framework within those parameters. CWW mentors the organisations to foster trust and work towards building an inclusive, cohesive organism; this management "style" is crucial and avoids a great degree of imperiousness. Farmers need to personally and professionally accept the manager in charge, which can be achieved by honest and transparent cooperation with all members on a regular communicative basis (Basterretxea & Martinez, 2012; Obern & Jones, 2007).

2.3.2 Trust and Education

The attitude of the cooperative's members can represent a critical obstacle to manage. Research shows that members' professional behaviour is highly influenced by their perceptions and attitudes. Hence, the perceptions and beliefs of members need to be comprehended in order to understand their consequential attitudes and behaviour that reflect on an organisation's success (Bhuyan, 2007).

Key determinants in shaping the attitudes and perceptions of cooperative members are trust and education, two aspects that are often underestimated and disregarded. Because members, the farmers, are often not aware of the aim and long-term objectives of a cooperative, they may not feel recognized or listened to by a cooperative's management. Additionally, many farmers may have perceived corrupt behaviour of cooperative managements before, which will result in distrust for the organisation from the start. They will thus develop negative attitudes towards the organisation, which can result in disloyalty and opportunistic behaviour, whereby farmers seek short-term economic benefits and sales outside the cooperative framework, damaging the organisation's aggregated product volume and coherence (Bhuyan, 2007; Jensen & Miller, 1947; Obern & Jones, 2007). Lack of a formal education may result in farmers not understanding the long-term objectives and economic benefits of the organisation. This, too, can result in individualistic tendencies, especially when farmers face low incomes and are dependent on immediate results, opportunistic behaviour is more likely. Cooperatives often fail in providing adequate educational programs to farmers, which would ensure more constant communication and the transfer of information about what a cooperative is doing and aiming for in the long-term (Jensen & Miller, 1947; Obern & Jones, 2007). Hence, through educational programs and trust building, cooperative management can keep the gap between famers' expectations and their perceived intention and emphasis as narrow as possible.

2.3.3 Information

A consequence of the democratic shape of cooperative managements often results in a lack of transparency to outsiders, with no data available for external investors to analyse. The effect of this is to increase the weighted cost of debt for cooperatives in general. In order to seize opportunities of commercial sources of credit, cooperatives should streamline and modernise their information flows. This means for instance aligning their financial layout with standardised accounting practices; irrespective of their purpose and role cooperatives should thus practice budget management, as they may be more attractive for commercial entities when they create more simplified, transparent account overviews. According to the agricultural investment firm ResponsAbility; obtaining certifications from conferences, networks, chambers of commerce, and national boards (e.g. Ivoirian Cocoa Board) greatly enhances a cooperative's visibility and transparency. These systems, most specifically Fairtrade, require extensive audits and large amount of crosschecks (questions, documents, verification) and therefore provide a comprehensive, transparent foundation for external capital investors. When these proven systems are not in place, ResponsAbility encourages and trains its client cooperatives to maintain simple Excel-format financial spread sheets that give a clear and concise overview of their fundamentals such as the number of active suppliers over the total number of registered suppliers, a solid indication of trust in the workings of the cooperative. Some education about corporate finance is thus indispensible in order to create an understanding of the need to align finances with operating structure and to shape the perception of a cooperative as a vertical extension of members' farms (Barton, 1989).

3. Practical Experience

The practical issues that investors and the client have faced in dealing with cooperatives strongly complement and correspond with the above theoretical findings. Christian Aid indicated that from their experience one of the main challenges for cooperatives is a lack of entrepreneurial experience and expertise at the head of an organisation, which often impairs comprehensive economic analysis and allows short-sighted perspectives. As emphasised by the theoretical analysis above, a lack of education as well as experience of elected farmers on membership boards can pose a formidable problem whilst regular rotation practices obstruct the development of a more sophisticated knowledge base among board members. Furthermore, Christian Aid often experienced a lack of trust from members in cases where cooperatives are dependent on a central organisation, such as an investor, which may not trust the competences of the elected farmers in cooperative boards and hence tries to maintain tight control. These situations lead to uncertainty of management responsibilities and control, resulting in inefficient practices and unclear governance. On the other hand, in cases where a competent entrepreneur led the organisation and sufficient trust between members and leaders was created, the decision-making process was generally able to proceed much faster and more efficiently because the manager was allowed a certain scope of autonomous authority (Bonnieux & Jibaja, 2015; Heywood & Preciado-Awad, 2015).

A further issue that had become apparent in the client's experience with cooperatives were transparency issues with organisational data on profits, progress, and operations stemming from the lack of expertise and capabilities in management. These transparency issues led to major barriers in being able to attract external investors. Many cooperatives do not have the sufficient information tools and practices to store and represent data in an organised way. The consequence of lacking or inappropriate tools to structure and provide information is the neglect by investors; without a transparent picture, the risk of investing is too uncertain and high to proceed (Bonnieux & Jibaja, 2015).

A final issue highlighted by the client, is the instability of cooperative membership, often provoked by past corrupt behaviour by management boards. Many investors have experienced such corruption problems at cooperatives and in one case a cooperative fraudulently acquired certification in order to provide collateral for a loan. This type of corruption represents a wide spread issue especially in Africa. However the aforementioned lack of transparency means cases are often only identified post-ante. Calculating for this risk, investors indicated they are often forced to demand much higher interest rates from cooperatives; investors only engage in investment if they are fully convinced by the cooperative's potential, as any default will lead to the complete loss of investment. The inherent risk that investors feel is present in these circumstances is helped only slightly by using export contracts as collateral, as in practice most cases cannot be taken to court as the process would be too long and costly to be worthwhile; ResponsAbility indicated to give up or restructure financing in these cases in the hope of future success (Bonnieux & Jibaja, 2015).

PART II: Case Studies

On the basis of the theory and investors' experience presented above, the main challenges for cooperatives in attracting external financial capital can be grouped into three fields: (1) an appropriate business model and structure, (2) ownership mechanisms that are appropriate for both members and investors, (3) good management, trust and education. In considering these three points, the authors selected two cooperatives for case study analysis. Both of these cooperatives were chosen as case studies because they have well-organised business models and have successfully attracted external finance recently. Furthermore, in order to draw conclusions at a broader level, the two cases are geographically dispersed and belong to regions the client is active: the sugar cooperative "Manduvira" is based in Paraguay, Latin America, whilst the "Kibinge" coffee cooperative is located in Uganda, Africa.

4. Manduvira Sugarcane Cooperative, Arroyos y Esteros, Paraguay

Manduvira is a smallholder sugarcane farmers' cooperative in Arroyos y Esteros, Paraguay with about 1,700 members (as of 2013) of which more than 1,000 are organic sugarcane producers. The cooperative promotes certified organic sugar production, processing and marketing, and also provides microcredit support to its members. Most of Manduvira's farmers cultivate an average of two to four hectares of land, exclusively for sugarcane production. The cooperative provides each farmer with a wide range of services; banking, credit, social services such as medical and educational help, technical assistance for sugarcane production as well as processing and marketing of members' production.

After establishing itself as a cooperative of savings and credit in 1975, it experienced bankruptcy in the mid-1980s because of "too-easy-access" to CREDICOPE, a government loan scheme for farmers in Paraguay (Vasquez-Leon, 2010). By restructuring its debt in the 80s and 90s, Manduvira was able to restart its operations as a marketing cooperative dealing with sugarcane syrup from members, who processed sugarcane in their 150 home-based sugar mills. In 2013, annual revenues totalled approximately $6 million, of which 91% came from sugar sales and 5% from financial services.

The tumultuous history of Manduvira throughout its existence explains the choices that led to their current business model, defined by (1) the ability to acknowledge the strategic importance of the strengths of collective action, and (2) its ability to use Fair Trade certification to occupy a niche position and market. Manduvira is now one of Paraguay's main sugar exporters and its destinations are mainly European countries. There had been a strong desire to own their own mills and in the early 2010s, Manduvira was able to build its own sugar mill allowing it to increase production volume and acquire full control over industrial processes. This sugar mill has opened for business in April 2014 and has been continuously expanding its capacity usage.

4. 1. Business Model, Finance and Management

4. 1. 1. Collective Action

In 1990s, the profitable prospects of the organic sugar market persuaded Paraguay's private-sector industrialists to enter the sugarcane processing market, followed by their purchase and renovation of "Oficina Tecnica Industrial, S.A." (OTISA), a local sugar mill built in the 1950s. Local farmers would come to sell their sugarcane to OTISA at US$12 per ton as opposed to the US$16 paid at other mills, but OTISA benefitted from having Fairtrade certification at the time (Vasquez-Leon, 2010).

Initially Manduvira did not have enough bargaining power to intervene in price negotiations against OTISA. However, Vasquez-Leon (2010) points out circumstances changed when "local agricultural committees", assemblies organised by farmers' family groups, collectively stood up against OTISA by discussing many socioeconomic and political issues, including complaints against OTISA being in the committee. Committee leaders became aware of Manduvira's potential to collectively negotiate with OTISA breaking its monopoly. Hence, farmers consulted with the Manduvira's manager and increased the number of memberships.

There was initial apprehension to engage in negotiations with OTISA due to the fear it would stop the purchase of sugarcane. Led by Manduvira's initiative, in 2003 farmers held off on harvesting for several days in order to agree on higher prices with OTISA. They successfully managed to improve sales conditions, drastically changing the power balance with OTISA. Hence, local farmers became aware of the strategic importance of collective action and became convinced to sell their products through Manduvira. In the 2000s Manduvira leveraged the power of viable competition and decreased OTISA's monopoly power by concluding processing contracts with other mills.

4. 1. 2. Fair Trade

A corner stone of Manduvira's success has been receiving the Fairtrade certification; whereas usually the severe environment of the conventional sugar market prohibits small-scale farmers in Paraguay to compete, Fairtrade certification indicates that a product fulfils certain standards related to labour laws, environmental impacts, but also guarantees adequate payment for the Cooperative. Furthermore, with certification the price of refined sugar has been increased by 1.5-2.5 times (Gudoshnikov, 2001). According to the Fairtrade Foundation, this qualification ensures prices for "sustainable production" costs and acts as a safety net for farmers. The Fairtrade premium (the extra payment intended for social goals made to certified producers) increased while more farmers became certified.

OTISA was the first organisation to obtain Fairtrade certification for sugar in Paraguay. It was expected to contribute heavily to poverty alleviation of sugarcane farmers by providing them with Fairtrade premiums. However, as indicated above this was not the case. When Manduvira obtained the Fairtrade certification in 2004, it improved the situation for many farmers decreasing the threat from OTISA's monopoly; Manduvira successfully encouraged other mills and farmers to acquire certification by FLO. As a result, Manduvira was able to realise sugar exports by small farmers to European countries for the first time in Paraguayan history (Aguilera, 2015).

The Fairtrade certification did not only increase price-levels, but also strengthened credibility and business opportunities for Manduvira: when Manduvira faced a shortage of operation money during the first year of export, “many people said we would fail” (Aguilera, 2015). However, the FLO provided a good channel for communication with buyers in Europe, of which many were interested in directly cooperating with local farmers. Furthermore, a 60% upfront payment included in FLO rules, allowed Manduvira to receive compensation two months prior exportation to cover their operating costs; these payments were crucial for the launch of Manduvira’s export business.

4. 2. External Financing Accountability

4. 2. 1. Potential of Organic Sugar Market

Before Manduvira owned its own sugar-processing mill, Manduvira’s production capacity was 6,200 tons per year by renting private mills with a processing capacity of around 60 tons per day for 90 days. However, Manduvira received orders almost 3-4 times its output level of around 20,000 tons sugar annually for more than five years in advance (IDB, 2010). This functioned as “good pressure” for Manduvira to expand its business. The introduction of a new mill has allowed the maximum amount of sugar processed to be more than 100 tons per day for over 180 calendar days per year. This surge of processing will require an additional 3,000 hectares of sugarcane farmland on top of the current level and will benefit another 500 farmers (IDB, 2010). Production forecast for 2014 sets 12,000-15,000 tons and for 2018 a maximum volume of 20,000 tons annually (Aguilera, 2015).

4. 2. 2. Manduvira’s Accountability to External Investors

To acquire external financing, cooperatives are generally required to provide detailed information about their financial status and business prospects to investors, which can often be difficult as discussed above. In the case of investment for Manduvira’s mill construction, multiple international financial institutions as well as local entities were involved. At the end of 2011, Manduvira received

US$13.6 million in externally financed loans by a syndicate of lenders. Finance by external investors accounted for 67%, which included Oikocredit (US$ 2.9million), ResponsAbility (US$ 2.6million) (OIKO CREDIT, 2012) and the Inter-American Development Bank (IDB). Technical assistance aid worth US$250,000 from IDB should increase capacity-building in order to obtain a better yield from sugarcane improving industrial processes (IDB, 2010). The remaining 33% came from domestic banks and the Fairtrade premiums Manduvira received.

According to IDB (2010), before the investment, Manduvira had US$3.3 million of assets, US$0.9 million of equity and US$2.4 million of liability. Its annual sales amounted to US$3.8 million with a net profit of US$126,260 for 2009. Compared to these figures, US$13.6 million represents a high sum, about 4 times the existing total assets. Therefore, Manduvira is required to continuously present clear and creditable information disclosure of their business workings, risk and operations. Therefore, Manduvira established a secretariat with expertise in management and accounting for the continuous communication with investors. This organisational structure was established endogenously, in order to be accountable not only to investors, but also to its members internally. On top of these organisational strides, the credibility of cooperatives with Fairtrade certification is seen as easier to judge due to former audit procedures (Bonnieux & Jibaja, 2015). In addition, financial institutions can evaluate Manduvira's financial status through former short term financing of operational and trading activities. This allows financiers better judgement on long-term investments (Bonnieux & Jibaja, 2015). The operational costs of Manduvira are covered by local banks and other cooperatives (55%), financial entities in Europe such as TWIN and Incofin (15%), as well as revenue from sales (30%) (Aguilera, 2015).

For these reasons Manduvira was eligible to acquire high and long-term loans. According to the IDB (2010), what guarantees the continued sustainability of the investment for the lenders are (1) promising improvements of the business model, which reduces costs of processing and transportation, (2) appropriate technical assistance and good practices for organic and Fairtrade certification, and (3) the increase in output, which will allow Manduvira to maintain its leading position in a constantly growing market.

4. 3. Management and Internal Accountability

The quality of Manduvira's Fairtrade certified products, the trust built up through on-time delivery, and the well organised channels of communicating information are all aspects of Manduvira's business strength. In addition, special emphasis should be put on Manduvira's effective internal management mechanisms including the involvement of members.

4. 3. 1. Ownership and Control by Members

Two General Assemblies

Manduvira ensures members involvement through two annual assemblies. The "General Fairtrade Assembly" discusses the distribution of Manduvira's Fairtrade premium. Half of this premium is generally distributed across all members, while the rest is reinvested. The 50% ratio has been an unwritten rule since 1999, although the total premium was invested fully into the mill's construction from 2010 to 2014. Secondly, the "Ordinary General Assembly" in accordance to Paraguayan law reports the annual fiscal balance, approves important future investments, and elects the representatives for the Executive Committee. Topics discussed in the "General Fairtrade Assembly" are also ratified in the ordinary assembly. The assemblies are not only a forum to discuss business related issues, but also feature discussions of other areas related to members' social lives such as financing educational programs or medical services; these services strengthen the dependence and commitment of members to the cooperative as such services are underprovided by the Paraguayan government.

Two years ago, members in the assembly decided to deny future memberships for new farmers in order to avoid any free-rider problems associated with new members and to enable existing farmers to harvest their maximum output to be processed in the new mill. This increased the commitment that farmers have to the cooperative and mill-construction project. As a rule of thumb, a high ratio of active suppliers over total members in a cooperative indicates good trust between a cooperative and its members (Bonnieux & Jibaja, 2015). The IDB's (2010) analysis concluded that the new plant would benefit a total of 1,200 farmers in terms of increased income from products. This has been a strong reason for most of the members actively supplying their products to the cooperative, and therefore has also solidified its safety for external investment.

Creation of Joint Venture: Mill Construction

Whilst Manduvira maintains 100% of the voting rights for members in its General Assembly, it has established a joint venture as a separate entity from the cooperative, which holds all the assets of the sugar mill factory. In this "trust", Manduvira and external financers share equity: 60% is owned by the cooperative and 40% is by investors. This separate capital structure intends not to dilute the ownership rights of members in the cooperative whilst providing a controlling mechanism for external investors because it allows them to intervene in the management of the factory (Bonnieux & Jibaja, 2015).

4. 3. 2. Management of the Cooperative

As in most traditional cooperatives, members elect an Executive Committee with limited terms in Manduvira. However, the committee delegates their authority to an administration council, and this council delegates it to the general manager, who has profound expertise in running businesses and makes most of the practical decisions in operation. This is an absolute strength of Manduvira compared to other cooperatives, in which one of the farmer members serves as the general manager of the cooperative (Bonnieux & Jibaja, 2015). Manduvira has a well-structured organisation under the general manager, consisting of departments, which have expertise in specific fields (see Figure. 1). Each department has developed its know-how gradually during Manduvira's long history. The accounting department for instance previously enumerated all financial information on their documents, but have been undergoing self-improvement to disclose information in a more organised way by introducing some professional methods and tools: it uses Excel spread sheets to summarize financial information and storage information in each department. Furthermore, Manduvira is now developing an internal system to aggregate accounting information in the organisation (Aguilera, 2015).

Figure 1: Structure of Manduvira's Organisation

From Manduvira (2015), translation by LSE project team

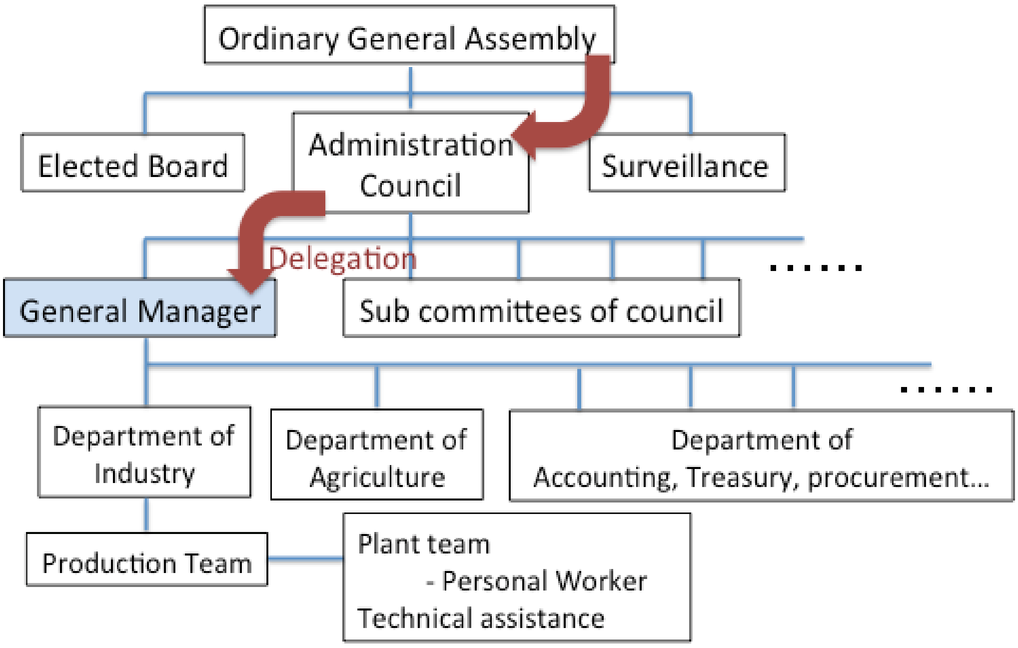

Figure1. Structure of Manduvira's organization
Reference: Manduvira Translation: LSE project team

The issues and ideas identified by the management body, such as the introduction of its accounting system or the medical care service in the district is reported to the assembly. Members are able to discuss matters with sufficient data and background knowledge provided by management to come to solutions within the assembly. Thereafter the management body implements the resolution. By means of this mechanism, Manduvira has been able to successfully implement its business strategy with a long-term perspective whilst ensuring sound commitment by all farmers. According to Aguilera (2015), general manager of Manduvira, "farmers do not feel that there is a need to 'control' the cooperative, because they feel Manduvira is *their* cooperative. They started it together, gained better sales conditions with the best market price of sugarcane in Paraguay, expanded its functions to support farmers' lives such as medical service, education and money lending. All of the above decisions were approved collectively by all members". This indicates farmers are fully convinced that they are involved in all decision-making steps and understand the project's background and necessity resulting in true loyalty. Furthermore, the provision of extra services such as health or educational services increase the members' dependency and gratitude towards the organisation.

This mechanism has enabled stable operation and production outputs, which is indispensable to keep good relations with buyers. Buyers seek long-term stable partnerships and need to be able to rely on their producers. Proven tracks of records with one buyer led to many contracts progressively and a considerable size of sales with lots of years of experience.

5. Kibinge Coffee Cooperative, Masakaa District, Uganda

Kibinge cooperative, located in the Masakaa district of central Uganda, was founded as an association in 1995 by four dedicated coffee farmers interested in addressing the challenges faced by coffee producers in terms of production processes and market access. After struggling for 15 years, the association made the deliberate decision to become a member-owned cooperative in 2009 in order to generate more sustainable profits for both the farmers and the organization. This has enabled it to invest more in its facilities and processing capacity and to provide a better income for its members; it became Fairtrade certified in 2011 and in 2014, Kibinge was crowned the winner of Fairtrade International Small Producer of the Year for Africa Award (Fairtrade, 2014).

The cooperative remains true to its mission of improving the lives of farmers and community members and recent projects include electrifying a local health centre, building VIP-latrines for community schools and upgrading the community access roads. Guided by principles of integrity, professionalism, competence, respect, fairness and transparency, Kibinge's membership and staff continues to grow: to date, the coop has 2,015 members and employs 21 full time staff (Kibinge Coffee, 2015).

5.1 Business Model

5.1.1 Major Activities and Partnerships

Kibinge's major activities include: buying, processing, and exporting of coffee beans, training of farmers in good agriculture practices, provision of financial services at an affordable rate using a recently created savings and credit unit (SACCO), supply of agro-inputs, and initiation and management of community projects. In order to improve its activities and increase their scope, the cooperative partners with multiple actors both in the private, public and donor communities and works closely works with both the central and local government of Uganda by supporting government led initiatives and in adhering to government cooperative as well as coffee production and marketing standards. In 2014, for instance, Kibinge hosted the district's Coffee Trade show. Kibinge is also a member of the Uganda Coffee Development Authority (UCDA), which is Uganda's government's coffee production and trade regulatory agency (Kibinge Coffee, 2015).

5.1.2 Fair Trade Certification

Fairtrade is also one of Kibinge Co-op major partners, it has provided technical trainings on Good Agricultural Practice (GAP), which has enabled farmers to develop and implement farm food safety plans; prerequisite conditions for GAP certification, which is a ticket for exporting agricultural products globally. Other trainings on Post harvest handling, bacterial detection and collective marketing have also been provided by Fairtrade. As a result, the cooperative now gets higher yields from the farmers and is able to market their products with greater confidence in the international markets (Fairtrade, 2014). By being able to access Fairtrade Premium funds, the cooperative has been able to establish the farm supply shop and the savings and credit unit. Part of the Fairtrade Premium was also used to buy a plot of land on which the cooperative plans to build its future home. The site will accommodate a modern factory with the technology to process coffee beans from start to finish, it will house the savings and credit unit, the farm supply shop, and it will also serve as a coffee resource centre.

Kibinge has performed well in complying with Fairtrade standards. According to the General Manager, David Lukwata (2015), the partnership has “given us global exposure. We have contacts everywhere now – networks here in Uganda, the Fairtrade network in Africa (Fairtrade Africa). When we became certified, we became known. Buyers from all over the world contact us directly – before we even contact them – because we are Fairtrade certified. We have an export license and we’ve won international awards”. Solidaridad, a chemical company, also provides Kibinge co-op farmers with trainings on safe, efficient and effective chemical use. The coop also started coffee farmers’ environmental committee for the coffee farmers to help protect the wetlands in the county.

5.1.3 Value Chain Development Process

Kibinge’s coffee value chain starts at the production of coffee by cooperative members for which the cooperative supports farmers in various ways to ensure high productivity. Farmers can access the farm inputs like seedlings, fertilizers and tools at the farm shop within Kibinge facilities whilst quintessential extension advisory and support services are also available to the farmers at no cost. After production, the coffee cherries are harvested by the farmers and delivered and bulked at Kibinge’s own processing unit for hulling. A team of Kibinge Coffee experts carry out quality control analyses to ensure that the coffee beans are devoid of any impurities and dried to the required standards before packaging. The coffee beans are then stored and graded by UGACOF, one of the companies that manage coffee exports in Uganda (Lukwata, 2015).

5.2 Finances

5.2.1 Traditional Membership Model

All members of the coop pay an annual membership fee of £1.16 and each member is required to buy a minimum of two shares at £2.32 each. Presently, the largest shareholder has 75 shares whereas the average shareholding is around 40 shares per member-farmer. By principle, no member is allowed to buy over one-third of the cooperative’s total share capital. In 2013/2014, the coop received £390 as annual membership fees and sold shares worth £3,400 to members. Dividends are shared among members at the end of each year to reward hard work and celebrate success (Lukwata, 2015).

5.2.2 Modern Investment Model

To diversify its revenue streams, Kibinge has successfully implemented certain innovations, enabling it to attract investment finance from financial and donor institutions both in Uganda and abroad. This has meant that in the past two years, the coop secured grants worth £35,000 from donors like DANIDA, USAID, USADF and BTC. Most of these grants have been invested in the community projects. Simultaneously, Fairtrade certification and the associated fair trade premiums (£84,000 in 2013/14 from coffee sales in Europe) have been instrumental for the continued growth of the cooperative. It should be noted that commitment of donors as well as profits accruing from Fairtrade premium puts Kibinge's asset position in good shape and makes it easier to attract additional external financing. ResponsAbility is currently going through a process of due-diligence with Kibinge for a potential investment relationship. Furthermore, in 2013 the coop partnered with Barclays Bank to distribute 2,500 fichus trees to its farmers; shades from fichus trees provide a favourable ambience for coffee trees to thrive in whilst the leaves act as a source of organic fertilizer (Fairtrade, 2014; Kibinge Coffee, 2015).

5.2.3 Product & Service Sales

Kibinge Cooperative sold coffee worth £524,000 to coffee exporters in 2013/14. The SACCO unit also disbursed loans worth £56,818 at 2.5% interest rate, which has generated gross profits of £16,000 in the first year of operation. The newly established farm-input supply shop at Kibinge coop also generated revenues worth £1,818 in 2013/14 (Lutwaka, 2015). Kibinge's ability to combine both the traditional and modern revenue streams while also selling goods and services to both the farmers in Kibinge sub-county and coffee consumers in Europe has enabled it to stay afloat and continue operating in a very profitable manner.

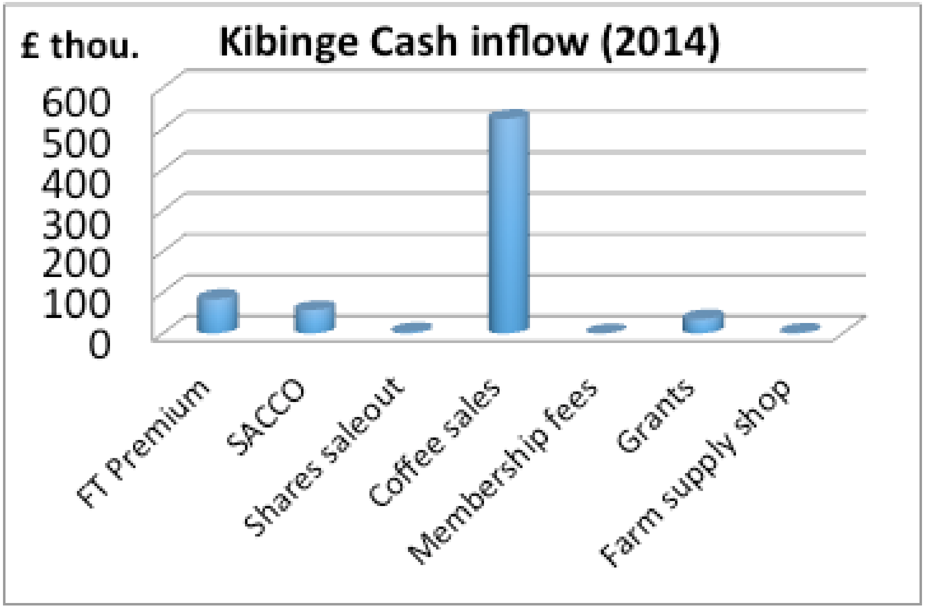

Figure 2: Kibinge Cash Flows
From: Kibinge Coffee (2015)

5.3. Leadership, Management and Membership Structure

Over 80% of Kibinge's members are illiterate smallholder farmers most of whom have only attained primary school education. This could have negative implications for the management and effective operation of the cooperative, as generally high rates of ignorance slow down the adoption rate of new ideas, innovations and technologies (Ferrier, 2004). However the cooperative has implemented an innovative management system to deal with this issue.

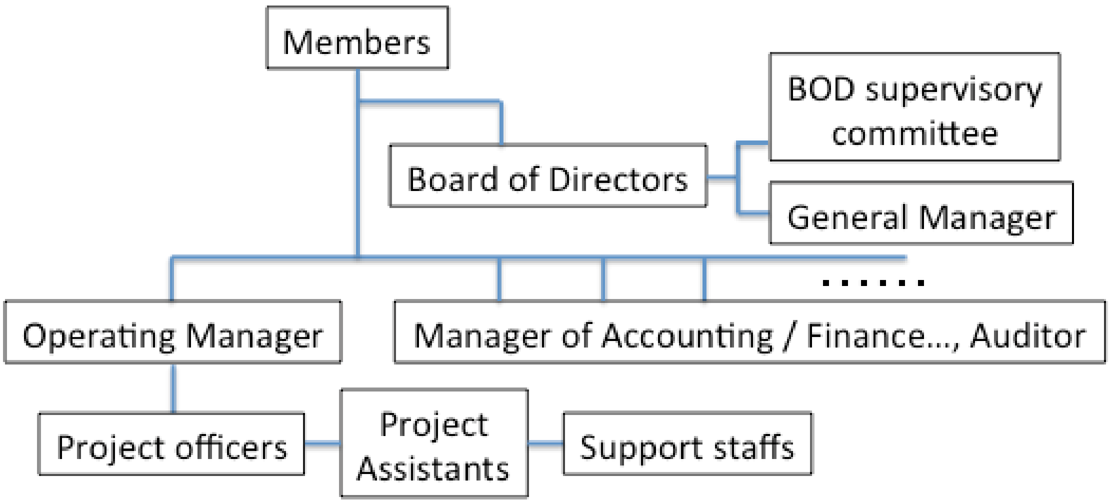

Figure 3: Structure of Kibinge's organisation
From: Kibinge Coffee (2015)

The cooperative's 2,015 farmer-members are organized in 48 farmer groups that operate on the village level. Each group has a leadership structure and these report to the designated village cooperative representative who is a coffee farmer, too. A large part of the management teams' members, including the General Manager, have diplomas. Furthermore, the cooperative continuously runs a capacity building programme where the coop gives staff members the opportunity to acquire more skills and knowledge to deliver effective results. All members attend an annual general meeting at which necessary consultations and discussions are held on the future direction of the cooperative. The management and the board of directions has some limited powers to make certain informed decisions of during the day to day running of the cooperative. The management must however provide candid accountability to the whole member base at all times. Kibinge does this by declaring and displaying business financial records and reports to all members, its partnership with well-established institutions like Fairtrade and USADF has been instrumental in enhancing transparent accountability systems to both funders/investors and the members, an asset which has contributed to the continued trust and cooperation between the coop and the various stakeholders. One of the major challenges Kibinge continues to face is the illiteracy of members, which slows down operations and makes it difficult for farmers to fully commit to the cooperative's management. In order to promote commitment and enhance trust among members, Kibinge is making efforts to build local leadership by using small farmer group platforms and also providing special capacity building packages to the farmers. Similarly, it implements community projects such as the development of social infrastructure in the region (Kibinge Coffee, 2015; Lutwaka, 2015).

6. Comparison and Final Remarks

Although both cooperatives share several similarities in their successful models, their differences are mostly pronounced in the specific challenges faced within their business operations. Both Manduvira and Kibinge deal with agricultural products, which are highly volatile in the global markets. The constant growth and expansion of the organic sugar and coffee markets make it attractive for companies from other countries to gradually enter these sectors. This trend can cause drastic changes of the global market and pushes demand toward those countries with a large potential for production, reducing the competitiveness of both coops in the process.

Manduvira's challenge is to make sure that their business model is able to survive and keep pace with today's growth. Manduvira faces definite financial risks due to its recent high investment, which is based on predicted market conditions. It will be essential to maintain its relationship to external buyers by means of long-term contracts in order to maximize the capacity and profit potential from their newly owned mill. As for Kibinge, it still has a lot of space to improve its business management structures although their business prospects seem sufficient. In the future it could employ an advanced model of structured capital such as Manduvira's, employ stronger governance through a management body led by business experts, and contribute to raise the level of literacy so members can soundly commit to cooperative management. Crucially, these changes should be generated endogenously, which would make members feel reassured with their ownership of the cooperative.

Additionally, unlike Manduvira, which has built a long-term relationship with its financiers and attracted more external financial investments in the form of patient capital from social credit institutions, Kibinge has only just started this process and has recently been assessed by ResponsAbility for a potential lending relationship. Kibinge still receives grants and donations from aid Agencies such as USAID and BTC, whereas Manduvira does not. Being associated with such agencies could bring bankable advantages such as more name-recognition and a seal of trustworthiness, aspects rated highly by investors.

Looking at the organisations' cooperation with governments, it should be noted that Kibinge actively makes effort to connect with the central and local governments of Uganda, whereas Manduvira deliberately tries to be independent from the Paraguayan government to minimize the influence from the unstable political conditions. However, the Ugandan government's support to Kibinge has been minimal and mainly restricted to regulation and the provision of access to external funding opportunities, rather than providing funds itself.

PART III: Implications

The identified business success factors drawn from the theoretical and practical analysis include the following: trust and understanding between members as well as buyers, good governance with clear communication processes, transparency of data as well as business expertise to identify business opportunities. All these factors can contribute to an enhanced level of investors' confidence towards a cooperative organisation, enabling external financing. Both Manduvira and Kibinge have progressively expanded their business functions through persistent adaptation and optimization of their business models. The two case studies show how the identified success factors can be facilitated and which instruments can be used to overcome key issues associated with the cooperative structure and principles as well as its inherent hurdle of attracting external financing support. The following business implications drawn from the two case studies emphasise the instruments and activities to be implemented to achieve above mentioned success factors and refer to Figure 4.

Certification by External Agency

Partnering with a socially established third party, Fairtrade, gave both Manduvira and Kibinge the credibility and opportunity to connect with external buyers and investors. In addition, Fairtrade has actively supported the co-ops financially, through the Fairtrade premium and its rule of upfront payment by buyers to producers. These functions have allowed circumvention of the initial bottleneck of limited access to external financing and therefore, cooperatives need to push for the accomplishment of certification by external audits in order to draw attention towards the organisation. It needs to be noted that cooperatives should ensure good reputation with their buyers, too, as buyers are a crucial linkage to investors in terms of recommendations.

Innovative Ownership Structure

Buyers as well as investors struggled with coordination and governance problems caused by the ownership structure of cooperatives. Hence, Manduvira combined traditional and modern forms of financial structuring to fuel its business operations. Manduvira's members hold all ownership and voting rights in the cooperative's decision-making process, similar to other conventional cooperatives. However, the innovative capital structure that Manduvira has employed for its mill construction involved the establishment of a joint venture, being satisfactory both for existing members and international investors. The authors emphasise that the developed structure was only possible after Manduvira's management body had accumulated sufficient experience and developed expertise in finance. Kibinge has managed to maintain a traditional structure with success, as evidenced the many recent grants but may be required to adapt its model in the future if it were to seek further capital development.

Efficient Information Tool

Investors traditionally face transparency issues when analysing cooperatives' financial data. Cooperative management thus needs to be transparent and accountable in their business activities towards their investors as well as their members. This can only be achieved through efficient information tools and integrated operational processes that enables to structure organisational data. Manduvira started on a very small scale, physically handwriting and filing all informational data – at this point of time no investors were involved in the process. However, Manduvira's manager points out that clear data transparency was also necessary to provide the members with a good understanding of the organisation's long-term benefits and objectives. At the moment, Manduvira is persistently optimizing their information tools through the aggregation of information from different departments into one excel document. These efforts emphasise the need for cooperatives to be transparent and accountable in their business activities towards both their investors and their members; a situation that can only be created throughout efficient information tools and integrated operational processes that structure organisational data. For instance, by means of using a mission statement, information on decisions and their desired aim can be expressed to members.

General Manager with Expertise

Many cooperatives lack good governance with clear communication processes and a division of managerial responsibilities. Distinct internal management mechanisms are necessary to achieve both strategy management and sound involvement of members. In Manduvira's case, members deliberately delegate their authority to a general manager for the strategic management of the organisation. This allows management to draw upon sufficient expertise to sustain its current business model while supporting accountability instruments for investors and internal members alike. Kibinge has also structured a management body to deal with everyday business operations and in order to provide cooperative members with sufficient information and background data. However, its organisational structure is relatively dispersed whilst the discretion of the general manager is limited to some extent compared to Manduvira.

Effective business expertise on the leadership level as well as collective support and understanding of cooperative members has consistently been a key success factor for the development of efficient business operations. The example Manduvira demonstrates the need for including members in the decision making process in order to assure their understanding of and guarantee support for any and all business activities.

Based on these findings, the authors strongly recommend cooperative structures that have an experienced entrepreneur at the head of the organisation closely collaborating with its members. This structure is only possible when the general manager fully enjoys members' trust and reflects a collaboratively communicating rather than the autocratic guidance of the organisation. The authors recognise that not all cooperatives may be willing to adopt such a structure, however this may be different when external financing bodies make this part of conditionality for loans. Extensive research resulted in the idea of changing the rotational systems of management in more traditional cooperatives, by only rotating (a different) part of a board every so many months, new entrants can be actively taught the skills of the trade by remaining executive members.

Making the cooperative a "style of living"

Finally, in order to fully attain cooperative members' loyalty, the organisation should try to make "cooperative a style of living". Manduvira and Kibinge both engage in activities outside of their core business such as providing education to members' children by community schooling or supporting local health centres. Hence, other areas of member's life are dependent on the organisation, increasing their trust, loyalty, and gratitude towards the cooperative. In addition, technical assistance for production and support for credit opportunities should evolve members' educational level and business understanding. It should be a cooperatives mission not only to aggregate production to increase economy of scale, but also to provide greater life style to its members and their families.

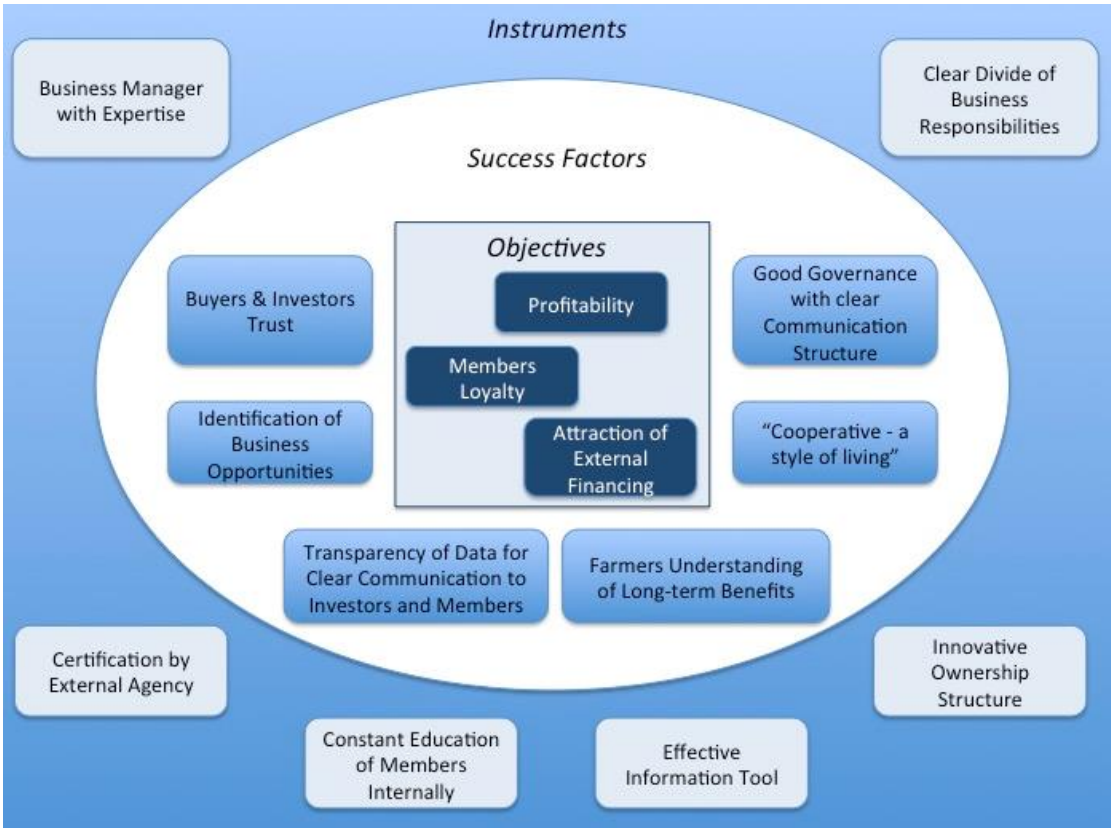

Figure 4: Policy Implications

7. Conclusion

This report was conceptualised in order to analyse the existing void in comparative literature on the reasons for success and failure of cooperatives, particularly with regards to the attraction of external financing. While the concept of cooperatives is rational and opens up vital opportunities, it has been evidenced both in the literature and within the experience of our client, Christian Aid, and many of those involved in the cooperative sector, that there are a myriad of challenges cooperatives face that do not apply to the traditional limited company business structure.

The authors have first focussed on the financial constraints inherently present in the traditional cooperative business model. Cooperative principles set clear limitations for the possibility of obtaining leverage, increasing equity, and promoting internal investment. Therefore, many cooperatives have either opted for radically changing their business models in order to accommodate leveraged financial flows and external investors, or converted to conventional IOFs (Investor-Owned-Firms). For the purpose of this report, the options, which maintain the intended cooperative function and principles, have been investigated thoroughly and the evidence demonstrates that ownership structures can be managed to this effect. Within the case study of Manduvira the authors demonstrated that creating an external separate legal entity is a remarkably effective way of achieving this.

Lack of professionalised management is another critical factor restraining cooperatives in several crucial ways. From a neo-classical firm perspective, managers within cooperatives can present a strong information asymmetry problem, if they fail to actively involve their membership base. However, decision processes are likely to be slow and inefficient, when the full membership-base is included in every incremental step of the decision-making process. Both case studies show that a clear mission statement by leadership is conducive to eliminating governance issues, whilst involving members in the finals step of decision-making processes. A strong manager with expertise enjoying the trust of members is crucial for communication and representation towards long-term investors as well as for the identification of business opportunities. Whilst the authors found that not every cooperative may be willing and able to professionalise its manager, basic education or the ability for farmers to learn on the job by creating a rotating system of board management can provide a tangible improvement.

The literature review and practical experiences show that data transparency organised, structured and disseminated through effective information tools is another key to success for cooperatives. Not only members need to understand the current position and long-term objectives of the cooperative, but the organisation also needs to be presentable towards buyers and potential investors. From looking at both case studies, these issues can be resolved by providing internal education for process optimisation to members and going through the process of seeking certification from third parties, which carries the added benefit of increasing visibility. Furthermore, innovative solutions have been provided by investors such as ResponsAbility, which provides information training and tools as part of its investment, as well as the targeted consultation work of Challenges Worldwide.

In conclusion, cooperatives have a strong place in the modern global marketplace, and by creating innovative private-sector-inspired business models will be able to attract the investment, technical expertise, and advise they need. By emphasising strong and accountable leadership, which upholds the virtues of transparency and trust, cooperatives such as Manduvira and Kibinge show that the cooperative model can in fact become attractive to external investors needed to sustain business growth, challenge the status-quo and lift millions of farmers out of the poverty line.

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Appendix

Terms of Reference - Successful Co-operatives

Purpose / role of the project

- In order to promote the Participatory Market System Development approach (PMSD), Christian Aid (CA) currently supports a number of cooperatives to achieve sustainability and receive investment.
- Due to the nature of CA's work, and its emphasis on the poverty-alleviating aspects of agricultural cooperatives, the project will solely focus on the agricultural sector in at least one of the regions of activity (Africa, Asia, and LAC).
- This project team was established to analyze elements of successful co-ops with reference in particular to their investment model (in particular equity by external investors) , management and partnership structures, to establish practical guidelines for cooperatives in order to elevate their business into an investment-ready state (rather than a general theoretical template of a business model) whilst keeping in mind and safeguarding the coexistence of growing economic development, external financial inflows, and perpetuation of the core values of cooperative philosophy.
- Furthermore, a focus will be placed on small-scale cooperatives as an approximate 80% share of the project, whilst the remaining 20% will take into account larger-scale cooperatives.

Membership

- The project team consists of 4 members, Alena Schultheiss, Donnas Ojok, Hidehiko Ishii and Kilian Koffi.

Working method

- The project will be based on case studies of existing successful cooperatives and of successful external investments into coops. These case studies will be conducted by means of desk research, interviews, and potential consultations with investment experts, cooperative sector players and relevant ministries.
- Both internal and external factors should be accounted for in the research. Including, but not limited to:

1) Management structure, and the technical and human resource capacity to implement a sustainable business model and reach an investment-ready state without dilution of social benefits and gains associated with co-operative model.

2) Barriers to receiving external investment and possible ways to overcome them.

3) The agricultural sector will be the sole focus of research. No specific cooperatives determined for focus.

Project procedure

- Regular Skype conferences will be held in relation to updates between client and project team, decreasing in frequency once terms and scope are determined. Agendas of the meeting will be circulated beforehand.
- Confidential materials and copyright: The team shall not use and/or share CA's organizational documents without prior consultation.
- Research interviews shall take into consideration LSE's and CA's ethical and professional standards
- The Project report (10000 words, supplemented by a 1000 word executive summary) to be completed by the 27th of April.
- A Final presentation of the project will be given to CA at the end of April or beginning of May.