

Managing farm business

**BUSINESS OPERATION STATUS OF CHINESE FARMER COOPERATIVES:
A 6-YEAR TRACKING INVESTIGATION OF COOPERATIVE A**

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Abstract

The number of farmer cooperatives in China increased dramatically after implementation of the Farmer Cooperative Law in 2007. Based on a 6-year tracking investigation of Cooperative A in Zhejiang Province, we employ a descriptive and case study approach to provide an in-depth understanding of the operation status of farmer cooperatives after introduction of the Cooperative Law, and attempt to discover how cooperative directors seek diversified development paths while regarding the farmer cooperative as the basis. This paper finds that obtaining subsidies from the government is one of the main objectives for the establishment of farmer cooperatives. Farmer cooperatives are not operated in accordance with traditional cooperative principals after establishment and there are operational problems, such as the cooperative director holding substantial power over common members and the lack of profit distribution mechanisms. Cooperatives implement diversified business models to achieve greater benefits (e.g. agritourism and fruit stores). Additionally, changes in organizational type from farmer cooperatives to family farms, to align with new policies, has also become increasingly prevalent. Finally, we conclude that most farmer cooperatives in Zhejiang Province are not true cooperatives, existing in name only. Both farmer cooperatives and family farms are Family-controlled Agribusiness Company-like Entities.

Keywords: Farmer Cooperative, Family Farm, Agribusiness Model Diversification, Family-controlled Agribusiness Company-like Entity

1 Introduction

Agricultural production in China has been conducted in a fragmented, small-scale manner for a long time. Farmer cooperatives are perceived as one way to resolve the conflict between “small-scale production” and the “big market”. The number of farmer cooperatives increased extraordinarily after the implementation of the “Law of the People’s Republic of China on Specialized Farmer Cooperatives” in 2007. There were 26,000 farmer cooperatives in 2007, and the number increased to 1.91 million with over 100 million registered members by June 2017, accounting for 46.8% of total farmers in China. However, there are existing studies (Pan, 2011; Narita, 2011; Jia, 2016) that have identified problems farmer cooperatives encountered during development, pointing out a considerable number that are neither functioning properly nor in line with the cooperative law. Other problems (Hu et al. 2016) such as over-intervention of government have led to quality negligence in pursuit of cooperative establishing speed, unfair distribution mechanisms, and lack of financing institutions.

Based on the past 6-year tracking investigation of Cooperative A in Zhejiang Province, we employ a descriptive and case study approach with the purpose of providing an in-depth understanding of the operation status of farmer cooperatives after the introduction of the cooperative law in 2007, and attempt to find out how cooperative directors seek a diversified development path while regarding the farmer cooperative as the basis.

2 Case study

We selected Zhejiang Province as the research area for the following reasons: Firstly, the per capita disposable income of rural residents in Zhejiang reached 24,956 yuan (3641 USD) in 2017, which ranked top among provinces of China. Secondly, Zhejiang put the “Zhejiang Farmer Cooperative Law” into practice in 2005, which was the first provincial-level cooperative law in China. The National Farmer Cooperative Law was also based on the Zhejiang Farmer Cooperative Law. Therefore, Zhejiang Province is regarded as the representative of the most agriculturally developed region in China. With regard to farm cooperatives, we selected Cooperative A that we had been tracking since 2012 for a case

study. Moreover, this cooperative was awarded the title of National Demonstration Farmer Cooperative and could be regarded as representative of large-scale cooperatives in Zhejiang Province.

1) Establishment of the Cooperatives

The director of Cooperative A, with his wife, had a grape growing area of 2 hectares before the cooperative was established. In 2005, the director and six other members established Cooperative A with a registered capital of 480,000 yuan. The main business involves growing and selling grapes. The relationship among cooperative members consists of mainly families, relatives and friends revolving around the director (member 1). In Cooperative A, there are three members who are relatives of the director while the other three members are friends of his (Figure 1).

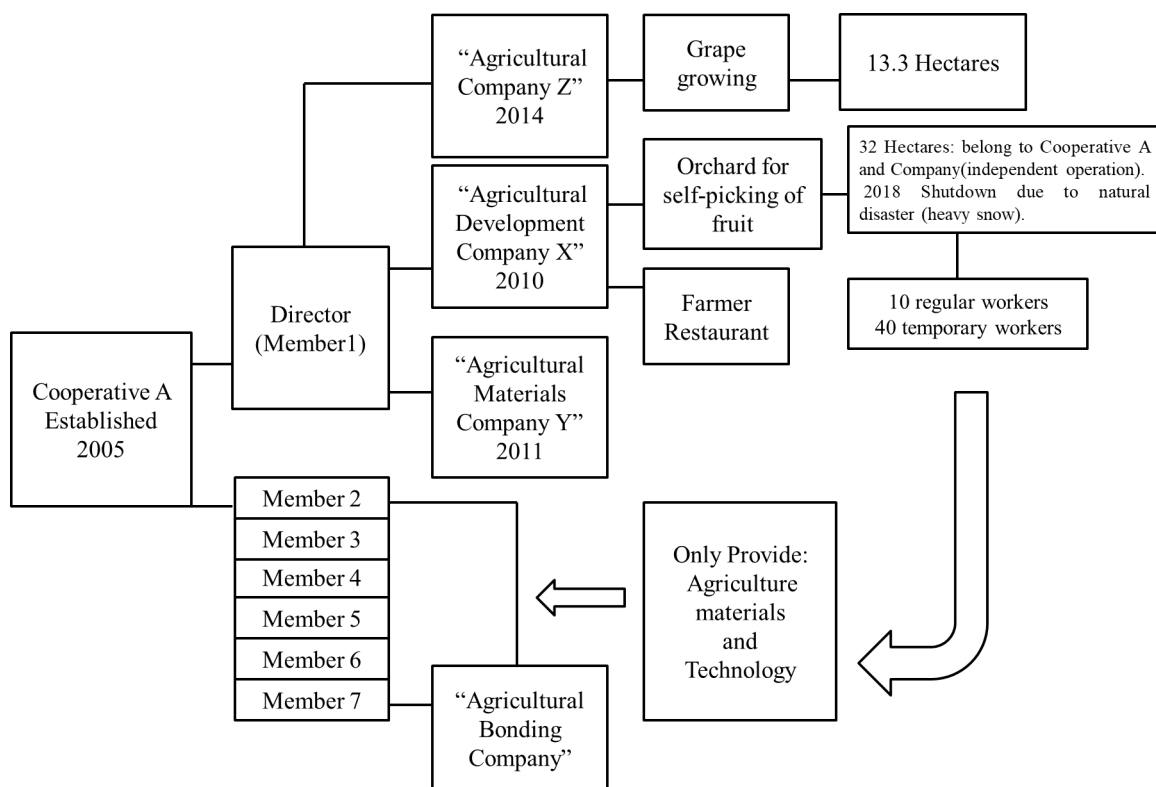


Figure 1. Development of Cooperative A

Source: Based on field survey in Zhejiang Province in 2018

2) Development of the Cooperative A

The total growing area of core members in Cooperative A increased from 4.8 hectares in 2005 to 65.1 hectares in 2014. In 2010, the director contracted another 30 hectares of land from the township government. He then set up an “Agricultural Development Company X” in 2010 and an “Agricultural Materials Company Y” in 2011. In 2014, the director established a third company Z with another 13.3 hectares of land for the purpose of growing grapes. Company X is an agritourism company based on the rebuilding 32 hectares of growing areas into an orchard, which incorporates fruit picking, production, leisure and catering activities, Company Y sells agricultural materials such as pesticides and fertilizers to members and non-members. There are 10 regular farm workers working in his production base and 40 temporary workers during harvest season. Some of the farmer workers own small plots of land while others have migrated from elsewhere. However, the agritourism business of company X was suspended due to damage to facilities caused by heavy snowfall in February 2018. At present, the director is focusing solely on the business of company Z.

3) Service of cooperative A

According to the interview with the director, the services that the cooperative truly provides to its members are merely technical training and a discount price when common members purchase pesticides and fertilizers. Neither unified sales nor a unified brand is involved in the business of Cooperative A, each member takes responsibility for their own marketing and therefore there is also no profit distribution.

When asked what made him establish the cooperatives at the first place, he stated, “Cooperatives are eligible to apply for subsidies from the government.” Subsidies received since the establishment of Cooperative A are listed in Table 1. (There are mainly three types of subsidies; subsidy granted after the purchase of machinery, government subsidy and technology aid).

Table 1. Subsidies* of Cooperative A (10 thousand yuan)

Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Coop	0.5	1	5	28	45	108	155	135	160	142			
Company*						50	26	65	105	46	320	40	25
Total	1456.5												

Source: Based on field survey in Zhejiang Province 2018.

Note: The subsidies shown in this row are under the name of a company.

4) Sales channels of cooperative A

In 2014, 55% of the products were directly sold to buyers who drove their trucks to the production base, followed by fruit picking in the orchard and supermarkets, which accounted for 25% and 10%, respectively (Table 2). Online sales and wholesale markets accounted for 5% each. However, the proportion of direct-sales from production base dropped sharply, from 55% in 2014 to 5% in 2017; and proportion of sales through wholesale market has increased to 50%. This is mainly due to the gradual shift of the director's management strategy from grape cultivation to agritourism, resulting in a decline in grape production in total compared to 2014. Therefore, the grapes that were not sold via direct sales and were not considered to be first class quality were then sold mainly through wholesale markets.

The growth in online sales has also reflected this change due to the fact that many visitors would purchase products online after their self-picking experiences to the orchard. The price for self-picking is 20 yuan per kilo, which is the highest price among all the sales channels, this is because tourists who do not have professional picking skills generated a lot of waste, and picked grapes usually require better packages than those for other sales channels, thus the cost of the activity is higher.

Table 2. Sale Channels of Cooperative A in 2014 and 2017

Sales Channels	Proportion		Price: Yuan per kilo		Source of customers	
	2014	2017	2014	2017	2014	2017
Supermarket	10%	5%	12	10	Zhejiang Province	Huzhou City
Online-Sales	5%	10%	12	15	Huzhou City	Zhejiang, Shanghai
Direct-Sales	55%	5%	7	5	Anhui Province	Anhui Province
Fruit Picking	25%	30%	20	20	Shanghai, Hangzhou	Huzhou City
Wholesale Market	5%	50%	5	4	Huzhou City	Xuancheng City

Source: Based on our field survey in Zhejiang Province in 2018.

Note: The author could not obtain the other members' sales information since there are no unified sales in Cooperative A. The author therefore used the numbers from the director's own production area (based on the director's estimation).

3 Result and Discussion

1) Establishment of cooperatives

The establishment of farmer cooperatives has been influenced by state intervention, as obtaining subsidies from the government is one of the main objectives for farmers to set up cooperatives. There are supporting policies which provide cash rewards or subsidies to newly established cooperatives, or to cooperatives that meet certain criteria. In most cases, these criteria generally concern the scale of the cooperative, including the number of members and size of the production area, the total amount of capital the cooperative owns, the frequency with which technical training courses are organized, and the number of farmers it helps to gain incomes and employment. In addition, the successful establishment of farmer cooperatives is also usually counted as one of the items in the evaluation of performance of local officials in some areas.

2) Governance of cooperatives

Farmer cooperatives are not operated in accordance with the traditional cooperative principals after establishment and there are operational problems, such as the director of cooperatives holding substantial power over other members and the lack of profit distribution mechanisms. The governance of farmer cooperatives relies heavily on personal connections rather than formal institutions. Instead of being owned collectively by members, a study conducted by Liang and Hendrikse (2013) has also showed that cooperatives are actually controlled and owned by their entrepreneurship in terms of

capital investment and authority through the management of cooperatives, whereas common farmers are satisfied to sell their products at reasonable prices. Through the interview with the director of the cooperative and farmers, the authors also found that the majority of common members joined the cooperative only through verbal agreements, which led to the “large-scale” cooperative existing in the name only. The cooperative was actually only operated by the cooperative founder or a small group of core members, which deviated from the “cooperation” principles.

3) Diversified paths of farmer cooperatives

Farmer cooperatives attempt to pursue diversified business models in order to achieve greater benefits (carrying out agritourism and setting up company/fruit stores). Apart from the Cooperative A mentioned in the case study, during our visit in Zhejiang the authors noticed there were also cooperatives setting up “Family Farms”, operating a farmer cooperative and a family farm at the same time. (This change of organizational type will be discussed in the next section). This is because the concept of “Family Farm” was referred to in No.1 Central Document for the first time in 2013. Therefore, local governments started to come up with preferential policies to support the development of the family farm. With regards to local government policies, family farms are treated in the same way as farmer cooperatives after the promulgation of the Farmer Cooperative Law back in 2007.

4) Motivations Behind the Transitions

The establishment of farmer cooperatives was carried out under recommendations from local officials. One director said in an interview, “Locals officials suggested that I set up a farmer cooperative. I then collected identification cards from four of my farmer friends and registered our farmer cooperative, but this farmer cooperative has not really been in operation over the last few years.” Another director said, “In 2001, I used the name of farmer cooperative when I was marketing my oranges in the cities, because I think ‘cooperative’ sounds more formal than individual farmer or small trader. Our cooperative was officially set up in 2005 under the recommendation of local officials. Besides receiving some subsidies such as for machinery from the local government, the cooperative has not really been in operation over the last few years”.

When asked what made them want to establish the company, some believed that products marked with a company brand are able to gain more market recognition than brands from cooperatives. When asked why they transitioned to the style of a family farm, they mentioned the fact that farmer cooperatives are not given very good recognition by banks and credit institutions, mainly due to their loosely-regulated setup conditions. In contrast, family farms have clear property rights, which makes it easier for them to gain access to capital than farmer cooperatives. With more capital available, these farms are able to expand production.

5 Conclusions and Suggestions

Although the statistical data showed that the number of farmer cooperatives in China increased dramatically after the implementation of Farmer Cooperative Law in 2007, there are still a larger number of them that are not functioning properly. Farmer cooperatives were in line with the requirements specified by the Farmer Cooperative Law as well as having a sound organizational structure when registering. However, issues such as core members holding great power over common members and lack of profit distribution mechanisms appeared after the establishment of such cooperatives. The establishment of cooperatives has been influenced by state intervention, as obtaining subsidies from the government is one of the main objectives for farmers to set up cooperatives. The development of farmer cooperatives will go in a different direction once the policy changes.

Farmer cooperatives carry out diversified business models in order to achieve greater benefits, which can happen in two ways: 1. Cooperatives conduct agritourism 2. Cooperatives set up new agricultural companies to open fruit stores. Moreover, the changing of organizational type from farmer cooperatives to family farms, in order to align with new policies, has become increasingly prevalent. On the other hand, what does carrying out diversified business models bring to these farmer cooperatives in the future? Whether or not they will shift from emphasis on agriculture production to retailing and service industries should be taken into consideration.

Our investigation also reveals that most of the cooperatives in Zhejiang Province are

not true cooperatives, rather existing in name only, as they are currently no different from agribusiness companies in terms of their business models and decision-making structures. From the point of the characteristics mentioned above, we think it's proper to call these types of farmer cooperatives as Family-controlled Agribusiness Company-like Entities.

The promotion of family farms in 2013, together with the encouragement and support for the consolidation of household plots being amalgamated into family farms in 2014, has reflected the efforts made by the central government to expand the scale of agricultural production (farm enlargement).

Farmers with larger growing areas or strong marketing abilities have distinguished themselves among small-scale farmers through their intention to integrate into downstream activities, for instance, managers of cooperatives opening retail stores (downstream integration).

Even if the farmer cooperatives are controlled by their respective managers, governance is still centered on managers' family operations. Irrespective of what business models farmer cooperatives apply, cooperatives we have investigated have established companies as well as hiring paid employees. These directors of farmer cooperatives seeking diversified paths could be viewed as a positive response to the industrialization of agriculture brought about in the current environment. Although this method of business may or may not become the mainstream in the foreseeable future, it does, however, exemplify the state of governmental guidance for agricultural production at present.

Local governments are inclined to align with the policies implemented by the central government regarding support for the development of agriculture. Local government is embracing an approach that views local companies, farmer cooperatives and capable entrepreneurs as the carriers of policy implementation. However, there are instances that show that many support policies lead to quality negligence in pursuit of speed of production or come to an untimely end due to personnel changes. For instance, government officials accused of embezzlement or subsidy fraud have either been dismissed or are under ongoing investigation, which is not considered to be an isolated phenomenon in Zhejiang Province. Nevertheless, more consideration must be given to the sustainable development of agriculture rather than simply offering temporary support.

In addition, the case study also exemplifies the present guidelines of government policy regarding benefiting both producers and consumers of agricultural products through nurturing new types of agribusiness entities. However, in order to be more competitive, these agribusiness entities should pay increased attention to establishing brands and reputation for quality over quantity, especially under the strategy of rural revitalization.

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