Agricultural Cooperatives as a Form of Diversification

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As I discussed in my last newsletter, agricultural cooperatives can be viewed as an extension of the farm firm. That is part of the justification for the cooperative to retain profits to re-invest in the cooperative. Those investments allow the members to reduce input costs and/or improve marketing opportunities relative to what the member could do on their own. Because today's agricultural cooperatives are complex organizations it is impossible for every member to use every aspect of the cooperative. That leads some members to complain that the cooperative is diverting profits for its own separate objectives. Just like government, we are all in favor of the services that we use; we just wish they would discontinue everything else! The missing element from that thought process is that agricultural cooperatives are also a source of diversification for their farmer members.

A member of an agricultural cooperative owns a small portion of an agribusiness firm. When that firm is supplying them with inputs or marketing their specific commodity, the cooperative is acting as an extension of the member's farming operation. When the cooperative firm is performing other services it is still creating profits that flow to the members. Many cooperatives operate on a single patronage pool so those benefits flow directly. Even when there are separate patronage pools, the diversified areas of the cooperatives help to spread fixed costs and benefit all members. Most farming operations are by their very nature specialized. That makes the diversification effect of cooperative patronage particularly beneficial.

As in any activity of the cooperative, diversification is beneficial when the business areas are profitable and generate returns commensurate with potential risks. The pros and cons of diversification in corporate firms has been extensively debated and researched. The consensus conclusion is that diversification is beneficial when the new business area aligns with the key competencies of the firm. When considering diversification, cooperative boards shouldn't just ask themselves "is this something we can do?" instead they should ask "is this an area where we have a competitive advantage?" Diversification works best when it allows the cooperative to utilize existing technology, expertise and competencies in another market area. Strategies to create integrated solutions and services for farmer members often further diversify the cooperative.

Members generally benefit either directly or indirectly when the cooperative does not have all of their eggs in one basket. We just need to make sure there are no rotten eggs in the new basket!

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