

Financing of Co-operative SocietiesSURVIVAL - THE NAME OF THE GAME?

by

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A copyright claim could not be laid to the title of this article - it was born out of a recurrent comment of many Co-operative Managers who kindly gave some of their valuable time to inform me about current problems and practices within the Co-operative Movement. Their acute awareness of the Movement's struggle for survival as a major retailing organisation was apparent in discussions and for the insight which they tried to give me to the Co-operative Movement and its present problems, I owe them my gratitude and would express to them my sincere thanks.

Concern

Over the past few years, considerable concern has been expressed in Co-operative publications and comments have been made in the national press about the Co-operatives' share of the retail trade of this country. Nielsen's survey, reported in "Marketfact" of 5th July, 1979, showed that the Co-operatives' share of Grocers' sales over the period 1974-1978 averaged 13.7% whilst over the same period, the share of the multiples

averaged 49.5%. The percentage increase in Grocers' Sales between 1977 and 1978 was 10.1% for Co-operatives against 15.3% for multiples. Both the market share and the percentage increase in sales are below the level which would be desired by the Co-operative Movement.

Garth Pratt, writing in the "Co-operative Review" of August 1979 outlined many of the problems currently facing the Co-operative retail movement and pinpointed capital expenditure as one of the major problems pointing out that as compared with capital expenditure by Co-operatives "investment by private retailers was much more formidable".

It was revealed that only a satisfactory net surplus level would provide, within the Movement, the reserves which were so essential if funds were to be built up to form the basis of an investment programme. Without such surpluses, where might Co-operatives turn to obtain the type of finance necessary to support an investment programme which would enable the retail Co-operatives to continue to play their role as a major and competitive consumer organisation?

The Future Role of Retail Co-operatives

The question of capital expenditure cannot be divorced from that of capital acquisition and utilisation.

Before analysing these factors, it would be advisable to examine some of the basic philosophies of the Movement and ask, are these basic philosophies to be adhered to in the future or do they require to be reconsidered in the light of current practices?

The principles advanced by Robert Owen were: the abolition of a system of private profit; production for use by voluntary associations of consumers; common ownership of the means of production by the voluntary accumulation of the profits of combined enterprise; the utilisation of the wealth of the community for the improvement of the character and happiness of mankind. How far in the struggle to keep alive the Co-operative retail structure, does present practice relate to these basic principles? The second and third of the basic principles would appear to be more applicable to manufacturing Societies than to retail Societies. As far as the first principle is concerned, can those who manage retail Societies honestly say that they subscribe to the principle of the abolition of private profit? Within the Co-operative Movement, more and more one hears the term 'profit' rather than the term 'surplus' being used. Are Co-operative Societies now seeking blatantly to become profit making organisations and, if so, could it not be argued that the collective membership merely constitutes another private body in the general retailing sphere of the country?

Have we now come to the stage where at top management level a selection has been made of one of the possible chief aims advanced in the conclusion of "Consumer Co-operation in Great Britain" by Carr-Saunders, Florence and Peers, viz: "It is for others to work out in practice what the future of the Co-operative Movement is to be - either a reasonably efficient large scale business aggregation or a new system of economic organisation". If it has been decided that the Co-operative retail organisation aims to be "a reasonably efficient large scale business aggregation", then in terms of current competition it will require to be more than reasonably efficient for there are signs that the high degree of competition in the retail trade is not going to diminish in the foreseeable future. Can it be said that one of the major aims of most retail Societies today is to meet the fourth principle? If this were the case, then the second of the Carr Saunders principles would be advanced and energies would be devoted to creating "a new system of economic organisation". However idealistically desirable these aims may be, in practice the survival of retail outlets is dependent upon their ability to attract customers who exercise effective demand for without customer support any possibility of making a surplus or profit vanishes and, therefore, finance cannot be available for the implementation of ideals. In the retail trade, possibly more than in any other area, the effective demand of the cash customer must be wooed - no longer can loyalties be taken for granted.

Members - Customers?

In the early days of Co-operation, membership of and loyalty to the Societies was attracted through the existence of dividend based on the purchases of the members. These dividends, which were frequently allowed to accumulate, often provided a valuable means of saving from a very tight budget. In the period from 1950, dividend has almost ceased to exist and has been replaced in some areas by trading stamps but now, as more and more large stores are opened, the trend is towards simply cutting the prices of the goods. What problems have these changes brought about for retail societies and what further problems are likely to follow?

First, in many Societies, members now see no advantage in sticking loyally to the Co-operative shop.

There are clear signs that housewives have reverted to "shopping", are no longer content to give loyalty to any one shop or organisation but now seek what they believe to be the best value for their money.

In this competitive climate, how does a Co-operative retail Society hope not merely to retain its membership but to increase that membership and turn it into a body of people who support Co-operative stores by spending their money in the stores.

In all the publicity which has appeared recently, there has been a notable absence of information about the benefits of membership of a Co-operative Society.

In some areas where trading stamps have been totally abolished benefits available to members may well be available to any customer. This question of membership is vitally important, for the basic capital of most societies is subscribed by the members. This basic capital generates the initial activity and only after the activity has been successfully established can there be supplementation of capital by reserves or loans.

Problems in attracting members may not be due solely to the apparent decline in the benefits of membership but may come from the ideologies of the Movement. To many potential customers the idea of membership might be repugnant as the Movement through the Co-operative Party is allied to the Labour Party. Having regard to the political structure of the country manifest in most post-war general elections, it could be expected that many people who do not support the Labour Party, would not wish to bring trade to a Co-operative Society and would certainly not consider becoming members of such Societies. The extent to which the political tie of the Co-operative Party with the Labour Party reduces the number of potential members and therefore the amount of capital available to the Movement, would be difficult to determine,

but it could be a vital factor to retail Co-operative Societies who seek to increase their share capital by increasing the numbers of their members.

Problems of Financing Retail Societies

A look at the balance sheets of retail Societies reveals three items which feature prominently under the heading Sources of Capital: Share Capital, Reserves and Loan Capital.

Share Capital. This item accounts for anything between 20% and 50% of total funds. It is capital contributed by members, is affected by the numbers of members and may be withdrawn virtually on demand. To increase the amount of share capital coming into an organisation obviously something must be done to increase the numbers of members or to persuade existing members to commit more of their cash to the share capital of the Societies. In "Co-operative News" of August 22nd, 1979, Mr. Edgar Evans in his article "Co-op. Great Britain Ltd." posed the question "What about the shareholders?" and provided the answer "For all of them dividend would be based on their capital holding". The withdrawal facility creates a lack of permanency in the capital structure and can bring some real headaches to managers of Societies. To try to introduce a more stable position, today some Societies sell Bonds on which a stated fixed return is given. This practice is not without its problems for

it means that Societies which operate in the Bond market must somehow ensure that they have available sufficient funds to meet the interest as and when it falls due. A further problem arises here in that the return given on such Bonds should be at a rate of interest similar to rates being offered by other organisations - in particular one thinks of the SAYE scheme where the rate of return is guaranteed, is not dependent on the selling organisation making a surplus and carries an exemption from tax liability on the interest accruing to the Certificate Holder.

If there were to be widespread attempts by Co-operatives to raise capital by Bonds, it might be better if only one organisation were to sell the Bonds and in this respect perhaps the projected Co-op - Great Britain Ltd. could undertake the task with profit to the whole Movement. If Societies were to operate independently in raising capital via bonds, it might be extremely difficult to provide "umbrella" cover to assist weak Societies who either over-reach their trading capabilities or who simply go through a bad patch. Once Co-operatives operate widely in the Bond Market they acknowledge that the average person who invests money in an enterprise does so partly for the return on his capital, partly for the security which certain investments seem to offer, and today partly in the hope that the return will help to hedge against the ever present inflation.

Reserves. These funds, built up from the trading surpluses, may be utilised for fixed investments in the form of land and buildings, fixed assets such as machinery or equipment, investments which will bring in a return (these may be placed inside or outside the Movement) and for providing working capital. It seems to be the general practice to hold these within the Movement but there are signs that Societies are investing part of their reserves outside the Movement. When a Society undertakes a major capital project and finances this project from reserves it may become more vulnerable to the highly liquid situation which could arise if members suddenly start to withdraw their capital. Linked to the Reserves there may be Superannuation Funds which, if retained within the Society, operate in assisting the funding of activities. The retention of such funds could be a potential danger to the contributors to the funds if the Society should suffer set-backs. Under the present structure of the Movement, it would be expected that in such an eventuality, other Societies would carry out a life-saving operation. Such an operation would be more effectively carried out if there were one national body organising the funds on a central basis.

Loan Capital. The proportion of Loan Capital varies from one Society to another, ranging on average from 20% to 30% of total funds. In most cases, but not all, this money is borrowed at fairly low rates of interest from the Co-operative

Bank. Some Societies do borrow from private banks but as the rate of interest is usually higher than that of the Co-op Bank, this method is not widely employed. Some successful Societies which have accounts with a Joint Stock Bank may be able to have overdrawing facilities and in this way interest is payable only when the account is overdrawn. The existence of these facilities can bring to a Society a measure of resilience, for the facility can be used if it is needed and, if it is not needed, there is no charge.

Working Capital

Capital is required not merely to finance large projects but also to cover the day to day running of the organisation and great care must be taken to ensure that this capital is not held too long in one area of operations. This means that strict control must be kept on stock levels, on all accounts due and on expenses. This is particularly important in a situation of high inflation. Under Working Capital, may be considered "Rolling Liabilities", ie, funds which are held within the business for short periods but which must be paid out at a specified time, eg, various taxes and insurance payments. As the sums to cover Rolling Liabilities may be very large, it may be possible to enter the lending market and put these funds into use as "Day" money thereby receiving some return on the amount held.

Working Capital may be slightly augmented by utilising fully the credit facilities accorded to the organisation by its creditors and by linking this usage with a reduction or at least a very strict control on the length of credit which would be allowed to the Society's debtors. In this area of credit control, there appears to be little use made by Co-operative Societies of the system of Factoring. This system may cover not only a Factor taking over the book debts of the organisation but also taking over all the paper work associated with these debts. While Factoring may increase the cash flow, in general Factors are willing to take over the debts of organisations which have a fairly large turnover and usually charge a fee between $1\frac{1}{2}$ - 2% of total debtors. As Factoring undoubtedly saves the cost of paper work and ensures that Societies, at a cost, may have their debtors translated into ready cash, it might be beneficial if the Movement were to set up its own Factoring system. If such an organisation were introduced and linked to modern accounting and controlling techniques, it could provide a valuable central service to Societies.

Conclusion

To keep pace with the giants of the retail trade the Co-op Movement must clearly set its objectives bearing in mind the severe competition and falling margins which currently exist in retailing. Capital expenditure has been shown to be vitally necessary and the Movement will hope to raise internally as much of its required capital as it possibly can.

To achieve this aim, earnest consideration must be given to methods of attracting members and to persuading both members and non-members to increase their trade with Co-operatives. Some way of introducing a degree of permanency into the capital structure must be sought to try to introduce greater stability into the funding of Societies. Full use should be made of modern control techniques to ensure that cash flow problems are reduced to a minimum. In order that surplus may be achieved to provide the reserves necessary to finance expansion, methods of improving turnover must be found.

All these problems relating to finance, turnover, expansion lead us back to the vital question - is the high pitched degree of activity necessary to ensure the survival of Co-operatives in the retail sector, a sign that modern Co-operatives are merely "large scale business aggregations" and, as such, must adopt business methods similar to those of their competitors?