

# Agricultural Cooperatives in Japan: An Institutional Approach

by

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## Abstract

How can we explain the reason why cooperatives have evolved so differently? This article argues that the institutional framework gives a decisive influence in organizational evolution and the historic path has been taken by interaction between institutions and organizations. The Japanese agricultural cooperatives are analyzed from institutional perspectives. They were created at the end of the 19<sup>th</sup> century under overwhelming European influence but evolved as a quite different model under the strong impacts of industrial policies and institutions. They developed as multi-purpose cooperatives bearing triple natures as state agency, pressure group and cooperative per se. The new economy is shifting public policy from protectionist to pro-competition and the resulting institutional changes are posing challenges to cooperatives. Their future depends on their willingness to innovate themselves by adjusting to the new environment while applying cooperative advantages.

## Introduction

Cooperative organizations throughout the world have demonstrated a vast diversity by regions, countries and sectors. They are so heterogeneous that it is hardly possible to make the meaningful comparison without applying appropriate methods, although the Co-operative Identity Statement of the ICA may serve as a common denominator. How can we explain the reason why they have evolved so differently? It can be attributable to the diverse cultures and ideologies. But even within the same countries we can observe stark contrast in the evolution and the nature of cooperatives.

The institutional framework has a fundamental influence on the formation and the evolution of organizations that have to operate under given sets of rules. In fact, the historical evolution has witnessed the interaction between institutions and organizations. The institutions include the legal and administrative system and pervasive practices. They are influenced by the socio-economic policy and culture.

This article analyzes the Japanese agricultural cooperatives from an institutional

perspective. They have been created at the end of the 19<sup>th</sup> century under the overwhelming European influence but evolved to be quite a unique and different model. They have grown as multi-purpose cooperatives bearing triple natures as state agency, pressure group and cooperative per se. The institutional arrangements and state's industrial policies have heavily affected such an evolution, as they were dependent on agricultural policy and developed strong lobbies. As a result, they have quite different membership, governance and management systems, structure and functions in comparison with their counterpart in the industrial countries.

The new economy is causing a drastic shift in the policy direction from protectionist to pro-competition since the global economy and IT revolution is dismantling the existing boundaries and barriers among nations and industries. The institutional framework is also changing through the liberalization of trade and deregulation of industries, posing unprecedented challenges to cooperatives. It is up to them whether or not they will tap the opportunity by adjusting to the new environment while making use of cooperative advantages.

### **Institutions and organizations**

A vast diversity is a prominent feature of cooperative organizations in the world. They have been created by people to meet their common needs at the grassroots level and in many cases grown organically into regional or national movements. Although they have been influenced by some ideas and experiences originated elsewhere, they have evolved to be quite distinctive organizations in different countries. They have taken diverse development paths in different sectors even in the same country. So we need to apply appropriate methods to understand them and make meaningful comparisons among them.

How can we explain the reason why cooperatives have evolved so differently? It can be attributable to the diverse culture dominating them and ideologies held by their founders and leaders. The collective work in "Consumers against Capitalism" explores the historical analysis of consumer co-ops in 10 industrialized countries from a cultural perspective (Furlough and Strikwerda, 1999). It describes how consumer co-ops have developed the prominent working class culture as one of three pillars supporting the labor movement in the late 19<sup>th</sup> and early 20<sup>th</sup> centuries but could not sustain it in the wake of the emergent capitalist culture based on ideology of "consumerism", which became individualistic, acquisitive and oriented toward notions of pleasure and desire. It explains why they could not adapt to the new environment brought by mass production and a mass consumption system, and attributes their incompetence to the cultural-ideological constraints of leaders. That is surely part of the reasons but there would be other factors associated with the profound socio-economic transformation. Especially the traditional links with the labor and trade union movements have almost completely withered in the post-war era (Bir-

chall, 2001) when some consumer cooperative organizations have accomplished impressive success in some countries whereas the others have shrunk or collapsed. So a wider perspective is needed for a more comprehensive understanding.

Another collective work in “Agricultural Co-operatives in the European Union” sponsored by COGECA offers a comparative study of agricultural co-ops in 15 EU countries (van Bekkum and van Dijk, 1997). It describes the position of agriculture in the national economy, the brief history and statistics of cooperatives, and compares their structure, membership, capital formation, taxation, R&D, marketing and internationalization. It distinguishes two main solutions to improve the effectiveness of co-operatives for the future; the countervailing power cooperative model (*e.g.*, wheat pools) and the entrepreneurial cooperative model (*e.g.*, new generation co-ops). The former is based on the economy of scale attained by pooling bargaining power but increasingly facing the stiff price competition resulting from trade liberalization, while the latter promotes product differentiation and consumer loyalty through forward integration into value-added activities but requires changes in legislation for its development. Finally it suggests that the European Commission should induce member states to adopt the competition law setting common rules at the EU level, work on harmonization of legislation on the cooperative business form and enact the European Co-operative Statute.

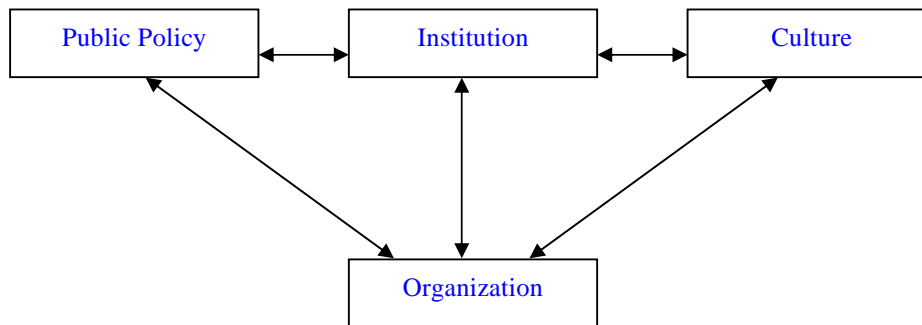
In the light of the institutional perspective underlying this article, the new institutional economics shows that institutions matter in the evolution of organizations. Institutions are “the rules of the game in a society or the humanly devised constraints that shape human interaction” (North, 1990). They include both formal constraints (legal and administrative system, contracts, etc.) and informal ones (conventions, codes of conduct, etc.). The institutional framework fundamentally influences what organizations come into existence and how they evolve. In turn, organizations influence how the institutional framework evolves. Organizations are created in the wake of opportunities resulting from the existing sets of constraints, and in the course of attempts to accomplish their objectives become a major agent of institutional change. Institutions affect the performance of economies, and different performance over time is explained by path dependence. They give fundamental influence to organizations’ economic and social performance, both positively and negatively.

The comparative institutional analysis seeks to explain why the economic systems have not converged into the Anglo-American system, which is often seen as a universal model by the mainstream neoclassical economics, but have rather evolved differently in Europe, Japan and other regions, suggesting plural evolutionary equilibriums (Aoki, 1995, 2001). The analysis aims to find sources and conditions generating “the gains from diversity” using universal tools of analysis. It also suggests “institutional complementarities” in that some institutions are reinforced by others, which means that they become stronger against the environmental changes. For example, the Japanese corporate governance system is compatible with contingent monitoring of main banks and lifelong employment while the American system is based on principal-agency theory (shareholders controlling managers to maximize

share values) backed by corporate control market and external labor market.

Institutions are also influenced by the public policy on the one hand, and culture on the other. Especially the change in socio-economic policy surely induces the transformation in institutions; *e.g.*, the shift to pro-competition policy will lead to abolition of rationing or quota system. Even the changing culture may result in changes in regulations and norms of behavior; *e.g.*, increasing tolerance to smoking marijuana led to its legalization in The Netherlands. These elements also contribute to deciding the historical path of organizations. But the emphasis here is on the interaction between institutions and organizations, while the public policy is also analyzed as a determinant factor changing both of them.

**Chart 1: Interaction between public policy, institution, culture and organization**



### **Institutional framework of cooperatives**

The institutional framework of cooperatives is composed of the specific cooperative legislation, administration and convention, which directly influence the cooperative behavior. However, the wider socio-economic institutions also place the constraints and rules under which cooperatives operate. Being economic enterprises, they have to comply with competition laws and various socio-economic regulations. Institutions and public policies aiming at promoting specific industries are also affecting the cooperatives.

The cooperative legislation includes both statute and common laws. It may be backed by the provisions in the Constitution. It constitutes the overall framework of the cooperative activities, but the extent of constraints varies from one country to another. It can be neutral to any organizational form and give equal treatment to cooperatives as seen in most of industrialized countries. It can favor cooperatives by allowing a supportive treatment in taxation and subsidies while placing them in the strict control as in the case of many developing countries. It can be restrictive by

prohibiting some areas and modes of operations (Japan, Korea, etc.). The single cooperative laws covering all sectors are adopted in many countries while the separate laws are in effect to supervise specific sectors in other countries. In the latter case sectoral cooperatives tend to take different paths of evolution. In some countries there exist no separate legislation for cooperatives, which are regulated by the general civil-commercial laws (Denmark, Switzerland, etc.). The model bylaws are provided to help societies to make their own bylaws or rules.

The administration system concerning cooperatives demonstrates even greater diversity. The cooperative ministries or registrars in the developing countries have exerted the overwhelming power for almost all aspects of cooperative activities, including management, capitalization, auditing, education and training. The governments that have seen cooperatives as the engine for development policy have provided promotional measures and imposed strict regulations. In contrast, the function of juridical bodies concerning cooperatives is generally confined to the general supervision in the industrialized countries but can include various extension services when the governments seek to utilize cooperative channels to promote the public policy as often seen in the agricultural sector. Cooperatives are also subject to the regulations made by relevant authorities, *e.g.*, cooperative banks are often supervised by the ministry of finance. The taxation system also constitutes an important framework for cooperative activities.

The convention and tradition also shape the institutional framework. The traditional community ties in villages, often reinforced by ostracism, have been conducive to foundation and continuation of agricultural cooperatives. The common bond nurtured around communities, workplaces or religions have been the driving force in creating credit unions. The preference for collective action to individual choice might be seen in the Asian values motivating cooperation. This helped Asian cooperatives to run business based on traditional groups, but their performance was a mixed one. The dominant gender bias in the society has discouraged women from active participation although they constituted the bulk of farmers and consumers who use cooperative services. The pervasive practices in labor relations, education and employment are also affecting the cooperatives.

The competition laws and socio-economic regulations also influence cooperative activities. The voluntary agreements on fair competition in each industry supplement the legal enforcement. The cooperatives are often seen to exert the countervailing power by organizing small producers or consumers against monopolies and promote competition. So, they are exempted from cartel prohibition as in the case of the Capper-Volstead Act (USA) of 1922 or the Anti-Monopoly Law (Japan) of 1947. But even in that case cooperatives are not allowed to use unfair transaction methods or raise price by restricting competition. Had they grown so as to exert market power, they could be questioned on seller's monopoly or buyer's monopsony. Cooperatives are also affected by economic regulations for eliminating new entries where state monopoly or licensing exist for some products and services (liquor and cigarette, staple food, utility, and so on). Social regulations concerning consumer safety and labeling, labor

standards, environmental protections, etc., are applied to all organizations irrespective of their legal forms.

The industry-related regulations have the strong influence where the economic policy tries to promote or protect the specific industries characterized by lower productivity. Especially the strong agricultural policy has given the major influence to the structure and behavior of agricultural cooperatives in many countries. The restrictive commercial policy aiming at protecting small retailers has also influenced consumer cooperatives in some countries.

### **The case of multi-purpose agricultural cooperatives**

Cooperatives in Japan started at the turn of the 19th century under the overwhelming European influence. As Johnston Birchall pointed, after the first attempts at modern cooperation in the Asia-Pacific region made in Australia around the 1860s, cooperation came next to Japan (Birchall, 1997). By the end of the century there were around 450 agricultural cooperatives, which were organized along Raiffeisen lines. The Industrial Cooperative Law was enacted in 1900 after German legislation. However, the Japanese cooperatives have evolved along a quite different model, the multi-purpose agricultural one. The hypothesis that the institutional framework has contributed to the evolution of a unique cooperative model is to be tested hereafter.

#### ***The industrial cooperative law of 1900***

The *Industrial Cooperative Law* was enacted by the government aiming to improve productivity and help farmers to counter moneylenders. It had the paternalistic elements reflecting the top-down approach initiated by bureaucrats. The cooperatives had been placed under almighty government control; the governor could give permission to their establishment, suspend or dissolve them, order reporting at any time, make inspection, reverse the resolutions of general assemblies and order reelection of office bearers. The Law was all embracing; it governed credit, marketing, supply and production (later replaced by service co-ops), and allowed the multi-purpose model. It mainly targeted to serve agricultural co-ops in the rural area but also covered credit and consumer co-ops in the urban area.

The state had vital roles in promoting and regulating cooperatives. The rural industrial co-ops had been set up in all villages around 1920 and covered all farmers in the 1930s. Organizationally they had taken over the character of villages based on both territorial and vocational homogeneity of farmers, resulting in almost compulsory membership. More importantly they were largely dependent upon government's direct assistance for creating cooperative federations and the Central Industrial Co-op Bank as semi-governmental organization. They were used as the agency for implementing government's agricultural policy. For example, they took the merchants' share in rice marketing as the government intensified its control of distribution and

price by the Agricultural Warehouse Law of 1917 and the Rice Control Law of 1933. Likewise the MAFF (see f.n. 1) Ordinance for Improving Fertilizer Distribution of 1930, which prioritized cooperative channels, enlarged their handling of fertilizer at the expense of merchants. To save farmers from bankruptcy under the rural recession by providing low-interest loans to replace the high interest usury, the government money was channeled through the Central Industrial Co-op Bank and primary co-ops according to the criteria set by the MAFF.

Thus rural industrial co-ops were integrated as part of a government system for implementing the agricultural policy while they came to organize almost all farmers and had the capacity to lead them. At the same time, their growth had induced the anti-co-op campaigns by rural merchants around 1930. In this period they started developing the prototype of multi-purpose co-ops covering the four functions of credit, marketing, supply and service as they took over the economic activities from rural merchants. But it was after the Great Depression that industrial co-ops became important players in the rural economy. The proportion of multi-purpose co-ops consolidating four functions rose from 31 in 1932 to 71 percent in 1937. However the potential of multi functional operations was not fully realized since landlords and tenant farmers had not necessarily have homogeneous interests and there were often conflicts between them. The former had often dominated the cooperatives while the latter had sought to take over the leadership.

The other root of agricultural co-ops was farmers' associations organized under the Farmers Associations Law of 1899. They were created de facto compulsorily in all villages to channel government subsidies for introducing modern technologies and facilities aiming at increased productivity and self-sufficiency when Japan was moving to import rice. From the beginning they were not spontaneous associations but parastatal organs to implement the agricultural policy as a branch of the MAFF.

During World War II the whole agricultural sector was reorganized into the state body to strengthen the control of farmers aiming at increasing food production. The *Agricultural Organizations Law* of 1943 integrated rural industrial co-ops, farmer associations and other farmer organizations (livestock, sericulture and tea growers co-ops). With this, industrial co-ops became the wartime mobilization mechanism for controlling farmers with compulsory membership, completely losing a residual cooperative character.

### Separate legislation and transition to agricultural cooperatives

The end of World War II opened a new way to the cooperative legislation; separate legislation was introduced under the American Occupation in 1945-1951. In this period the General Headquarters (GHQ) of the Occupation Army ruled Japan aiming at demilitarizing it and transforming it to the democratic state in accordance with the Potsdam Declaration of 1945. In the economic arena it introduced the key democra-

tizing measures; dismantling the *Zaibatsu* (financial combines controlled by core families) by the Anti-monopoly Law of 1947, legitimating the trade unions by the Trade Union Law of 1945 and the agrarian reform by the Land Reform Law of 1946.

The process of cooperative legislation was part of such an overall transformation and heavily influenced by so-called New Dealers who were seeking economic democracy. The Anti-monopoly Law (Article 24) exempted certain cooperatives from its application except for the restrictive trade practices, following the example of Capper-Volstead Act of 1922. Such co-ops should be established based on the legal provisions and meet four requirements: a) aiming at mutual benefits among small producers or consumers; b) voluntary and open membership; c) equal voting rights for each member; d) limited compensation when distributing surplus. Thus the Anti-monopoly Law defined the criteria for Ideal-type cooperatives to be applied to all kinds of co-ops.

The *Agricultural Cooperative Law* was enacted in 1947 after the agrarian reform was introduced. As early as December 1945, General MacArthur of the GHQ issued a Directive for Farmers Liberation to democratize rural economy by liberating farmers from landlords exploitation and government controls which had brought the poverty-stricken villages to be attributable to Japan's militarism and expansionism. The former objective was achieved by Agrarian Reform while the GHQ intended to realize the latter by dissolving the Agricultural Organizations and establishing the agricultural cooperatives anew, based on democratic principles. The law was redrafted several times in the light of the differing opinions between the GHQ and the MAFF; the former insisted to separate the credit business from other businesses like in other industrialized countries while the latter persisted in maintaining the multi-purpose model. Finally, the GHQ made concession and the Law was enacted. In the process of transformation in 1947-1948 the MAFF took the measures called "comprehensive succession"; properties, offices, boards and employees of the Agricultural Organizations were taken over by multi-purpose agricultural co-ops. In 1948 ca. 17,000 Agricultural Organizations had been transformed into more than 22,000 agricultural co-ops and 400 federations. Thus the agricultural co-ops had inherited the basic character of the industrial co-ops as the state agency. This process resulted in lack of consciousness that farmers should spontaneously set up their co-ops; for many of them the signboard was changed to co-ops overnight. What is more, the Ministry continued to favor the multi-purpose model and to authorize only one co-op in one area on the ground that competition among many co-ops could weaken their financial basis. This measure has led to the territorial monopoly, depriving farmers of the choice. In 1948 the national federations for guidance, marketing and supply were formed and finally the Central Union of Agricultural Co-ops (CUAC) was set up as the apex organization in 1954. Moreover, agricultural co-ops had been assisted by the state through rehabilitating and promoting measures *i.e.*, laws for rehabilitating ailing co-ops (1951), creating federations (1953) or promoting mergers among co-ops (1956, 1961).

In this period the other cooperative laws were separately enacted to serve the specific needs of co-ops in other sectors: The Consumer Co-op Law of 1948 for



consumers, the Fishery Co-op Law of 1948 for fishermen/marine product industry, the Small & Medium Enterprises Co-op Law of 1949 for small businesses, the Credit Bank Law of 1951 for urban businesses, and the Labor Bank Law of 1953 for workers, etc. Such separate legislation has given great impacts to cooperative organizations; it has driven co-ops to take quite different paths, which made it difficult to conduct the joint actions and formulate the common strategy. The separation of regulatory bodies has contributed to divergence, often spurred by the sectionalism of the ministries.<sup>1</sup> The other problem is the legal vacuum for the newly created co-ops including worker co-ops, hybrid co-ops, etc.

### *Agrarian reform and land ownership*

Some institutional frameworks have influenced the evolution of agricultural co-ops. First of all, the GHQ urged the Japanese government to undertake the Agrarian Reform, which created a large number of landed farmers by redistributing landlord's estates and split land ownership into small farms in 1946-47. As a result, large-scale and absentee landlords had disappeared while emergent owner farmers had more homogeneous interests in joint actions and their needs could be conveniently met by all-embracing services provided by multi-purpose co-ops. The *Agricultural Land Law* was enacted in 1952 to protect owner farmers by placing various restrictions to the transfer of land; restricted lots' space for ownership, prohibition of absentee landlords, controlled rents for tenants and permission required to cancel leasing contracts. It also confined farmland ownership to farmers and did not allow corporations to enter. These restrictions contributed to maintaining small ownership of land while hampering the expansion of farms' scale through concentration of land use and/or ownership to entrepreneurial farmers.

In addition, the rapid economic growth triggered skyrocketing of land prices to the extent of prohibiting farmers to buy at earnings discounted price while farmers in suburban areas could become upstart millionaires by selling land after getting permission for conversion from cultivation to other development purposes. Since the cost of ownership for farmland was very low in terms of property and inheritance tax, farmers chose to retain land expecting a huge gain in the future. These factors have contributed to the delay of concentration of land to viable farmers and retention of part-time farmers. The law was amended several times but could not reverse such trend. Agricultural co-ops pursued an egalitarian approach and tended to maintain a current structure based on owner farmers, reflecting interests of part-time farmers as against entrepreneurial farmers, and strongly opposed new entries from the non-agricultural sector, especially joint stock companies. Thus it can be said that they contributed to status quo in land ownership.

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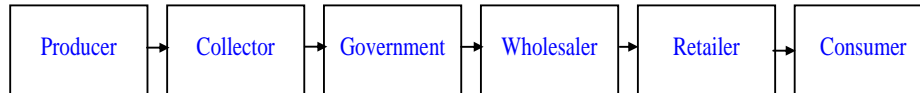
<sup>1</sup> Ministry of Agriculture, Forestry and Fisheries (MAFF) for the first industry co-ops, Ministry of Health, Labor and Welfare (MHLW) for consumer co-ops, Ministry of Finance (MOF) for credit co-ops and labor banks, and Ministry of Economy, Trade and Industry (METI) for SME co-ops, etc.

As a result, the land ownership remained small (on average 1.5 hectare per farm), which largely inhibited rationalization and mechanization. While farmers' overall standard of living had been enhanced thanks to off-farm incomes and their income had surpassed workers' income in 1970, the productivity of agriculture was not improved as expected by the *Agriculture Basic Law* of 1961. The diversified diet of consumers accompanied with westernized lifestyles resulted in the sharp increase of import of food and fodders. As a result, the food self-sufficiency rate on calorie base has dropped substantially from 79 percent in 1960 to 40 percent in 2000.

#### ***Stable food control system and institutional credit system***

The stable food control system has also constituted an important institutional framework. The *Stable Food Control Law* was enacted in 1942 to control the production and distribution of staples such as rice, wheat, and so on, under the wartime economy, in which they were wholly collected and rationed to cope with the severe shortage of food during and immediately after the war. This system had provided for the institutional framework of controlling price and quantity of staple food as well as a distribution channel. The government bought all the crops in the initial stage, set prices and margins for buying, wholesaling and retailing, and controlled the entire international trade. The distribution channel was fixed to a singular line from farmers to consumers, leaving no room for choice (Chart 2). Agricultural co-ops were assigned as sole collecting agents; from primary co-ops to provincial federations and national federation (Zen-no). Only licensed wholesaler or retailers could deal with staples. When the urgent food crisis was overcome and the oversupply became the major problem since the 1960s, it was modified to accommodate more market mechanism, but the basic idea was not changed.

This system has brought some significant effects on agricultural cooperatives. First of all, farmers pressed the government to raise rice price beyond equilibrium while the higher price stimulated the overproduction. Cooperatives strongly mobilized farmers to rice price campaign in parallel with trade unions' drive for higher wages since the 1960s but soon had to cooperate with the government's program of cutting back on the acreage under cultivation. Secondly, the raised price helped marginal farmers to remain in unprofitable farming, which might otherwise resist. They were employed in factories and other businesses to earn a living and constitute a bulk of cooperative membership. They were concerned with multiple services provided by co-ops, rather than competitive marketing capacity. Thirdly, cooperatives became almost a monopoly in collecting government controlled rice and commanded nearly 30 percent of wholesales. They could automatically earn handling charges and deepened dependence on rice distribution as a mainstay of marketing business. Zen-no (National Federation of Agricultural Co-ops) exerted decisive power in maintaining higher price in the quasi market for rice price. As such, cooperatives contributed to the continued existence of food control system for more than 50 years.

**Chart 2: Distribution channel of staple food**

The character of co-ops as a state agency is more apparent in their credit business. The MAFF developed two kinds of “institutional credit systems” since the middle of the 1950s. One is the credit of the Agricultural Finance Corporation, which gives public funds’ long-term loans to farmers at low interest rate where the whole business in contacting the debtors is entrusted to agricultural co-ops. The other is the co-ops’ credit for Agricultural Modernization, *i.e.*, the low-interest loan (with part of the interest being subsidized by the government) which sets the terms of loans while leaving co-ops only to handle the administrative work. This meant that they were deprived of autonomy in making use of their own funds, thus becoming the state’s subcontractors.

In short, agricultural cooperatives have been involved by the state as a major player for implementing agricultural policies through various legal-administrative measures and subsidies/loans, ranging from the macro policies such as the price maintenance scheme covering more than 90 percent of farm products; the selective expansion/reduction of production; the financial stabilization scheme; the reform of farming infrastructure, etc., to the micro policies such as modernization of farm facilities. The co-ops have been often designated as the sole agent to implement the promotion measures. They have also acted as subcontractors to channel the public money to farmers. Thus they have been “institutionally” ensured to benefit from promotion measures and subsidies.

Such commitment with the public policies has given another dimension to the co-ops as one of the strongest pressure groups. As the farmers’ income was largely dependent on the agricultural policies, they became very active in pressing the government to raise the controlled prices for rice and milk and stop the liberalization of agricultural imports. To attain such objectives, they organized from time to time nationwide campaigns, often mobilizing thousands of farmers. In the national/municipal/local elections they sponsored MPs who could represent their interests in the parliament/councils and press the government. Taking these factors into consideration, it is argued that the evolution of agricultural co-ops has resulted in the three-fold combination of state agents, pressure groups and co-ops per se (Fujitani, 1992).

#### ***Evolution of the multi-purpose model of agricultural cooperatives***

The multi-purpose agricultural cooperatives undertake multiple functions such as marketing, supply, finance, farming guidance and other services in the same organization while single-purpose agricultural co-ops are specialized in one function. The desirability of multi-purpose versus single-purpose co-ops has been often propagated

(Watkins, 1967:53-54; Rana, 1974:3-5; Madane, 1990:52-55), but there seems to be pros and cons; it largely depends on the socio-economic background where co-ops operate and the choice farmers have made.

This model has spread in some Asian countries including Japan, Korea, Taiwan, Sri Lanka, Iran, etc. But the most typical case can be found in Japan. To propagate his notion of a cooperative community, Laidlaw (1980:66) mentioned the Japanese multi-purpose cooperative as an example:

Consider what the rural multi-purpose cooperative does and what it provides in the typical Japanese setting. It provides farming inputs and markets the agricultural product; it is a thrift and credit organization, an insurance agency, a center for consumer supplies; it provides medical services, and hospital care in some places: it has extension and field services for farmers, and a community center for cultural activities. In short, this kind of cooperative embraces as broad a range of economic and social services as possible. Life for the rural people and the whole community would be entirely different without such a cooperative.

Such a comprehensive approach was necessary and possible owing to cohesive rural communities. The main crop has been rice grown in the paddy fields, which required the collective actions such as water management, vermin extermination, planting and harvesting, and so on. The traditional community tie had facilitated such joint actions, often enforced by ostracism. Even before the Meiji Restoration in 1868, there existed mutual help schemes such as “Yui” (joint work for planting and harvesting) and “Koh” (rotating credit society). At the same time, farmers had homogeneous interests in joint actions and their needs could be conveniently met by all-embracing services provided by co-ops. For instance, farmers could get credits when they bought agricultural inputs and machineries while they could pay back when their crops or livestock were sold. They could benefit from co-ops’ farm guidance services combined with supply and marketing plans. They could insure their life and properties against risks of accidents and bad crop while they could receive medical and social services when necessary.

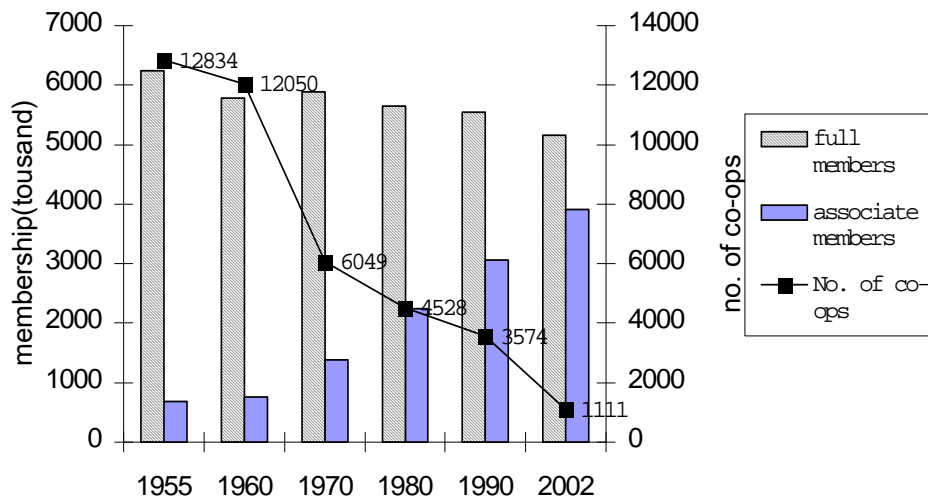
In the process of evolution, agricultural co-ops have even expanded their multi-purpose character including insurance, health and social care, food processing, land development and housing, travel, culture, funeral, and so on. But the supply and marketing businesses have been constantly losing money while the surplus generated by the credit and insurance businesses have been used to offset the deficits. In each business area the national and provincial federations were set up and were affiliated with the national and provincial unions as apex organizations. Thus they developed three-tier *keitou*, the hierarchical agricultural cooperative system.

## Economic and social performance of cooperatives

It looks like contradictory to see that the institutional framework has helped the expansion of the agricultural cooperative system although it has not contributed to the increased productivity of farmers. Rather it can be explained that the cooperative system has effectively served the needs of a homogeneous membership characterized by small ownership with low productivity.

The number of JAs (the new logo standing for Japan Agricultural Co-op adopted in 1992) has been drastically reduced due to the perpetual mergers, accelerated in the 1990s to create financial and managerial capacity (Figure 1). Their membership exceeds 9 million, organizing most of the farming population while regular members have been declining since the 1970s, reflecting the ever-shrinking industry. Only farmers and agricultural juridical persons are eligible for regular members. The membership has been based on households, traditionally represented by male farmers as landowners. So, female farmers constitute 13 percent of co-op membership or 0.2 percent of board members although they contribute to two thirds of the work force. Recently agricultural co-ops have made efforts to increase female members by encouraging plural membership from each household, but the sheer gender imbalance is still to be remedied.

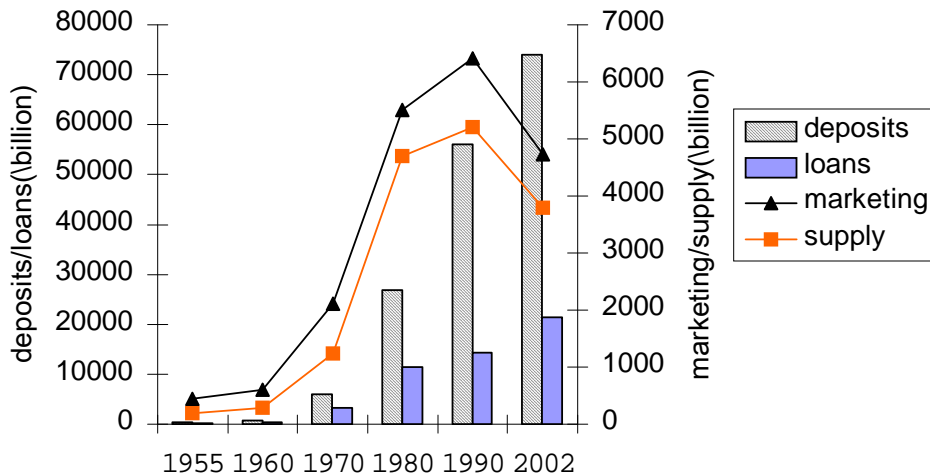
**Figure 1: Evolution of JAs and membership**



The urbanization of suburbs resulted in the inclusion of local residents, suppliers and others as associate members without voting rights. Originally co-ops accepted non-farmers as a result of comprehensive changes further to the Second World War, but associate members drastically increased since the 1960s, as they wished to use cooperative services such as banking and insurance. This process triggered the controversy between a functionalist versus a communitarian view. The former insisted that co-ops should stick to agriculture and concentrate to serve farmers' professional needs while the latter advocated that co-ops could accept interested residents as associate members and turn into community-based organizations serving a wider spectrum of needs. In the end the reality superseded the former idea: co-ops evolved into community enterprises and increased dependence on financial services. However, the increasing number of associate members is generating serious governance problems as to how to involve them in decision-making.

As a result of the evolution supported by institutional framework, agricultural co-ops became a powerful body of agri-business. The deposits and loans have significantly increased, which made JA the largest bank in terms of deposits and assets (Figure 2). Zenkyoren (National Federation of Agricultural Insurance Co-ops) is also the largest insurance company in terms of long-term contracted amount. Zen-no is comparable to the biggest trading firms. However, the marketing and supply business largely declined in the 1990s, accumulating a great amount of losses. It became difficult to offset these losses by the shrinking profits in the financial sector due to stiffer competition. The market share largely varies from regulated products to freely traded commodities. Generally, JAs have enjoyed a high farmer patronage for rice and milk but face stiff competition from non-agricultural operators such as trading firms or meat packers who promote the vertical integration in broiler and chicken production. The deregulation of food distribution policy brought the intensified competition and resulted in the slightly decreasing patronage of farmers (Table 1).

**Figure 2: Evolution of JA businesses**



**Table 1: JAs' farmers' patronage (%)**

	1995	1996	1997	1998	1999
Gov. controlled rice	98.8	99.3	99.2	98.4	97.8
Vegetables	98.5	93.2	93.6	93.1	93.4
Liquid milk	95.8	93.5	93.8	93.0	92.7
Broiler & chicken	81.6	47.7	52.4	40.1	43.0
Cattle	87.8	87.1	86.4	87.8	87.2
Pig	94.6	93.8	93.0	93.1	91.0
<b>Total marketing</b>	<b>92.7</b>	<b>91.2</b>	<b>90.6</b>	<b>90.4</b>	<b>87.9</b>
Fodder	77.2	72.7	72.9	71.4	69.8
Fertilizers	85.8	85.0	84.6	84.4	83.2
Pesticide	72.1	70.1	69.4	69.0	67.8
Machinery	75.5	74.6	73.9	72.9	71.8
<b>Total supply</b>	<b>73.5</b>	<b>72.0</b>	<b>71.8</b>	<b>70.6</b>	<b>69.8</b>

At the same time, co-ops have played the pivotal role of maintaining the social cohesion of rural communities. Although there exist competing businesses in villages with some density of population, it is inconceivable to live in under populated villages without comprehensive services provided by co-ops, involving a wide spectrum of farmers' life from cradle to grave, often without covering expenses. Co-ops have been often seen as stable employers comparable to village administration offices. However, they could not stop the overall reduction of population in rural areas and the decay of marginal villages.

#### *New economy causing institutional changes*

We have witnessed the overall shift from state control to market mechanism since the late 1980s. This shift of power has been prompted by so called New Economy. The barriers set by borders among nations or industries have been substantially lowered by the advent of global economy and information technology. The roles of states have been questioned and institutions are being redesigned to meet the new requirements brought by changing paradigms.

The institutional framework of cooperatives also undergoes drastic changes. In the field of cooperative legislation, paternalistic laws based on state's protection and control are being replaced by more liberal ones based on the autonomy and self-responsibility of cooperatives in developing countries and economies in transition. The expected role of administration systems on cooperatives is also changing from top-down dictating to horizontal partnership. This explains the background of adopting the ICA Statement on Co-operative Identity (1995) and new ILO Recommendation 193 (2002) replacing Recommendation 127 (1966).

The magnitude of changes in the institutional framework of industries is even greater. The big bang in the financial sector has changed the face of industry, where the Anglo-American business models are often seen as global standards. The traditional agricultural policy is giving way to more competition and consumer orientation under the WTO Agreement, which requires the liberalization of trade and overall reduction of state subsidies. The food standards are being harmonized under the universal rule settings enacted by the FAO/WHO CODEX Alimentarius Commission, lowering national barriers. The food processing and retailing is an arena where multi-nationals are competing to dominate the markets beyond frontiers, although national commercial policies are far from harmonization and are still being fought among conflicting interests. The overall withdrawal of states from social service provisions opened new opportunities to the private sector including cooperatives and nonprofits. In short, the power shift from states to markets leads to the reorientation of public policies and institutions from protection to competition. Such paradigm changes in the New Economy pose both threat and opportunities to cooperatives.

### *Deregulation challenges agricultural co-ops*

Multi-purpose agricultural co-ops are facing the challenges caused by deregulation and liberalization. The global economy has pushed governments to reduce public spending and open the domestic market. The traditional protectionist policies gave way to pro-competition in conformity with the GATT Agreement on Agriculture in 1993, urging a wider use of market mechanisms. The agricultural market for major products including beef, orange and rice was opened to the foreign producers in spite of strong resistance from agricultural co-ops. In addition, the 1990s witnessed a number of deregulation measures. The staple food control system was replaced by the *Foodstuff Law* in 1994 that brought market-based pricing, easier entry and free access to distribution channels, leaving the state limited functions such as minimum access import and staples stockpile preparing for emergency. It meant that the government's hard control system was replaced by the soft system where co-ops had to assume some responsibilities for production adjustment and stockpiling. The Agricultural Land Law has not yet been changed, but a joint stock company was allowed to enter the industry as an agricultural production corporation in 2000. Farmers' needs are also changing and diversified, which makes the co-op's egalitarian approach more difficult. More entrepreneurial farmers tend to do direct transactions with suppliers or buyers where they find the economic advantages by doing so. The *New Agriculture Basic Law* of 1999 is meant to spur such directions and bring considerable changes to the agricultural co-ops' dominance in marketing and promotion measures. Some business leaders and politicians question even the exemption of co-ops from the Anti-Monopoly Law or insist to sever financial business from JAs.

Under such circumstances, cooperatives have to strengthen the cooperative identity by sticking to their membership and attaining independence from the state, restructure the business to meet the diversified needs of farmers and promote sustain-



able agriculture, streamline the whole system by promoting mergers and integrating into two-tier organizations. The multi-purpose model will be maintained provided the drastic restructuring measures are undertaken to solve structural imbalance, since financial functions can no longer earn sufficient surpluses to offset the loss-making functions because of stiffer competition. Norinchukin (Central Cooperative Bank) made the vertical integration to create a JA bank system with a stricter discipline and a larger safety net against insolvency. Zenkyoren (National Mutual Insurance Federation of Agricultural Cooperatives) absorbed the provincial federations to create a single insurance co-op. Co-op's marketing and supply functions are also pursuing "selection and concentration". It means 12,000 depots for supplying fertilizer/pesticide will be concentrated in 300 regional warehouses and unprofitable retail outlets, and service stations are to be separated as subsidiary companies.

But these have to accelerate such a restructuring process to remain as viable business organization supported by farmers and consumers. The Minister of Agriculture urged co-ops "to reform or to dissolve" and set up the Commission on Agricultural Co-ops, which produced a report in March 2003 (MAFF, 2003). The Commission pointed out that co-ops should increase farmers' income by active marketing of products and reduction of input costs, and drastic rationalization of supply/marketing businesses so as to pay without compensation from financial businesses. It also recognized that the government's stance of using co-ops as its agents had inhibited their independence and recommended a clear-cut division of roles, confining the former to regulatory supervision. In particular, the government is requested to make equal treatment of co-ops and other farmer organizations as regards channeling subsidies and closely monitoring co-ops' unfair trade practices, in collaboration with the Fair Trade Commission. It is ironical to see that co-ops are requested to become independent by a government that used them as effective means to implement a public agricultural policy.

## **Conclusion**

Organizations evolve to adapt to the changing environment in economic systems, social structure, demography, technology, the dominant culture and ideology. Institutions constitute very important components of such environments. It seems that organizations may adapt to institutions too successfully and become "institutionalized" as in the case of Japanese agricultural co-ops, which had evolved to act as agents for implementing public agricultural policy. It is also evident that organizations cannot escape institutions and we need to be alert to the institutional changes that may cease to be positive and turn into negative effects. This is what happens to the agricultural co-ops, which are struggling to adapt to the new environment, strengthen their core competence and realign their structure. But it is generally observed that the speed of reforms is not high enough to meet the requirements of the

time while there still are gaps in the perceived crises and future directions amongst co-op leaders. Some co-ops are shifting to the new directions by innovating operations and finding new markets, while the others are kept in organizational inertia. On the other hand, entrepreneurial farmers and non-agricultural businesses started a number of experiments to bring about innovations in the food system, often being encouraged by the government's scheme which allows operators to make trials for structural reform in special zones. The agricultural co-ops can no longer ignore such initiatives and try to involve themselves in such ventures, instead of resisting them to maintain the existing institutional framework. They are expected to rejuvenate their organizational structure and business practices to accommodate the diversified interests of members in the era of New Economy.

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