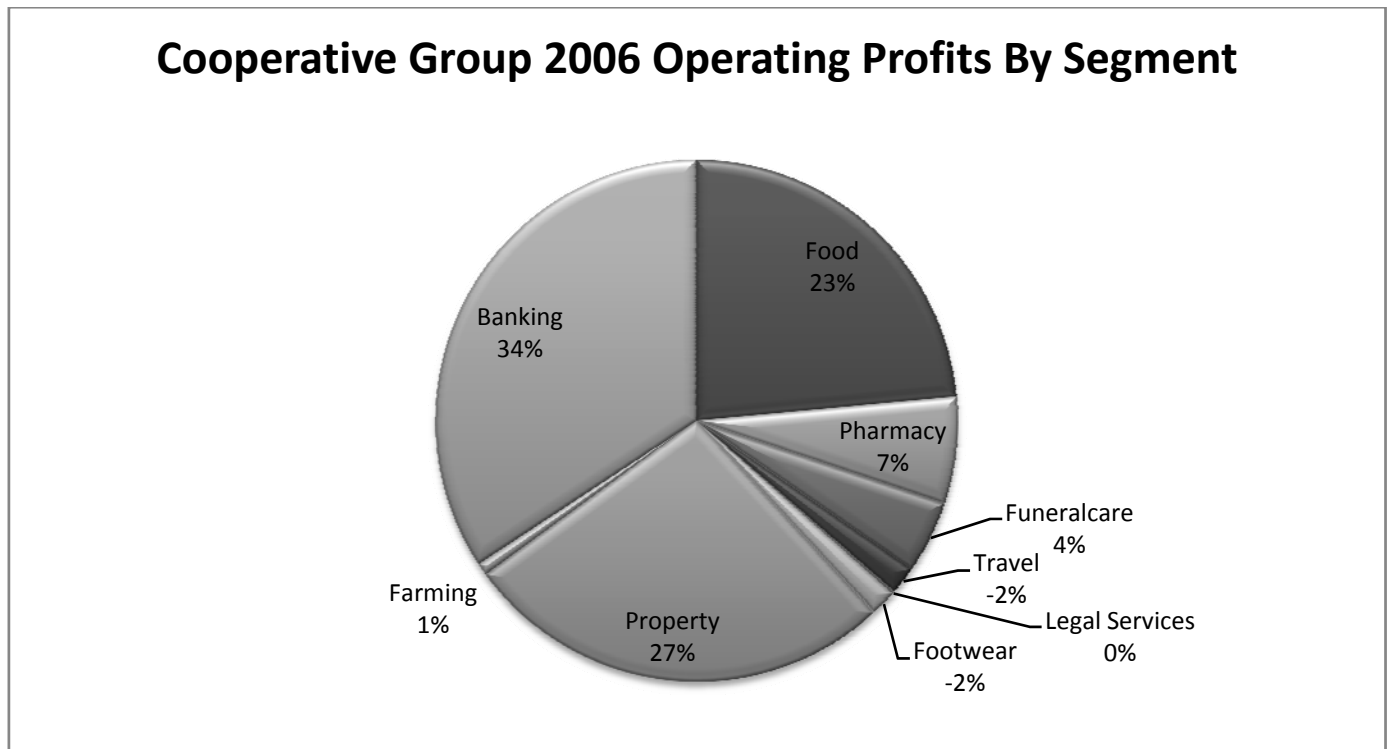


MN4203 Logbook on the Cooperative Group

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This paper discusses the strategic behaviour of the UK-based Cooperative Group, a consumer-owned buying collective, during the last twenty years. One of the great advantages of consumer-owned business reporting is that there is much less incentive to lie, spin results or hide behaviour due to the consumer-owned nature of the business – a genuine effort is made to give full & total transparency into every aspect of the business. Hence as it has less need to, the business press tends to not bother analysing performance except to exclaim surprise and give awards¹, and thus I have chosen to use almost exclusively the Cooperative Group's own reports up until 2006. Mainly due to a lack of availability of any other literature specific to the Cooperative Group's activities in 2007, I have also made occasional use of officially sanctioned 'blogs' in which regional committee meeting minutes are publicised.

Quick Overview & History



With a turnover of over £8bn in 2007², the UK's Cooperative Group is the world's largest consumer owned business³, the world's eighth largest cooperative³, Europe's largest funeral services provider², the UK's largest farmer, the UK's third largest travel services provider and pharmacy⁴ and the UK's most consumer liked banking and

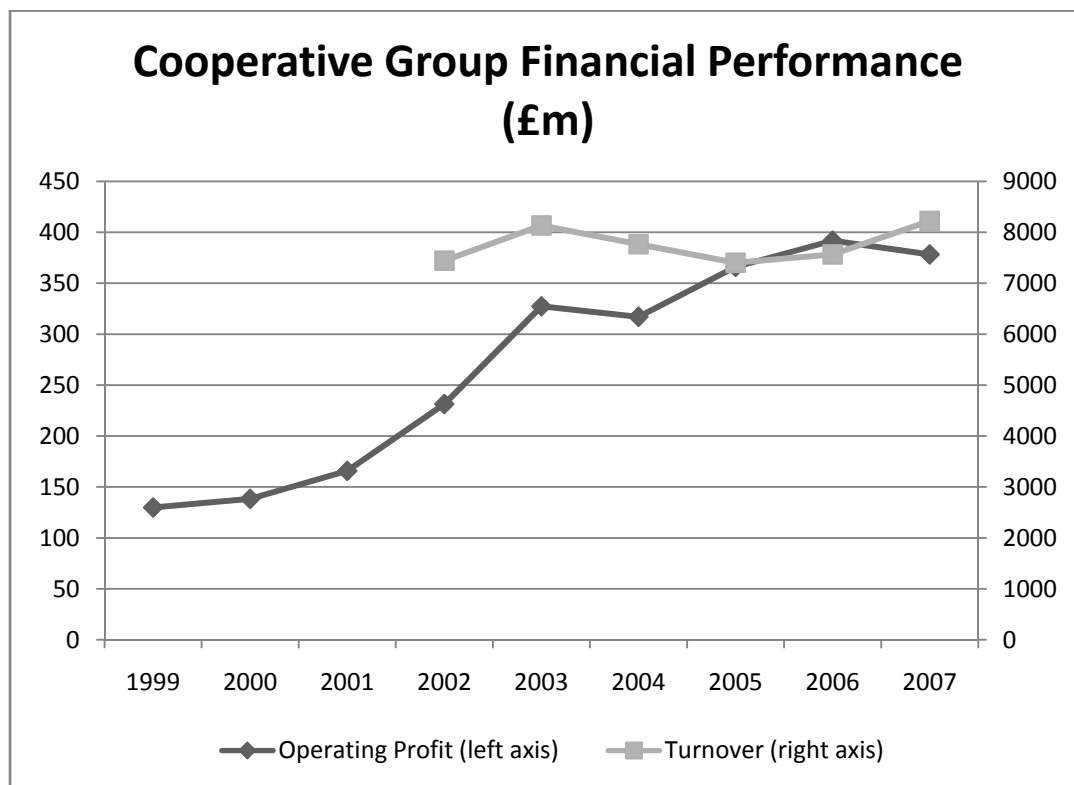
¹ For example, the Cooperative Group's Financial Services 'Sustainable leaders' unit trust beat all other UK companies based trusts in 2006 with an outstanding return of 29.4% during the year (as against 13.3% of the average unit trust performance).

² Estimated from the Cooperative Group's 2007 interim report.

³ According to the International Cooperative Alliance 2007 Annual Report. Also from that report: worldwide, cooperatives have a turnover of nearly £500bn, around one fiftieth of world GDP, and the United Nations estimated in 1994 that the livelihood of nearly 3 billion people, or half of the world's population, was made secure by co-operative enterprise. Every OECD country has an important & very successful cooperative based component of their economy ranging from 0.5% (Australia) to 16.1% (Finland) of total GDP.

⁴ From the Cooperative Group's 2006 Annual Report.

insurance provider⁵. In fact, the Co-op is Britain’s most trusted brand⁶ by quite some margin, and any excess profits are returned to members as dividends. Due to being managed extremely conservatively, most large consumer owned cooperatives never make a loss and I could not find any evidence that the Cooperative Group ever has in 150 years of operation.



Furthermore for the last five years, financial & market share performance has been excellent in all business segments except for travel & footwear despite undergoing three major mergers since 1999 – and this is with very stiff head-to-head competition against multinational retail giants such as Tescos, Alliance Boots and HSBC. This is a particular surprise given that the cooperative movement in the UK had been in decline during the 1990’s, during which the Co-operative Wholesale Society Ltd (CWS) – one of the larger cooperatives – had just about seen off a hostile demutualisation takeover attempt by Andrew Regan. This led many to write off the cooperative movement as shortly going the way of British coal mining in the 1980’s – which in 1999 prompted leading trade union activists to petition the Labour government to arrange a new Cooperative Commission.

The previous Cooperative Commission in 1956-1958, chaired by then Labour party leader Hugh Gaitskell, had been strongly capitalist in its recommendations which as a result were largely ignored at the time. The 2000-2001 Cooperative Commission, chaired by the then General Secretary of the TUC, John Monks, has this to say about the 1956-1958 Commission in their final report:

“The example of the 1958 Independent Co-operative Commission (see Annex 7) was very much in the minds of those drafting the Report. That earlier report had been prescient in its analysis, and right in nearly everything it recommended: and yet the Movement had failed to implement it. That must not happen this time.” (Process & Overview, 2002 Cooperative Commission Final Report)

⁵ The public seem to feel they are more fairly treated by the Co-op than by other banks – here is only a short list of the consumer awards they have recently received: four year finalist in ‘What Mortgage’ top lenders of the year, five year consecutive winner of best online banking service by ‘Your Money’, consecutive leader of Corporate Responsibility Index, voted ‘Most Gay friendly’ bank by ‘The Gay Times’, winner of independent LEX survey of 8000 mortgage holders, winner of best customer service award by Guardian readers.

⁶ Source: The National Consumer Council May 2006 *What Assures Consumers* report.

In parallel to the Cooperative Commission, and pre-empting its conclusions, the newly revitalised (post-Regan takeover attempt) Cooperative movement set about enacting a wave of mergers and consolidations with the biggest, the merger of the Cooperative Group and United Cooperatives, only being completed last July. A significant harmonisation of branding of all Group members into a single logo and identity has been taking place since 2000 with (historically speaking) radically deep cuts into loss-making parts of the Group. It has created its first new unique market segment since its creation of full internet banking via Smile in 1999 in the form of the new Cooperative Legal Services Group in 2006. Things have not looked better in twenty years, yet how did this arise?

Strategic Analysis

Like all cooperatives, the Cooperative Group is managed on a far more democratic basis than traditional corporations which directly interact with their shareholders only once a year at an Annual General Meeting. Wide consultations are performed before enacting any major decision not just with members, but also with stakeholders across the greater community in combination with biannual regional meetings. This makes strategy formulation extremely slow indeed, and is also inherently highly conservative as such a large population tends to be very risk adverse and thus will tend only to clone initiatives from obvious successes invented years (sometimes decades) beforehand by traditional profit making firms. Nevertheless, over the last twenty years the Cooperative Group has had a continuing first mover advantage in a surprisingly large number of areas including equal employment opportunities⁷ (pre 1980's); sustainability (1970's); ethical trading, investment & behaviour⁸ (since 1844); organic & ethical sourcing⁹ (1990's); internet banking (Smile) and legal services¹⁰ (2000's) – and furthermore is widely seen as such by the public without the cynicism normally granted to such endeavours by a corporation. Even more surprisingly, once begun, the Group has consistently maintained its lead in each of these areas, thus proving the adage “Slow and steady wins the race” (2006 Annual Report).

One can therefore clearly see that the Cooperative Group adopts evolutionary rather than revolutionary strategic change – indeed, it has no choice given that the Board of Directors must undergo years of consultation with others before change is even decided upon. However, the major upside of this is that strategic change is definitely thought through extensively beforehand, and furthermore such wide consultation effectively eliminates any marketing requirements later on as all the voting consumers will have already debated it at length with word of mouth (the most effective form of marketing) taking care of the non-voting consumers. As it has such a well primed market ready and waiting for executive initiatives, success *among its membership* is almost guaranteed and its track record over the last century is nearly perfect – one of the major reasons it is nearly always profitable. Another advantage of innovating after the leaders is that you can skip making the mistakes they made, and make incremental improvements with the benefit of hindsight. This however leads to one particular problem with cooperatives in general – they are a closed circle, and if you don't know anyone who is a member who sings their virtues, then the lack of marketing means that the wider public is often clueless that anything new has happened.

⁷ They were one of the first businesses in the UK to adopt an anti-discrimination employment policy back in the 19th century well in advance of government legislation. Even today, the Group employs a higher percentage of women, non-whites, former criminals, the old, the disabled and those of non-Christian religion than any other company in its sectors (source: The Cooperative Group 2006 Sustainability Report, independently audited by *Opportunity Now*).

⁸ Specifically, they have refused to interact (unless there is no choice) with companies involved in the arms trade, global climate change, genetic engineering, animal testing and use of sweated labour.

⁹ They were one of the pioneers of Fairtrade™, a movement which has now spread out into a multitude of organisations including St. Andrews University itself which has committed to purchasing only Fairtrade fruit and coffee.

¹⁰ Due to a loophole under rule 3 of the Employed Solicitors Code 1990, cooperatives may provide legal services for members – thus bypassing the long-standing tradition that only individuals may own a law practice in Britain. This will likely begin hitherto unknown full competition in the legal services – which in this author's opinion is about time given the extortionate, shoddy & incompetent service which is all too common.

This therefore indicates a problem with spreading marketing information outside the membership which is already strongly biased in favour of making a positive evaluation. One might think that the Cooperative Group would use a cooperative network level (how it interacts with its ecosystem of firms) strategy rather than a competitive one, but you would be wrong. As implied by its name, the Group is in fact a group of smaller cooperatives each of which have *voluntarily* joined and can (and occasionally do) internally vote to secede at any stage – this makes a merger very different from when one corporation buys another one. The reason to join is a shared vitriolic dislike of non-cooperative provision of goods & services such that cooperatives provide their own banking, farming, insurance, pharmacy, ... etc. Other cooperatives, even non-member cooperatives, are treated favourably while all other providers viewed with suspicion, sometimes bordering on fanatical dislike. As a result, not only does the Cooperative Group refuse to sell many common goods and products (e.g.; most kinds of fish), it also simply refuses to deal at all with a large minority of FTSE 100 companies and indeed goes out of its way to publicise negative information about most of its competitors (e.g. its dissemination of the BBC's *Whistleblower: Supermarkets* programme of May 2007 showing how Tescos and Sainbury's routinely change the 'Use By' dates on food, particularly meat¹¹). This kind of scare tactic carries far more weight due to high public trust in the brand to such an extent that eight out of ten consumers don't trust the food that they buy (2004 NOP study commissioned by the Co-op – *Shopping with Attitude Report*).

Similar scare tactics and negative information warfare campaigns are carried on at every level of the business – between heavy & sustained negative campaigning against GM use by anyone at all levels right through to negative campaigning against the for-profit insurance & banking companies as being “untrustworthy”. On their website in the 'Media' section, there are no less than eight clearly labelled reports with titles such as “Blackmail Report” on how non-cooperatives use advertising to target children to blackmail their parents or “Food Crimes Report” on how non-cooperatives use food engineering to make unhealthy food look good for you. In my opinion, this sort of negative campaigning is really actually aimed at getting government to enact regulation to ban methods competitors commonly use, and in this the Cooperative Group has been outstandingly successful. Successes detailed by the Group's Annual General Reports 2003-2006 and the aforementioned reports include product ingredients labelling, the ban of milk production hormone use in cattle in 2000, the mass hysteria over and probable future ban of GM food, the addition of recommended drinking limits (alcohol units) to alcohol, the addition of health warnings to tobacco and the labelling of eggs as being free range, cage produced etc. Even the recent flooding in the south has been used to advocate new regulation in the insurance industry favouring mutualised insurance providers (see Cooperative Financial Services Press Page announcing a £100 Christmas gift to families still living in alternative accommodation). One can see that rather than competing head-to-head via promotional vehicles, the Cooperative Group prefers to lobby for their elimination. In fairness, they also publicise their own mistakes – for example, the Group's 2006 Sustainability Report even lists three incidents of verbal abuse to workers in Malawi making products for the group along with thirty-two breaches of excessive working hours in Turkey, China, UK, Malawi, Maldives, Brazil, Thailand, Madagascar and Pakistan. Nevertheless, one cannot fail to be impressed by the outright hostility with which the Cooperative Group treats non-cooperative firms.

While at a group-wide scale major strategy initiatives are planned in great detail by wide consensus and thus give a classic example of organisational dynamics (that individuals have little power in forming strategy) in action, quite a different example emerges at smaller scales. A great deal of autonomy is given to individual workers and subgroups – once a general initiative has been agreed by the membership, a great deal of scope is afforded to those who actually enact it. This is probably due to the high trust levels imparted to not just managers but also to lowest level workers to complete their job in any way they think best, even if that means being initially very incompetent and making a financial loss in the short-term as they find their feet. The Group feels it is very important that people are allowed to determine their own work environment rather than have a uniform look imposed on them by Head Office

¹¹ See <http://news.bbc.co.uk/1/hi/business/6676345.stm> .

– this even extends to a majority of the funeral-care outlets not using the Co-op branding at all¹² (2006 Annual General Report).

In this sense, at smaller scales the Cooperative Group is almost uniformly an example of organisational leadership (that individuals can make a big difference in forming strategy) in that individual outlets are highly heterogeneous in the items they stock, how they are managed and even whether they are a profit-making or community-serving outlet. To explain this latter point, the Group is unique among commercial enterprises in permitting remote stores to be run permanently at a slight loss because it has been judged by the local Cooperative Group committee to be too detrimental to the often very aged local community to close the store. All of these factors add to the quirkiness of Cooperative Retail outlets, because customers get a unique experience in each store which imparts an ‘old-fashioned’ image to them¹³. In the last five years, a roving task-force has been built up which regularly surveys outlets and can step in to save failing outlets with advice and training before they go bankrupt – though rarely is a manager fired or demoted as it would seem that social stigma and shame at having been seen to fail causes them to move on without forcing the issue. Social pressures to perform, rather than financial, are the key driver in the Cooperative Group (source: Cambridge Cooperative Regional Group Blog, November 2007).

Due to this participative environment, job satisfaction is very high, as is on-the-job learning and adaptation. Workers feel very good about their jobs and their companies with the only consistent complaint being insufficient pay. More than half of the workforce are also members receiving dividends and a 10-20% discount in Cooperative outlets. Worker turnover is lower than other enterprises in the same sector, and only 12% of workers dislike their job mostly due to a perceived lack of openings for career progression (2006 Sustainability Report). The Cooperative Group clearly marries together organisational leadership and organisational dynamics in a unique and successful fashion.

My conclusion is that the UK’s Cooperative Group has done well during the last five years because globally speaking, cooperatives are doing well in every single part of the world and have done so for many decades now (ICA Global 300 Report 2006)¹⁴. Having been dented in the 1990’s by a loss of focus caused by the failure of Communism, the Cooperative Group has simply been catching up with its historical trend of over 160 years. It also has helped that cooperatives have returned to fashion in the last five years – the member demographics of the Group show a rapidly rising under-30’s segment which if unchecked, will leave the Group’s voting membership mostly composed of the young and the very old – a unique situation to be sure (Cambridge Cooperative Regional Group Blog). The Group itself isn’t sure why there has been a return to popularity among the young especially after so many decades of “uncoolness”, but it has commissioned research to find out which is due to report in 2008. Committee suggestions include a rising concern about climate change and globalisation as key factors attracting the young, but my own investigations showed that most new young members were joining for the Cooperative Bank and Insurance Services, not for Food¹⁵.

¹² Instead they present themselves as a family owned business e.g.; “McPhearson & Brothers” with the Co-op leaflets discreetly placed in the waiting room.

¹³ This doesn’t apply to Cooperative Financial Services which are consistently rated as class leading – indeed, the Cooperative Bank is a full central clearing bank.

¹⁴ For example, they are widely credited with saving Argentina after its government bankrupted itself.

¹⁵ My own investigations here meant that I spoke with Mr. David Bean, former sabbatical officer of the St. Andrews Student’s Association, now working in the main strategy office of the Cooperative Group.

A Reflection on the Nature of Strategy as an Area of Study¹⁶

My primary observation is that texts on strategy concentrate far too much on success and nothing like enough on failure, despite that strategies for failing well are vastly more important than those for success in the long-term. Judging by the reading I have done in this field it seems barely acknowledged outside Eastern texts of which Sun Tzu's 孫子兵法 (The Art of War) is a good example¹⁷. There is a particular predilection in the West for success stories of which strategy gurus Charles Handy and Michael Porter are very typical¹⁸ or for that matter the classic business text *In Search of Excellence*¹⁹, and while of course no one likes hearing about failure all the time, I would posit that perhaps that has more to do with failure not selling well in the Anglo-Saxon business culture rather than for any logically consistent justification.

The reason that this is so important is because 99.9% of new firms fail and 100% of all firms fail eventually – it's just a question of time. This fact is explored in depth by renowned British economist Paul Ormerod in his book *Why Most Things Fail – Evolution, Extinction & Economics* (Ormerod, 2005) where he shows that the statistical failure profile of the top one hundred British and American firms over the last century precisely matches that of the failure profile of species that have lived on this planet according to the fossil record. Those firms that lived the longest got into trouble several times, but it was because they failed *successfully* that they went on to fight another day. A good contemporary example is how Microsoft initially completely underestimated the popularity of the Internet and invested significant resources into developing their own proprietary networking strategy based on the then dominant AOL bulletin board system – but once realised, quickly backpedalled and had successfully U-turned within two years (Shapiro & Varian, 1998). We will never know the fate of Microsoft had they not realised where the market was going in time, but certainly IBM's misreading of consumer needs around 1995 with its OS/2 Warp operating system allowed Microsoft to steal the popular operating system crown which has since yielded billions of dollars in profits – which had IBM been smaller and not so divested across other markets, would have almost certainly been fatal.

Strategy in my opinion is fundamentally about converting uncertainty (unpredictable randomness) into risk (probabilistic outcomes of known futures). As economics can only deal (currently) with risk²⁰, and insurance and capital finance can certainly only deal with risk and risk alone²¹, there is a financial accounting requirement to reduce all possible futures down to a set of anticipated futures some of which are listed in the annual financial report to shareholders – an example of this is that no less than fourteen pages in the Cooperative Group's 2006 Annual Report is dedicated exclusively to risk management. Strategy therefore is about taming the future – making sense of it, rationalising it, pushing it into a box small enough that we can wrap our heads around it.

¹⁶ Yet again I have had to use academic papers mostly from Economics rather than Management in this discussion because despite my annual complaints to the Management school, JSTOR via Athens access still won't allow access to the vast majority of peer reviewed Management journals despite the assurances I was given in May 2007 that this would finally be fixed. Please contact Dr. Manouche Tavakoli about this matter.

¹⁷ I specifically used the manager's translation (Michaelson, 1999).

¹⁸ I caveat this statement with the warning that I have only read one book from each, those being (Handy, 1976) and (Porter, 1980).

¹⁹ Most unfortunately, as noted by *Business Week's* November 1984 edition, one third of the businesses described as embodying excellence in the book had suffered major financial problems since its publication in 1982.

²⁰ This is due to a problem in the foundations of microeconomics called indeterminism which leads to breakdown of economic equilibrium without severe restrictions on the modelling of uncertainty. See (Arrow, 1951), (Debreu, 1959), (Newbury & Stiglitz, 1982) summarised in (Mas-Colell, Whinston, & Green, 1995) section 17.

²¹ The most obvious example being how in the Capital Asset Pricing Model (CAPM) a beta value is assigned to every stock which is a statistical measure of risk based on past performance (Sharpe, 1964).

However, it is the sheer *unpredictability* of the future which makes strategy impossible to always get right. The Cooperative Group has such an outstanding strategic track record because it follows after much hindsight where others have already gone and it has a guaranteed market for its goods & services – two things most normal firms cannot have. Therefore because uncertainty has already been almost entirely converted into risk for it, it very rarely fails. I do find it very interesting that there is a long tradition of insurance companies being mutualised – the German Gebäudeversicherung ran successfully for 230 years with excellent cover and very low costs as compared to their demutualised successors (Epple & Schaefer, 1996). One of the fascinating results of introducing competition to the hitherto monopoly is that the quality of insurance cover has been greatly reduced – the much smaller competing insurance companies simply cannot afford to take on the risk of extraordinary events (acts of god) happening, precisely because *when* (not if) these happen cannot be planned for.

Nevertheless, the world we live in is the way it is. Στρατηγός (strategos) led the Athenian council in ancient Greece; successful strategy has underpinned the rise of our civilisation to its present day; and strategy will be required to prevent climate change wiping most of us out. The fact we have achieved and can achieve so much is because strategy *works*, and thus its study will always be essential.

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The Cooperative Group Annual & Interim Reports:

<http://www.co-operative.co.uk/en/corporate/reportsandpublications/>

The International Cooperative Alliance: <http://www.ica.coop/>

The year 2000 Cooperative Commission Report: <http://www.co-opcommission.org.uk/>

Two blogs for Cooperative Group leadership committees were used at:

1. <http://devon-co-op.blogspot.com/>
2. <http://cambridgeco-operation.blogspot.com/>