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Is there a co-operative advantage? Experimental evidence on the economic and non-economic determinants of demand

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ABSTRACT

Focusing on consumer co-operatives, I test the conventional economic worldview that relative price is a main determinants of consumer behaviour using survey instruments in a classroom setting. I examine the role which non-economic variables such as 'warm glow' might play in determining demand. My findings challenge the narrow economic worldview that only economic variables count; but support a core assumption that economic variables are of fundamental importance to individual's choice decisions. Significantly, individuals are willing to pay higher prices for co-operative products even if they are not co-op members. However, as the price of co-operative products increases relative to the products of non-co-operatives, demand falls amongst both non-members and members of co-operatives. But demand is more inelastic for co-op members. When price is the same for co-ops and non-co-op, even non-co-ops members prefer to purchase products sold by co-operatives. The co-operative advantage provides co-ops with a protective belt against competition from non-cooperatives. This also speaks to the potential strength of consumer co-ops in competitive markets. Firms that invest in both economic and non-economic determinants of consumer demand, should be characterized by a significant competitive advantage.

1. Introduction

In a very broad sense, using data derived from a classroom experiment, I test the hypothesis that a consumer co-operative holds a competitive advantage on the market over investor owned firms by virtue of it being a co-operative. A consumer co-operative is a member-owned (in this case, consumer-owned) and democratically run business oriented towards the mutual benefit of its members (Altman, 2009; Birchall & Ketilson, 2009; Birchall, 2003; International Cooperative Association, 2016; Novkovic, 2006).

I ask if consumers are willing to pay something extra, if necessary, when the preferred commodity is sold by a consumer co-operative. Moreover, I ask if the consumer is willing to purchase a product supplied by a co-operative (or a co-operative product) over the same-priced product sold by a non-co-operative or investor-owned firm. If this is the case, the co-operative provides its products with an additional characteristic desired by the consumer that improves her or his utility or wellbeing.[1] This additional and positive characteristic is a function of the product being sold by consumer co-operative—this member-owned and democratically operated business. More specifically, I present results from a survey-based classroom (lab) experiment that interrogates the conventional economic hypothesis that consumer choice is largely a function of relative prices, given income, as opposed to other non-economic factors. This is the first survey experiment on co-operatives of this type. There are no systematic scientific published studies that attempt to determine the extent to which pro-co-operative preferences exist. Hence, a significant gap in the literature and related understandings of what drives the demand for the output produced by co-operatives from co-operatives members and from individuals who are not members of co-operative. We do, however, have some evidence that consumers have a liking for such output and might pay somewhat more for co-operative output.[2]

My findings challenge the narrow economic worldview that economic variables alone count; but support a core economic assumption that economic variables are of fundamental impor-

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[1] On modeling the demand for a commodity in terms of the various characteristics it embodies, see Lancaster (1966).

[2] The Co-op Group (2004), of the United Kingdom, produced a very general survey where most respondents indicate that they would pay "a little more" for ethical products. See also footnote 3.

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tance to individuals' choice decisions (Altman, 2005a, 2005b, 2006). I find that individuals are willing to make material sacrifices to reward organizations that have certain preferred or desired characteristics. In this experiment, the desired characteristic of a product is a function of it being sold by a consumer co-operative. This preferred characteristic provides co-operatives with a co-operative advantage on the market. In my experiment, even individuals who hypothesize themselves not to be members of a co-operative are willing to forfeit some income to purchase a product sold by a consumer co-operative. However, both hypothesized members and non-members of co-operatives exhibit negative elasticities of demand with respect to relative price increases in co-operatives. Demand is negatively affected by price increases. Price matters, but not as much as is hypothesized in the conventional economics worldview.

For the purpose of the experiment, it is assumed that consumer co-operatives do not derive an advantage in terms of superior productivity or in terms of the quality or uniqueness of the good or service supplied. This is made explicit in the questions asked to subjects in the experiment. The co-operative advantage, where one exists, is situated in buyers deriving a non-material benefit by purchasing from a consumer co-operative. This, in turn, increases the consumer's level of wellbeing or utility from what it might otherwise have been. This non-material benefit can take on many forms, such as sympathy and empathy or support for a particular organizational form like a co-operative. But this article does not address the issue of what exact non-material considerations best explain the co-operative advantage. Following Andreoni (1989, 1990) some economists would dub this non-material benefit as a warm glow effect. So, for example, for pro-co-operative individuals, an action favoring co-operatives, such as purchasing products from consumer co-operatives, enhances their level of wellbeing. It makes them feel better. The specifics of this, warrants further study.[3]

In the experiment, it is recognized that members of consumer co-operatives receive a year-end bonus, based on the economic performance of the consumer co-operative. This is a traditional characteristic of consumer co-operatives. But such bonuses tend to be relatively small and the size is subject to volatility. No such material benefit exists for non-members. But such bonuses are not very different from what is offered by many non-co-operative retailers and wholesalers that take the form of member discounts or year-end bonuses based on the value of purchases. Therefore, it is possible that co-operative members have some material interest in purchasing from their co-operative, although bonuses are not a function of own-purchases. Non-members of a co-operative have no such incentives.

2. What is a consumer co-operative?

Consumer co-operatives are owned by members, which can include employees. The co-operative is owned and operated in terms of one-person one-vote or one member one vote. This would be opposed to the investor-owned firm where voting depends on the extent of ones investment in the firm. The consumer co-operative builds, at least in theory, upon member-consumers having an active say on how the co-operative functions in terms of what it sells, how it sells, how it relates to its community, and how profits or surpluses are disbursed. For example, surpluses can be used to re-invest in the co-operative, build-up capital reserves, disperse to members as bonuses, invest in the community, or some combination of the above (Altman, 2009; International Cooperative Association, 2016).

A key distinguishing feature of consumer co-operatives is that they should be configured to best meet the preferences of their member-owners in terms of product type, quality, and price. Moreover, the objective of the co-operative is not to maximize the difference between unit cost and price, but rather to charge the lowest price possible, given quality and the investment requirements of the co-operative. But consumer co-operatives typically charge the market price for their product. However, any surplus accrued is supposed to be directed toward investment purposes, disbursed amongst members, or invested in socially beneficial projects as decided upon by members. It is important to reiterate that a key difference between a traditional retailer and the consumer co-operative is the overriding importance in the co-operative of the member-owner. No one member can have a greater ownership or membership share than another (Altman, 2009; International Cooperative Association, 2016).

A labor or worker owned consumer co-operative is a type of multi-stakeholder co-operative, where the co-operative is owned and governed by both workers and consumer stakeholders in the co-operative (Girard & Langlois, 2009; Lund, 2015). A subsidiary hypothesis tested in this paper is whether hypothetical non-members and members of a multi-stakeholder co-operative would be more likely to purchase from the co-operative. Here there might be more of a member incentive to purchase from the co-operative, since the employment of worker members can be positively affected.

3. Theoretical context

It is important to place this co-operative experiment in the context of economic theory. In terms of conventional price theory, if the consumer co-operative provides no advantage in terms of price or quality over the non-co-operative, the co-operative holds no material advantage over the non-co-op or traditional investor-owned firm. And, if the consumer is a simple wealth maximizer, any increase in the price of products supplied by the consumer co-operative relative to products supplied by non-co-operatives, holding quality constant, should result in the collapse of the co-operative's market share. When co-operative prices are equivalent to non-co-operative prices, co-operative members should be expected to purchase from the co-operatives if the co-operatives sell products more closely aligned to the preferences of co-operative members as compared to what's offered in the investor-owned firms and if a year-end bonus is expected. However, non-co-operatives members should be indifferent between purchasing from a co-operative as opposed to a non-co-op or an investor owned firm. Therefore, for any such group of consumers, on average, 50% should make their purchases from co-operatives all other things being the same (a 'random' disitribution).

However, if a warm glow is derived from purchasing products sold by co-operatives there would be a co-operative advantage for clear non-material considerations. In this case, one could predict that, ceteris paribus, individuals with such pro-co-operative preferences would purchase from a co-operative, even if they were not co-op members, if there is no difference between the co-

[3] Related to the warm glow effect is the notion of psychological ownership wherein individuals feel an affinity towards a product or the origins of a product (Jussila et al., 2015). This can arguably have a positive effect on the purchaser's level of wellbeing yielding, one might argue, a utility enhancing warm glow to the purchaser. One might also refer to identity economics, as articulated by Akerlof and Kranton (2010), where an individual's utility or wellbeing is increased if he or she is able engage in behaviour that results in the individual being better able to connect with or be part of what he or she identifies with. This could be, for example, another individual, group, or organization, such as a co-operative. This also relates to social cohesion and identity-enhancing social capital (Christoforou 2013), where the latter two variables contribute to enhancing an individual's utility or wellbeing. There is also a literature making reference to the positive non-material benefits of being associated with a co-operative (Brown, 2006; Fairbairn, 2004, 2005; Johnson, 2015; see also Uslaner, 2005).

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