

## **Member Loyalty in Co-operative Enterprises: A Preliminary Assessment**

Tim Mazzarol

*UWA Business School, University of Western Australia, Crawley Western Australia*

Email: [tim.mazzarol@uwa.edu.au](mailto:tim.mazzarol@uwa.edu.au)

Geoffrey N. Soutar

*UWA Business School, University of Western Australia, Crawley Western Australia*

Email: [geoff.soutar@uwa.edu.au](mailto:geoff.soutar@uwa.edu.au)

Elena Mamouni Limnios

*UWA Business School, University of Western Australia, Crawley Western Australia*

Email: [elena.limnios@uwa.edu.au](mailto:elena.limnios@uwa.edu.au)

Paper presented at the 26<sup>th</sup> Annual ANZAM Conference, 5-7 December 2012, Perth WA.

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### ABSTRACT

*Co-operative enterprises are a unique form of business, part social and part economic in nature. They are created for the benefit of their members, who are also their owners, customers and suppliers. An important issue in the sustainable development of co-operatives is their ability to deliver value to members. However, the unique nature of their business model makes the relationship with their members, and therefore the nature of how value recognition leading to member loyalty is understood somewhat complex. In this study we propose a model of member loyalty in co-ops that highlights the importance of affective commitment and identification with the co-op as key mediating variables.*

**Keywords:** cooperative advantage, customer value, customer satisfaction and loyalty, collaborations and networking

### INTRODUCTION

Co-operative enterprises are a unique form of business. They are member-owned businesses that exist for the economic and social benefit of their membership. Unlike many conventional investor owned firms (IOF), the co-operative (in most cases) is governed by a highly democratic system of “one-member-one-vote” rather than the more traditional “one-share-one-vote” model of the IOF (Bacchiega and de Fraja 2004). While the IOF is established primarily as a vehicle to maximise shareholder returns through profit taking, the co-op is concerned with enhancing the economic benefits of its members (Birchall 2004). As its membership is also engaged with the co-op in a patronage relationship (e.g. as suppliers and buyers), this can mean that the co-op’s purpose is to pay higher prices to suppliers and charge lower costs to buyers (Bontems and Fulton 2009). This need to deliver value to its members while also retaining sufficient retained earnings for sustainable operations and growth is one of the key challenges facing co-operative enterprises (Mooney et al 1996).

The co-operative is a hybrid business form that serves both economic and social purposes (Levy and Davis 2008; Novkovic 2008). This dual function or “symbiosis” has been a feature of the co-operative business since the foundation of the Rochedale Society co-op in England in 1844 (Fairbairn 1994). Important issues for co-ops are how well they service the needs of their members, and how well they manage what is essentially a network of small firms, or households within a

community (Helemberger and Hoos 1962; Staatz 1983). The success and sustainability of the co-op is likely to depend on how well it delivers not only economic capital value, but also social capital value to its membership, and the ability for members to recognise this (Mancino and Thomas 2005; Novkovic 2008).

This paper outlines the findings from a pilot study into the factors motivating co-op members' intentions to remain loyal to their co-operative. It is part of a wider study that is seeking to better understand the forces impacting on the success and sustainability of the co-operative business model. The key research question guiding this study was: "How does a co-operative measure and communicate the true value of membership?" Related to this were questions as to the co-op's role in capturing value in an integrated or vertical value chain, and what are the most appropriate means of communicating value to members? In this study the focus was on investigating the relative importance of financial, function and emotional value on a member's commitment and identification with the co-op, and how these factors influence a member's decision to remain a member.

## **LITERATURE REVIEW**

The foundation principles of the Rochedale Society of Equitable Pioneers remain today as the guiding principles of the global co-operative movement (ICA 2012). This early co-op was founded on the basis that its members' investment capital was not to accrue any direct financial return by way of speculative capital gain. The members' economic rewards for their investment was a fixed rate of interest and the ability to trade with the co-operative and receive market prices without credit or profit taking. Any profit generated by the co-op was to be distributed to members commensurate with the amount of patronage each member provided. Some profits were to be set aside for the common good of enhancing member education and welfare (Fairbairn 1994).

Over the years the nature of the co-operative business and how it deals with members' ownership rights and benefits has evolved. By the 1930s there was a move towards the payment of fixed interest rates on investment capital and for member-investors to have first claim on any profits, after paying out expenses and interest charges in proportion to purchases or patronage (Hall and Watkins 1937). How members' ownership rights and rewards for differential levels of patronage are

recognised has been one of the most complex areas of co-operative governance for much of the past 200 years (Fairbairn 1994).

### **Design of the Co-operative business and generic problems**

According to Staatz (1987) the co-operative business suffers from two limitations. The first limitation is the way individual members are able to secure incentives for their membership. A second limitation is the lack of common interest amongst members who are often motivated by different goals. In many respects the co-operative is an alliance or strategic coalition of otherwise individual smaller businesses (e.g. farmers, small retailers), or households (Staatz 1983; Sexton 1983; 1986). Others have identified a series of “generic” problems that beset the co-operative and often threaten both its success and survival (Cook and Iliopolous 1999; Nilsson 1999; Hardesty 2005).

The first of these generic problems is the risk of members’ free riding, by either not giving all their patronage to the co-op, or joining the co-op late and reaping the benefits of the investment made by more established members without having to pay a premium price for share capital (Cook 1995). A second problem is related to the different horizons that the member and the co-op’s board have about the future strategic direction of the organisation. For the member, their strategic horizon is often much shorter than is the case for the Board of the co-op. This problem is also accompanied by a third problem relating to the portfolio of assets that are controlled by the member (as a farmer or small business owner), and the co-op board; which has the collective needs of the entire membership as its responsibility. These horizon and portfolio problems often lead to members pressuring the co-op to pay out dividends or lower service fees so as to satisfy their short term interests, rather than investing in the long-term development of the co-op for the benefit of all members (Nilsson 1999).

Other “generic” problems that co-ops face are those relating to control and influence costs (Cook 1995). These relate to the divergence of interests between the members and the co-op board and management. They impact on the managerial need to find an appropriate balance between satisfying the needs of the member, while simultaneously looking after the wider needs of the co-op and the broader membership are inherently complex challenges (Cook and Iliopoulos 1999). In co-ops where the members are primarily interested in seeking benefits from patronage and can best obtain such benefits via collaboration the co-operative is likely to be sustained (Nha 2006). For example, in

agricultural producer markets, co-ops typically help to set or stabilise market prices (Haller 1992).

However, where the members begin to see their investment in the co-op as being of more value than their patronage, the pressure to demutualise and move towards becoming an IOF emerges as a major threat (Nilsson 2001). An attempt to address these generic problems and avoid the risk of demutualisation has seen the emergence of new approaches to how share capital is allocated and patronage rewarded within co-operatives (Chaddad and Cook 2007). In the United States during the 1990s the so-called “New Generation Co-operatives” emerged, which sought to better recognise member ownership rights by allowing share capital to be accumulated through patronage, and both valued and traded, but linked to the volume of a member’s patronage with the co-op (Cook 1995; Cook and Chaddad 2004).

### **The importance of member identity, commitment and loyalty**

While these economic benefit issues relating to the need to balance the member’s roles as a patron and investor continue to be important, there is a concurrent perspective that highlights the need to recognise the critical role of member identity and commitment (Fulton 1999). The co-op builds its members’ commitment around trust and the sense of identity with a collective organisation (Ole Borgen 2001). The co-op’s ability to engender loyalty and commitment from its members is likely to depend on its ability to develop a reputation for being effective as an agent for its members, which works to enhance members’ economic and social well-being (Fulton and Giannakas 2001).

Research into the nature of how trust works in co-operatives suggests that it needs to be viewed as grounded in both cognitive processes and affective responses (Morrow, Hansen and Pearson 2004). This indicates that member trust in the co-op’s board and management results in enhanced levels of satisfaction and commitment to the co-operative’s strategic goals (Hansen, Morrow and Batista 2002). Other research has found linkages between member property rights and trust. According to James and Sykuta (2005) a positive correlation exists between property rights, organisational structures that engender a perception of equality and mutual interest, and member trust in the co-operative. However, there is more work to be done in understanding this dynamic. As others point out, there is a potential trade off that emerges when the co-operative begins to move from the traditional co-op structure to a more IOF like entity such as the US New Generation Co-operatives.

By introducing changes to property rights and share ownership that shift the focus away from patronage towards investment, the co-op risks damaging its members' trust and commitment (Cook and Iliopoulos 1999).

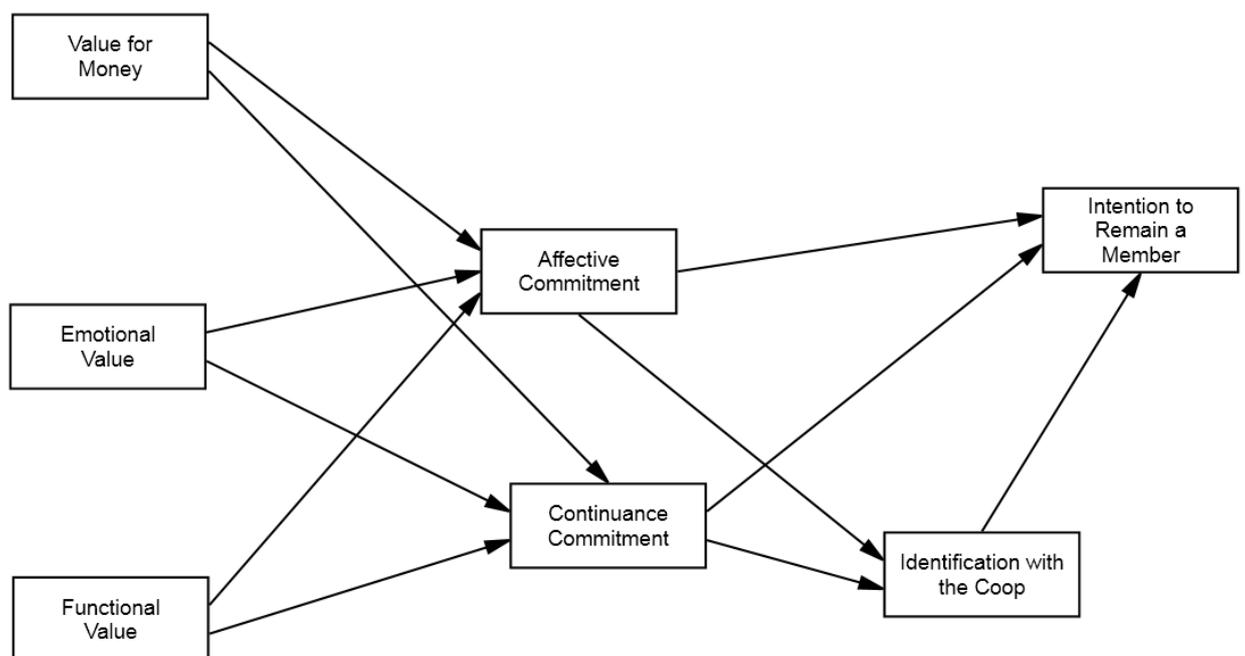
### **The need for further research and the lessons from marketing science**

There is a need for more research into the nexus between member benefits through patronage, member property rights, organisational design and member, identity, trust and loyalty with the co-op (James and Sykuta 2005). Further, this research needs to involve more robust methodologies (Morrow et al 2004), and the trade-off between member engagement for economic benefit and member sense of participation in a more social purpose (Nippierd 1999; Nembhard 2002). In seeking to address these gaps in the extant literature much can be learnt from the work already undertaken in the field of marketing. The field of marketing science has undertaken numerous studies aimed at measuring customer perception of value (Sweeney and Soutar 2001), customer loyalty (Bloemer, deRuyter and Wetzels 1999), and trust (Brunetto and Farr-Wharton 2007).

According to Dick and Basu (1999) consumer loyalty is based on the customer's attitude towards a given product or service provider, and their desire to continue their patronage is mediated by social norms and situational factors. Consumer loyalty is also understood to be related to customer satisfaction, which is frequent or cumulative. It moves through distinct phases that are cognitive, affective and conative, and finally action oriented (Oliver 1999). Early research suggested a relationship between customer loyalty and service quality (Zeithaml et al 1996), although there was some contrary findings (Cronin and Taylor 1992) that has been accredited to measurement issues and the influence of mediating factors (Zeithaml 1988; Dick and Basu 1994). For example, the nature of perceived value is a multidimensional construct that is determined by trade-offs over price, quality, emotional rewards and social acceptance (Sweeney and Soutar 2001; Sanchez-Fernandez and Iniesta-Bonillo 2009).

To examine these issues we developed a conceptual model as illustrated in Figure 1. This proposes that the member's decision to remain a member of their co-op is influenced by their perception that their membership offers value for money and functional value (e.g. good service) (Söderland 2002). However, we also assumed that emotional value (e.g. how they felt about their

relationship) would also play a role as this is consistent with what is already known about customer perceived value (Sweeney and Soutar 2001). However, the model also assumed that these three factors would be mediated by affective commitment and continuance commitment. In their study of a person's commitment to an organisation, Allen and Meyer (1990) identified the importance of affective, continuance and normative commitments. The first relates to the individual's emotional attachment to, identification with, and involvement in the organisation. Continuance commitment is their sense that they should remain loyal to the organisation because to leave it would incur costs. Also added to the model was the importance of the member's ability to identify with the co-op. This draws upon the theory that co-ops are formed as a result of community identity (Birchall and Simmons 2004), as well as the social identity theory (Tajfel 1978).



**Figure 1: The Theoretical Model of Co-operative Member Loyalty**

## METHODOLOGY

To test the model a pilot study was undertaken involving a survey of members from a large agricultural co-operative. A questionnaire was developed that measured nine constructs with a total of 48 items that were drawn from the literature or developed specifically for this study. Table 1 lists

these and provides an example of each item. The pilot questionnaire was distributed as part of an annual member survey circulated to around 2,500 farmers of whom 770 replied, providing a response rate of around 31%, which is very good for this type of survey and suggests the results provide a good snapshot of members' views. The data were analysed in a variety of ways to better understand the relationships of interest and the results obtained and their implications are discussed in subsequent sections.

## THE RESULTS

In the initial data analysis phase, the various scales that were included in the co-operative members' value model were examined to ensure they had appropriate measurement properties. The initially suggested items came from a variety of sources, as can be seen in Table 1, which also provides example items and the initial number of items used to measure the constructs of interest. As the constructs were to be used to estimate an underlying member value model, it was seen as being important to ensure they had acceptable measurement properties. Consequently, confirmatory factor analysis procedures were used to examine this aspect, as they allowed an examination of the constructs' unidimensionality, reliability, convergent validity and discriminant validity. These aspects are discussed in turn.

**Table 1: The Study's Constructs**

Construct	Sample Item	# of Items	Source
Functional Value	The co-op can be counted on to perform well	6	Sweeney and Soutar (2001)
Emotional Value	I feel good about my relationship with the co-op	6	Sweeney and Soutar (2001)
Value for Money	I am sure the co-op is worth the money it costs me	3	Sweeney and Soutar (2001)
Affective Commitment	I am proud to be associated with the co-op	12	Allen and Meyer (1990)
Continuance Commitment	I would give up a lot if I left the co-op	5	Allen and Meyer (1990)
Co-operative Identification	I feel like an owner of the co-op	5	Developed in the Present Study
Community Aspects	I give back to my community through my involvement with the co-op	3	Developed in the Present Study
Intention to Stay with Co-op	I plan to remain a member of the co-op in the future	3	Söderlund (2002)

Unidimensionality can be assumed if the suggested constructs fits the data well and their standardised coefficients are significantly different from zero and greater than an absolute value of 0.60 (Bagozzi and Yi 1988). In this case, the chi-square statistic was used to assess for and items were removed from some of the constructs to ensure the remaining items fitted the data. This was seen as important as one of the purposes of the present phase of the study was to reduce the total number of items in subsequent phases. In order to ensure there had been no loss in information in reducing the number of items, correlations were computed between the revised scales and the initially suggested scales, as suggested by Thomas, Soutar and Ryan (2001). Following Fornell and Larcker's (1981) suggestion, construct reliability and AVE scores were also computed for each construct to test reliability and convergent validity. The results obtained are shown in Table 2.

**Table 2: The Constructs' Measurement Properties**

Construct	Goodness of Fit <sup>1</sup>	Final # of Items	Range of Coefficients	Construct Reliability	AVE Score	Correlation with the Initial Scale
Functional Value	4.44 (5, 0.49)	5	0.72 – 0.86	0.90	0.64	0.99
Emotional Value	4.52 (2,0.11)	4	0.75 – 0.87	0.87	0.63	0.95
Value for Money <sup>2</sup>	0.10 (1,0.93)	3	0.77 – 0.86	0.86	0.68	na
Affective Commitment	4.35 (5, 0.50)	5	0.71 – 0.81	0.88	0.59	0.97
Continuance Commitment <sup>2</sup>	0.28 (1, 0.60)	3	0.61 – 0.79	0.75	0.51	0.92
Co-operative Identification <sup>2</sup>	0.54 (2, 0.76)	3	0.67 - 0.77	0.75	0.51	0.98
Intention to stay with Co-op <sup>2</sup>	1.99 (1, 0.16)	3	0.77 – 0.86	0.87	0.70	na

1 Chi-square statistic, with degrees of freedom and significance in parentheses

2 As there were only three items, two error variances were constrained to be equal to obtain the desired degree of freedom

As can be seen in Table 2, all of the constructs had very good measurement properties. Further, as can be seen from the final column in Table 2, no information was lost when items were removed from a construct to ensure acceptable measurement properties, as the correlations between

the scores when all of the items were used and the scores when the revised items were used ranged from 0.92 to 0.99.

**Table 3: AVE Scores and Shared Variances**

Construct	Functional Value	Emotional Value	Value for money	Affective Commitment	Continuance Commitment	Co-op Identification	Intention to stay with Co-op
Functional Value	0.64						
Emotional Value	0.70	0.63					
Value for Money	0.55	0.58	0.68				
Affective Commitment	0.62	0.75	0.56	0.59			
Continuance Commitment	0.38	0.44	0.40	0.46	0.51		
Co-op Identification	0.48	0.59	0.46	0.58	0.40	0.51	
Intention to stay with Co-op	0.49	0.52	0.42	0.57	0.53	0.47	0.70

The discriminant validity of the various constructs was also assessed using the approach suggested by Fornell and Larcker (1981), in which the shared variances between the constructs (i.e. the square of their correlations) are compared to their AVE scores. If the AVE scores of any pair of constructs have AVE scores that are greater than their shared variance, discriminant validity can be assumed. In this case, the shared variances and the AVE scores can be seen in Table 3. As can be seen from the table, a small number of the shared variances exceeded the smaller of the two AVE scores, although there were no pairs for which this difference was very great, as the largest shared variance was 0.75 (between affective commitment and emotional value). Consequently, it was decided to also check whether all of the correlations were significantly less than one, as this has also been suggested as a measure of discriminant validity (Bagozzi and Yi 1988; Sánchez-García and Currás-Pérez 2011). A bootstrapping approach with 1,000 bootstraps and a 95% confidence interval, which is provided in SPSS, was used to do this. As the upper limit was of interest, only these values were examined. It was found these values ranged from 0.67 to 0.86, suggesting that, while there positive relationships, it

was reasonable to assume all of the constructs had discriminant validity and that the constructs should be examined separately in the subsequent analysis.

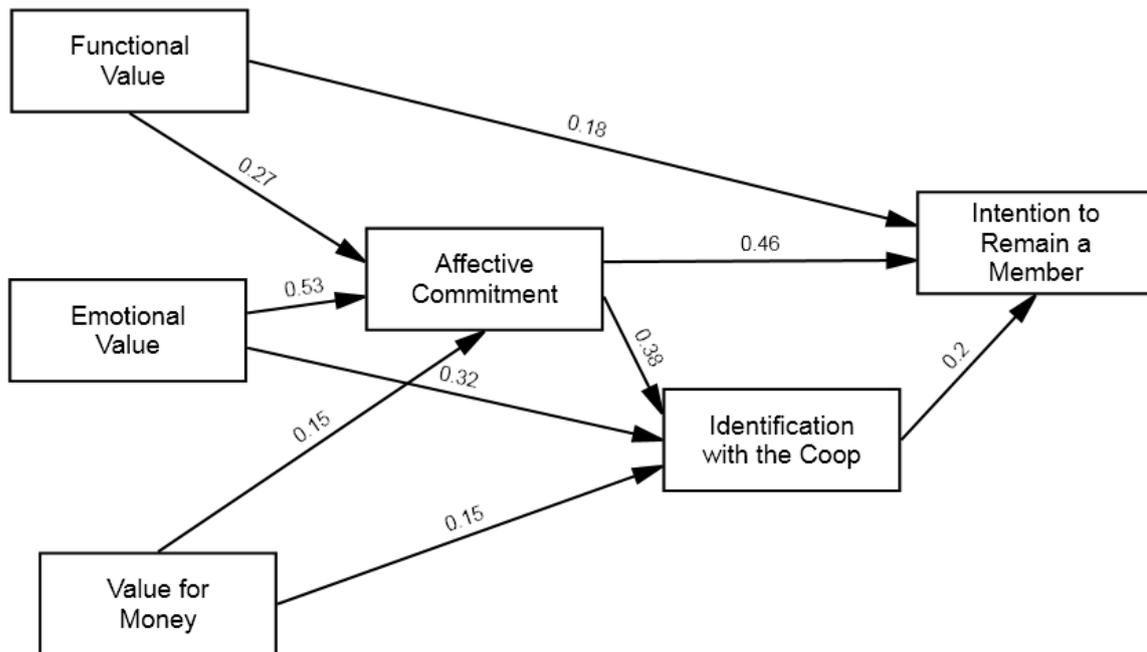
Before examining the relationships between the constructs, it is useful to examine their descriptive statistics. Consequently, means and standard deviations were computed for each of the eight constructs. The means and standard deviations on the 5-point scale used, which ranged from strongly disagree (1) to strongly agree (5), can be seen in Table 4. Overall, respondents had a moderately positive view of the Co-op, with the means ranging from a value of 3.41 (value for money) to 4.04 (intentions to stay), although the standard deviations on the 5-point scale suggested there was reasonable variability in these responses. Interestingly, the highest mean was for the intentions construct, suggesting most respondents intended to stay as customers of the coop.

**Table 4: Means and Standard Deviations**

Construct	Mean	Std Deviation
Functional Value	3.72	0.63
Emotional Value	3.65	0.63
Value for Money	3.41	0.75
Affective Commitment	3.84	0.64
Continuance Commitment	3.74	0.66
Co-op Identification	3.54	0.70
Intention to stay with Co-op	4.04	0.55

Of more interest were the relationships between the constructs, which was shown in Figure 1. As can be seen in that figure, it has been suggested that the three value components (value for money, emotional value and functional value) influence members' commitment (affective and continuance) to the Co-op that, in turn, influence members' identification with the Co-op and, subsequently, their intention to remain a member of the Co-op. This model was therefore estimated using the AMOS Structural Equation Modelling software (Arbuckle 2010). However, the initially suggested model did not fit the data very well (chi-square statistic = 117.6, df=7;  $p < 0.001$ ), suggesting some revisions were needed. An analysis of the significance of the paths and the modification indices suggested the removal of the continuance commitment construct and some alternations to the initially specified

paths, leading to a revised model, which can be seen in Figure 2. The revised model fitted the data well (chi-square statistic = 5.54, df=3;  $p < 0.14$ ) and all of the paths were significant well beyond the 1% level, suggesting it was worthwhile to look at the relationships in detail.



**Figure 2: The Revised Model**

As can be seen from the standardised coefficients that are shown in Figure 2, emotional value seemed to have the strongest impacts on the constructs it was thought to influence (affective commitment and identification with the co-op), while functional value and value for money had smaller impacts. Further, functional value, affective commitment and identification with the co-op both influenced people’s intention to remain a member, although affective commitment seemed to have a greater impact than the other two constructs. The construct “overall value” was

These perceptions were examined further by undertaking a bootstrapped estimation of the model with 2000 bootstraps and 90% confidence intervals to ensure stability. In the first instance, the lower values of the emotional value coefficients were 0.47 and 0.24 respectively, while the upper limits for value for money relationships were 0.20 and 0.22 respectively and the upper limit for functional value’s relationship with affective commitment was 0.20, confirming the suggested

strengths of these relationships. Similarly, the lower limit of the affective commitment – intention coefficient was 0.38, while the upper limits for the functional value and identification with the co-op coefficients were 0.26 and 0.28 respectively, confirming the relative importance of affective commitment.

As there were mediating variables in the model, it was also seen as being important to examine the total effects (i.e. the direct and indirect effects) that the various constructs had on people’s intention to remain a member of the co-op. The AMOS software provides this information, which is shown in Table 5, in which the final row (intentions) is of most interest. As can be seen in the Table, affective commitment seemed to have the greatest impact on peoples’ intention to remain a member, followed by emotional and functional value, with the other constructs seemed to have less effect. This view was again examined through the bootstrap results. The lower bound for affective commitments’ total effect was 0.47, while the upper bounds for functional value and emotional value were 0.38 and 0.41 respectively, supporting the initial suggestion. Further, the lower bounds for functional value and emotional value were 0.27 and 0.30 respectively, while the upper bounds for value for money and identification with the co-op were 0.14 and 0.26 respectively, suggesting emotional and functional value had greater effect.

**Table 5: Standardized Total Effects**

Construct	Value for Money	Emotional Value	Functional Value	Affective Commitment	Identification With the Co-op
Affective Commitment	0.15	0.53	0.27		
Identification With the Co-op	0.21	0.53	0.10	0.38	
Intention to Remain a Member	0.11	0.35	0.32	0.54	0.20

## CONCLUSIONS AND IMPLICATIONS

What is clear from this analysis is that it is the emotional connection members have with the co-op (i.e. emotional value and affective commitment) that are the key drivers of loyalty (intention to remain a member). Managers need to be aware that, while functional value and value for money have some impact, these are not as important as the emotional constructs. This has some important implications as it suggests that member loyalty to the co-op may be built on foundations that are stronger than a pure transaction cost relationship. The co-operative's ability to deliver good economic benefits to its members is clearly important (Tennbakk 2004), particularly within agricultural supply chains (Giannakas and Fulton 2005). The co-operative plays a critical role in many markets by empowering the smaller producers and helping to "keep the market honest" (Drake and Llewellyn 2001), and enriching the overall "biodiversity" of the business environment (Haldane 2009). However, the ability for the co-operative to engage the membership on a much more emotional and affective level, leading to enhanced identification with the organisation, seems to be of significance in determining whether they will maintain their loyalty.

The importance of member identity and commitment to the co-operative has been recognised in the academic literature for some time (Fulton 1999; Cotterall 2001; Fulton and Giannakas 2001; 2007). Previous studies have also highlighted the importance of both cognitive and affective dimensions on the development of trust and commitment by members in their co-operative (Hansen, Morrow and Batista 2002). This study builds on this work and underlines the importance of co-op managers and boards in recognising that as member-owned businesses they have a potentially different relationship with their members than is the case for IOF. Members are not just customers or suppliers, nor are they investors. Their roles as patrons, investors, owners and members of a wider community are all very important, albeit complex, aspects of their intention to remain with the co-op.

For managers and boards of co-operatives this study's findings imply the need to engage with members on a much wider and deeper level than simply seeking to offer good value for money and quality services. Members seem to also have emotional value and affective commitment drivers that enable them to identify with the co-op and retain their loyalty to it. However, our study has some

limitations. It was only a pilot survey designed to test the scales and assess the general validity of our theory. Further research is needed before too many general conclusions can be drawn. The co-op that was surveyed was an agricultural co-operative and may have unique characteristics that will not transfer onto other types of enterprise. For example, retail co-ops, co-operative banks or financial mutual businesses may have quite different dynamics. In those institutions the dependency of the member on the co-op and their overall level of engagement with it may be reduced. Future research will aim to explore these issues through the collection of a larger sample with members drawn from a wider range of co-ops of different kinds. However, if future research does suggest that emotional value and affective commitment have strong or equal importance to financial and functional value in determining member loyalty, it will have significant implications for how co-ops are managed.

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