

**EVOLUTION, GROWTH AND DECLINE  
OF THE COOPERATIVE SECTOR  
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## **Introduction**

Cooperatives are user-owned, user-controlled and user-benefited organizations. They could be agricultural, non-agricultural, unions or Savings and Credit Cooperatives (SACCOs). They operate in different sectors of the Economy including agricultural, handicraft, Jua Kali, transport, housing development, building and construction, consumer services, banking and insurance.

In Kenya, cooperatives and in particular agricultural cooperatives do play a major role in production, primary processing and marketing of agricultural and livestock commodities. The general objective of the organizations is to promote the economic interests and general welfare of members in accordance with cooperative values and principles. The performance of Agricultural cooperatives is critical in economic growth and poverty alleviation in the country.

The justification for cooperatives arises from their potential in maximization of profits, harnessing various skills with members, enhancing advocacy and bargaining power, enhancing financial accessibility, boosting social capital, promoting investment, providing educational opportunities, improving market access and contributing to poverty reduction.

The crucial roles of cooperative movement or producer organizations are well recognised and stipulated in the Strategy for Revitalizing Agriculture (SRA). It is clear that Kenya's agriculture is predominantly small scale accounting for 70% of the total agricultural output and 70% of marketed agricultural produce. Processing and marketing is organized through farmers' organizations,

cooperatives and statutory bodies. Through the SRA, the government recognises the need for urgently improving management structures and accountability of cooperatives. The organisations are expected to take over the roles that were previously undertaken by Statutory Boards and Parastatals.

## **Evolution of Cooperatives and Genesis of Problems Plaguing the Movement**

### ***Pre- independence Era***

Informal producer organizations have been in existence in Kenya even before colonial period. However, formal organizations particularly cooperatives started as early as 1908 and membership was limited to white settlers. The first cooperative was established at Lumbwa - Rift Valley, in present day Kipkelion area.

In 1944 colonial officers opened the door for Africans to form and join cooperatives. It was also recommended that a registrar of cooperatives be appointed. In 1945, a new Cooperative Societies Ordinance was enacted which allowed African participation in the cooperative movement. In 1946, a department of cooperatives was established and a registrar of cooperatives appointed. By 1950 most colonial civil servants began to support and encourage the development of cooperatives and by 1952, about 160 cooperatives had been registered.

The *Mau Mau* rebellion of early 1950s had a negative effect on the cooperative members of staff who withdrew to join pro-independence forces. However cooperatives continued to grow. The reason for this growth was application of the *Swynnerton* plan of 1954 on Developing African Agriculture and

Improving Land Tenure. By 1958 there were over 400 registered cooperatives.

***Post- independence but Pre-liberalization Era***

The post independence era saw the rapid rise in number of producer organizations and the consolidation of the ones that already existed. At this time, the government saw the cooperative movement as a vehicle to the introduction of African socialism, and for strengthening common ties between the people from different regions of Kenya. In 1963 there were about 1000 cooperatives, which rapidly grew in number to 7000 by 1999.

The need to build human capacity and increase the capitalization of the cooperatives saw significant government initiated donor assistance to cooperatives to rectify the many personnel and capital related constraints that were affecting them then. Indeed, in 1967, the government initiated The Kenya Nordic Cooperatives Development Program (KNCDP), which was funded by donor agencies of the Nordic countries. Donor assistance was also sought from the World Bank, United States, and Germany.

The government also extended subsidized services to the cooperatives movement such as access to government interest rate controlled credit and free extension service through the then newly formed Ministry of Cooperative Development (this became a full ministry in 1974). Producer cooperatives were also directly linked to government parastatals. No individual private traders were allowed to compete with cooperatives. Cooperatives were linked to state run marketing corporations like National Cereals and Produce Board, Cotton Board of Kenya, Pyrethrum Board of Kenya, Coffee Board of

Kenya, Kenya Meat Commission, and Kenya Cooperative Creameries. Most of the cooperative members' produce was sold to these corporations and the latter then linked the cooperatives to the world market. These linkages excluded the participation of private traders in the marketing of the agricultural produce.

However, this cooperative setup was not without certain demerits. Firstly, problems that affected the corporations directly affected these cooperatives. The former experienced high transaction costs as a result of inefficiencies in their operations. Payment to cooperatives was then reduced and delayed for long periods. These cooperatives and other producer organizations attached to the corporations became weak or totally collapsed. For instance, a two-year delay in pyrethrum payments in early 1990s initiated a period of extended decline in production as farmers became disenchanted with the crop and uprooted it. This caused an almost collapse of pyrethrum cooperatives in the country.

The direct intervention by the government in management of cooperatives compromised the principles of member owned and run organizations. Government involvement hindered the emergence of member-controlled cooperatives since members relied on government to safeguard their interests. As a result, equality, equity, solidarity, democratic principles, self-responsibility, and self-help that are important pillars of successful producer organizations were thus hindered. This caused the cooperatives to be run as if they were government owned instead of privately owned member organizations.

***Era of liberalization, structural adjustment programs and privatization***

Since the early 1980s, most countries in Sub-Saharan Africa have been undertaking economic reforms under the Structural Adjustment Programs (SAPs). The SAPs were intended to accelerate economic growth through liberalization and structural reforms. In line with these policies, the Kenyan economy has undergone major transformations. Wide ranging trade and macro economic policies that impact on production costs, incentive structures and the competitiveness of various sectors have been implemented.

In 1986 the government introduced a Sessional Paper on 'Renewed Growth and Economic Management of the Economy'. The paper stipulated that the government would move towards liberalization with a view to, among other things, remove all monopolistic trends, divest government investment in commercial activities, and encourage the private sector to get more involved in the running of formerly government owned and run parastatal organizations.

The 1990s saw the promotion of regionalization and globalization policies whose key component has been reduction or removal of tariff and non-trade barriers to trade across countries. The reduction and removal of tariff and other trade barriers have resulted in withdrawal of direct and indirect protection to domestic competition.

Prior to liberalization, agricultural markets were characterized by pervasive government controls. After liberalization, there were reforms that included: removal of price controls, liberalization of domestic and external trade, decontrol of interest rates, introduction of foreign exchange retention schemes and liberalization of exchange rates, tax reforms and

Government expenditure rationalization. The reform process was expected to reduce costs in input and output marketing systems by encouraging more private sector participation in the market. During this period, the Kenyan economy was experiencing adverse economic conditions. In addition, serious indiscipline had emerged in the financial sectors leading to the collapse of a number of financial institutions. As a result, cooperatives, which were banking with these institutions, ended up losing large deposits in the collapsed banks.

The liberalization period brought a wind of change in the structure and the running of the cooperatives. Having been fully dependent on the government for the control of markets and funding, it was difficult for them to suddenly start operating on their own. These institutions were not prepared to compete with private firms that brought in high levels of competition.

The advent of economic and political liberalization in early 1990's heightened the need for liberating cooperatives from government control. A new policy was consequently formulated by 1997 to provide for a member based, autonomous and member controlled movement. The aim was to enable cooperatives make independent decisions concerning operations of their business and to have a level playing ground like the rest of the private sector. New legislation was also put in place to implement this policy the same year.

The Sessional Paper no. 6 of 1997 outlined the government's role as facilitative in nature i.e. create an enabling environment for cooperatives to operate. The other role was regulatory particularly in the

formulation of policies and legislation. This meant no direct involvement in the running of the cooperatives.

Liberalization saw the mergers and splits of various cooperative societies. They split into small uneconomic units. High levels of mismanagement mainly fueled this, and other factors beyond management's control, like fluctuating market prices. Political influences could not be avoided and some individuals in management used their positions to gain political leverage.

The Cooperative Societies Amendment Bill of 2004 sought to re-introduce some degree of government control. As much as the government should not completely leave the cooperative sector alone without any form of regulation, it should explicitly define a clear point of intervention without prejudicing its own efforts of embracing the principle of a free market economy.

**Role of agricultural cooperatives**

The main task of agricultural cooperatives has been to collect farmers' produce, store it and then transport it to designated buyers and agents. They also received payments for the produce delivered and passed this to the members. In addition, cooperatives have been important in the delivery of various inputs including fertilizers, pesticides, fungicides and other crop protection chemicals, pumps for spraying crops and livestock dairy meal and other materials essential in the dairy industry. These roles have however diminished following collapse of the organizations.

**Structure of cooperative movement**

The structure of agricultural cooperative movement in Kenya has individual members at the bottom of a

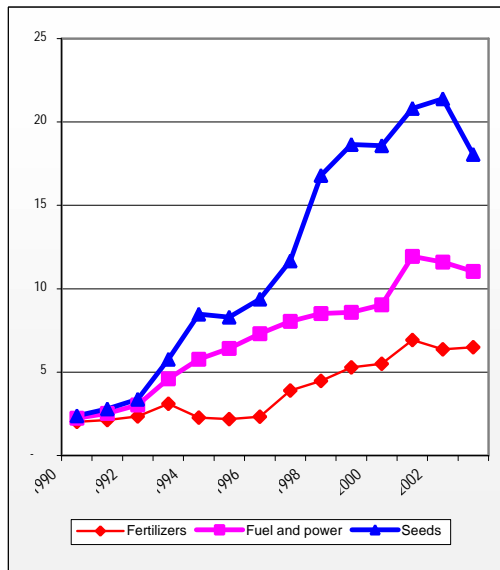
pyramidal organisational structure and the Kenya National Federation of Cooperatives (KNFC) at the top as apex body. SACCOs fall under Kenya Union of Savings and Credit Cooperative Union (KUSSCO) under a similar structure.

In case of agricultural cooperatives members comprise of farmers producing coffee, cotton, milk and so on. On the other hand, in the case of SACCOs members generally consist of workers under the same employer. Cooperatives are entities well recognized by the Law of Kenya. Cooperative Societies join at regional level to form Cooperative Unions. The apex body of cooperatives in the country is KNFC. KNFC handles issues of both national and international policy that have a direct bearing on the cooperative movement.

**Structural and managerial factors attributed to poor performance**

The factors that have influenced the performance of cooperatives particularly in the liberalized era are: Lack of training and preparedness by cooperatives, Poor sequencing of the reform policy, Loss of government protection, Political interference, Inadequate legal reform, Slow decision Making process, Government policy and international prices, Infrastructure and weather conditions, Competition from other players such as hawkers and private processors, High cost of farm inputs. Figure 1 gives an indication of the increasing cost of farm inputs over time.

**Figure 1: Agricultural Input Price Indices, 1990 - 2003 (1982 = 100)**



Source: Economic Surveys

### **Impact of collapse of cooperatives on performance of agriculture**

Although there are a few cooperatives that have been successful in the challenging liberalized and privatized economy, most cooperatives have performed poorly. They are unable to provide their members with services and support that they initially were formed to provide. The weakening of these cooperatives has affected food security and income of the members.

Analysis of trends in performance of major crops revealed the impact of collapse of cooperatives on agriculture. Based on data from national economic surveys, Ministry of Agriculture Crop Development Division and FAOSTAT, this study observed unfavourable trends in performance of most agricultural crops.

Coffee production declined by more than 50% between 1988 and 1998. The decline in cooperatives' production was more pronounced (61%) than the estate sector. The liberalization of the coffee sector was poorly timed, was wrongly sequenced, was not well monitored and

lacked preparation of the stakeholders. Cooperative societies, Unions, marketing and input agents that offered services like credit, farm inputs and extension services were adversely affected.

Tea has generally experienced an increase in production and favourable international prices. It has had record performance in production, yield and earnings. The increase in tea production is attributed to both the expansion in area and increases in yields. Between 1979 and 2001, area increased by about 53 percent while the yields have more than doubled. The largest increase in production has been by the small-scale producers. Increase in tea yields may be attributed to an effective system of providing farm inputs particularly fertilizer to farmers through tea factories that are run by farmers' representatives (Board of Directors). Tea payments have also increased thus raising the earnings per unit production thereby motivating farmers to invest in tea. The tea industry also realized an expansion in tea processing capacity hence reducing the factory congestion that used to limit area expansion. Capacity expansion also has ensured tea quality and hastened payments to farmers.

Similar to tea, horticulture has registered positive growth and this is attributed to efforts of private sector in conjunction with Government agencies. Export horticulture industry is shifting toward higher value per unit products like vegetable pre-packs and flowers, and away from bulk packed French beans that used to be a prominent driver of tonnage. Formation of producer groups in the industry is being promoted as a viable strategy to overcome the challenges facing the industry.

Pyrethrum in Kenya is entirely done by small-scale farmers most of whom are organized in cooperatives. The cooperatives are involved in collection of flowers, drying and delivering to the Pyrethrum Board of Kenya on behalf of farmers. Following the liberalization of the agricultural sector, the pyrethrum cooperatives have been weakened. As a result, they are unable to support the producers. This coupled with other problems affecting the pyrethrum industry have caused pyrethrum production to decline. Other factors that have influenced this production includes adverse weather conditions; ethnic clashes; low profitability of the pyrethrum enterprise; competition from other enterprises; the labour intensive nature of the crop; unavailability of planting material; and inadequate extension services among others.

Cotton is a key industry crops in Kenya yet its production had over time declined. The reduction in the importance of cotton in Kenya was largely attributed to the collapse of cooperatives that had supported farmers to produce and market the crop. The decline in cotton production is attributed to the reduction of purchased inputs particularly insecticides.

Sugar production in Kenya has stagnated at 400,000 tons while domestic consumption has been increasing and by 2001 it was estimated at over 600,000 tons. The gap between the production and consumption has been increasing. But the decrease in production is not the only challenge facing the domestic sugar production. Its cost of production and processing are more than double that of sugar from other countries such as Sudan. As a result, sugar consumers pay up to three times the world price for sugar.

The production of maize has been fluctuating with a general declining trend. The deficits of maize production in the country have normally been corrected by imports. Given a rising population and no dramatic change in tastes, imports of maize could be 65 percent as large as domestic production by 2010.

Wheat production is projected to decline given current trends in production – that is stagnant or declining- and rising demand, consumption and imports. Large tracts of land on which competitive wheat systems may be expanded or developed on a sustainable basis do not exist in Kenya. Recent institutional agreements between the government, growers and importers have given the wheat industry some breathing space and protection, but maintaining current production is probably a best-case scenario. If the domestic wheat marketing agreement is not sustained, if COMESA neighbours object to the restrictions and taxes on bringing wheat into Kenya then much of the domestic industry will be under threat.

On the whole, cooperatives have been unable to provide farmers with credit and farm inputs for financing production. Households thus have been unable to produce enough staple crops for their own consumption. The fall in income from the sale of food crops have also implied that disposable incomes used to buy food requirements from the market have fallen. This has therefore adversely affected household food security. Other household needs such as school fees and medical have equally been adversely affected.

### **Conclusions and recommendations**

To maximize benefits from the increasingly segmented pieces of land, it would be important for small-scale farmers to form or join groups that will enable them benefit from economies of scale among others.

The poor performance of cooperatives after liberalization as a result of the hasty implementation of the policy underscores the need for training and preparedness for such reforms.

Helping producers get organized and strengthening their capacity is one of the ways to contribute to the fight against rural poverty. Strengthening cooperatives capacity is also an investment in social capital that complements investments in other forms of capital: human, physical and financial. In order for cooperatives to really contribute to reducing rural poverty and play other essential roles effectively, specific actions must be taken to help strengthen them. Building of the capacity of cooperatives should improve their bargaining power, and thus contribute to a more growth enhancing allocation of public goods at all levels – local, regional and national.

Within local communities, strong cooperatives provide the backbone for development of the agricultural sector. Cooperatives facilitate development of agriculture and agricultural related activities, thereby, increasing the local resource base needed to finance local public services or investments.

Cooperatives can contract with processing and marketing enterprises to deliver production extension services to farmers as a part of the credit -input package. Development of effective contract enforcement mechanisms is in this regard deemed essential.

To promote growth and ensure that the poor participate in and from the growth, a number of policy measures will need to be put in place. First, maintenance of a stable macroeconomic environment while improving the allocation of public spending is imperative. Second, improving food security, by increasing the productivity of smallholders and facilitating the move of smallholders away from production for subsistence towards more commercialised agriculture. Third, strengthening competitive environment and build firms' capabilities for investment by improving governance, and improving the delivery of services (energy, telecommunications, transportation, and water). Improved rural infrastructure is critical to success of cooperatives.

Unlike SACCOs that participate in annual ratings in large numbers, only a few agricultural cooperatives are involved. It would be important for all cooperatives to be encouraged to participate in competition for the *Ushirika* day. This would promote efficiency and transparency in activities of the cooperatives.

### **Interventions Necessary to Revitalize Agricultural Cooperatives**

The performance of cooperatives in the liberalized economy in terms of providing services to farmers has been poor. There is therefore need to assess how government, donors and other stakeholders could support the cooperatives to enable them evolve as organizations that supports members in a more sustainable way.

#### ***Legal reform***

Cooperatives require assistance to formulate, finalize and implement legal reforms to bring them in tune with economic reforms. In particular, cooperatives requires assistance in preparation and review of cooperative

Society by-laws, training of cooperative leaders and members on these by-laws and training members on their rights and obligations under the new Cooperative Society Act. Assistance also needs to be provided in formulating a code of conduct for cooperative society members management committees and employees that would be enforceable legally.

***Development of a model for cooperatives management and accounting systems***

To overcome the problem of poor and inefficient management systems, the cooperative movement requires to be assisted to invest in developing sound management and accounting models for adoption by agricultural cooperatives in a more liberalized economy. This would enhance accountability through strengthening of the watchdog systems such as improvement in accounting, budgeting, and internal and external accounting. Penalties for fraud and misappropriation of funds could also be made hush within the legal framework.

Agricultural cooperatives will require assistance in hiring qualified and experienced management employees, who could meet the new challenge of competition with other businesses. In addition assistance would be required in training such staff, particularly on the job training.

***Investment in information technology***

Areas such as information technology are important in order to ensure that transparency and accountability of cooperatives to members are assured. However, investment in such areas are capital intensive and the members may either not be able to invest in them or that they may be unable to raise the funds necessary for this. Assistance would therefore be required to enable

cooperatives invest in information gathering, inputting, processing and dissemination. Such investment includes purchase and installation of computers, related softwares and training of the personnel to run and manage them. This is likely to help the processing of production, marketing and payment data, which then could enhance timely payments to members.

***Education of members***

Most producers are still ignorant of how the liberalized economic environment operates and particularly on how it relates to the cooperatives. Poor governance has also stemmed from uninformed cooperative members who are manipulated by a few individuals in electing cooperative official. Assistance is therefore required in investing in training programs that create awareness to the cooperative members on their rights. This would in turn make them demand for good governance, transparency and accountability. Institutions such as cooperative college are poorly equipped to undertake such functions. Cooperative civil education could therefore be undertaken through the Non-governmental education while the formal training on the need and operation of the cooperative movement could still be financed through the existing cooperative institutions.

***Other interventions:***

- Support visits by new cooperatives management to successful cooperatives. Study tours to successful cooperatives at all levels are a very effective training tool.
- Arrange exposure tours for key government officials that will demonstrate how free cooperatives can successfully improve members' livelihood and cooperate with government.

- Support the development or upgrading of regional cooperative training centers.
- Most cooperative development activities should include establishing cooperatives supported market information center for key domestic and export crops that forecasts and communicates demand and prices to producers, identifies buyers, and communicates supply availability to qualified buyers.
- Develop an Africa-wide Web based network to capture and share

cooperative s' lessons learned and Best Practices.

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