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SMALL- AND MEDIUM-SCALE ENTERPRISES IN
THE UNION OF SOVIET SOCIALIST REPUBLICS: THE CO-OPERATIVE SECTOR*

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Introduction

1. There are two types of co-operative, i.e. the "traditional" one comprising collective farms, consumer and housing co-operatives, and enterprises producing consumer goods, and the "new" type, which has emerged over the past two years. Although collective farms are established according to co-operative rules, they are too large to be discussed in this context. Of the "new" co-operatives, only about 30 per cent are engaged in productive activities, the remainder being engaged in services. Government decisions from 1986 and 1987 regulated the "new" co-operatives. Co-operatives producing consumer goods may be large or small. They are increasingly restructuring their operations according to common co-operative principles with less state influence than before. Since they are engaged in the production of all kinds of consumer goods, as well as the delivery of services, and make optimum use of the available labour potential including increasing the income of the labour force, the Government encourages their establishment.

2. As at 1 January 1989, there were more than 100,000 new co-operatives. However, only 60 per cent were operating. All co-operatives employed a total of about 1 million persons, with half of them holding more than one job. Over the first nine months of 1988, all co-operatives marketed Rbl 2,623 million worth of goods and services, or about Rbl 54,000 per co-operative. As a co-operative has, on average, 16.2 employees, this figure translates into Rbl 3,331 per member. The average monthly income of a co-operative was Rbl 6,000, and average monthly earnings amounted to Rbl 123 per member.

3. 35.3 per cent of all co-operatives are engaged in services, 22.5 per cent in the production of consumer goods, 12.7 per cent in catering, 6.2 per cent in trade and procurement, 4.1 per cent in processing of secondary raw materials, and 19.4 per cent account for all remaining activities (medical care, sports, construction, consulting, etc.).

4. Table 1 gives a breakdown of co-operatives in the various Republics for the first nine months of 1988. The figures show that co-operatives are most common in the Baltic Republics, Armenia and Georgia, and less numerous in the Central Asian Republics. The largest co-operatives by turnover are in Latvia, Georgia, Moldavia and Estonia, the smallest ones in Tadjikistan, Turkmenia, Azerbaidjan, Byelorussia and Kirghizia.

Table 1: Distribution of co-operatives by Republics

<u>Republic</u>	<u>Number of operating co-operatives (thousand) (percentage)</u>		<u>Turnover for three quarters of 1988 (Rbl million) (percentage)</u>		<u>Average turnover per co-operative (Rbl 000)</u>
Russian Federation	24.1	49.7	1,389	53.0	57.6
Ukrainia	8.1	16.7	375	14.3	46.3
Kazakhstan	2.6	5.4	109	4.2	41.9
Uzbekistan	2.3	4.7	115	4.4	50.0
Byelorussia	1.7	3.5	63	2.4	37.0
Armenia	1.8	3.7	97	3.7	53.9
Georgia	1.6	3.3	115	4.4	71.9
Lithuania	1.24	2.6	62.5	2.4	50.4
Moldavia	1.0	2.1	69	2.6	69.0
Azerbaijan	0.96	2.0	34	1.3	35.4
Latvinia	0.8	1.6	90	3.4	112.5
Kirghizia	0.73	1.5	28	1.1	38.4
Estonia	0.7	1.4	48	1.8	68.6
Tadjikistan	0.56	1.2	18	0.7	32.1
Turkmenia	0.3	0.6	11	1.4	36.7

Institutional and legal aspects

5. The co-operative movement in its new form with less state intervention is only making its first steps. Decisions of the USSR Council of Ministers adopted late in 1986 and in 1987 created only a temporary and very limited basis for the establishment and operation of co-operatives set up mostly in cities. The Co-operation Act, adopted by the Supreme Soviet on 26 May 1988, expanded considerably the field of operation defined by the above decisions; it also laid down the general principles of operation of old and new co-operatives, including collective farms, consumers' and housing co-operatives. On the whole, the law creates favourable conditions for massive establishment of co-operatives in cities and the countryside in various fields. It also limits noticeably interference of government agencies in the day-to-day operation of co-operatives, as discussed further below. They also set out conditions for the establishment and operation of co-operatives of various sizes. Co-operatives may hire labour under labour contracts. Three persons are the minimum requirement for setting up a co-operative. The proportion of co-operative members and hired labour is not determined. The law does not determine earnings of either labour or co-operative members, but earnings are now strongly effected by taxation. According to the newly-adopted Decree of the Supreme Soviet Presidium of 23 February 1989, rates of the co-operatives' profit tax will be established by the republican and regional government agencies and, as a rule, will be above 35 per cent of gross profit. Hired labour and co-operative members have to

pay income tax like anybody else. The law does not determine distribution of profits. Thus, it is up to the co-operative to decide what portion of its earnings it wishes to reinvest, how much it wants to pay its members and how much it decides to spend on social costs. Share accumulation is not determined by the law either. However, the borderline to associations for operating business jointly is clear. Dividend payments are also not governed by law.

6. The Co-operation Act has proclaimed the full economic and legal independence of co-operatives as well as their legal and economic equality with state-run enterprises. This is a major achievement. However, this principle has not been proclaimed consistently enough. For instance, the purchase of raw materials and equipment is more difficult for co-operatives than for state-run enterprises. Negligible quantities of raw materials and new machinery are apportioned to them by the State Committee for Supplies, and they also have to pay higher wholesale prices than state-owned enterprises. They are forced to buy raw and other materials, food-stuffs and other goods at state-owned shops (provided these shops wish to sell to them), or at "collective farm" markets at retail prices, or through commercial advertising at contractual prices which are higher than state retail prices. Co-operatives often purchase goods through casual channels which are not always legal (e.g. so-called shadow economy). In any case, co-operatives are more affected by market shortages of raw materials and equipment than state enterprises.

7. Co-operatives are granted independence by the USSR Co-operation Act regarding economic management, planning, pricing and distribution of profits without interference of government bodies. They may elect executives and set up territorial and sectoral unions and associations. Co-operatives and their unions may establish their own credit and financial institutions, develop training activities, participate in the social security scheme, enter foreign markets and establish joint ventures with Soviet (state and co-operative) enterprises and foreign firms.

8. "Duties" of co-operatives vis-à-vis the government include registration of the statute of newly-established co-operatives with local governments, payment of taxes, basic book-keeping, observance of instructions regarding safety, labour protection, hygiene and environmental protection. Raw materials have to be used prudently. Government agencies are bound by the Co-operation Act to assist co-operatives in every way in their operations by supplying legal, economic and social information, helping with advertising, arranging for the training of their personnel and making available land, buildings and other capital goods, as well as leasing entire state enterprises. The law also decides that the government should create and maintain, through the state-owned mass media, a climate conducive to the growth of co-operatives.

Economic and financial aspects

9. In the Union of Soviet Socialist Republics, relatively small enterprises belonging to the co-operative sector co-exist with large, state-owned concerns engaged in the productive and services sectors. Thus, co-operatives complement large-scale enterprises producing consumer goods in meeting unsaturated demand. However, unlike many market economy and some other centrally-planned economy countries, their production facilities are usually out-of-date.

10. The co-operative movement is still young. Facilities are often obsolete, professional training is inadequate and deficiencies of the overall economic situation affect the sector more strongly than large industries. Thus, co-operatives are experiencing economic and financial difficulties. Many of them have not yet learned how to calculate their costs, prices and profits. Prices for consumer goods are rising due to insufficient supply of consumer goods to the markets and little competition of producers. Co-operatives therefore do not feel forced to reduce production costs and calculate prices in conformity with available markets like market economy country entrepreneurs would. Therefore, they can hardly afford to expand their businesses and buy modern machinery.

11. Marketing is still far from being perfect. Local authorities wish to sell products of co-operatives separately from products of state enterprises at special co-operative shops, special sections of supermarkets, or at special sections of "collective farm" markets. Thus, there is no real competition between co-operatives in consumer markets, all the more since "co-operative" shops and special sections of supermarkets usually belong to state retail trade enterprises. Also, the independence of the co-operatives' pricing policy proclaimed by the Co-operation Act was substantially limited by the Government Decree of 5 January 1989. Now co-operatives have to fix their prices and margins along with those of state-run enterprises.

12. However, there is very little effective control of state agencies over the operations of co-operatives, calculation of retail prices, costs, earnings and quality of products. Control exercised over the activities and issues of state enterprises is also poor. In many other countries, control is exercised on a selective basis both by special government agencies or by, for example, consumer associations in the United States of America. In the United Kingdom, the quality of food products is controlled by the Ministry of Agriculture, Fisheries and Food. In most market economy countries, producers delivering poor quality products or charging excessive prices are being fined by the court.

13. Advertising and commercial information are very important for co-operative small- and medium-scale enterprises. However, both instruments have not been adequately developed in the Union of Soviet Socialist Republics. Co-operatives have no country-wide information bulletin. Some cities, e.g. Moscow, Kiev, Tallinn and Vilnius, produce advertising bulletins on an irregular basis which are poorly designed and printed and often contain unverified information. These papers do not really meet the advertising needs of co-operatives. The press at large sometimes publishes co-operative-related figures and articles which improves the situation. However, a specialized newspaper for country-wide distribution is urgently needed.

14. Availability of financial resources poses a problem which cannot be overestimated. The financial requirements of co-operatives are only partially satisfied by specialized state banks like the Zhilsotsbank, Promstrojbank and Agroprombank. They very often refuse to extend loans to co-operatives.

15. Under the Co-operation Act, co-operatives may establish their own financial institutions. However, as most of them lack the capital required to do so, such banks exist only on paper. Less than a third of two dozen banks registered with the USSR State Bank as of 1 January 1989 had sufficient authorized capital enabling them to start commercial crediting and ensure long-term expansion of these operations. Among these banks is the First Joint State and Co-operative Bank in Leningrad with capital of about Rbl 5 million.

16. The establishment of a co-operative bank, even if it has adequate authorized capital, is only the first step. To operate successfully, the bank needs to have a sufficiently diverse and flexible strategy, use interest rates as an instrument to foster the co-operative sector and base its lending operations on an analysis of the economic and financial situation of the co-operative in question which it has prepared itself. Experienced staff should talk to the management of co-operative customers. Unfortunately, even powerful specialized state banks are unable to undertake these tasks themselves. Also, the model statute of the co-operative bank adopted by the State and providing for an arbitrarily set ceiling of interest rates and control over all operations by the USSR State Bank does not promote the development of banking business in the co-operative movement.

17. According to the Co-operation Act, the establishment of co-operative banks and other financial institutions is the prerogative of co-operative unions and associations, while the initiative regarding commercial services is fully in the hands of certain co-operatives. So far, in the Union of Soviet Socialist Republics we can trace the same effective link between financial business, co-operative industrial production and commercial services as in the market economy countries.

18. The management of most newly-established organizations and enterprises has no experience in commercial operations. Many of them do not have the necessary background and are solely guided by the principle of maximizing profits and individual earnings. Co-operatives do not operate on the basis of well-defined programmes and strategies. Lack of a "normal" business-like approach and professional management skills of small co-operatives is closely related to the overall economic environment and some juridical uncertainty of co-operative law. As a result, most of today's co-operative activities including marketing, computer programming, medical care, show business, etc. have merely filled a wide gap in the state sector of the Soviet economy.

19. Co-operatives are trying to achieve economic self-sufficiency and take a more active part in formulating the government's policy regarding co-operatives. They realize that it is necessary to merge into larger unions and associations. So far many of them have been opposed to merging for fear of "red tape".

20. Territorial co-operative unions (sometimes called co-ordination councils or associations) have already been set up in many Soviet cities and regions. The first inter-regional co-operative unions are also consolidating. One of them is the Interregional Co-operative Federation based in the city of Naterezhnye Chelny. This Federation unites co-operative unions from 30 cities from different Soviet Republics having a total number of more than 4,000 co-operatives. Sectoral co-operative unions such as the Association of Catering Co-operatives in Leningrad, the USSR Union of Construction Co-operatives, the Union of Medical and Health Improvement Co-operatives, Association of Machine Building Co-operatives and the USSR Union of Science and Technology Co-operatives, are also beginning to form.

Social aspects

21. The development of the "new" co-operative movement has caused a number of social problems. As the Co-operation Act regards work in a co-operative as the principal form of employment, the issues dealt with by this law and the others which are only touched upon need to be dealt with in greater detail.

22. Many practical problems have arisen which are of an objective (such as a certain vagueness of legislative acts) or subjective nature. For example, some co-operatives try to avoid social legislation and restrict their social insurance deductions as many people also work in another job. Other subjective issues are the disappointment of some co-operative workers with official trade unions or the arbitrary rule of local officials.

23. For the above reasons, work on social issues does not progress satisfactorily. The author knows of only one successful attempt by co-operative workers to set up a trade union in Leningrad.

24. Some co-operatives are rather reluctant to pay for welfare, scientific research and training of personnel as well as for the activities of co-operative unions and associations. The reluctance to pay for social activities may be explained by the poor general development of institutional welfare schemes and modern social training programmes. However, positive changes seem to emerge in this field.

25. The above-mentioned drawbacks have noticeably affected the work of co-operatives engaged in social and welfare activities as well as in related spheres (sports, medical services and recreation) where there are very few, widely dispersed, unprofitable co-operatives. Also, new co-operatives engaging in these fields are often badly equipped, have low-skilled staff, deliver poor services and are only profit-oriented.

26. Some co-operatives have labour-related problems. In accordance with the Co-operation Act, they hire labour for fixed salaries. These workers do not have a share in the co-operative's profits. Their salaries may be ten times lower than the ones of co-operative members who do little work. This often leads to friction and a bad reputation of co-operatives in public opinion. Therefore, many co-operatives do the exact opposite by hiring few workers and having them participate in the profits. This reduces profitability of the co-operative which may be driven into bankruptcy. To remedy the situation, labour-related legislation also dealing with social welfare issues should be passed.

27. Treatment of customers by co-operative staff often leaves something to be desired. There is no real interest to serve customers' needs or to attract new customers by offering additional services such as home-delivery of goods or after-sales services. This is partly due to lack of training.

Case study: Co-operatives in Estonia

28. Co-operative economic activity in Estonia is characterized by fast development, continuing polarization of public opinion, and fierce discussions about the role of co-operatives in the future centrally-planned economy.

29. Estonian government organizations had planned to set up one to two co-operatives in every town and district by the end of 1987. However, the number of co-operatives increased faster than expected. At the beginning of 1988, 613 co-operatives were registered. The adoption of the USSR Co-operation Act accelerated the process. During 1988, the number of co-operatives in Estonia rose to 1,300. Currently, 3 per cent of Estonia's labour force is engaged in non-traditional forms of economic activities such as subcontracting, leasing of state enterprises, individual or domestic enterprises, co-operatives, etc. About 60 per cent are employed by co-operatives.

30. As already stated, co-operative development was different in the various Republics, especially at the beginning. As outlined in table 2 below, development also differed from one sector to the other.

Table 2: Distribution of Co-operatives in the
Union of Soviet Socialist Republics and the Estonian Soviet
Socialist Republic by sector, as at 1 January 1988

(Percentage)

<u>Co-operatives in</u>	<u>USSR</u>	<u>Estonian SSR</u>
Catering	25.1	11.2
Services	22.4	60.0
Production of consumer goods	25.9	7.5
Processing of secondary raw materials	14.0	21.3
Other	12.6	-

31. In 1987, per capita production of the co-operative sector in Estonia was 4.5 times larger than the national average. Service co-operatives were doing particularly well. The amount of services delivered by co-operatives in Estonia was 12.1 times larger than the national average; 4.5 times larger than the corresponding figure for Lithuania which comes second among the Republics; and 7.5 times larger than the average figure for Latvia which comes third of all Republics.

32. The volume of turnover of service co-operatives in Estonia was only surpassed by the Russian Federation and Ukraine in the first year of operation.

33. Catering co-operatives in the Baltic Republics were doing similarly well. The excellent results of the Estonian catering co-operatives therefore seem to be due to the innovative potential of the Estonian service enterprises resulting from the economic experiments started in 1985.

34. As a result of the Estonian experience, most co-operatives are now closely linked to state enterprises which subcontract work to the co-operatives.

35. Another modus operandi for co-operatives is leasing of state enterprises (entirely or partially), whereby state-owned production facilities are used for the production of goods and services.

36. This arrangement facilitates the start-up of operations of co-operatives and the number of new producers is therefore growing. For example, the delivery of services to Estonian consumers by co-operatives and contract enterprises has reached one third of the total. For example, the number of co-operatives' taxis in Tallinn exceeds the number of those belonging to the state company.

Public opinion regarding co-operatives

37. Co-operatives feature prominently on mass media. There is much debate and the central issue is the "quick money" which individual and co-operatives supposedly make.

38. While preparing for a television link-up between Leningrad and Tallinn in October 1987, Leningrad sociologists distributed a questionnaire asking people for their opinion regarding individual and co-operative entrepreneurs. More than 5,500 persons replied by mail or telephone.

39. 53 per cent of the Leningrad audience and 31 per cent of that in Tallinn distrusted co-operatives and individual enterprises. A comparison of the data collected in both cities leads to the conclusion that the number of co-operatives and individual suppliers in the two markets has a bearing on public opinion. Also, it seems that support as well as distrust depend primarily on personal experience. Among those who never bought products or services from co-operatives, 76.7 per cent were against them, while those who had at least once bought from a co-operative or individual enterprise were largely in favour (85 per cent).

40. In Tallinn the climate is more favourable. Also, public opinion seems to be more varied than in Leningrad, depending on age, sex and social status (workers, students, engineers, etc.).

41. Experience accumulated at the early stage of development shows that co-operatives are established mainly by three social groups, i.e. engineers, office employees and industry workers. Two thirds of them are involved in the co-operative development on a part-time basis, i.e. in addition to their main job. But the number of persons working mainly in co-operatives increases rapidly.

Prospects and bottlenecks

42. The first two years of the new co-operative development give us sufficient data to work on a model for future co-operative development. The basic issue is the role co-operatives will play within the framework of the centrally-planned economy.

43. There are two kinds of enterprise engaged in production. Traditional state enterprises are established by government agencies, centrally managed and vertically administered from "top to bottom". On the other hand, co-operatives are established upon the initiative of citizens and managed according to the reverse principle from "bottom to top". They determine the degree of integration within the overall economy. The Co-operative Law spells out the equality of both forms of enterprise as the principal agents of the centrally-planned economy.

44. It is very likely that in the near future co-operatives will to some extent replace the state sector in certain important branches of the national economy.

45. Such a viewpoint may provoke serious opposition, and it is likely that some central authorities will try to reduce the co-operatives' growth potential within the framework of a centrally managed economy. The recent taxation rules adopted this year are a case in point.

46. Despite of the above-mentioned difficulties which are mainly due to inexperience of new co-operatives, their number has developed rapidly over the past two years. The increase in employment, growth in volume of goods and services produced, and growth rates of labour productivity were slightly lower. It should be pointed out, however, that labour productivity in the co-operative sector grew at a higher rate than that of state enterprises, although the latter are better equipped and employ better skilled personnel.

47. The Decree of the USSR Council of Ministers No. 1405 of 2 December 1988 has made it easier for Soviet enterprises including co-operatives to establish foreign economic ties. This, apparently, will enable co-operatives to improve their technological basis and markedly increase labour productivity and the efficiency of their inputs as well as boost the production of goods and services and increase co-operatives' share in the consumer market. The ensuing increased utilization of foreign equipment, supply of equipment and raw materials not by centralized bodies but on a retail basis, accelerated establishment of joint ventures with foreign partners, and the leasing of state enterprises by co-operatives together with other positive changes in the national economy will positively influence the structure of Soviet co-operatives. Production will be increased, public catering improved and goods and services now in short supply will be amply provided.

48. Bearing this in mind, it is obvious that in future there will be a growing need for setting up joint ventures with foreign firms, especially in high-technology industries. A number of Soviet co-operatives have already established such relations with companies from Finland, Italy, the Federal Republic of Germany, Venezuela, Belgium and other countries. There is a great potential for further development of such ties, especially regarding co-operation with small-scale enterprises in market economy countries.

49. One should not over-estimate the capabilities of co-operatives making their first steps. Undoubtedly, only a few dozen of the existing thousands of co-operatives are capable of carrying out independent foreign trade such as the Moscow co-operative at 36 Kropotkinshaya Street, or Tallinn Iris. The majority of co-operatives is by far too inexperienced to get involved in foreign trade and need a guide in the complex world of economic events and interrelations. They need help and advice of middlemen and consulting services in the field of international marketing and business co-operation. Commercial banking is also required for the financing of profitable co-operation between co-operatives of the Union of Soviet Socialist Republics and small concerns abroad.

50. Co-operatives and other forms of small businesses should be managed by persons distinguished by their strong, high entrepreneurial skills and broad perspective. The number of persons with these qualities is not yet large enough. The establishment of relevant training facilities would help to raise their number. There is great demand for managers of co-operatives and other small-scale businesses.

51. There is a large number of persons who want to become entrepreneurs and would like to undergo training, but up to now there is no entrepreneurial development institute. There is no doubt that international co-operation in setting up a training system for small-scale enterprises would be only useful for our co-operation development.

52. The requirements of co-operatives and small enterprises should be spelled out by co-operatives and small enterprises themselves. For example, the Estonian Small Enterprise Association founded in December 1988 was a step in this direction.

53. To sum up, many of the difficulties experienced by co-operatives are inherent while others are caused by external factors. External difficulties arise from the imperfection of the relevant legal regulations, envy of socially passive groups of the co-operatives' high incomes and, resulting therefrom, the opposition of some officials. Internal difficulties include the absence of a vertical structure and integration of co-operatives,

different levels of supply, production and sale of products, absence of horizontal integration as apparent from the weakness of co-operative unions, shortage of information and newspapers covering co-operatives, and the availability of only meagre financial and material resources. These deficiencies foster the operation of false co-operatives. In addition, co-operatives' employees are not very skilled and lack proper training in the legal, economic, financial and managerial fields as well as at the general level of social culture.

54. Eliminating these bottlenecks will take a lot of time and growth in the number of co-operatives will be faster than improvement of their products and services.