Cooperative Strategy and Liquidation in the Bordeaux Wine Industry

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The option to exit for cooperatives which have successfully reduced the market imperfections is rational (Nourse, 1942). Cook (1995) extends the theory in considering that cooperatives which have reached this turning point face three options: (1) exit; (2) continue in forming strategic alliances utilized as equity-capital-seeking strategy; (3) transition by shifting to a new model that tempers the disincentives stemming from the cooperative ownership structure.

Bordeaux wine cooperatives seem to be in this phase. Indeed, the policymakers of the Bordeaux wine industry encourage the cooperatives to form unions, \textit{i.e.} to follow the “continue” option (see the document, “Bordeaux demain” established by the CIVB, 2010). Some of them have successfully implemented strategy of vertical integration. If we follow the Cook prediction, we can suppose that the cooperatives which have not adopted any of these two strategies, \textit{i.e.} which have opted for the \textit{statu quo}, may be engaged in an exit process.

Cross and Buccola (2004) show that information asymmetry with the lenders makes the cooperatives able to liquidate by distributing equity to their members, often by raising the transfer prices paid for member raw products. In other words, the cooperative can choose the exit option at the expense of the lenders through an overpricing of the cooperative member products. The end of this liquidation process should be a bankruptcy which can take lenders and regulators by surprise (Cross \textit{et al.}, 2009).

As such, this raises the question of whether the Bordeaux wine cooperatives which have opted for the \textit{statu quo} are not engaged in such liquidation process. There is an empirical challenge because this liquidation process is neither immediate nor easy to detect. Generally speaking, Cross \textit{et al.} (2009) propose a method based on a comparison between the price paid to the

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cooperative members and the price offered by the investor-owned agribusiness to characterize the liquidation process. However, we cannot use this method in the Bordeaux wine industry because investor-owned wineries are still rare in Bordeaux. As a result, we cannot refer to an “investor-owned-firm contract price” to assess whether the price paid to cooperative members is overvalued or not.

Instead, we propose to examine the relationship between the financial characteristics of the cooperatives and the price paid to cooperative members according to the options they follow: (1) statu quo (exit); (2) union (continue); (3) vertical integration (transition). We expect that cooperatives with a long term horizon, i.e. cooperatives which move toward union or vertical integration, are willing to preserve their financial balance. Therefore, the price paid to cooperative members should decrease with the leverage or the deficit for cooperatives which have opted for union or vertical integration. To test this hypothesis, we propose the following econometric model:

\[ P_p = \beta_0 + \beta_1 DS \times LEV + \beta_2 CV \]

\( P_p \) is the price paid to producers. \( DS \times LEV \) is a cross-variable used to compare the effect of the leverage (\( LEV \)) on the price paid to producers according to each downstream strategy (\( DS \)). \( CV \) represents the following control variables: downstream strategy (\( DS \)), sales of the cooperatives, value of the wine sold by the cooperatives per hl and processing costs per hl. According to our hypotheses, \( \beta_1 \) should be negative when the cooperatives behave over the long term, i.e. when the downstream strategy is union or vertical integration. By mirror effect, if \( \beta_2 \) is null or positive, we suspect a liquidation process.

Our database encompasses information from the 39 Bordeaux wine cooperatives (exhaustive sample) over a 5-year period (126 observations). It consists in a merge of accounting data, information on the wine distribution channel, the volume of processed wine, the number of cooperative members and the area they are operating on, so that we can apply our empirical strategy to detect a risk of liquidation in a cooperative group (each group is here defined by the downstream strategy).

The results of our multivariate analysis (we apply a feasible generalized least square approach adjusting for heteroskedasticity and autocorrelation) show an overpricing of the material provided by cooperative members (10% of the average price) belonging to cooperatives which have opted for the statu quo strategy.

However, the analysis of the cross-variable contradicts our hypothesis: the leverage has a significant negative effect on the price paid to cooperative members for the statu quo cooperatives, a positive but weakly significant effect for cooperatives in union and a positive and significant effect for cooperatives which have implemented a vertical integration strategy. We can explain this result by the policy of the cooperative lenders: they restrain the credit availability to less proactive cooperatives and more generously finance cooperatives engaged in continuation or transition strategies. This partly contradicts the liquidation process established by Cross and Buccola (2004) and provides an interesting insight on the financial constraints of cooperatives (Chaddad et al., 2005) and the possible role of bank relationship (Petersen and Rajan, 1994) in their survival and development.
References


