



MERCOSUL's Agricultural Cooperatives: an essay about internationalization strategies

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Abstract

This work evaluates the importance of internationalization strategies for agricultural cooperatives in the MERCOSUL customs union (composed of Argentina, Brazil, Paraguay, and Uruguay). After an overview of the cooperative agriculture sector and the current agribusiness trends in the countries, internationalization strategies and trade expansion opportunities are discussed. Changing business environments marked by increases in competition, consolidation, technological innovation, multinational firms, and international relations are cited as reasons for internationalization, a process that could benefit agricultural cooperatives by creating economies of scale and geographical and ownership benefits. The following are given as necessary prerequisites for entering into internationalization schemes: access to primary goods or customers, a reputation for quality, flexibility, innovation, and know how. A discussion of barriers to the internationalization of cooperatives is also presented, such as spatial/geographic contradictions, finance difficulties, governance, and cultural problems. Next, all the possible options are given in the Export/Import, Foreign Direct Investment, and Commercial Agreements areas. The article concludes by noting that despite the difficulties of creating international cooperative systems, the construction of farmer-owned international business agreements and structures holds promise for assuring survival of small scale producers, combating trends that decrease margins for primary product producers.

Keywords: agricultural cooperatives, MERCOSUL, internationalization



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1. Introduction

The MERCOSUL customs union was formed in 1995 by Argentina, Brazil, Paraguay, and Uruguay to stimulate development by eliminating internal trade barriers and establishing a common external tariff. The fourth largest trading bloc in the world, MERCOSUL has a combined population of nearly 224 million inhabitants and a net GDP of 639 billion dollars. MERCOSUL's agriculture sector, which makes up 9.92 percent of total bloc GDP, an average of 22% of the workforce, and 33% of the total exports is supported by an extensive network of cooperatives that provide credit, supplies, processing, and marketing assistance. Cooperatives are member-owned and controlled businesses that return all operating profits to members either through in-kind services or patronage checks based on use volume. As a response to current market conditions and globalization pressures, cooperatives are increasingly undertaking internationalization schemes, defined here as the implementation of a strategy of greater presence in international locations.

The new realities of globalization are currently prominent in the planning and consideration of the agricultural cooperatives of MERCOSUL. Recent regional cooperative conferences and events have focused specifically on issues of regional integration and globalization¹, cooperative industry fairs emphasize their international dimensions², and a program has been launched to support the cooperative sectors of Latin American countries in formulating policy positions and political strategies regarding the proposed Free Trade Area of the Americas (FTAA)³.

The most prominent cooperative MERCOSUL-wide body is the Specialized Meeting on Cooperatives in MERCOSUL (RECM), an entity within the MERCOSUL bureaucracy formed in 2001 and made up of representatives from co-ops and government actors. Presently the group is working to harmonize cooperative legislation within the block and ensure that the interests of cooperatives have a voice in bloc decision-making. A coordinated effort to occupy political leadership and maintain influence in the legislative process is also taking shape with the formation of a group of law-makers who are co-op members and who advocate on behalf of the sector. Members view the RECM as both a means to explore business and economic relationships and as an opportunity to share experiences and concerns of cooperatives on a regional level.

Agricultural cooperatives in MERCOSUL vary tremendously in size, sector, organization, and level of integration in the global economy. To illustrate the diversity between countries and cooperatives, presented below are the characteristics of agricultural cooperatives by country, as summarized in Table 1. In addition to diversity in size and sector,

¹The International Cooperative Alliance of the Americas (ACI)'s November 2004 Buenos Aires, Argentina conference was entitled "Cooperative Integration: Equality, Social Wealth and Work" and the cooperative sector's program at the 5th World Social Forum in Porto Alegre, Brazil in January of 2005 was entitled "Cooperative Planet: A Fairer Globalization for All"

² The FENACOOP trade show reserves an entire section for international exhibitors

³ The Canadian development agency ACIDI in conjunction with ACI Americas sponsors the PRICA (Regional Process of Cooperative Integration of the Americas) program.



the agricultural cooperatives of MERCOSUL also vary greatly in economic power and export activity.

Table 1: The Agricultural Cooperatives of MERCOSUL

MERCOSUL country	No. of Ag. Coops	Members	Cooperatives average size Members/coop	Products
Argentina	800	80,000	100	Grains, Beef, Fruit, Wool, Honey, Tobacco, Grape, Yerba Mate, Tobacco
Brazil	1519	940,482	619	Wheat, Barley, Oats, Milk, Cotton, Pork, Chicken, Soy, Coffee, Grapes, Corn, Rice, Beans
Paraguay	100	135,000	1350	Cotton, Soy, Corn, Milk, Yerba Mate, Beef, Peanuts
Uruguay	139	39,049	281	Milk, Grains, Sorghum, Sunflowers, Corn, Wool, Honey, Beef, Lamb, Citrus

Market structure changes in the agrifood sector has impacted each of the four MERCOSUL countries' agribusiness sectors. Important trends include: the consolidation of large grocery store chains and the introduction of mega-chains such as Carrefour and Wal-Mart the increased dominance of a few multinational agribusiness firms in the inputs and marketing sectors. Such pressures translate into smaller margins for small-scale producers and even their exclusion from markets (Dirven 1999). Producers compete more fiercely to produce efficiently and at low cost while being more vulnerable to increasingly volatile international markets.

The economic growth experienced by MERCOSUL countries in the last decade has changed food consumption patterns. Consumer has been consistent with Bennett's law that states that an increase in disposable income will lead to a decrease in the consumption of grains and staple carbohydrates and an increase in the consumption of proteins and processed foods. This trend increases the demand for processed goods and ready-to-eat products and value added food stuffs. Working to vertically integrate businesses to control more stages of the production chain and participate in the industrialization processes not only allows firms a competitive edge in their position in the market, but also contributes significantly to profitability. Numerous agricultural cooperatives in the MERCOSUL region have advanced food processing and marketing operations.

For the MERCOSUL cooperatives, business strategy, either geared towards international markets or for intra trade block exchange is important for the agroindustrial system in which cooperatives play an important role. Soybeans are very important in international markets and dairy products are also important commodities in intra-bloc business. The transnational strategy cooperatives implement may even determine business success for cooperatives organizations.

The agricultural cooperatives of MERCOSUL face a unique set of challenges and opportunities resulting from globalization, raising such questions as Which forms of international business do cooperatives choose and why? and What are the possibilities for increasing cooperation among cooperatives on trade? This paper's objective is to discuss the business advantages, difficulties, trends, organizational forms, and strategies of agricultural cooperatives' internationalization in MERCOSUL countries.

To address those questions, this article first describes the agricultural cooperatives of MERCOSUL in quantitative and qualitative terms, detailing sectors for which



internationalization is particularly relevant. Next it evaluates the reasons for, benefits of, prerequisites for, and barriers to the internationalization of cooperatives. Then it presents models of internationalization, gives examples of their implementation and analyzes why some particular strategies are in use and others have not yet been implemented. Finally it suggests which internationalization strategies hold promise for possible for the agricultural cooperatives of MERCOSUL.

2. The internationalization process and cooperatives in Mercosul

The cooperative system is a network of connected economic and social actors. Community and local level farmers organizations are connected to regional, state, national, and international bodies through sharing of cooperative identity, economic relations, and social relationships. Considering the question of why and how cooperatives internationalize, we must recognize that strategies and outcomes will impact actors on various levels and in various ways. Social capital and Social networks are important to define cooperative efficiency; this kind of capital is only created on the community level (Faulkner e Rond 2000, Granovetter, 1985). In this case, the local focus of co-operatives is the most important difficulty to the internationalization process.

Cooperatives were originally formed to correct market defects and provide services for relatively culturally homogenous members in geographically bounded areas (Cross and Buccola 2004). The current onslaught of globalization (the lowering of barriers to the cross-border movement of capital, people, ideas, technologies, and culture) alters the business environment in which cooperatives function and advances internationalization. (Tallman, 2002). Five groups of changes: competition, consolidation, technological innovation, multinational firms, and international relationships are discussed, followed by a summary of potential benefits that could be derived from internationalization schemes.

A sharp increase in competition, owing to processes of liberalization, privatization, and international sourcing of labor and primary and processed goods has impacted cooperative businesses (Stanford and Hogeland, 2004; Cook, 2000; Clamp 2000). Lower market prices imposed by rival firms pressure companies to decrease costs, increase efficiency, and seek out new markets. Baird et al's 1994 study shows a positive relationship between the rate of change in an industry (as perceived by firm management) and internationalization. Agriculture in MERCOSUL countries, particularly in Brazil is undoubtedly a rapidly changing sector, suggesting that internationalization may be accelerating as well (Bialoskorski Neto, 2001).

In conjunction with competition is the intense trend towards consolidation or the horizontal integration of firms. Farina (1999), Jank et al. (1999), and Heffernan and Hendrickson (2001), discuss the rapid rate of mergers and buy-outs of domestic companies by global firms in the food industry. The latter note that, "trends suggest six or fewer global food retailers will evolve over the next few years," a formidable change with wide-sweeping implications for all links in product production chains. As the market becomes more concentrated, a small group of businesses will pressure producers to be price takers and conform to standards and practices imposed by the consolidated companies. The process of consolidation changes the structure of demand for food production in addition to creating extremely large and powerful corporations.

The dominance of multinational firms in the agricultural input, marketing, and food retailing sectors is an important indicator of the changing global business environment



(Clamp, 2000; Farina, 1999). Stanford and Hogeland (2004) posit that, “To gain the volume necessary for scale economies or—increasingly—contracts with prominent retailers such as Wal-Mart, cooperatives may need to source globally.” Business strategies are designed taking into consideration a combination of individual country evaluations and the global perspective. Firms without the same reach and market power may languish in comparison with their competitors.

Technological advances also create pressure on firms to consider internationalizing their operations. In agricultural terms, this is most evident in examples of improved cultivation, processing, and transportation techniques. Obtaining the capital goods necessary (advanced farm implements, GPS systems, computer hardware/software for management) for integration in the global system presents a challenge both in terms of financing and in human resource development. Firms increasingly seek international linkages to stay up-to-date.

The important component that impacts the present business environment is the increasing of international relationships. As both source providers and destination buyers increase in the likelihood of being of non-domestic origins, firms are pressured to gain knowledge and capacity to deal in the international marketplace.

The benefits of internationalization are threefold. Firstly, the process of globalization may provide firms with economies of scale by combining the efforts of multiple firms to bid on contracts, order inputs, or gain power in the market. Secondly, internationalized firms may enjoy ownership advantages that give them leverage to make deals and develop a reputation in the business community. Thirdly, in the case of Foreign Direct Investment, a firm that internationalizes may gain location advantages by being present and able to participate in foreign market. Some multinationals only accept bids for inputs from firms already in the manufacturing or processing country so having a presence may be tremendously helpful.

2.1 Prerequisites and barriers to internationalization of cooperatives.

Cook (2000) sets out three criteria that cooperatives should meet in order to be able to compete and participate effectively in the international marketplace: access to raw material supplier or customer, a reputation for assured supply and quality, and persistent innovation in a rivalry-intensive set of industries. In addition, a skill-set related to international business, including cultural, linguistic, and technical know-how is essential. Support for producers who seek to expand internationally is often available through government programs or industry organizations.

Baird (1994) also cites the need for established planning and strategy systems. Doing international business requires flexibility, responsiveness, and constant reevaluation of performance, goals, and methods. Without a management infrastructure designed to specifically formulate company policy in international markets, firms may experience problems with sales, long term viability, and stagnation.

Many observers have raised questions about the viability of applying the cooperative business model on the international level. According to Errasti et al (2003), “Nowadays, following the cooperativist formula, due to obstacles of an economic, juridical, and cultural nature, it is not easily possible to organize production abroad nor to form strategic agreements aimed at creating joint venture firms.” Four main concerns have been raised including spatial/geographic contradictions, financing, governance, and cultural problems.

The different spatial domains of cooperatives (largely local or regional) and multinational corporations (international or global) are also said to be problematic due to the difficulty of addressing members’ particular (and regionally based) needs while simultaneously attending to global environments and pressures (Stanford and Hogeland 2004; Cook 2000). Fairbairn (2002) summarizes the problems as follows, “members feel less



attached to organizations that seem more remote or harder to understand. There is less trust or loyalty when the cooperative's overall direction eludes easy grasp, or is active in many product lines or regions."

Cooperatives have traditionally faced difficulties in borrowing and accessing credit, a problem that may inhibit the development of international strategies that, depending on their form, may require large capital investments. This problem may be exacerbated by the risk aversion and skewed incentives for investment as described in Cook, Chaddad, and Iliopoulos (2004).

Governance challenges are due to arise from internationalization (Cook 2000). Even on the regional level, controversies arise around the issues of just representation of entities from diverse geographic origins. When interests groups within a cooperative perceive divisions among members, building consensus may be difficult.

Even in the face of globalization of culture and the increase in international communication and understanding, major cultural differences between cooperatives are bound to arise. This may take form in cooperative philosophy or cultural norms or shared understandings (Errasti et al 2003). Difficulties with language and communication may arise along with challenges of harmonizing ideas about future objectives and plans.

3. Strategies for Cooperatives to Internationalize

International business generally takes three forms: Imports/Exports, Foreign Direct Investment, and Commercial Relationships. Cooperatives choose their strategies based on an internationalization of business, only import or export products, that is the most common strategy, but there are also an internalization of the organizational structure like foreign direct investment. These strategies are chosen in function of the number of factors such as product characteristics, location of buyers and consumers, investment possibilities, and long term objectives. This discussion explores the formation of internationalization strategies related to cooperatives both hypothetical and already in use. After the basic formation of each model is presented, considerations of its viability are given, followed by examples.

3.1. Import/Export

The agricultural cooperatives of MERCOSUL are currently highly involved in export activities, particularly of chicken, wheat, soybeans, milk, and coffee. In Brazil alone, agricultural cooperative exports were worth \$1.3 Billion dollars in 2003. A recent World Trade Organization report notes that within the worldwide trend towards processed goods being exported more than primary goods, Brazil is an important exception. In 1990-1991 47% of Brazil exports were processed products and in 2001-2002, that percentage had dropped to 40%. Meanwhile, the trade in agricultural goods has been increasing at an annual rate of 4% annually, about twice as fast as agricultural production has been growing. In Latin America 29% of merchandise exports are agricultural goods⁵.

There are three possible business formations available for cooperatives seeking to be involved in Export/Import activities. The first model involves a cooperative from one country exporting its product to a cooperative from the same sector in a different country (see Figure 1). The importing cooperative may attain economies of scale, be able to contract with larger retailers by supplying a greater quantity, and be able to spread their brand image to a greater audience. Benefits derived from value added processing would be distributed depending on which entity is responsible for industrialization and packaging activities. This technique would be applied to cooperatives with existing importing and exporting activities and

⁵ Mexico is excluded from this definition of Latin America

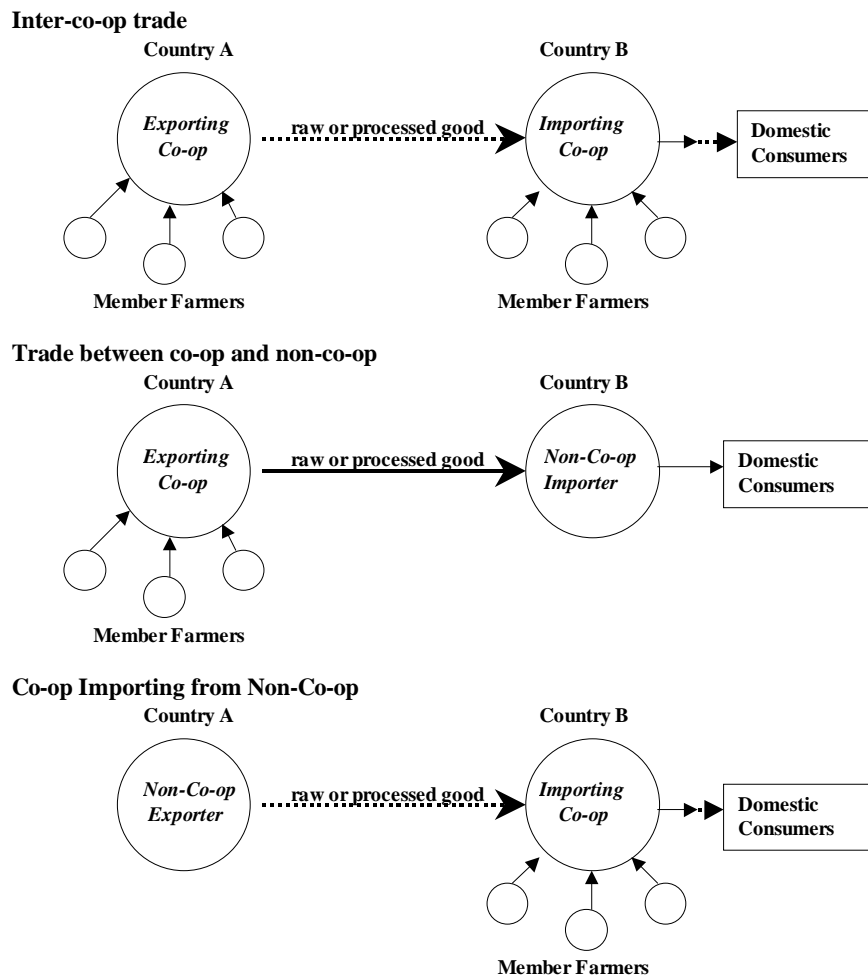


therefore does not fundamentally change the structure of the cooperative. Any additional workers needed to expand the operation would neatly fit into existing employee categories. This model, as far as we know, is not currently in use by any MERCOSUL cooperatives. Coops producing processed goods in the same sector in different countries have often approached the market as competitors rather than partners.

The second example, Trade between a Co-op and a non Co-op, is the most prevalent type of business internationalization strategy. In the soybeans agro-industrial system and others this is the most important strategy to attain advantages in international markets. The business model of the trading partner is irrelevant to the transaction and questions of social responsibility are not considered. Major exporters in MERCOSUL using this strategy include the most important grains cooperatives like COAMO, COMIGO and CAROL and SanCor, Aurora, and Cooxupé with others commodities.

The third strategy, Co-op Importing from a Non-Co-op is another possible formation that international business could take, like fertilizers and others inputs, although the nature of agricultural cooperatives with their members supplying the bulk of product inputs, it is not likely.

Figure 1. Models of cooperatives internationalization – Import and Export





3.2. Foreign Direct Investment

Foreign Direct Investment (FDI) is the most prominent and popular strategy for internationalization in the food industry today. Cook (2000) notes two trends related to U.S. agroexports: first, that since the 1960's U.S. firms have been exporting less bulk food products and more processed food products and second, that FDI for food processing overseas is increasingly at a greater rate than export values (almost four times greater in 1992). In the MERCOSUL countries, this influx of foreign capital has been significant particularly after political and economic reforms of the 1990's.

Although a number of agricultural cooperatives have been active in implementing Foreign Direct Investment, currently the model of establishing a foreign office without incorporation of foreign members is most prominent. Clamp (2000) explains that in the specific case of the Mondragon cooperative corporation which has extensive international holdings through the attainment of manufacturing plants in newly industrializing countries, *“the...cooperators have not seen the extension of ownership beyond their own region as part of their mission.”* This perspective, while present in the expansion of cooperatives, is not the only interpretation for the international expansion of cooperatives, as shown by the enthusiasm among observers for the creation of viable business models more consistent with the cooperative model.

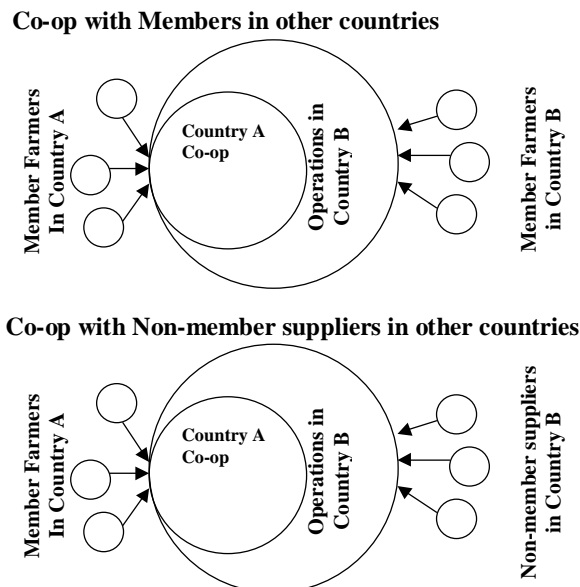
Errasti (2003) suggests two strategies for designing a Foreign Direct Investment plan that included elements of cooperative organization. The first is to transform foreign affiliated companies into cooperatives or foster cooperation between interdependent cooperatives in different countries and the second is to find help/collaboration from other cooperatives when considering installation in another country (through technology transfers or joint businesses). Clamp (2000) notes that options that would create full ownership include mergers and acquisitions or internal venturing and partial ownership possibilities include joint ventures and minority investments, which are oftentimes strategies for attaining knowledge or on-the-ground experience/market background.

The two possible strategy formations for cooperatives to participate in Foreign Direct Investment are shown in Figure 2. The first type, a co-op with members in other countries, is not currently in use in MERCOSUL. The LAR cooperative in Brazil has foreign investments in another country, and its Brazilian members that have land and function as part of the Co-op in another country. Their experience has been abroad with agricultural research in others countries. However, the cooperative do not have foreign members.

The second strategy for Foreign Direct Investment in Figure 2 is a Co-op with Non-member suppliers in other countries. The massive Argentinean dairy cooperative SanCor, with operations in various countries, have foreign investments in Brazil to distribute products. The gains from this strategy return to the co-op members in the home country. This strategy could also hurt cooperatives in the areas the investing co-op undertakes production by creating competition and causing them to lose their scale economies.



Figure 2. Models of cooperatives internationalization – Foreign investments



3.3. Commercial Relationships

Commercial Relationships are another option for increased international participation without the necessity of obtaining foreign holdings. Such relationships could take the form of Research and Development partnerships, cooperative agreements, distribution agreements, joint bidding or joint licensing (Cook 2000; Clamp 2000). Opportunities for commercial relationships may be less risky in terms of investment and commitment but beneficial for preparation of entry into new markets, exploring other opportunities, or creating strategic alliances.

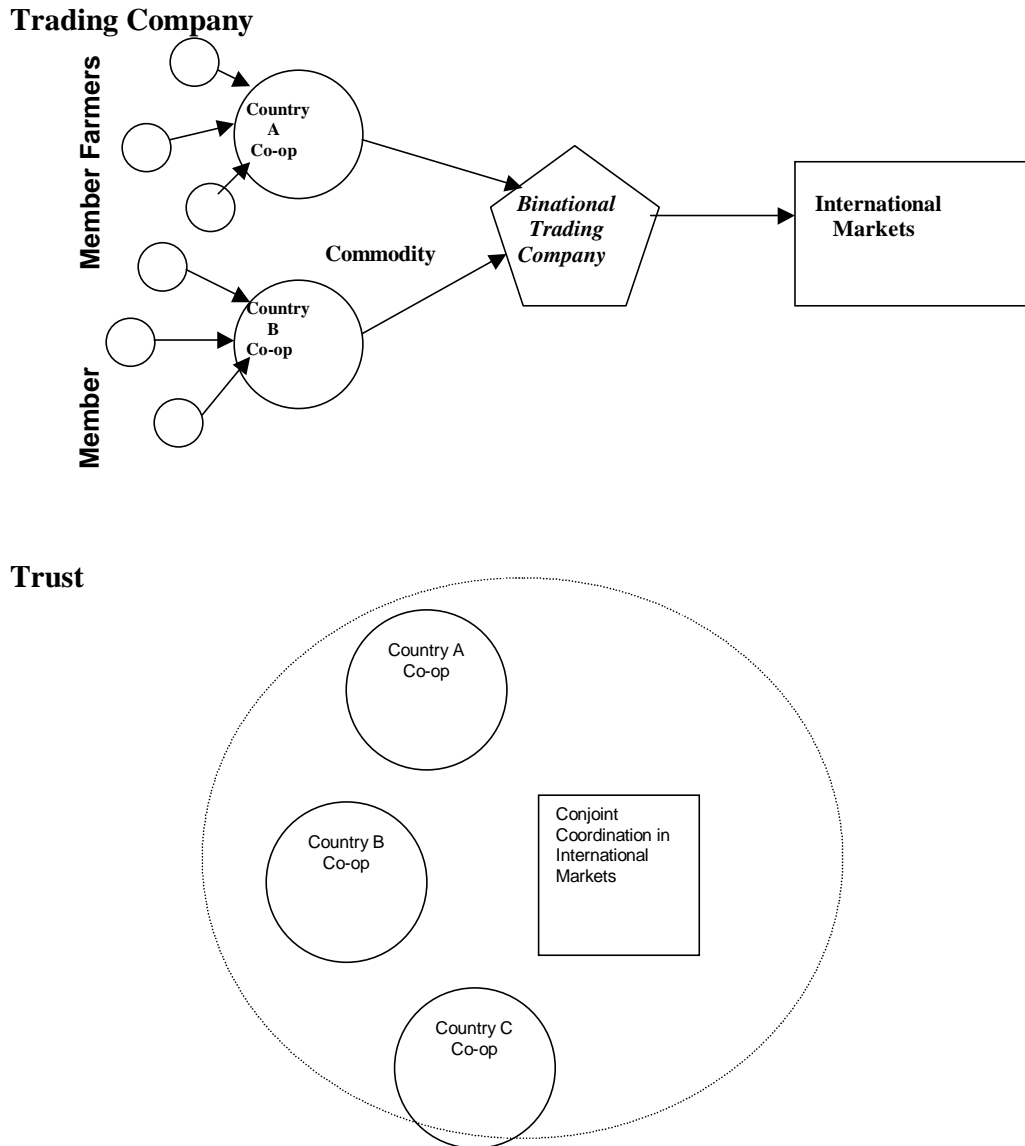
The Trading company model for International Cooperative Business (shown in Figure 3) is based on a situation of two cooperatives in different countries that produce the same, commodity-like product for export to a third market. The two cooperatives form a binational trading company that brokers sales on behalf of its members. If combined product volumes are sufficient, the trading company may be able to negotiate better prices for cooperatives by avoiding external middle-men and wielding the power of volume. Opportunities for sales directly to cooperatives in third countries also may exist. The challenges arising from this model are to form the trading company while maintaining cooperative integrity and to ensure that the administrative costs of creating and running the trading company are less than the economic benefits received from it. Due to the limited function of the trading company, a basic format might be established that returns profits to members based on use volume, like any other co-op.

The second model for Commercial Agreement (the bottom half of figure 3) is the creation of a trust that would hold back a certain percent of the harvest in an attempt to influence international prices. This formation is only possible for a market in which member cooperatives together produce a large portion of the total world production. Additionally, it faces difficult collective action problems, in the case of one co-op wanting to benefit from



selling its product in a high demand market before the other members had agreed to the sale. Coordination of this scheme would necessitate highly trained and knowledgeable managers to be successful.

Figure 3. Models of cooperatives internationalization – Commercial agreements



4. Discussion and final considerations

In the course of analysis, a pattern emerges about the internationalization strategies chosen by agricultural cooperatives in MERCOSUL. First presented are the strategies in use with reasons they favored. Next the strategies that are not in use are shown with reasons they have not yet chosen. Finally, a few suggestions are made regarding the future possibilities for cooperative participation in the international market.

As seen in table 2 below, the internationalization strategies currently in use in MERCOSUL countries include co-op export to non-coop, co-ops with operations in other countries both with foreign members and co-ops with operations in other countries without



foreign members. All of these strategies allow a coop great flexibility regarding sales strategies, maximizing the number of potential buyers and allowing for rapid changes in approach depending on market volatility, a crucial component for all elements in agriculture. All of these strategies also maintain a centralized and supreme governance structure, not having to submit to the wishes of partner companies or cooperatives (the obvious exception is structure of cooperatives with other countries with foreign members, though integrating member interests is significantly less problematic than integrating an entire other organization's interests into the governance structure).

The internationalization strategies not presently in use, inter-coop trade, co-op importing from non-coop, trading company, and trust are somewhat more difficult formations. Inter-coop trade would require market synergies between two co-ops are not present. Co-ops importing at all would require a special set of conditions to justify the action. Establishing a trading company, while viable in the soy sector, would be a relatively complex proposition requiring professional evaluations of viability and an expectation of efficiency to compensate for the costs of assembling and maintaining such a venture. The idea of a trust, also a possibility in the soy sector, would need to be composed of cooperatives with great confidence in the others and would need to be administrated by highly-knowledgeable agents.

The cooperative soy sector of MERCOSUL could benefit from exploration of possibilities for collaboration and cooperation in trading their product on the international market. Either with the establishment of a trading company or with the formation of a trust to pool resources and impact prices, positive outcomes could be attained to benefit cooperative members.

Table 2: Internationalization Strategies observed in MERCOSUL's agricultural cooperatives

Internationalization Strategy	In use	Not in Use	Difficulty	Consistency with Coop Values	Cases
Import/Export					
Inter-coop trade		X	+++	++	
Co-op exporting to non-coop	X		-0-	-	Most common, all cooperatives that export. Grain, Poultry, Dairy, Coffee products etc
Co-op importing from non-coop	X		-0-	-	
Foreign Direct Investment					
Co-op with Foreign members		X	++	++	
Co-op with investments in another country	X		+	--	Sancor Lar
Commercial Agreements					
Trading Company		X	+++	+	
Trust (Strategic Alliance)		X	++	++	



The consolidation of many firms in the agrichain and the introduction of globalization-related market pressures have created a new set of challenges for agricultural cooperatives in the four MERCOSUL countries. Combating the pressures for change requires the creation of new forms of international strategies, both in collaboration with private firms and with cooperatives in other countries. The models of internationalization of cooperatives presented in this work vary from those already in use like exporting to non-co-op firms, and Foreign Direct Investment without members in other countries to those that are hypothetical like the formation of an international cooperative trading company.

We can conclude from studying the structures in use that co-ops seek internationalization strategies that provide flexibility and keep them competitive in the market. Although international cooperative businesses face problems with issues of legal structure, financing, and cultural issues, the cooperative community should be proactive in seeking trans-national alliances and business relationships to solidify cooperatives' position as an innovating player in the global business environment. The formation of food system market structures born out of principles of democracy and transparency could be positive for both producers by supporting fair prices and for consumers by encouraging food security, safety and health.

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