A successful case of contract farming in Brazil

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Contents

- Evolution of the Brazilian poultry industry
- The central role of contract farming
- The case of “Pif Paf Alimentos – Minas Gerais State
- Critical success factors
- Conclusions
Poultry: a success story

- In 1980, it took 7 weeks to grow a 1.8kg bird, with a feed conversion rate of 2.05 kg/kg
- In 2006: 43 days, 2.34 kg and 1.83 kg/kg

- Between 1990 and 2006, production increased at a rate of about 9% per year

Poultry consumption is rising at 6.2% a year
Exports also keep rising: 15% per year

Growing exports of poultry cuts: 1637 thousand tons in 2006; US$1.9 billion
Chain organization

- Most production under closely coordinated integration contracts (75% x 25%)
  - small and medium sized producers predominate
- Highly concentrated processing sector: 4 largest firms control 38% of production; 8 largest: > 50%
- Geographical concentration in the southeast, with tendency for expansion in the central-western states

The Case of Pif-Paf Alimentos

- Mid-sized company located at Southeastern Minas Gerais State, Brazil
- Produces broilers under contracts with some 600 farmers
  - Slaughters 170,000 birds/day
- Has developed an effective contract design linking payment to production performance
  - farmers have incentives to continuously improve technical performance
How the contract works

- Pif-Paf provides one-day chicks, feed, veterinary inputs and technical assistance
- Farmer invests in the facilities and is responsible for production costs in items such as labor and energy
- Pif-Paf guarantees the purchase, under a pre-agreed price determination system

Price is established through a punctuation system, taking into account the following variables:
- Death rate (%)
- Feed conversion
- Daily weight gain
- Loading time during broiler delivery
- Quality of management
- Injuries (%)

Final Price/kg = Total points obtained x base price negotiated previously to the growing cycle

<table>
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<th>Death rate (%)</th>
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<th>1.2</th>
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<th>3.2</th>
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<td>38</td>
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<td>18</td>
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<td>Feed rate (kg/kg)</td>
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<td>...</td>
<td>60</td>
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Main benefits for farmers

- Pre-financed inputs
- Technical assistance
- Guaranteed market
- On-farm use of manure
- Increased credit worthiness

Why it works

- Firm negotiates prices and discusses punctuation tables with producer’s association
- Firm is rigid with regard to non-performance: non-performing farmers are replaced: 5% are eliminated every year
- Firm provides incentives for improved technical efficiency, via the punctuation system;
- Firm creates a “depreciation” fund, depositing a percentage of the revenues in a farmer’s account, which can be used for facility maintenance and upkeep
- Farmers have the added incentive to utilize a by-product in additional agricultural enterprises
- Disputes are mediated by the producer’s association
- Trust has been built
Critical success factors

■ Basic tenet
  - contractual relationships will only be sustainable if partners perceive that they are better off by engaging in it
  - Corollary: contract farming will fail if parties do not develop mutual trust and reciprocal dependency (SYNERGY is the key word)

■ The importance of the enabling environment
  - No successful contracting scheme can exist or remain sustainable where the institutional and political setting is not conducive to it

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Critical success factors

■ Minimization of contractual hold-ups
  - farmer: enhancement of bargaining power via collective action
  - firm: group negotiation; improved communication; quality and scope of services provided; strict treatment of defaulters; extended contract duration

■ Need to countervail uneven balance of power
  - promote farmers association
  - mediation, instead of legal action
Conclusions

- Contract farming can be a very effective way to promote value chain financing

- FAO is developing a web based “Contract Farming Resource Center”
  - for more information, check www.fao.org/ag/ags/index_en.html

Thank you!

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