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# COMMITTEE ON COMMODITY PROBLEMS

## INTERGOVERNMENTAL GROUP ON TEA

### TWENTY-THIRD SESSION

Hangzhou, the People's Republic of China, 17-20 May 2018

## FOSTERING SUSTAINABILITY IN TEA PRODUCTION AND TRADE: ASSESSING THE IMPACT OF CERTIFICATION SCHEMES ON FARM INCOME, INCLUSIVE RURAL DEVELOPMENT AND MARKET ACCESS

### I. INTRODUCTION

1. This report aims to guide discussions on tea certification during the 23rd session of the Intergovernmental Group on Tea (IGG-Tea) to be held in Hangzhou, China, from 17 to 20 May 2018. The paper presents the impacts of sustainability certification in the tea sector, focusing on its effects on farm income, market access and rural development. It also highlights possible factors reducing the positive impact of certification and makes recommendations towards enhanced sustainability in the industry. The analysis builds on a literature review and a set of interviews<sup>1</sup> with major stakeholders including four of the major tea certification schemes. In 2015, at least 538 000 hectares (or 14.2 percent of the global tea area) were certified by the four major certification schemes, namely: Fairtrade, Organic, Rainforest Alliance, and UTZ. Assuming that no multiple certification is occurring, 717 000 hectares (or 18.9 percent of the global tea area) were compliant with one of these schemes – average 628 000 hectares (16.5 percent). Kenya, India, and China accounted for the largest area of certified tea production in 2015.

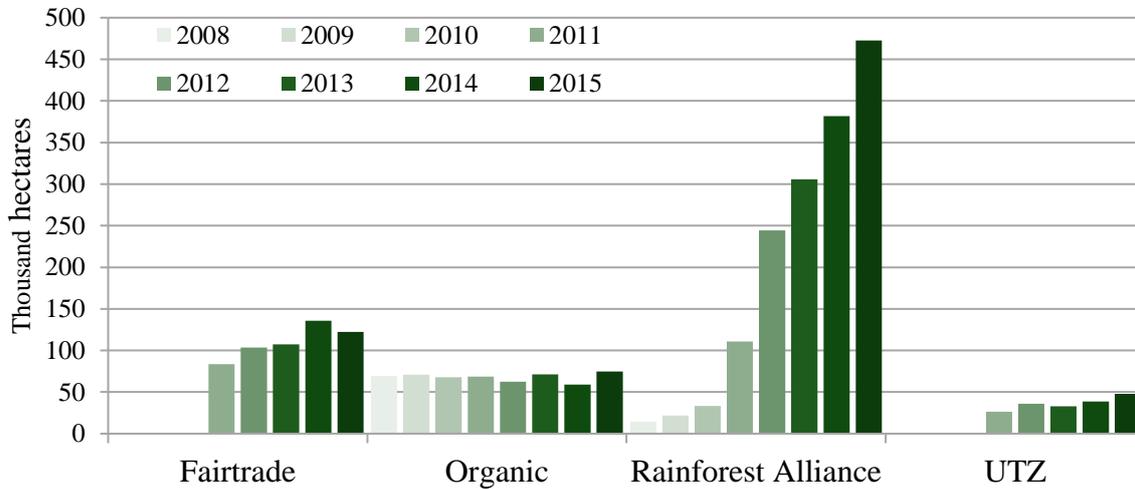
<sup>1</sup> The findings are supported by 29 coded interviews conducted between February and March, 2018 with certification schemes, businesses, control bodies, NGOs, researchers and other stakeholders involved in certification.

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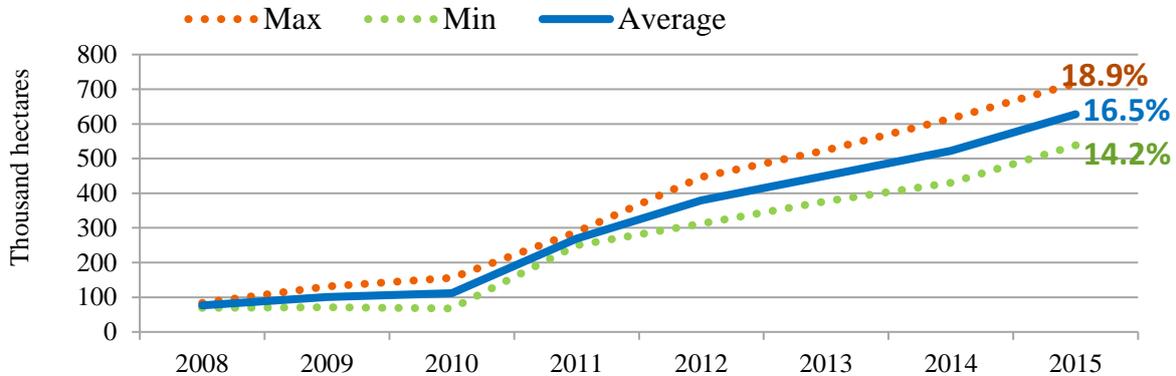
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Figure 1: Production area by standard, 2008–2015



Source: Lernoud *et al.*, 2017

Figure 2: Certified production area, 2008 –2015



Source: Lernoud *et al.*, 2017

## II. SUSTAINABILITY ISSUES IN THE TEA SUPPLY CHAIN

### a. Economic sustainability

2. The tea sector is characterized by many interconnected issues including oversupply, low prices, lack of transparency at auctions, low wages as well as low demand for certified goods.

3. Major tea markets such as Russia, India, China and Pakistan do not always demand certification. Where demand for certified goods is insufficient, the product is often sold on the conventional market and producers do not receive a premium, despite having invested in sustainability

certification. This discrepancy between supply and demand for certified tea is generally perceived as a barrier to increased farm income.

4. Approximately 85 percent of tea is sold by multinationals, and one-fifth is controlled by just three of them. The relative power of downstream supply chain actors can negatively affect producer prices. Many stakeholders in the industry, particularly producers, have the perception that tea prices are too low. Lower prices typically result in lower wages, as producers seek to reduce costs to remain competitive.

5. Tea auctions, responsible for 70 percent of tea sales, are characterized by anonymous transactions, in which several “middle men” (agents, importers, retailers, etc.) are involved. Anonymity means that buyers can easily switch between suppliers. The various intermediaries reduce margins for primary tea producers, impair price discovery and, overall, reduce market transparency. Furthermore, tea sold at auctions is often retro-certified, which means that certified tea is sold as conventional produce at the auction. It is only declared as certified, when companies know how much certified tea is demanded on the market. As a result, tea producers only learn how much “certified” tea they have sold, when (if) they receive the price premium.

6. Wages make up a significant part of the production costs. Even when minimum wages are met, they do not always represent living wages. However, there are limits to raising wages. Increasing wages without improving productivity adds to unit costs of production and can mean that producers push themselves out of the market. The fear of losing competitiveness therefore keeps a lid on, or even generates downward pressure on wages. Overall, the sector is faced with the challenge of preventing a “race to the bottom”, not only for wages, but also for social, environmental and occupational health standards.

#### **b. Social sustainability**

7. Major social sustainability issues in the tea sector include: labour shortages, poor working and living conditions, gender inequality and discrimination.

An ageing workforce and the rising youth disinterest in tea farming are resulting in a labour shortage in many tea estates. Similarly, higher wages and new job opportunities outside the tea sector, in conjunction with the real or perceived amenities of urban lifestyles are further reducing the available workforce.

8. Major problems regarding working conditions in the sector include low wages, long working hours, no or limited paid leave, and vulnerable or inexistent job contracts. They also include child labour, exposure to pesticides and insufficient personal protective equipment.

9. Estates are generally responsible for providing certain basic services to workers, such as housing, sanitation, health, water and education, which are not always adequate. There are numerous reports of discrimination against selected communities, migrants, and in particular against women. The gender bias is said to be particularly pronounced on the estates. While supervisory and management functions are typically assumed by men, women are often assigned to do the hard, physical field work. At the same time, women often have less access to resources, such as land and finances.

#### **c. Environmental sustainability**

10. Tea production can also have several environmental sustainability issues, including:

- Deforestation: Tea plantations are often found in areas of high biodiversity and are associated with the destruction of tropical forests. The drying process can require up to 1 hectare of timber for every 3 hectares of tea.

- Erosion and decreased soil fertility: Various factors such as monoculture production, cultivation on sloped lands, and forest removal have led to soil erosion and decreased soil fertility.
- Agrochemical use: Pesticide and fertilizer use is common on tea plantations, and has both social and environmental implications.

11. Climate variability, incidents of frost and prevalence of pests, also have an influence on tea production, and are beginning to affect productivity.

### **III. IMPACTS OF CERTIFICATION AND BARRIERS TO IMPROVEMENT: FARM INCOME, MARKET ACCESS AND RURAL DEVELOPMENT**

12. Most available literature recognizes that, in principle, certification schemes have positive impacts on the various dimensions of sustainability. In practice, however, the results are highly context and location-specific and depend on the type of certification scheme. Even where positive effects exist, they are often small and limited to a few beneficiaries. More generally, many certification schemes are said to soothe the conscience of retailers and consumers rather than address the needs and interests of the workers and producers.

#### **a. Impacts of certification through training**

13. Training is generally associated with positive impacts for farm income, market access and rural development. A literature review found that an increase in training is associated with:

- Better safety measures for handling chemical inputs, as well as reducing their use, which can have a positive impact for both the individual user and the wider community.
- Higher yields and better quality.
- Better management practices in producer organizations, including better record keeping and accounting.
- Improved gender equality.

14. However, it is difficult to ascertain the extent to which training is responsible for such positive outcomes, as it is often a part of a broader developmental effort, delivered by a wide range of different and often external organizations. Furthermore, there are issues with the uptake of training, especially where this clashes with long-standing norms, such as gender roles or farming practices.

#### **b. Impact on farm income**

15. While there is a growing perception that certification can result in higher incomes for producers, the evidence is not conclusive. A review of the literature in conjunction with targeted interviews suggests that (i) both income and costs increase as a result of certification and therefore do not always result in higher net returns and that (ii) the right enabling environment is critical to reap the full benefits of certification. Easing access to foreign markets and facilitating trade in certified tea have been identified as important “companion factors” in making certification schemes effective in raising farm income.

#### ***Prices***

16. Certification generally offers producers better prices for their products and raises farm income. However, several factors need to be in place to ensure a positive practical effect on price and income. These include:

- Ensuring a significant price transmission from the final consumer level down to the primary producer.

- Upholding full transparency on how the premium is spent. The onus here is largely on the producer organizations.
- Ensuring tea auctions maintain fully transparent transactions. In some cases, as little as 10 percent of certified tea is sold as “certified” and farmers do not receive premiums for the rest. In such cases, it is less likely that they will notice an increase in price and income.
- Maintaining certification labels along the various stages of the value chain. Some companies source certified tea to reduce risks in the supply chain but do not label the products as such. This can reduce or entirely eliminate the premium.
- Managing the transition from conventional to certified tea. For smallholders, one of the biggest challenges is the transition to certified production. This is when they have to make the initial investments to meet the standards set by the certification schemes, while the related price premiums are not yet available.

### *Yield and quality*

17. Evidence of the impact of certification on yield and tea quality is mixed. Yields and quality can also be affected by other factors such as weather or other developmental efforts, which makes it difficult to isolate the effects of certification.

18. Where certification effects have been isolated, they suggest that benefits are most prominent where less efficient farming practices are used. Here, certification can significantly improve yields, notably when combined with training. Again, there are important exceptions to the generally positive effects. For example, land reallocation to buffer zones – as required by some certification schemes - can result in lower yields.

19. The quality of tea is often a more important contributor to farm income than the mere quantities produced per unit of land. For improved quality, training is an even more important factor. A major challenge here is that the efforts to improve the quality of tea at the farm level can be seriously diluted along the value chain. Many big tea companies blend high quality tea with lower quality tea to meet the demand of the inexpensive mass markets. Such practices can lead to lower prices for farmers.

### *Costs and other indirect impacts*

20. In about 60 percent of all schemes, the costs for certification are borne by the producers. Although these costs are generally shared by many farmers within a cooperative, the expenses for monitoring, documentation, awareness building, training and planning can be burdensome. This is particularly true for organizations in the process of preparing for certification, since these costs are borne before the benefits of higher prices can be reaped.

21. In addition to the higher operating costs, there are capital expenditures to meet and maintain certification requirements. They include construction and maintenance of production and processing facilities, or pipelines for drinking water.

22. Certification can also have indirect positive impacts on farm income. Where training enables farmers to produce more food in their own gardens, they can sell excess produce on local markets.

### **c. Sustainability certification and market access**

23. There is a growing recognition that certification plays a positive role in facilitating access to certain markets, and therefore acts as a “licence to trade”. Some certification schemes help producers sell to big tea companies, such as Unilever, who demand “certified” or “sustainably sourced” produce. Certification also helps attract committed buyers and therefore enhances market access. However, rather than seeking new certified suppliers, companies often ensure that existing suppliers become certified. In such cases, certification does not increase market access, but merely maintains the existing one.

24. Overall, available evidence suggests that certification can increase market access for producers. The actual effects, however, depend on several factors, including the available physical and market infrastructure, the ability to reap the benefits of economies of scale and scope and the presence of efficient producer groups.

*i. Physical access and infrastructure*

25. Producers living far from markets and/or with poor access to telecommunications and transportation infrastructure, may face greater challenges in accessing the market and are also less likely to be “certified”.

26. While certification schemes do not address these issues directly, they may have some indirect and generally positive impacts on them. For instance, the Fairtrade community premium has been used to build or fix roads or bridges, or pay for better transportation infrastructure, enabling better access to the market. Many stakeholders in the tea industry believe that “certification has enabled supply chain actors to move closer to the suppliers”.

*ii. Role of the market structure*

27. There are different channels through which market structures affect the benefits of certification schemes. Alternative market channels such as auctions or direct sales clearly affect the extent to which benefits are transmitted from consumers or processors down to the producer. Auctions are generally believed to reduce market transparency and tilt market power towards one party, notably large buyers. Combined with retro-certification, this can limit producers’ access to certified markets.

28. Direct sales offer a common alternative to auctions. While direct sales may reduce market asymmetries relative to auctions, they can also cut out services provided by intermediaries such as risk management. Likewise, direct sales can make producers even more dependent on a few or only one buyer, leaving them with less bargaining power.

29. The benefits arising from a buyer-seller relationship depend very much on the buyer. In some cases, certification has enabled producers to set contracts with big producers, in which a pre-determined price and duration are set. This enables producers to sell a much smaller share of their tea at auction.

30. Another channel that influences the effectiveness of certification schemes is the degree of vertical integration. In general, vertical integration is believed to be beneficial for smallholder producers and certification can reinforce these benefits. Where vertical integration creates additional employment opportunities, there is a need for producers to reap a larger share of the profits. Vertical integration of producers into the processing chain is particularly important for green tea, as the leaves must be processed within hours of picking. Without vertical integration, the urgency with which they need to sell the tea weakens their ability to negotiate a better price.

*iii. Role of economies of scale and producer groups*

31. The ability of producers to meet certification requirements depends on several factors, including existing assets and history with certification schemes. Larger producers can more easily absorb costs and have more consistent and reliable supplies, offering buyers better quantity and quality assurances.

32. In some cases, certification schemes do not work directly with smallholders. For example, UTZ certifies tea estates that can source a certain share from independent smallholders certified through the estates. Smallholders generally need to be part of a producer organization in order to access the market for certified products.

#### **d. Certification and rural development**

33. The links between certification schemes and rural development are difficult to isolate and even more difficult to quantify. Some of the most commonly studied indicators include livelihood (e.g. wages and working conditions), wellbeing (e.g. health and food security), gender equality and child labour. However, the exact impacts of certification on these outcomes are difficult to gauge, owing to the lack of data and the need for complex measurement approaches<sup>2</sup>.

##### *i. Livelihood*

34. Several impacts of certification on livelihood have been noted, including:

- Increased rural employment associated with certified value chains.
- Minor increases in contracts and paid leave.
- Improved relationships between management and workers.

35. However, there are several factors limiting the ability of certification schemes to influence wage increases, such as:

- Institutional factors: for example, in Assam, where approximately half of India's tea is produced, a minimum wage advisory board was established in 2014 to define a new minimum wage for tea plantation workers. Before the committee's recommendations could be put into law, the Assam Tea Planters Association challenged the decision, resulting in a legal battle and stalling the wage increase.
- Power asymmetries: In order to raise wages, profit margins would have to be redistributed along the supply chain. This shift is difficult to achieve in a context of unbalanced power in the chain.
- Competition: Raising wages makes estates less competitive. Wages would therefore need to be raised across the sector to be effective.
- Setting wages: Because most certification schemes rely on wages defined by government or collective agreements, it is difficult for them to have an impact on the issue.

##### *ii. Wellbeing*

36. Although there are still problems with access to basic needs, some studies have associated certification with:

- Improved sanitation facilities and access to health services.
- Fewer health problems due to lower pesticide exposure.
- Improved access to drinking water, food security and housing.
- Better participation in decision-making by community members.

37. However, these factors are not only difficult to measure and enforce; the fact that many of these services, which normally fall under the purview of governments, are often the responsibility of tea estates complicates any objective assessments. There are also disagreements about who should provide which services, and loopholes may be taken advantage of by both sides.

##### *iii. Gender inequality and discrimination*

38. Most studies did not find statistically significant improvements in gender equality as a result of certification. There is some evidence suggesting that certification has resulted in an increased awareness of gender issues, joint financial decision-making, increased ownership of tea bushes by

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<sup>2</sup> Random Control Trials (RCTs) would be the preferred measurement approach, but they are costly and pose important moral questions.

women and greater female participation in producer organizations. However, these changes are generally very minor and still require additional support. Furthermore, instances of sexual harassment are still registered in the industry. Similarly, migrant workers generally remain the lowest paid and most disadvantaged workers on certified tea estates.

39. It is clear that certification alone cannot effectively address all of these issues. Instead, a broader change in mind-set and social norms is required for an effective impact.

*iv. Child labour*

40. Social standards in certified value chains generally have a positive impact on child labour. However, this is often only the case for households above the subsistence level. Child labour is not as much of an issue where schooling has been prioritized, and especially where free primary education is available.

41. In spite of possible improvements, there are still several barriers to addressing child labour. Parents often do not have viable alternatives for their children (schools, child care, etc.). Some families lack the necessary resources to pay school fees or depend on additional income earned by their children.

42. If farms lose their certification because they do not meet child labour standards, this does not solve the issue. Instead, it potentially limits their access to other benefits associated with certification.

#### IV. CONCLUSIONS

43. Certification schemes generally have a positive effect on farm income, market access and rural development. However, there are still several challenges inhibiting their effectiveness. It is necessary to monitor and safeguard the social and environmental standards that underpin the certification schemes. If left unattended, the excessive use of chemical inputs, long working hours, gender biases, or occupational health issues can result in serious reputational risks and undermine the certification schemes. However, many of these topics (e.g. gender equality, livelihood improvements, wellbeing) need to be addressed with specific and targeted policy measures.

44. There is also a need to manage the expectations associated with certification schemes. While certification schemes can contribute to other desirable outcomes such as gender equality, food security or poverty reduction, they cannot be expected to have a major positive impact on all sustainability issues<sup>3</sup>. Instead, certification schemes should be used in conjunction with other tools to reach acceptable environmental and social standards.

45. Perhaps most importantly, there is strong evidence that the effectiveness of certification schemes depends on the enabling environment in which they are established. In the tea sector, there is a particular need for more market transparency. This could be achieved through producer organisations, fair contract farming, and strengthening vertical integration. In addition, functioning physical and market infrastructure have been identified as critical elements for certification schemes to deliver the desired benefits for tea producers and their families.

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<sup>3</sup> Trying to use certification schemes as a single instrument to meet multiple objections is a violation of the Tinbergen principle, which requires at least as many instruments as there are objectives.