



**Food and Agriculture Organization  
of the United Nations**

**A Review of Existing Organisational Forms of  
Smallholder Farmers' Associations and their Contractual  
Relationships with other Market Participants in the East  
and Southern African ACP Region**

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January 2010

AAACP Paper Series – No. 11

**ALL ACP AGRICULTURAL COMMODITIES PROGRAMME**



## **Acknowledgements**

This document has been prepared as a contribution to the All ACP Agricultural Commodities Programme with funding from the European Union, by Nigel Poole, Centre for Development, Environment and Policy, School of Oriental and African Studies, University of London.

It was commissioned by the Trade and Markets Division, FAO.

## **Disclaimer**

The views expressed in this working paper are those of the author and do not necessarily reflect those of the Food and Agriculture Organization of the United Nations.

## *Preface*

This report was commissioned to inform interventions in support of processes of sector strategy initiated under the EU funded All ACP Agricultural Commodities Programme.

More specifically, the purpose of this report is to review existing organizational forms of smallholder farmers' associations and their contractual relationships with other market participants considering the prevailing structure of sectoral value chains, drawing on various types of academic and other literature and experiences of project initiatives and policy interventions across a range of countries and sectors in the East and Southern African ACP region.

In association with a related assessment of alternative mechanisms of state support to value chain development (see AAACP Paper Series No. 9), the review serves as a contribution towards the fulfilment of two key outputs specified in the project logframe of the EU AAACP, namely:(a) synthesis of options and diagnosis of the commodity chains and livelihood systems analysis results; and (b) elaboration on the incorporation of relevant strategy recommendations and action plans into national development plans and policies in country specific cases.

In practical terms, the two studies will form a basis of recommendations focussed on ensure smallholder farmer participation in, and benefit from, the processes of value chain development underway in the cassava sector in Zambia under the EU AAACP.

The key insights from the experiences reviewed have been developed within a framework utilising transaction cost thinking and concepts from the organisation and business development literature. They illustrate how, in African agricultural markets, 'institutional innovation' is needed in respect of new 'rules of the game', and also new types of organisation, ie 'new players in the game', both within rural areas and also for linking rural supply and urban consumption.

The study argues that it is often small-scale institutional innovations in local market organisation and other non-price factors that are likely to stimulate smallholder participation in markets, particularly for staple foods in Africa. Efficient market organisation not only involves more but also better linkages between different economic players, which in turn require investment in various forms of human and social capital.

On this basis, the report suggests that the international donor community can play a key role in system or sector-wide initiatives. Besides encouraging institutional innovations, specific investments in human and social capital and business and sectoral organisation are also needed to enable new ways of organising people and markets to work for the poor - including agricultural smallholder collective enterprise.

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## *Executive Summary*

Considerable changes have occurred in the global agricultural economy over the past decade. Growing urban demand in developing countries, greater influence of the private sector in linking smallholder farmers to more dynamic markets, increasingly vertically coordinated supply chains, a recognised need to support smallholders as a means of tackling poverty, and more stringent food safety standards are just a few of the issues. The recent dramatic food price increases have been attributed by commentators to a variety of sources – poor harvests in major producing regions, low stocks, depreciation of the US dollar, financial speculation, inappropriate energy policies and diversion of agricultural production into biofuels, other linkages to non-agricultural trade and investment patterns. The rise of agricultural sector superpowers, such as some South American countries in grains, sugar cane and other global commodities, has made international markets more competitive. Climate change is already posing agroclimatic challenges, and the probability of more severe impacts in the near future will exacerbate the threats to producer livelihoods, particularly in marginal regions of developing countries. Also, HIV/AIDS and migration are having complex effects on rural economies, not just changing the patterns of demand. Are smallholder farmers' associations yet another problem, or are they part of the solution to rural poverty?

Often it is small-scale institutional innovations in local market organisation that are likely to stimulate smallholder participation in input and output markets, particularly in staple foods markets in Africa. 'Institutional innovation' is needed in respect of new 'rules of the game' and new types of organisation, ie 'new players in the game', within rural areas and also for linking rural supply and urban consumption. So, too, are specific investments in human and social capital and business and market organisation: new ways of organising both people and markets to work for the poor. Nevertheless, a resurgence of interest in farmer organisation, although coming at a time when there are renewed goals for agriculture and the rural sector, is surprising: there has been a history of organisational failure in many developing regions over the last two or three decades.

A review of literature and experiences is timely: in order to look to the future, there is a need to understand existing organisational forms of smallholder farmers' associations and their contractual relationships with other market participants within the context of prevailing sectoral value chains in the East and Southern Africa ACP region. Specific examples of smallholder farmers' associations and their contractual arrangements are considered in this report. In the light of changing global contexts, we seek to provide some indication of best practice for policy on smallholder farmer associations to guide

poverty reduction policies through potential intervention strategies for specific products and markets.

The fundamental question is how can better organisation of people and markets reduce hunger, improve rural market performance and contribute to wider economic growth? The report tackles a series of issues concerning collective economic organisation in Africa.

### *Potential unrealised?*

The historical outline of farmer associations in Africa that follows illustrates the diversity of group types, ranging from small informal farmer groups to large, tiered farmer cooperatives, different sources and levels of initiatives and interventions, a variety of contexts, and changing policy approaches. A persistent theme in the literature is that farmer groups:

- Lack capital to grow in scale and complexity, particularly investment in physical assets for value addition through processing and manufacturing;
- Lack management capacity and good organisational governance;
- Compete in markets against economic forces that confound their traditionally bureaucratic and unresponsive structures and strategies.

Besides internal organisational weaknesses and the lack of market competitiveness, unstable agricultural policies have created a disempowering external environment. As a result, in general neither statutory nor voluntary forms of association and collective enterprise have generated significant and sustainable agribusinesses in Africa.

### *Collective organisation: can it contribute to more equitable and efficient markets?*

There are theoretical explanations of the failures of collective organisation but at the same time, the fundamental reasons for collaborating hold true: the potential for exploiting production and managerial economies of scale, overcoming market entry barriers, reducing transaction costs and cultivating supply chain relationships. Collective decision making may be cumbersome, and top-down decision making may be undesirable. But new forms of collective enterprise illustrate that innovative business models can work: 'new generation cooperatives' may provide solutions to some of the historical and structural problems of cooperatives. There are alternative management structures and financial resources - either philanthropic support; or external equity investment with a capacity to exert leverage through management building; or invitations to bondholders with a financial stake but without governance rights. These strategies offer the possibility of external capitalisation without diluting membership control.

Despite a history of operational failure, statutory arrangements such as levies and marketing boards are also mechanisms with potential to overcome market failures and the provision of public goods. Also, much may be learnt also from experiences elsewhere, such as the 'interprofessional' model for sectoral vertical and horizontal coordination.

### *Can African cooperatives work?*

Traditional cooperative organisations do not easily deliver on social as well as economic objectives, and social policy is better separated from enterprise policy. Supply chain linkages can deliver on social and environmental management responsibilities, but these are often mediated by donors, NGOs and philanthropic organisations, and are linked to niche and vulnerable markets inaccessible to the majority of smallholders. Smallholder associations have a potentially valuable advocacy role in politics, but the converse is not true: political subversion leads to inequity and inefficiency. However, sufficient examples of successful formal cooperatives exist – or more broadly, collective enterprise – to argue that collective ways of organising agricultural marketing can work in Africa. Many features may differentiate the successes from the failures, but it is uncontroversial to state that marketing organisations must be entrepreneurial. The essential skills may not exist at grassroots level, but organisational hierarchies such as 'tiered' cooperatives can source external management input and equal private sector performance, by forming commercial subsidiaries that permit organisations to retain cooperative principles.

The approach of external supporting organisations must be patient and realistic. Collective enterprise may not always work because usually there are threshold levels of asset requirements and of external support for successful group formation and operation. It is clear that collective enterprises are 'organic': they learn and grow, sometimes fail, and sometimes need to rise from the ashes of incompetence and corruption. The path to maturity is usually long, and needs supportive investment through a range of planned and sequenced business services, with an exit strategy emplaced to ensure progress towards sustainability. And there is no 'one size-fits all', and no guarantee that individual successes can be upscaled and replicated.

The bulk of evidence so far shows that it is the agricultural middle class who are the growers of high value, highly specified products. While the poor can still benefit through economic multipliers, other approaches and other local, staples markets matter to most African smallholders. Nevertheless, it is possible that such caution reflects a lack of innovative approaches by researchers and development workers to organisational development and supply chain linkages.

### *What part does the institutional framework play?*

The importance of the historical, political and market context within which smallholder enterprise operates is clear. Institutions frame the relationship between state and the 'citizen' and 'organisations', mediating the flows of technical support towards the grassroots, and advocacy towards the state, and the relationship of politics to local development processes. The purpose of the formal legal and regulatory framework, such as competition and business laws and cooperative laws is, in part, to shape the environment and enable business to operate effectively. This may or may not happen in practice: producer organisations often are surrounded by legal restrictions, and micro-, small and medium-sized enterprises often go unrecognised by the state as policy stakeholders. Where sectoral policy is increasingly directed towards scale, efficiency and new technologies to address food security objectives for growing populations in an era of climate change and social transformations, the needs of smallholders may be unrecognised and underprovided. Weaknesses in transport systems and infrastructure, and certain restrictive trade practices within and between African countries also impose heavy burdens on local or regional trade. Such formal business and legal frameworks, policies and priorities are critical to economic empowerment of the rural poor. Direct intervention should have a 'light', 'enabling' touch: correcting specific market failures, without otherwise intervening in commercial chain activities.

Empowering collective organisations requires 'voice' to countervail urban biases. Institutional innovations envisaged to re-vitalise or re-envision collective enterprise include new rural and cooperative business models that may require new legislation. Innovation must be informed by, adapted and implemented by knowledgeable stakeholders, specialists and entrepreneurs who understand the realities of collective farmer organisation: above all, farmers must participate. To some extent these players must be arbitrageurs of stakeholder relations between the rural sector and government officials who may have limited awareness of participatory process, of the complex operations of cooperatives and rural business activities. New specialist structures may be needed to undertake this role, cutting across disciplines and organisations and relevant ministries; specialised organisations can be contracted from the private sector and civil society to link central policy and procedures with practice at the periphery.

### *What part do international donors play?*

Most successful cases of collective enterprise creation have depended on a substantial degree of intervention from NGOs and international donors. The challenge is to move beyond 'point' or individual interventions to 'system' changes, initiatives that address sectoral weaknesses and market and public sector failures. Sectoral investment

approaches can be used by international donors who may have comparative advantage in attracting interest and commitments from the range of supply chain or network players: research and development, input suppliers, producers and downstream traders, processors, manufacturers and retailers. International donors can best employ their financial and human resources to address sectoral failures that cannot be addressed by the state or the private sector. They can also exploit a comparative advantage in 'trust', a potentially more objective analysis and less conflicting incentive structure than the state and possibly some civil society organisations.

#### *How can agribusiness reduce poverty?*

Sufficient examples of successful collective and collaborative supply chain enterprise exist to provide reassurance that private sector linkages can engage smallholders in markets. Yet, as noted, these are most likely to reach the agricultural middle class, and the rural poor may be only indirect beneficiaries through labour markets and other multipliers such as services and downstream industry. Nevertheless, the private sector processing, manufacturing and distribution sectors need raw materials, and commercial linkages can be formed on satisfactory terms. Partnership programmes can provide the essential capacity building to create viable business relationships in competitive markets.

Private firms do exercise corporate social and environmental responsibility, and valuable examples from major agrifood firms are beyond the scope of this paper. Nevertheless, it is not philanthropy but profitability that drives the private sector. Agribusiness partnership programmes cannot necessarily be mainstreamed. Where commercial linkages work, donors and the state should not crowd out the private sector.

#### *What sort of markets matter to African smallholders?*

The real challenge for pro-poor development initiatives is to reach the poorest (agriculture-dependent) smallholders with the lowest level of household assets who cannot easily turn to income earning opportunities other than agriculture. It is the domestic markets for lower value and bulk commodities such as staple products that are most closely linked to poverty, under-nutrition and ill-health in East and Southern African countries. These markets have been less touched by programmes and projects. For many African smallholders, such domestic markets are much more important than export markets, even if they are not so politically attractive to donors and NGOs. Equitable rural development may be best stimulated through sectoral intervention in bulk pro-poor products and commodities that are produced, traded and consumed locally, giving rise to broader economic multipliers – staples such as cereals and root crops, and other fruits and vegetable for which local markets already exist or have been developed.

## 1 Introduction

Considerable changes have occurred in the global agricultural economy over the past decade, with even more dramatic market changes in the past two years. Among the pressing problems, poverty remains endemic and persistent. The food price problem is not over (FAO 2008; FAO 2008); and the new scramble for African resources including agricultural lands and water is under way. The need for a global agricultural supply-led response has been articulated recently by Piesse and Thirtle (2009). Nor is the food availability problem over. Investments in agricultural research and the development of new technologies have had 'proven successes' during the past 50 years (Spielman, D. J. and Pandya-Lorch, R. 2009), and the capacity of the productive sector to respond is not in doubt (Agrimonde® 2009; FAO 2009). Nevertheless, political will to make the necessary investments in agricultural research is lacking. Moreover, investments in agricultural research and production require complementary investments in processing, marketing and distribution: investments in rural energy, water supplies, information, communications and logistical infrastructure are necessary to reduce transformation and transaction costs (North, D. C. 1990).

### 1.1 The development potential of better market organisation

Often it is small-scale institutional innovations in local market organisation and other non-price factors, rather than 'macro' trade and price policies, that are likely to stimulate smallholder participation in input and output markets, particularly in staple foods markets in Africa (Alene, A. D., Manyong, V. M., Omany, G., Mignouna, H. D., Bokanga, M. and Odhiambo, G. 2008; Barrett, C. B. 2008). With the correct support and appropriate institutional organisation, many of the challenges enumerated above may also present a great number of opportunities. Indeed, the World Development Report 2008 states that 'a key issue for development is enhancing the participation of smallholders and ensuring the poverty reducing impacts of agricultural growth' (World Bank 2008: 12). Expanding agricultural markets can multiply development of other sectors such as non-farm employment, and generate development. Traders, moreover, are a market nexus with potential to efficiently deliver inputs and multiply interventions such as the provision of finance throughout the market system. Better market organisation not only involves more but also better linkages between different economic players, which in turn requires investment in various forms of human and social capital.

#### 1.1.1 Potential unrealised?

Yet, smallholder collective action has a troubled past, in respect of both voluntary and statutory forms of association. By the 1990s the general consensus was that cooperatives in Africa were failing (Develtere, P., Pollet, I. and Wanyama, F. 2008), and

for multiple reasons. This report also looks at the historical context because 'it is of prime importance to understand how cooperatives were introduced, what cooperative philosophy was construed and how this is related to cooperative behaviour, both social and economic, that existed in the region' (p. 2). Dependency on government agricultural policies at the end of the colonial period and into the independence era restricted the development of strategic enterprise and despite liberalisation policies aimed at encouraging enterprise during the 1990s. The lack of documentation since that time has meant that little is known regarding the impact of these policies. Major considerations for developing better ways of organising markets for the poor are the following:

### *1.1.2 Collective organisation: can it contribute to equitable and efficient markets?*

The resurgence of interest in farmer organisation, coming at a time when there are renewed goals for agriculture and the rural sector, is surprising, given the history of failure in many developing regions over the last two or three decades and the persistence of poverty even in the more successful developing countries. An historical analysis of the policy climate raises the question whether the resurgence of interest in farmer organisation is a full revolution of the development policy wheel. Answering this requires coverage of the agricultural policies pertaining to market development over a given period of years. Is it possible to identify political, economic, technical and social 'environmental' changes that suggest that *external conditions for successful farmer organisation are any more propitious than in the past?* A second point of the review is to understand the previous experience of general disappointment in organisational performance, and from the learning experience to ascertain whether current types of intervention are different; in short, *is the organisation model and its internal conditions any more propitious than in the past?* A positive answer to either of these questions would suggest that the turn of the policy wheel is not merely recycling past ideas, but potentially progressing in some given direction.

### *1.1.3 Can African cooperatives work?*

While many cooperatives may have struggled and disappeared, others have recast themselves in order to cope better with the changes in global markets. Cooperatives and rural associations are now resurgent business forms in Africa. It is - once again - accepted that farmer organisations offer a way to exploit the potential of collective action in order to access markets more effectively, to take advantage of organisational opportunities to overcome financial - cash and investment - constraints, and information asymmetries, and to exploit scale economies in production and marketing. The potential therefore for farmer associations to improve the livelihoods of the rural population and contribute to a decrease in poverty may well depend on a new generation of dynamic and alternative forms of commercial organisation. With rapidly changing global contexts,

what forms of smallholder farmer associations have found success and can these models be replicated? What support is necessary and feasible?

#### *1.1.4 What part does the institutional framework play?*

Market activity usually must operate within a broader framework of both formal and informal constraints that regulate economic activity. Institutions supporting a pro-poor commercial environment are likely to include both private commercial initiatives and also public policy interventions. Policies on competition, for example, can be locally targeted and help to restrain anti-competitive market structures and conduct, and serve as a framework for sectoral support from the public and donor sectors. Moreover, there are roles for civil society and advocacy organisations in building markets and necessary forms of institutional capital, such as an efficient regulatory environment, business ethics, social and environmental responsibility, competition policies, and consumer education. Similarly, multi-stakeholder interventions are necessary for the formation of social, economic and organisational capital such as efficient farmer associations.

#### *1.1.5 What part do international donors play?*

Donor participation is critical, but donor ideology has also influenced the choice of organisational forms and marketing interventions. Donor policies and projects are in turn influenced by pragmatic considerations such as how aid can be most easily dispensed, targets met, and supporters satisfied. This probably applies just as much at the beginning of the Twenty-first Century as during the Twentieth Century, and the danger of interventions representing prevailing conventional wisdom remains alive.

#### *1.1.6 How can agribusiness reduce poverty?*

The extent to which economic development and wellbeing can be generated by supporting the agricultural activities of the poorest is a moot point. Reduction of poverty among the poorest may be more likely to come through interventions targeted at the not-so-poor, with resulting multiplier effects through the labour market, for example. Businesses may select against the extreme poor in such a way that agriculture, producer organisations and market integration are not a viable pathway out of poverty. These limits to direct intervention for poverty reduction are not well understood.

#### *1.1.7 What sort of markets matter to African smallholders?*

If the poorest agricultural smallholders are unlikely to be beneficiaries of commercial interventions because of resource constraints, market and public sector failures, and barriers to entry, are there alternative product markets in which they can engage to enhance their own food security and boost the local economy?

## **1.2 Organisation of the report**

This report examines the structural and managerial characteristics of rural collective organisations in East and Southern Africa. Each section ends with key points or specific insights into the issues surrounding smallholder farmer associations and their potential role in market development and poverty reduction.

In the section 2, the terminology of the subject matter is explained, and then key concepts are introduced that underlie the literature on smallholder farmer organisation. These are the New Institutional Economics concepts of transaction costs, applied principally to exchange between buyers and sellers in agrifood markets, but also concepts of business management within collective organisations. Attention is drawn to the need for entrepreneurship and deliberative processes of learning and development for smallholder organisations. Some readers may prefer to skip this more theoretical section, but on which the report later draws and without which it would be incomplete.

In section 3 the report takes a long view of organisations by considering the historical, political, socio-economic and cultural factors in the development of collective organisation across a number of countries. The literature comes from a variety of sources: supply chain management, marketing, policy and governance. It encompasses academic research, policy documents and 'grey' literature from NGOs and other market players. The review seeks to advance an understanding of the different roles played by government and the private sector and analyse the structural characteristics and policy interventions that have contributed to collective organisation and enterprise. Through the use of examples and case studies, the report illustrates organisations in practice and considers the factors contributing to their successful participation in markets.

A section is dedicated not to African organisations but to examples of organisational and institutional innovation from advanced economy countries. These cases suggest how new models of collective enterprise can be developed and might serve as examples for revising, or 're-envisioning' cooperative organisational models in Africa.

Section 4 reviews the external environment, taking this as international agribusiness and the global agricultural economy and policy. It comments on the need for a balanced perspective on the market opportunities and challenges, and notes that where smallholders have been successful in penetrating high value markets, often this is the result of context-specific interventions that may not be easily scaled up or replicated. It is made evident that a) opportunities for smallholder market entry, and b) the

contribution of farmer associations to poverty reduction, are both likely to be context-specific, and should be locally-determined.

Section 5 presents tools and typologies of farmer associations and presents examples in selected African countries. Importance is attached to the interrelationship between the organisation and the environment, including the supporting organisations and the institutional framework. This includes informal issues and trends towards inclusive approaches and stakeholder participation. These approaches are important inasmuch as they pay heed to significant social, cultural and political issues such as empowerment. These are generally of secondary importance to commercial organisations, notwithstanding the spread of the concepts of the three 'Es', or the 'Triple Bottom Line', of 'economics, equity and environmental management'. A series of key lessons establish a link between theoretical considerations and empirical experience.

Section 6 examines different types of inter-organisational coordination in African markets. Examples of smallholder-business engagement illustrate how specific businesses are willing to link with smallholders. The focus is on the private sector perspective on viable, or optimum, supply chain linkages and helps to frame the possibilities of external interventions and the significance of facilitating technologies such as IT.

The final section 7 suggests a framework and analysis of how organisational types and linkages can be established with the external market environment through innovations in organisational structure, governance and enabling institutions.

## 2 *Sectoral terms and context*

This section introduces the diverse terminology used throughout the literature in referring to associational forms of smallholder farmer organisation.

Subsequently, key concepts are introduced that underlie the literature on smallholder farmer organisation. These are the New Institutional Economics concepts of transaction costs, applied principally to exchange between buyers and sellers in agrifood markets, but also, briefly, of management processes within collective organisations. Attention is also drawn to the need for entrepreneurship and deliberative processes of learning and development for smallholder organisations. Some readers may prefer to skip this more theoretical section, but on which the report later draws and without which the report would be incomplete.

There follows an introduction to the history and evolution of collective organisation in the agrifood sector, summarising the economic and social principles underlying forms of collective organisation, and highlighting potential conflicts and tradeoffs between cooperation as a social movement and as a form of business enterprise. Space is given to the mechanisms that have caused the spread of collective organisation from advanced to developing countries, with a particular focus on Africa. Attention is drawn to how government sponsorship of cooperatives was often subverted by political objectives, and how voluntary collective organisation has been supplanted by statutory forms, and how these tendencies have been promoted by external donor organisations. Subsequent poor performance of state managed market organisation led to the enactment of policies of market liberalisation but did not elicit the expected private sector response. The supply chain integration that has occurred has been driven in high value markets by commercial firms while there has been a return – once again - to collective forms often initiated by external stakeholders to address the systemic weaknesses of market organisation among poorer smallholder farmers. Finally, examples of organisational and institutional innovation from advanced economy countries suggest how new models of collective enterprise can be developed and might serve as examples for innovative organisational models in African agriculture.

### **2.1 Collaboration: terminology and rationale**

The term 'smallholder farmers' association' is taken to refer to diverse types of groups who act collectively in order to benefit either as individuals or as a group. For some this may mean formal shared ownership and have democratic rights in decision-making processes at the grassroots level. For other groups it may mean an informal set of social

and business connections among farmers and between farmers and traders. The terminology used in the literature does not always differentiate between these diverse groups and uses terms such as cooperatives, farmer collectives, farmer associations, rural community enterprises, rural producer associations, community enterprises, micro and small enterprises, and farmer organisations (Donovan, J., Stoian, D. and Poole, N. D. 2008: 15). These groups usually are bound together with a set of common economic goals, and often a concurrent objective of social cohesion and community development: economic and social inclusion. Collaboration can achieve inclusion through leveraging the characteristics of structure, strategy, performance and empowerment (Box 1):

### **Box 1 Rationale for collaboration**

#### **Economic inclusion**

Economic inclusion is closely linked to optimum scale, recognising that small organisations may fail because they do not achieve the minimum efficient scale, and also that large organisations can suffer from diseconomies, especially managerial diseconomies of scale. Economic inclusion may embrace elements such as:

- Structure: through which an organisation achieves critical scale and increased access to markets. Advantages of scale include:
  - reduced costs for inputs, transformation and transaction functions
  - increased volumes, improved quality and timing of services and deliveries to market, associated networking advantages
  - potential for added value products
  - greater choice of routes to market.
- Strategy: through which the organisation develops 'market power' in negotiation through scale and the creation and/or exploitation of sustainable competitive advantages
- Performance: whereby the organisation achieves higher levels of efficiency and effectiveness – and perhaps equity – in production and marketing functions

#### **Social inclusion**

Empowerment is the principal mechanism for achieving social inclusion, which is mainly concerned with the creation of social and other forms of capital assets. Empowerment may be consistent with economic objectives, but can also create conflict and attenuate organisational performance. Empowerment and creation of social assets comes about through:

- participation and self-empowerment – voice
- individual and corporate capacity building
- representation and democratic governance
- female and 'minority' participation
- advocacy.

Source: adapted from Kachule, Poole and Dorward (2005).

## 2.2 Some theoretical considerations

### 2.2.1 *Market coordination: institutions, organisations, and transaction costs*

The respective roles of free markets and administered economic activity were one of the topics of greatest political and economic significance in the 20th Century. Into the new Century, neither free marketeers nor central planners have generated evidence sufficient to justify a polar conclusion about the respective coordinating roles of the 'visible' and 'invisible' hands. North's thesis (1990), now widely acknowledged, is that historic development has proceeded most effectively where economic activity has been supported by an institutional framework of incentives and both formal and informal constraints. He argues emphatically that it is the lack of institutional development that has characterised the low level of economic development in poor countries: business culture, societal norms and formal laws which fail to provide incentives for economic activities, such that economic organisations – firms, cooperatives and individual engagement in markets – are more 'redistributive' than 'productive'. Transaction costs are often at a level that prohibits remunerative exchange: 'The costliness of information is the key to the costliness of transacting, which consists of the costs of measuring the valuable attributes of what is being exchanged and the cost of protecting rights and policing and enforcing agreements. These measurement and enforcement costs are the sources of social, political, and economic institutions' (p. 27). Consequently, 'the inability of societies to develop effective, low cost enforcement of contracts is the most important source of both historical stagnation and contemporary underdevelopment in the Third World' (p. 54). Fafchamps and Minten (1999) introduce the human element into considerations of market exchange in a succinct fashion: without supporting institutions, 'the free market remains nothing but a flea market' (p. 31). In short, institutions must be created to support productive patterns of exchange between economic organisations, be they individual traders, collective organisations, or private firms.

According to some analysts, planned coordination has a more important role in economic exchange than market coordination as a generator of economic growth: 'History shows that the driving force of successful capitalist development is not the perfection of the market mechanism but the building of organizational capabilities' (Lazonick, W. 1991: 8). Hall and Soskice's treatise on institutions and economic development (Hall, P. A. and Soskice, D. 2001) distinguishes between 'liberal market economies' and 'coordinated market economies' as environments which offer different possibilities of institutional support, legal frameworks, industrial relations and strategic management. The result is distinctive forms of capitalism, varying according to the form and strength of the institutional framework.

### 2.2.2 *Institutions*

The introduction into economics of the study of transactions is attributed to the US political economist John R. Commons. In the tradition of the American Institutionalists analysing collective action, Commons was searching for an economic theory of the part played by collective action in the control of individual action. The three constituents of collective action were, he believed, conflict, dependence and order – important characteristics of the intra-and inter-organisational relationships of farmer enterprise: for example, *conflict* over objectives of different stakeholders; *dependence* on external support; *order* in terms of governance and accountability. The unit of investigation that would encompass these three constituents was the transaction: 'so I made the transaction the ultimate unit of economic investigation, a unit of transfer of legal control' (Commons, J. R. 1934: 4).

The fundamentals of Old Institutional Economics (OIE) concern the organisation and control of the economic system. The forces governing economic outcomes were regarded as mediated not first and foremost through the price mechanism, but through power relations, legal rights and the role of the polity – again, relevant to farmer associations. The operation of the price mechanism was not disputed but institutions were held to supersede prices in importance: 'It is simply not true that scarce resources are allocated among alternative uses by the market..... The real determinant of whatever allocation occurs in any society is the organizational structure of that society - in short, its institutions' (Ayres, C. E. 1957: 26).

A tenet of OIE is that economic power is an important factor in the allocation of resources and in the distribution of gains from exchange. Power structures, therefore, mediate the terms of how smallholder organisations can access downstream markets. Also, OIE emphasises behavioural assumptions that are not simply self-maximising, and in many respects reflects more faithfully the behaviour of economic agents than common assumptions under prevailing neoclassical approaches, especially when collective action shapes the maximising calculus.

### 2.2.3 *Market analysis frameworks: SCP, SCM and NIE*

The organisation and performance of markets has been analysed for decades within the framework of 'industrial organisation' (IO), or structure-conduct-performance (SCP). Scherer and Ross define industrial organisation as 'how productive activities are brought into harmony with the demand for goods and services through some organising mechanism such as the free market, and how variations and imperfections in the

organising mechanism affect the success achieved in satisfying an economy's wants' (Scherer and Ross, 1990: 1).

The contemporary multiplication of 'hybrid' forms of interfirm organisation - arrangements intermediate between spot exchange and vertical integration - poses important challenges for economists within an IO framework as much as for firm managers. The importance of understanding the vertical coordination of economic exchange becomes increasingly evident as the choice of organisational relations in many markets, including the agrifood industry, shifts away from reliance on spot exchange within free markets. There has been a fundamental change in supply chains in the advanced economies, a shift from competitive vertical relations towards the cooperative organisation of the supply chain, or supply chain management (SCM). This process has been impelled not just by firm strategy but by the dynamic demand characteristics of food markets and the supply conditions characteristic of primary agricultural products. In particular, the consumers' search for quality, safety and value-for-money, combined with the other pressures on food firms, is restructuring the supply chain. The costs that 'efficient consumer response' and closer market coordination aim to save are analogous in part to Coase's 'marketing costs' (1937) which have been popularised since as transaction costs (Williamson, O. E. 1975; Williamson, O. E. 1985).

New (1997) has drawn attention to the context of SCM in industrial societies. He cited three issues of ethical significance: the exploitation of poor producers in developing countries; power imbalances in the corporate economy; and 'environment' in a general sense. Many others could be added. According to New, consumption involves issues of both efficiency and justice: 'There is a direct connection between the design and operation of the supply chain and the social and economic experience of those with the least power.... Even in the developed world, the issue of relative power affects the interpretation and meaning of supply chain innovations' (p. 19).

The study of contractual relationships has become central to public policies and firm strategies for market development. Mighell and Jones (1963) published the seminal work on the use of contracts as mechanisms of vertical coordination in the food system. By vertical coordination, they meant 'all the ways in which the vertical stages of production are controlled and directed, within firms (by the administration) and between firms (by the price/market mechanism)' (p. 10). The means of vertical coordination include open market prices, government controls, use of different forms of contracts, and integration.

In discussing the different forms of agricultural contracts, they proposed a typology, the significant differences within which lie in the extent to which specified processes or stages in production are transferred between the parties:

- market-specification contracts occur where the producer transfers part of the risk and management function to another for at least one production period;
- production-management contracts call for a more direct participation by the contractor in production management;
- in resource-providing contracts, the contractor also provides inputs, the producer is paid for his management, and the contractor assumes much more of the production risk.

Between these types of contract the boundaries are imprecise (Mighell and Jones, 1963: 13-14). However, this simple approach to mechanisms of coordination abstracts entirely from the institutions of power and wider – network-type economic relationships.

#### *2.2.4 Inter-organisational transactions*

At a conceptual level, writers have voiced concerns about the lack of application of conventional analysis to problems of interfirm contractual arrangements in real markets. Williamson built on Coase's 1937 theory of the firm to analyse his preoccupation with the coexistence of markets and hierarchies for economic coordination (Williamson, O. E. 1975; Williamson, O. E. 1985). His thesis was that variation in and evolution of organisational forms depends on the technology of transacting and the incentive to minimise transaction costs. What differentiated his analyses from the typical SCP approach, according to Williamson, was the treatment of the internal decision making process of the firm and how exchange activities are assigned to different organisational forms or 'governance structures': they are either integrated within the firm, or undertaken through spot markets, or by some form of intermediate contractual ('hybrid') relationship. What has come to be known as the Transaction Cost Economics (TCE) branch of New Institutional Economics (NIE) is directly concerned with the issues of market organisation, and the concepts are particularly helpful in understanding the challenges of farmer collective organisation.

The work of Coase, Williamson and others has resulted in Transaction Cost Economics becoming one of the most influential branches of the New Institutional Economics school. Transaction costs are now widely held to be an important explanation of the vertical arrangements within markets and industries generally.

### 2.2.5 Transaction costs

Coase argued that the main reason why it is profitable to establish a firm is that there is a cost of using the price mechanism. The costs of 'organising' production through the price mechanism are those of price discovery and negotiating contracts. Thus, firms exist for efficiency reasons. When the cost to an economic agent of procuring goods or services using the price mechanism (the market) exceeds the cost of self-supply (integration), then the agent will internalise the supply, and a firm will come into being.

New Institutional Economics (NIE) is concerned with transaction costs and the organisation and development of economic activity. 'At the heart of institutional economics is the making, monitoring and enforcing of contracts' (Hubbard, M. 1997: 240). Although Williamson traced its origins to the 1930s, NIE derives its concern with transactions costs, and little else, from OIE.

In Transaction Cost Economics (TCE), it is the transaction rather than the commodity that is the unit of analysis. A transaction is a process linking various functions, involving the exchange of information, goods, services, money and property rights. Transaction costs are the costs of these exchanges and arise whenever there is any form of economic organisation, be it within a vertically integrated firm, in a market or in a command economy (in which transactions are largely absent). Transaction costs are of both an *ex ante* and *ex post* kind:

1. *ex ante* costs:

- searching for potential exchange agents (buyers or sellers);
- screening potential agents for characteristics such as honesty, creditworthiness;
- bargaining over terms of exchange and price determination;

2. *ex post* costs:

- transferring property rights;
- monitoring compliance with contractual terms;
- enforcing sanctions in the event of non-compliance.

The true costs of exchange therefore comprise a) the orthodox neoclassical transformation costs associated with the production and distribution of goods and services, and b) the transaction costs of searching, measuring, mediating and monitoring during the exchange process incurred in order to bring together buyers and sellers and complete the exchange. The total costs of economic activity are then made up as follows:

$$\text{costs total} = \text{costs transformation} + \text{costs transaction}$$

The source of transaction costs is the complexity and uncertainty of the real economic environment: 'The ease or difficulty of contracting, and the types of contract made, are determined by the level and nature of transaction costs, underlying which is the extent of imperfect information involved in making a transaction' (Hubbard, M. 1997: 240).

The basic concepts underlying TCE are certain assumptions about behaviour, and certain dimensions of transactions.

### **Behavioural assumptions**

Regarding behaviour, man is perceived as being motivated by the conventional maximising calculus constrained by bounded rationality and influenced by opportunism.

#### ***Opportunism***

This is a negative self-maximising attribute, a predisposition to lie, cheat, or steal.

#### ***Bounded rationality***

The capacity of the human mind for formulating and solving complex problems is very small compared with the size of the problems whose solution is required for objectively rational behaviour in the real world.

### **Transaction dimensions**

According to TCE, there are three important dimensions of transactions: asset specificity, frequency of transactions, and uncertainty due to lack of information and informational asymmetry, leading to adverse selection and moral hazard.

#### ***Asset specificity***

Asset specificity refers to a situation where durable investments are associated with a particular transaction, and where the redeployment of such investments is not possible, or at best the recovery of which would give rise to considerable sunk costs. Three types of asset specificity are found:

- site specificity: firms or plants are located in close proximity in order to economise on labour skills, transportation costs, inventories;
- physical specificity: plant, machinery and technology that are specific to a transaction;
- human specificity: specific labour skills, social and managerial relationships, and process economies derived from cost reductions through learning by doing and from information sharing.

#### ***Frequency of transactions***

In a world of impersonal exchange, buyers and sellers are dealing with multiple individuals, and can acquire very little information about them. Where the exchange is

not repeated, opportunism creates the need for third-party enforcement of contractual terms. On the contrary, in an ideal world when transactions are frequently repeated, the buyers and sellers are known or easily identified. Repeated transactions between the same players therefore lead to self-enforcing cooperative solutions. Also relevant to frequency is the size of the transaction: the smaller the transaction, the less the incentive to opportunism.

### **Informational asymmetry and agency problems**

Imperfect information, therefore, underlies transaction costs, and differentiates NIE from neoclassical market analyses. Uncertainty arises in exchange for a number of reasons (Jaffee, S. 1995):

- information is asymmetric, that is, usually held unequally between contracting parties: buyers of agrifood products usually know more about market prices and demand conditions, and sellers know more about the characteristics such as quality of the raw products;
- in most explicit contracts, and in all implicit contracts, property rights are unlikely to be completely specified, and are therefore subject to non-excludability and non-transferability;
- there are agency problems which arise from potential conflicts of interests between transactors. The tendency to engage in either cooperative or competitive behaviour creates uncertainty and requires monitoring and enforcement.

The relationship between two firms is of the 'principal-agent' type if the information and actions of the secondary (agent) firm are hidden from the primary (principal) firm. Where the interests of the agent do not coincide with those of the principal the primary firm must provide an incentive to align the otherwise conflicting interests. Two important results of the principal-agent problem are adverse selection and moral hazard.

Through adverse selection, high quality goods are displaced by those of lower quality, and consequently the market is characterised by only poorer quality products and lower prices (Akerlof, G. A. 1970). This is true especially if seller reputation is unimportant and sellers of higher quality goods are unable to signal high quality. Moral hazard arises when imperfect monitoring due to lack of information facilitates opportunistic, ex post, usually hidden default with respect to contractual agreements. Moral hazard, like other forms of opportunistic behaviour, is attenuated under conditions of long-term relationships (Holmström, B. 1979).

### *2.2.6 The significance of transaction costs in agrifood markets*

TCE regards the choice of vertical coordination mechanism on the spectrum from spot markets to vertical integration as a decision variable. In short, the multiplicity of contractual arrangements arises because transactions differ and efficiency is realised only if coordination mechanisms are tailored to each transaction. TCE adopts a comparative approach to the microanalysis of coordination mechanisms, what Williamson calls 'the institutions of governance'.

It is usually assumed that the objective of the economic agent is to minimise the sum of transaction and production costs; that is to say, transactions are assigned to different coordinating mechanisms to minimise total costs. In short, as Wallis and North argue, 'people maximize net benefits' (Wallis, J. J. and North, D. C. 1986: 97). Transaction costs are major determinants of forms of market organisation and how sellers and buyers in agrifood markets choose to contract. The significance of the transaction costs of searching, etc, is that if total costs exceed the net benefits of exchange, buyers and sellers are unable to agree terms and markets probably will fail. New Institutional Economics, therefore, provides a framework, albeit partial, for understanding optimal organisational arrangements for agrifood enterprises.

### *2.2.7 The problems of collective business management*

When collective action is considered, and enterprise becomes conflated with social action, the maximising objectives becomes much less clear, be they individual or collective, owner versus management, social or economic. The question not addressed by Wallis and North, is 'which people?' It is not only the transaction costs of the market that come into play, but also the transaction costs within an organisation, especially of a collective organisation: the costs of managing implicit contracts between a range of diverse stakeholders and reconciling competing objectives.

## **Entrepreneurism**

It is because of this complexity that other insights from the field of business management also matter. To reduce a wide field of study to brief concepts, it is the way that an organisation identifies market opportunities, and applies resources, expertise and leadership that determine its performance. Institutional innovation:

'.. means novelty, new things being done, or old things being done in new ways. This presupposes opportunities, vision, risk-taking and resources. These values must be shared by organisations and their staff, and both must be entrepreneurial. Entrepreneurial organisations have particular characteristics in terms of culture and personnel. There must be a fit between culture, structure, resources and the tasks... Managers must be 'intrapreneurs' (Wickham, P. A.

2006): entrepreneurial managers who work within the confines of a mature organisation, but with vision, embracing novelty and risk-taking' (Poole, N. D. and Penrose Buckley, C. 2006: 55-6).

The roles of management in a commercial agrifood firm are to:

- Identify market opportunities for agricultural products, raw or transformed
- Attract and manage the human and financial resources necessary to access these markets
- Lead and direct the organisation as a whole, and manage wider stakeholder relationships

To be succinct, contemporary commercial organisations need to be entrepreneurial. This is a characteristic not commonly associated with the traditional cooperative.

Entrepreneurism needs to be inbuilt, and conflicts with collective governance structures: vision and risk-taking are unlikely to be present within bureaucratic structures, which characterise many forms of collective enterprise. Governance structures often curtail management freedom. Equally, the necessary internal skills and resources are often not present in rural grassroots organisations. This suggests a long and steep learning curve for many collective forms of smallholder farmers.

### **Building organisations**

There is no one model or set of key success factors for successful organisational development, but success depends on 'organisational fit' (Korten, D. C. 1980). 'Fit' is a concept widely recognised in the management literature, which has been used in analysis of the agrifood sector<sup>1</sup>. 'Organisational fit' in rural development, Korten argued, is the extent to which program design, beneficiary needs and the capacities of the assisting organisation are productively aligned. Essentially, key variables are the task, the context, and the organisation. 'Fit' can be conceived as a function of:

- the organisation membership
    - need and effective demand for services
    - participation in organisation management
  - the organisation itself
- 

<sup>1</sup> See, for example, García Martínez, M. and Poole, N.D. (2004). Analysing linkages between strategy, performance, management structure and culture in the Spanish fresh produce industry. *International Food and Agribusiness Management Review*, **7**(4): 16-39.

- governance structures, de jure and de facto
- management skills and capacity
- the services provided by the organisation
  - complexity of the mix of services necessary to meet objectives
  - service delivery systems

The concept of 'fit' can be applied not only at the level of the membership and the management of the organisation, but also between a grassroots form of organisation or association, higher 'tiers' of organisation that are common in cooperatives, and the supporting organisations that are commonly found in the agrifood sector of developing countries. These are the commercial partners, NGOs and other supporting organisations, donors, and the public sector organisations – all stakeholders within the complex of the market system.

Korten (1980) also addressed organisational development and suggested three stages that may underlie successful capacity building. Organisational performance and development are more or less successful, according to the way that the tasks, and the organisation itself, develop within a particular context. This he called the 'learning process' approach. He envisaged three stages in the learning process, during which organisations first learn to be effective (a time of investment in knowledge and capacity building); then efficient (reducing the input requirements in relation to outputs - or services – delivered); and lastly to expand (growth to maturity). Regarding expansion, optimal organisation size for a particular context – of people, products, services, and environment – may vary, and the advantages and disadvantages of scale must be specifically considered. Efficient scale may apply to a range of organisation sizes, and may also change with the wider environment, technology and political processes. Once again, there is no single model or blueprint for optimal size and development pathways.

### *2.2.8 Organisational structure, environment and culture*

There is an enormous literature on organisational management and cooperation from which to derive a framework for understanding the characteristics of collective farmer groups. From the management literature, such as Handy, and many reviews and summaries such as Chirwa *et al* (2005), Berdegúe, Biénabe and Peppelenbos (2008), and Markelova, Meinzen-Dick, Hellin and Dohrn (2009), the following features of group management are known to be important for farmer associations:

#### **Group characteristics**

- Origin – self- or externally initiated
- Coherence with (pre-) existing organisations and culture

- Size – number of members
- Composition – homo-/heterogeneity in respect of social and economic characteristics
- Internal governance – representation, transparency and accountability
- Leadership style – participation or hierarchy and elitism
- Management skills – training and professionalism
- Capital investment – fixed physical and other assets, including intangibles
- Motivation and objectives – focus, complexity and boundaries
- Formalisation – constitution, registration, federation/integrative structures

On these, there is no absolute guidance about what does and what does not work, but under varying circumstances, different blends of characteristics can enhance or impair group performance.

### **External environment**

From the NIE perspective, organisations are shaped, by, and through advocacy also shape, the external environment, that may be more or less favourable. These ideas are developed in subsequent sections on actual cases of farmers associations but it is sufficient here to highlight the importance of a range of institutional and organisational factors in the environment external to the actual farmer association:

- Supporting relationships and organisations – public/private/NGO sector facilitation
- Political environment – dis- or enabling legal and cultural framework
- Communication and logistics infrastructure

There is no doubt about the importance of a propitious facilitating environment and good physical and other infrastructure as a foundation for good performance.

### **What product?**

Finally, for farmer organisations there is another set of factors affecting an organisation's operations, which are the technoeconomic characteristics of products and/or services:

- Complexity of service provision – range of inputs/products or services
- Bulk and value/value-added of inputs/products or services
- Quality characteristics, standards and differentiation
- Processing and manufacturing opportunities
- Market type and distance – local/domestic, national/urban and export

The literature provides pointers to technoeconomic characteristics that are conducive to good performance of agricultural organisations, such as high value products and markets rather than bulk commodities which can cover the transaction costs of organisation, but

again there is no absolute guidance about what does and what does not work (Hellin, J., Lundy, M. and Meijer, M. 2009).

## **2.3 Key insights**

The theory introduced here suggests many hypotheses about farmer organisations concerning which the review sections that follow will tend to endorse. Significant points among these which raise transaction costs and constrain management performance are:

- Behavioural assumptions: within collective forms of social and economic organisation there will be complex and often conflicting incentive structures that will tend to impair organisational efficiency and effectiveness
- Limited and asymmetric information: within organisations and between different market players available, high levels of uncertainty are characteristic about stakeholder behaviour, institutions such as laws and the policy environment; and specific agribusiness features such as product market requirements, quality assurance, traceability and certification
- Management skills: generally these are inadequate to manage complex structures; agency problems are common, and the lack of entrepreneurship limits strategic vision
- Asset specificity: investment is a requirement: for capacity building, resources are often available; for necessary physical capital and public goods, there are significant internal and external financial constraints
- Repeat dealing: clientisation is important for building a market presence, interfirm relationships, skills and reputation; these learning processes take time, often more time, and an ability to absorb mistakes and losses, than is widely understood and accepted
- Donor fads and fancies: imposition from external agencies of dominant, yet changing development paradigms ignores the need for 'fit' and patience in organisational learning.

## **2.4 Synthesising a framework**

Among the possible approaches to consider collective forms of linking smallholder farmers in Africa to new market opportunities, transaction cost concepts are widely used to explain the phenomena – or obstacles – to successful exchange. Transaction cost economics also provides insights into the successful management of internal complexities of collective organisations. In addition, the field of business management, or more precisely, entrepreneurship, adds a sharp challenge to the analysis of organisations that attempt to engage in increasingly sophisticated and competitive markets. The management issues underlying the growth and development of successful collective enterprises will also inform the following discussion of linking smallholder

farmers to markets, and of the institutional innovation that may be necessary to drive existing forms of association towards more effective market linkages that contribute to the overall agenda of reducing rural poverty.

Drawing on the renewed interest in New Institutional Economics, two key concepts in the reappraisal of agricultural marketing intervention approaches policies are 'institutions' and 'organisations'. A simple typology of initiatives to address market failures and imperfections can be envisaged and represented in a matrix framework:

#### *2.4.1 Institutional interventions*

As noted, institutions are the rules of the game, humanly devised constraints that shape human interaction and structure incentives in human exchange - they reduce uncertainty by establishing a stable structure to human interaction (North, D. C. 1990). Institutional change shapes the way societies evolve through time, define and create, expand and limit the set of choices of individuals. Such institutions can be formal or informal, created or evolving, written and unwritten. They include mechanisms for monitoring commercial arrangements, enforcing contracts and ascertaining and punishing violations.

Institutional innovations could be the formalisation of contracts between sellers and buyers of agricultural produce in order to reduce the uncertainty caused by low levels of trust and limited possibilities of redress, which is the situation which obtains in much of Sub-Saharan Africa (Poole, N. D., Seini, A. W. and Heh, V. 2003). Also in Ghana, improved use of intellectual property rights legislation should help develop innovative and productive activities across an range of markets in which small firms engage (Sey, A., Lowe, B. and Poole, N. D. 2010 forthcoming). Another type of intervention suggested is the need for an independent audit body for monitoring and improving the performance of farmer organisations in Malawi (Kachule, R., Poole, N. D. and Dorward, A. 2005). An innovation such as a professional and independent regional or national ombudsman for auditing grassroots associations could help both performance and accountability.

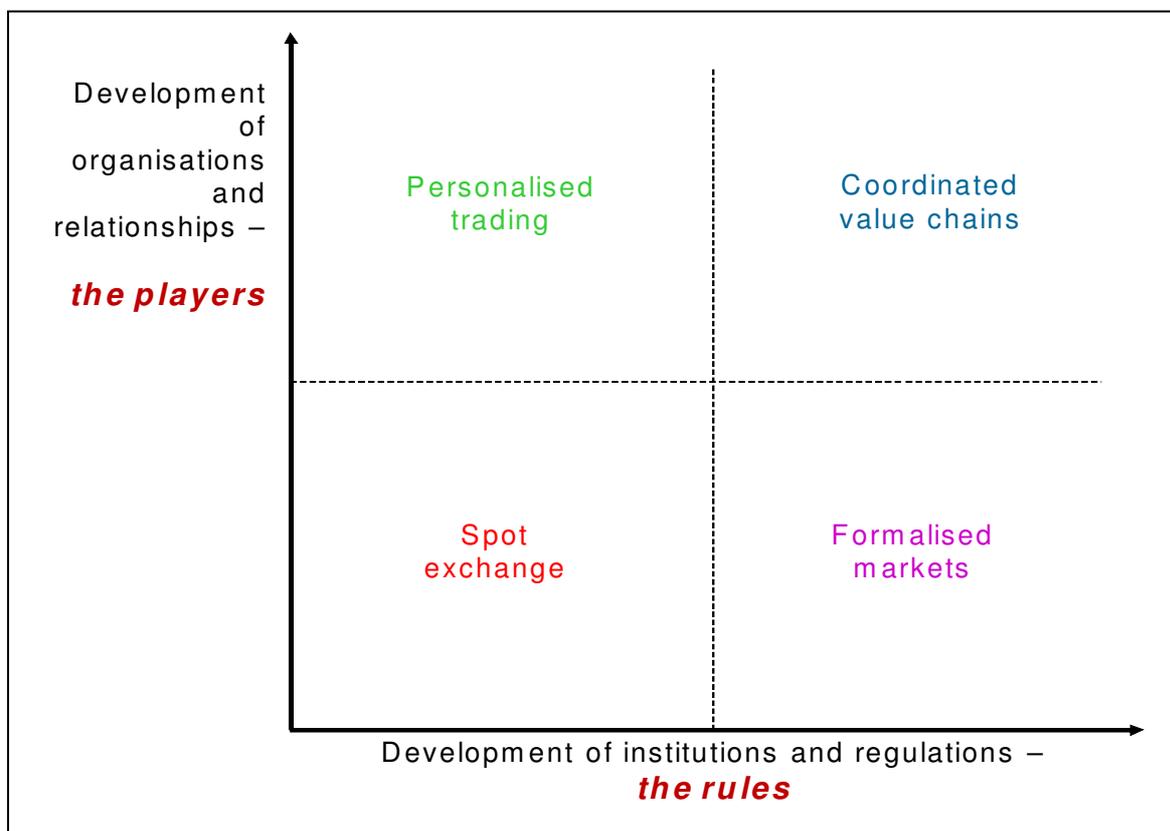
#### *2.4.2 Organisational interventions*

Like institutions, organisations provide a structure to human interaction - but they are the players of the game rather than the rules (North, D. C. 1990). They are political, economic, social, educational bodies: public and private sector and civil society organisations, and groups of individuals bound by some common purpose to achieve joint objectives. They are influenced by the institutional framework and in turn, influence institutions, for example, through the advocacy common among collective organisations, and lobbying of private sector and other interest groups. In subsequent sections, cases

of cooperative development are presented that demonstrate organisational innovation to improve governance, enhance market orientation and facilitate capital raising.

The interplay of organisations (players) and institutions (rules) can be depicted as giving rise to a simple typology of market exchange (Figure 1a). Interventions can be primarily of the organisational type, or can be attempts to change the institutional framework within which farmers and organisations operate. Most historical and current policies for the development of markets and to increase smallholder access will embrace elements of both approaches. The respective policy interventions (and commercial initiatives) suggest how different types of market exchange might result from different (external) interventions or (private) initiatives.

**Figure 1a Interventions, initiatives and market types**

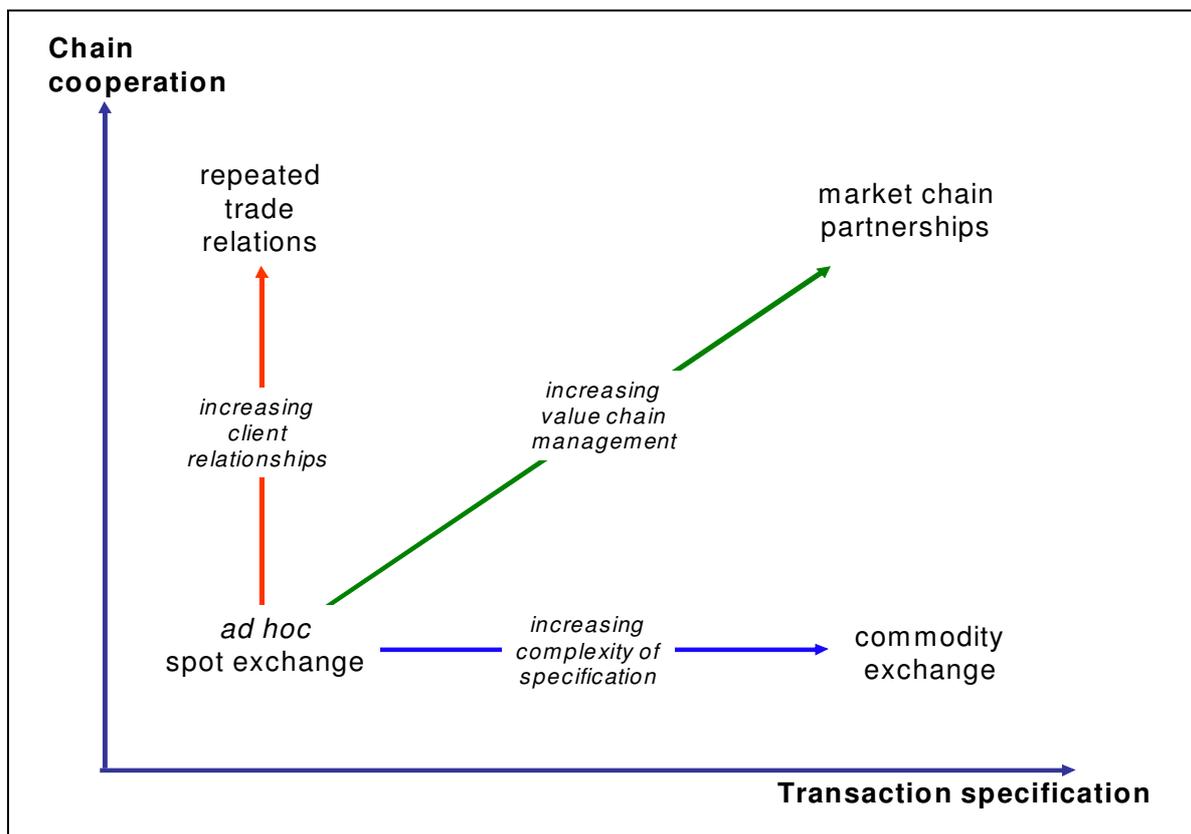


Agri-food markets are becoming more complex and demanding. As the proportion of agribusiness transacted in spot markets declines, organisational and institutional innovations are necessary in order to mitigate the uncertainties arising through more complex contractual arrangements. That is to say, for smallholders and their associations to move from upwards and to the right from the bottom left quadrant requires investments in institutional and organisational development.

The model suggests clues as to the sort of approaches to developing different markets and sectors in developing countries. Cooperation can take various forms: either collaboration institutionalised within voluntary organisations, or through the framework of formal institutions and regulations, or through informal institutions (eg inter-personal and inter-firm relationships).

Such cooperation between sellers and buyers is a fundamental means to reduce transaction costs, and opens up possibilities of value chain management – eg improved production and marketing specifications, and sharing of skills, information and investment - that can also lead to better intra-firm management. Such a dynamic can be depicted by adapting the model to show how increasing cooperation and information sharing shifts the interfirm relationship towards more effective market coordination and higher level participation in the chain of value from supplier to consumer (Figure 1b).

**Figure 1b Trajectories of increasing cooperation and coordination**



### 3 *A long view of agricultural cooperation*

#### **3.1 History and evolution of collective organisations**

From the earliest times there has been a distinction between the cooperative 'movement' which was rooted in historical socio-political conditions, and the cooperative as a business enterprise. The economic and social dilemma, and an anticompetitive dimension posed by the dual nature of collective organisation and enterprise, were captured by an early critic who commented that 'a farmer-owned, farmer-controlled cooperative [is] a legal, practical means by which a group of self-selected, selfish capitalists seek to improve their individual economic positions in a competitive society' (Babcock, H. E. 1935: 153).

The current state of farmer associations in Eastern and Southern Africa has much to do with the Nineteenth Century of models of collective economic organisation, of the prevailing policies of donor organisations, and the political economy of specific countries and regions. The next section will trace the historical and political background.

##### *3.1.1 Origins and principles of collective enterprise*

It was before the 13th Century, in France and Switzerland, that the milk producers of Gruyère and Emmenthal formed farmer cooperatives with specific economic objectives: to pool the milk from several herds and thereby accumulate sufficient liquid milk to make cheese. The benefits from large scale enterprise were shared among the members of the group in proportion to their use of its services.

Most modern cooperatives trace their heritage to the Industrial Revolution. In the UK the first attempts to set up cooperatives date from the late eighteenth century. They were workers' consumer cooperatives and some went so far as to have an organisational structure: members' meetings, an elected management committee, and a distribution of profit among the members. Their success was short-lived, however, because of structural problems that are persistent – or permanent - weaknesses: they lacked capital and ran up debts; they lacked management expertise; and they were opposed by other economic and class interests.

The 'Rochdale Equitable Pioneers' was the first true cooperative formed in 1844 in the northern UK town of Rochdale. A group of poor cotton weavers pooled resources and set up a shop selling staple foods. Soon the cooperative membership was opened to all customers who became shareholders with democratic decision-making rights. The principles set out by the Rochdale Society in 1844 have influenced the way in which

cooperatives have been managed throughout the world ever since. Frederick Raiffeisen set up the first agricultural cooperatives in conformity with the 'Rochdale Principles' in Germany in 1849. He emphasised the role of the savings and loan function of the cooperative to achieve financial independence from usurious moneylenders and added a principle of collective financial responsibility. The first laws on cooperatives were promulgated in the UK in 1852 followed by Prussia in 1867, in order to formalise existing practice that followed the Rochdale and Raiffeisen 'Principles'. The Rochdale Principles, adopted by the International Co-operative Alliance (ICA) in 1937, were updated in 1995, and broadly underlie most forms of association of smallholder farmers (Box 2).

## **Box 2 Cooperative principles and identity**

- **Voluntary and Open Membership:** Co-operatives are voluntary organisations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political or religious discrimination.
- **Democratic Member Control:** Co-operatives are democratic organisations controlled by their members, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. In primary co-operatives, members have equal voting rights (one member, one vote) and co-operatives at other levels are also organised in a democratic manner.
- **Member Economic Participation:** Members contribute equitably to, and democratically control, the capital of their co-operative. At least part of that capital is usually the common property of the co-operative. Members usually receive limited compensation, if any, on capital subscribed as a condition of membership. Members allocate surpluses for any or all of the following purposes: developing their co-operative, possibly by setting up reserves, part of which at least would be indivisible; benefiting members in proportion to their transactions with the co-operative; and supporting other activities approved by the membership.
- **Autonomy and Independence:** Co-operatives are autonomous, self-help organisations controlled by their members. If they enter to agreements with other organisations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their co-operative autonomy.
- **Education, Training and Information:** Co-operatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their co-operatives. They inform the general public - particularly young people and opinion leaders - about the nature and benefits of co-operation.
- **Co-operation among Co-operatives:** Co-operatives serve their members most effectively and strengthen the co-operative movement by working together through local, national, regional and international structures.
- **Concern for Community:** Co-operatives work for the sustainable development of their communities through policies approved by their members.

Source: <http://www.ica.coop/coop/principles.html>. Accessed 15 December 2009

According to the ICA a cooperative is an association of persons united voluntarily to meet common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise. The core values of cooperatives are self-help, self-responsibility, democracy, equality, equity and solidarity.

### 3.1.2 *The spread of collective organisation and enterprise*

As the cooperative ideal spread in Europe the initiative was generally of well-meaning private citizens. The sector developed in Africa mostly as the result of intervention by colonial administrations. Kenya's first cooperative was founded in 1908 (Box 3). The first cooperative in Uganda was a growers' association in 1913. Although quickly abandoned, it paved the way for the Buganda Growers' Association founded in 1923 and later the Uganda Growers' Cooperative Union in 1933 (Young, C., Sherman, N. P. and Rose, T. H. 1981: 58). In the Belgian Congo, cooperatives emerged in the 1920s. In South Africa also in the 1920s, cooperatives were introduced to promote the interests white farmers, and exercise control of prices through agricultural marketing boards (Develtere, P., Pollet, I. and Wanyama, F. 2008: 11). Box 3 outlines the varied origins and forms of models of collective enterprise and associated organisational features in Africa.

#### **Box 3 Models of collective enterprise in Africa**

- The unified cooperative model: rooted in the British colonial administration and aimed at developing a single cooperative movement. The structure comprises levels with primary cooperatives at the base, followed by secondary regional societies, federations and unions and an apex organisation at the highest level.
- The social economy tradition: defined by the shared social and economic objectives of members. Developed generally in Francophone and Hispanic countries, this cooperative model can take the form of mutual societies, associations, foundations and trusts.
- The social movement tradition: based primarily on collective action and is embedded in the Belgian tradition of cooperative organisation. The cooperative is viewed by members as a social movement that may encompass women's groups, farmer organisations, trade unions etc. The model has been an influence in the development of cooperatives in Central Africa.
- The producers' tradition: viewed primarily as a functional organisation enabling farmers to participate more effectively in markets, thereby improving their capacity to achieve social objectives. This model stems from a Portuguese tradition of cooperative organisation.
- The indigenous tradition: unlike the preceding four is rooted in endogenous organisation. These forms of organisation are to be found in countries with a limited colonial history, such as Ethiopia, Liberia, Egypt and Sierra Leone. Indigenous models are based within local frameworks of understanding and respond to local socio-economic challenges.

Source: adapted from Develtere *et al* (2008)

Among the early cooperatives that also emerged from the colonial authorities were those aimed at lifting the peasant farmer out of subsistence, and modernizing the agricultural sector. Young *et al* (1981) identified the introduction of cash crops in British-ruled Africa such as sugar, cocoa, cotton and coffee as a principal stimulus for the creation of cooperatives in order to counteract the disadvantages of trade felt by the peasant farmers. In the cases where cooperatives were a private initiative, for example in East Africa, often the impetus came from emerging (African) private traders who wished to challenge the supremacy of the existing (Asian) traders, in order to promote their own advantage rather than that of community association.

#### **Box 4 History of co-operatives in Kenya**

'The first Kenya's Co-operative Society [sic], Lumbwa Co-operative Society, was formed in 1908 by the European Farmers with the main objective of purchasing fertilizer, chemicals, seeds and other farm input and then market their produce to take advantage of economies of scale. In 1930, Kenya Farmers Association was registered as a Co-operative Society to take over the role of supply of farm input played by Lumbwa Co-operative Society. The African smallholder farmers fought for formation of their own Cooperatives and later in 1950's they were allowed to promote and register Co-operatives for cash crops like coffee and pyrethrum. Consequently at independence in 1963, there were 1,030 Co-operative Societies with 655 being active with a total membership of 355,000...'

Source: <http://www.scccportal.org/Default.aspx?ID=827&M=News&NewsID=1934&PID=69>.  
Accessed 18 December 2009

The kind of cooperative inherited by the newly independent developing country governments in the 1950s and 1960s was generally an organisation instituted to promote the interests of its members as perceived by outside agencies. Cooperation was seen by the new governments as an institutional vehicle to replace the foreign trading interests, some of whom withdrew at independence, others of whom wielded too much economic power. The existing cooperative enterprises also could be used to meet the political, social and economic problems and challenges, particularly in relation to rural development.

### **3.2 The political economy of agricultural collective organisation**

#### *3.2.1 Political subversion of collective organisation and enterprise*

Cooperatives were also been seen as a form of social organisation aimed at unifying interests, which often were political. In Tanzania, grassroots cooperatives were encouraged prior to independence and after, resulting in them gaining considerable political strength, so much so, that the government abolished cooperatives in 1976,

replacing them with parastatal crop authorities. The resulting drop in agricultural production over the next 5 years resulted in their re-establishment in 1982 (Lele, U. and Christiansen, R. E. 1989: 18).

Socialist states elsewhere adopted cooperatives as a form of social organisation and political control, as well as economic organisation. For example, after independence in Mozambique, the Third Congress of FRELIMO in 1977 released a report noting that 'The co-operative movement, under the leadership of the Party, constitutes a huge mobilisation of the great masses of peasants for the organised, conscious and planned participation in the socialist development of the whole country' (Harris, L. 1980). Such ideals have been reformed as a consequence of the liberalising tendencies during the latter part of the Twentieth Century (Lamont, J. T. J. 1993; Spooner, N. 1994 ).

### *3.2.2 Models of 'statutory' association*

It had been hoped that the early marketing cooperatives might increase the bargaining power of producers. The experience proved to be unsatisfactory. 'Free-riding' was one reason: when fruit producers' cooperatives in Canada and Australia tried to store part of the crop in order to market it later in the year they found that non-members profited most from any rise in price - temporal arbitrage; so-called free-riders were able to sell their produce without bearing any of the cost of storage. Non-members also benefited from the efforts of cooperatives in opening up distant markets without bearing the costs of membership. It was the failure of cooperatives to secure the economic position of producers in a time of severe agricultural depression which led to the introduction of statutory - legal - marketing powers: some sort of government intervention was necessary to secure the cooperation of non-members and thereby market the whole crop. Thus compulsion replaced the voluntary cooperation of the Rochdale Principles as a new policy instrument to achieve similar objectives.

State marketing boards were set up in many countries under British colonial influence, and were also represented in the Francophone world by *Caisses de Stabilisation*. Marketing organisation became of increasing importance during World War II. West African oil palm produce and groundnut marketing were brought under government control in 1942. The Cocoa Control Board was renamed the West African Produce Control Board, (WAPCB), with jurisdiction over Nigeria, Ghana, Sierra Leone and the Gambia. According to Abbott and Creupelandt (Abbott, J. and Creupelandt, H. 1966), the objectives were:

- obtaining funds for sales promotion, research and extension;
- raising the bargaining power of agricultural producers on domestic/export markets;

- improving marketing organisation and methods by regulating quality and packing standards, market procedures, sales practices, by raising the scale of operation and setting up needed marketing and processing facilities, and facilitating a more precise adjustment of the quantities and types of produce sold on particular markets;
- equalising returns from sales to different price markets or outlets;
- sheltering producers and consumers against the impact of sharply fluctuating internal and external prices.

### *3.2.3 Donor support for state intervention*

The expansion of state marketing in the post-colonial and independence period could not have been undertaken without the provision of aid from bilateral and multilateral donors, whose investment policies constituted an endorsement of such a strategy. Marketing boards were a convenient counterpart agency for aid donors whose programmes of food aid, infrastructural investment and rural development projects were increasing in importance. A common typology for classifying the services and objectives of such marketing boards was that proposed by Abbott and Creupelandt and reflects an era of strong market intervention (1966):

- advisory and promotional activities directed towards producers
- regulation and control of production and of marketing activities
- non-trading price stabilisation
- price stabilisation through trading
- monopoly export marketing
- monopoly domestic marketing

In six African countries, between 1970 and 1987 the value of external assistance constituted between 35% and 70% of government expenditures (Lele, U. and Christiansen, R. E. 1989). In Tanzania by the end of the 1970s nearly 400 parastatals handled production, processing, transport and marketing of goods and services, and the prices of nearly 1000 commodities were controlled. A 1988 World Bank report documented that over the period 1974-1985, Sub-Saharan Africa received more World Bank support than Asia and Latin America, involving some 48 food crop projects, 45 export crop projects and 17 livestock projects that had some marketing components, with significant intervention through collective marketing organisations. The donor perspective was influenced by the following factors within the policy environment:

- parastatal projects were easy to appraise
- for monopoly organisations there was no alternative
- the recipient government was supportive
- ease of project management – marketing organisations were discrete entities

- policy support for taxation of agriculture to mobilise public-sector revenues

The Francophone Sahelian also states all intervened on a massive scale with similar objectives. In general, the development of market organisations was dependent upon, or reflected, the economic and political history not just of the individual country, but also of the broader context: where export crops were involved, a country's trading partners was a factor which contributed towards the nature of domestic 'institutional' development. Access to markets was facilitated by the close industrial relationships with major private sector buyers, foreshadowing the supply chain linkages with international manufacturers and distributors that drive contemporary agrifood markets.

On the whole the picture given in the literature about the performance of state-managed marketing is a gloomy one. Marketing boards were weak organisations which achieved little success, with multiple, unrealistic and conflicting objectives. And in general, food crop or domestic marketing boards faced more problems and were less likely to succeed in their objectives than those concerned with the export of high value agricultural products (Arhin, K., Hesp, P. and van der Laan, L. 1985). Poor, local producers were affected most by the systemic failure. This differentiation – or inequity –between the beneficiaries of statutory marketing and those excluded from market opportunities was a structural characteristic that has been replicated latterly in supply chains to non-traditional, high value domestic and export markets (Reardon, T., Timmer, C. P., Barrett, C. B. and Berdegué, J. 2003; García Martínez, M. and Poole, N. D. 2004).

What is generally absent in developing economies is the coordinating activity of industry bodies, and role which marketing boards could still play. An example from Spain demonstrates how 'interprofessional' organisations unite sector stakeholders (Box 5).

#### **Box 5 'Interprofessional' or umbrella organisations**

The *Interprofesional Citrícola Española*, or Intercitrus, was formed in 1993 after years of strife within the citrus sector. It is constituted as a form of association under the cooperative Law 19/1977. Intercitrus is based on the French '*interprofessionale*' model and combines all parties in the industry: farmer organisations and the cooperative sector; independent traders and exporters; and the citrus processing industry. The operative principles of Intercitrus are to represent the interests of the sector as a whole - for example, by lobbying; equality in representation between the constituent subsectors; unanimity in decision making. As an institutional mechanism for introducing 'orderly marketing', there is a similarity between the '*interprofessionale*' and the marketing boards of the UK and elsewhere.

Source: authors

### **3.3 Better marketing: public intervention or private initiative?**

The potential for a response from the private sector to economic incentives and opportunities should have created a sense of optimism in creating efficient and competitive markets, and overcoming the livelihood constraints of poor producers and traders. The propensity of many African peoples to engage in trade should have been a sound foundation for market-led economic growth. However, the results of market liberalisation were disappointing. The radical reduction in state intervention and not-infrequent collapse of organised marketing systems did not stimulate a strong private sector response, nor generate higher levels of competition. As traders have not been willing or able to fill the void, farmers were left without market outlets. Most farmers without commercial knowledge or experience have been unable to engage successfully in marketing their produce on their own account. The weak development of many poor economies, both in historical developing regions and in so-called 'transition' economies led to greater pragmatism among donors and international organisations, a move towards empiricism and away from political and economic dogma. Market coordination has to some extent supplanted the ideology of pure competition.

Much is still not understood about the impact of fluctuating policies. Some negative underlying assumptions about the role of private traders persist and shape the willingness to involve private enterprise in market development (KIT and IIRR 2008). The literature also records perverse results of liberalisation: for example, in Southern Africa price deregulation has led not to the expected efficiency effects but to increases in market margins (Traub, L. N. and Jayne, T. S. 2008). Overall, there is considerable ambivalence concerning 'state withdrawal' and the persisting unpredictability of intervention (Jayne, T., Govereh, M., Mwanamo, A., Nyoro, J. and Chapoto, A. 2002). An unstable institutional environment is one of the principal factors why the private sector may choose to avoid engagement with agricultural marketing.

## Box 6 Summarising characteristics and limitations of collective organisations

Common characteristics?

- Too many complex functions and objectives
- management and decision making remote from membership control
- 'élite capture' for the benefit of the few rich and powerful farmers and politicians
- subject to direct government interference in management
- inadequate finance and excessive operational costs
- weak management and capacity building
- sensitivity to patterns of social organisation and cultural differences
- less success with food crops that are bulky and of low value, and crops that require complicated and expensive processing
- important role in input supply, especially where low margins discourage private traders and where adulteration of inputs is prevalent
- potential stimulus to competition with private sector enterprises

Limited expectations?

- Cooperatives cannot be expected to surmount external constraints in the macro policy environment, pricing policies, lack of forex, inadequate infrastructure, and poor regulatory functions. They are not an intermediate instrument for the management of marketing by the government
- Any form of grassroots organisation is likely to need support as it engages in activities that have been hitherto outside its experience. The assumption of new responsibilities requires training and education, and skills often absent among the membership
- Is 'associative enterprise' a movement, or an alternative form of business organisation?

Source: authors

### 3.4 Supporting collective organisation?

Intervention in agricultural markets has not generally worked in Africa. It is curious, nevertheless, that in some advanced agricultural economies, statutory intervention has been retained throughout an era of intense economic liberalisation (Box 7).

#### Box 7 Meat and Wool New Zealand

Meat & Wool New Zealand (M&WNZ) is incorporated under the Companies Act 1993, and is a membership organisation with voting rights proportionate to livestock holdings. It receives statutory levies from members paid on all livestock slaughtered and all wool sold. M&WNZ aims to improve farm profitability through investing levies in research, development and extension, market access and development, and human resources, working across a wide portfolio of business activities where collective organisation can achieve what farmers cannot individually achieve. Farmers periodically consent to the levy: in August 2009 they voted to continue paying levies on sheepmeat and beef (but against continuation of the goatmeat and wool levy). Source: <http://www.meatnz.co.nz/main.cfm>. Accessed 22 December 2009

The deepening depression over poverty reduction and rural development in poor countries and the formalisation of the Millennium Development Goals at the turn of the century has led to a reappraisal of policy approaches and instruments to hitherto intractable problems. International donors and NGOs have re-engaged with the rural sector in general and agricultural development in particular. More widely, the limits of liberal policies are being drawn in by increasing policy intervention – the ‘post-Washington Consensus’ - such as the return to input subsidies in Malawi, and the spread of conditional cash transfer payments (CCTs) as a measure to promote an inclusive social policy and longer term institutional development (Bastagli, F. 2009). The latter is true not just in Latin America but also, for example, of the Social Cash Transfer (SCT) programme in Zambia<sup>2</sup>.

Collective organisation has re-emerged as a development theme, not to support agricultural élites, and not just for agricultural development but for growth, poverty reduction and environmental management more generally (World Bank 2008): ‘Civil society empowerment, particularly of producer organizations, is essential to improve governance at all levels...’ (p. 2); performance and competitiveness are key words, and operationally producer organisations are said to be constrained by ‘legal restrictions, low managerial capacity, élite capture, exclusion of the poor, and failure to be recognized as full partners by the state’ (p. 14). Farmer organisations continue to offer a way for smallholder farmers to reduce transaction costs and overcome barriers to market participation by raising their bargaining power with traders and wholesalers (Thorp, R., Stewart, F. and Heyer, A. 2005). Further benefits of collective action include greater accessibility of finance, technology and market information (Markelova, H., Meinzen-Dick, R., Hellin, J. et al. 2009) With respect to cooperatives, Cook and Chaddad explain that the role of a cooperative for a individual producer had been to improve farmer returns by

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<sup>2</sup> ‘Social cash transfers (SCTs) have become increasingly popular in Sub-Saharan Africa, because growth-centred development policies have failed to reduce poverty. SCTs support the consumption of the poorest, and allow them to invest in human and other forms of capital that reduce the intergenerational transmission of poverty... SCTs are effective tools of basic social protection. As with most things, however, a one-size-fits-all approach is inappropriate. Expectations about impact need to be moulded by programme design and initial conditions, and vice versa’ Tembo, G. and Freeland, N. (2009). Social Cash Transfers in Zambia: What Is Their Impact? One Pager. Brasilia.

lowering production and transaction costs (...) counterbalancing the negative economic impacts of market power and reducing producer income risks' (Cook, M. L. and Chaddad, F. R. 2004: 1251). From a policy perspective, facilitating collective action among smallholder farmers can result in increased agricultural production as well as adding value through processing.

Specifically they are linked to market access and reduction of transaction costs, gaining economic scale and market power, formation of social capital, gender inequalities, provision of technical assistance and input services, and a techno-economic 'leader' role, and advocacy. A key issue is the provision of resources and strengthening organisational capacity, while avoiding dependence. But there is also recognition of the change in context and the external market conditions: '... the world of value chains and global market forces is creating new challenges for their organizations. The challenge for the organizations is how to respond; for governments and donors it is how to assist without undermining the organizations' autonomy' (World Bank 2008: 154).

Recognising the vacuum left by the withdrawal of the state from agriculture in many developing regions, a role is once again envisaged for organisations that retain some of the attributes of marketing boards with statutory powers, including levies, particularly for product research and development, and international marketing. 'Widely adopted in industrial countries, such levies have been underused in developing countries, despite their potential to resolve underinvestment and improve the demand orientation and effectiveness of research' (World Bank 2008). Local organisations can also be a vehicle for increasing investment among smallholders in technology and other productive assets (Barrett, C. B. 2008).

While such observations are realistic for many contexts, they remain the observations – or wish list – predominantly of external players, made within a given set of external conditions and from a given political and philosophical viewpoint. While the concepts are likely to have relevance, it is difficult not to interpret such initiatives as rolling back liberal economic approaches by a few decades. Institutional innovations in advanced economies are addressing specific weaknesses of farmer organisations, notably weak management and under-capitalisation. Many organisations in Africa are also exhibiting characteristics that depart somewhat from the structure and objectives common to traditional cooperatives. Examples of these will be discussed later.

### **3.5 A wider perspective: business services, chains and networks**

The policy climate for developing countries has evolved substantially since the reforms of the 1980s and 1990s. Newer policies have encouraged the provision of business development services to stimulate the private sector became a focus of interventions. Recently, considerable attention has been attached to improving the performance of the wider business environment (White, S. 2005). Latterly NGOs have become a significant channel for linking poor people to markets. The entry of individual and corporate 'philanthrocapitalists' (eg the Gates-Rockefeller Alliance AGRA see <http://www.agra-alliance.org/>) as donors has added a further dimension to the political economy of poverty reduction through market liberalism. The concept of BDS itself has evolved into newer formats (Hitchins, R., Elliott, D. and Gibson, A. 2005; Chartock, A. 2006). 'Making markets work for the poor' (MMW4P) (Ferrand, D., Gibson, A. and Scott, H. 2004; Meyer 2006) is an approach adopted by various bilateral and multilateral agencies which stresses the process of creating opportunities through increasing access to markets, achieving equitable and remunerative prices for goods and services, and reducing risk. A critical appraisal is appropriate: while MMW4P envisages commercial interventions and is 'pro-competitive structures', it is weak in the policy dimension and draws back from advocating innovative public policy interventions (Poole, N. D. 2009). Linkages of enterprise concepts to movements advocating collective organisation are also weak.

Development practitioners have also drawn on the value chain approaches more commonly used in advanced economies and international commodity exports to analyse and improve the performance of market systems. The emergence of value chain analysis as an analytical framework is traced to the work of Gereffi (1994; Bair, J. 2005; Donovan, J. and Poole, N. D. 2008), and represents a private enterprise perspective on the inclusion of producers in market activities. The ability of farmers, for example, to add value requires 'upgrading' skills, product development, business processes, and through investing in physical capital formation. From a development perspective, 'upgrading' - often with associated capital requirements - is especially important and a range of activities for which farmer associations are an appropriate vehicle. As with MMW4P approaches, value chain analysis has to be translated into action by taking into account the wider stakeholder context: an inclusive 'task-force', such as that used in the development of the cassava sector in Zambia, is necessary to effect policies for a specific sector, in what may be an ongoing process rather than a one-off 'intervention' (Chitundu, M., Droppelmann, K. and Haggblade, S. 2009).

Another current 'action research' approach to improving smallholder inclusion in commercial markets is the participatory market chain assessment model, PMCA, (Bernet,

T., Thiele, G. and Zschocke, T. 2006). Developed by CIP in South America among indigenous potato growers, it purports to be a sectoral initiative, and has been applied in Africa, also among Ugandan root crop growers and other vegetable sectors (Horton, D. 2008). Through these policy approaches runs an increasing focus on poverty reduction through establishing sectoral linkages between private enterprise and the rural poor. It is a process that is inclusive of all stakeholders, but intensive and costly in application, and once again limited in its 'replicability' and 'scaleability'. Nevertheless, the trend in participative and inclusive approaches to market development interventions focused on the poorest addresses a critical need for new policies that include farmers' voices – at least in Zambia (Concern Worldwide 2008).

Among the most innovative forms of intervention are in fact market developments that arise not from the donor and (I)NGO community but from private sector initiatives. These are both commercial enterprises developing supply chain relationships such as in high value horticultural produce from Kenya (Jaffee, S. 2003), ensuring procurement of certified produce such as to meet demand in the fair trade and organic sectors, and the new phenomenon of philanthrocapitalists who may invest equity in local production systems. Innovation in equity finance of market-oriented agribusiness initiatives is a means not only of overcoming capital shortages in rural enterprises. Exercise of financial leverage may be a mechanism whereby investors can build the necessary management capacity (Poole, N. D. and Penrose Buckley, C. 2006). This is one of the critical areas where collective organisations such as farmer associations generally have unexploited potential. New models of cooperative organisation and management in advanced economies are probably the most innovative form of collective enterprise in the global agricultural economy.

### **3.6 The new models of cooperation**

Sound financial management, good organisational governance and the potential for free riding, remain problems for the more complex cooperatives. Prowse (2008) contends that while there are opportunities to be taken advantage of by producer organisations there is a danger of expecting too much from them. This point is also made by Bernard and Spielman, *inter alia* (2009). Prowse points out that the World Development Report 2008 argues that in order for producer organisations to succeed in contract farming they need to be involved in policy reform, commodity exchanges, technical support, research and management. He argues that the report does not distinguish between different types of producer organisation and that more attention needs to be placed on producer organisations that resolve the perennial problem of mixed objectives: organisations which are market-oriented rather than those that are socially or community-oriented.

Moreover, producer organisations need to be clearer about their aims, and that this should be reflected in their organisational structure. He cites the market-oriented NASFAM in Malawi as one such producer organisation (See Section 5.5). Further, it is suggested that managerial mechanisms for resolving disputes between farmers and firms need to be more developed.

Section 6 briefly leaves Africa to introduce the latest innovations in reformulating the incentive structures in collective marketing that are being developed in more advanced economies: these are new models for cooperative enterprise. They illustrate how institutional innovation in the form of newer governance systems, ownership patterns and financial management within collective organisations has, *inter alia*, permitted cooperative organisations to overcome the problems mentioned above.

### *3.6.1 Market re-orientation: evolving models of collective organisation*

Looking at the cooperative, the dominant form of association, the traditional model has always faced theoretical and empirical challenges that have required some adaptation as the internal market-orientation and the external competitive environment have developed. This is true globally. For example, in the 1990s, Dutch fruit and vegetable cooperatives recognised that they faced changing market conditions: higher standards of quality control and assurance, the various needs to deliver larger volumes, exploit scale economies and create bargaining power, and add value through banding and product innovation. They addressed the capital-raising limitations and governance/decision-making constraints of the traditional cooperative model by integrating the wholesaling function (Bijman, J. and Hendrikse, G. 2003). NASFAM has been cited as an innovative form of organisation. Elsewhere such downstream integration has often taken the form of establishing wholly-owned, commercially-oriented marketing subsidiaries of traditional producer-owned organisations. Among such organisations, perhaps the most significant international cooperative in the agrifood industry is the Fonterra Group of New Zealand (Box 8).

## Box 8 The Fonterra Group

The Fonterra Co-operative Group, formed in 2001, is the world's largest dairy exporter, and includes around 70 trading companies throughout the world. It is also New Zealand's largest company and has around 16,000 employees. Responsible for a quarter of New Zealand's exports, Fonterra processes around 90% of the milk produced in New Zealand and exports 95 per cent of New Zealand's dairy products to more than 140 countries. Customers include some of the biggest firms in the global food industry including Coca-Cola, Danone, Domino's Pizza, Kraft, Mars, and McDonalds. Share ownership is restricted to the 11,000 New Zealand dairy farmers who supply milk to Fonterra. Shares are held largely in direct proportion to the amount of milk supplied in a 12-month dairy season. Capital is raised from investors through issues of retail fixed rate bonds. Among its objectives, profitability is foremost, enabled through developing relationships with customers, global sourcing, growth, and risk management. 'The composition of the Board is a significant element in the governance of the co-operative. The Board is comprised of up to 13 directors. Under the Fonterra Constitution, nine of the directors are elected from the shareholder base (Elected Directors), and four are appointed by the Board and approved by shareholders at the annual meeting (Appointed Directors)'.

Source: <http://www.fonterra.com/wps/wcm/connect/fonterra.com/fonterra.com/Home/>.

Accessed 21 December 2009

Three commercial alternatives to the traditional cooperative model are proportional investment cooperatives, member investor cooperatives and the so-called new generation cooperatives. Proportional investment cooperatives restrict ownership rights to members. These ownership rights are the same as a traditional cooperative in that they are non-transferable, non-appreciable and redeemable. However, investment from members is expected to be proportional to their patronage. Member investor cooperatives depart from the traditional form of cooperative as returns to members are distributed in proportion to shareholdings in addition to patronage, whether through dividends in proportion to shares or through appreciability of shares. Finally, there is the innovative form of new generation cooperative.

### 3.6.2 'New Generation Cooperatives'

The theme of market-oriented producer organisations runs through the literature on so-called 'new generation cooperatives' and extends this commercial orientation further by linking ownership rights, investment and governance. Here we examine the model in its most developed form through examples from the USA and consider the possible applications of the model to specific supply chains in the African context.

Since the mid-1990s, new farmer-owned associative models have emerged in the US. In 1995 Cook hypothesized that issues concerning property rights would result in a

necessary restructuring of cooperatives (Cook, M. L. 1995). At the same time, Fulton (1995) had also hypothesized that technological change and member individualism would become barriers to cooperative growth and success in the US agricultural market. In this changing context, Cook has subsequently suggested that cooperatives would either exit the sector altogether, or would make moderate changes to the cooperative structure, or finally would make a radical departure from the existing cooperative norm (Cook, M. L. and Chaddad, F. R. 2004: 1249). What has emerged in this last type of change is a form of 'associative' farmer organisation that has departed significantly from the traditional cooperative, but referred to as a 'new generation cooperative'.

Cook and Chaddad (2004) consider cooperative models in the United States. They draw attention to the limitations of 'Rochdale-adherent' cooperatives for enterprise development: ownership rights are restricted to member patrons, residual return rights are non-transferable, non-appreciable and redeemable and benefits are distributed to members in proportion to patronage, although investment may not. They point out that many traditional cooperatives are now investing in limited liability companies, joint ventures or forging other strategic alliances thus developing a vertical investment structure to overcome the constraints of the traditional financial model.

In new generation cooperatives, ownership rights are restricted to current member patrons, but they are both tradable and appreciable. Ownership rights are in the form of tradable and appreciable delivery rights which are restricted to members. Members purchase delivery rights on the basis of their expected patronage. This way capital investment is proportionate to usage. Members also exercise governance responsibilities in proportion to patronage rather than through a one man-one vote system. Ownership rights are not usually redeemable (Cook, M. L. and Chaddad, F. R. 2004: 1249-1250).

Following these initiatives in the US, there has been increasing interest elsewhere in new generation cooperatives as a way of solving known disadvantages of cooperative management. Much of the literature has emerged from NIE analysis, and has focused on property rights in conventional cooperatives. One such analysis is provided by Poulton and Lyne (2009) who consider the application of institutional economics to market development with reference to market coordination. The author examines the issues facing producers within cooperatives and consider the benefits to be gained by the new generation cooperative model.

Like Cooke and Chaddad, Poulton and Lyne's NIE analysis suggests that the problematic characteristics of traditional cooperatives result in a number of consequences:

- The free rider problem: benefits are accrued by individuals who have not invested to the same capacity as others. These individuals may be new members, or non-members who are able to market their produce through an open cooperative.
- The horizon problem: this problem arises when cooperative members under-invest in long-term intangible assets (such as market research or product promotion) because they are unable to make capital gains. New members on the other hand are able to benefit from past investments without necessarily paying a higher share price.
- The portfolio problem: compared to investor-owned firms, cooperative members are not able to diversify their own asset portfolio and therefore are not able to take advantage of their own risk preferences, instead being controlled by a risk-averse majority.
- The control problem: this is the cost of monitoring managers to ensure that they make the right investment decisions. This is considered relatively high in traditional cooperatives compared to investor-owned firms where dividends are proportional to investment and investors are able to internalise the benefits of monitoring efforts. Furthermore members of investor-owned firms are able to sanction managers by disinvesting, and managers are often shareholders as well, and therefore have a personal incentive to behave and manage appropriately.
- The influence problem: traditional cooperatives are also at a disadvantage when it comes to seeking external capital for specific purposes as these assets increase financiers' exposure to risk. This problem raises the cost of external equity, and who manages the organisation. Investor bonds may allow external equity without a dilution of member-ownership and control.

Once again, such reforms to the traditional cooperative model have been found effective, but in a context markedly different from that affecting African smallholder farmer associations. It is argued by Donovan *et al* (2008) that existing cooperatives may find that such 'hybrid' cooperative forms will provide new opportunities to overcome some of the challenges felt by traditional cooperatives, such as investment and governance constraints. It is difficult to see the model being transferred 'as is'; however, attention is drawn to the need to develop innovative institutional and organisational relationships that are appropriate for African smallholders, including ways other than the 'soft' option of human capacity building– such as bonds – that might overcome the 'hard' capital problem. As in the case of new commercial and donor relationships, data and literature are not yet available for external analysis.

### *3.6.3 The 'offensive cooperative'*

Whilst traditional cooperative forms have been described as defensive, aimed at protecting farmers and minimising risk, new generation cooperatives can be seen as 'offensive'. Offensive cooperatives have sought ways to cope with falling profit and 'add value' to their produce at least in part due to their freedom to access and manage capital. Thus, the growth of new generation cooperatives has necessitated a 'realignment of their ownership structure' (Cook, M. L. and Chaddad, F. R. 2004: 1251). Characteristics of such new generation cooperatives are a closed membership, a contract-based membership, and a homogeneous membership with common objectives and strategies (usually only the top 5% of producers who are able to access sufficient capital etc).

Cook and Plunkett (2006) have developed the analysis of the new generation cooperative by offering the concept of 'collective entrepreneurship': a form of economic behaviour adopted by 'formal groups of individual agricultural producers that combine the institutional frameworks of investor-driven shareholder firms and patron-driven forms of collective action'. These patron-driven organisations they call 'offensive cooperatives', for their commercial rent-seeking orientation rather than the traditional 'defensive' model designed to correct 'market-failure'. As yet undeveloped and under-researched, this notion of collective entrepreneurship introduces more pointedly the hypothesis that the economic behaviour of groups – including groups of developing country smallholder agriculturalists – can escape the constraints of bureaucracy and learn to be entrepreneurial.

### *3.6.4 Is the 'new generation organisation' transferable?*

The theme of institutional organisation is recurrent in the literature relating to both developed and developing areas. What is needed is institutional and organisational innovation in relation to collective enterprise. From Canada and the US the work on new generation cooperatives provides an interesting approach to ownership and rights to control. In these countries, new generation cooperatives are seen to provide a solution to some of the historical and structural problems of cooperatives including issues of inadequate property rights and equity problems. Whilst the literature on new generation cooperatives may not be immediately applicable to farmer organisations in the African context, what can be useful is a greater understanding of where cooperatives may begin to make some transformations. In the area of financial management, whilst collective decision making may be cumbersome, and top-down decision making is undesirable, there may be grounds for seeking alternatives - either in the form of a philanthropic benefactor whereby decisions are made on behalf of a (no doubt) trusting collective of smallholders; or an investor model: external equity investment with capacity to exert

leverage through management building is another potential model. Alternatively, bondholders with a financial stake but without governance rights offer the possibility of investment without diluting membership control.

### **3.7 Key insights**

This section has outlined the historical development of cooperatives in the developed and developing world. It has been shown that farmers act collectively in order to overcome issues of scale, lack of working capital and lack of power in the market (among other factors). However, since the first organised cooperatives, regular themes continue to challenge the operation and success of farmers groups such as:

- Lack of capital to grow in scale and complexity, particularly investment in physical assets for value addition through processing and manufacturing
- Lack of management capacity and good organisational governance
- Competing market or economic forces that confound traditionally bureaucratic and unresponsive structures and strategies

This section has also illustrated the dual nature of farmer groups in acting as both business and social movement. This has historically proven difficult to manage and resulted in inefficient management and poorly defined goals. Yet farmer groups continue to exist and are indeed encouraged by many as a response to imperfect markets and low participation of small scale farmers in those markets.

In understanding what does and what doesn't work for farmer groups, an historical analysis can indicate areas of promise and areas of failure. In this regard, clearly, intervention has been a necessary factor in providing farmer groups with working capital, supporting management structures, improving marketing strategies, assisting with market linkages and facilitating legal frameworks. However, the capacity of external actors to really benefit farmer groups whilst offsetting the negative impacts of intervention has proven elusive.

Some clear lessons emerge from the analysis of the external policy and economic environment:

- Policy: development policies partly reflect political trends and 'received wisdom' in major donor institutions and bilateral organisations concerned with international development. Equally, the domestic policy and regulatory environment and the linkages with the external environment shape policy design and implementation. Development policies dating from the mid-20th Century have had a formative impact on the shape of agricultural markets in Africa, and during recent decades policies have

been ill-conceived and changed dramatically. The changeable winds of agricultural policy, among other wider influences, have impinged with destructive effects on the rural populations.

- State versus market: underlying the policies is the ideological and pragmatic debate about the appropriate role of the state in improving market performance and economic growth. The shift from intervention to free market solutions and latterly a shift back towards invoking a gentle but visible hand of intervention illustrates the power of international and domestic policy – or dogma - over empiricism in this most contested of areas. There is compelling evidence from the literature concerning transition and developing countries, the 'East Asian miracle', and the 'Green Revolution', that major improvements in well-being have been accompanied, if not stimulated by, judicious state involvement, including improving the economic and business framework of institutions, and direct provision of public goods and services where markets fail.
- Stakeholder participation: the rise of the stakeholder concept and the resurgence of participative approaches have illustrated the poverty of previous policies and conceptually narrow directives by policymakers. The demand has shifted towards complex policy 'interventions' that are multi-stakeholder and inclusive, rather than 'magic bullets'.

While much can be learnt from a substantial review of experiences of collective organisation, some additional points to note are the following:

- Objectives: traditional cooperative organisations do not easily deliver on social as well as economic objectives; social policy is better separated from enterprise policy
- Social and environmental responsibilities: commercial supply chain linkages can deliver on social and environmental management responsibilities, but these are often mediated by donors, NGOs and philanthropic organisations, and are linked to niche and vulnerable markets inaccessible to the majority of smallholders
- A role for the state: statutory arrangements such as levies and interprofessional organisations have proven potential in advanced economies to facilitate market development; however, they do not substitute, but complement, efficient market coordination and investment by the state in public goods; intervention must have a 'light touch', resembling a coordinated market economy
- Advocacy, but limited politics: while smallholder associations have a potentially valuable advocacy role in politics, the converse is not true: political subversion leads to inequity and inefficiency

- Organisational and institutional innovation: advanced economies have permitted the development of innovative institutional and organisational forms which serve as examples for developing regions
- No panacea or magic bullet, but contextualisation: models of institutional and organisational forms must be developed locally
- Entrepreneurism and capital: marketing cooperatives must be entrepreneurial, and enterprises can be opened up to external capitalisation – and management input - by philanthropic organisations and maybe also commercial investors
- New generation models: among the less poor new cooperative models may be able to revitalise the local agricultural economy and multiply development by creating opportunities for poverty reduction among the poorest through the labour market and through the promotion of general economic development.

## **4** *Challenging external environments*

Changes in African economies have been brought about by a number of national and international factors. With the abandonment of government marketing and commodity boards, a reduction in state intervention, decentralisation, democratisation, reduced barriers to trade through liberalisation, emerging market conditions have created an environment in which African producers find themselves facing new challenges as well as new opportunities. Farmers now have to deal with the uncertainty of liberalised markets as well as the uncertainty that characterises their immediate natural environment. Uncertainty affects the ability to fulfil trade contracts or indeed survive through the lean season. Market opportunities also have their barriers in the form of standards and regulations, certification costs, quality assurance and traceability. Yet, new approaches in the areas of microfinance, commercial partnerships and new forms of organisation may assist the greater participation of smallholders in markets. With poverty remaining a real issue in all African countries, increased participation in global markets may be seen as not merely a trade opportunity but a chance to raise agricultural output and improve livelihoods.

One significant area that this report does not touch on is the changes and stresses in production systems and the natural resource environment due to climate change, water shortages and other resources depletion. Comments in the introduction hinted at the potential supply response arising from innovation in agricultural technologies. The brief section that follows concerns post-harvest challenges that are institutional rather than the serious physical, climate-related or technological challenges.

### **4.1 Regulations and increasingly specific market demands**

One of the most pronounced changes in the global agricultural economy has been a prolific increase in food safety standards. Increasingly produce must conform to a required standard of quality and homogeneity and farmers must offer reliable and consistent delivery. Institutions must be in place to provide certification and monitoring. These changes over the past ten to fifteen years have resulted in many smallholder farmers being excluded from global and domestic urban markets (García Martínez, M. and Poole, N. D. 2004). This issue has been taken up by a number of authors who seek ways of increasing smallholders' ability to gain access to these valuable markets (Reardon, T. and Berdegué, J. A. 2002; Narrod, C., Roy, D., Okello, J., Avendaño, B. and Thorat, A. 2009). Nevertheless, the barriers to entry and sustainable involvement in non-traditional high value agrifood (niche) product markets in which conditions fluctuate with variations in the economic climate are significant obstacles to realising agricultural

and rural development on a wide scale (Carletto, C., Kirk, A. and Winters, P. 2007; Donovan, J. and Poole, N. D. 2008; García Martínez, M. and Poole, N. D. 2009).

## **4.2 Consumer preferences**

Increasingly diverse consumer preferences in the areas of fair trade and organic produce alongside an increasing interest in responsible or sustainable sourcing linked to corporate social responsibility is influencing agrifood markets (Vermeulen, S., Woodhill, J., Proctor, F. and Delnoye, R. 2008). Like food safety standards, mechanisms providing monitoring and certification of fair-trade and organic produce must be available to smallholders. Social responsibility in supply chains is now receiving more attention than ever before both from traditionally interested parties such as NGOs and advocacy organisation as well interested private sector and philanthropic institutions. This sector of the market is likely to be a challenge to smallholders as well as offering opportunities. It is also subject to market and economic fluctuations (García Martínez, M. and Poole, N. D. 2009), as consumer willingness to pay is not constant. The characteristics of such niche markets also require critical examination: major food manufacturers (eg Cadbury) are facing incentives to 'mainstream' premium market practices such as fair trade and organic; meanwhile, the limits to volume and price premia may impel organic producers to reconvert to conventional in order to achieve an economic threshold of productivity.

## **4.3 The rise of supermarkets in developing countries**

The rise of supermarkets in Africa has a huge impact on small-scale farmers. In Kenya alone figures from 2003-2005 show that 225 supermarkets and 209 hypermarkets existed (Neven, D. and Reardon, T. 2004). This phenomenon is the result of both supply and demand factors. Increased urbanisation alongside more women in the workforce have resulted in greater demand for convenience shopping and convenience food. Lower prices of processed food have fed in to this changing demand. Rising real mean per capita incomes and a rise of middle classes in African cities has increased demand for processed foods and 'western style shopping'. The expansion of refrigeration also has contributed to the growth in demand for supermarkets, as has the increase in car ownership and improvements in public transport. On the supply side, liberalised economies have attracted foreign investment, and advances in technology and the practice of efficient consumer response (ECR) has enabled supermarkets to coordinate supply (Reardon, T., Timmer, C. P., Barrett, C. B. et al. 2003).

Small-scale farmers have the opportunity of increased outlets for their produce in national and regional markets. In South Africa, 55% of national food retail is supplied by supermarkets and in Kenya supermarket output accounts for 30% of all food retail. According to data published by FAO in 2003, supermarkets in Kenya bought three times

more the volume of produce than the Kenyan export market. Reardon *et al* argue (2003) that the increase in supermarkets in the developing world presents many potential possibilities as well as challenges for small farmers. The significance of the supermarket phenomenon for smallholder suppliers is great, and the barriers that smallholders face in export markets is being replicated – for higher value produce – in domestic markets. It is evident from the grey and academic literature that there is a strong potential for commercial linkages between smallholders and other farmers and the private sector for traditional agricultural export commodities (beverages such as coffee, cacao and tea, and fibres such as cotton), particularly those for added niche characteristics such as organic and fair-trade, and for high value non-traditional agricultural exports (fruits and vegetables). The technoeconomic characteristics of these products are amenable to grading and standardisation, and to sophisticated quality control systems, the resources required for which generally are beyond the capacity of smallholders.

Domestic markets for lower value and bulk commodities such as the staple products that are most closely linked to poverty, under-nutrition and ill-health in East and Southern African countries have been less touched by these driving forces. For many African smallholders, domestic markets may be much more important than export markets (Diao, X. P., Dorosh, P. and Rahman, S. 2003). The potential for boosting these apparently lower value sectors has been demonstrated in the case of cassava in Zambia, due in part to the public sector investment in agricultural research (Chitundu, M., Droppelmann, K. and Haggblade, S. 2009), even if they are not so politically attractive to donors and NGOs.

#### **4.4 Challenges and opportunities?**

The potential for agricultural development to positively impact on smallholders depends on the capacities of market actors including government, agroindustry, traders, and producers to make product and input markets work more efficiently and effectively, and on the capacities of the rural poor to organise effectively into viable businesses capable of engaging with markets (Donovan, J., Stoian, D. and Poole, N. D. 2008). However, producer organisations are surrounded by legal restrictions, low managerial capacity, exclusion of the poorest and often a failure to be recognised by the state as policy stakeholders. Furthermore, in each market sector there are likely to be challenges and opportunities that require different strategies: a given approach may not work for all situations, and disaggregation is necessary as much in analysis as context-specificity is in intervention (Poole, N. D., Gauthier, R. and Mizrahi, A. 2007; Chitundu, M., Droppelmann, K. and Haggblade, S. 2009; Poole, N. D. 2009).

In high value markets opportunities exist due to the expansion of supermarkets, as noted above (up to 6-7% each year) in developing countries. For traditional bulk exports, it is suggested that governments should play a role in regulating fair and efficient operations in marketing (World Bank 2008). For the bulky, low value domestic staples markets, reducing transaction costs and risk could be ameliorated through the development of commodity exchanges and market information systems such as rural radio and messaging systems. Barrett (2008) argues that the conceptual and empirical evidence on smallholder participation in the trade in staple grains in eastern and southern Africa points to interventions in producer organisation, reductions in transaction costs, and investment in production technologies and other assets. Such interventions could be 'micro-interventions', context-specific, and may not be easily 'upscaleable'. Weaknesses in transport systems and infrastructure also are often a fundamental constraint. Certain restrictive trade practices within and between African countries also impose heavy burdens on regional trade.

Making these trends benefit the rural poor requires improved market infrastructure, risk management strategies, support to smallholders and collective action through producer organisations. The World Development Report 2008 recommends that donors and governments assist by facilitating the organisation of farmer producer groups, training for group leaders and facilitating inclusion of women and young farmers (World Bank, 2008: 14). Further options include the use of targeted vouchers for farmers to purchase inputs and stimulate demand in private markets as well as making subsidies available to cover start up costs of entry to private distributors. This, the World Bank argues, will require a joint effort between public legislative bodies and private institutions to ensure food safety, risk assessment and good practice. These emerging trends in both global and African markets have had a knock on effect on supply chains in the areas of organisation, management, technology, industry structure, procurement and standards and finance and may work to either include or exclude smallholders (Vermeulen, S., Woodhill, J., Proctor, F. et al. 2008).

#### **4.5 Key insights**

- The principal lesson from a brief examination of the external environment is that opportunities in national and international markets for entry by farmer organisations often are finely balanced by a range of barriers to smallholder participation.
- Cases of successful entry often are often the result of 'point' rather than 'system' interventions, ie context-specific, not typical of the rural economy. Yet the requirement for 'scaleability' and 'replicability' is a response the demand for donor- and budget efficiency, and the need to meet international policy targets and goals.

- On the other hand analytical approaches to identifying and resolving the weaknesses of agricultural development and poverty reduction will be the result of local analysis and idiosyncratic approaches and interventions rather than generalisable 'blueprints'.
- Balancing opportunities against barriers requires recognition of significant barriers to high value markets that operate against the mass of the smallholders. Successes often are the result of individual interventions rather than sectoral initiatives.
- In each market sector there are a likely to be challenges and opportunities that requires different strategies: a given approach may not work for all situations, and disaggregation is necessary as much in analysis as specificity is in intervention.
- The development of global agribusinesses and agri-superpowers – essentially an increase in industrial scale and efficiency, and, hence, global competition – is likely to whittle away the opportunities for smallholders;
- Policy makers will increasingly look to scale, efficiency and new technologies inaccessible to smallholders to address food security objectives for growing populations in an era of climate change and intense social and demographic transformations.

## 5 *Smallholder farmer associations in East and Southern Africa*

The cooperative model is the dominant form of farmer association. This has evolved significantly in advanced economies through institutional innovation by:

- exploiting flexibility in the regulatory environment, innovative management structures have been created that overcome management weakness by introducing outside skills;
- curtailing the democratic principle that creates inertia, stakeholder incentives and participation are rewarded;
- semi-separation of the commercial activities and prioritisation of the commercial objectives, enterprise and performance have flourished.

Moreover, the Achilles heel of collective enterprise has long been capital raising on a significant scale. This has become possible by changes in organisational concept and structure:

- increasing member investment, for example in proportion to throughput or equity (in the New Generation Cooperative model) and
- securing other forms of investment (in the European and New Zealand model); and in a few cases in Africa, by
- creating loan guarantee funds and providing insurance for collateral

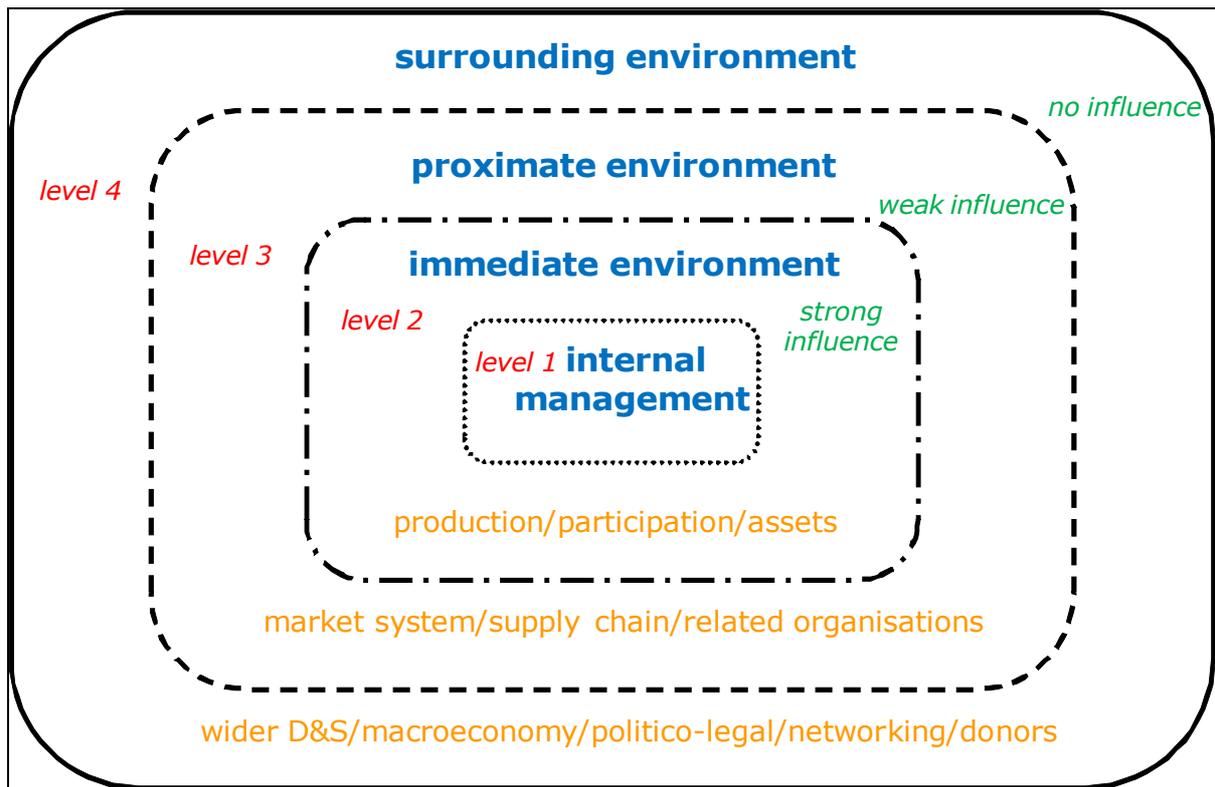
Where institutional innovation has not occurred – in many developing economies – the organisational model is still beset by the familiar weaknesses of inadequate management, elite capture, inefficiency, complex and conflicting objectives, lack of accountability, undercapitalisation, resulting in basically poor business performance.

Detailed examples from the literature on specific farmer associations in East and Southern Africa are not widely available. Some of the published literature covers supply chains, other focuses on the work of NGOs and donors working with smallholder groups and cooperatives. Most studies are sectoral in nature. Nevertheless, in the following section we look at some facets of the market and institutional environment within which farmer associations operate in Africa, and then some specific examples.

### **5.1 Smallholder association environment analysis**

Attention has been drawn earlier to the importance of the historical, political and market context within which smallholder enterprise operates. Understanding the interaction between the organisation and the external environment is essential. A framework for analysing the internal and external influences on smallholder associations has been derived from the marketing and management literature (Figure 2).

**Figure 2 Smallholder association environment analysis**



Source: adapted from Kachule, Poole and Dorward (2005).

The four levels of the environment move from the central, fundamental, internal management of the 'grassroots' smallholder association, which in the Malawian context is the club. Level one, the club management, interfaces directly with the level two environment and of the membership of the club and its activities: its production and output, and any assets that together make up the grassroots club organisation. In terms of control, the grassroots smallholder association can exert strong influence over its internal (level one) and immediate (level two) environments.

In relation to the grassroots smallholder association, the level three environment includes related and supporting organisations with which the club has direct contact, but only limited influence. These are commercial input and finance suppliers and marketing organisations; associations and/or apex organisations that facilitate and provide services; and the market systems into which farmers are inserted and which fulfil some or all of the functions of transport, storage, processing and exchange (of goods, services, finance, information, etc).

The level four environment is the wider economy: characteristics of supply and demand of the same or competing products, the macroeconomic variables which impinge on system stakeholders, the political and legal environment, and the donor and

international community. National public sector organisations can be found within both level three (eg those such as Ministry of Agriculture and level four (other ministries and executive entities of government that are not directly connected to the particular production and marketing systems).

The environmental analysis was used to identify problems within a range of ten Malawian smallholder associations, which are summarised below:

**Level 1 internal management environment**

- weaknesses in grassroots club management and finances
- a low level of management skills among organisation executives

**Level 2 immediate membership environment**

- ineffective democracy and organisation
- lack of membership commitment
- poor farming production systems
- low product quality
- insufficient physical assets and infrastructure

**Level 3 proximate market chain environment**

- inefficiencies in supporting organisations
  - lack of timeliness in service provision
  - poor quality technical services and inexpert advice
  - failure of services due to
    - low and variable prices
    - withdrawal of services
    - internal mismanagement at association or apex level
- poor logistical infrastructure and communications

**Level 4 surrounding macro environment**

- low and variable prices for products due to unfavourable demand conditions, often due to competition with substitute products
- high interest rates
- uncertainties from or within due to:
  - legal framework
  - political will
  - donor climate

Based on a postal questionnaire of producers, visits and interviews at club chairman and association executive levels, a typology was derived to summarise the characteristics of the 10 organisations in terms of origins, structure, support and objectives. The diversity of linkages to other organisations illustrates the complexity of the institutional

environment within which smallholder associations operate, and the relationship management challenges confronting association leaderships.

## **5.2 Organisational typologies and organisational development**

Within the Malawi situation, a variety of organisational types were identified that are more or less representative of many small scale farmer associations. It is not an exhaustive account: Malawi is one of a number of African countries where parastatals such as ADMARC still exist with considerable influence over the operation of other independent market players. Here the focus is on collective organisations that include smallholder farmers and traders.

### *5.2.1 Large diverse service providers*

NASFAM and the NGOs Action Aid, Care and Concern Universal were organisations formed out of external (donor) initiatives, often building on a foundation of clubs formed during an earlier era, or existing Village Development Committees. They are not typical of indigenous farmer associations, but are common types in many African countries where attempts have been made by external players to indigenise an external initiative:

- complex organisations usually providing, or facilitating provision of, a range of services to members at the club level
- input/output services, training and capacity building, provision of information and technical advice, advocacy;
- clear vertical structures and constitutions providing accountability and transparency;
- skilled executive leadership and trustees creating efficient service delivery and networking;
- considerable donor support;
- a strong commercial orientation within a broad 'empowerment' and livelihoods agenda.

### *5.2.2 'Phoenix' organisations*

These were specialised indigenous organisations that developed through crises or the collapse of a precursor, such as the Smallholder Coffee Farmers' Trust that emerged from the 'indigenous' Mzuzu Smallholder Coffee Association; and ASSMAG that emerged from the 'indigenous' National Smallholder Seed Producers' Association. This pattern of organisational development through a 'learning process' is not uncommon. They had the following characteristics:

- inefficiency and corruption within the secretariats of the previous organisations left an 'opportunity space' for the new organisation led by an active membership;
- members assumed previous liabilities;
- focus on cash commodities with strong market linkages;
- governed by effective constitutions:

- strong vertical organisation co-existing with democratic procedures;
- transparency, accountability and effectiveness;
- leadership varies:
  - ASSMAG has strong farmer representation and active trustees including independent members;
  - SCFT has active member-leaders, and little dependence on the secretariat.

### 5.2.3 *External initiatives in transition*

These associations were responses to opportunities perceived by outsiders, therefore not indigenous but an external initiative. These were still between launch and take-off:

- 'soft-focus' hierarchical organisations:
  - MALEZA: broad-based enterprise development;
  - IDEAA: diversifying from staples to high value products and information;
- member-driven organisations for specific crops:
  - PAMA: umbrella organisation for paprika clubs and associations;
  - ZIPATSO – a 'phoenix' organisation, a tangerine production and marketing group looking for outlets.

### 5.2.4 *Transition stages of collective organisations*

There is a learning process for organisations to grow to maturity. Commenting on the transition process, Donovan *et al* (2008) suggested that the period from launch, through take-off to sustainability could be a long period of time. In fact, writing for the Ford Foundation, they referred to organisational 'maturity', which embraced notions of organic development, sustainability and independence, and argued that this process could take years or decades, and that short-cuts were necessary from a donor perspective (Box 9).

#### **Box 9 The 'long and winding road' towards viable RCEs**

'It is the rule rather than the exception that RCEs reach maturity only after three to five decades – despite or, at times because of, intensive, albeit often disarticulated, interventions from government agencies, NGOs, development projects, and the like. The long duration of this process will increasingly become an obstacle for smallholders, RCEs, and development agencies, given rapidly globalizing markets for agricultural and forest products where these enterprises meet with both new opportunities and increased competition. It is imperative to identify viable shortcuts to RCE development, based on enabling political and legal frameworks, harmonized and aligned development interventions, and, most importantly, the delivery of effective and well articulated technical, business development and financial services'.

Source: Donovan, Stoian and Poole (2008: 93)

Two important considerations stand out concerning the type of interventions in both the institutional framework and more directly within the organisations concerned that might promote organisational learning and lead to organisational maturity. First, the potential shortcuts presuppose **coordination** among implementing and facilitating organisations in the surrounding environment from the public sector, civil society and the private sector. Understanding this environment and the tensions within are important for identifying innovation possibilities and intervention points. Various conditions need to be satisfied:

- joint planning is necessary through inclusive, deliberative fora in targeting interventions and initiatives in respect of, for example, gender issues;
- assuring sustainability requires the planning of tangible and intangible investments and the planning of the scaling down and withdrawal;
- sustainability also requires appropriate sequencing of interventions such as training and professional services support so that enterprises 'learn to walk steadily before they jog and then subsequently run';
- there needs to be a willingness to search out and experiment with alternative organisational models that are most appropriately adapted to local circumstances.

Secondly, **realism** is necessary in respect of:

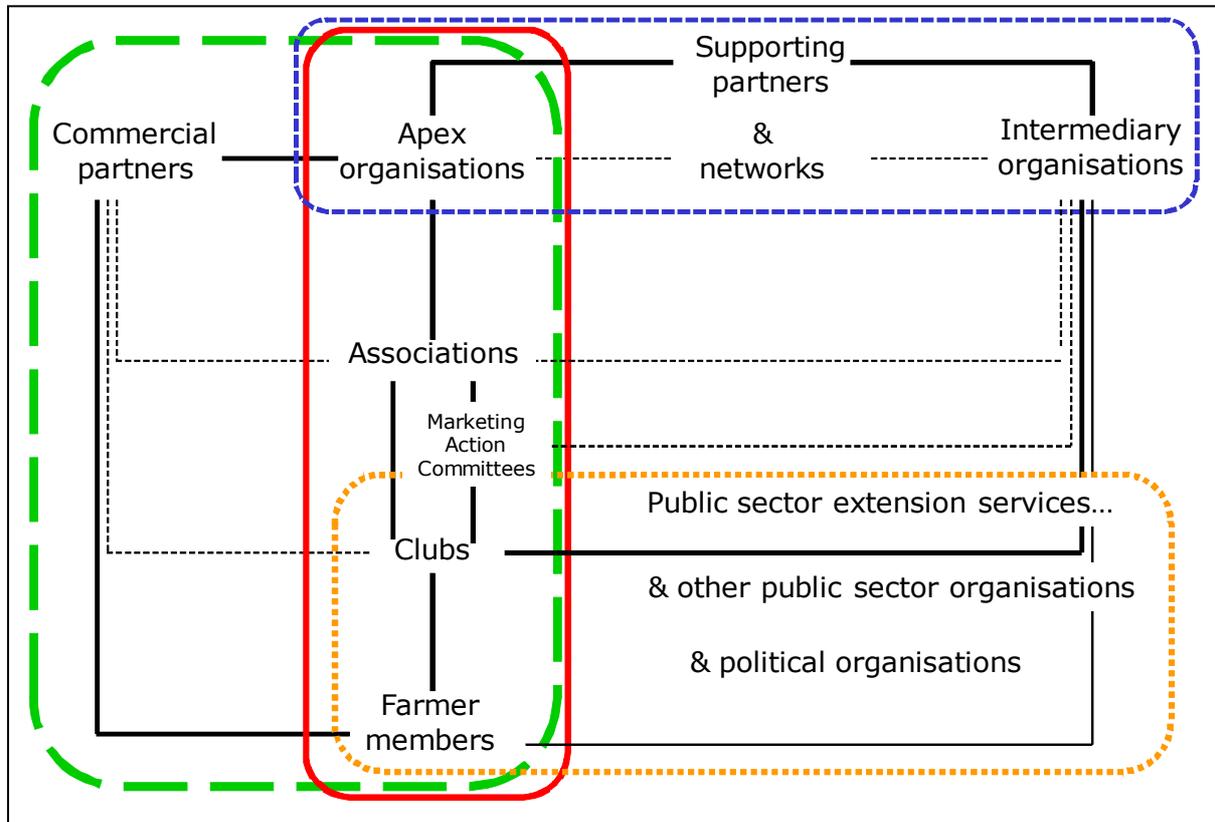
- time frames for skills development and organisational learning; in Korten's terms, 'learning to be effective, then efficient and then expanding' to take advantages of the scale economies arising from collective organisation takes time and specific investments;
- expectations concerning relationship building among value chain participants; the incentive structures of transactions within organisations, and between organisations and their supply or value chain partners and other organisations within the external environment require specialised understanding and sophisticated management of tradeoffs;
- priorities: is there a hierarchy of objectives nested within the ideal 'Triple Bottom Line' of economics, equity and environment? Different stakeholder objectives need to be reconciled.

### **5.3 Mapping sector structure and organisation**

In the Malawi study a conceptual map of the organisational environment was helpful in order to define more clearly the nature of the diverse organisations and their relationships to external stakeholders. The focus was not so much on supply chain linkages, but on supporting organisations. Nevertheless, commercial relationships were often mediated through supporting or apex-type organisations, and an attempt was

made to map and differentiate these relationships with commercial partners from relationships with other spheres including the public sector organisations – and the political context - and the external support organisations Figure 3).

**Figure 3 Organizational networks and interest groups**



Source: adapted from Kachule, Poole and Dorward (2005).

A map of the organisational and institutional environment highlights the incentive structures operating, enabling identification of interest groups and understanding of how smallholder associations can manage a network of relationships with different and competing objectives and priorities. In the case of Malawi, these interest groups can serve as both entry points for coordination of investments in sectoral development, and as groups for externalising or engaging in advocacy in relation to the wider environment on issues of sectoral importance (Figure 3).

- Organizational capital formation: the grassroots smallholder association or club is usually linked through second tier associations or marketing action groups to apex organisations. Apex organisations typically are national and international NGOs, and provide and facilitate a range of services to clubs, associations and cooperatives. Linkages are more or less formal, and in many cases are defined by governance principles (eg representativeness and democracy) and governance structures

(statutes and constitutions) that are often critical factors in smallholder association performance. This complex of organisations and relationships is grouped in the solid box in Figure 3;

- Delivery of training for technical skills development with a concomitant danger of political subversion: the grouping of public sector organisations and grassroots organisations within the small dotted box in Figure 3 highlights the relationships between the state and the 'citizen', which encompasses potential flows of technical support towards the grassroots, and advocacy towards the state, but also identifies relationships of potential political interference in local development processes;
- Commercial relationships and supply chain management: the focus on business skills and development within the dashed box groups the tiers of producer organisations with commercial partners at different levels of the supply chain, from inputs and technical advice to marketing of raw products, and storage, processing, manufacturing and distribution functions (large dashed line box in Figure 3);
- Advocacy and governance: apex and supporting organisations and networks within the large dotted box in Figure 3 constitute a group of sector players that link to the public sector at the national and international level as advocacy groups for good governance, and efficient, effective and enabling national and international institutional frameworks.

#### **5.4 Oromia Coffee Farmers Cooperative Union**

The Oromia Coffee Farmers Cooperative Union in Ethiopia was founded in 1999 comprising 34 coffee cooperatives representing 22,503 smallholders. The Union was formed in response to the collapse of the price of coffee and market liberalisation, which placed farmers in the region into mounting debt as exporters defaulted on their payments. The Oromia Union was the first cooperative in Ethiopia to enter the fair-trade and organic overseas market. The Union was set up by existing primary cooperatives and financed entirely by them through affordable share prices. The second tier organisation now includes 129 primary organisations and cultivates 163,192 hectares of which 50,692 are certified organic. Farm size averages one to two hectares. Important characteristics of Oromia are:

- Market: 50% of the cooperative's coffee is sold locally and 50% is exported. The cooperative participates in fair-trade only, organic only, fair-trade and organic and conventional markets. Over 40% of the cooperative's export sales go directly to the fair-trade organic sector.
- Organisation: Oromia is a democratic organisation affiliated to a membership-based secondary cooperative. Representatives from all cooperative societies attend assemblies. Board members are elected by regional representatives. In these respects,

it has retained the traditional form of cooperative organisation, and espouses the Rochdale/ICA Principles.

- Contractual arrangements: The cooperative provides technical assistance and training, facilitates market linkages, ensuring certification standards, packing and distribution. The fair-trade premia go directly to the cooperative societies and are used for health, water, sanitation and education. Of other revenue, 30% is placed in the Cooperative fund, 5% of which goes on operating costs. The remaining 70% goes to the member societies which pay individual farmers based on the amount of coffee sold to the cooperative.
- Supply chain: The market chains for coffee in Ethiopia are either private sales or sales through cooperatives. The supply chain is long with coffee beans passing to numerous traders before reaching auction. The majority of farmers sell privately but get lower returns for their produce. For the Oromia farmers marketing and distribution is managed by the cooperative. Having succeeded in becoming a direct exporter of its members' coffee, the cooperative has eliminated 2 or 3 stages in the supply chain resulting in greater profit for the farmers
- Physical capital: the strength of the organisation within the supply chain is exemplified by substantial investments in physical infrastructure for storage and processing of coffee: tens of pulperies, hulleries and warehouses.

The growth and transition stages of Oromia are illustrative of a necessary learning process: the organisation cites its success as being rooted in a number factors, first, the managerial capacity which had experienced and committed leadership; second, that the organisation emerged from a participatory dialogue between farmers and government officials ensuring that it had the backing of the government as well as the farmers. These principal factors ensured that the cooperative secured political support as well as retaining its connection to the membership base. The cooperative has utilised the premiums gained from fairtrade and organic contracts to address social objectives such as setting up potable water projects and the building of schools and clinics. The biggest challenges facing the cooperative are not unexpected: in the first place, a shortage of capital; secondly, there has been difficulty in maintaining good stakeholder relations with government due to high personnel turnover in government departments, limited education and awareness by government officials and other market participants of the complex operations of cooperatives.

## **5.5 National Smallholder Farmer's Association of Malawi (NASFAM)**

NASFAM is a specific case that was included in the study by Kachule, Poole and Dorward (2005) that transcends the conventional smallholder organisational environment in

Malawi. It shares characteristics with a new generation of cooperative enterprises that are attempting to transcend the problems of weak management, undercapitalisation and ineffective entrepreneurial orientation which have been referred to earlier.

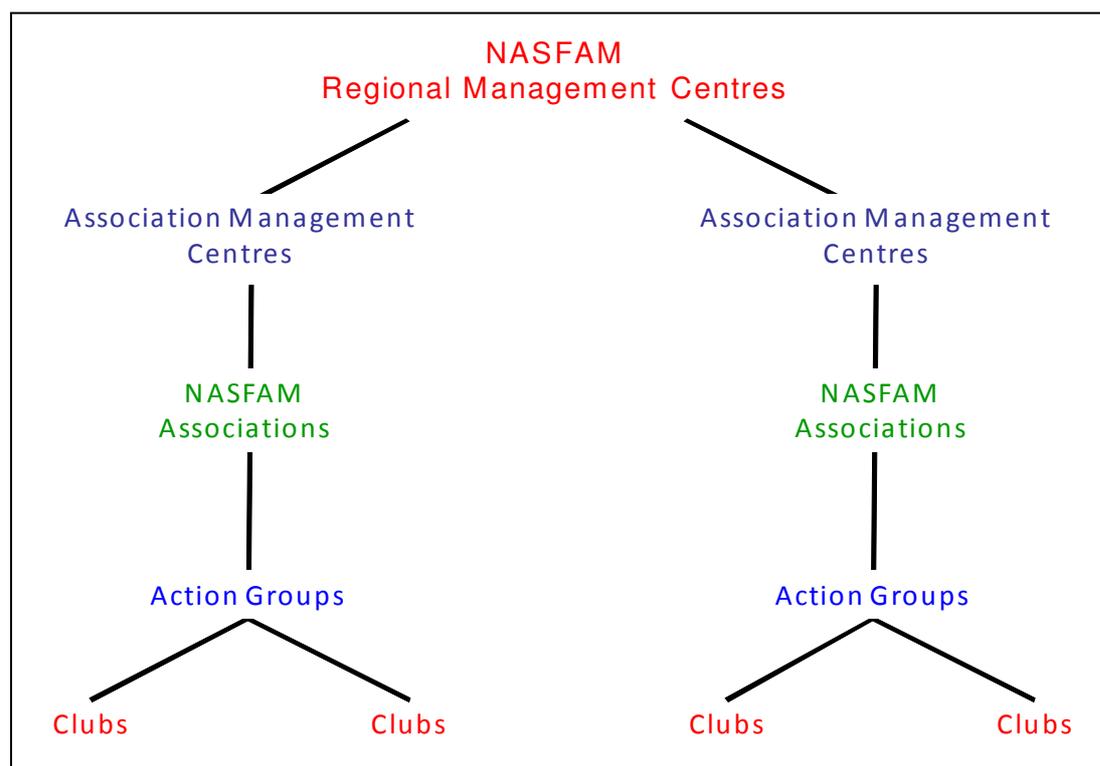
### *5.5.1 Origins*

The association was founded in 1997 as a farmer directed business system. Its 100,000 participants are smallholder farmers with less than 1 hectare of land. NASFAM came into being after a USAID-funded Smallholder Agribusiness Development Project (SADP) was implemented by Agricultural Cooperative Development International (ACDI/VOCA). This project supported smallholders through improved access to inputs and higher returns on agricultural sales, information dissemination and the promotion of collective action through farmer associations. The objective behind this project was to increase smallholder participation in previously restricted markets such as burley tobacco. Prior to liberalisation, high value crops were the sole domain of the estate sector, however, during the 1990s with the help of the SADP farmers were organised into 'group businesses' linked to farmer association structures that provided inputs and services such as credit and knowledge transfer and information dissemination. Eventually the smallholder groups became formal associations as capacity increased. Aware of the benefits of collective action, fourteen associations formed to make the National Smallholder Farmer's Association of Malawi in 1998.

### *5.5.2 Structure and operations*

NASFAM has been described as a 'democratic bottom-up organisation'. Unlike many cooperative organisations there are no government officials on the board of NASFAM. Its success lies in the ability 'to develop the commercial capacity of its members and to deliver programmes that enhance their productivity' (Prowse, M. 2008: 4). NASFAM provides credit, extension and training, uses economies of scale to reduce transport costs and actively seeks external markets for export of produce. It has been able to do this with success because of its strong and transparent institutional structure which keeps its commercial business separate from development and training programmes. The impact of NASFAM has also been attributed to its apolitical stance and its consistent donor support from USAID. This support continues to be important in the functioning of the organisation, and it is not possible to comment on the likelihood of independent organisational sustainability. It works as a multi-functional, multi-sectoral organisation. Operations are divided between the commercial and development sectors, registered as a profit company and as an NGO. Figure 4 below illustrates the organisational structure:

**Figure 4 NASFAM structure**



Source: authors

### 5.5.3 A 'new generation association'?

An important characteristic of NASFAM is how it has developed an innovative structure that is a complex evolution of the cooperative model. While at grassroots level the association has cooperative characteristics, commercial and other entities have been created to handle functions that are typically circumscribed by the traditional cooperative structure, the commercial and business services functions. Nevertheless, these subsidiary organisations fall ultimately within and under the cooperative structure. This type of innovative development of the traditional cooperative model has been common in advanced economies (eg in the European Union) where cooperatives form a large part of the agricultural economy and yet have needed to escape the constraints, particularly affecting commercial activities and capital raising, of the strict adherence to the Rochdale Principles. Further discussion of innovative forms of cooperative organisation outside Africa will be given in the next section.

Thus, NASFAM's associations jointly own the NASFAM Development Corporation (NASDEC) which is a not-for-profit company which owns two subsidiaries, the NASFAM Commodity Marketing Exchange (NASCOMEX) and the NASFAM Centre for Development Support (NASCENT). NASCOMEX runs the revenue generating private sector and marketing services whilst NASCENT provides policy advocacy and outreach, information

services, and advice on HIV/AIDS and gender issues. Both NASCOMEX and NASCENT are run by advisory councils whilst NASDEC is governed by twelve directors, eight of which are democratically elected by NASFAM associations, and four are appointed for their technical and commercial expertise.

According to the Strategic Development Plan NASFAM's primary objectives continue to be a challenging balance of the social, technical and economic, but with an emphasis on the latter:

- Increased commercial revenue and profit
- Improved crop quality and quantity
- Enhanced association performance
- Expanded member livelihoods
- Expanded influence on policy
- Enhanced systems performance

## **5.6 Collective and community-based management organisations**

### *5.6.1 Rural community-based enterprises*

Another form of farmer association has been referred to as the rural community enterprise (RCE): 'a business based on the production of agricultural or forest products and services, which are owned by small- and medium scale producers and pursue multiple objectives including profit maximisation as only one among many goals' (Donovan, J., Stoian, D. and Poole, N. D. 2008: 12). The less restrictive (in terms of legal structure) and more commercial typology is favoured by the Ford Foundation. Rural community enterprises have affiliated memberships or registered community members. They are legally registered in diverse forms as a cooperative, association or incorporated company. The objectives of the enterprise may range from employment, capitalisation, public services and resource management. Policy making, management and decision making are commonly undertaken by a board of directors and a general assembly and residual claims tend to be distributed through usage or equal distribution among members (Donovan, J., Stoian, D. and Poole, N. D. 2008).

Rural community enterprises act in a similar way to other forms of collective action in that they seek to increase economic and social empowerment through scale: lower costs, increased bargaining power in the market, democratic decision making rights and access to political and legal arenas, and increased access to services. External players such as NGOs and donors have played a significant role in promoting local enterprises as poverty alleviation programmes. However, externally driven organisations have usually met with failure. At the same time internally driven enterprises have suffered from lack of funds

and inadequate capacity. The evidence suggests that a role exists for external actors in the development of rural community enterprises, but that attention should be given to issues of dependence, governance and ownership for these partnerships to succeed in the long term: development and exit need to be planned.

One area where such enterprises tend to depart in practice from the cooperative model that persists in Africa is that in the latter a role often is played by the public sector in the governance of the organisation. As noted in the overview of the development of collective organisations in developing countries, cooperatives tend to be connected with or even embedded within government structures. For example, in Malawi, each cooperative is required to have a government appointee on its board. Collective organisations of a more commercial orientation, so-called RCEs are likely to have governance structures free of state involvement, and hence are likely to be freer from subversion by political élites.

As an organisational innovation, the closer link to the private sector than to the public sector enhances the prospects of an entrepreneurial, market-oriented approach rather than a bureaucratic ethos. Donovan *et al* (2008) cite diverse cases in which a range of organisational players is involved in sectoral development. One example is the Ghanaian cooperative Kuapa Kokoo (Box 10):

## Box 10      Kuapa Kokoo

Ghana partially liberalized cocoa markets in 1992. Several community leaders saw an opportunity to sell their cocoa to the Cocoa Marketing Company (CMC), the state-owned single exporter of Ghanaian cocoa. No official support was offered to would-be licensees, as it was believed that this would constrain competition and the emergence of a new private sector. Considerable obstacles had to be overcome in order to obtain a licence to trade. By mid-1993, when regulations were to be implemented for the upcoming season, smallholders attempting to start a new, collectively organised company had been effectively thwarted. While they were looked on favourably by some in CCB, they lacked capital and credibility. At this point, community leaders linked up with two development NGOs, SNV and Twin Trading. Each offered support to the local efforts to launch a new producer organisation. There was a short and intense mobilization: awareness-raising and village-level discussion and the idea of starting a new organisation was followed by an upsurge of local interest in joining the initiative. About 2000 smallholders from 22 villages organised their facilities to satisfy the authorities and committed to deliver at least 100 MT of cocoa beans per village. The cooperative was formed, named Kuapa Kokoo Ltd, with a handful of local leaders representing three regions and with financial backing from a loan guarantee by Twin Trading. Kuapa Kokoo presented a business plan to the CBC to obtain a licence to trade, which was approved.

In 1998, with The Body Shop, Twin helped Kuapa Kokoo set up the Day Chocolate Company. Through the intervention of DFID, who provided another loan guarantee, it was possible to issue one-third of the shares of Divine Chocolate to Kuapa Kokoo. The other investors were Twin Trading (53%) and Body Shop International (14%). 'Divine' fairtrade branded chocolate was launched. With the support of other organisations, including Christian Aid, Divine has secured considerable market penetration through the UK supermarkets. All of the cocoa in Divine Chocolate comes from Kuapa Kokoo and is purchased on fairtrade terms. Divine bought 1,200 tons of cocoa from Kuapa Kokoo in 2006. However, 98% of Kuapa Kokoo's production is sold at commodity prices to the state-run marketing board in Ghana. Kuapa Kokoo invests a fairtrade premium into schools, clean drinking water, mobile medical clinics, and entrepreneurship projects for the significant percentage of women farmers who are Kuapa Kokoo members (60% of the national executive board of Kuapa Kokoo are women). In 2006 The Body Shop donated its shares in Day Chocolate to Kuapa Kokoo giving Ghanaian farmers a 45% stake. In the following year Divine was launched in the US.

Sources: adapted from Donovan, Stoian and Poole (2008) and <http://www.divinechocolate.com/about/default.aspx>

### 5.6.2 *Collective natural resource management organisations*

An increasingly significant form of smallholder association has developed in order to manage natural resources. While this form of association does not necessarily have a commercial focus – although it can be linked to both marketing of natural resource products and environmental management – the dilemmas concerning intra-community

management and relations with external stakeholders have lessons for marketing organisations, particularly regarding smallholder participation in community initiatives.

Exclusion of poor people from environmentally sensitive areas and regulation of anthropogenic disturbance has been the common approach of governments to resource management. This approach has largely failed and new approaches are based on devolving responsibility back to local communities. Community-based natural resource management (CBNRM) is a collective institutional innovation to common pool resources such as land, forest, water, wildlife, fisheries, biodiversity and the economic and ecological systems related to these resources. Community-based management initiatives may be a local response to threats and opportunities and as such are rooted in cooperative economic organisation at the community level; latterly they have become a social or political movement arising from within the wider civil society to address the failure of top-down policy processes, and to integrate better the interests, livelihood capitals and participation of poor people. Like the historic approach to marketing cooperatives, they are increasingly a public policy approach to address the same issues of rural organisation. Community-based initiatives are often hosted or initiated by intermediary organisations such as NGOs that bridge the gap between civil society and local or national government.

The concept is one of devolving resource sovereignty to local beneficiaries, based on two affirmations:

- As a matter of principle, people have rights to share in policy formulation and interventions; and
- in practice, the responsibility for the local organisation is likely to be exercised in a manner that is more sustainable, equitable and efficient when primacy is given not to the state but to local communities.

A third related issue is the funding of the marketing initiatives for commercial products generated out of the natural resources. Together these characteristics and operational issues concern the empowerment of local communities and depend on the effectiveness, efficiency and equity with which policies are designed and implemented.

## **5.7 Participation and adaptation**

There has been an historic tension between external policy interventions and local development initiatives to promote poverty reduction and enhancement of the livelihoods of poor people. Collaborative efforts have been made through participatory approaches (see Bernet *et al* (Albu, M. and Griffith, A. 2006; 2006; Devaux, A., Horton,

D., Velasco, C., Thiele, G., López, G., Bernet, T., Reinoso, I. and Ordinola, M. 2009), through deliberative fora such as the 'stakeholder task force' approach (Chitundu, M., Drogelmann, K. and Haggblade, S. 2009); and through documentation of collaborative supply chain ventures (KIT and IIRR 2008), all of which approaches attempt to overcome various sectoral and institutional barriers.

Community management of natural resources-based activities (enterprise and conservation) give important insights into the participative processes that may enable superior organisational performance at the grassroots level (Markelova, H., Meinzen-Dick, R., Hellin, J. et al. 2009). A fundamental question is whether through devolution of sovereignty, community-based approaches can achieve sustainable community development and economic objectives at the same time. In theory, the economic and social potential through the participatory processes of community-based management is linked to the nature of the goods and services that are provided by collective organisations. As noted, these include:

- economies of scale in transformation (including production, distribution, innovation, finance)
- access to resource base and external services (finance, business development and technical)
- economies of scale in transaction costs;
- possibilities of exclusion through creating barriers to entry (membership) – but which may conflict with community ownership;
- security/society/identity/sense of belonging/consensus; and
- collective coordination efficiencies which can exceed competition efficiencies from market solutions and at the same time overcome the under-provision of public goods such as social development and capacity building, and also resource management.

#### *5.7.1 Participation in 'Bright Spots'*

Community based initiatives can resolve the sustainability-development dilemma. The IWMI report on 'Bright Spots' in African agriculture has highlighted the processes of development of successful enterprises and communities. Bright Spots are described as 'small communities or households that have improved their livelihoods and natural resources significantly despite having degraded biophysical and socioeconomic conditions around them' (Penning de Vries, F. W. T. 2005). The problem of capture of the benefits by local élites is ever-present, and is likely to be compounded where local institutions which lack genuine democratic processes and organisational capacity interact with corrupt intermediary or public sector organisations. The equity of intra-community

processes is of equal significance, and needs to be addressed constantly in promoting all kinds of smallholder farmer organisation.

### *5.7.2 'Fitness' and local adaptation of institutional innovation*

The concept of organisational fit was introduced earlier and comes into play also when considering the relationships between grassroots organisations and actors from the external environment, be they (I)NGOs, civil society, the public sector, or private enterprise. Adopting innovative approaches to policy formulation and rural organisation may help to address obstacles within the external stakeholder environment – including donors themselves. Traditional government ministries responsible for agriculture and pro-poor development, and many (I)NGOs may not have the organisational culture and human resources that are appropriate or necessary to promote participative approaches to grassroots organisational development. New specialist structures may need to be created to undertake this role from within the public sector, cutting across disciplines and organisations and relevant ministries; or specialised organisations can be contracted from the private sector and civil society to link central policy and procedures with practice at the periphery. 'One size', in terms of external initiatives, will not fit all cases: not only must there be 'organisational fit', but also fitness, or adaptation to complex, diverse institutional situations and location-specific characteristics of markets and society.

## **5.8 Key insights**

This section provides an account of a range of farmer associations, their characteristics, interactions with other market participants such as the state, public sector as well as (I)NGOs. By examining specific organisations it is hoped that we can determine elements of success and the causal factors for this success. In the case of NASFAM, a large and complex association including primary cooperatives in its structure which has at its core a well structured and clearly defined boundary between its business enterprises and its developmental and social objectives. It also has a substantial degree of intervention from NGOs and the international public sector. So what makes this organisation successful? Three factors stand out: first, its multifunctional activities, providing credit, training and technological advancement to farmers, second, its strong transparent institutional structure which keeps its commercial and social objectives separate, third, its activism in seeking external markets.

This section also describes smaller organisations whose nature fits more of a traditional cooperative model and yet these organisations are innovating in their approach to management and their interactions with other market participants. The Oromia Cooperative has succeeded in finding itself niche markets to supply and has managed to by-pass traditional routes to external markets by becoming the only direct exporter of its

members' coffee, thereby reducing the length of the supply chain. In these more commercially oriented organisations, the key defining factors here are the lack of government involvement and the emphasis by the organisation on its commercial activity. This conclusion accords with that drawn by Chirwa *et al* (2005) and much of the other literature on farmer association performance and constraints: independence from direct public sector intervention is desirable, but support from other stakeholders over a limited period, and carefully designed to respect the local environment, is essential.

There is also the issue of empowerment and decision making as illustrated in the example of community-based management programmes. The lessons that may be learned from these organisations are that local empowerment and decision making are key approaches to common resource management. How local communities of people organise themselves to successfully manage resources provides insights into management strategies that are useful for market-oriented collective organisations. Two contrasting views sum up the potential of farmers' associations:

- Collective action can work, 'But a healthy dose of realism is needed when considering the applicability and effectiveness of collective marketing. If the incentives and enabling conditions for farmer groups to form and operate successfully are missing, collective marketing will not be profitable or sustainable' (Markelova, H., Meinzen-Dick, R., Hellin, J. et al. 2009: 6). Barham and Chitemi (2009), and Bernard and Spielman (Bernard, T. and Spielman, D. J.) , likewise, from their respective experiences in Tanzania and Ethiopia, are cautious about the limitations to collective models of organisation, and acknowledge a 'threshold' approach to requirements for successful group formation and operation. Indeed, Bernard and Spielman go further to say that 'the burgeoning interest in farmer cooperatives in Ethiopia and beyond is not amenable to the "one size fits all" strategy that is rapidly evolving (p. 67).
- Nevertheless, pessimism about smallholder incorporation in high value supply chains may reflect a lack of innovative approaches by researchers and development workers.

Both theory and empirical experience suggest that in a given development context:

- Few grassroots associations of smallholder farmers can become commercial learning organisations without external support
- Entrepreneurism is essential: there must be a minimum level of local initiative and leadership and culture of social organisation – human and social capital thresholds must be reached, preferably through demand-led provision
- The poorest smallholders tend to be excluded from participation in and/or management of commercially oriented collective organisations

- External intervention is necessary in business development to build on local initiatives through capacity building, physical investments and creation of supply chain linkages to final markets
- Farmer-level associations and higher tiers of cooperative organisations need to be subject to external scrutiny for accountability and performance purposes
- Complementary investments in public goods such as information and communications infrastructure may be necessary – basic physical capital is essential to reduce costs and product losses
- Sustainability requires that an exit strategy be planned
- Direct intervention by government organisations probably tends to create distortions, encourage political patronage, and may be unduly bureaucratic and poorly adapted to local circumstances
- The institutional framework for organisational development should permit and encourage novel forms of association, drawing necessarily on expertise in business management and learning from successful examples from other environments
- The benefits of collective organisation are linked mostly to exploiting scale economies and reducing transaction costs, opportunities for which arise in high value complex markets such as exotic fruits and vegetable exports
- Management challenges are greater for high value, non-traditional exports with complex technoeconomic characteristics than for standardised, bulk or traditional agricultural products
- Equitable rural development may be best stimulated through intervention in bulk pro-poor products and commodities that are produced, traded and consumed locally, giving rise to broader economic multipliers – staples such as cereals and root crops, and other fruits and vegetable for which local markets have always existed or have been developed
- Agricultural production and rural marketing 'thinking' must be supported by 'business thinking' in respect of managerial capacities and organisational structures and development

## 6 *Contractual arrangements: seller-buyer linkages*

The potential for private investment to improve the livelihoods of smallholder farmers very much depends on the type of contractual arrangements and the relationship between the private investors and the rural farming communities. Figure 1 sketched a framework for understanding the interplay between interventions, initiatives and market types, and how cooperative trading relationships can lead to closer market coordination and create potential efficiency gains. The contractual arrangements in smallholder markets can differ between crop sectors and are influenced by prevailing local and global markets. In African markets the seller-buyer linkages are constructed according to local contexts. These contexts vary in terms of the infrastructure available such as road access, storage facilities, sanitation, loading facilities, telecommunications and transport. There are also variations in knowledge and business skills between buyers and sellers. Typically, formalised market information and contract enforcement are weak, therefore the relationship between buyers and sellers is key to the functioning of markets.

This section of the report examines different types of inter-organisational coordination in Africa. What immediately follows are comments on typologies found in the literature. Succeeding section discuss different market linkages in greater detail, using examples from Africa, moving from independent trading through specified contractual formats to more cooperative supply chain linkages arising from different market and institutional players and technological drivers. The final section presents case studies that illustrate the trend toward closer vertical coordination in buyer-driven chains and networks.

### **6.1 Types of seller-buyer linkages**

On typologies, Mighell and Jones published the seminal work on the use of contracts as mechanisms of vertical coordination in the food system in the early 1960s (1963). By vertical coordination, Mighell and Jones meant 'all the ways in which the vertical stages of production are controlled and directed, within firms (by the administration) and between firms (by the price/market mechanism)' (p. 10). The means of vertical coordination include open market prices, government controls, use of different forms of contracts, and integration.

In discussing the different forms of agricultural contracts, they proposed a typology, the significant differences within which lie in the extent to which specified processes or stages in production are transferred between the parties:

- market-specification contracts occur where the producer transfers part of the risk and management function to another for at least one production period;

- production-management contracts call for a more direct participation by the contractor in production management;
- in resource-providing contracts, the contractor also provides inputs, the producer is paid for his management, and the contractor assumes more of the production risk.

These fundamental concepts are the basis for subsequent typologies which have been developed to give recognition to forms of institutional innovation that have arisen in the intervening period. For example, Shepherd (Shepherd, A. 2007) lists a range of types of market linkages between primary producers and diverse types of market intermediaries. On occasions, farmers can market their product directly to consumers at the farmgate or in local farmers' markets. Traders who buy at the farmgate or at market will be local or regional traders. In addition, farmers can sell through a leading farmer, or through a collective organisation, or to an agroprocessor or exporter. Contract farming schemes operate primarily for the more commercially oriented – larger scale, more highly capitalised, more 'professional' farmer. Transactions cost theory, and many empirical studies, suggested that cost and risk reduction are important drivers for both sellers and buyers in determining the chosen marketing arrangements. Efficient forms of exchange are shaped by the degree of development of the institutional environment and the complexity of the product and market system.

The review by Benfica *et al* (2002) outlines different types of arrangements characterised according to the level of vertical coordination between farmers, traders and processors:

- spot market trading - processing/trading with independent producers
- contract coordination - processing/trading with contract farming
- vertical integration - plantation agriculture with processing
- rural association and cooperatives - community integration

Focussing on three major sub-sectors in Mozambique; maize, cashew, and cotton, Benfica *et al* consider the advantages and problems of three common alternative contractual arrangements between farmers and investors which are developed below. Cooperatives and rural associations, they argue, do not fit into the same continuum of vertical coordination. Nevertheless, in Mozambique, NGOs are a chosen vehicle for promoting rural collective organisations by identifying business opportunities, encouraging and facilitating group formation, provision of technology and inputs, and facilitating market linkages, even with large scale processors in contract farming schemes. 'From a poverty reduction standpoint, perhaps the most salient aspect of these arrangements is the local ownership of the processing facilities. This ownership means

that any profits from processing are more likely to be spent or re-invested locally, rather than expatriated or spent on non-local tradables. Thus, consumption linkages, multiplier effects, and potential poverty alleviation are potentially very strong' (2002: 12).

## **6.2 Independent producers**

Spot market trading/processing with independent producers involves transactions between agro-industries and independent smallholders without a contractual arrangement. In this situation, the relationship is a marketing one in which each party makes their own independent decisions based on their knowledge of the market, conditions and preferences. This form of arrangement benefits from flexibility and the ability to respond quickly to market conditions 'on the spot'. Maize, the staple crop in Mozambique, is traded predominantly through independent producers. It is labour intensive and in high demand. Production is dispersed throughout Mozambique and producers sell to traders independently. The problems associated with this arrangement are typical of the high transaction costs, limited market power of producers and poor infrastructure evident in rural marketing in Africa:

- Price uncertainty
- Inconsistent quality
- Unstable supply
- Limited bargaining power of the independent producers
- Lack of reliable storage facilities
- High costs and losses due to inadequate transport links and market information

By way of alleviating some of these problems, contract farming is considered as an alternative arrangement. However, for this to be viable productivity needs to be increased for farmers to take a greater return on their produce, and the risk of default needs to be reduced through stronger contract enforcement. Benfica *et al* (2002) argue that contract farming may be more successful than independent arrangements if certain requirements are met, such as an emphasis on premium prices for quality produce, a strengthening of the legal system, facilitating the development of farmer associations including literacy and capacity building programmes in rural areas. (These characteristics are often enjoyed by organisations, including traditional cooperatives, which have access (often donor-supported) to higher value markets and fair trade, or 'ethical', premia).

The cashew trade in Mozambique is also dominated by independent producer arrangements, under which, it is the processors who face the barriers to success such as:

- Competition with exporters
- Inconsistent quality and supply

- High dispersion of sources
- Lack of capital

For the farmers, cashew production is a high risk activity and characterised by unreliable income generation (Benfica, R., Tschirley, D. and Sambo, L. 2002: 43). Farmer productivity is low due to a lack of inputs, in particular disease control. The case of cashews is illustrative of the significant impact of the technoeconomic complexity of both product and processing on marketing arrangements and the constraints to market access of the poorest smallholders. Given sufficient support, it is evident that farmers can become organised and trained to deal in higher value markets, but the appropriate organisational models may be complex and non-replicable (Hellin, J., Lundy, M. and Meijer, M. 2009), and capacity building interventions therefore costly.

### **6.3 Contract farming**

Contract farming entails an agreement between the farmers and processors. These agreements can be formal or informal. Farmers may benefit from services provided by the processing firms such as credit, seeds, fertiliser and technical assistance. This type of contract has developed in Sub-Saharan Africa as a response to imperfect markets and poor service provision (Benfica, R., Tschirley, D. and Sambo, L. 2002). Contract farming may nevertheless result in the exclusion of the poorest households who lack the assets and resources to overcome entry barriers.

Cotton production is characterised by a high need for inputs and processing, thus making contract farming arrangements most common. However, there is a high degree of credit and input market failure. The cotton market is hindered by the following problems:

- High default rate on seasonal credit for production due to price competition in the output market
- High default rate due to weak legal system causing poor enforcement and loan recovery
- Farmers' dependence on cotton companies for inputs and finance
- Poor market information and high infrastructure costs

For the cotton sector, the author of the study argues that it is unlikely that alternative contractual arrangements would be more beneficial. However improvements, can be made through strengthening farmers' bargaining power in the market by encouraging the formation of collective farmer associations (Benfica, R., Tschirley, D. and Sambo, L. 2002: 45).

The cotton sector study by Poulton *et al* (2004) in Ghana, Mozambique, Tanzania, Uganda, Zambia and Zimbabwe examined the phenomenon of small independent sellers and their relationships with buyers, which were difficult to characterise as just one type of contractual arrangement. However, they explored the problems identified by Benfica *et al*, highlighting the interplay between the prevailing market structure and optimum market coordination mechanisms between producers and the large scale buyers and processors. They identified three prevailing patterns of farmer-buyer linkages:

- 'concentrated, market-based' sectors which were successful in meeting common coordination challenges while still maintaining reasonable prices to producers
- local monopoly systems with direct purchases which offered a workable solution to coordination problems but lacked any competitive dynamic
- sectors with multiple small players which were fiercely competitive, but lacked effective coordination.

They concluded that different sectoral structures are observed in the different study countries, with a different role for the state appropriate for each organisational and institutional context, which depends on the recent history and policy framework. Consequently, different types and levels of institutional intervention were necessary to facilitate exchange and create the information about relationships that reduces transaction costs: 'All sector types, therefore, face their own particular challenges in striking the competition-coordination balance' (Poulton, C., Gibbon, P., Hanyani-Mlambo, B. *et al*. 2004: 535).

Other literature on improving contractual relationships points to the role of cultural ties and suggests that social relationships can have a positive effect on agricultural trade. Benfica *et al* (2002) describe the role of ethnic ties between Mozambican traders and Indian buyers in the cashew sub-sector in decreasing transaction costs of trade. Social relationships have also proven to be a factor in successful economic exchange between markets actors in Madagascar (Fafchamps, M. and Minten, B. 2002). The importance of interpersonal relationships have been shown to have a positive impact in the areas of credit provision, risk sharing, trade flows, circulation of information, market opportunities, risk mitigation, market regulation and the regularity of trade flows (Barr, A. M. 1997; Fafchamps, M. and Lund, S. 1998). Fafchamps and Minten's research in Madagascar indicates that successful traders are successful because of the social networks that they have developed: 'The capacity to successfully join networks of solidarity may well be critical to their long-term prosperity as it shelters them from some of the risks of business and enables them to invest more, grow more rapidly' (1999: 30). In a later paper they argue that improving market efficiency would rely on the

development of 'supportive institutions' that would favour social networks built on trust (Fafchamps, M. and Minten, B. 2002: 203).

## **6.4 Enhanced private sector supply chain linkages**

This section aims to outline some of the farmer-private sector strategies that have emerged as a result of changing contexts in global markets.

### *6.4.1 Supply chain networks*

The institutional mapping of farmer associations in Malawi in an earlier section highlighted the complexity of the organisational environment, but perhaps underplayed the significance of linkages between smallholder associations and the private sector. There is a growing phenomenon of specialization in multi-agent supply chain arrangements whereby small-scale farmers engage with multiple stakeholders from both public and private spheres. Among others, two case studies of successful collaborations can be found in Tanzania and South Africa. In South Africa, Thandi group, a wine and fruit group has collaborated with Capespan an exporter who provides mentorship, financing, skills transfer and capacity building of the Thandi initiative.

In Tanzania, with the assistance from a development agency, the Mara Smallholder Horticultural Project has formed itself into marketing groups with direct links to suppliers of horticultural produce for hotels and camps. With support in the areas of knowledge and skills each group currently has a vegetable marketing committee that collects produce from individual farmers, grades, packs and delivers to the hotels. Prices are pre-agreed with the farmers. The potential to link agricultural production to other economic sectors such as tourism has been noted elsewhere (Donovan, J. and Poole, N. D. 2008), although the likely extent of the impact of such approaches to rural poverty reduction in Africa are probably limited.

Recent commercial initiatives have also come about through the involvement of NGOs. A case in point is NASFAM, although at a smaller scale, local NGOs can have a facilitating capacity in making buyer- seller linkages more effective. However, Shepherd (2007) illustrates that this may carry risks, particularly of dependency. In South Africa for example, an NGO facilitates a link between a pulping company and small-scale contract farmers. The NGO manages a program which aims to commercialise timber production on subsistence farms. Farmers enter in to a purchasing agreement with the company and in return they receive assistance in the form of tree seedlings and an interest free loan for planting, maintaining and weeding the plantation. Farmers also benefit from technical assistance from extension officers. This assistance is managed by the NGO on behalf of the company. Despite high returns for farmers, the level of dependency is

possibly too high and too costly for the company. Shepherd considers this high level of dependency unsustainable.

Commenting on the feasibility of small farmers accessing new supermarket supply chains in Kenya (in particular fresh fruit and vegetables), Neven and Reardon (2005) consider three areas in need of attention:

- creation of efficient supply chains
- increase in scale of production and marketing among smallholders
- high working capital requirements to meet post-harvest specifications, and organisational costs

Neven and Reardon argue that the supply chains need to be redesigned to incorporate the 'creation of new market facilitators' such as outgrower schemes. They advocate the development of new, smaller farmer markets near local residential areas that are able to facilitate an effective procurement system.

In other areas direct links between farmer and retailer have been possible and successful through initial support from local NGOs. Small-scale farmers in southwest Uganda are now supplying an urban fast-food outlet. Working as a group, farmers are able to stagger planting times in order to be able to achieve regular and standard supplies of potatoes. Relationships between the farmers and the retailer have been strengthened through personal visits. This has been essential to the success of the contract as trust is achieved through communication and interaction between all parties and enabled the NGO to have a lesser role in the continuing buyer-seller link. For a depiction of the supply chain for potatoes to Nando's which illustrates the complex institutional arrangements, see Kaganzi *et al* (2009).

We have noted on various occasions that smallholders find access to high value non-traditional export markets very demanding. Nevertheless, Narrod, Roy, Okello, Avendaño, and Thorat (2009) conclude from their study of collective action and public-private partnerships in Kenya and India that pessimism about smallholder incorporation in high value supply chains may reflect a lack of innovative approaches by researchers and development workers: in their cases, public-private sector collaborative actions enabled farmers to overcome significant food safety barriers. But the responsibilities of each type of player (public and private sector) was distinct: farmers need to establish good commercial linkages with buyers; the government has a role in correcting specific market failures, without otherwise intervening on commercial chain activities.

#### 6.4.2 *Philanthropic initiatives*

Market interventions for supply chain development are coming from an increasing diversity of sources compared with the historic state-managed initiatives. The provision of alternative sources of capital enables the development of supply chain linkages through market-oriented interventions. One new type of organisational player is the philanthropic organisation, parallel in some ways to the NGO sector. An example of this form of supply chain is the Rwandan Farmers Company. Owned in trust by The Clinton Hunter Development Initiative (CHDI) all profits are returned to the farmers. With a \$100 million investment over 10 years, CHDI seeks to act as a catalyst for sustainable economic development. It works with national governments, communities and other stakeholders to assist with production as well as initiating social programmes in the areas of health, water and sanitation. In the case of Rwanda, CHDI assisted the government in the purchase of fertiliser, which is reported to have resulted in an increase in coffee crop yields of 240%. The company then aided 6,500 coffee farmers in setting up Misozi Coffee Company which by the end of 2007 had increased its sales by 30% and production by 20%. The Misozi Coffee Company is now part of a larger group of farmers who market their own coffee under the brand name Rwandan Farmers and sell direct to the retailers in the United Kingdom. This way, farmers receive 100% of the profit.

A similar approach is now being replicated in Malawi where cotton and wheat are important commodities. Such intervention in staple foods rather than high value export crops is novel, even though market access is more simple and transaction costs lower (Hellin, J., Lundy, M. and Meijer, M. 2009). For wheat, a strong domestic demand has meant that Malawi imports 80% of its wheat, despite being a country capable of producing local wheat. CHDI has assisted the Neno Hills Farmers' Association in gaining access to funding which has enabled them to purchase improved wheat seed and fertiliser. CHDI has bought the harvest of a local wheat miller at a 50% higher price than received in the previous period. The role played by philanthropic organisations in acting as a catalyst for change in markets is an interesting one as it serves to bring external investment and technical support with a sense of social responsibility.

#### 6.4.3 *Commercial interventions*

A recent issue of the journal Food Policy was dedicated to research on commercial collaborative supply chain activities in different regions around the world. Narrod *et al* (2009) examine the response of farmer groups to increasingly stringent food safety requirements. Increased concerns for food safety has resulted in organised producer groups formulating new strategies for coping with these demands. In the developing

world smallholders are faced with increased market demands yet continue to be constrained by issues of scale and lack of information. As noted earlier, producer groups have been shown to overcome these issues through collective behaviour and coordinated actions. Narrod *et al* (2007: 10) outline clearly the role of collective action in overcoming the challenges of food safety standards:

- Procurement of information about markets and the process of contract formation
- Dissemination of information relating to food safety standards
- Undertaking lumpy investments
- Procurement of cheaper inputs through bulk buying
- Accessing extension services
- Establishment of traceability systems
- Maintaining a group monitoring system
- Collective marketing leading to reduced costs and uncertainty
- Grading and certification
- Collaboration with marketing experts
- Maintaining a group monitoring system

Despite the exclusion of many smallholders from supply chains that have stringent food safety standards, some smallholders have succeeded in gaining and maintaining access to this market. Narrod *et al* (2009) consider the innovative institutional mechanisms that have aided smallholders retaining these market linkages, namely various internal collective organisational initiatives combined with external private-public partnerships. In Kenya, farmer groups have been the dominant link between smallholders and the market. During the 1990s farmer group size was reduced to fewer than 30 per group in order to facilitate third party monitoring. Farmer groups also began to monitor themselves. This was achieved through a system of penalties for violation of rules. Smaller groups meant that it was easier to train farmers and use self-monitoring as a mechanism to keep costs down for buyers. The way in which membership was organised was also transformed. Membership became controlled with new members only being accepted by recommendation of existing members and then being subjected to a vote by all members based on their conduct in other social or economic organisations. The groups are governed by an elected committee that enforces rules and negotiates contracts with exporters. The farmer groups are financed by member contributions. Narrod *et al* (2009) argue that these adaptations to the traditional organisation of farmer groups enable them to participate in more complex food markets.

The second mechanism, public-private partnerships, has assisted in the setting up of farmer groups. The Government of Kenya in partnership with the Japanese International

Cooperation Agency (JICA) established a company to mobilize and recruit smallholders groups. Other public- private partnerships include the Business Management Service Development Programme (BMSDP) run by DFID and the Horticultural Crops Development Authority who together trained horticulture service providers to serve smallholders. NGOs have also formed partnerships with private firms to train and provide financial assistance to farmer groups to enable them to secure certification.

Barham and Chitemi (2009) considered key factors in the success of farmer groups in Tanzania to be group maturity, strong internal organisation and functioning group activities. They also conclude that a strong asset of natural capital – enabling satisfaction of the technoeconomic demands of product markets - was essential to improving market opportunities. Their study examines Agricultural Marketing Systems Development Programmed (AMSDP), a planned change initiative in Tanzania which aims at improving smallholders market access through reforming the regulatory and taxation systems; (2) improving market infrastructure; (3) establishing agricultural marketing information systems; and (4) strengthening producer groups and creating market linkages.

#### *6.4.4 ICT innovations and e-markets for smallholder inclusion*

Information and communications technology is undoubtedly having a massive impact in developing countries. Liberalisation has led to a dramatic expansion of radio services in many developing countries, with content often well-targeted to local users. There are many initiatives to put in place new ICT such as internet access, satellite, cellular and mixed information and communications technologies. Such interventions often concern the provision of market information and the linking of sellers and buyers. Some ICT initiatives derive from donors, such as the Rockefeller-funded Kenyan Agricultural Commodities Exchange, KACE (Adesina, A. 2004; Mukhebi, A. 2005).

MISTOWA (Box 11) enables users to access web-based market services: offers, transport, and storage and market news, in addition to prices, by commodity, region, country or market:

## **Box 11      E-information systems for farmer and trader organisations**

Following the structural adjustment-induced redesign of West African cereal boards at the end of the 1990s, RESIMAO (Réseau des Systèmes d'Information de Marché de l'Afrique de l'Ouest) was created as a network of market information systems for West Africa in 2000 in Bamako, Mali, now serving various other Franco- and Anglophone countries. The primary function is regular price data collection for a range of crops in hundreds of national markets which is undertaken primarily by national public sector staff. Data currently available on the internet sites are maps, regional price averages and locations, prices for the last 4 days, and network facilities to plot dates and analyse trends. The intention is to use diverse media for dissemination – GIS, internet-based systems, bulletins, radio, TV and SMS. One of the partners is MISTOWA (Market Information Systems for Trader Organisations in West Africa), a 4-year regional project begun in 2004 and implemented by IFDC and mainly funded by USAID. Its aim is to strengthen the capacity of farmers and traders to access and use the data, with the ultimate aim of promoting agricultural trade in the ECOWAS region...

Source: Poole (2006: 35)

Dramatic increases in the level of connectivity in telephone connectivity have occurred since the liberalisation of the telecommunications sectors in many developing countries that have permitted the expansion of cellular networks. Probably the biggest impact of technological innovation has been the use of cell phones to increase access to marketing, anecdotal reports of which testify to an extraordinary growth in farmer-market communication. Focusing on specific IT interventions may miss the point that organic growth of this commercially-driven market has been dramatically important. Nevertheless, doubts persist about the extent and speed of rollout of new technologies to remote areas with low populations and difficult terrain, and also about the inequity effects that may result: such interventions are unlikely to be 'pro- the poorest', those remote and small-scale farmers and associations with limited economic and social assets.

ICT innovations and electronic marketing is generally targeted at individual farmers. While there are general limitations to such interventions, particularly if they are heavily donor-funded, there are also questions about whether these approaches to market development can be of help to the poorest farmers and to smallholder farmer associations. Nevertheless, anecdotes about the experiences of farmer organisations in Malawi suggest that making a computer and internet connection available to each organisation would be of massive assistance in improving internal organisation and business management, and access to external markets. In these respects there is a considerable potential role for private sector donors and investors, coupled with training in business management from civil society and third sector organisations.

## 6.5 Case Study: Twin Trading Partnership

Supply chain development initiatives driven by private capital have significant potential for scale and replicability, and therefore poverty reduction impact. Many have begun through the intermediation of NGOs and some, such as the Kuapa Kokoo-Divine Chocolate enterprise in Ghana have been converted into viable commercial enterprises, independent, it is hoped, of donor support, and therefore sustainable (Donovan, J., Stoian, D. and Poole, N. D. 2008). To the extent that such initiatives can be driven by private capital, the impact can extend beyond the scope of donor-driven market access projects. Apart from Kuapa Kokoo, various examples exist, and this section introduces one such case.

The Twin Trading Partnership is owned by small scale-producer organisations and works with 39 producer groups in the sectors of coffee, cocoa, sugar and nuts across Asia, Africa and Latin America. As well as working with producer groups, Twin is one of the main companies behind other 'ethical' organisations such as Cafédirect, Agrofair, Divine, Liberation and OKÉ. Together with the Fairtrade Foundation, Oxfam, Root Capital, Hivos, World Bank, Fairtrade Labelling Organisation (FLO), Twin invests in supply chain management, strengthening producer organisations, fair trade brands, information and knowledge generation with the aim of influencing policy and increasing market awareness amongst producer partners.

Twin has 24 farmer organisations with over 1000 cooperatives representing over 163,000 farming families. Twin Trading offers the following business support services:

- Planning and forecasting
- Contract administration
- Logistics and shipping
- Quality control
- Price risk management
- Pre-finance
- Market analysis

Twin also runs a Producer Partnership Programme that aims to strengthen the internal management systems of member producer organisations (Box 12):

## Box 12      Features of the Twin Producer Partnership Programme

- Governance and organisational strengthening: with the management and elected leaders of producer organisations providing workshops, advice and mentoring on cooperative practice, leadership, internal communication, understanding the market and business context
- Business basics: supporting producer organisations to develop business skills and systems for accounting, harvest planning, basic quality control. This is achieved through direct coaching and consultancy and the design of easy-to-use tools
- Certification: assisting producers to maintain Fairtrade and organic certification by providing information and training on standards, and giving direct support before and after inspections. Twin has also developed internal control systems and lobbies certification bodies to ensure that standards work for smallholders
- Planning and evaluation: Twin supports producers in the areas of operational planning, strategic planning, and evaluating individual activities and events. This is achieved through workshops, coaching and consultancy
- Price risk management: helping producer organisations develop risk management tools and strategies. Twin provides training on risk management at a basic and advanced level and offers regular market updates and analysis
- Quality control systems: providing technical support and advice to nut and cocoa producers to improve product quality and develop quality control systems. Twin has also developed training resources and workshops on quality control systems at all levels including cupping workshops for farmers, and zoning programmes to identify high quality coffees
- Quality management systems: increasing efficiency and sustainability in producer organisations enable them to manage different voluntary and obligatory market requirements in one integrated management system
- Training of Trainers: Twin has developed participative and dynamic training methods and is developing an on-line learning resource for its producer partners
- Advocacy and Networks: By representing the interests of producers and developing producers' capacity to defend and promote their interests in key arenas Twin works to increase producers' voice. Because the producers have a majority stake, Twin represents the interests of small-scale producers in the market...

Source: <http://www.twin.org.uk/PPP#Governance>. Accessed 15 April 2009

A subsidiary of Twin Trading is Liberation. Liberation works with 22000 smallholder producers in Asia, Africa and Latin America. In Malawi, Liberation buys from the Mchinji Association of Smallholder Farmers, MASFA, as subsidiary of NASFAM. Approximately 30% of MASFA's output is Fairtrade. In Mozambique, Liberation deals with the cooperative Ikuru which has 8500 members organised into smaller collectives producing peanuts, cashews, sesame and beans. Members of Ikuru also produce for the organic market. The producers own a collective share of 42% of the company.

The company strategy is based around member ownership and supply chain management. Its website compares the following supply chains (Box 13):

### **Box 13 Liberation perspective on supply chains**

- The traditional supply chain: you have a farmer or farmers' co-operative which sells goods to the middleman, who sells them to a local exporter, who sells them to an importer in Europe, who then sells them to the retailer. Everyone along the way demands some margins that affect the price you pay for the finished product which does not take into account the real cost of production and living expenses of the farmers.
- The fair trade supply chain: replaces the middleman and the exporter with a farmers' co-operative who then sells their goods directly to an importer in Europe, who sells on to the retailer. As you can see by shortening the supply chain more profit stays with the farmers since there are less margins to be paid, as well as all the knowledge from exporting their own products.
- The Liberation supply chain: takes fair trade to the next stage bringing producers right up the supply chain replacing the last link, the importer, through a farmer- owned brand, which empowers smallholder producers by involving them in ALL decisions taken and maximising THEIR profits. Through Liberation's supply chain farmers sell DIRECTLY to the retailers in Europe.

Source: adapted from [http://www.chooseliberation.com/about\\_us/](http://www.chooseliberation.com/about_us/). Accessed 17 December 2009

With these organisations, the focus is on ensuring that farmers get access to markets and that the company has access to producers who are able to fulfil their contract. Twin Trading describes itself as a commercial business. Not enough is yet known about the commercial orientation, sustainability and poverty reduction impact of such new initiatives: reliable literature is scarce, but there is potential to develop primary analytical research in this area and also action research by donors to design and evaluate alternative models.

## **6.6 Key insights**

These examples serve to reiterate some of the points already made about organisations

- Firstly, context specificity prevails: organisational types and institutional frameworks and market linkages are significantly and historically path-dependent, and of these, market linkages above all are influenced or determined by the technoeconomic characteristics of the specific agricultural products concerned.
- Also, it is self-evident but easily ignored that the private sector processing, manufacturing and distribution sectors need raw materials, and the cases presented illustrate how commercial linkages can be formed which have the effect of linking producers to markets on satisfactory terms. Partnership programmes such as that

operated by Twin can provide the essential capacity building to create viable business relationships in competitive markets. While little attention has been given to private firms' efforts in exercising corporate social responsibility, it must be acknowledged that there may be valuable examples also from major agrifood firms such as Nestlé which are beyond the scope of this paper.

- Nevertheless, it is not philanthropy but profitability that drives the private sector, nor that partnership programmes such as Twin can necessarily be mainstreamed.
- Examples of the impact of new technology illustrate how markets can be expanded to include smallholders, even though there remain barriers to entry by the poorest. But new technologies such as IT – and maybe other technological and institutional innovation – may be best introduced not through project-type interventions but as constituents of an enabling framework with public good characteristics. Public-private sector partnerships are likely to play a part in the delivery of such public goods.

## 7 *Conclusions*

This paper has sought to review the various types of organisational forms of farmer associations and the different relationships that they have with other market participants. The outline of the historical emergence of farmer associations in Africa has illustrated the diversity of group types, ranging from small informal farmer groups to large farmer cooperatives, different sources and levels of initiatives and interventions, a variety of contexts, and changing policy approaches. What unite these groups are the challenges that are posed by the context of the African market in today's global agricultural economic climate, and the need to build effective enterprises in local markets that can multiply development for wider poverty reduction.

### **7.1 Recapitulating collective weaknesses**

It has been noted that traditional farmer organisations face a number of internal and external difficulties and contradictions. Internally:

- the question of origin, be it a grassroots initiative or an external intervention plays an important part in shaping the structure and performance of a collective organisation;
- there are often mixed and sometimes conflicting objectives;
- often there is a lack of start up finance and capital accumulation, weak internal management capabilities, opaque governance and accountability;
- skills fall short of adequacy making organisational capacity inefficient.

External challenges include

- high barriers to entry and asset threshold requirements prevail in competitive markets - strict food standards, certification requirements, and changing consumer preferences and demands.
- unsupportive public policies that may constrain innovation, lack of government or political backing – or on the contrary, political patronage and interference;
- inadequate transport and communications infrastructure;
- weak business, legal and regulatory structures.

Regarding the donor environment:

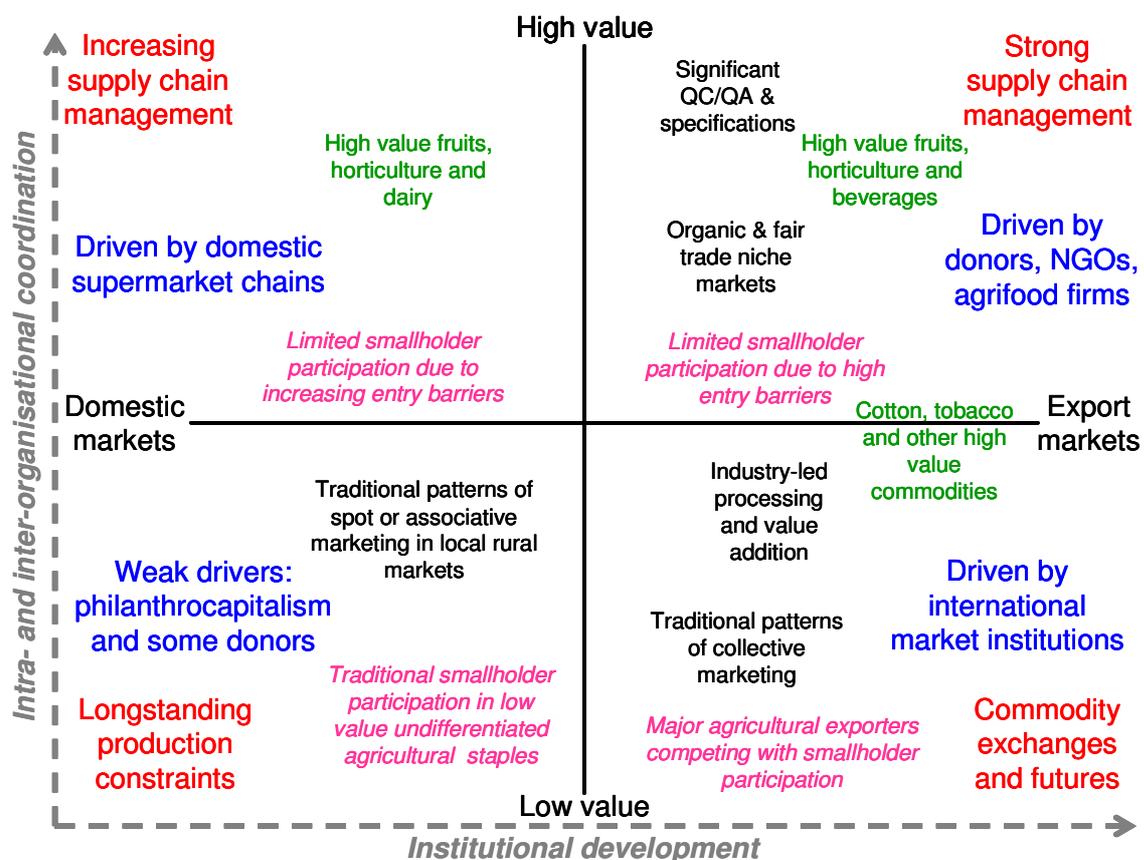
- intervention can be ideologically driven and excessive;
- initial support levels may be unsustainable;
- insufficient recognition may be given to the long-term nature of organisational learning and capacity building.

## 7.2 Diagnostic and summary framework

The framework offered at the beginning suggests a typology of two types of internal initiatives and/or external interventions, institutional and organisational innovations, which can usher in a more entrepreneurial and more focused collective organisation. Broadly speaking, these innovations should be aimed at redressing the management and organisational weaknesses that impair commercial performance, and reducing the transaction costs that cause weak or missing markets in Sub-Saharan Africa.

By means of a summary, the following conceptual map of organisations, market linkages for smallholder farmers, and intervention patterns (Figure 5) is a first effort to provide a framework for analysing potential interventions. Apart from the organisation itself and the external market and institutional environment, the product and market types in respect of technoeconomic characteristics and potential for poverty reduction are important dimensions in the developing agricultural economy which map, albeit imperfectly, onto the dimensions of institutions and organisations presented in Figure 1.

**Figure 5 Mapping markets, interventions and initiatives**



Source: authors

### *7.2.1 Products and markets*

There is a relationship between the product and market type, and the form of market organisation and contractual relationships. Many of the initiatives and interventions discussed have been concerned with the bottom right, top right and increasingly the top left quadrants: these are characterised by higher level of business organisation and/or stronger institutions. But smallholder participation in these markets is limited because of the weaknesses summarised above. Where smallholders do participate, often it is the result of specific and costly interventions, related to 'complex' (high specification) products requiring sophisticated linkages to niche markets that are not really viable opportunities for the majority of poor smallholders. The sustainability of such initiatives is more likely if they are led by the private sector rather than donors and civil society, although the contribution of supporting organisations may be very helpful. However, these success stories are not easily replicable and upscaleable.

Markets in the bottom left quadrant, arguably most important for wider poverty reduction, have enjoyed little attention: these are staple foods such as cereals and roots with little value addition entering traditional rural market systems. These sector have the potential to boost the availability of local food supplies (obviously not the same as entitlements). Opportunities exist for a multiplying effect within the local economy as increased production leads to demands for labour, and marketable surpluses require transport, storage and processing services.

### *7.2.3 Intervention options*

This diagram aids in our understanding of farmer organisations and the different markets in which they participate. We can consider commercial institutions, (I)NGOs and public sector initiatives to be operating most effectively in the bottom right, top right and top left quadrants. Notable innovation has occurred which is the development of retailer-led national and international market or supply chains. But these link to growers of higher value products who are the agricultural middle class, and employ contract farming models. There are some exceptional cases of collective enterprise, usually with considerable external management and financial support. Generally these are sectors and initiatives are the 'low hanging fruit' of agricultural marketing in East and Southern African countries. These markets do not exhibit sectoral market failure. Therefore, replicable, upscaleable sectoral investment is unjustified and probably would tend to crowd out the viable private initiatives. They do not reach the mass of smallholder farmers.

Yet, the real challenge for pro-poor development initiatives is to reach the poorest (agriculture-dependent) smallholders with the lowest level of household assets who cannot easily turn to income earning opportunities other than agriculture; the bottom left quadrant. Targeting these farmers means innovations in markets for bulk staple commodities grown for incomes and consumption– for example in Sub-Saharan Africa, for products such as cereals and starchy staples. It is in this quadrant that local and regional markets can be strengthened, and where historical and 'outmoded' patterns of intervention (such as marketing boards) have been least supplanted by organisational and institutional innovations such as the more entrepreneurial initiatives by intermediary organisations, the more sophisticated commercial supply chains, the more advanced trading mechanisms such as futures and electronic markets.

We have cited approaches and interventions such as CHDI, and grain warehousing systems, and some new production technologies are examples where the domestic low value 'staples' sector has received support. CHDI works in the export sectors of coffee and cotton but is also beginning to intervene in domestic sectors such as wheat production in Malawi. The initiative has aided wheat farmers to access capital for inputs and assisted in the organisation of 1200 wheat farmers. CHDI has also negotiated higher prices for wheat. The cassava value chain in Zambia is also receiving sector-level support, with the aim of linking smallholder production to the many potential industrial markets. Another example is potatoes (admittedly to a high value market) in Uganda. There are important lessons from the other quadrants, such as the Twin Trading partnership scheme and Kuapa Kokoo, which suggest how business development services and organisational development can be shaped to serve the poorest. The Liberation approach to participatory processes has proved to be a valuable experience, even if inclusion of the poorest on a widespread scale is unlikely. Large numbers of farmers can be involved, but these linkages are still 'point' initiatives rather than sectoral interventions. It is in this quadrant that markets in Africa are least perfect, or fail, with negative consequences for local food security and wider economic development.

Institutional and organisational innovation can be:

- Group performance and auditing – much is known about how and how not to initiate farmer groups. External assistance is needed in building sustainable business models. One potential intervention to improve a) the institutional environment and b) business performance, is the creation of a national organisational capacity or 'ombudsman' to monitor and audit grassroots organisations and to improve organisational accountability;

- An ombudsman-type organisation can also be tasked with coordinating the regional or national delivery of the needed complex of business development and information services, with the aim of managerial capacity building. Together with the auditing role, higher levels of managerial skills can shorten the duration of the organisational learning cycle, and attenuate the wasteful experience of 'phoenix' organisations and 'not-so-creative destruction' among farmer groups. Independence from Ministries of Cooperatives is important, to ensure an entrepreneurial rather than a bureaucratic skill set and culture;
- Cooperative innovation – relaxing the Rochdale/ICA Principles to introduce into cooperative governance higher level management capacity and more external finance. New models of cooperation may reconcile or simplify the complex incentive structures and agency problems within collective organisations. Again, local business and legal skills are needed, as well as new legislative frameworks for associative organisations;
- Finance – sources additional to members and donors are equity investments by philanthropic organisations and bond issues to private investors which will help to overcome capital constraints and yet not necessarily dilute member ownership. On the other hand, new modes of investment may enable investors to 'leverage' improved management capacity;
- Contracts - adopting written standard form contracts may furnish two major advantages over existing verbal agreements. The first is the planning purpose: it may be that the greatest value of standard contracts is to reduce uncertainty by specifying the terms of an agreement; second, adoption of written agreements may boost the informal 'rules' of business attitudes and ethics;
- Sectoral initiatives – drawing on the interprofessional model, the formation of industry 'umbrella associations' for promising sectors can replicate the efficiencies sought through commercial supply chain management driven by private sector firms: functions such as sharing of information, participatory problem diagnosis, joint investments, contractual clarity and informal remedial mechanisms.

#### *7.2.4 Entrepreneurial characteristics of the farmer group*

Examples from the literature illustrate that factors such as group size (Narrood, C., Roy, D., Okello, J. et al. 2009), asset endowments, functioning group activities and strong internal organisation (Barham, A. and Chitemi, C. 2009) affect the success of farmer groups in effectively participating in markets. Other work highlights the skills base necessary to ensure sustainable market linkages (Shepherd, A. 2007). Another area that has been illustrated in the literature is the degree to which groups can respond to changing consumer demands. This has been illustrated in the case study of the Oromia Coffee Farmers Cooperative Union which made an early entry into the fairtrade and

organic overseas market and become a direct exporter. With a threshold level of entrepreneurial skills, such farmer groups can become responsive businesses.

#### *7.2.5 Focus on business: re-envisioning cooperatives*

A further issue regarding the structural management of farmer organisations is the need for clearly defined boundaries between the organisations' social responsibilities to members and its commercial aspirations. Social empowerment must not be confused with economic empowerment. One organisation that has achieved such clarity through structural means is NASFAM. An important characteristic of NASFAM is how it reflects a complex evolution of the cooperative model similar to that in European countries with a strong cooperative tradition, and elsewhere, such as Fonterra. While at grassroots level the association has cooperative characteristics, commercial and other entities have been created to handle functions that are typically circumscribed by the traditional cooperative structure, the commercial and business services functions. Democratic characteristics are retained to varying degrees.

To sum up, organisational and institutional innovations have enabled the following:

- exploiting flexibility in the regulatory environment has permitted the development of innovative management structures that overcome management weakness by introducing outside skills;
- curtailing the democratic principle that permits inertia has created new stakeholder incentives, and ensures that participation are rewarded;
- with the semi-separation of the commercial activities and prioritisation of the commercial objectives, enterprise and performance have flourished;

Moreover, the Achilles heel of collective enterprise, capital raising on a significant scale, has become possible by:

- increasing member investment, for example in proportion to throughput or equity (in the New Generation Cooperative model) and
- securing other forms of investment (in the European and New Zealand model); and in a few cases in Africa, by creating loan guarantee funds, issuing bonds, and providing insurance for collateral

Where institutional innovation has not occurred – in many developing economies – the organisational model is still beset by the familiar weaknesses of inadequate management, élite capture, inefficiency, complex and conflicting objectives, lack of accountability, undercapitalisation, resulting in basically poor business performance.

### *7.2.6 The role of external players*

(I)NGOs, Government, private firms, philanthropic institutions, partner agencies all have a role to play in facilitating the movement of commodities or produce from farm to market. However, what is apparent from the literature is that the potential for these external players to have a positive and sustainable impact on farmer groups may depend on their coordinated ability to shift the focus from production to market interventions.

The development of farmer organisations in many countries in Africa will continue to depend on external players for investment, equity, management and technological inputs. What is necessary is a realistic timeframe? Achieving sustainability is a very long term process: if 'economic sustainability', or organisational maturity means 'independence of outside agencies', then considering the common trajectory of farmer collectives, such initiatives may take years or decades to reach maturity. They suggest a wide range of measures that might begin to hasten this process.

### *7.2.7 The supply chain*

Creating links between farmers and traders, importers or even retailers, thereby cutting out middlemen and maximising profit margins for farmers is one approach common to the fairtrade sector and is also utilised by philanthropic institutions. Supply chain shortening is usually combined with modifications in the structure of the organisations, skills and management capabilities, processing and marketing. Such chain or sectoral approaches are sometimes rooted in an adversarial approach to marketing and contractual relationships, and do not necessarily reflect the positive and sometimes essential functions of market traders, nor the principles and practice of collaborative and cooperative modern supply chain management.

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