Can value chain development create rural employment and alleviate poverty?

By Hans Posthumus[1]

International development initiatives increasingly focus on economic growth and poverty alleviation by improving access to existing markets for poor producers and consumers and make the benefits of well functioning markets more widely accessible to the poor. Value chain development is one of the major tools therein. This article introduces the changing agricultural context and factors influencing rural employment. It describes the increasing casualisation and feminisation of labour as well as increasing inequalities within chains. It concludes that value chain development does not automatically leads to employment creation, but that there are certainly opportunities for employment creation if this would be made explicit in the selection of sub sectors and value chain development interventions.

A value chain can be described as the full range of activities necessary to bring a product from its conception to its end use including its disposal. A value chain is often defined by a combination of the raw material and the market, e.g. organic tomato juice for Italian food retailers. Value chain analysis allows understanding (international) competitive challenges, to identify relationships and vertical coordination mechanisms, to understand how chain actors deal with power and who governs the chain. Developing value chains is often about improving access to (new) markets and ensuring a more efficient product flow while ensuring that all actors in that chain benefit equally in relative terms.

Recent Developments in the international agribusiness sector

Three main factors have changed the structure of the agribusiness sector worldwide (Humphrey, 2005).

- Large supermarket chains have emerged and gained an important share of international markets. From a large number of rather small retailers focusing on selling products supplied by others, we now see a small number of powerful giants that dominate the market and determine what needs to be produced and under which conditions.
- Increased concentration is also taking place at various other points of the value chain including input suppliers and food processors.
- A third important factor is the increase of global standards, mandatory by the public sector or set by companies that determine production standards and increase entry barriers.

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- *The five largest food chains in Europe increased their share of total retail food turnover from 13% in 1990 to 26% in 2000. The top five food retailers in the US increased their share of the United States market from 27% in 1992 to 43% in 2000.*
- *Just four supermarket customers account for 13% of the sales of Unilever, one of the world's largest producers of food and personal care products. For the food and tobacco industry as a whole, the mean concentration ratio rose from 44% to 53% and the top 100 companies increased their share of output from 51% to 75% (in the USA between 1967 and 1992).*
- *The cost of certification [for EurepGAP] alone comes to US $6000 for a group of about 25-30 farmers with individual costs of US $200 for an average farmer with two hectares.*

(Jacobson, Wrigley, van der Laan, Cotterill and The Services Group quoted in Humphrey, 2005)

The above developments threaten pro-poor development (Altenburg, 2006) and international changes are replicated at local levels. Lead firms, predominantly based outside the developing countries, create powerful brand images that shift power and value away from developing countries. Innovations are known to generate most economic rents and these giants, well embedded in knowledge networks, are most innovative and thus benefit most. Regional retailers in developing countries are applying these global practices in their local supply chains. Improved infrastructure and more demanding consumers will enable them to gain power and change local agricultural structures. The question is whether these changes in local value chains are also threatening pro-poor development or whether they can bring benefits to developing economies.

Well functioning value chains are said to be more efficient in bringing products to consumers and therefore all actors, including small-scale producers and poor consumers, should benefit from value chain development. Imbalances and uncertainties, characteristic for spot market sales in developing economies, can be avoided, reducing risks and costs. Yet many disadvantages for producers active in global value chains are related to their distance to the market.

Reardon (2003) argues that that the rapid proliferation of supermarkets across East and Southern Africa is transforming the food systems. In South Africa, supermarkets account for more than 55% percent of national food retail. Kenya alone has some 200 supermarkets and 10 hypermarkets, accounting for up to 30% of food retail in the country. These supermarkets already buy three times more produce from local farmers than the volume of produce that Kenya exports. Even though others caution that the supermarket share of fresh food retailing is much lower than for processed and packaged food, it certainly shows that local markets are considerable and that food supply systems are changing.

Recommendation: Donors and NGOs should direct more attention to promoting the development of local (and regional) value chains. The almost customary focus on global markets needs to be addressed: for the majority of local producers, global export markets are often less rewarding than assumed. The size and growth of local and regional markets might offer opportunities for many more producers.

Changing rural economies as a consequence

Two interesting developments related to global value chains can be observed: On the one hand the increased concentration often results in small holders being excluded from participation. For example, the number of Kenyan small holders producing fresh fruits and vegetables for export markets declined from 75% in the early 1990s to a mere 10-20% by the late 1990s (Dolan, 2004). On the other hand, the number of global value chains touching ground in developing economies is rising, offering opportunities for producers to participate in more than one value chain and creating access to new markets.

Larger commercial farms are in a better position than small holders to enter into global value chains. They are more likely to meet the increasing standardisation and are able to produce sufficient volumes. However, international competition is fierce, markets are volatile and there is a continuous decline of prices. Producers are under pressure to increase their flexibility and to reduce costs. They can do this by reducing their permanent employment positions and increasing the use of temporary workers, or by outsourcing the production completely.

The above developments have led to restructuring agribusiness. Larger commercial farms are changing their function in the value chain. As argued by Kaplinsky (2000), profits are less likely in production and more and more outside that area. So commercial farms take on processing functions and contract others, often smallholders, to supply them with produce. Delegating implies investing in suppliers by providing information and transferring knowledge but unfortunately it often also results in transferring risk to the producers who are at the same time pressurised to reduce costs.

Recommendation: Donors should facilitate the development of local standards and certification systems to enhance value chain performance. Limited certification possibilities and lack of standards not only limit access to global markets, but the emerging retail chains in local markets will likewise result in uncertified local producers being excluded from local markets. Local standards should result in improved chain performance and inclusion rather then exclusion.

Also changing rural employment patterns

Although the percentage of people living in rural areas has declined and agricultural labour has shrunk as a percentage of the total labour force in the years 1960-1990 (Hurst 2003), agriculture is still the main source of income for the rural population, including agricultural workers. Three factors influence rural employment patterns.

- The first being the HIV/AIDS pandemic with its devastating effect on the composition of the (rural) population. In many regions the most productive strata of society have disappeared.
- The second, more positive trend is the effect of migrants on their homelands. Whether they have migrated to urban areas or across national borders, many send remittances to their families that can be used to create enterprises. Returning migrants may bring with them new knowledge and skills, reversing the “brain drain” into a “brain gain” effect.
- The third factor that influences rural employment patterns is the aforementioned restructuring of agriculture. Dynamic markets and powerful actors located near the consumers force upstream processors and producers to increase their flexibility. Flexibility and cost reduction are achieved by increasing the number of casual workers at the expense of permanent employment positions. These changes result in *casualisation* and *feminisation* of labour as well as upstream and downstream inequalities (Hurst, 2003).

Casualisation. The number of permanent employees in the agricultural sector is decreasing, i.e. the Ugandan cut flower industry in which 75% of the workforce is now employed on a temporary basis. The salaries of permanently employed agricultural workers are already low and the wages that temporary workers receive are even lower, and their income often falls below the poverty line. Temporary workers are also more exposed to exploitative arrangements, due to a low degree of organisation and resulting low priorities by unions or governments.

Feminisation. The number of female employees is increasing. Up to 40% of the workforce in Latin America is female, while statistics in Africa suggest even higher and increasing female participation rates. Young female workers are believed to be better at certain jobs, to be more productive and less demanding than their male colleagues. One may argue that this trend is positive for the empowerment of women yet there are signs that the men are shifting to more lucrative jobs.

Employment conditions vary along the chain (Dolan, 2004). There appears to be a relationship between the lower margins and worse employment conditions upstream as compared to higher margins and better conditions downstream. Inequality is thus increasing and chain upgrading has merely increased the need for more unskilled work. These unskilled labourers run the risk of being replaced due to technological innovations taking place in the near future.

Governments face the challenge of improving employment conditions for employees without jeopardising the competitiveness of the employers in the value chain. They also need to decide whether they should strive to create high quality employment for a few or unskilled labour for the masses. These are tough decisions that require more in-depth analyses and more attention of policy makers.

Consumer and political pressure to ensure that private sector operations are socially responsible is on the increase in developed and developing countries. Many global buyer driven chains are already demanding good governance from their suppliers. Creating employment and ensuring better employment conditions could thus be part and parcel of interventions that aim to develop value chains

Recommendation: Donors should assist government and other decision makers in steering the process, from the analyses up to defining policies and creating an enabling environment. Donors and NGOs can play a role, both in developing and developed countries, to promote and enforce CSR by raising consumer awareness and pressure.

UNICEF reports how four major companies (Reebok, Levi, Pentland and Ikea) have adopted codes of conducts for labour standards in general or incorporate a specific prohibition on child labour. Reebok states that they will not work with business partners that use child labour and have started independent audits of its standards. Levi states it will actively support the development of programmes for the educational benefit of younger people. Pentland states that it will only do business with suppliers that adopt and implement their own standards, but limits its policy to their direct suppliers yet encourages their direct suppliers to do the same. Ikea demands from their suppliers that they take measures to ensure that no child labour occurs at their own production sites nor at the workplaces of their suppliers. (UNICEF's Child labour Resource guide)

Targeting smallholders – a two edged means for creating working places

Small holders are considered to be the backbone of rural economies. Therefore many efforts are made to link small holders to what appear to be promising value chains. Sometimes farmers are merely linked to one actor in a value chain and although this can be an effort in itself, it is not the same as developing a value chain.

The question arises whether small holders are best equipped to enter these more demanding value chains. Agro industrial firms prefer to contract wealthier farmers that are able to invest more and require less assistance, resulting in lower transaction costs (Swinnen and Maertens, 2006). A case study in Vietnam revealed that 95% of the farmers supplying to supermarkets owned more land than the average Vietnamese farmer. In the rice sector most farmers are supplying to traditional markets, while supermarket-driven chains are supplied by companies buying from medium to large scale farmers (M4P, 2005).

The so-called “rural poor” are those that are employed by these farmers rather than the employing farmers themselves. Targeting small holders might have some spin-off effect on employment creation, but the general assumption that small holder production is more labour intensive and creates more employment than commercial farming, has not been proven true. Interventions that target estates are likely to have a larger effect in terms of employment creation. Yet more often than not, interventions to enhance the performance of commercial estates are hampered by a discussion on the limitations of public money being used for such private sector actors. This is regrettable because innovative forms of public private partnerships can lead to highly leveraged and sustainable interventions.

Notwithstanding the importance of the above for economic development, the question for donors is whether targeting small holders creates employment for the poorest segments in a rural society.

Selecting sub sectors for promoting employment

Some 40 countries depend on a single commodity for more than 20% of their export income. Such high dependence on few commodities results in economies being highly sensitive to (global) shocks. This suggests that many developing economies need to focus on diversification.

With agriculture being the main income earner, gradually developing more sub sectors and value chains appears a realistic strategy.

More attention is needed for the identification and selection of potential sub-sectors before embarking on value chain analyses and development. The local economy and international environment need to be mapped, identifying opportunities and matching these with competitive advantages. Selection criteria for the various sub sectors need to be developed and sub sectors need to be compared. If employment creation is the objective, then employment criteria need to be included in the sub sector selection process.

This does not justify endless analyses delaying concrete action, yet insufficient analyses combined with unclear objectives and targets may result in failures. For many of us supporters, these failures are then renamed *lessons learned*, yet the real casualties are among the private sector actors and the poor that are threatened in their existence.

Opportunities need to be sought to increase value in the developing economies. This will not be easy given the powers of branding increasingly applied by the global buyers, leaving producers with very meagre margins. Kaplinski (2000) found that producers receive as little as 4-8% of the final price for raw cotton and tobacco and 11-24% for jute and coffee, while 27% of the final price for fresh vegetables from Africa accrued to the European retailers.

As advocated by Fairbanks and Lindsay (1997), there will always be another country offering a better price. Competing on low prices is often translated into low wages, implicitly depriving workers from development benefits. Unless margins can be obtained by adding values, the downward spiral of lowering prices and reducing wages continues.

Leverage points for selecting interventions

In order to achieve the desired effect on employment creation or inclusion of small holders, one is often tempted to look only at the target group itself. However, identifying leverage points should have a multiplier effect and hence a more durable impact can be obtained for larger populations than for the identified beneficiaries only.

In order to develop value chains, joined efforts are required by all actors relevant to that chain, i.e. the private chain actors, the private and public servicing industry as well as other public and civil society actors. The objective should be to enhance performance of the entire chain and to create win-win situations. It is likely that any analysis will identify various nodes that require interventions in order to improve overall performance of the chain.

The domestic beef market in Zambia had been analysed. Poor animal health, low productivity and gaps in supply/demands were identified as the main constraints. Rather than opting for direct interventions in the beef sector, one looked at the constraints behind the constraints: why were the supporting veterinary services not performing as desired? By addressing the "problem behind the signal" one designed interventions in the veterinary sub sector and achieved leverage and systemic change for the beef sector (Bear, 2007).

Fair Trade coffee has been on the (Dutch) market for almost 20 years but never gained more than a market share of a mere 5%. The numbers of small holders that benefit from the fair trade principle remains limited since major companies do not wish to pay the stipulated fair price.
The UTZ CERTIFIED initiative was launched five years ago, and offers assurance of social and environmental quality in coffee, yet leaves the price negotiations to the market actors. Major buyers like Ahold and Sarah Lee have joined and suppliers include plantations, where many workers will now benefit from improved (minimal) social standards.

Although striving to enter niche markets such as the fair trade, organic or ethnical markets may well serve a large number of producers; it is probably no answer for the majority of the producers Looking for alternatives in the processing industry implies looking for innovations that are applicable to the entire sector and that may be challenging but necessary to trigger lasting systemic changes.

Recommendation: practitioners should develop and test models that are not only replicable or that can be upscaled, but also, or mainly, result in systemic changes in the sector.

Realism is asked for

Value chain development may bring prosperity to chain actors and may improve the conditions for a limited number of farmers and agricultural workers. Promoting value chain development results in local economic development, but it will not automatically create large scale rural employment. Contract farming will provide income to those with land and other assets, while jobs in agro industries will provide unbiased employment possibilities to the poor.

Although it would be tempting to enforce the improvement of labour conditions, this would imply increasing costs and within the present cost oriented global competition result in losing market shares. This does not withstand the moral duty of public private and civil society actors to combat child labour at all costs, which is not only the result of poverty but also the cause of poverty in many countries.

Over-simplification must be avoided and expectations need to be tempered. Alike micro-finance that was initially sold to the public as the answer to rural poverty, care should be taken that the same mistake is not made with "value chaining" and that expectations are raised that won't be met. Value chain development is no panacea to rural poverty.

Tracking changes and impact

If the impact of value chain development in general is not always clear, the effect on rural employment is even vaguer. Current research has not yet provided a systematic assessment of the impact of these changes on agricultural and processing jobs (Gereffi and Sturgeon, 2004) and impact assessment focussed on workers is relatively new.

There are several reasons for measuring the impact of donor interventions. It enables practitioners to verify whether the set objectives and targets have been achieved, to justify and obtain support from donors as well as to showing results to stakeholders including beneficiaries, but most of all, measuring enables understanding the rather complex reality of value chain development. Measuring the impact of value chain development on rural employment is complicated and faces three main challenges (Altenburg, 2006).

- The first is the complicated mapping of trade-offs and side effects: how does one judge the positive effect on one group of chain actors in relation to a negative effect for another group in the chain?
- Related is the second complication of attribution and counterfactual problems: can these changes be related to the intervention and what would have happened without these interventions?
- The third is even more challenging: how does one deal with the time aspect and compare direct gains versus future losses?

Irrespective of the above complications, impact must be measured along the chain, from input suppliers all the way to retailers. These effects must be measured at the level of the companies, but also at the level of the workers and at the levels of their households. Measuring at company and worker level should provide quantitative and qualitative data: information regarding the number and type of employment, the characteristics of jobs, the absolute and relative income levels and security thereof, as well as the quality of the work and productivity figures (Barrientos, 2005).

Such detailed measuring is extremely sensitive, complicated and expensive. The question arises as to who is able and willing to finance such impact assessments. The private sector will only be interested in financing such impact assessments if they are able to benefit from it: either to improve their operations or to improve their position. In both cases private sector actors are unlikely to make those results public. That leaves the public and civil actors: governmental, non governmental and donor organisations. Now that the latter have embraced private sector development as an important strategy for poverty alleviation and appear willing to finance interventions in that field, one would expect donors to be equally eager to finance research that demonstrates the impact.

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