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EDITORIAL REVIEW

Alternative marketing strategies for smallholder farmers

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Introduction

Throughout much of Asia, the marketing and distribution system for fresh fruits and vegetables is experiencing a period of unprecedented change. Probably, the most significant driver of the change has been the dramatic expansion in retail market share held by the supermarket chains. Facing saturation in their home markets, most of the world's leading retailers have now established themselves in the region with varying degrees of success. Today, modern retail formats account for more than 50% of sales in much of the region [1, 2].

Unlike both Europe and North America where retail sales are stagnating and the only real growth in the market arises from consumers purchasing more expensive, better quality food [3], Asia provides a very attractive market. On the demand side, economic growth and rising household incomes are fuelling the demand for a greater range of high quality products. On the supply side, trade liberalisation is making it easier and cheaper to import, thereby providing an assured supply of good quality produce [4]. However, in an industry that offers significant economies of scale in purchasing and procurement, mergers and acquisitions are resulting in greater consolidation, not only reducing the potential number of buyers, but significantly altering the manner in which producers transact with institutional buyers.

In Asia, most of the fresh produce is distributed and sold through a complex network of wholesale and retail markets. In the wholesale market, prices are determined primarily by supply and demand. Many buyers seek to purchase the best quality produce available on the day at the best price. However, prices are highly variable day-by-day and even hour-by-hour, and both the quantity and quality of the produce offered for sale is highly variable, occasioned by the weather and seasonality of supply [5]. Given the inherent variability in quality, produce is made available on the market floor for inspection by potential buyers. However, this method of sale not only results in a substantial reduction in product quality but as the product itself is handled a multiple number of times, further reductions in product quality are inevitable.

For the supermarkets, these variations in quality and price and the inconsistent supply are unacceptable for it makes it impossible to adequately price the product in-store or to engage in any generic promotion or merchandising of the product. For most retailers, fresh produce is regarded as the key determinant in the consumer's choice of store because it provides an attractive, fresh and colourful display and is a symbol of the pervading quality standards throughout the store [6]. While shopper's accord great importance to the quality, price, range and availability of fresh produce [7], fresh produce also generates some of the highest profit mar-

gins of any product category in store. However, while fresh produce is high profile, the products are highly perishable and very sensitive to mishandling and damage at all levels of the supply chain [8]. Consequently, the potential for product loss and wastage is high.

Transacting with institutional buyers

In order to maintain product quality and provide a more consistent supply, institutional buyers are engaging in long-term relationships with preferred suppliers. Leenders and Fearon [9] suggest that preferred suppliers are those who seek to identify new ways of developing products and services that will allow their customers to perform their activities more economically. A preferred supplier will provide products to the quality specified and deliver on time, as promised, at a competitive price. Furthermore, a preferred supplier will react favourably to unforeseen needs such as suddenly accelerated or decelerated volumes of business, changes in product or delivery specifications, service problems or any other legitimate request. Preferred suppliers will provide technical support and other expertise when requested by customers or whenever the supplier believes it can assist the purchaser to remain competitive.

For the suppliers, while these arrangements may not necessarily result in a better price, they do provide access to shelf space, a guaranteed market for produce of an acceptable quality and security in the knowledge that the partners have a financially secure trading arrangement [7]. Preferred suppliers are rewarded with volume growth, which makes it more worthwhile to invest in the economies of scale and improved technology. Various benefits may also accrue from the exchange of sensitive market information. Preferred suppliers get feedback from retailers on the consumer acceptability of new varieties and new products, and get greater product support and assistance in new product development. Preferred suppliers may participate directly in the planned growth of the retail business, which, in turn, greatly facilitates their own planning processes.

However, as the cost of maintaining a large number of preferred suppliers is increasing, greater numbers of retailers are delegating the responsibilities of procurement to dedicated wholesalers and category managers. These category managers are private firms who are responsible for sourcing, importing, transporting, pre-packing, labelling, bar coding and preparing the product to meet the supermarket's specific requirements [10]. Reardon *et al.* [11] differentiate between two types of market intermediary: (i) dedicated suppliers or specialised wholesalers who supply one or two supermarket chains and are in charge of supplying an entire category to the supermarket's predetermined quality standards; and (ii) traditional wholesalers who serve a variety of clients, one of which may be a supermarket chain.

Depending on the level of market sophistication, Shepherd [12] identifies seven alternative means by which fresh pro-

duce can be purchased by the supermarkets: (i) direct, uncontracted purchases from farmers by individual supermarkets; (ii) from wholesalers, who either work directly with farmers or through the wholesale market; (iii) purchases through independent procurement companies (dedicated suppliers) who often work with farmers approved by the supermarket chains (preferred suppliers); (iv) purchases through government-sponsored distribution centres; (v) informal farmer groups, farmer associations or cooperatives; (vi) large individual farmers, who often sub-contract part of the supply to smaller farmers; and (vii) leasing of space within the store on a commission basis to traders, farmers and cooperatives.

Irrespective of the means supermarkets use to procure fresh produce in order to protect both the integrity of their brand and their market share, most modern retailers require their suppliers to take all reasonable steps to ensure that the food they sell is safe [13]. All major supermarkets now require fresh produce to come from suppliers who have an appropriate accredited quality management system. A genuine and visible quality management program is now a prerequisite for any fresh produce supplier who wishes to sell to the supermarkets [3].

Invariably, the quality standards set and enforced by the supermarkets are more demanding than those established in the public arena [14]. In some instances, this is a positive development, particularly when public sector food safety systems are inadequate and thus the standards imposed by the supermarkets reduce the food safety risk to consumers. However, Humphrey [15] describes how the challenges posed by food safety requirements are often extended to consider labour and environmental standards. Here, the challenges arise primarily from social activism and the supermarkets desire to be perceived as a good corporate citizen. Concerns with labour issues are an extension of mobilisations around labour standards in manufacturing and various campaigns against high-profile companies such as Nike and Levi-Strauss. Environmental issues have been raised partly as a result of concerns about the environmental impact of farming (pesticide run-off, erosion, declining soil fertility) and partly because of the impact of environmental conditions such as water quality and soil contamination on food safety.

However, private standards are often regarded as a major constraint for smallholder farmers who struggle to achieve these standards. While Shepherd [12] describes how impractical it is to expect small subsistence farmers to provide a safe water supply, provide toilets and hand washing facilities for workers, construct packing houses with cement floors and to maintain the records that traceability requires, smallholder growers acting individually are unable to provide the consistency of quality and supply that is demanded by the supermarkets [2, 16].

Smallholder farmers wishing to supply the supermarkets must accept that traditional religious or social obligations,

which in the past may have led to them stopping most on-farm operations for some time, cannot stand in the way of a commitment to supply supermarkets 365 days of the year [12]. Furthermore, farmers must accept that a proportion of their produce will fail to meet the buyers stated requirements and thus they will need to make alternative arrangements to dispose of it.

In transacting with the supermarkets, purchase prices are often negotiated for a fixed period, such as a week, but are renegotiated downwards by supermarkets if market prices decline in that period [12]. There is, however, no provision for renegotiation upwards if prices rise. Suppliers sometimes have to pay transportation charges from the distribution centre to the individual stores and promotion fees when a product is featured in an in-store promotion. Discounts are required when new stores are opened and penalties are invariably levied for failing to supply agreed quantities. Furthermore, farmers' cash flow problems are exacerbated by the fact that many supermarkets withhold payment for up to 90 days.

For practical purposes, supermarkets prefer to transact with small producers through intermediaries (wholesalers or producer organisations) [2]. Without such an intermediary, it would be much more convenient and efficient for institutional buyers to deal with large-scale producers, who have the capacity to deliver large volumes on a regular and timely basis and can more easily ensure food safety and quality standards.

In order to deal with the quantity and quality parameters and food safety issues, supply contracts are gradually replacing the role of spot markets. Contracts exist with a range of modalities from verbal contracts to contracts with weekly price negotiations and volume agreements per cropping cycle [16]. For most small producers, the concept of a formal contract, or at least a commitment to supply an agreed quantity of a product at an agreed time, is problematic. This becomes more of an issue where producers are geographically scattered and have limited access to market information.

Alternative routes to market

While the institutional market will inevitably grow in importance, Cadilhon [this issue] discusses grower direct marketing systems. Direct marketing by farmers is viewed by many as a possible mechanism to enhance the returns to primary producers by eliminating market intermediaries. Direct marketing systems include; (i) farm gate sales; (ii) farmers' markets; (iii) U-pick and We-pick operations; (iv) community supported agriculture and buying clubs; (v) gift baskets and mail order; and (vi) e-commerce.

For the producers, grower direct marketing is perceived to offer a number of benefits including increased consumer satisfaction, stronger local communities and improved environmental sustainability. Grower direct marketing provides a means of reinforcing the links between farmers and consumers through physical contact and information sharing. Under

many of the community supported agriculture schemes, consumers agree to prepay a certain amount of money to producers or to invest in the production system directly in exchange for receiving fresh produce at their door or at a designated delivery station. While this arrangement enables farmers to diminish their sensitivity to risk, consumers benefit through obtaining farm fresh products and an opportunity to experience a rural lifestyle. Under those direct marketing schemes where the consumer harvests the produce themselves, farmers can save on seasonal harvest labour and save altogether on transportation and packaging costs. Grower direct marketing has also been identified as an effective tool in the promotion of local products, given that the geographic link between the produce and a locality is embodied by the farmer who is selling the produce.

However, direct marketing requires producers to identify markets, choose the products and services that are most appropriate for the identified market and to interact with consumers to improve product quality and services. Indeed, when farmers venture into direct marketing, they are confronted with consumers and their individual requirements, an interaction that is traditionally performed by the retailers. To truly benefit from direct marketing schemes, farmers must invest a significant amount of time in building a sustainable customer base. Significant capital investments may also be required in the construction of appropriate retail outlets or alternative distribution systems. At the farm level, U-pick operations have the potential for product to be lost through consumption and inclement weather and without adequate training consumers can damage the plants.

Saili *et al.* [this issue] elaborate on the role of farmers' markets as a means for producers to sell their produce directly to end buyers. While farmers' markets provide many opportunities for producers: minimal marketing, packaging and promotion costs; higher prices than the wholesale market; an established customer base; and a convenient testing site for new products, there are also significant drawbacks associated with: the need to transport the produce to market; limited sales volume; a variable customer base; food safety concerns; and increasing regulation.

For the consumers, shopping at farmers' markets enables them to achieve price savings without compromising quality. Consumers enjoy cheaper products due to the elimination of a long supply chain, with the added advantage of fresher products, often with superior taste. Farmers' markets also offer greater variety, including exotic and traditional products, organically grown produce and ethnic foods, which are not ordinarily found in supermarkets. Farmers' markets allow not only the rich to buy, but all consumers have access to healthy and fresh products, thereby reducing any income inequalities in terms of access to food.

As the need for smallholder farmers to collaborate is widely supported if they are to meet the needs of institutional buyers,

Murray-Prior [this issue] discusses the circumstances under which collaborative farmer groups are most likely to succeed. Traditionally, collaborative marketing groups have been formed as a means of increasing bargaining power in a situation of market failure arising from *ex ante* market power, *ex post* market power and asymmetric information. However, collaborative marketing groups have also been established to take advantage of government support programs and where it is more efficient for producers to invest in downstream processing and marketing.

Two factors appear to be critical to the successful establishment of collaborative marketing groups: (i) a comparative advantage; and (ii) a reasonable level of trust amongst the members of the community seeking to establish the collaborative marketing group. Without a comparative advantage over alternative forms of marketing, collaborative marketing groups are doomed to fail because of the inherent weaknesses that make them less efficient than the alternatives. Situations in which collaborative marketing groups may have an advantage are when farmers are dealing with monopsony or oligopsony situations; when farmers are making high levels of transaction-specific investments; when there are substantial economies of size; when services are not provided by the private sector; and when a collaborative marketing group can access higher-priced markets.

Trust has a positive impact on collective effort. Members of a collaborative marketing group need to trust their organisation, its management and its leaders. This leads to lower transaction costs and provides the collaborative group with an advantage over other forms of organisation. In part, the level of trust is related to the level of social capital within the community. Social capital refers to the shared knowledge, understandings, norms, rules and expectations about patterns of interactions that groups of individuals bring to a recurrent activity [17].

However, for a number of reasons, the performance of cooperatives, especially in developing countries, has failed to meet expectations. Lele [18] suggests that the reasons for this include: a lack of understanding of the actual constraints and solutions facing smallholder farmers; insufficient emphasis on the internal prerequisites of good leadership, management, experience and technical know-how; and the lack of external prerequisites for the effective functioning of organisations such as government policies, input distribution, infrastructure development and regulatory functions.

Given the many impediments, both internal and external, that constrain the development of collaborative marketing groups, contract farming is emerging as an alternative strategy for the vertical coordination of procurement operations by institutional food buyers [Singh, this issue]. The essence of such arrangements is the commitment to provide an agricultural commodity at a specified time, price and place, and in a specified quantity, to a known buyer. Farmers often prefer contracts

because it provides access to credit and a more certain price by shifting part of the risk of adverse price movement to the buyer. Farmers may also get access to new technology and inputs through contracts which otherwise would be beyond their reach. Contracts help improve product quality by introducing incentives and penalties and it is often suggested that contract farming is the only way to make small scale farming cost competitive.

However, despite the potential benefits of contract farming, there is much debate about the extent to which smallholder farmers are actively engaged. Most agribusiness firms prefer to transact with larger farmers because of their capacity to produce better quality crops due to more efficient and business-oriented farming methods and larger volumes of produce which reduce the cost of collection; improved traceability due to the absence of pooling; and their capacity to bear risk in the event of crop failure. Small farmers, therefore, are potentially excluded from many aspects of contract farming.

Given the weak bargaining position of most smallholder farmers, there is evidence to suggest that unscrupulous agribusiness firms often manipulate the provisions of the contract in their own favour. Contracted growers often face many problems such as unanticipated product rejection, delayed deliveries at the factory, delayed payment and low price. Furthermore, while contracts protect the buyers' interest, they seldom cover the farmer's production risk and they generally offer prices that are based on open market prices.

Potentially, contracting can lead to the delocalisation of control over resource allocation and work routines, compromise farmer autonomy and the economic dynamism of farmers and rural communities. Contract farming can lead to the adoption of homogeneous farming practices, posing food safety and ecological concerns. The over exploitation of groundwater, soil fertility decline, increased salinity, monocultures and pollution are typical examples of environmental degradation due to contract farming.

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