

# Lessons learned

## Commodity value chain development projects

Sustainable inclusion of smallholders in agricultural value chains



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These notes are “living” documents and will be updated periodically based on new experiences and feedback. If you have any comments or suggestions, please contact the originators.

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## List of acronyms

ASMED	Afghanistan Small and Medium Enterprise Development Project funded by USAID
CAIM	IFAD-funded Convergence of Agricultural Interventions in Maharashtra's Distressed Districts Project
CNCFTI	National Forum on the Industrial Tomato Value Chain in Senegal
IIED	International Institute for Environment and Development
LAADCO	Liberia Agriculture and Asset Development Company
LEAD	USAID-funded Livelihoods and Enterprises for Agricultural Development project in Zimbabwe
NAEB	Rwanda National Agricultural Export Board
NRGP	Northern Rural Growth Programme
PPPP	public-private-producer partnership
PRICE	Project for Rural Income through Exports
PROCAVAL	IFAD-funded Small-scale Producers in Value Chains and Market Access Project in Nicaragua
SAED	Senegal River Development Agency
SOCAS	Senegal Canned Food Company
USAID	United States Agency for International Development
VC	value chain

## Introduction

The traditional IFAD project approach had the objective of supporting small-scale producers and different segments of the rural poor population: the major entry point for project interventions was through working with these target groups and their associations such as cooperatives. Part of this support involved facilitating linkages to markets.

While this approach is still applied in a significant number of projects, most newly designed IFAD projects are either “value chain projects” or include a value chain (VC) development component. These projects adopt a VC approach based on a comprehensive analysis of the entire VC, from producers to end-market consumers, but their main objective remains firmly based on empowering small-scale producers and the rural poor.

The purpose of this Lessons Learned note is to provide design teams with observations based on lessons from IFAD and other donors’ projects that may help in the design of VC projects. This document is part of a comprehensive knowledge toolbox, which also includes a Teaser and a How To Do Note on *Commodity value chain development projects*.

## Context and challenges

Developing VCs is widely considered to be a suitable approach to inducing growth in rural areas and increasing the availability and marketing of agricultural products. Significant growth in the number of VC development initiatives has occurred over the past decade. The assumption is that the development of VCs is a suitable instrument for inducing economic growth, addressing food supply shortages and enhancing rural livelihoods. In addition, the widespread alarm following the 2008-2009 global food price spike has driven more and more private companies to seek sustainable sources of raw materials and supplies and to expand their outreach to poorer rural and the growing number of urban consumers in developing countries as part of their strategies for building long-term business competitive advantage.

IFAD’s portfolio has shifted significantly towards VC programmes over the last ten years. However, although there is no doubt that there has been a very important shift, the data show that this trend has been somewhat exaggerated. The criteria for what is considered a VC project at IFAD are not always clear.

The greatest increase in commodity VC projects occurred around 2005, at the same time as IFAD’s Private Sector Development and Partnership Strategy was adopted. VC development projects today focus more directly on the private sector. This is a substantive change from the “farm-to-market” projects of the past.<sup>1</sup> Most, albeit not all, earlier projects made support to cooperatives the centrepiece of market access for smallholder producers. In contrast, the current generation of commodity VC development projects seeks direct collaboration with the private sector.

Support to commodity VC development in IFAD projects varies greatly from country to country and is commodity-specific. While some projects link smallholder farmers to supermarkets, exporters or large processing units, most projects work with smallholder farmers to link them to new and emerging chains. This variation results from the multiple roles of the private sector in different chains and the diversity of VC models. Most IFAD-supported operations, even when they are called “value chain development projects”, address only partial elements of a VC, with limited support to the overall commodity VC development.

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<sup>1</sup> Independent Office of Evaluation, *IFAD’s Private-Sector Development and Partnership Strategy, Corporate-level evaluation* (Rome: IFAD, June 2011).

Figure 1 illustrates the pyramid of 500 million smallholder producers. Rural dwellers can be very generally classified into three groups:<sup>2</sup>



source: OXFAM - IIED (2012)

**Figure 1: The smallholder pyramid**

- At the top of the pyramid is a small subset of producers who are better organized and have access to finance, productive assets, expertise and information. They already participate fairly effectively in VCs but their capabilities could be strengthened.
- The largest segment of the pyramid is composed of small-scale farmers who are less formally organized, have fewer assets and skills, face difficulties in obtaining access to services, tend to sell in local or informal markets and may derive part of their incomes from waged work.
- The bottom (base) of the pyramid is made up of the poorer segments of the rural population – people with the fewest assets or skills; landless, youth, widows, ethnic minorities, etc. – who generally depend on off-farm and labour opportunities or informal/formal social welfare programmes and who sell occasional surpluses to local markets.

Most VC development programmes supported by IFAD strive to apply a VC approach to all three segments of the smallholder pyramid. However, each segment poses different *challenges*.

When working with those at the top of the pyramid, the challenge is to engage them as drivers (e.g. “lead farmers”, small and medium-sized enterprises) for other, less developed and organized producers by disseminating knowledge and skills and creating additional demand and jobs for smallholders in the middle and bottom layers.

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<sup>2</sup> This typology is adapted from B. Vorley, L. Cotula and M.-K. Chan, *Tipping the Balance: Policies to shape agricultural investments and markets in favour of small-scale farmers* (Oxford, United Kingdom: Oxfam International, 2012).

Smallholders in the middle layer could be helped to transition to the top of the pyramid. The challenge is to enable them to become more reliable partners of local, national or even international VC business actors in a rewarding and sustainable way. If the associated risks are adequately mitigated, smallholder farmers' participation in well-organized VCs can translate into higher incomes: for example, farmers' incomes in Guatemala, Indonesia and Kenya increased by between 10 and 100 per cent through participation in VCs (World Bank World Development Report 2008).

Smallholders at the bottom of the pyramid can be assisted in earning more from employment or microentrepreneurship by becoming more productive participants in VCs. In general, however, involving the rural poor requires extra efforts and investments, making them costly to reach in VC development interventions. Poorer women and men producers, processors and traders face difficulties with access to markets because they lack information, are unable to meet product and delivery requirements,<sup>3,4</sup> and have limited or no access to finance. Balancing poverty reduction goals with the commercial objectives of the VC is, therefore, a challenging goal; farmers and their organizations require high levels of support before they can be progressively integrated into VC markets and take advantage of the opportunities offered.<sup>5</sup>

## Lessons learned

### Responding to market requirements

The market is the basic driver of all VCs. Without market demand from consumers, there is no force pulling a farmer's products and no VC. Consumers purchase products that meet their preferences and the VC responds by providing goods according to these preferences.

A key element of a VC approach is understanding the market requirements that are most relevant to small-scale farmers and using this understanding to guide producers in making decisions that will optimize the use of available resources (land, labour, savings, etc.). When there is a market orientation to production, farmers produce in response to what the market requires in terms of crops, timing of delivery, quality, packaging, prices, etc.

Different VCs offer different opportunities and constraints for farmers. After analysis of market requirements, it may be concluded that the barriers to entry to a VC serving export markets are too high for poorer farmers who lack the necessary equipment and skills; these farmers may, therefore, be better off optimizing production for domestic or local markets, at least initially. Projects that help farmers to serve local markets can be just as valuable as those helping them to enter international markets. The key is to base production decisions on an analysis of market realities.

### Considering multiple VC intervention points

The traditional entry point for IFAD projects is the primary production level, i.e. building the capacity of IFAD's target groups – including the more vulnerable groups – to gain access to markets and engage in business relationships along the VC. However, inherent to a VC approach is recognition that intervening elsewhere on the VC can have a highly beneficial impact on IFAD's target groups. VC projects can, therefore, have multiple points of entry at different nodes along the VC, such as production, collection, processing, transportation, wholesaling or retailing.

<sup>3</sup> C.R. Farnworth, Module 5: Gender and Agricultural Markets. In *Gender in Agriculture Sourcebook* (Washington, D.C.: World Bank, 2008). <http://worldbank.org/genderinag>

<sup>4</sup> J.A. Berdegue and T. Reardon, The retail-led transformation of agrifood systems. In C.R. Farnworth, J. Jiggins and E.V. Thomas, *Creating Food Futures: Trade, Ethics and the Environment*. (Farnham, United Kingdom: Gower Publishing; London: International Institute for Environment and Development [IIED], 2008). ISBN 978-0-7546-4907-6.

<sup>5</sup> I. Guijt and E. van Walsum, Balancing business and empowerment in fair fruit chains: the experience of Solidaridad. In C.R. Farnworth, J. Jiggins and E.V. Thomas, *Creating Food Futures: Trade, Ethics and the Environment*. (Farnham, United Kingdom: Gower Publishing; London: IIED, 2008). ISBN 978-0-7546-4907-6.

For example, improving the efficiency and capacity of processors or other downstream actors can create additional demand and higher prices for crops, with direct benefits for small-scale producers.

Taking a “win-win” perspective on the distribution of financial benefits along the VC can often be a cost-effective way of increasing farmers’ incomes. A VC approach recognizes that a critical component of rural producers’ empowerment may be accomplished by assisting the buyers or processors supplied by small-scale farmers, as illustrated in Case study 1 on bird’s eye chillies in Rwanda.

### **Case Study 1: How downstream interventions can directly benefit small-scale producers – the bird’s eye chilli VC in Rwanda**

Under the IFAD-funded Project for Rural Income through Exports (PRICE), the Rwanda National Agricultural Export Board (NAEB) is implementing activities for upgrading the horticultural VC. Based on a review of promising crops, NAEB’s VC specialists selected bird’s eye chilli as a promising VC, as it has a robust international market and a willing local private-sector exporter, PEBEC, which already buys crops from small-scale producers. Bird’s eye chilli can be intercropped with bananas, a main staple of Rwanda, so it is a particularly interesting crop for land-constrained farmers.

Working with PEBEC, NAEB found that post-harvest drying, done in the open air on tarpaulin sheets, was a major weakness in the bird’s eye chilli VC. The drying process was slow and yielded a high percentage of low-quality or spoiled chillies. Through PRICE, limited technical and financial assistance was provided to the bird’s eye chilli exporter to help it to purchase and install improved solar dryers near the farmers’ fields, with much higher throughput and better quality. This allowed the exporter to purchase more bird’s eye chillies at a better average price. If a traditional approach had been taken (e.g. increasing farmers’ yields per hectare) *before* this link in the VC had been strengthened, farmers would not have benefited and could even have been worse off. With the new driers, both the bird’s eye chilli exporter and the farmers will benefit financially. This win-win result is a key outcome for a VC project.

### **Paying attention to the political, policy and regulatory framework in the selection of VCs to be supported**

Some commodities in some regions may not always be ideal candidates for a VC approach. For example, crops of high political value, such as rice in South Asia, often have serious market distortions (input subsidies, price floors, pan-territorial pricing, export bans) that discourage the private-sector involvement implicit to a VC approach. For example, in Zambia, a country with massive agricultural potential, maize has traditionally been so heavily subsidized that promising new cash crop VCs (such as soybean) have been crowded out because most small-scale farmers are not interested in them. However, it is interesting to note that better trained and more entrepreneurial small-scale farmers in Zambia are increasingly realizing that growing unsubsidized soybean gives better real returns than maize because of the large inefficiencies in the public sector-driven maize subsidy programmes. The arrival of maize inputs a month after optimal planting dates and the government’s payment of sales proceeds six months after delivery have tipped the balance towards soybean production.

In these cases, IFAD policy engagement – in collaboration with other development partners and country stakeholders – may help establish a more favourable environment for sustainable VC growth.

## Creating incentives for the private sector to provide goods and services for small-scale producers

Wherever possible, a VC approach seeks to create incentives for business companies to provide the necessary goods and services for enabling small-scale producers to expand their participation in the VC, as either suppliers or business partners. This has proved to be far more effective than relying on free-of-charge, but often substandard or unreliable, government services that risk crowding out possible private investments. Even multinational input suppliers are seeing the benefits of marketing to small-scale producers and recognize that unless they market their goods and services in ways that truly add value for farmers, they will not be able to sell them. See Case study 2 on the horticulture VC in Kenya.

### **Case Study 2: Bayer CropScience and the horticultural VC in Mount Meru – how a chemical company, a bank, Kenyan exporters and small-scale farmers upgraded their VC and expanded sales in the European market**

Small-scale horticultural farmers in Mount Meru on the slopes of Mount Kenya were at the mercy of local brokers who provided the only market for their crops. Prices fluctuated wildly and harvests sometimes went unsold. Farmers had limited capacity to identify pests and diseases, select the right crop protection products and apply them properly. Export producers such as Indu Farms and FrigoKen had previously sourced from these small-scale farmers to supplement their own production but struggled to obtain regular supplies of safe and healthy food. Smallholders' crops were often sprayed haphazardly and sometimes with low-quality or even chemical pesticides. As standards in the European market tightened with the introduction of EurepGAP (now GlobalGAP) good agricultural practices, exporters were no longer able to source from small-scale farmers.

The local office of Bayer CropScience saw this development problem as a business opportunity that would support its long-term strategy for serving the US\$1-billion plus Kenyan horticultural market. Bayer helped organize the farmers into groups and provided them with training on the proper handling and application of pesticides, fungicides and insecticides and on the importance of using registered inputs. Bayer introduced the farmers' groups to product exporters and convinced the exporters that with proper support and training the farmers' groups could become reliable suppliers. By organizing into groups, the farmers were able to lower their costs by making bulk purchases through the local Bayer distributor in the Mount Meru area, Farmers Centre. Even so, organic inputs cost much more than others and are beyond the reach of most small-scale farmers. Equity Bank saw an opportunity to solve this problem and achieve its goal of expanding its agricultural loan portfolio. The bank structured a deal with exporters such as Indu Farms and FrigoKen to handle all crop payments to farmers, which enabled it to deduct input loan repayments before remitting the balance of payments for produce to the farmers. Equity Bank also provided training in financial literacy to farmers' groups, covering how to budget and plan for the future. Group clerks now keep detailed records of deliveries and payments so that farmers can be assured that they are being fairly treated.

## Providing complementary VC services that are public goods

Some VC upgrading interventions may be difficult to provide on a profitable basis. For example, a VC approach requires that small-scale producers or their organizations have the skills to analyse market opportunities/risks, develop a crop or farm plan to respond to these opportunities and manage their enterprises commercially. These needs can be addressed by skills development training but there may not be a self-sustaining business model for providing training services. Basic agronomic training (as opposed to crop- or input-specific training) is also not easy to provide on a commercial basis and traditional government extension services have not been able to fill the resulting gap. Basic infrastructure (feeder roads, electricity, large irrigation systems, etc.) is a typical public good that is critical for the viability of the whole VC. Provision of public goods is a clear entry point for intervention by the public sector (donors or governments), lowering private companies' transaction costs and risks of engaging with small-scale producers. IFAD should help governments explore efficient and effective ways of providing these services and leveraging private-sector investments.

### Sustaining the inclusion and income benefits of small-scale farmers, women and youth

Sustainable inclusion of small-scale asset producers and rural people in VCs is a particular challenge. VC activities tend to be concentrated on wealthier farmers and small-scale investors in farming. Private-sector companies also prefer to concentrate their suppliers geographically, as clustered suppliers generally perform better and more efficiently than spatially dispersed ones.<sup>6</sup> The market-driven development of VCs thus tends to favour larger, geographically concentrated producers. This poses a challenge for the inclusion of smallholders and family farmers, the target group for IFAD's VC interventions. A fundamental task for IFAD is investing in and supporting small-scale producers and small-scale processors who have the potential to become competitive and – with further support – remain engaged in the chain.

The inclusion of women and youth in a chain is particularly difficult, as they typically lack access to credit, transportation, productive assets, communication and information. Women's participation is further restricted by the roles assigned to them in many societies, making it difficult for women to produce the quantities required by VC buyers. When women are included, there is high risk that they will be excluded as the chain expands and becomes more successful. The expansion of VCs often leads to the exclusion of commodities that are traditionally defined as "women's crops". When the marketing of commodities increases incomes, men take charge. As women and youth are a core target group, IFAD programmes should focus on including them in the VCs being developed but many ongoing programmes fail to do so.



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Armenia - Farmer Market Access Programme

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<sup>6</sup> H. Schmitz, Collective efficiency: Growth path for small-scale industry, *Journal of Development Studies*, 31(4): 529–566 (1995).

### Monitoring the development impact of smallholders' inclusion in VCs

A central assumption is that the inclusion of smallholders in the VC will automatically lead to sustainable income benefits. However, this assumption may be wrong.<sup>7</sup> As VCs mature and larger business actors become involved, market concentration can weaken the smaller suppliers within the chain. Certain key actors, typically the lead firm, have the capability to define and impose the conditions for contracts and subcontracts in their supply chains (e.g. product and process standards, quantities and delivery conditions). Subordinate partners in the supply chain are in a weak bargaining position because lead firms can swap suppliers or at least threaten to do so, squeezing their partners' profits and appropriating a larger share of the total gains of the VC.<sup>8</sup> Most successful agricultural VC programmes – including many of IFAD's – use lead firm or contract farming models as drivers of the VC development process. Lead firms and contract farmers often gain in market power as the VC reaches scale so regular, careful monitoring of farm gate prices and margins is essential. Only regular monitoring will detect structural shifts in the power structure of the chain and IFAD's VC programmes must include mechanisms for facilitating such monitoring.

### Promoting farm and off-farm microentrepreneurial development along VCs

Support to microentrepreneurial development has often proved to be a key part of an effective VC development project, particularly when rural people face challenges to becoming involved in primary production because they lack assets and skills or when they are less interested in it (often youth). Microenterprises can also provide services and inputs (veterinary, maintenance of equipment, extension, etc.) that are a critical part of the VC upgrading strategy. Support to microenterprises has been effective in several IFAD-funded projects (see Case study 3), including in Western and Eastern Africa. See Case study 4 on the Goldtree oil palm smallholder development programme in Sierra Leone.

#### Case Study 3: The Northern Rural Growth Programme (NGRP) in Ghana

The goal of this programme is to achieve sustainable rural livelihoods and food security in northern Ghana, particularly for people who depend on marginal lands, such as rural women and other vulnerable groups. The Northern Rural Growth Programme (NGRP) focuses on strengthening linkages among the various actors in agricultural VCs – including producers and their organizations, suppliers, service providers, financial institutions, aggregators, “off-takers” (such as processors, traders and exporters), researchers and administrators. The programme supports private-public partnership arrangements to ensure that smallholders have access to finance and markets.

The programme includes a specific window for “women's crops” to promote VC development. This has facilitated women's access to land and other productive resources and women have been able to triple their incomes through direct linkages to international markets. Women have also increased their participation in other commodity windows and women VC actors are now represented on district VC committees. Women account for two-thirds of programme participants. The programme works with the gender desk officers of district assemblies and government institutions and has also engaged with paramount chiefs to enhance women's economic empowerment through access to land.

<sup>7</sup> E. Biénabe, J.A. Berdegué, L. Peppelenbos and J. Belt, *Reconnecting markets: Innovative global practices in connecting small-scale producers with dynamic food markets* (Farnham, United Kingdom: Gower Publishing; London: IIED, 2011).

<sup>8</sup> G. Gereffi, J. Humphrey and T. Sturgeon, The governance of global value chains, *Review of International Political Economy*, 12(4): 78–104 (2005).

### Case Study 4: The Goldtree Oil Palm Smallholder Development Programme in Sierra Leone – how VC projects can foster microenterprise development and the empowerment of women and landless youth

Sierra Leone's tragic ten-year civil war destroyed the oil palm industry. In the largest post-war foreign direct investment in Sierra Leone's agriculture sector, Goldtree Holdings, backed by the African Agriculture Fund (AAF), developed a small core plantation of oil palm and constructed the country's only functioning oil palm mill in the Daru area of south-eastern Sierra Leone. Goldtree's strategy is to source more than 90 per cent of its production through small-scale farmers. In partnership with Goldtree Holdings, AAF's Technical Assistance Facility, managed by IFAD and funded by the European Union, set up a smallholder outgrower support programme. Center Point, the programme's experienced oil palm industry specialist, immediately saw that significant rehabilitation and improved maintenance procedures were essential to increase the very low productivity of the oil palm farms, otherwise using supplies from smallholders would not be economically viable. The problem was that the oil palm farmers lacked the labour resources to devote to the crop, especially as they were also producing cocoa and the staple foods of rice and cassava.

To respond to this challenge, Center Point and Goldtree have developed an oil palm subcontractor support programme. Farmers with landholdings (mainly youth, with women accounting for nearly 50 per cent) have been trained in modern rehabilitation, pruning and maintenance operations. Because these operations require specialist skills, other farmers will find it advantageous to outsource them to the trained youth. To ensure that the subcontractors are paid promptly and fairly, Goldtree is setting up a system for recording subcontracted labour and will pay the subcontractors directly through deductions from the payments it makes to the farmers.

While the programme is still in the early stages of development, Goldtree and Center Point estimate that microentrepreneur subcontractors should be able to earn US\$5–10/day, which may not seem much in global terms, but is far higher than the current wage for unskilled rural labour in Sierra Leone (approximately US\$2.50/day).

### Adapting a VC approach in constrained circumstances

In certain circumstances, a VC approach may seem difficult or inappropriate. For example, food-insecure, isolated, resource-constrained rural populations in a recent post-conflict or insecure zone may appear to have little immediate opportunity to participate in VCs. In these circumstances, investments in building social, physical or natural resource management assets may be essential activities that have food security and risk reduction benefits, while also laying the foundations for a population to participate in VCs as circumstances change.

Even in highly constrained environments, a VC approach can have a large pay-off for the rural poor if the appropriate system and commodity are chosen, as in Case study 5 on Afghanistan.



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Guatemala - National Rural Development Programme: the Western Region

### Case Study 5: VCs in insecure regions – small-scale production of saffron in Herat, Afghanistan

Applying a VC approach to raise the incomes of poor, remote farmers in war-torn Afghanistan may seem to be an unreachable goal but the Afghanistan Small and Medium Enterprise Development (ASMED) Project funded by the United States Agency for International Development (USAID) did just that. Even more remarkably, it also enticed a Dutch partner to make a significant, long-term investment. Saffron has attracted the attention of donors in Afghanistan because it has the potential to compete with illicit opium as an attractive cash crop, has large employment-creating potential and does not compete with other crops (except opium) for water and labour. Similar to opium, saffron's extremely high value-to-weight ratio means that the very high-cost transport by foot of small quantities of product is economically viable. However, efforts to develop the sector have faced challenges, which have been exacerbated by the security situation and include suboptimal agronomic methods: poor-quality planting materials (saffron bulbs); inadequate procedures, materials and equipment for on-farm processing, drying, grading and storage; inadequate storage, drying, testing, grading and packaging at the trader/wholesaler/exporter level; and lack of understanding of international market requirements.

ASMED was approached by Herat-based saffron trader Afghan Saffron, which purchases and exports about 4 per cent of national saffron production. Afghan Saffron partnered a Netherlands bulb production company, Blue Green World, in a VC project for: providing small-scale farmers and their associations with access to affordable, high-quality planting materials and extension and training services in saffron growing; collecting fresh saffron flowers from farmers; processing (picking, drying, grading, storing, packaging) the saffron under controlled, hygienic conditions acceptable to international buyers; and establishing linkages to high-value international markets in Asia, Europe and North America, which pay good prices for assured quality. The project results exceeded projections, even though the security situation in Herat Province deteriorated; Herat is the only province in Afghanistan where cultivation of the opium poppy decreased in 2013 and much of this reduction can be attributed to the presence of saffron as an alternative crop.

The key success factors identified include: i) a flexible project implementation structure that responds rapidly to private-sector proposals across a number of agricultural VCs; ii) the participation of highly qualified private-sector partners capable of solving problems as they arise throughout the project and not just during the detailed VC analysis; iii) use of exclusively local private-sector entities to provide technical and business support to local farmers (outsiders would not be accepted and would face serious security risks); and iv) close collaboration with Netherlands aid organizations for information exchange and acceleration of the due diligence process for the Netherlands partner.

### Broadening the inclusive approach to wage labour development

Given the limited potential for VCs to absorb poor smallholder producers, inclusion should be defined broadly. Well-functioning VC programmes induce rural growth and IFAD can help the poor to share in the direct and indirect benefits of this growth. Specifically, IFAD could do more to facilitate opportunities for the poor to work in rural wage labour on larger farms or in enterprises. Although a few IFAD programmes already include support to wage labour opportunities, it is not a common feature. Employment generation projects should also promote the introduction of a decent work agenda (i.e. workers' rights, social protection and social dialogue)<sup>9</sup> and the principal of equal pay for equal work.

<sup>9</sup> The International Labour Organization (ILO) is the leader in promoting the decent work agenda, see <http://www.ilo.org/global/about-the-ilo/decent-work-agenda/lang--en/index.htm>.

### Addressing the possible trade-offs between product specialization and diversification

Participation in VCs may expose small-scale farmers to new opportunities but also to new risks. Poor rural people usually depend on multiple and complementary livelihood activities to protect them from shocks. Expanding cash crop farming to the detriment of food crop farming might have a negative impact on household food security if not carefully planned. Projects using the VC approach need to assess and monitor the impact of planned interventions on household food security to find an appropriate balance between food and cash crop production, particularly if rural producers have very little surplus beyond subsistence.

Project design teams should check that, wherever possible, VC projects do not detract from food security and nutrition by working with farmers and their associations to ensure that: i) sufficient household labour, inputs and land are devoted to staple food production, to provide a minimum level of food security in case of production or marketing problems with the cash crop, or shortages of other food crops; ii) when the cash crop is also a staple food (e.g. rice or maize), farmers do not commit all their production to sales but leave a reserve for household food security; and iii) ways of integrating food security crops with cash crops are explored in a mutually supportive fashion. See Case study 6 on integrating food security and cash crops in Zimbabwe.

Experience in efforts to balance food security and cash crop production has demonstrated that: i) food security concerns can be addressed through a commercial VC approach, even when the VC concerned is for a non-food cash crop; and ii) the key to success for all VC projects is to take a market-oriented approach, identify the right partners and develop solutions that provide real financial benefits for all parties.

#### **Case Study 6: Integrating food security with cash crops using a VC approach – cotton and sorghum in Zimbabwe**

The cotton industry in Zimbabwe depends on a network of more than 100,000 small-scale growers. The multinational company Cargill entered the Zimbabwe cotton market in 1996 but by the early 2000s it was facing a dilemma: despite providing seeds, other crop inputs and training to its small-scale growers, yields were continually declining. Part of the problem was that farmers were exhausting the soil by planting cotton year after year but another issue was that farmers were using the fertilizer provided for cotton on their maize crops. Cargill's initial response was to stop providing fertilizer to many farmers but this merely depressed yields further. The situation was also worsening for the farmers. In addition to getting less for their cotton crop, farmers' food production was declining. The reason for this was that maize does not perform well in much of Zimbabwe's mainly semi-arid cotton-growing regions and some farmers were experiencing maize crop failures every three years. Hardier sorghum and millet are more appropriate food crops in these regions but Zimbabwean tastes have shifted over the years and most people strongly prefer maize for preparing the staple *sadza* over the coarser alternatives.

The USAID-funded Livelihoods and Enterprises for Agricultural Development (LEAD) project worked with Cargill to find a solution: Cargill encouraged sorghum production by providing farmers with improved seeds and fertilizer. The costs of the first year's inputs were covered by a grant from LEAD but eventually inputs were included in the overall credit package for farmers. Cargill also encouraged the practice of rotating cotton and sorghum. At harvest time, Cargill accepts farmers' deliveries of sorghum, which is purchased by large-scale animal feed operations and the largest local brewer of traditional beer (which includes sorghum). All partners have benefited from the programme. Farmers' cotton yields have increased (initially because they were using the fertilizer provided and later because of the benefits of rotating cotton with sorghum). With cash earned from their healthy sorghum crops, they can purchase local maize produced in the wetter regions of Zimbabwe. Cargill's cotton throughput has improved and local feed manufacturers and brewers have increased production and profits with the additional sorghum available on the market. Cargill has expanded the programme to include soybean and maize input packages (where agroclimatic conditions permit), to the benefit of all parties.

## Helping VC players to build trust and understand the value of long-term relationships

A critical success factor of any well-functioning VC is the level of trust and collaboration among its actors. Building trust and commitment to engaging in long-term relationships rather than looking for opportunistic, short-term, price-related gains is a key activity for ensuring the sustainability of a VC development initiative. This means promoting a transparent flow of information along the chain, communicating information about prices and quality standards to overcome typical information asymmetries between small-scale producers and private companies and facilitating and brokering contractual arrangements that are beneficial for both parties. For small-scale farmers, engaging in a long-term relationship with a commercial partner often implies the possibility of receiving financial and technical support to improve the quality, and consequently the price, of their products. This support is often embedded in contractual arrangements (e.g. contract farming), as in Case study 7 on Liberia and India.

### Case Study 7: Promoting long-term relationships between small-scale farmers and private companies in Liberia and India

In Liberia, a very promising partnership has been instituted among the Ministry of Agriculture, IFAD and the Liberia Agriculture and Asset Development Company (LAADCO), a private-sector exporter of cocoa and coffee. The Smallholder Tree Crop Revitalization Support Project has three components: i) construction of rural road networks; ii) rehabilitation of 1,000 hectares of cocoa and coffee plantations through links between smallholder farmers and the private sector; and iii) institutional development of three cooperatives. The project runs from 2012 to 2017, with LAADCO providing technical and extension services as well as financing; so far, it has invested more than US\$1 million, with an additional US\$5 million committed for project scale-up to another 15,000 hectares of cocoa or coffee. Approximately 1,000 farmers have already benefited from improved commercialization (prices have increased by 50 per cent compared with those previously paid by market intermediaries), larger quantities sold and better product quality.

In India, the IFAD-funded Convergence of Agricultural Interventions in Maharashtra's Distressed Districts Project (CAIM) is linking a significant number of smallholder farmers to the United Kingdom market for high-value baby maize. FieldFresh Foods, a private agribusiness company, provides the market link and supports farmers through a contract farming arrangement. CAIM acts as a facilitator, putting the company into contact with the farmers. The first season of production began in August 2012, with 100 farmers contracted to cultivate baby maize on 100 acres (about 40 hectares). In the second year, operations had expanded to 400 farmers on 400 acres (about 160 hectares). Farmers benefit through increased volumes sold, higher-quality produce, which now meets international standards, and increased prices. Long-term contractual arrangements and access to financial services and inputs have improved farmers' livelihood situation and farmers feed the maize plants to livestock, which has improved milk production.

## Acknowledging the diversity of business models that allow the sustainable inclusion of smallholders in VCs

Producer organizations are the typical entry point for IFAD projects (*producer-driven models*). Evidence from the field and the literature shows that this model has limitations and alternative models (*buyer- or intermediary-driven models*) are equally effective in achieving the necessary economies of scale for access to production factors and services, and efficient delivery of products. Whatever the option adopted (producer-, buyer- or intermediary-driven), some sort of organization of farmers is required. Farmers' organizations can reduce production costs by achieving economies of scale for procuring inputs, reducing produce collection costs, enhancing value-added through processing and better handling/storage, and helping producers cope with asymmetrical relationships in chains. They can also be extremely effective in representing farmers' interests and improving their bargaining power with private companies. See Case study 8 on Nicaragua and Paraguay.

### **Case Study 8: Supporting the development of strong farmers' organizations and their market contacts in Nicaragua and Paraguay**

In Nicaragua, the IFAD-funded Small-scale Producers in Value Chains and Market Access Project (PROCAVAL) supports farmers' cooperatives in improving their market access. The project facilitates communication and contacts with potential buyers, primarily by investing in capacity-building for cooperatives so that they can create contacts and develop and maintain sustainable relationships with profitable markets. For example, PROCAVAL has supported cooperatives in selling to coffee shops nationally because profitability is higher in this market than from international exports of green coffee. Another aspect of the project is strengthening the organizational capacity of cooperatives to ensure that increased earnings benefit their members. The project has also invested in public infrastructure, such as feeder roads to reduce transportation costs and losses during the transport of produce to markets.

In Paraguay, the IFAD-funded Empowerment of Rural Poor Organizations and Harmonization of Investments (Paraguay Rural) project provides support to small-scale producer organizations in various VCs to diversify production and obtain access to more profitable markets. Farmers' organizations are supported through the financing of business plans and are then responsible for identifying and implementing possible new business ventures. The organizations are strengthened so that they can identify their own training needs and hire appropriate trainers for capacity-building. The project facilitates collaboration with potential buyers and the rural banking sector to improve access to markets and credit. In some VCs, the project has facilitated the negotiation and implementation of contracts between buying companies and farmers' organizations. Experiences in the Paraguay Rural Project have laid the groundwork for a more market-oriented design in new projects, such as the Inclusion of Family Farming in Value Chains Project, with stronger emphasis on relationship-building between farmers' organizations and companies.

### **Strengthening sector and producers' associations for VC coordination and policy dialogue**

National and regional organizations can play important roles in VC projects. There are various models of association, with different memberships and mandates.

**National farmers' associations** (e.g. apex-level cooperatives or farmers' unions), when well managed, can be a highly effective means of facilitating dialogue between farmers and government. They can be well placed to provide national- and international-level information of great use to their members and can have the necessary influence to organize attractive financial and supply contracts. Due diligence is required to ensure that organizations are truly representative, responsive to their members' needs and concerns, and competent. These organizations sometimes adopt policy positions that are incompatible with a competitive VC approach (e.g. on issues such as price floors, subsidies, etc.) but this is also the case with national farmers' organizations in developed countries.

**Sector associations** seek to bring all or most members of a given VC together to work on programmes that are of interest to all. For example, the Eastern Africa Grain Council brings together producers, traders and processors to disseminate information on standards, trade, stocks and prices, providing an invaluable service for all actors in grain VCs. The Cotton Association of India represents the policy interests of cotton growers, ginners, brokers and importers/exporters, and provides services that include fibre testing, speedy arbitration of disputes and policy dialogue. These organizations can be useful partners for VC projects, particularly on policy issues. See Case study 9 on Senegal.

### Case Study 9: National Forum on the Industrial Tomato Value Chain in Senegal (CNCFTI)

Introduced in the Senegal River Delta in 1970/71, Senegal's industrial tomato sector has developed rapidly over the past 20 years, with sharp increases in area and tonnage. Access to credit has contributed to the flow of funds to producers, resulting in increased production. Between 1997 and 2006, industrial tomato production quadrupled from 20,000 to nearly 80,000 tons, while production of fresh tomatoes for the market grew from 5,000 to 45,000 tons. Today, the tomato sector is highly integrated. The Senegal Canned Food Company (SOCAS), a private company and major industry player with processing plants in Savoigne and Dagana, establishes contract agreements with local producers; CNCFTI, representing the Farmers' Union, the processors and the government, establishes production and marketing conditions (quantity, quality, price, payment terms, delivery, packaging, handling); and the Senegal River Development Agency (SAED) provides technical advice to producers and serves as Secretariat to CNCFTI. Most production is managed by smallholder farmers, all of whom are members of the Farmers' Union. They have access to irrigation (especially drip irrigation) and credit. A unique feature is that both the processors and the farmers contribute about half a per cent each from sales to a guarantee fund, which serves as collateral to the banks providing credit to producers.

The creation of CNCFTI in 1988 was in response to characteristics of the industrial tomato sector, including the geographic concentration of production, the high level of integration, the fragility of the product and the importance of producer organizations. CNCFTI is now recognized by the state, with statutes, internal regulations and periodically renewed governing bodies. Major members of CNCFTI report that producers are now interacting with other industry players, thanks to the experience in industrial processing they have gained through SAED. CNCFTI is made up of representatives of the different occupations and institutions involved in the industrial tomato chain and comprises: i) the Farmers' Union (as a strategic partner; ii) the Processing Industry Union (as a strategic partner); iii) financial institutions (as associate partners); and iv) public institutions (as associate partners).

## Strategic recommendations

Drawing from these lessons learned, this section outlines strategic recommendations for the design of VC projects. All of these points are elaborated in the How To Do Note on designing commodity VC development projects.

- **“VC approach” versus “VC development project”.** The VC approach is being increasingly adopted as an analytical and operational tool for the latest generation of IFAD-funded projects. However, in the context of IFAD's mandate, this does not necessarily mean that all IFAD projects should directly address the comprehensive development of an entire VC; instead, they can focus on specific elements of a chain.
- The VC approach is not a blueprint but needs to be adjusted to each country/context based on a systemic and comprehensive examination of the interactions between small-scale producers and other VC actors (including both micro and macro aspects). This enables the identification of **key entry/leverage points** to make a VC work better for small-scale producers. By looking beyond bottlenecks at the production level, the VC approach helps identify issues at different levels of the VC or in the business environment (legislation, regulatory framework, policies, infrastructure, etc.) that affect producers' capacity to be sustainably included in a particular VC.
- An essential area for **policy dialogue** is the role of the government and the overall public sector in creating the enabling environment and institutions for better functioning VCs and in providing public goods to address market failures (e.g. transportation infrastructure, public food standards) and to create incentives to make investment in a VC and partnership with small-scale producers economically more viable and/or less risky for the private sector.

- At the project design stage, there may not be enough time and resources to carry out an in-depth commodity VC study. However, it is critical to identify in advance the commodity VCs in which there is a business case for involving small-scale producers – i.e. **in which small-scale producers have a comparative advantage** – and in which VC actors are committed to engaging in mutually rewarding win-win arrangements. A more comprehensive analysis of the commodity VC should be carried out during implementation, using a **participatory** approach with VC players.
- It is important to realize that the **poorest segments of the rural population (the bottom of the pyramid)** are often unable to meet the requirements for sustainable integration into dynamic VCs (modern markets). However, less competitive and demanding traditional (local) markets can offer many opportunities for these segments of the rural population.
- It is also critical to analyse the **roles of women (and youth)** within the VC. Typically, women and youth face additional constraints in obtaining access to assets (e.g. land) and services (credit) and are underrepresented in farmers' organizations, despite the enormous amount of work they do at particular stages of the production and marketing process. VC opportunities may exist in farming (e.g. branding of women farmers' produce), off-farm microenterprises or wage employment.
- VCs evolve continuously and can change rapidly. The focus should, therefore, be on **building the capacity** of VC actors to remain competitive, particularly by responding to and/or anticipating market and VC changes. **Flexibility** in project design is critical to allow adjustment in a very dynamic context.
- IFAD does not implement its projects directly; government is the implementing agency. The relationship between the public and private sectors is often a country-specific challenge so a third-party **facilitator/broker** is needed to build **mutual trust** among the different parties (farmers' organizations, private sector companies, the government) and to help identify issues of common interest for a more efficient and profitable VC.
- It is important to analyse all the possible **business models** that allow sustainable inclusion of small-scale producers in VCs, in addition to IFAD's typical project entry point (producer organizations in producer-driven models). Evidence shows that alternative buyer- or intermediary-driven models can be equally effective in achieving the necessary economies of scale.
- A critical dimension of a VC is the type of **contractual relationship** between small-scale producers (suppliers) and large-scale investors such as agribusiness companies (e.g. processors or exporters). **Contract farming** has become increasingly important in modern markets – particularly for highly perishable and labour-intensive crops – and may generate win-win situations. However, for both parties (small-scale producers and agribusinesses) there are also risks, which depend on context-specific factors that need to be carefully analysed (e.g. the law enforcement environment, the bargaining capacities of producers and their organizations, the motivation of agribusinesses, the nature of the commodities). Alternative contractual arrangements such as management contracts, tenancies and joint ventures all have their own advantages and disadvantages, depending on the context (Vermeulen and Cotula, 2010).
- **Fair and transparent governance** of the VC is key to ensuring better quality and consistency of production and stable benefits for small-scale producers. The agreed terms of trade, quality standards and pricing structure (including premiums and penalties) throughout the chain should be made clear from the outset. Support to small-scale producers in contract negotiations with other VC actors is a crucial area of intervention for a development project. Governance should be carefully monitored during implementation to ensure that communication flows along the chain and that no actor takes an "elite capture" attitude.

- The constraints faced by small-scale producers and rural microenterprises and small and medium-sized businesses in obtaining access to **working and investment capital** in the context of the VC should be analysed. Among VCs, the financing arrangements between buyers and suppliers are many and varied. Tripartite arrangements involving farmers, buyers and a financial institution are also possible. Cash flow problems resulting from delayed payments from buyers can be addressed by the piloting of factoring and warehouse receipt schemes, while leasing of small production equipment may also be an option. IFAD should map all existing arrangements throughout the chain to determine whether there is a financing gap and whether additional financing mechanisms may be needed.
- Integration into a VC requires a high level of **product specialization** (technology, farming practices, certification, etc.), which conflicts with the natural tendency of small-scale producers to diversify. This makes small-scale producers potentially more exposed to risks (climate change, natural and market-related). A VC approach should help to identify strategies and mechanisms for sharing risks and costs more equitably throughout the chain (equitable risk management business models) and look for innovative risk management instruments (e.g. weather index insurance, guarantee schemes).
- The VC approach offers opportunities to identify from the outset **win-win, public-private-producer partnerships** (4Ps) at the local, domestic and global levels, building on current trends that go beyond fair trade and corporate social responsibility. For sustainability, it is critical to leverage **incentives** that increase the competitiveness of the VC, generate wealth for all participating actors and put the private business sector in the driver's seat of VC development.



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