Using a value-chain approach to empowering the rural poor in Kenya, Tanzania and Mozambique

Making Markets Work for the Poor (M4P)

Stellenbosch

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Making Markets Work for the Poor M4P In Southern and Eastern Africa

TECHNOSERVE
Business Solutions to Rural Poverty

Today's Discussion

TechnoServe's Approach

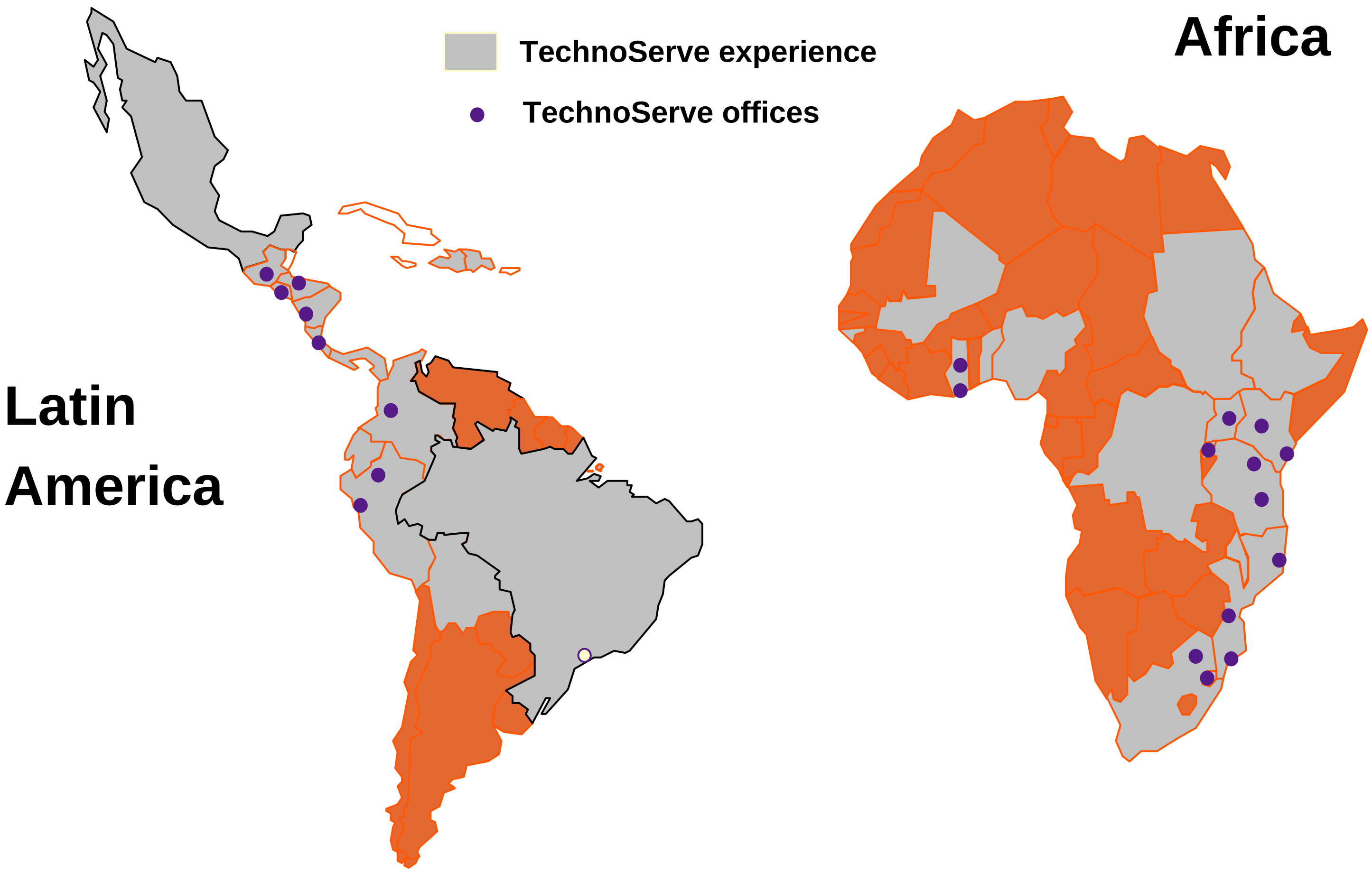
Value Chain Case Studies

Lessons Learned

Who We Are

- A U.S.-based, nonprofit economic development organization.
- Philosophy: Private enterprise can drive economic growth and positive social change; a hand up is better than a handout.
- History: Founded in 1968 by businessman Ed Bullard, who pioneered the private-enterprise approach to solving poverty.
- Staff: Talented business advisors, many of them former management consultants or industry experts.
- Partners: Leverage the expertise of strategic corporate, non-profit and government partners.
- Funding Sources: U.S. and foreign government agencies, multi-lateral organizations, corporations, foundations and individuals.

TechnoServe has 39 years' experience across Latin America and Africa



TechnoServe's Mission: Create income, employment and opportunity by improving industry competitiveness for rural poor

Our core beliefs…

- **Private companies** are essential to grow industries, improve incomes and create employment
- **Sound business strategies** and **excellent execution** make companies successful
- To increase incomes for rural poor in the long term we have to focus on **improving company level performance** to **enhance industry competitiveness**

Our approach…

- **Client selection:** We identify entrepreneurial men and women that want to build businesses
- **Business development:** We use proven business methodologies to help them plan, market, operate and expand their business
- **Best practice mentoring**: We leverage entrepreneurs to improve competitiveness and bring in global best practices through mentorships with our network of corporate partners
- **Policy**: We tackle industry constraints to ensure the entire industry value chain is competitive and positioned for sustainable growth

A tool that we use to define development opportunity is value chain analysis, looking at each discrete step in the life of a product, the players at each step, how value is added, and how much they earn for that value created

Production

- Add value through bulking from the small scale producers
- Ensure reliable supply of high quality inputs and fair price to the community

Processing

- Process and package
- Reach internationally competitive cost and quality

Marketing

- Brand the products and build reliable distribution
- Access international markets and pursue local markets

Viable, sustainable, and value-added business

Enabling environment

Facilitate transition to processing via incentives and assistance of the private and public sector

In 2005, TechnoServe-assisted businesses generated $50M in revenues and bought $35M in products from 143,000 rural producers

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TechnoServe applied tailored approaches to three African industries to sustain and grow industry competitiveness

Banana	COLLAPSED: (Kenya) The banana value chain was long – involving several middlemen – thus distancing the farmer from the value received farther down the chain
Coffee	UPGRADED: (Tanzania) The coffee value chain was compact, resulting in a low-quality commodity product, which was then sold through the auction for lower prices
Cashew	RATIONALIZED: (Mozambique) The cashew value chain needed to be “rationalized”; it was a confused value chain under great scrutiny and pressure, with much of the raw product being exported before any value addition

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Value Chain Case Studies – Banana

Lessons Learned

In Kenya and Uganda, bananas needed to pass through a long value chain before reaching the retailer

Producer	Transporter	Multiple Brokers	Wholesaler	Retailer
▪ Most farmers tend to be small scale (<1 ha) ▪ Limited knowledge of market information ▪ Negotiations based on size and type ▪ Limited ability to wait (perishable product)	▪ Transporters bring from farm to collection center ▪ May have pricing power depending on competition ▪ Limited ability to wait to sell (perishable product)	▪ Generally 1-3 brokers ▪ Roles include bulking and transporting to larger markets	▪ Sell to urban retailers or directly to consumers ▪ Can also serve as broker ▪ May extend limited credit to brokers	▪ Range from those selling in central markets, supermarkets, and on roadside ▪ Generally do not store significant inventory • Purchase frequency high

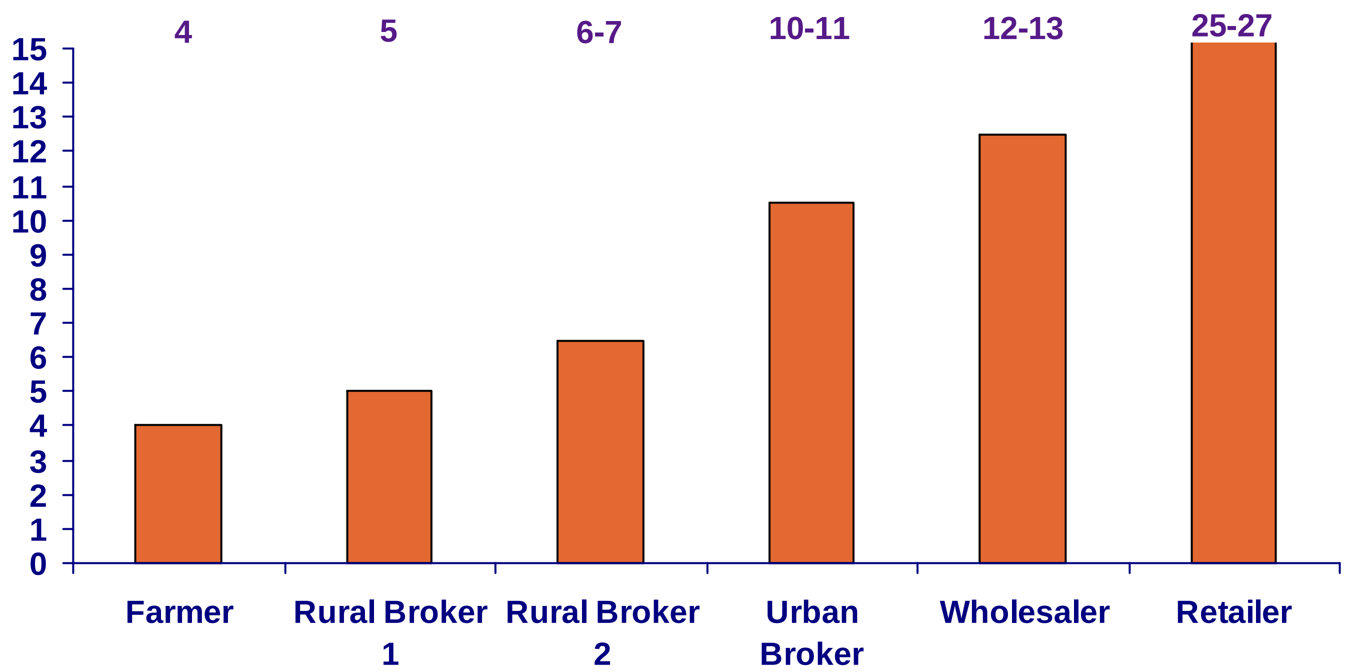
Opportunity: Change the logistics of the supply chain, bulking the bananas via larger business groups and connecting them directly to urban wholesalers

Source: TechnoServe Analysis.

In the traditional banana model, long value chains were limiting margins for the smallholder farmer

Kenyan Dessert Example

Selling price by vendor (Kenyan shillings/kg)



Farmer Retains ~10-20% of Retail Price

Source: TechnoServe Analysis.

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For the banana industry, TechnoServe condensed the value chain to increase its efficiency

Producer | ***Transporter*** | ***Multiple Brokers*** | **Wholesaler** | **Retailer**

Producer

- Through collective action, farmers take on additional roles creating efficiency and minimizing players:
  - Grading
  - Bulking
  - Transport
- With reliable markets, farmers are now credit-worthy
  - Partnership with micro-finance loan enables previously unbankable farmers to source loans

Transporter / Multiple Brokers

- *Transportation and brokerage now executed by producer*

Wholesaler

- Former brokers create formalized banana trading businesses due to increased capacity; they now handle transport and are able to service more sophisticated markets

Retailer

- Wholesalers are often able to access retail markets as well, dedicated retailers now have reliable access to quality, market-differentiated products

Source: TechnoServe Analysis.

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In the traditional banana model, long value chains were limiting margins for the smallholder farmer

Kenyan Dessert Example

Selling price by vendor (Kenyan shillings/kg)

- 2,500 farmers income increased 150%, from ***$100K to $250K total income***

Additional Roles:

Farmer	Wholesaler	Retailer
Grading Bulking Transport	Add'l Transport	Market Differentiated product

Farmer Retains ~30-40% of Retail Price

Source: TechnoServe Analysis.

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Value Chain Case Studies – Coffee

Lessons Learned

The coffee value chain lacked key sub-steps to facilitate productivity, quality, and market access for small farmers

Producer	Agent	Export
■ 90% of Tanzania's Arabica crop produced by 400,000 small-scale growers on plots of 1 hectare ■ Use 'back-yard' processing techniques that result in low quality ■ Lack of quality incentives and non-existent extension services result in low farm productivity • Yields fell from 270 kg/ha parchment in the 1970s to 170 kg/ha parchment today	■ Most producers sell their crop to traders or cooperatives that do not provide incentives for quality	■ All coffee sold through national auction – wholesalers lacked direct marketing opportunity

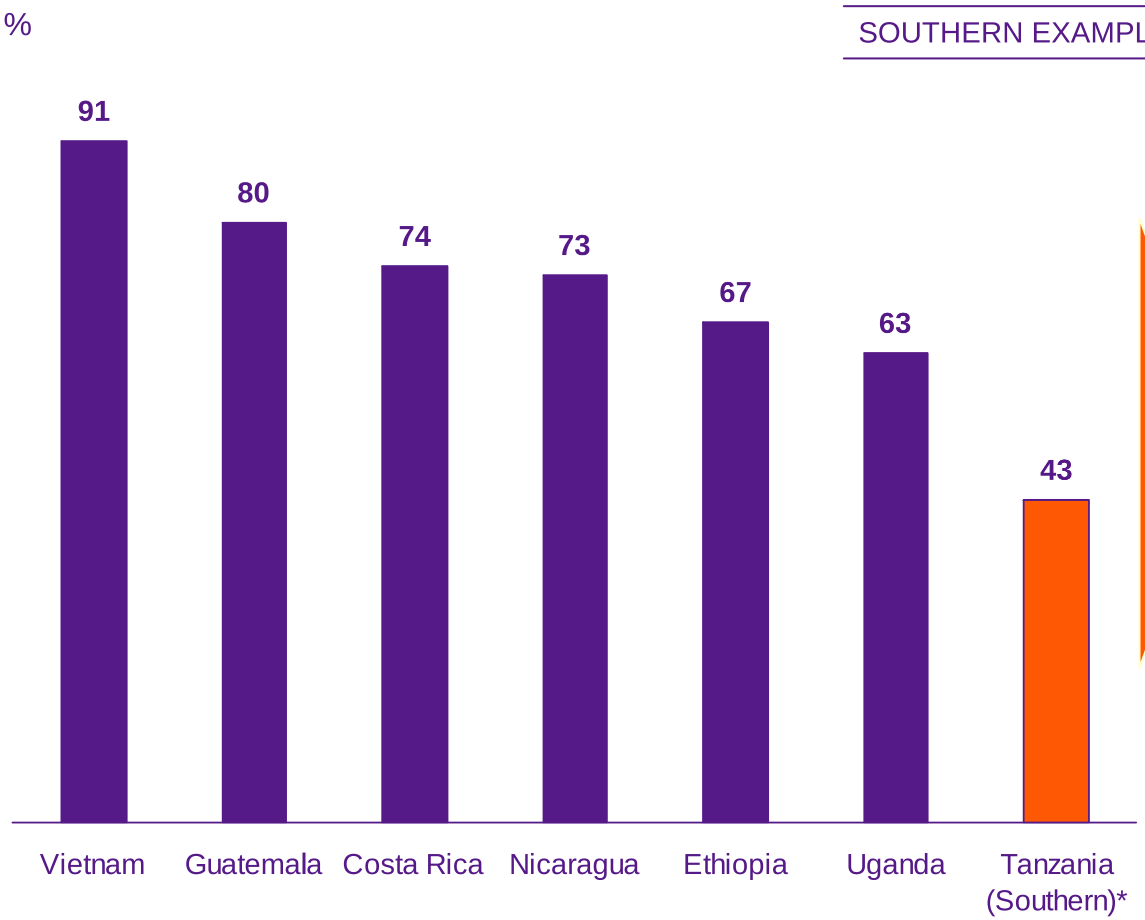
Opportunity: Regain Tanzania's position as a supplier of specialty coffee (high of 17% of production in 1970s, down to 1.7% in 1998)

Source: TechnoServe Analysis.

Value chain issues meant that Tanzanian smallholders were receiving less of green coffee selling price than competitors

Percent of FOB Getting to Smallholder Farmer

SOUTHERN EXAMPLE



- Smallholder profit just 20% of farm gate price
- Smallholder annual earnings just $65 / year*

*This was calculated using data from farmers in Southern Tanzania

Source: McKinsey International Coffee Comparison Report - July 2003; AKSCG accounts; Interviews with smallholders; team analysis

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As of 2001, interventions targeted every stage, focusing on producer development, credit / market linkages and quality-focused processing

- *TechnoServe facilitated **KILICAFE**, a unique business-focused consumer cooperative that sells services to its smallholder-owned farmer business group members - transparently passing on quality-based incentives*

Producer

- Initiated development of production department and best agricultural practices
- Coffee diversification-ventures in banana proved to be success

Pulping

- *55 of 104 FBG's currently using **Central Pulpery technology***
  - *CPU's improve quality, pricing up 70%; free families from labor intensive task of home processing*

Milling

- *Farmer retains product; now contracts milling himself/herself*

Warehousing

- *Deferred sales allows premium pricing to flow to farmer*

Auction / Direct

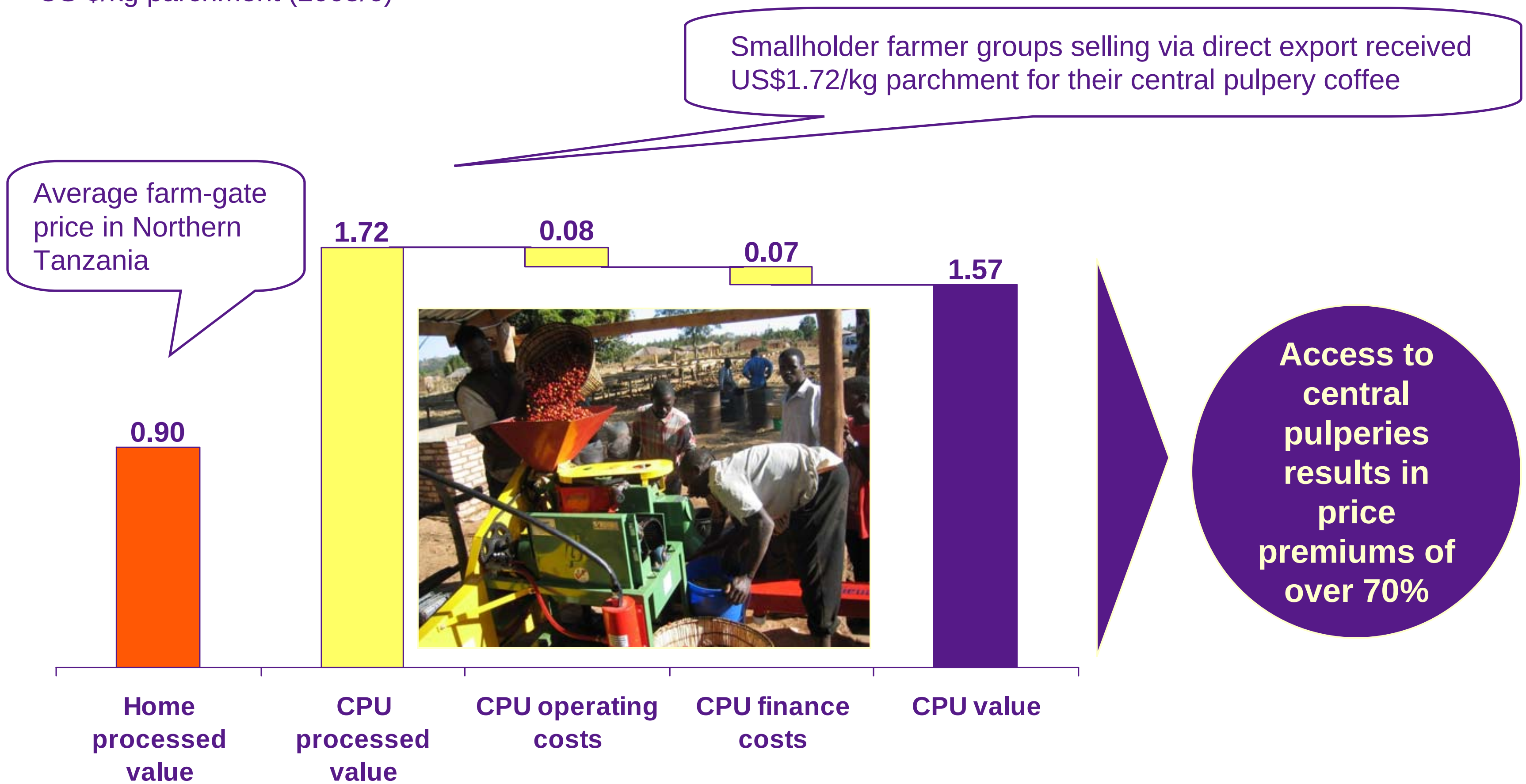
- Increase in % of Direct Exports (DX) is due to rapid expansion of CPU's
  - >30% KiliCafe coffee projected to sell direct in 06
- 15 containers sold by direct export to Starbucks, Peet's, Gepa and Unicafe

Source: TechnoServe Analysis.

Value chain assistance provided through the implementation of Kilicafe and CPU's resulted in double prior price for farmer

Home Processed v. Central Pulpery (CPU) Value

US $/kg parchment (2005/6)



* Average of three KILICAFE producer groups employing best practices.

Source: TechnoServe Analysis.

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Value Chain Case Studies – Cashew

Lessons Learned

In 2001, the Mozambican cashew value chain consisted of production and export of raw cashew nut to India

Mozambique (Production; Raw Nut Marketing / Aggregating)

External (Raw Nut Export; Primary Processing (India); Final Processing (India or Final Markets); Retail / Consumption)

Production	Raw Nut Marketing / Aggregating	Raw Nut Export	Primary Processing (India)	Final Processing (India or Final Markets)	Retail / Consumption
▪ ~1M smallholders earning ~ $35 gross income p.a. ▪ Little public sector, civil society or private sector support/ impact ▪ National production <25% of historic high ▪ Cashew quality is relatively poor	▪ Series of 2-3 traders/middle-men from farmer to exporter ▪ No payment for quality and poor post harvest handling results in loss in income of up to 5%	▪ ~5 large exporters, 20+ smaller ones ▪ >98% exported to India	▪ Many manual technology processors creating large number of jobs	▪ E.g. Kraft / Planters ▪ Earnings depend on channel (hospitality vs. retail), packet size, etc.	▪ Two major kernel import markets (excl. Indian internal demand, which is world's second largest) • USA 50% • Europe 29%

Opportunity: Good industry fundamentals, with demand outpacing supply each year and an existing processor base willing to invest and see others invest alongside

Source: TechnoServe Analysis.

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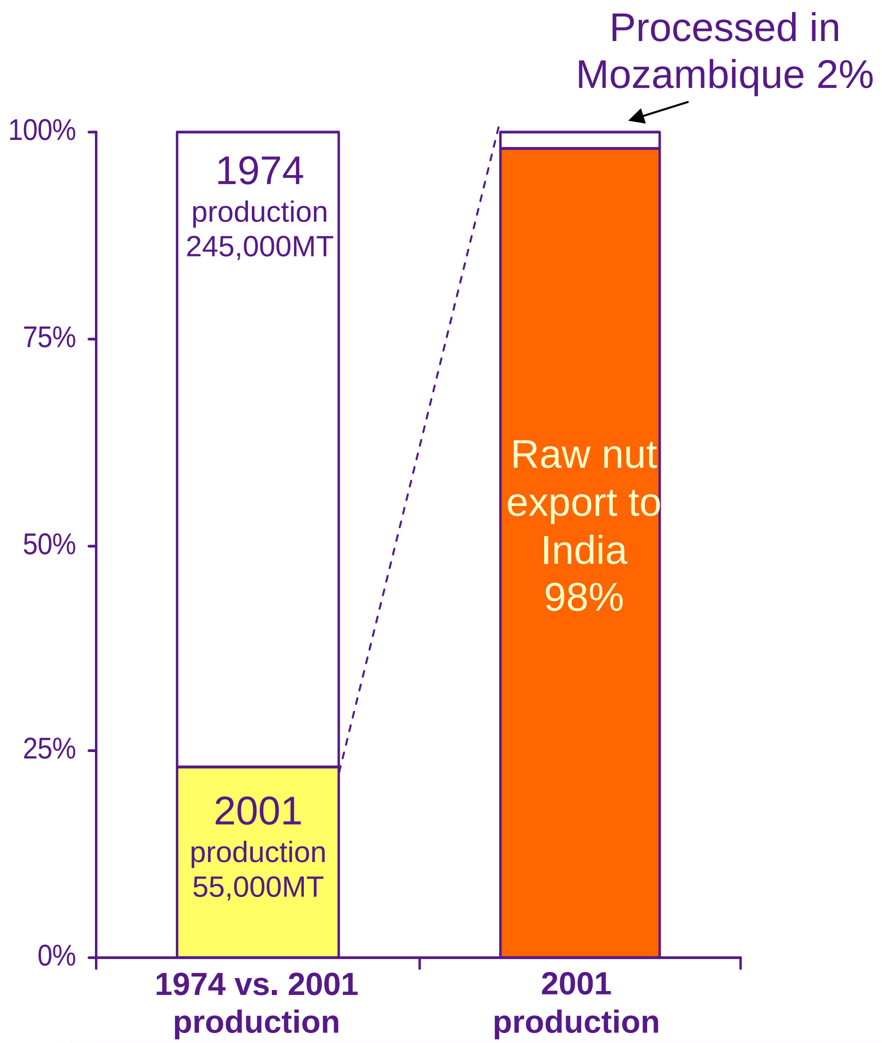
Production had declined, there was almost no processing and farmers stood to lose their single market



Impact of Raw Nut Export

- **98% of production at risk of losing market –** Indian demand for Mozambican raw cashew nut is declining owing to:
  - Competition from higher quality raw cashew nut origins especially South East Asia and West Africa
  - Planting in India to reduce reliance on imports
  - Traceability regulations in largest kernel markets in developed countries
- **No potential for contract farming** / private sector investment in farming
- **No benefit from domestic processing** industry in terms of jobs, export earnings and rural economic activity

Sources: TechnoServe Analysis

TechnoServe has assisted to build Mozambique's processing industry to create a local market for farmers

Mozambique | **External**

Production → **Raw Nut Marketing / Aggregating** → **Raw Nut Export** → **Primary Processing (India)** → **Final Processing** → **Retail / Consumption**

Production
- Growing relationships with private sector market (~200,000 farmers supply local processors)
- TechnoServe led a quality census and training program to improve post-harvest handling

Raw Nut Marketing / Aggregating
- Processors increasingly go direct to farmers
- Processors can pay more for quality (up to 15% premiums in 2005/06 season)

Raw Nut Export
- Raw nut export persists for ~65% of cashew

Final Processing
- E.g. Kraft/Planters
- Earnings depend on channel (hospitality vs. retail), packet size, etc.

Retail / Consumption
- Two major kernel import markets (excl. Indian internal demand, which is world's second largest)
  - USA 50%
  - Europe 29%

Primary Processing (Mozambique)
- ***>35%** processed in country*
- *>4,000 jobs created in rural or small settlement areas*

Source: TechnoServe Analysis.

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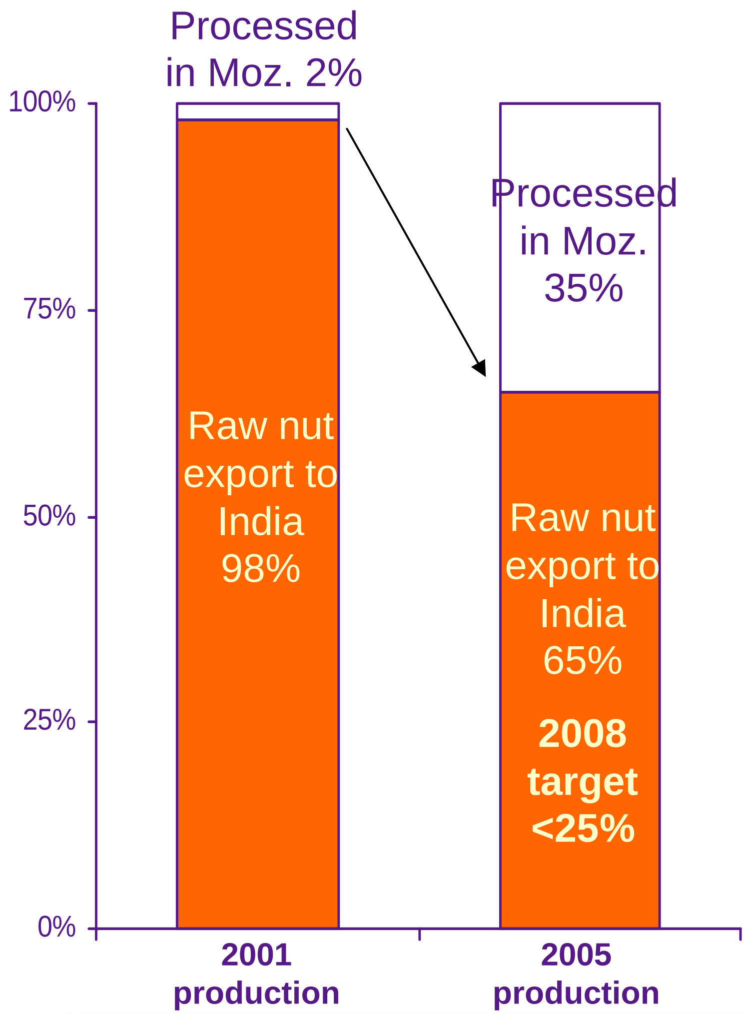
Future farmer income has been secured and a platform provided for growth and rural poverty reduction



Impact of Raw Nut Export

- **Smallholder farmers**:
  - Secure local market created for 200,000 farmers
  - Relationships with rurally located processors are being developed and premiums are being paid for quality (up to 15% over the market price)
- **Factory employees**
  - 15 factories employing over 4,000 workers in rural or semi-rural areas, where there is often little of no other permanent employment options
- **Community and economy**
  - US$ 7.1 million in earnings from kernel exports (kernels have ~50% higher value than raw nuts)

Sources: TechnoServe Analysis

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Tailored approaches to these three industries has resulted in significant impact in each…

Banana

- Wholesaler truck utilization up 2.5 times (2 day trip instead of 5)
- Geographic extension from Kenya to Uganda and Tanzania
- Farmer impact even greater in Uganda with income up 3x

Coffee

- From 2002 to 2006, sales up from $750,000 to $4 million
- Working capital revolver with commercial bank up from $150,000 to $1 million
- Farmer count up from 5,000 to 10,000
- Kilicafe doing its own marketing (Japan, RSA) and footing our bill

Cashew

- From no factories to 15 between 1,000 and 2,500 tons
- Processors have formed their own brand of Mozambican cashew
- Methodology extended to TZ and KE in a 4-year, $6 million, three donor, three country program
- Utilizing the Ea/So Africa program to establish a W. Africa program

For a value chain approach to increasing income of the rural poor, donors, stakeholders and partners should consider the following:

Industry-Specific Approach	Each industry must be analyzed and understood for its own dynamics. One must have a solid analytical understanding of the value chain commercial links from player to player and economics of each
Coordinated Effort	Each step in the value chain must be examined, to include production, processing, distribution and marketing, as well as policy
Progressive Approach	Progressive approach is required over time and entails addressing all steps in the value chain to meet the needs of the market. That is, progress in one area reveals needs in another (e.g., taxation & marketing in coffee)
Movement up Value Chain	Provide opportunity for producer to participate further up the value chain in additional value added activities and through direct market access (e.g., bulking & transport in banana; pulping, milling & warehousing in coffee)
Key Inputs	Identify key inputs lacking in the supply chain in order to make it work for the producer: inputs and credit (cashew), agronomic training (banana), enabling policy (coffee and cashew) working capital financing (Kilicafe in coffee)
Sufficient Timeframe	5-7 years are required to build a self-sustaining, competitive value chain – shorter approaches will not sustain gains or build local capacity

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