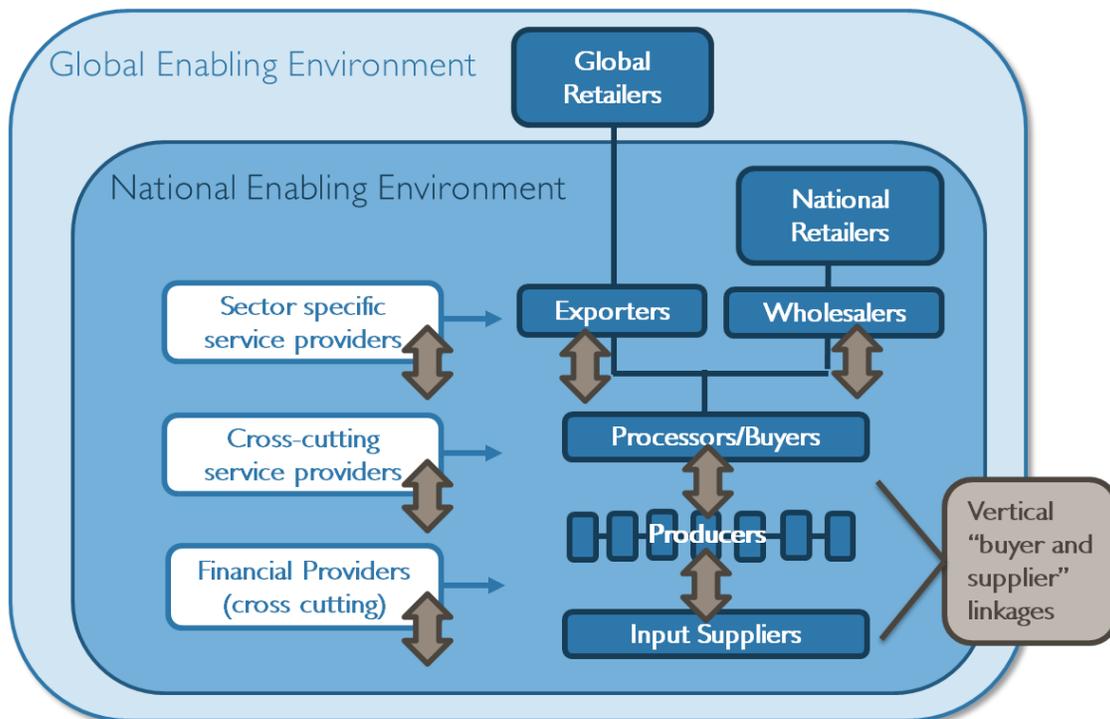


### III. Linking Extremely Poor Producers to Buyers and Suppliers

#### A. Buyer and Supplier Linkages for the Extremely Poor

Extremely poor producers are linked to a range of micro, small, and medium enterprises that buy from and sell to each other, including wholesalers, retailers, exporters, traders, middlemen, input dealers, suppliers, and service providers.



#### 1. Why are Linkages with Buyers and Suppliers Challenging for Extremely Poor Producers?

Challenges exist, as extremely poor producers:

- ▶ Buy inputs in such small quantities and so infrequently that it is not worthwhile for input supply firms to make an effort to sell to them
- ▶ Produce in such small quantities that it is not worthwhile for buyers to make an effort to buy from them
- ▶ Do not feel comfortable interacting with larger or more formal businesses as they do not understand their business culture and norms
- ▶ Do not feel comfortable negotiating business contracts, or even basic pricing and ordering
- ▶ Are influenced by informal rules and norms that limit their ability to interact with other businesses or their ability to benefit from commercial transactions in any significant way

## 2. How Can Buyer and Supplier Linkages be Used to Benefit Extremely Poor Producers?

Change within market systems, such as agricultural market systems, involves shifting production systems from drawing on indigenous or local knowledge to ones that depend on technical knowledge from input suppliers or buyers and meet consumer preferences.

Besides financial benefits, mutually beneficial linkages between extremely poor producers and their buyers or suppliers can transfer knowledge, information, and technical, financial, and business services from one business to another. These non-financial transactions are important parts of buyer-seller relationships and are vital for practitioners to understand. The levels of trust and the volume and quality of information and services disseminated often determine the distribution of benefits between businesses and producers. Understanding the informal rules and norms that govern behaviour and transactions (including gender issues), particularly in the informal sector, becomes especially important in the context of extremely poor producers, as do the gender issues to be considered (discussed in more detail later in this guide).

Benefits of mutually beneficial linkages with buyers and suppliers include:

- Mutually beneficial business relationships
- Effective knowledge and information transfer
- Meeting appropriate quality standards
- Beneficial embedded services
- More equitable financial flows

The following table addresses strategies to facilitate mutually beneficial relationships for extremely poor producers with their buyers and suppliers. The table lists the outcomes of beneficial buyer and supplier linkages and the associated role of the practitioner organisation in facilitating each of these. Practical examples are given to assist understanding and applicability to practitioners' field-based contexts. Use this to identify the role that development projects can play in facilitating beneficial linkages between extremely poor producers and their buyers and suppliers.



## Effective Vertical Relationship Facilitation Strategies

This table identifies effective facilitation strategies for mutually beneficial buyer and supplier relationships with extremely poor producers.

Practitioner role in facilitating beneficial buyer & supplier linkages	Practical examples
<ul style="list-style-type: none"> <li>Facilitate the development of strong, long-term, mutually beneficial business relationships that recognise and function alongside informal rules and norms that impact extremely poor producers</li> </ul>	<ul style="list-style-type: none"> <li>Rather than focusing on increasing one-off sales, facilitate the development of long-term, win-win business relationships</li> </ul>
<ul style="list-style-type: none"> <li>Facilitate the effective and smooth transmission of information and knowledge from buyers or input suppliers to extremely poor producers</li> </ul>	<ul style="list-style-type: none"> <li>Information on quality standards and specifications, such as food regulations, food safety, food controls, or nutritional certifications</li> <li>Knowledge on how to use inputs most effectively or how to use specific equipment to improve a product in a way that the final consumer would most value</li> </ul>
<ul style="list-style-type: none"> <li>Facilitate beneficial embedded service arrangements</li> </ul>	<ul style="list-style-type: none"> <li>Such as linkages to businesses that pay for crops before they are harvested to reduce initial cash needed by extremely poor producers</li> <li>Such as how to comply to food safety standards or other certifications needed in order to be able to participate in the market, or how to accurately label food as required by the market</li> </ul>
<ul style="list-style-type: none"> <li>More equitable financial flows</li> <li>Facilitate more win-win financial flows in which both sides are receiving higher profits or more stable income flows</li> </ul>	<ul style="list-style-type: none"> <li>Such as ensuring that producers can earn a living from what they get paid while buyers are still able to make adequate profits to stay in business</li> <li>Such as using the receipt from a warehouse to show how much produce they have stored there (awaiting a better market price) as collateral for credit from a bank. This is referred to as the warehouse receipts model.</li> </ul>
<ul style="list-style-type: none"> <li>Increased trust levels</li> <li>Facilitate processes that increase trust</li> </ul>	<ul style="list-style-type: none"> <li>Take small steps to slowly demonstrate trustworthiness from both sides</li> </ul>

### 3. What Types of Buyer and Supplier Linkages are Most Suitable for Extremely Poor Producers?

The most common types of vertical linkages that extremely poor producers might have are:

- Linkages between producers and input suppliers
- Linkages between producers and their buyers

Market linkages can range from informal agreements with local traders to formal contracts with exporters. It is important to understand the types of linkages that could exist and to determine what type of linkage would be most appropriate for a particular producer or group of producers at a particular time.

**Reality check on challenges:** Think about the case of a contract with an urban supermarket 50 km away to supply a certain quantity of produce at an agreed upon price. The advantages of this are that producers are guaranteed a market and a price. However, can the producers maintain a consistent supply that meets the quality standards?

Keep in mind that developing business relationships is an iterative process in which learning and reflection lead to action, which leads to more learning and reflection and potentially a different action (or type of linkage). Extremely poor producers will typically need to begin working quite informally with local traders to build trust and confidence. Then, as they become more confident in their own production systems over time, producers may decide to work with a higher level of buyer or search for a contract with a small supermarket. As they begin to become more capable, they may start to think about how they can sell their produce to exporters or larger, global buyers.

The field example “Taking Gradual Steps” demonstrates how important it is to take small steps in supporting extremely poor producers to build business relationships with others in the marketplace rather than expecting them to move too quickly in being able to take on new business relationships successfully.



#### Field Example: Taking Gradual Steps

In Indonesia, World Vision is working with extremely poor cocoa producers who are now developing relationships with Cargill and Mars. It has, however, taken some time for them to be confident in dealing with this level of buyer. The cocoa farmers started by dealing with the local collector, and then after some time, they began dealing with the wholesaler at the port, and now they are beginning to talk to the large exporters. To try to work with Cargill and Mars from the start would have been a number of steps too far ahead of the extremely poor producers' capabilities.

The following is a matrix of several common forms of market linkages and their advantages and disadvantages for producers. Use the matrix to help determine which form would be most appropriate for the producers with whom you are working.



## Benefits of Different types of Vertical Linkages

This matrix analyses different types of linkages between poor producers and their buyers and suppliers.<sup>1</sup>

Type of Linkage	Collective Activity	✓ Advantages for extremely poor producers	✗ Disadvantages for extremely poor producers
<b>Producers to traders</b>	<ul style="list-style-type: none"> <li>Producers usually act on a one-to-one basis with traders</li> <li>May work together informally to bulk-up produce to reduce costs and attract larger traders</li> </ul>	<ul style="list-style-type: none"> <li>Requires high level of trust. Such trust is likely to ensure long-term sustainability</li> <li>Formal farmer organisations not usually needed</li> <li>Traders may provide training in production and handling</li> </ul>	<ul style="list-style-type: none"> <li>May need to accept short-term deferred payment</li> <li>Limited access to high-value markets</li> </ul>
<b>Producers to retailers or their wholesalers</b> <i>(including restaurant chains and supermarkets)</i>	<ul style="list-style-type: none"> <li>May require formal group structure, particularly when buyer does not want to deal with producers individually</li> </ul>	<ul style="list-style-type: none"> <li>Reliable market at agreed upon price</li> </ul>	<ul style="list-style-type: none"> <li>Must meet variety, quality, and safety specifications</li> <li>Must be able to supply agreed quantities at all times (this may place producers in conflict with social obligations)</li> <li>May have to accept deferred payment of up to 90 days</li> </ul>
<b>Producers to retailers' village agents</b>	<ul style="list-style-type: none"> <li>A local person who is part of the community, often a successful local farmer, acts as a sales agent to a local agrodealer, and serves a large group of farmers</li> </ul>	<ul style="list-style-type: none"> <li>Poor producers trust the local agents</li> <li>Agents are able to bulk sales orders for greater efficiency for the retailer</li> <li>Decreased transport costs as retailers make bulk deliveries to the agent who disseminates locally to farmers</li> </ul>	<ul style="list-style-type: none"> <li>Only works in areas where retailers have established a village agent model (although project could initiate this)</li> </ul>
<b>Producers to agro-processors</b>	<ul style="list-style-type: none"> <li>Farmer groups can bulk-up produce for collection by processor</li> </ul>	<ul style="list-style-type: none"> <li>May provide secure market at agreed price</li> <li>Offers additional access to</li> </ul>	<ul style="list-style-type: none"> <li>Lack of market for the processed products, thus jeopardising sustainability</li> </ul>

<sup>1</sup> Adapted from Shepherd, Andrew W. 2007. Approaches to Linking Producers to Markets. Agricultural Management, Marketing and Finance Occasional Paper 13. p. 8-9

Type of Linkage	Collective Activity	✓ Advantages <i>for extremely poor producers</i>	✗ Disadvantages <i>for extremely poor producers</i>
	<ul style="list-style-type: none"> <li>Groups can facilitate supply of inputs and provision of technical assistance</li> </ul>	<ul style="list-style-type: none"> <li>local market</li> <li>Inputs may be supplied on credit</li> <li>Technical assistance may be provided</li> <li>Processor often provides transport</li> <li>Potential for producers to sell larger volumes</li> </ul>	<ul style="list-style-type: none"> <li>Must meet variety, quality and safety specifications</li> <li>Open market price may be higher than that agreed with processor</li> <li>Risk of delayed payments</li> </ul>
<b>Producers to exporter</b>	<ul style="list-style-type: none"> <li>Often involves grouping of producers</li> <li>External assistance may be required</li> </ul>	<ul style="list-style-type: none"> <li>Potential high returns if quality can be achieved</li> <li>Inputs and technical assistance may be supplied on credit</li> <li>Exporter often provides transport and packaging</li> </ul>	<ul style="list-style-type: none"> <li>Export markets are inherently risky</li> <li>Compliance with standards (e.g., organic, quality and traceability, fair trade) can be problematic, even with technical assistance</li> </ul>
<b>Producers to larger scale farms</b> <i>(through formal contract farming arrangements)</i>	<ul style="list-style-type: none"> <li>Company may prefer to group producers, formally or informally, for input and output marketing and extension</li> <li>External assistance may be needed to support producer groups</li> </ul>	<ul style="list-style-type: none"> <li>Inputs may be supplied on credit. In the case of crops that take a long time to produce, such as palm oil, tree crops, or sugar, credit is essential and may be provided for subsistence expenses</li> <li>Technical assistance may be provided</li> <li>Crop marketing organised by company</li> </ul>	<ul style="list-style-type: none"> <li>Companies often require external agency (bank) to finance credit provision</li> <li>Frequent mistrust between producers and companies</li> <li>Contracted price lower than market price may lead to side-selling</li> <li>Difficulties may be experienced if development organisation withdraws</li> </ul>



### **Field Example: Agrodealers use Village Agents to Serve Extremely Poor Producers in Kenya**

In Kenya, access to inputs is a major constraint to improving farmers' yields and quality. The Kenya Markets Trust supports agrodealers in setting up village agents to serve rural farmers. The project supports agrodealers on how to select and manage local agents, who are often successful farmers themselves, to work on a commission basis to distribute inputs to local farmers. The farmers trust the agents as they are from their local community, and they learn about what inputs are available and how to apply them. The agents bulk the farmers' orders and places one large order with the agrodealer, which makes it more cost effective for agrodealers to work with poor farmers as this decreases the cost per transaction. Through village agents, agrodealers are able to provide inputs to farmers in very rural areas, and farmers are able to access inputs at a reasonable price without high transport and intermediary costs.

Therefore, in working with farmers in Assosa, Ecopia was able to secure a large supply of high quality mangoes, and also provide additional income opportunities through a new market for the mango farmers.



The worksheets linked below allow practitioners to apply their understanding of commercial linkages to their own decision-making and contexts in order to feed into their strategies on how to most effectively facilitate market development for the benefit of extremely poor producers.

*Worksheets:*

- [Vertical Linkages Analysis Worksheet](#)
- [Vertical Linkages Facilitation Worksheet](#)

#### 4. What Types of Contracting Arrangements Are Most Suitable for Extremely Poor Producers?

Different types of contractual relationships require different abilities and commitments from extremely poor producers. Practitioners often support extremely poor producers in being able to enter a particular type of agreement, which may at first seem particularly attractive and successful, but may ultimately not be matched to the capacities of the extremely poor producers, resulting in failure.

The goal for practitioners is to move market systems from spot interactions to more dependent and predictable market relationships governed by contractual arrangements. These shifts can provide extremely poor producers with important advantages through increased incomes. Such shifts can also affect gender roles and relations (as discussed in more detail in the section on gender later in this Field Guide).



### Vertical Contractual Arrangements

Below are descriptions of forms of contractual arrangements that are or could become relevant to extremely poor producers.<sup>2</sup>

Name of Contract	Contract Description
<b>Spot market</b> <i>(immediate sale)</i>	Product is bought for cash and delivered immediately. Transactions are completely market-based. Contracts are verbal and often anonymous.
<b>Forward contracting</b>	A transaction where a commercial buyer and seller agree upon delivery of a specified quality and quantity of goods at a specified future date before the goods are produced. The price is agreed upon in advance.
<b>Regular sub-contracting of suppliers</b>	Buyer has a list of preferred suppliers (producers / farmers) with whom forward contracts are made regularly. This provides security and reduces search costs on both sides.
<b>Outgrower schemes</b>	A larger farm contracts with neighbouring producers to complement its own production volume. Outgrowers receive technological services but may sell to other buyers as well.
<b>Contract production/ Contract farming</b>	The producer / farmer works for one buyer exclusively for a particular crop/product. Product and technology are clearly specified. The producers / farmers receive the necessary inputs.

The chart that follows shows examples of typical contracting types relevant to extremely poor producers, some more so than others. Moving down the chart, several factors intensify or increase:

- ▶ Intensity of relationship (trust, collaboration)
- ▶ Form of communication (frequency and type of interaction)
- ▶ Level of ability (complexity of arrangement)
- ▶ Level of commitment

For example, contract farming requires more trust, collaboration, communication, and frequent interactions than do one-time sales.

<sup>2</sup> Adapted from GTZ. 2007. Value Links Manual: The Methodology of Value Chain Promotion. [http://www.value-links.org/manual/pdf/valuelinks\\_complete.pdf](http://www.value-links.org/manual/pdf/valuelinks_complete.pdf) p. 124



## Characteristics of Vertical Contractual Relationships

This matrix analyses different contractual arrangements relevant to extremely poor producers.<sup>3</sup>

<i>Select type of contract project is considering facilitating</i>	<i>Consider characteristics and decide if contract type is appropriate for producers that the project is targeting</i>			
<b>Contract Type</b>	<b>Intensity of Relationship (Trust, Collaboration)</b>	<b>Communication (Frequency, Type)</b>	<b>Level of Complexity (Ability Level Required)</b>	<b>Level of Commitment</b>
One time sales/spot market	Lowest	Lowest	Lowest	Lowest
Forward contracting	Low	Low	Low	Low
Regular sub-contracting of suppliers	Medium	Medium	Medium	Medium
Outgrower schemes	High	High	High	High
Contract production/ Contract farming	Highest	Highest	Highest	Highest

Worksheet:

- [Contract Applicability Assessment Worksheet](#)

Worksheets in this section:

- [Vertical Linkages Analysis Worksheet](#)
- [Vertical Linkages Facilitation Worksheet](#)
- [Contract Applicability Assessment Worksheet](#)

Click on a worksheet title above to download a Word file of the worksheet. (Note: your computer must be connected to the Internet.) If this does not work, go to the [Field Guide resource page](#) on the Microlinks web site, scroll down to the Field Guide Table of Contents, and click on the worksheet title.

<sup>3</sup> Adapted from GTZ. 2007. Value Links Manual: The Methodology of Value Chain Promotion. [http://www.value-links.org/manual/pdf/valuelinks\\_complete.pdf](http://www.value-links.org/manual/pdf/valuelinks_complete.pdf) p. 124