

**Market Development and Smallholder Farmers-  
A Selective Literature Survey**

**(Background Paper for the “Second Economy Project”)**

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## 1. Introduction

This paper is part of a larger study which investigates the opportunities and challenges in promoting smallholder farming as an element in the second economy development strategy. Within the context of this larger research initiative, this paper sets out to both feed into other elements of the whole project and to draw on relevant evidence produced in the related papers. It is hoped that this rounded or holistic research approach will positively enrich the evidence-based policy development and practice in the interest of resource-poor smallholder farmers.

The content and scope of this paper is limited to the linkages of market development and smallholder farming. This paper has been drafted with the upfront awareness and knowledge that modern smallholders are rarely if ever autarkic agents that we encounter in large volumes of the literature on this subject. On the contrary, smallholders engage with “the market” in multiple ways and capacities. How smallholders interact with the land market, which is of course a crucial farm input market for food security or marketable agro-food production, can be taken as an illustrative case in point. Even in contexts where smallholders have fairly ill defined and insecure land tenure rights, they occasionally act on the demand side of this market and at other times on the supply side. Many informal farmland rental and sales markets exist in large parts of *developing countries*. As active agents in these markets, resource-poor farmers sometimes demand land (say, renting-in) in prosperous seasons and often supply land in the rental or sales markets in the off-seasons to search for other types of employment. Incidents like this, where smallholders function as consumers and suppliers along the agro-food chain, get repeated across a spectrum of other input and output markets.

What this last point implies is that any meaningful exercise to map the multiple ways in which smallholders interact with markets can potentially span an enormous field of research. However, to give and maintain focus in this synthesis overview, keep it informative and fill a critical niche identified in the larger project, this paper will concentrate on farm (or agro-food) output markets. This means tracing the flow of marketable surpluses of smallholders beyond the farm gate into local, national and global markets, of course depending on the availability reliable evidence. More specifically, the scope of this paper is defined in terms of the following key questions:

- How do smallholder farmers interact with agro-food output markets?
- What are the opportunities and constraints of integrating smallholders into farm output markets?
- Flowing from the above findings, what are the lessons and implications for agricultural marketing policies?

Raising the general level of well-being of society is positively correlated with the rise and growth of markets. One implication of this hypothesis or ‘stylized fact’ for smallholder farmers is that in order for them to raise the efficiency of their productive activities, they need to integrate into a system of market relations. What drives this result is the competitive pricing mechanism which automatically regulates how markets work. In

other words, prices naturally and instantaneously adjust to efficiently allocate resources to the most productive activities and market actors (Barret and Matumbatsere 2005). A spin-off from incorporating resource-poor small producers into “the market” is a higher standard of living, usually reflected in reduced levels of poverty, inequality and unemployment. Pro-poor farmer development policies, as this narrative suggests, must therefore be grounded in this logic of the market. A concrete task for policymakers that flow from this perspective is to foster ‘market development’ or, more precisely, facilitate the most suitable conditions for markets to emerge, flourish and operate without any impediments.

The potential or real benefits of developing markets for smallholders are directly relevant to South Africa’s second economy project because its primary goal is to craft a mix of strategies to uplift targeted underdeveloped regions (The Presidency 2006, 2007)<sup>1</sup>. Households in remote rural villages in the former homelands, home to almost all the 3-4 million smallholder farmers, form a key target group in this development strategy. Poorer farmers who have gained land and other farming assistance through the land reform process since 1994 form a relatively smaller percentage of this category of rural small producers (Zimmerman 1999, Kirsten and van Zyl 2000). What both “established and emerging black smallholders” have in common though is that they farm mainly to add to household food security. Surplus production has remained rare in this rural context. Moreover, the accidental but limited excess farming output is usually sold in local markets (within the village or a nearby makeshift open/roadside market).

Reasons for the limited scale of production fall into two categories: First, historical barriers constructed through apartheid socio-economic engineering reinforced the spatial isolation of the country-side. Within that segregated development model the meager village-level purchasing power became a structural blockage to expanding income from the sale of agricultural output (Makhura, Goode and Coetzee 1998). (A limited number of white commercial farmers, heavily subsidised through a variety of direct and indirect forms of state assistance, evidently made a living from farming profits.) Second, the delivery of agricultural support to small farmers after 1994 has remained at woefully inadequate levels. (The barriers that resource-poor farmers had to confront to enter input and output markets proved difficult to overcome in practice, such as: participation in rural land and labour markets, access to credit and other financial institutions, storage facilities, accessible roads and reliable transport networks, information and know-how on contracts and prices, technology and communications networks, etc. Zimmerman (1999) gave a fairly elaborate yet rigorous early warning of how costly it might be to bridge these formidable impediments to would-be land reform beneficiaries.) Taken together, these two sets of obstacles do account for the persistence of the deep-seated or structural nature of deprivation and inequity that define contemporary development debates (Aliber, et al 2006). The second economy project is striving to better understand these challenges with the aim of uprooting them.

Breaking these structural constraints and fast-tracking agricultural assistance that would enable smallholders to access larger markets are important goals given the rural realities sketched above. In fact, there is a body of evidence which suggests that developing

markets for resource-poor smallholders could have large-scale spillover effects (bigger multipliers from stronger backwards and forward linkages) on their productive capacity, income and local employment (Wynne and Lyne 2004; Hendricks and Lyne 2003; Matungul, Lyne and Ortmann 2001; Vink 2004). What this implies in terms of real-life policy is that interventions need to ensure that as smaller producers integrate into agro-food markets, they also retain the benefits of greater market participation.

This paper briefly evaluates some of the advantages (or disadvantages) of integrating smallholder farmers into agro-food markets. Clearly, the value-added of such an evaluation to policy-relevant research must start with some working definition of ‘the market’ even before dwelling on how smallholders interact with actors along the agro-food value chain. This paper does not offer an exhaustive assessment of the intricate theoretical controversies on the role of markets in economic development.

## **2. Understanding “Market Development”**

A market, broadly defined, is any setting in which sellers exchange goods and services with buyers. Needless to say, actors within the market space interact on the basis of clearly defined rules of exchange (which generally entails an agreement on price, quality, quantity, delivery time, and so forth). This common or generic view of ‘the market’ paints the picture of a static structure that has existed since the beginning of time. Yet exchange, which is arguably the distinguishing characteristic of any market, is a social activity which marks the break-up and end of earlier societies centered on inward-looking and self-provisioning household units. But the widely accepted textbook view of the market creates the picture of an asocial and static structure. This perspective is generally silent on the origins of markets, how markets change over time and how smoothly markets function in reality. In contrast to this restricted notion of markets, to gain a comprehensive understanding of market development in the agro-food sector calls for a larger contextual and longer-range historical examination of markets.

Market development is a more flexible concept which stretches across a wider terrain of issues. One part of this concept covers how and why markets became established in specific socio-economic contexts in the past. The transformation of agriculture has arguably been one of the most important outcomes following the creation and expansion of markets in the economic history of countries or regions of the globe. As this market-based system solidified into the foundation of a society, farming also became incorporated into a fully-fledged exchange based activity. Studies that look at market development for smallholders from this historical angle, contribute to our knowledge of markets in at least two ways (Harriss-White 1999, Mazoyer and Roudart 2006). Firstly, these studies counter the idea of the ‘timeless existence of markets’ which is popular in mainstream economic analyses of markets<sup>2</sup>. Furthermore, this perspective of markets is also useful for a second reason, which is closely related to the first. It stresses that real-world markets are far from being agent-neutral institutions but, on the contrary, are arenas in which powerful economic agents can wield considerable control (Harriss-White 1999<sup>3</sup>).

### 3. Smallholders and the Globalization of Agro-food markets

The market-oriented focus which characterizes today's agricultural marketing policies can be traced back to the late 1970s and early 1980s. Globally, policy thinking from that period onwards started moving away from the state-directed approach to agricultural marketing which was common in most developing countries with a large agricultural base, including in Africa. Almost every newly independent and post-colonial state after the Second World War subscribed to a heavy interventionist role for government in the economy. In the agricultural sector, however, this model had disappointing outcomes for many smallholders, lost its credibility and paved the way for rethinking agricultural development policy. Some of the most devastating results of this older model included several years of negative growth rates in agricultural output and resource transfers from agriculture through taxation. Kherallah et al (2002) cite evidence to show that the growth in per capita value added for Sub-Saharan Africa was -0.7 for the period 1965-1980, compared to -0.2 for all low-income countries under this older model. Moreover, the marketing boards, operating under the weight of bloated bureaucracies invested little in the agricultural inputs and market infrastructure. The pricing philosophy which guided these marketing boards was to deliver low cost food to urban areas, with little attention to the negative consequences unsubsidized low prices on smallholder farmers<sup>4</sup>.

Price risk is one of the key risks associated with the development of markets. Markets increase the risks and uncertainties smallholders face as they integrate into markets. Studies generally report a rise in the frequency and magnitude of price shocks in market-oriented environments. The consequences of such shocks are very unevenly distributed across different farming households but tend to move in tandem with a farmer's wealth status (Jayne et al 2006, Barret and Dorosh 1996). Dealing with price risk is therefore a critical area for policy intervention. Barret and Dorosh (1996) have observed in a low-income agrarian economy, like Madagascar, that food price volatility is closely associated with the introduction of liberalized markets in agriculture. The price of the dominant food crop in Madagascar, rice, increased quite steeply after the initial wave of market-oriented reforms in the second part of the 1980s and thereafter moved higher albeit more gradually.

With the globalization of agro-food markets in eastern and southern Africa, according to Jayne et al (2006), the trend is for virtually all staple foods get priced in terms of its global price. In this import parity pricing regime, the domestic prices of staples on average are kept on par with the world market prices for a commodity. At the same time, in such a liberalized pricing regime, the instabilities of global prices get transmitted into domestic price fluctuations. This affects the distribution of the benefits of higher prices across smaller and larger farmers. A relatively smaller number of farmers with higher levels of productive assets have profited more than resource-poor farmers. Jayne et al (2006:335) therefore emphasize that "linking African farmers to markets must take account the inequality of productive assets, which contribute to highly concentrated patterns of the agricultural surplus generation within the smallholder sector". In Southern Africa, capital-intensive commercial farmers in South Africa, by far the dominant maize

exporters throughout the region, have reaped most of the benefits of liberalized agricultural markets.

What this illustrates is that participation in markets for staple foods is strongly correlated with the asset holdings, even among small farming households. Most African smallholders that grow staple grains have access to farming plots of 3ha or less. But within this sector, landholding patterns vary across regions in a country and between countries. For example, 80% of smallholders in Malawi possess less than 1 ha of land, whereas in Kenya and Zambia the average land holding falls somewhere between 2.5-3ha (Jayne et al 2006:333).

On the consumption side, two consequences of this development deserve to be mentioned, albeit merely in passing. Firstly, a big-bang opening of agro-food markets has raised the risks for and threatened the food insecure consumers for whom the cost of their staple food has drastically escalated. Secondly, it has stimulated the switch to cassava as a food crop in some countries because it is a more tolerant to drought. (Case studies drawing on data from Malawi, Zambia, Tanzania and Kenya reported significant rises in the cassava cultivation in the period 1994 to 2004 when the adoption of import parity pricing was dramatically expanding.) Another result has however been threatening food insecure consumers for whom the cost of their staple food is escalating.

Table x: Staple Food Markets among Smallholders (based on Jayne et al 2006:335)

| Rural group/category  | Market activity: buying and selling   |
|---|---|
| Smallholders selling staple grains  | Minority of smallholders (1-3% of rural population) with 4-20 ha and highly capitalized accounting for 50% or more of marketed maize/grain sales; sub-section of 10-20% of rural population selling small quantities of grain/maize |
| Smallholders buying staple grains   | At least 40-60% of rural population with small asset holdings and low income  |
| Smallholders selling and buying   | Seasonal distress buying and selling of grains; 10-20% of rural population selling and buying grains within the same year   |
| Households neither buying nor selling maize (for example Zambia and Mozambique) | Small proportion of rural population consuming maize; switched to cassava   |

Source: Jayne et al (2006: 334-335)

#### 4. SA Marketing Policy Space and Smallholders

In his foreword to a study on market deregulation in South African agriculture, commissioned by the Free Market Foundation, Prof Duncan Reekie, had the following to say:

“In short, South Africa is a successful pioneer in agricultural deregulation. The market rules in almost every sector; from maize, to wheat to fruit. (There are still some sectors where little has been achieved – most notably sugar). Market control, not state control, unambiguously best serves farmers, consumers, and the economy at large.” (cited in Vink and Kirsten, 2000)

This liberalization and deregulation of agricultural markets in South Africa followed global trends which had gained an unstoppable momentum in the 1980s. Moreover, these market-oriented reforms coincided with macro-level political economy reforms during the decade leading up to the end of apartheid in 1994 and this dramatically altered the environment for South Africa’s farming sector.

In this section we review how the country’s agro-food marketing policy context has evolved since the end of apartheid. The first part of this review concentrates on changes in the agricultural policy environment with the aim of throwing some light on opportunities and challenges to integrate smallholder farmers into markets. The next part reviews the limited and thinly scattered evidence on the marketing activities of small holder farmers. A specific obstacle faced in this synthesis of evidence has been the lack of a comprehensive database on the market activities of the smallholder farmers—especially black farmers in former homeland districts and several commercial farming districts<sup>5</sup>.

Before 1994 the political economy of apartheid essentially structured the linkages of resource-poor black farmers to agricultural markets. A decade before the end of apartheid, the old regime had embarked on reforming the agricultural sector, meaning phasing out state protection and control boards in agriculture. At that time, the chief instrument used to overhaul how agriculture would operate henceforth was the 1984 White Paper on Agriculture. This policy document, despite its far-reaching market-oriented reforms, was however still exclusively catering for a segregated and whites-only farming sector (consistent with the dominant thinking of that time, it was an ad hoc reform without getting rid of the fundamental pillars of apartheid). A separate set of policies applied to former independent homelands or TBVC states, hosting the majority of small-scale farmers. In these communal areas, the FSP programme crafted by the DBSA advocated a shift away from the centralized farming systems under the investment corporations which ostensibly promoted a large-scale farming model, according to Vink and Kirsten (2000).

In post-apartheid South Africa, the Marketing of Agricultural Products Act no 47 of 1996 (Marketing Act for short) outlines the parameters within in which smallholder farmers interact with agricultural markets. It provides the basic template for all policies that focus

on agro-food markets, such as the Strategic Plan for Agriculture of 2001, the Broad Based Black Economic Empowerment in Agriculture (Agri BBBEE), land reform programmes and the CASP. This Act is a pivotal instrument which regulates the workings of the post-apartheid agricultural sector.

The new agricultural marketing policy framework introduced by the Act is clear to see from its stated goals and other legislative stipulations. Firstly, the Act extends the scope of deregulating and liberalizing all spheres of agriculture (Section 2)- a move that had started from the mid-1980s onwards under the pressures of local and global forces. In a sense the Act was basically fast-tracking the reforms of agricultural markets inaugurated by the 1984 White Paper. Secondly, it repealed the separate legislative instruments which had governed agricultural marketing in the former homelands. Ignoring for the moment the actual pace of these reforms in real-life, what the Act accomplished was to bring black smallholder farmers under one national agricultural market policy regime, boldly articulated in the 2001 Strategic Plan for Agriculture (NDA 2001).

Furthermore, the Act established the National Agricultural Marketing Council (NAMC), outlining its roles and composition. As a statutory body, the NAMC advises the Minister of Agriculture and Land Affairs on a range of agricultural marketing issues, including the links between agricultural marketing policies and other 'national economic, social and development policies and international trends and developments' (Section 9 e (ii)). Section 4 of the Act stipulates criteria for NAMC membership. Members will include individuals with practical experience of "the production and marketing of agricultural products by small-scale and previously disadvantaged farmers." (Section 4 (2)(e))

The four main objectives of the Act are in briefly stated in Section 2(2):

- Increase the market access for all market participants
- Promote the efficiency of the marketing of agricultural products
- Optimize export earnings from agricultural products
- Enhance the viability of the agricultural sector

From the viewpoint of the Act, small-scale farmers seem to be equivalent to other actors along the agricultural marketing chain. Whilst this notion of equal treatment is commendable, the 'level playing field' decreed in policy does not immediately mirror what actually existed in the real world. There is no special mention of "smallholders" as such, but they seem to be lumped with other competitors in the market place, including well-established large commercial farmers. In one part, Section 16 which deals with agricultural exports, there is an occasional reference to small-scale farmers and the specific requirement that this category of farmers be included in agricultural export chains.

Two years after parliament had passed the 1996 Marketing Act (it came into effect in January 1997), the Ministry released a discussion document on agricultural policy<sup>6</sup>. In his foreword to this paper, the then Minister Derek Hanekom, sketched what had become, at least in policy circles, a popular vision of the 'a transformed farming sector':

“We also foresee a much larger role in future for small- and medium-scale commercial farming, based on family-managed farms producing largely for the market, investing in their land, using improved inputs and hiring labour...  
‘... For the poorer rural households, which derive only a small part of their income from farming, we expect to see increases in production of food for their own consumption, and occasionally entry into local markets to sell surplus produce...’ (MALA 1998).

This discussion paper confirmed the non-interference of government in agricultural markets through prices and subsidies due to potential distortions these can exert on economic performance. In contrast to the outmoded apartheid era farming-model the paper reinforced the need for a shift away from a farming sector heavily dependent on state support and controls. It called for fostering efficiency enhancing competition throughout the agricultural sector. But in the radically deregulated environment, resource poor farmers, especially smaller communal farmers and land reform beneficiaries will find it hard to compete against ‘established historically advantaged farmers’. Markets often fail, the document emphatically noted on several occasions, and this is a compelling rationale for selective state support to smallholder farmers in domains such as access to market information and extension services. In this context of market failure, in both potential and real terms, state support ought to be selectively targeted and indirect (with the emphasis on establishing a conducive regulatory environment). And where the need exists for public goods in order to ease the participation of smallholders in agricultural markets, service provision through public-private partnerships must be explored as an option.

This market-oriented approach to the sweeping agricultural reforms would be endorsed in the 2001 Strategic Plan for Agriculture, both as a guiding conceptual approach to policy and in terms of the rolling out of support services to small farmers. The adoption of a deregulated and liberalized framework for agricultural output, according to the Strategic Plan, tops the list of fundamental and most far-reaching policy shifts of the 1990s. Henceforth, the model would be for “market forces to direct business activity and resource allocation” (DoA 2001:4) in the sector. Smaller farmers, either those entering the sector through land reform or those in communal areas, will be assisted to gain greater access to markets. Greater market access will be facilitated, on the one hand, through the removal of ‘entry barriers’ - ranging from lower (subsidized) inputs costs as well as opening of ‘new (niche ?) local and exports markets’ to this categories of farmers (DOA 2001:10-12). On the other hand, strategic partnerships between smallholders and large-scale commercial farmers and commodity producers associations should be forged (DOA 2001:10).

Among the challenges that the liberalized agricultural markets posed for resource-poor new entrants into the farming sector, the Strategic Plan specifically highlighted anti-competitive practices along the agro-food value chain and price risks. On both the input and output within the farming sector, some actors control input supplies and have the power to inflate farming costs. As the Strategic Plan specifically highlighted:

“Increased market concentration among input suppliers and distributors as well as increased domination by multinational firms may negatively affect the competitiveness of the agricultural sector. The power of these firms and the lack of competition within the sector may result in high intermediate input prices.” (2001:13)

And on the output side, it notes the emerging dominance of supermarket chains have emerged as dominant players in agro-food value chains what this has in store for farmers:

“Retail chains have become large and extremely powerful in negotiating and determining producer prices locally and internationally. Farmers have as a result been at a disadvantaged in price negotiations”. (DOA 2001:14).

In summary, it is quite clear that from 1996 onwards, agricultural marketing policies basically set out to liberalize and deregulate the full agricultural value chain as articulated in the Marketing Act. This policy definitely recognizes black smallholder farmers as stakeholders in farming and acknowledges the need to improve their access to agro-food markets (especially export markets) as a path to wealth and higher welfare. Complementary policies that were adopted later, such as the Strategic Plan in 2001 and AgriBEE in 2006, more explicitly recognized the need for supportive measures and interventions to allow smallholders meaningful market access. But how has this altered agricultural marketing policy context affected the prospects of smallholder farmers in practice?

Vink (2004) has done a descriptive overview of how the production and marketing of major groups of farm commodities have changed under the deregulated and liberalized agricultural regime. Across all the major commodity groups- specifically, field crops, livestock and horticulture- state interference in farm output markets has almost completely disappeared. This has compelled large-scale commercial farmers to raise their productive efficiency in order to be more competitive. Although a few opportunities have opened for smallholders, there seem to have been no large-scale integration of smallholders into the liberalized agricultural markets up to 2003. Noteworthy developments following the implementation of this new framework are:

1. A *flexible pricing regime* has replaced pan-territorial and pan-seasonal price fixing by state agencies. This rewards for differential product qualities and relocation of the production of certain commodity types. However, this seems to have benefited well-networked farmers in the large-scale commercial sector. For they had access to information and complementary resources which enabled them to seize opportunities offered through the more competitive supplier prices.
2. *Localized and smaller-scale agricultural processing* has been encouraged. Approximately a third of the maize crop is evidently locally processed by a growing number of on and off-farm smaller millers.
3. *Heightened levels of buying and selling in local informal markets*, such as informal meat markets in townships that procure meat mainly from smallholder farmers. However, these are typically “open roadside markets” where it remains

unclear what quality meat ends up in informal markets and to what extent there is adherence to food safety and hygiene standards of meat on display.

Overall, however research and comprehensive data on better market access for black smallholders, let alone the extent to which their increasing integration into markets have raised their levels of well-being, remain poor or non-existent. Sections of the NAMC web site dedicated to disseminate this specific kind of research evidence, displayed only a small and fragmented list of what appears to be outdated reports.

## **5. Some Evidence on SA Agricultural Markets**

Resource-poor small farmers that produce a marketable surplus, especially staple food producers, tend to sell directly to consumers. However, farmers with a larger marketable surplus or with a direct “commercial orientation” (Makhura et al 1998) generally sell a larger share of their output through other intermediaries (retailers, wholesalers and processing establishments). To start this overview of evidence on market access of smallholders, this section starts with pulling together lessons from three typical forms of downstream linkages of smallholder farmers: to fresh produce markets, informal markets and supermarket chains. Institutional reforms bearing on the agricultural sector and the “supermarket revolution” (World Bank 2008) have introduced significant changes in the agro-food value chains. These have opened a new range of opportunities and challenges for smallholder farmers. Take the case of supermarket chains, for instance: they have intensified competition over local demand while at the same time opening a market outlet for smallholders producing high-value farm produce.

As a result of the growth of South African supermarkets and their movement into smaller rural towns, the farming market space became radically altered. Alongside this development, rural poor households (including many smallholder farmers) are increasingly net consumers rather than net producers of foods and they tend to purchase their food from the expanding network of supermarkets in nearby rural towns and cities. These expanding trends in the sources of local food purchases in communal villages have been observed in both Limpopo and Transkei in the post-1994 era (D’Haese and van Huylenbroeck 2005, Kirsten et al 2007). Supermarkets are making foods available at lower prices than informal vendors in local markets because of the economies of scale advantages this ‘networked retailer’ enjoys in procurement. Their competitors for the local demand, especially informal traders, have often been forced out of business because they are unable to withstand the “competitive pricing” of these large retailers. But arguably the most important function of these ‘supermarket networks’ in the context of agricultural markets remains the extent to which they impact on smallholder farmers or draw smaller producers into agro-food networks often under their control.

The Johannesburg Fresh Produce Market (JFPM) is the largest fresh produce market in Southern Africa and an important outlet for smallholders in Limpopo Province. The JFPM board has been active in expanding access to its trading facility to smallholders as well as informal traders. Examples of how the JFPM board has been trying to improve

market access to smallholders include the following: It is conducting targeted extension officer training programmes, especially for extension officers in the Vhembe district (Limpopo) Department of Agriculture, so that extension officers are better able to convey or transmit market information (such as prices, packaging, quality, storage and delivery times, market agents, etc) to farmers in localities more than 300 kilometers from the market. It regularly runs small farmer and informal trader open days in which these market actors are brought on tours to the JFPM facilities to raise their understanding of the workings of fresh produce markets and how it can benefit them. More recently, the JFPM and the Vhembe District Municipality teamed up to build a decentralized pack-house and grading point facility to integrate small and emerging farmers into fresh produce markets. This Vhembe fresh produce facility will significantly reduce the transport costs for smallholders and with modern cold storage facilities will enable smallholders to deliver better quality produce to the JFPM and capture more benefits from better market access.

Informal markets in which large numbers of small traders participate are common across the agro-food value chain. In their study of the Tshakhuma and Khumbe informal markets in the Vhembe district, Nesamvuni et al (2005) found that both markets trade mainly in sub-tropical fruits. Women comprise roughly two-thirds of the sellers, with another 30% mainly children, and 56% of women respondents reported income from trading as their only source of livelihood. Of greater relevance to this study is the extent to which these informal traders use smallholder farmers as their sources of supply. Smallholders supply a limited range of fruits with low input intensity and indigenous varieties (such as mango and avocado). However, most of the fruits sold in the market have been bought in relatively larger volumes from large-scale commercial farmers in the Levubu valley, transported and delivered to Tshakhuma and Khumbe by hawkers. To raise the supply of fruits from smallholders to these markets, Nesamvuni et al (2005) recommended downstream contract arrangements between smallholders and informal traders. But complementary investments in storage facilities and transport may be needed to improve the absorption capacity of these informal traders as well to reduce the rapid deterioration of produce on display that force traders to sell at huge discounts and often at a loss.

Downstream linkages of smallholder farmers with large-retail chains (or supermarkets) have received increasing attention in recent research (World Bank 2008) because supermarkets attract a mass consumer market. Supermarkets generally specialize in supplying a targeted group of customers with niche products of relatively high value. As such, it offers a potential market to smallholders that produce high-value agricultural foods, which are usually produced in smaller volumes. To explore ways in which smallholders can realize the advantages to be derived from access to this market, Louw et al (2007) suggest a more nuanced understanding of the purchasing strategies and other goals of supermarkets. Large supermarkets that serve mainly high-income groups need to be split from decentralized chains that procure their fresh agro-foods from local suppliers. The first type of supermarket chain operates a centralized procurement and distribution system which is designed to reduce transaction costs. Within such a system, separate and once-off transactions with scattered smallholders increase transaction costs and lower

efficiency (Louw et al 2007). To qualify as a supplier to large high-value supermarkets, smallholders need to comply with a host of standards, such as organic farming certificates, food quality and safety regulations and packaging criteria. As a consequence, smallholders may not be able to optimally exploit opportunities of these agro-food chains.

But localized supermarket chains, in contrast to the above type, often rely on small-scale farmers in close proximity to supply the fresh produce needs of their customers. Louw et al (2007) report case study evidence of the Thohoyandou SPAR, one of the largest supermarkets in Limpopo, as an example of a success story of the linkages smallholders managed to forge with a local supermarket in a specific municipal district. Smallholders supply up to 30% of SPAR's fresh vegetable sales, such as cabbages, spinach, carrots and beetroot. Prices and quality are verbally negotiated when farmers deliver the products to the store (following the inspection of a sample of the produce). Evidence from recent interviews with the SPAR manager revealed wide variations in the numbers of smallholders participating in this arrangement. In 2004, the number of smallholders participating in this arrangement had grown to approximately 23 but then declined to a more recent average of 15 farmers per year. Interest free loans and training programmes to ensure the supply of a better quality, provided by SPAR in the earlier period seems to have dropped from this arrangement.

Better and sustainable market access of smallholder to the opportunities opened by supermarkets turns on the strategies to reduce transaction costs. To lower the transaction costs for both the smallholders and supermarkets, Louw et al (2007:548) advocate strengthening forms of collective action among smallholders to promote equity and competitiveness. More specifically this should facilitate coordinated efforts to: train farmers in product quality and marketing, enable farmers to comply with delivery schedules, overcome transport problems, access cheaper inputs as a transitional stage to enter larger fresh produce markets.

Perret (2002), in a case study of the sheep market activities among farming households in a rural Transkei village (Xume) has found that a rural household typically relies on a mix of livelihoods activities. The norm is for the average household to rely on 2-3 sources of income. To contextualize his study, Perret (2002) cited evidence from the 1997 Rural Survey which found that only 3% of the farming households in Transkei and Ciskei regions had practiced farming with a "commercial orientation". However, in an effort to profile the typical households selling wool, meat or other farm outputs, this study developed a typology to profile 'marketing activities' among farming and non-farming households<sup>7</sup>. Within the non-farm group, in which off-farm workers form the majority (10-40% of households), sheep herding is as expected for own consumption. Yet even this group periodically sells 'small quantities of wool to speculators'.

Perret's (2002) own findings differ from the evidence in the 1997 Rural Survey. In his sample, 60% of household earned cash income from farming, yet only 9% of farmers earn their main cash income from farming. He found in Xume, that only 5% sell crops grown such as maize, bean, cabbage, pumpkin, potatoes and spinach. The focus is on

sheep farmers, selling both animals and meat (mutton). However, they have sell wool mainly to speculators.

(Calculations of the amount of income earned from farming naturally starts from adding up the monetary value of specific types of commodities sold. However, in addition to what and how much they sell, where sales take place (the geographic location of the market) and arrangements along the value chain also affect how much farmers earn from marketing their outputs.)

The overall picture emerging from the findings of a number of studies is that smallholders who are active in markets, run operations that are locally concentrated and within a limited range of commodities. Traditionally, outputs of smallholders have found their ways onto local informal markets and other regional municipal markets. But with the supermarket revolution, a growing number of smallholders supply niche products in variety of contract arrangements with supermarkets.

Makhura and Mokoena (2003) surveyed several case studies on market access for smallholder farmers and distilled the patterns of existing output sales among these farmers. This is a very useful way to gain some insights on the nature and extent of output market participation among smallholders and the typical characteristics of their transactions.

- Smallholder farmers that do sell agricultural produce, engage primarily in cash sales. In purposively surveyed farming households in the communal areas of Limpopo and KwaZulu-Natal, at least 50% of households had engaged in selling agricultural produce in 2001.
- Smallholder farming output supplements household subsistence directly or through barter transactions. It has been estimated that around 25% of the agricultural produce go into the consumption basket of the household. In some cases, almost 50% of the sampled households exchanged maize with local millers for maize meal.
- Households selling higher value farm outputs are more commercially oriented. Makhura and Mokoena (2003) report evidence that smallholders selling livestock and horticultural produce are more commercially oriented than those selling staple food crops like maize. Sales of lower-value crops tend to be subsidized by sales of the higher value crops.

Constraints that bar smallholders from greater market access to agro-food output markets are associated primarily with underdeveloped infrastructure, ranging from the non-existence of local market spaces to unreliable sources of market information. However, institutional arrangements along the value chain and policies rarely prioritize the needs of smallholders and thus effectively heighten the barriers to access markets. Among the major constraints underscored in Makhura and Mokoena (2003) and supported by anecdotal evidence from ongoing field studies are:

*Institutional responsibility:* State agencies with a mandate to promote greater market access for smallholders, specifically NAMC, NDA and PDAs, are poorly coordinated. Moreover, the CASP which has as one of its main pillars the goal of improving market access and infrastructure for small-scale farmers, highlights the role of local municipalities to invest in local market infrastructure which provides smallholders and traders with spaces to display and sell their outputs. Anecdotal evidence from Limpopo, where large numbers of smallholders farm on local irrigation schemes but depend heavily on the Fresh Produce Market in Johannesburg, a project to construct a municipal market for the Vhembe district has been on hold for several years partly due to poor cooperation and coordination among these public institutions.

*Bargaining power and discrimination:* In livestock auctions, for example, animals supplied by smallholders are often sold last and at lower prices. Smallholders rarely form part of marketing trusts. A related issue is the degree of participation of the smallholders in contract farming. Kirsten et al (2005), in a study for FANRPAN found South African smallholders to be poorly integrated in contract farming value chains. Among the reasons that account for this 'discriminating against' smallholders are: larger farmers are preferred because they are perceived to have greater management coordination; higher transaction costs are associated with smallholders. They found that increasing smallholder supply of fruit and vegetables by 10% through contract market arrangements has the potential to create opportunities for 11000 smallholders.

*Market information:* Access to information among smallholders is generally poor and is compounded by the lack of reliable and efficient means of disseminating information. Recent field evidence in a study among small-scale sheep farmers in Eastern Cape is a case in point to illustrate the need for public support for a reliable market information dissemination mechanism. Both woolgrowers and meat-sheep farmers get their information on market prices from a combination of three main sources: networking with white commercial farmers and 'speculative bulk buyers-farmers', an early-morning radio show in local languages and cellphones.

*Transport and road infrastructure:* Smallholders usually need to rely on public transport to bring their output to the market. Transport contractors are reluctant to service smallholders due to the poor quality of feeder roads in rural villages. Early findings from research among smallholder woolgrowers in the northwest corner of Eastern Cape show they need transport wool over large distances to access the market in Port Elizabeth. Their counterparts who concentrate on a meat-sheep variety seem to rely exclusively on white commercial farmers and 'speculative bulk buyers-farmers' to deliver their stock for sale to the big auction in Bloemfontein at a considerable cost deducted from the sale price.

*Assembly, storage and local processing:* Storage facilities are usually non-existent in rural areas and low volumes may not justify setting up such facilities in rural areas. Research from Limpopo indicate that smallholders (particularly those in horticulture in the rich Levubu valley) have through their own initiatives and associations accessed local pack houses to package and market their produce.

## 6. Conclusion

This paper has examined two interconnected issues. It has firstly explored the meaning of market development and what this means for the agricultural sector policies in modern times. A second and closely related question investigated was how to integrate smallholder farmers in agro-food output markets. Evidence examined in this paper suggests that greater market access for smallholders can be a route for them to raise farm productivity, incomes and escape poverty.

In summary, the global and South African evidence considered in this section show that smallholders do participate in a variety of farm output markets and actively seek to access larger markets beyond their immediate localities. But the degree to which smallholders participate in and share the benefits of greater access to agro-food markets depend on a combination of factors, such as the policy space, market infrastructure and how agro-food markets work in practice. Concentrating on the South African case, this review has observed that the country's agricultural marketing policy has evolved since 1996 to the point where policy makers now accept the need for direct interventions to improve access to agricultural output markets for smallholders. Marketing policies that cater for smallholders have an important role to play in reducing the costs to smallholders in selling their outputs through informal markets, supermarkets and regional fresh produce markets. In local informal markets, for instance, smallholders often find their prices undercut by produce that informal traders buy from large-scale commercial farmers. Even if a smallholder is able to supply a higher-grade product to local informal traders, individual smallholders find it difficult to match the volumes of larger farmers. Supermarket chains, on the other hand, provide a lucrative niche market for smallholders but these downstream linkages are limited to smallholders that meet product variety and quality standards.

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<sup>1</sup> The Second Economy Initiative forms part of the Accelerated and Shared Growth Initiative of South Africa, or ASGISA for short (The Presidency 2007, 2008). As an element of ASGISA, it follows the same analytical approach. This is of course logical because the overarching initiative and its subsections need to be consistent and coherent as a pre-condition for its success. This systematic framework or orientation consists of three logical steps and starts with fixing a range of economic growth and development targets. A next step, derived from the starting point, involves the identification of micro and macro constraints to reaching the stated targets. A final stage is to outline a series of interventions, both realistic and concretely measurable (quantifiable), to achieve its goals and bridge the constraints.

<sup>2</sup> Highly critical of market development in underdeveloped countries, Utsa Patnaik (1996:286) commented: "Market-friendly policies are seldom people-friendly...policies which are over market-friendly have destroyed Third World peasants' food security and created the conditions for famine in the past, and continue to have this effect in the contemporary world."

<sup>3</sup> Dorward, Kydd and Poulton (1998:40) use the New Institutional Economics perspective to describe the evolution of market-exchange in livestock in north-east Kenya from the 1920s to 1980. They highlight a range of factors which made the cattle market more competitive, particularly a court system which could enforce standardized weights coupled with better roads and telecommunications. Another interesting fact which had evidently aided market development over this long period was social capital as proxied on conversion to Islam also facilitated trade.

<sup>4</sup> Chris Barrett (1996, 1997) has extensively documented the case of agricultural market liberalization in Madagascar, which started in earnest in the latter half of the 1980s. Before then, the package of measures that characterized the state-centered marketing model for agricultural staples were:

- The state had monopsony power over the purchase of food staples and export
- Monopoly power in processing, distribution and storage

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- Active parallel markets were decreed illegal (Studies suggest that before the implementation of the reforms in the mid-1980s in Madagascar this markets comprised 50% of the domestic marketed volume for rice, the main staple crop). Interestingly, the liberalization and deregulation of food markets was part of the conditions attached to the 1986 loan from the World Bank. Research from other countries also indicate that macroeconomic adjustments, often externally induced, impact significantly on virtually all spheres of the agricultural sector. The 1994 devaluation of the CFA Franc transformed Burkina Faso's domestic informal beef markets (Hoffman and Bernhard, 2007). In the domestic markets, average cattle prices increased, local slaughter declined and squeezed the margins of domestic market traders.

<sup>5</sup> Perret (2001) gives some limited evidence on the 1997 Rural Survey. But this investigation was confined to the former homelands and this excluded farming activities among newer entrants who benefited from the land and agricultural reform policies.

<sup>6</sup> Aside from underscoring the key goals of the Marketing Act, this document articulated a commitment to improving "access to markets for small and medium scale farmers" (MALA 1998).

<sup>7</sup> The study defined more nuanced categories of farming groups than Jayne et al (2006) mentioned above, yet the findings of these two studies are remarkably similar.