

# Collective Action and Agroindustries



Two fundamental global economic tendencies have caused a shift in interest towards promoting rural agroenterprises and agroindustrialization to combat rural poverty. Increasing income levels and demographic changes, i.e. increased female labor force participation, has fueled demand for high-value and processed products. Structural adjustment and liberalization policies have reduced barriers to trade globally and allowed markets to reach even the most isolated rural areas.

#### SOURCE:

Johnson, N. and J. A. Berdegú. 2004. *Collective Action and Property Rights for Sustainable Development: Property Rights, Collective Action, and Agribusiness*. 2020 Focus Brief 11, International Food Policy Research Institute, Washington, D.C.

Together, these trends are fueling a process of agroindustrialization that is transforming agriculture in the developing world, most visibly in Asia and Latin America, with Africa beginning to show similar effects. Agroindustrialization brings major opportunities but also many challenges, especially to poor farmers and small agroenterprise entrepreneurs, most notable of which is equitable distribution of benefits.

The agroindustrialization process has three main characteristics.

1. Growth in off-farm agriculture-related activities, such as the supply of farm inputs or the processing, distribution, and sale of farm products. The suppliers, farmers, and distributors form supply or product chains.
2. Increased level of integration among actors in the supply chain, ranging from loose coordination to contracting, and even outright ownership.
3. Changes in products, technologies, and market structures accompany these shifts in number and integration of actors.

## **Implications of Market Orientation and the Importance of Collective Action**

Market orientation means adjusting production processes and products to respond to *specific* consumer demands and market signals and trends. Although many small farmers in developing countries will continue to grow subsistence crops, increased production for the market is the trend in many countries. What small farmers grow and how they grow them are increasingly determined by what urban consumers want.

Agroindustrialization processes are often accompanied and stimulated by liberalization of economic policy. This means that agroindustries — and the producers supplying them — must be competitive internationally to survive. To be competitive, agroindustries typically work only with farmers who produce the best quality products at the lowest possible cost. Often, the competitiveness of the agroindustry is strengthened through strict grades and standards, imposed on their farmer-suppliers through contracts. In negotiating and enforcing those contracts, power relationships between agroindustries and farmers — especially small and poor farmers — tend to be highly asymmetric, favoring industry.

Agroindustrialization processes are often accompanied by privatization of land and other natural resources. The rationale is to facilitate the development of markets that permit transfers of assets toward the highest productivity uses. Typically, this situation has meant a net transfer of productive assets from small farmers and poor rural communities to commercial growers and large-scale corporations, both domestic and multinational.

Where customary rights and communal ownership are important, the shift to private property may disadvantage those whose access rights are not recognized under the new regime. To the extent that these people are more marginalized in a society, there is the risk of widening existing inequalities. Similar patterns can be observed with shifts away from traditional labor exchanges toward wage labor.

Where the costs of accessing markets are high due to poor infrastructure, inadequate technology, or information barriers, collective action can help small producers be more competitive. A study of Associative Peasant Businesses in Chile found that cooperation benefited producers in markets where transaction costs were high and where product differentiation was important. In traditional markets for undifferentiated crops, no benefits to association were found. Associations were also found to be good vehicles for introducing new managerial and farming practices that enhanced farm profitability. Only about a fifth of these small farmer associations achieved their objective of helping their members participate in new markets, despite extensive government support.

The reasons for their many failures included, among others, their inability to:

- develop and enforce adequate systems of rules to direct relations among the members and between each of them and the organization;
- establish effective networks with public and market agents; and
- become competitive in the market in which they operate.

Cooperation can enable farmers to be more competitive.

## Implications of Integration for Small Farms and Firms

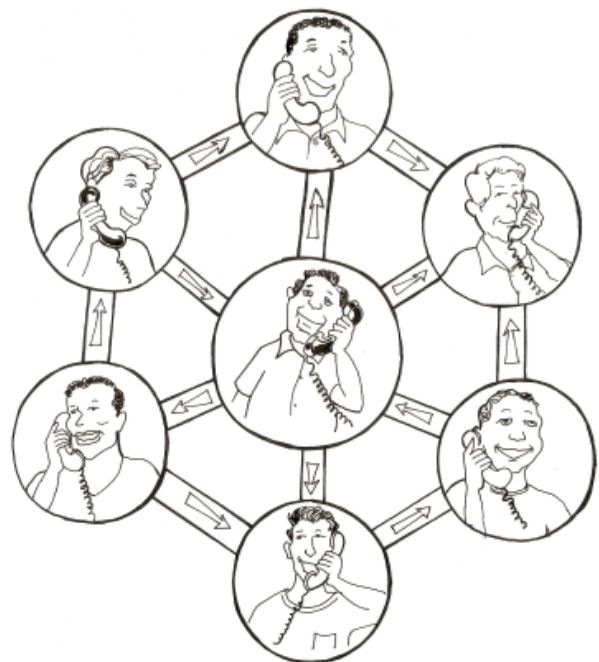
More striking than the changes in agricultural products and practices is the integration that has occurred in agroindustry over the past decade. The rise of mega-processors and retailers has resulted in very little produce being traded on the open market. A striking example is the rise of supermarkets in Latin America, which in a decade moved from 10–20 percent to 50–60 percent of the retail food sector. Collective action can sometimes allow producers to re-balance market power relationships and gain bargaining power in negotiations with big buyers.

A driving force behind this integration is the need to coordinate the timing and quality of purchases, and deliveries along the supply chain. Perishability was behind early integration, but other factors relating to economies of scale in the management of information about consumers and their preferences, for example, reinforced the trend.

In agricultural production, the increasing use of contracts by processors reflects this integration. Contracting can be positive for many farmers, but the small farmers are often bypassed because the transaction costs associated with managing the contract outweigh any productivity advantage the small farmer might offer. Since contracting is characterized by economies of scale, collective action among farmers, such as producers' associations, can make them competitive in an integrated supply chain. Collective action among farmers is, however, difficult to organize, coordinate, and manage.

A similar situation faces small agroenterprises. Even where farms and firms do not operate under contract, cooperating can help them negotiate better prices for inputs and outputs, manage crises, or improve local infrastructure.

Well-organized farmers have competitive advantages, but collective action at the local level is not likely to be enough to allow small rural enterprises to exploit new market opportunities fully. Whether they are acting individually or collectively, farms and firms need to stay informed about technological and managerial innovations, as well as emerging market opportunities in broader networks. A growing array of service providers — formal and informal, public and private — now exists to offer technical assistance, from quality control to marketing to financial planning. Firms



that identify and take advantage of these services are more competitive. A study in Colombia found that a 10 percent increase in the number of relationships that an agroenterprise maintained with other actors was associated with increases in income per worker of up to 18 percent. This means that for farms and firms that participate in technically demanding, information-intensive supply chains, managing their relationships can be as important as managing their production processes.



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External contacts are important, but internal relationships are also key to business performance and survival. Increased attention to promoting small enterprises is often accompanied by a push to form and legalize businesses. Decisions about how businesses should organize themselves are often made on the basis of legal costs and potential access to government subsidies for certain types of businesses.

Different organizational structures, however, have fundamental differences that firms need to consider.

- **Cooperative forms of organization** are based on economic and social objectives and require high levels of commitment and collective action to function. In practice, these levels of commitment are often hard to maintain, even if the groups are subsidized.
- **Partnerships** have lower legal and administrative costs, but they assume high levels of trust among the partners, a condition reflected in the shared, unlimited liability for the firm's obligations.
- **Corporations** have the highest administrative costs, but they may be the best structure for firms where investors do not share high levels of trust and are likely to change frequently.

Evidence from Colombia shows that no one organizational structure is best for either economic performance or social impact. The appropriate structure depends on the individual characteristics and objectives of the members.

## Conclusion

Agroindustrialization is transforming agriculture and rural communities in developing countries. As a result, farmers and entrepreneurs need to change the way they do business. Part of the solution is precisely that: to think about and organize themselves as a business and to be more attentive to market signals and opportunities. Because they are in markets that are not perfect, investment in collective action and networking can bring high returns.

The reality of agroindustrialization also means that the public and private sector research and development organizations that support agriculture and rural development must re-evaluate how best to support agroenterprise development through policy, technology, and institutional innovations. High-value products and opportunities for adding value should complement the focus on

productivity improvement in undifferentiated commodities. Capacity building in business skills, accompanied by more and higher quality business development services, can improve the competitiveness of small rural businesses.

A better understanding of how to develop and support networks, and innovative forms of organization beyond traditional agricultural cooperatives is also needed. On a more fundamental level, organizational and institutional innovations often arise in response to high transaction costs associated with market failures. Ameliorating these market failures, especially in the area of information and communication, will contribute to a more efficient and equitable agribusiness sector.

### **Suggested Readings**

Berdegúe, J.A. and G. Escobar. 2001. *Agricultural Knowledge and Information Systems and Poverty Reduction*. AKIS Discussion Paper. Washington, D.C.:World Bank.

Johnson, N., R. Suarez and M. Lundy. 2002. *The Importance of Social Capital in Colombian Rural Agroenterprises*. CAPRI Working Paper No. 26. Washington, D.C.: International Food Policy Research Institute.

Reardon, T. and J.A. Berdegúe. 2002. *The Rapid Rise of Supermarkets in Latin America: Challenges and Opportunities for Development*. *Development Policy Review*, 20(4): 371–388.