Chain Development in the Context of Market Liberalization: 
Upgrading of Pro-poor Agrichains under Conditions of Increased Competition
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Introduction
Market liberalization changes the way in which developing countries’ agricultural producers and processors integrate into global value chains. Two questions arise in this context: first, what are the actual patterns of integration, and second, if it benefits the poor. Traditionally, producers in developing countries have been integrated in global value chains as suppliers of primary agricultural products. Resource-poor producers reaped limited profits from the integration because they face entry barriers in meeting the requirements of global buyers in terms of quality standards or the necessary quantities. Those who do not participate in chain coordination, contracting and innovative technology are not profiting from the opportunities that arise from more open markets. It is by understanding the dynamics of value chain development that one can identify opportunities for developing countries in the context of market liberalization. This article discusses when marginalized agricultural producers and processors in developing countries are able to profit from market liberalization. It presents some considerations regarding strategies that can help to integrate marginalized economic agents of developing countries in global agricultural and food value chains.

Global Value Chains and Market Liberalization
Value chain coordination can lead to the integration of parts of the production process that are usually fragmented. Hughes (1994) defines value chains as institutional and organizational arrangements that allow buyers and sellers who are separated by time and space to progressively add and accumulate value as the products pass from one member of the chain to the next. Most advanced coordination is exercised in those chains where international suppliers or buyers manage and influence production, processing and marketing of products worldwide. Global value chains can be understood as networks of functionally interrelated producers and buyers that are involved on a global scale in processes of value creation as products pass across borders and between different actors in the chain (Gereffi, 2001.) In the current phase of globalization where individual and systemic competitiveness becomes increasingly important, chain coordination allows agents to reduce costs and risks in production, transport and storage and permits timely production in response to the demands of buyers and consumers. Efficient producer/supplier and buyer relationships with low transaction costs and increased liability can be established.

The formation of global value chains is influenced by the dynamics of market liberalization. Market liberalization changes the costs and availability of inputs and redefines the potential for marketing of products; while bringing more options for exporting products, it also boosts competition in local and international markets. The World Bank argues that market liberalization

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stimulates exchange with new business partners, which then increases the availability of knowledge and technology changes. It concludes that integration of local producers into the world economy can be a powerful instrument for developing countries to promote economic growth, development, and poverty reduction (World Bank, 2001.) Market liberalization attributes new roles and duties not only to primary producers, but also to other actors such as processors, transporters, marketers, input suppliers, consumers, the financial community, and policy makers, as well as interest groups and associations.

The causal relationships between market liberalization and chain coordination are reciprocal. On one hand, market liberalization has spurred the emergence of value chains by granting globally operating buyers and suppliers better access to markets. On the other hand, market liberalization results in part from the activities of interest groups representing globally operating chain actors who lobby for a better access to input and consumer markets (Gereffi, 2004.) Other factors as well as market liberalization explain the emergence of agricultural value and commodity chains: changing consumer demands, new food safety regulations and quality protocols, advances in production, processing, information and transportation technologies and increasing competition among buyers and suppliers of agricultural products. Market liberalization, in fact, can be seen as a prerequisite for chain coordination across boarders.

The importance of market liberalization as a tool for integrating producers from developing countries in global markets is reduced when markets remain distorted by barriers in both exporting or importing countries. Protection of agricultural producers is widespread in all developed countries. Additionally, developing countries also continue to protect some of their local producers to assure food self-sufficiency. The effect is that producer revenues depend partially on policy-created competitive advantages. With the exception of some niche markets, efforts to increase developing countries’ access to agricultural markets in developed countries have not yet been successful.

**Inclusion of Developing Countries in Global Food and Agrichains**

Commodity chains that involve developing country agriculture are often characterized by extensive buyer power resulting from the atomistic structure of primary production, that is, the participation of many small- to medium-size farmers. Coordination mechanisms in the chain influence how the value generated in the chain is distributed among its different actors. Based on the different characteristics of products, five categories of coordination may be distinguished:

1. **Traditional primary commodity chains:** The chains are governed by a handful of internationally operating traders, trade is centralized but traders exercise little control on production and quality. Quality is enforced through price and not through exclusion. Chain coordination tends to be loose and indirect. The main source of profitability is volume rather than margins. The economic development potential of such chains, in which developing countries are usually producers of the primary products, is limited because of inelastic demand but technical change can alter the chain dynamics, as exemplified by grain and beef production in South America. Typical examples for such chains include coffee, cocoa and cotton. Commodities such as rice, wheat, soy, and tea have similar features, but tend to include producers of larger size.

2. **Traditional plantation product chains:** The banana, pineapple, melon, palm oil, sugar, rubber and, to a certain extent, tea sectors are characterized by a high level of integration all through the chain up to the retailers. Primary production is carried out on relatively large estates in developing countries, which are in many cases owned by the international traders and processors. Alternatively, traders outsource production through contract farming. Technological innovations in production and processing are introduced by the internationally
operating traders. Quality is assured by traders in compliance with the latest retailer requirements. Developing countries profit from employment in primary production, but very little from the value added that is generated. These chains also have a limited development potential due to inelastic demands and the possibility that multinational traders have to move production to countries that offer the best economic opportunities.

3. **Processing and retailing chains:** In some sectors, such as canned food, milk and dairy or furniture, developing countries have moved from primary production to often labor intensive processing, profiting from cheap local primary production and local labor. Such chains are sometimes dominated by local large-scale agro-industries and cooperatives, and in other cases, by transnational companies. The latter aim at extending their presence in emerging developing country processed food markets. Similar motivations have led to the increasing presence of international food retailers and supermarkets in developing countries. This development has brought diversification of food products to developing countries. However, there are limits for small-scale production, because the processors and retailers demand certain qualities that many marginalized farmers cannot match. In some cases, the companies assist local producers to adopt new technologies.

4. **Fresh product chains:** In such chains retailers in high value markets in developed countries or increasingly supermarkets in developing countries set quality standards. This mainly applies to off-season products and exotic fruits and vegetables, fresh fish and crustaceans and special beef products. Suppliers profit from the sometimes large margins. Production is usually organized under contracts. Not many producers in developing countries are able to comply with the quality standards required. Participation in the chains requires rigorous application of latest technologies in production, storage and transportation. Some few countries such as Chile, Costa Rica and Kenya have been able to profit from such chains on a large scale.

5. **Alternative product chains:** Such chains relate to niche or high-value products, such as those that comply with ecological standards or fair trade regimes. The chains are governed by buyers in the North or by local buyers such as supermarkets and exporters. These buyers demand a certain quality and at times traceability to the origin of production. Local producers are often integrated in the chain through contracts that require specific practices in production and processing. It is by complying with the criteria established in the contracts that producers can sell their products. Each buyer may demand different qualities. Here, margins represent the main source of profitability for buyers. Where those chains deal with products produced by small-scale farmers, a mayor obstacle is organization and a homogenous high quality.

Distinctions between the categories of global value chains above illustrate that in the cases where greater profits from value added can be generated, it is the more advanced and better-endowed farmers and processors who obtain contracts with globally operating buyers or retailers. In this context, Kamplinski and Morris (1999) argue that chain coordination can increase the barriers of entry and result in a dualism: on one hand, a modern, commercial farming sector comprised of those with adequate scale and capital, and on the other a traditional, inefficient peasant sector to which the poor are effectively restricted.

**Upgrading of Local Agrichains and Other Strategies to Foster Integration of the Poor in Global Value Chains**

The structure of global commodity chains in a given market liberalization context determines to a great extent the opportunities opened for developing countries, especially for their peasant agriculture. For most small producers, market liberalization and chain coordination are phenomena that arrive as a given market condition. The question now is how they prepare themselves in order to access global value chains and how governments can help them in this
process. Gereffi (2001) argues that small producers participate in global commodity chains when they are able to profit from economies of scale, when they are involved in vertical integration, when governments support them through various programs. Gereffi together with authors like Gibbons (2000) considers technological “upgrading” an important strategy for integrating developing countries in global value chains. Upgrading can be understood as building technological and managerial capacity that allows actors in the chain to participate effectively in businesses. Upgrading means acquiring knowledge and technologies, but at a faster pace than competing chains and nations. Strategies for upgrading and integrating local producers in agrichains may include the following:

- Cope with entry barriers: Technical change or changes in products, marketing routines or access to more open markets can reduce entry barriers. Policy interventions and chain development agencies may also help farmers to access protected markets.
- Related to the above: capture higher margins of exports of existing forms of unprocessed raw material: This can be achieved by moving up the quality ladder, producing new forms of unprocessed raw materials, lowering production costs through innovation, increasing volumes and reliability of supply, and securing more remunerative contracts through future sales and hedging.
- Focus on intra-country and intra-chain distribution: Autonomous upgrading and inclusion may only be possible for a certain innovative or well-endowed farmers, in which case policies must be formulated for those who drop out or remain marginalized.
- Vertically integrating into intermediate and possibly final processing: relevant particularly for products that are consumed locally, but also for exports. Developing countries need to acquire knowledge and technology in order to innovate in the processing part of the agrichain.
- Upgrading of technological capabilities: acquire the necessary skills and technology to produce alternative and fresh products, and become involved in processing. Along with national research and technology transfer, sources of technological upgrading also include participating in networks led by developed country firms (Gereffi, 2001.)
- Upgrading of organizational capabilities and chain coordination: hinges on controlling the means of coordination rather than the means of production. Contracting is one means that reduces risks of buying and selling transactions in volatile markets. Informal networks and partnerships are important to exchange knowledge and technologies and develop skills.

In conclusion, this paper suggests that market liberalization opens opportunities for developing country producers and processors, but it is up to the producers to develop the necessary skills to profit from these opportunities. Given the reduced human, social and financial resources that small farmers command and the coordination problems they face, their access to high-value opportunities depends on external support, provided either by public agencies, private firms or NGOs. Many agricultural sectors in developing countries, particularly those dealing with low value and subsistence crops, still have a long way to go to achieve efficient contractual relationships between chain actors and develop systemic competitiveness. Programs must be established to foster the inclusion of marginalized, producers, both in the field of knowledge and technology or through better contractual relationships between chain actors so that risks are lowered and quality is improved.
Literature


