

# Upgrading opportunities for small-scale farmers in selected coffee value chains in Nicaragua

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## 1 Introduction

In the last decades, coffee markets have changed towards buyer-driven value chains. Product differentiation and high-value products play an increasing role due to changing consumer preferences towards healthy, organic, ethical or gourmet quality products.

Although substantial symbolic rents can be obtained by marketing differentiated coffees, farmers' gains of selling certified and high-quality coffees are small. More research is still needed to identify the income distribution along the value chain and to analyse the requirements for an efficient participation in these markets at production level.

Nicaragua has a good potential to participate in high-value coffee markets because of its favourable geographic and climatic conditions. This research aims at identifying the income shares of small-scale farmers in the value chain of Nicaraguan coffee and investigates the inherent governance structure, especially regarding transparency.

## 2 Methodology

The research took place in two regions in northern Nicaragua. Semi-structured interviews with small-scale farmers, key-person interviews and value chain workshops have been conducted with members of conventional cooperatives and of organic-fairtrade certified cooperatives.

Furthermore, coffee importers and roasters in Germany and the US have been interviewed using a semi-structured questionnaire.



Photo 1: Training on coffee quality with small-scale farmers in Nicaragua.

## 3 Results and discussion

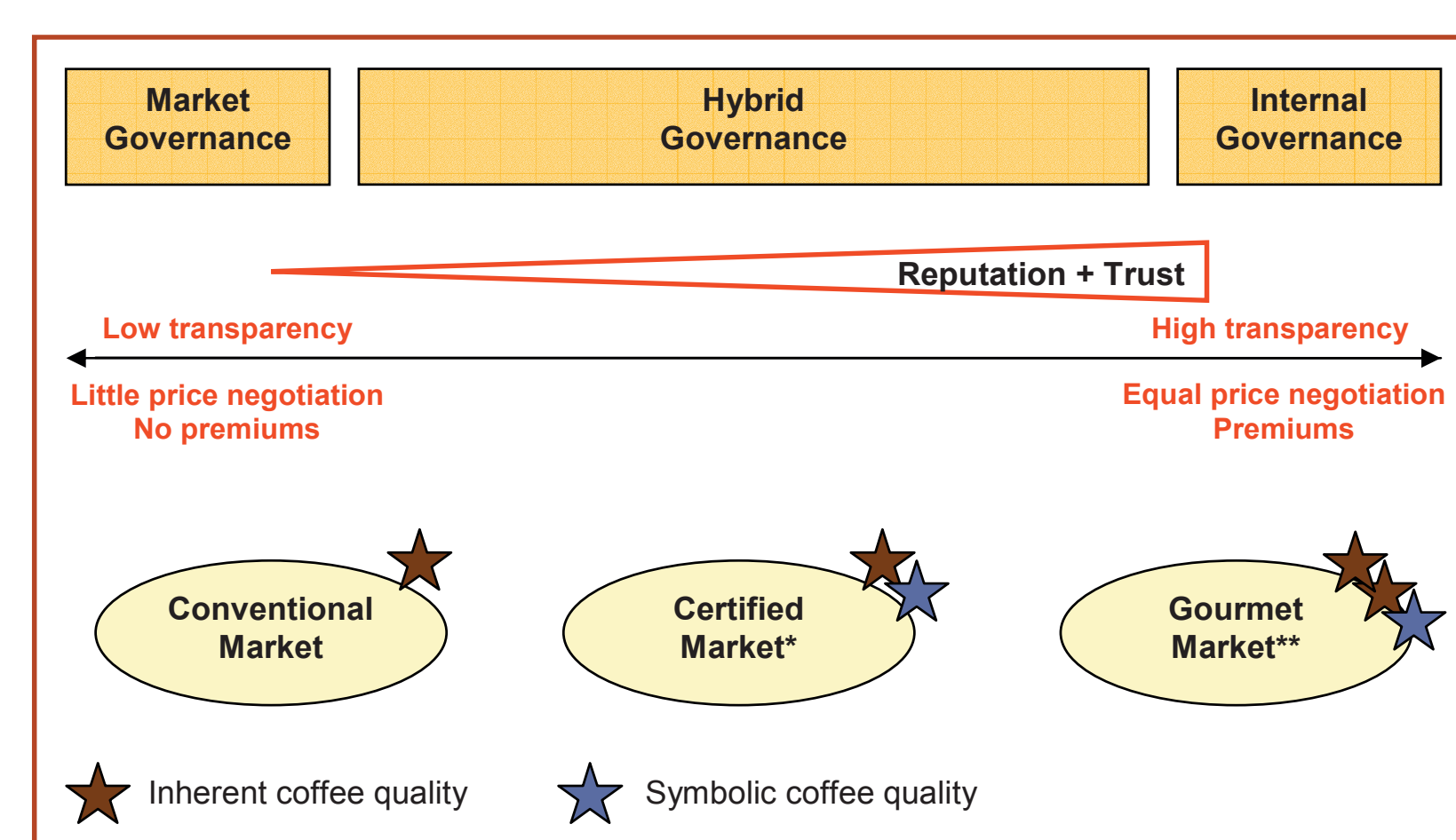
### Governance

Product standards, quality requirements and contract design are imposed by lead firms which are, in the case of this study, the buyers (importers/roasters) in consuming countries.

The lead firms manage information, resulting in very low transparency on prices and restricted knowledge about quality at farmer's level. Transparency, especially regarding standards, improves in certified chains but still, cost structures and prices are hardly communicated.

Quality requirements increase in certified and gourmet chains and while price premiums are paid for higher quality, farmers and cooperatives are often not aware where their coffee is finally sold and at which price. It resulted that farmers' income shares of the final retail price are currently lower in certified chains than in conventional ones, which may be explained by the relative high conventional coffee prices, economies of scale and marketing structures of the value chain actors.

Figure 1: Governance structures in different coffee value chains.



Source: based on key-person interviews and Ponte (2005).

Farmers thus lack bargaining power over prices and have limited access to information about quality issues and standards. Furthermore, they depend highly on other chain actors due to lacking knowledge and capacities. This is aggravated by a high degree of financial insecurity and dependency on annual credits for production.

To improve the participation of farmers and cooperatives in high-value coffee chains requires the creation of trust and reputation towards other chain actors, since governance structures in certified and gourmet markets tend towards deeper integration and are based on long term relationships (figure 1).

Additionally, increased information management and product definition regarding distinct quality attributes is important to enhance bargaining power at production level and to realize incentive schemes for quality production (Kaplinsky and Morris, 2000; Ponte, 2005).

Limitations for increasing the bargaining power at production level are currently the low educational level of farmers and cooperative staff in Nicaragua. Training is required and needs to be provided by either internal chain actors, (non-) governmental agencies or marketing institutions.

### Upgrading

The cooperatives engage in upgrading in order to strengthen their bargaining position and improve farmers' incomes. In Literature different upgrading categories are described (Laven, 2006).

Product upgrading activities are investments to improve inherent coffee quality and entering niche markets, e.g. for certified coffees. Depending on the standard, certification and the required quality, premiums are paid on top of the market price. The double certification, organic and fairtrade, is the best option for small-scale farmers regarding the high premiums paid in addition to the market price. Nevertheless, due to high production costs those premiums are usually not high enough to provide incentives to farmers for improving their quality. While individual premiums for higher quality are discussed within the cooperatives and are favoured by farmers, they are not compliant with the cooperatives' principles of solidarity.

Investments are made as well in process upgrading, e.g. in improved production management through extension, investments in wet processing at farm level and in cupping laboratories at the dry mill.

Furthermore, institutional upgrading is applied in the cooperatives, since they provide technical and financial assistance to their members.

Especially for Nicaraguan small-scale producers and their cooperatives there are high entry barriers for certified and gourmet markets. They face substantial transaction costs to adapt the production system towards the required standards, to improve information flows and quality. Still not all producers have access to their quality results, which would be needed if the farmer's bargaining position for better prices should be enhanced.

## 4 Conclusion

Analysis showed that communication among different chain levels is limited by organizational factors that result in asymmetric information. Farmers and their cooperatives provide information on product attributes to forward chain actors, but rarely receive information on market issues, prices paid at other chain levels or final product characteristics.

This lack of information limits the ability of small-scale farmers to successfully participate in upgrading activities and decreases their incentive to engage in certification and quality promotion programs.

Although cooperatives invest in upgrading related to inherent coffee quality, production and processing, further institutional upgrading to improve transparency is required. Enhanced knowledge transfer among chain actors could increase farmers' understandings of high quality coffee markets. The efforts of farmers to produce high quality products should then be rewarded by an adequate price which, until now, is often not the case.

### References

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Photo 2: Cupping of coffee in a cooperative's dry mill in Nicaragua.