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## Farmer's Perception of Transaction Costs in Vertical Integration Schemes: The Case of Poultry Producers in Rio Verde (Goias, Brazil)

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### Abstract

Since 1997 poultry production has been considered an option to add value to grains, produced in the municipality of Rio Verde (Goias, Brazil). Crop based protein (soybeans) and energy (corn) are converted into animal protein (poultry and pigs). The setup of big processing plants in the region created new economic development chances through enabling new income opportunities for small and middle sized farms by access to new markets. The region became nationally prominent in food processing. Processing plants moved closer to the sources of raw materials (grains) in order to (a) reduce transportation costs; (b) take advantage of (i) favourable environmental conditions; (ii) proximity of grain producing areas; and (iii) remarkable tax incentives. This study aimed at analysing the contractual relationship between processing industry and farmers, using a transaction cost economics (TCE) approach to describe relevant aspects of the producer's perceptions on the dependence on the contracting processors. In this case, contractual relations are coordinated by the processors and not the producers. Since they are in a dominant position, due to their large market-share, they often try to impose their rules and possibilities of negotiations onto potential raw material providers (farmers). We considered the two classical analytic categories: (a) behavioural assumptions (bounded rationality and opportunism) and (b) attributes of transactions (asset specificity, frequency and uncertainty). Our findings are based on a survey with 40 farmers providing poultry to a contracting processor. Key findings are that changes in the structure of management of the transaction between poultry producers and processors are efficient responses to the growth of specificity due to dedicated assets. From the farmer's perspective, there is a certain lack of information about the content of the contracts. This may enable some kind of opportunistic behaviour of contracting processor. However, vertical integration significantly reduces producer's risk. We conclude that farmers' dependence on processors is high on specialised small-scale farms and low for more diversified and larger farms.

**Keywords:** Chicken production, transaction cost economics, vertical integration