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Contract Farming or Contract Trading? – The Role of Intermediaries in Linking Farmers to the Market

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Abstract

Food security in developing countries depends on more than farming: it is just as important to understand how food becomes available for processing and marketing. One model for linking food production to processing and marketing is contract farming, benefiting both farmers and processing companies by e.g. lowering price volatilities and securing demand and supply. Research concerning contract farming focuses on both determinants and implications of farmer participation, and results are often mixed. To better understand the outcomes of contractual arrangements, our study focused on the specific governance structure between farmers and a Ugandan processing company. The company recently shifted from importing palm oil to focusing on locally sourcing edible oils from the production of hybrid sunflower seeds (provided by the processor) by small-scale farmers. The company uses three types of intermediaries: company agents, traders, and cooperatives. Our study thus addresses multiple gaps in the literature on market linkages: many studies focus on high-value export crops, while we examine a national food crop relevant to ensuring local food security; not many studies are located in Africa; and intermediaries are often studied individually, while in reality they often co-exist.

We studied four aspects of marketing relationships: technology transfer (i.e. hybrid sunflower seeds), provision of credit, purchasing agreements (including a price premium), and the inclusion of smallholders. We did a double-layered survey, including farmers and intermediaries from all three channels, and complemented survey data with qualitative data to gain further insights in the governance of relationships. With our focus on several intermediaries, we conclude that, in this case, the contract is not so much between the farmers and the processor, as hybrid seeds were widely available in the market. Instead, the contract is between the company and intermediaries through pre-financing the purchase of farmers' output, dependent on volume. The latter leads to the inclusion of larger farmers by the company agents and traders, whereas smaller farmers are more inclined to sell via the cooperative. Our results aid in the understanding of market linkages and can lead to better design of interventions, thereby improving farmer's livelihoods as well as regional food security.

Keywords: Contract farming, cooperatives, market linkages, traders, Uganda

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