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How transaction costs affect gross margins in informal vegetable value chains in northern Tanzania

Youri Dijkxhoorn[1], Behrang Manouchehrabadi[2], Henry Mvungi[3], Zablon Ernest[3], Bart de Steenhuijsen Piters[1]

[1] *Wageningen University & Research, Wageningen Social & Economic Research, The Netherlands*
[2] *Erasmus University Rotterdam, Erasmus School of Economics, The Netherlands*
[3] *World Vegetable Centre, Tanzania*

Abstract

Transaction costs, including negotiation efforts, risk management, and payment collection, are widely acknowledged in theory but rarely quantified empirically, particularly in informal markets. This study investigates how transaction costs influence profitability in the tomato and African eggplant value chains in Northern Tanzania. Drawing on Transaction Cost Economics, we collected primary survey data from 305 value chain actors operating in informal markets, monetized transaction costs, and evaluated their impact on the gross margin for the different value chain actors. Results show that wholesale traders and brokers invest more time in negotiating a deal and face higher risks (proxied by the likelihood of failed transactions). In both value chains, conventional gross margins were substantially higher for farmers than for midstream actors, with considerable variation across actor types. However, these raw figures do not yet reflect the costs each actor bears to complete a transaction. Once transaction costs were incorporated, margins for brokers and wholesalers declined sharply, in some cases by more than half, while retailers were less affected. Farmers' margins also declined after adjustment, though they remained substantially higher than those of midstream actors. These adjustments indicate that transaction costs are economically impactful and affect the distribution of returns across actors in informal value chains. Gross margin estimates alone therefore substantially overstate the effective profitability of intermediary actors, as they fail to capture costs associated with coordination, uncertainty, and failed transactions. Farmers' margins, by contrast, remained comparatively high after adjustment, indicating that the burden of transaction costs concentrates among midstream actors. These findings challenge the prevailing assumption that brokers and wholesale traders capture disproportionately high returns for minimal value added. Recognizing and quantifying transaction costs is therefore essential to inform policies aimed at improving efficiency and equitable value distribution in food value chains in low- and middle-income countries

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Contact Address: Youri Dijkxhoorn, Wageningen University & Research, Wageningen Social & Economic Research, Droevendaalsesteeg 4, 6708 PB Wageningen, The Netherlands, e-mail: youri.dijkxhoorn@wur.nl