

# Producer Organisations and vertical coordination; an economic organisation perspective

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# Outline of the presentation

- Vertical coordination
- Producer organisations
- Transaction Cost Perspective
- Issue in new functions
- Organisational issues
- Conclusion



# Changes in agrifood industry

- Liberalization and privatization
- Internationalization of agrifood supply chains
- Rise of supermarkets
- Shift from public to private food standards
- More product differentiation and market segmentation



# Motives for more vertical coordination

- Improve logistic efficiency
- Raise quality / guarantee quality
- Innovation / product differentiation
- Improve customer responsiveness / market orientation



# Definition of vertical coordination

- Vertical coordination is:
  - Aligning activities between sellers and buyers
  - Aligning activities among participants in a supply chain (A → B → C)



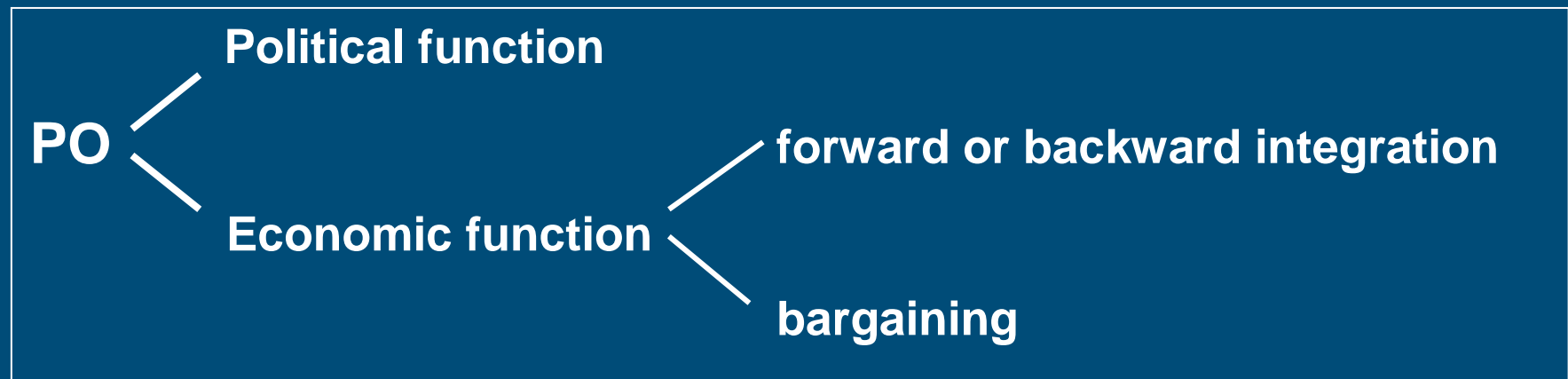
# Is there a role for producer organisations (POs) in vertical coordination?

- If so, what role?
- World Bank, IFAD, FAO, NGOs and many others do think there is role for POs in providing market access for smallholder farmers
- We focus on the role of POs in connecting farmers to high quality markets



# Producer Organisation: typology

POs come in many kinds: farmer organization, rural producer organisation; agricultural producer organisation, agricultural cooperative, farmer association, producer group, producer association, bargaining association



# Producer Organisation: definition

A PO is a formal, voluntary membership organisation set up for the economic benefit of agricultural producers by providing these producers with services in support of their farming activities, such as bargaining with customers, collecting market information, providing inputs, providing technical assistance, providing processing and marketing of farm products.



# Transaction Cost Theory

	<b>Governance problem</b>		
	<b>Asset specificity</b>	<b>Behavioural uncertainty</b>	<b>Coordination and adaptation</b>
<i>Direct transaction costs</i>	Costs of crafting safeguards	Screening and selection costs; Measurement costs	Finding information; communication and decision-making
<i>Opportunity costs</i>	Failure to invest in productive assets	Failure to identify appropriate partners; Productivity losses through reduced effort	Maladaptation; Failure to benefit from synergy



# Asset Specificity in high quality supply chains

- Particular partner transactions
- Quality enhancing investments become buyer-specific
- The number of buyers is reducing
- More targeted markets (organic, etc)
- Buyers may also make specific investments



# Behavioural Uncertainty in high quality supply chains

- High quality products are often credence products
- Quality requirements of (international) customers may change often and unexpectedly



# Coordination in high quality supply chains

- $A \rightarrow B \rightarrow C$  : Transaction between A and B is connected to transaction between B and C
- Connectedness is a typical coordination problem, requiring information exchange and central (or joint) decision-making
- Examples of connectedness:
  - When B has established a reputation/brand vis-a-vis C
  - When A, B and C align logistics
  - When A, B, and C jointly develop innovations



- What are the new demands on POs in supporting vertical coordination?
- What are the new functions of POs in reducing the transaction costs related to asset specificity, behavioural uncertainty and connectedness of transactions?



# Issue 1: Information exchange function

- POs will no longer collect market information, but customer information
- More marketing expertise is needed



## Issue 2: Technical assistance function

- POs will provide their members with technical assistance in order for them to be able to comply with high quality standards
- More technical expertise is needed



# Issue 3: Contract Farming

- POs will facilitate contract farming arrangements by providing their members with information, technical assistance, inputs, etc.
- More contracting skills are needed



# Issue 4. Professional Management

- POs will hire or develop more professional management
- Professionalize board members?
- Impact on allocation of decision rights between members/board and management?



## Issue 5. Size of the PO

- Supplying high quality markets may lead to smaller POs
- What does that mean for countervailing power?



## Issue 6: Multipurpose or single purpose

- We are likely to see a shift from multipurpose POs (with social, economic and political functions) to single purpose POs (with only economic function).
- What does that mean for social capital?



# Conclusions

- POs can combine vertical coordination (in the supply chain) with horizontal coordination (among producers), and therefore can play an important role in connecting (small) farmers to high quality supply chains
- However, this role is conditional on organizing efficient information exchange and efficient decision-making

