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Food security

Food security is high on the international agenda and dominates the development discourse. Through a series of Policy Briefs, each looking at a different topic within food security, the Royal Tropical Institute (KIT) aims to contribute to enhanced policy and practice on this issue.

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Domestic versus export markets: challenging the holy grail

The fascination for globalizing agricultural markets dominates the development agenda. In many developing countries however, domestic markets are growing, and offer significantly more potential than export-oriented chains, in terms of their contributions to the local economy, food security and poverty alleviation. This Policy Brief argues for an increased focus on domestic market development, particularly in sub-Saharan Africa.

CHALLENGING EXPORT-LED AGRICULTURAL DEVELOPMENT

Many African countries have long been heavily dependent on exports of traditional crops such as cocoa, coffee, cotton, sugar and tea. Together, these commodities account for 50% of Africa's total agricultural exports (Diao & Hazell, 2004). Yet a few countries, including Ghana, Ivory Coast, Kenya and Zambia, have achieved notable successes in exporting non-traditional, high-value crops. In Kenya, for example, exports of flowers, fruits and vegetables have increased fourfold since 1974, and horticulture is now one of the country's largest sources of foreign exchange earnings. In recent decades, development support has focused on creating and strengthening agricultural supply chains linking small-scale producers in developing countries to markets in developed countries. There is growing evidence, however, that in many cases, particularly in Africa, these interventions have not delivered the expected economic development or improved food security at the level of small producers.

According to FAOSTAT, for example, small and medium producers export only 3% of their total output. An analysis by IFPRI shows that even if Africa's traditional exports were to grow at a rate of about 6% each year, the real per capita agricultural income for all of Africa would grow by only an additional 0.3–0.4% (Diao & Hazell, 2004). At that rate, even the successful non-traditional exports would increase per capita agricultural income by just 0.2–0.3% per year, and more rapid growth is unlikely to translate into economic improvements within the next 10–15 years.

Clearly, exporting agricultural products has not contributed to a significant increase in farm income.

THE DOWNSIDES OF EXPORT-LED GROWTH

The export-led growth model has transformed the economies of Asian Tigers such as India, Indonesia and China. These countries have become competitive global players, and have succeeded in lifting millions out of poverty. However, it is now widely acknowledged that the export-led growth model has several downsides:

- the *'race to the bottom'*: to gain and maintain a competitive advantage in international markets, businesses are forced to cut corners, with negative effects on working conditions and the environment;
- most of the value added to products is exported; and
- the reliance on the changing patterns of demand and consumption in the importing countries has led to increased dependency and vulnerability of many developing economies.

Policy Brief 1

DEVELOPING DOMESTIC MARKETS

THE SUPERMARKET REVOLUTION
The rapid penetration of supermarkets in Africa has had significant impacts on domestic food supply systems. In many countries, the market share of supermarkets has risen from 10–20% to more than 50% in just 10 years. For smallholders, supermarkets present many challenges, such as meeting quality standards, but they also offer new opportunities as outlets for local produce. Reardon & Berdegué calculate that in 2000, supermarkets in Latin America bought 2.5 times more fruits and vegetables from local producers than the continent exported to the rest of the world!
(Reardon and Berdegue, 2007)

In view of the limited contribution exports can make to development, African farmers will need to explore other opportunities, in particular domestic food markets, which in many countries are growing rapidly. This growth is driven by a number of factors.

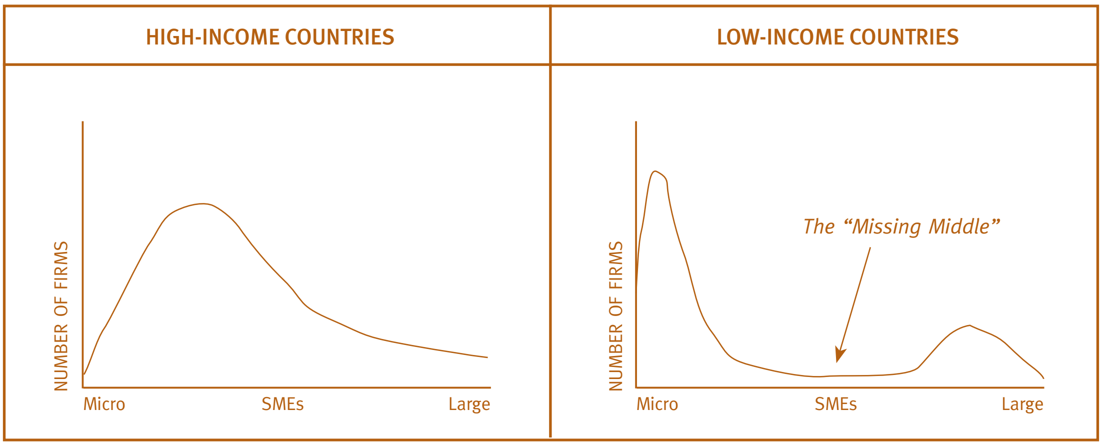
First, the population of Africa will continue to grow, particularly in less developed regions, from 1 billion to an estimated 2 billion by 2050. So too will the demand for agricultural produce and high-value food products. The middle class may hold the key to a rebalancing of African economies towards more dependency on domestic demand and away from a heavy reliance on exports, as well as to greater and more efficient poverty reduction and inclusive growth' (AfDB, 2011). The African Union Commission expects that the value of these markets will rise from US$ 50 billion in 2000 to US$ 150 billion by 2030 (UNIDO, 2010).

Second, the patterns of demand are changing. African populations are not only growing, but will soon be overwhelmingly urban. By 2050, about 60% of Africans – about 1.2 billion people – will live in cities, compared with just 28% in 1980 (FAO, 2009), and are already demanding higher-quality food and a more diverse range of products. Dietary patterns are also changing, towards foods with more calories, fats and protein (Reardon & Timmer, 2007), increasing the demand for value-added and processed food (FAO, 2009).

A third factor driving the change in demand has been the influx of foreign direct investment (FDI) in the agricultural sector. Since the market liberalization reforms of the 1990s, much of this investment has been concentrated in the food processing, retail and services sectors (Reardon & Timmer, 2007). FDI has introduced new benchmarks in terms of quality standards and consumer convenience and therefore changed consumer demands and purchasing patterns.

For farmers and small and medium enterprises (SMEs) in Africa, the benefits of supplying domestic food markets, in terms of both volume and economic value, could soon dwarf those of exporting to overseas markets. But harnessing this potential to boost local development, fight poverty and improve food security will require investments to increase the efficiency of agro-food chains, including domestic agro-processing industries. The collective potential income that farmers could derive at the farm level from increased trade in domestic and regional cross-border markets alone is expected to be as much as US$ 30 billion.
The African Agribusiness and Agro-industry Development Initiative (3ADI) estimates that developing the necessary market linkages could raise rural incomes by up to another US$ 60 billion (FAO/UNIDO, 2010).

Table 1: The "Missing Middle"



◀ THE "MISSING MIDDLE"
Small and medium enterprises (SMEs) typically employ between 10 and 250 workers, and form the backbone of modern economies. SMEs are often seedbeds of innovation and thus are crucial engines for economic growth. The agro-processing sector is typically SME based. In high-income countries, SMEs are responsible for generating over 50% of GDP and over 60% of employment, but in low-income countries they account for just 17% of GDP and 30% of employment.

The main reason for this difference, also called the 'missing middle', is that SMEs are often unable to obtain loans to start up or expand their businesses. Governments and development agencies need to address this lack of access to finance, as it is the key to local job creation, increased food security and poverty alleviation.

DOMESTIC AGRO-INDUSTRIES: NEGLECTED DEVELOPMENT POTENTIAL

Many developing countries face a persistent problem, however, in that the supply side of domestic food markets is not yet well developed. Agro-industries face high transaction costs and small profit margins, and they are not competitive as compared to imported food produce. Africa in particular has yet to make significant progress in improving the food processing sector and adding value to its primary agricultural products. African countries contribute less than 10% to global added value (FAO/UNIDO, 2010). This represents a significant loss of development potential.

At the World Summit on Food Security in 2009, various presentations noted that sub-Saharan countries face serious challenges if they are to meet the projected growth in the domestic demand for crop and livestock products. Developing an efficient and competitive agro-food sector, based on local sourcing, processing and retailing will require significant investments to improve agricultural output in food value chains and the necessary downstream support services. The FAO estimates that the total investments required will amount to some US$ 940 billion between 2006 and 2050 (FAO/UNIDO, 2010). About two-thirds of these investments will be needed to cover the capital costs of establishing rural and wholesale market systems, as well as cold and dry storage facilities, processing equipment and power supplies. Most of these investments will have to come from the private sector.

CREATING OPPORTUNITIES FOR LOCAL BUSINESSES

Since the 1990s it has been broadly accepted that support for the private sector is essential if developing countries are to achieve their socio-economic development goals, and public financial support has massively increased. In 2010, international financial institutions invested US$ 40 billion in private sector development.
A significant part of this external support was channelled to commercial banks on the assumption that they would provide loans to SMEs, but it is unclear whether these banks are really doing so. Indeed, a recent study of how these funds were allocated has shown that 40% went to international companies operating in Africa, while local businesses rarely benefited (Kwakkenbos, 2012). Only about 5–10% of the portfolios of commercial banks in Africa include agriculture and agro-industries, and loans are rarely extended to smallholders (www.mfw4a.org).

In a recent evaluation of projects funded by the International Finance Corporation, the World Bank (2011) found that less than half of the projects reviewed had been designed to deliver development outcomes, and just one-third addressed market failures, such as by enhancing access to markets or providing employment for the poor.

We do not argue against private sector investment as a means of achieving development goals, including improving food security. On the contrary! But the prevailing bias that favours the production of food crops and products for export rather than for domestic consumption suggests that the old image of the South as source for Western markets still prevails.

LOCAL SOURCING
International agribusinesses operating in Africa are increasingly sourcing their primary products from local suppliers.
The incentives to switch to local procurement are largely commercial, related to reducing supply chain risks and cutting costs related to imports. Establishing direct relations with local suppliers can enhance flexibility and enable better quality monitoring.
(Boomsma & Mangnus, 2012)

To achieve a large-scale impact on the food security of poorly endowed African households, a sincere paradigm shift among governments and their development partners is needed, towards supporting local market development by increasing the competitiveness of domestic food chains and agro-food industries. If enhancing Africa's food security is the goal, then Western donors and development partners should refrain from subsidizing export-oriented value chains that target high-end Western consumer markets (such as the fresh organic mango slices sold in Ahold outlets in The Netherlands). Rather, they need to develop a support framework for innovative local and Western agro-food business initiatives that focus on domestic consumer markets, particularly in Africa. These ventures require genuine risk capital that is currently not sufficient or available to them. Moreover, we suggest that any support to private sector actors, particularly commercial banks, should come with more stringent conditions, to ensure that the funds are used to invest in the agricultural sector and deliver on development results.

These conditions must also be more explicit. The impact pathways must also be more transparent in order to justify spending public resources on private companies.

AGRO-PROCESSING AND FOOD SECURITY

The FAO (2009) notes that local agro-processing of food commodities could improve food security in four important ways:

- by reducing post-harvest losses – by an estimated 50% for roots and tubers and up to 70% for fruits and vegetables;
- by extending the shelf-life of farm produce so that they can be transported to urban markets;
- by adding value, thus increasing farmers' incomes and their purchasing power;
- and by improving food quality and safety standards, and reducing food-based health risks.

THE WAY FORWARD

Many donors and development partners are now supporting private sector development in Africa, with the ultimate goal of poverty alleviation and improved food security. To ensure that this support is effectively contributing to these objectives, we propose that they focus on the following:

1. Providing clearly earmarked funds to support investments in local agricultural sectors, from production to agro-processing and retailing.

2. Lobbying towards national and sub-national authorities for an enabling environment that will encourage the development of SMEs and agro-businesses.

3. Placing more stringent con-ditions on the public funds provided to Western businesses operating in Africa, including a clear indication that they should focus on transferring knowledge, investing in local businesses and sourcing from local suppliers.

4. Building in safeguards that will guarantee inclusive development through smallholder-based production and supplier models with a genuine gender focus. ■

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