

Value chains to drive rural development

Policy makers frequently associate rural development with how 'value chains' work. A value chain is the set of activities whereby a company takes raw materials and turns them into finished products by adding value at each step. **PETER JACOBS** and **STEWART NGANDU** review how value chains can contribute to improving the living standards of rural communities, using examples like organic food, tourism and craft value chains.

Under apartheid, the state used an array of policies to direct the geographic spread of key economic activities and sectors. Policies fostered a highly skewed geographic concentration of economic sectors, with high value-adding industries in a limited number of cities. Rural homelands largely functioned as labour reserves.

Since 1994, the government has been searching for workable and lasting strategies to pull rural areas out of underdevelopment.

The Comprehensive Rural Development Programme (CRDP), launched in 2009, for instance, seeks to pool resources from multiple state departments to uplift the most downtrodden rural locations. Its emphasis is on 'participatory development' and suites of projects to fast-track the delivery of much-needed rural infrastructure and services.

The New Growth Path also spells out far-reaching goals. It aims to increase employment in agriculture, despite ongoing job shedding in the farming sector. It also wants to expand the number of smallholder farmers and help them to effectively participate in agricultural value chains.

WHAT IS VALUE-CHAIN ANALYSIS?

At its most basic level, a value chain refers to the movement or lifespan of goods and services through production, trade and consumption stages. Consumers form the downstream end of the chain, whereas the initial producers make up the upstream beginning. Between these extreme points of the chain are many other segments, markets and actors.

Value-chain analysis begins with a detailed map of the full economic value of a product or service at each stage in its production and distribution process. But it embraces a wider

domain as it also seeks to diagnose pro-poor impacts in supply chains.

Timothy Sturgeon and his colleagues at the Massachusetts Institute of Technology – leaders in this field – proposed the following core elements to guide such a step-by-step interrogation:

- geographic spread and character of linkages between tasks, or stages, in the chain of value-added activities;
- distribution and exertion of power among firms and other actors in the chain, and;
- roles of institutions in structuring business relationships and industrial location.

With any systematic application of these guidelines it ought to be possible to pinpoint 'who gets what' or how benefits are distributed along the value chain. Enabling poorer producers to move into higher-value segments in a value chain is broadly called 'upgrading'. It is a critical mechanism to redistribute benefits towards low-value upstream actors.

Functional upgrading refers to the progressively expanding mix of value-adding tasks devolved to marginalised producers, thus enabling them to capture a larger share of value-added returns.

Researchers who use these concepts and principles to examine the development potential of specific commodities usually rely on the following list of questions:

- Who benefits?
- How should the benefits be calculated?
- Are the gains equally spread between the participants?
- Are firms being upgraded or downgraded in the process? Upgrading is an essential aspect of ensuring a sustainable trajectory of economic development.
- What drives upgrading through the value chain? (upgrading of products, processes and functional upgrading)

EXAMPLES OF HOW VALUE CHAINS WORK

To demonstrate the policy relevance of value-chain analysis, we summarise insights from three value chains: organic foods, tourism, and crafts. Each case highlights the mechanisms through which the rural poor stand to benefit – especially in the long-run.

Organic foods: Since 2003 there has been a remarkable expansion in South Africa's demand for organic foods.

Total sales revenue from organic exports and local consumption increased from R5 million in 2003 to R100 million by 2008. Two major domestic retailers have been driving this growth: Woolworths and Pick n Pay. Available estimates suggest that formal retailers might control 90% of all organic sales in the domestic market.

South Africa still has to formulate a coherent set of laws governing standards for organic produce. Consequently, the retailers that dominate this industry currently define the 'quality dynamics' through standards and certi-

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fication. Certified organic food is predominantly consumed in metropolitan areas. Organic fresh produce sells at a considerable price premium. Experts say that organic produce might be healthier for consumers (particularly certified products) and organic farmers pride themselves on their environmentally friendly farming methods.

Consumers who understand the health and environmental benefits of organic produce are prepared to pay the price premium for organics, if they can afford them.

There is no precise figure on the total number of organic farmers and producers in South Africa. Estimates from the most recent research suggest that there are 250 to 300 certified organic farmers in South Africa farming on approximately 45 000ha. Cost is arguably the main barrier to the spread of organic farming: organic farming might be 20 to 30% more expensive than industrial farming models. However, organic farming tends to take place on smaller plots of land, which opens opportunities for smallholder farmers, besides other social and environmental benefits.

Other determinants of success in this lucrative value chain include: post-harvest handling practices, such as storage; transportation, costly and onerous certification to comply with

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standards, for example. This context requires more proactive approaches in supporting small-scale farmers' market access – beyond their reliance on non-governmental organisations. Policy needs to address the potentially exclusionary dynamics of the quality trends.

Tourism: Natural resource-based and cultural tourism offers sustainable livelihood opportunities for communities in marginalised rural areas. But the potential benefits that flow to the poor from such tourism value chains depend on many factors, such as market segments targeted, direct employment in the sector, and inter-sectoral linkages.

The direct impact of employment is closely related to wage levels in a particular segment of the tourism market and the degree of labour-intensity in locations where tourists spend their money. Non-managerial workers tend to earn very low wages, increasing their dependency on generous but precarious tipping.

Yet direct flows to the poor from tourism depend on their ability to find a job in the sector (hotel and restaurant workers, taxi drivers and guides), especially during the peak tourism seasons.

Such direct flows usually account for over half of all pro-poor benefit flows. Indirect linkages, through downstream crafts and local agricultural spending, could also account for sizeable pro-poor benefit flows. The strength of the relationship between the tourism and non-tourism economy is a crucial determinant of the developmental spillover along this value chain.


Crafts: Globally and in South Africa, the size of the creative arts industry is relatively large and the demand for crafts is projected to grow at above average growth rates in the near future. However, rural craft makers tend to sell their creative artifacts in local markets. Connecting these rural enterprises (e.g. self-employed, co-ops) into particularly high-value external markets is a challenge.

In order to market crafts as niche products, special attention must be paid to product design, development and branding, in addition to pricing, fair trade and sustainable craft source material.

Switching from informal and ad hoc seller-buyer transactions to cultivating durable relationships in a highly competitive supply chain will be another challenge. Moreover, survival in the niche retail sector is tough for both retailers and producers, as they target a more affluent but smaller segment of the market. ◀◀

This is a summary of a background report, *Spatial dynamics of agricultural and non-agricultural value chains*, completed for the 2011 Diagnostic Report of the National Planning Commission (NPC).

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Is it the right thing to do?

**Suffer the
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