



Aid for Trade and engaging with global value chains: developing trade and reducing food insecurity?

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Abbreviations

Abbreviation	Description
AfT	Aid for Trade
EPA	Economic Partnership Agreement
EU	European Union
FDI	Foreign direct investment
FTA	Free-trade agreement
GVC	Global value chain
HCDA	Horticultural Crops Development Authority
KFC	Kenya Flower Council
Ksh	Kenyan shilling
QMS	Quality management system
SSA	Sub-Saharan Africa

Executive summary

The World Trade Organisation-led Aid for Trade (AfT) initiative can be used to enhance global or regional value chains by working with the private sector and focusing on alleviating the binding constraints or market failures that hold back the appropriate functioning of value chains. For example, it can improve logistics, infrastructure or services. The research and analysis presented in this paper assesses the role of AfT in assisting the integration of agricultural producers in sub-Saharan Africa (SSA) into high-value agricultural global value chains (GVCs). The arguments for going into high-value (and high-sophistication) exports, and therefore for moving up GVCs, are about developing the economic structure, and thus increasing income, and thus reducing food insecurity.

Since the 1980s, when the latest phase of globalisation began, which is characterised by the fragmentation of global production across countries, agricultural producers in SSA have been increasingly integrated into the global trading system through their participation in GVCs. This has included through their integration within high-value agricultural GVCs such as horticulture. The rationale underpinning the adoption of some of these export-oriented growth strategies was an implicit assumption by donors that the revenues generated would subsequently be utilised for product and process upgrading, promoting the development of domestic capabilities, and increasing productivity and wage-earning opportunities.

This paper seeks to explore the following key questions: How has AfT been used to help developing countries to tap into high-value GVCs and global production networks? And how could the potential benefits of the above approach be enhanced and disadvantages be mitigated? These questions are assessed qualitatively, firstly through reviewing the existing literature, including AfT disbursements, modalities and the support used to assist different types of producers (and labourers) in participating in high-value agricultural GVCs. Secondly, the relative success and merits of such an approach are reviewed and assessed using a range of data sources, including in-country key-informant interviews.

One limitation of donor interventions in the sector to date is that they have still not adequately addressed asymmetries in the trading relations that exist between producers and buyers within the cut-flower GVC. Overall, it could be said that there is some evidence of some Kenyan firms moving towards a position of full-package suppliers. However, this shift seems to be limited to the largest group of firms, and has not necessarily been the case for small and medium-sized firms. It is this latter group of firms that also face increased costs in the Dutch market because of the inability of the Kenya Flower Council (KFC) to obtain mutual recognition of the standards its producers adhere to and those demanded in Dutch auction houses. This barrier to entry could result in the productive structure in Kenya remaining relatively polarised between very large growers and small growers, with medium-sized firms either reducing in size or being consolidated into larger firms (although much more evidence is needed to substantiate this hypothesis).

This paper has shown how the evolution of the cut-flower GVC has affected the participation and engagement of producers with this type of trade, which operates within a

hierarchical structure of governance with highly consolidated marketing and retailing nodes. It has argued that some of the more recent challenges for some types of producers require a greater consideration of power asymmetries among firms. In a globalising world where GVCs are increasingly important, the ability to shift goods in and out is essential to a country's competitiveness, and infrastructure and low tariffs matter. Yet the cut-flower industry also faces a set of non-tariff barriers. We can therefore see a situation arising where donor efforts to reduce the costs of certification and overcome other non-tariff barriers that can prevent traders from accessing external markets are being undertaken without necessarily considering the need to also influence the private relations that exist among firms operating within GVCs. The reasons for this are rather unclear.

A question arises, therefore, as to how the KFC can achieve the mutual recognition of standards by Dutch auction houses (which effectively operate as a private members' club). In effect, these auction houses can set whatever standards they want and so it is up to the KFC to reach an agreement with them. This could provide a new role for AfT. Such an approach could help not only to resolve some of the governance issues that exist between firms and buyers, but also to ensure that such firms are better able to influence the external governance structures within which they trade. Although the Kenyan cut-flower GVC has been in operation for a considerable amount of time, as is shown in this paper, only some types of firms have been able to obtain a more secure supplier position over time.

1 Introduction

The World Trade Organisation-led Aid for Trade (AfT) initiative can be used to enhance global or regional value chains by working with the private sector and focusing on alleviating the binding constraints or market failures that hold back the appropriate functioning of value chains. For example, it can improve logistics, infrastructure and services. The research and analysis presented in this paper assesses the role of AfT in assisting the integration of agricultural producers in sub-Saharan Africa (SSA) into high-value agricultural global value chains (GVCs). The arguments for going into high-value (and high-sophistication) exports, and therefore for moving up GVCs, are about developing the economic structure, and thus increasing income, and thus reducing food insecurity.

Since the 1980s, when the latest phase of globalisation began, which is characterised by the fragmentation of global production across countries, agricultural producers in SSA have been increasingly integrated into the global trading system through their participation in GVCs. This has included through their integration within high-value agricultural GVCs such as horticulture. The rationale underpinning the adoption of some of these export-oriented growth strategies was an implicit assumption by donors that the revenues generated would subsequently be utilised for product and process upgrading, promoting the development of domestic capabilities, and increasing productivity and wage-earning opportunities.

All trade takes place within value chains, but there are different types, as will be discussed below. The GVC approach is a distinct methodological tool that focuses on the dynamics of inter-firm linkages and international industrial organisation, as opposed to considering the production and export of goods in isolation. This study reviews and makes reference to specific GVCs and country case studies in SSA, including Kenya. It focuses on the country case study of Kenya because interventions to facilitate trade and producers' integration within GVCs have been ongoing for longer than the term AfT was agreed among World Trade Organisation members (in 2005), and there have been some shifts in approaches as lessons have been learnt.

This paper seeks to explore the following key questions: How has AfT been used to assist developing countries tap into high-value GVCs and global production networks? And how could the potential benefits of the above approach be enhanced and disadvantages be mitigated? These questions are assessed qualitatively, firstly through reviewing the existing literature, including AfT disbursements, modalities and the support used to assist different types of producers (and labourers) in participating in high-value agricultural GVCs. Secondly, the relative success and merits of such an approach are reviewed and assessed using a range of data sources, including in-country key-informant interviews.

The paper is organised as follows. The following section discusses recent trends in global production and trade. The next section discusses how development practitioners have adopted the GVC approach to identify the scope for potential intervention, and provides an overview of the different types of AfT and disbursement mechanisms. The next section reviews the existing literature related to the use of AfT and high-value agriculture and links

these interventions to specific value chain nodes, objectives and outcomes. We then proceed to focus on the country case study of Kenya, which includes the results of key-informant interviews with workers in the sector. The conclusion highlights the main policy lessons that may be drawn.

2 Trends in global trade, GVCs and the role of AfT¹

The GVC literature became prominent during the 1990s as product- and sector-specific studies were motivated by the need to better understand how producers engage with the process of globalisation and its implications for the development of productive capacity and capabilities. A number of comparative value-chain studies across sectors, including agriculture, have acknowledged changes in global production and methods of coordination, and have explored what this meant for firms and their labourers (Cramer, 1999; Daviron, 2002; Dolan et al. 1999; Ponte, 2002).


The GVC approach to analysis takes as its starting point asymmetric trading relations between developed and developing countries. Although the GVC literature continues to develop, both conceptually (e.g. increasing recognition of production networks) and empirically (e.g. by employing more robust research methods), the basic unit of analysis remains the same: looking through the GVC lens at production by firms and labourers that are linked to international markets and assessing their relative returns (e.g. wages, skills development) at a particular point in time, as well as over time.

The concept of a GVC refers to a configuration of coordinated activities that are divided among firms and have a geographical scale (Ponte and Gibbon, 2005: 77). To some extent, therefore, the GVC methodological approach follows a casual chain approach to analysis. It therefore focuses on the dynamics of inter-linkages and the way in which firms and countries are globally integrated. It raises the question of how producers (firms, regions or countries) participate in the global economy. Analysis goes beyond firm-specific linkages to reveal the dynamic flow of economic, organisational and coercive activities among producers in different sectors on a global scale (Kaplinsky and Morris, 2001: 2).

Some types of GVC governance may facilitate rapid producer upgrading, while others may hinder this process. For example, smallholders' engagement with global agribusiness may initially mean a rapid transfer of knowledge and expertise as producers are integrated into supply chains. Although this may mean that producers are upgraded at a particular point in time, it does not necessarily mean that this also happens over time, in terms of movement from one functional position in the GVC to another; for example, moving from being solely a producer towards a full-package supplier directly dealing with retailers. Table 1 summarises a classification of governance structures identified by Gereffi et al. (2005) with reference to the relationships that exist among firms organised within GVCs.

¹ This section draws on Keane (2012; forthcoming).

Table 1: Key determinants of GVC governance

Governance structure	Complexity	Codification	Capabilities	Degree of explicit coordination
Market	Low	High	High	Low
Modular	High	High	High	
Relational	High	Low	High	
Captive	High	High	Low	
Hierarchy	High	Low	Low	High

Source: Adapted from Gereffi et al. (2005)

2.1 GVC governance structures

The five types of GVC typologies are distinguished by their governance structures, which are functions of the complexity of the transaction, the ability to codify aspects of it and the capabilities of producer. Given this classification, the GVC approach considers trade to be embedded in, but also to a considerable extent determined by, specific (but changing) institutional structures and organisational aspects of international trade (Raikes et al., 2000).

However, external GVC governance structures usually remain outside of the modelling sphere of ‘which GVC takes what shape and why’.² The governance structures posited by Gereffi et al. (2005) do not include reference to external structures, including those negotiated by governments for private actors, but rather focus on the internal structures between firms and private actors. That is, it is fair to say that the GVC literature is not wholly satisfactory in respect of the links between different types of internal and external chain governance (see Keane, 2012).

For example, the depth of liberalisation of trade and finance undertaken by countries in SSA since the 1980s has determined the type of actors and firms involved with production and trade within GVCs. Since contract farming is a form of vertical coordination among firms, it means that attention must be paid to how global agribusiness accesses smallholder supply and the terms of sale. This means taking account of the playing field negotiated by governments for private sector actors. Much of the more recent debate as to how producers and farmers in SSA engage with buyer-driven GVCs highlights the tensions caused by, on the one hand, achieving rapid process upgrading for some types of producers but, on the other hand, raising barriers to entry for others. However, the literature is divided as to the circumstances when smaller – and poorer – producers (and farmers) are excluded from rather than included in high-value GVCs.

Adherence to the standards required to access higher-value markets may act as a catalyst of and spur to productivity (Jaffe, 2007), as well as increase incomes for producers and wage-earning opportunities (Humphrey, 2003). At the same time, this upgrading process may marginalise other producers who are unable to meet such demanding requirements (Dolan and Humphrey, 2000). One response therefore is to improve the organisation of producers so as to reduce the diseconomies of scale that result from procuring from individual producers. This would require purposive actions to be undertaken by the government with private sector collaboration.

This suggests that an understanding of the nature of value chain governance, as well as the permanent structural changes that may result, is crucial to understanding the dynamics of barriers to entry and the creation of rents. Increased coordination, when it is forthcoming between value-chain nodes, could be temporary and necessary in order to drive through innovations within a value chain at a particular point in time. The mechanisms through which coordination and the complexity of information are conveyed among actors trading within GVCs could, however, also become permanent and embedded within the external

² These include other external governance structures such as mandatory standards that producers must legally adhere to in order to access markets.

governance structures surrounding trade, either as de facto market access requirements or as benchmarks for which a priori capabilities are needed before being included within a GVC.

In effect, therefore, governance structures, both internal among firms, but also external and negotiated by governments for firms, may serve as barriers to entry and a force for both exclusion and inclusion. These structures may result in the creation of rents for some types of producers relative to others, which may be influenced by government action so as to facilitate entry into and participation in GVCs.

The export of products in the category of horticulture (such as green beans and cut flowers) has formed the basis of export-diversification strategies for many countries in SSA (Gibbon and Ponte, 2005; Humphrey, 2003). The growth of the horticultural industry in Kenya in particular is regarded as one of the major export success stories in SSA (Jenkins, 2005). Investment into the sector has taken the form of outsourcing production through developing contractual relations among firms across borders.

Movement into high-value agricultural GVCs has in some cases been facilitated by preferential market access into developed country markets. The tariff rent made available through preferential market access to some groups of countries relative to others has provided a form of locational advantage so as to attract investment. Preferential market access to the European Union (EU) market is recognised as having played a significant role in the development of the industry in Kenya during the 1990s (Stevens and Kennan, 1999). This level of access has thus far been maintained as a result of the initialling in 2007 of an Economic Partnership Agreement (EPA) between the East African Community and the EU that takes the form of a reciprocal free-trade agreement (FTA).

There are current uncertainties, though, since at the time of writing the EPA is yet to be signed and ratified. The external trading environment has therefore changed: prior to 2007 Kenya benefitted from preferential market access under the Cotonou Agreement, a non-reciprocal trade agreement. Stevens (2001) argues that trade analysis suggests that past EU trade policy effectively excluded many of the most important global suppliers from the UK market. However, this advantage has been eroded over time as the Cotonou Agreement has expired and as a result of the proliferation of FTAs more broadly. Trade preferences therefore play an important role in determining some of the power relationships inherent in GVCs as a variable part of external governance structures.

2.2 The role of AfT

It is increasingly recognised that countries may need further assistance to tap into the modern export sector beyond the tariff rent made available through the granting of a unilateral trade preference. Reductions in tariffs and non-tariff barriers have not always resulted in increased flows of trade, therefore partly in response to this AfT was developed as an instrument to assist countries in addressing other supply-side constraints, as discussed in detail by Basnett et al. (2012). Since then attention has shifted towards increasing the effectiveness of AfT. Table 2 provides an example of the coordination and market failures whose elimination may assist countries to tap into modern sector exports, including high-value agriculture. These types of interventions are then linked to AfT categories. Some of the challenges of operationalising these interventions are discussed in the following section.

Table 2: Market failures affecting entry into and participation in GVCs, and responses

Type	Examples	Responses	AfT category
Coordination	Externalities, complementarities ignored; linkages not exploited; no policy coherence	Capacity building for industrial policy	Trade development; trade-related infrastructure; building productive capacity
Technology: developing, adapting and adopting	Incomplete and imperfect information; network externalities	Promotion of technology transfer and adoption	Trade development and trade-related infrastructure
Skills formation	Externalities; imperfect information	Coordination and/or subsidies for training	Building productive capacity
Environment: protection, conservation, cleaner technologies	Negative externalities not accounted for	Product and process standards and regulations	Trade policy and regulations

Source: Adapted from Te Velde and Morrissey (2005)

3 The use of AfT to assist producers to enter and participate in high-value agricultural GVCs³

The following section briefly reviews the available literature on the assistance provided to producers in relation to entering and enhancing participation in the horticultural GVC in Kenya. The horticultural chain became increasingly dominated by large retailers by the late 1990s (Dolan et al. (1999)). As a result of these shifts production shifted away from smallholders towards large farms, many of which were owned by exporters. This is because sourcing from directly owned units means firms are able to exert greater control over production processes and are better able to comply with quality, environmental and social standards. Larger farms also have the necessary scale so as to buffer major investments in, for example, irrigation systems and other relevant technologies.

It is the consolidation of the marketing nodes of the horticultural GVC value chain, for example through supermarkets mergers and acquisitions, that results in a buyer-driven and therefore hierarchical governance structure, as discussed in the previous section. In striving for achieving economies of scale at nodes of production, some backward vertical integration took place between exporters and producers. This transformation meant that during the 1990s arms-length and market-based relations between independent firms were replaced with more hierarchical governance structures, with transactions being undertaken mostly on an intra-firm basis. Standards were harmonised across retailers in the UK and Dutch markets through the introduction of the EurepGAP standard (now known as GlobalGAP).⁴

Because this private voluntary initiative raised the standards bar, there were concerns that smaller producers would not be able to overcome the technical and financial barriers associated with obtaining certification and complying. In order to avoid the potential marginalisation of smallholders from the horticultural GVC in Kenya, donors intervened to cover the costs of compliance associated with the standard. At that time, donor support was crucial in subsidising the certification process for smallholders and therefore ensuring their continued participation in the horticultural GVC. However, it remains debatable how far the programmes supported by donors also subsidised exporters (and, indeed, buyers), given that it is difficult to assess whether the benefits accrued mainly to farmers or retailers (FAO, 2006).

³ This section draws on Keane (2012; forthcoming).

⁴ GAP stands for 'good agricultural practices'.

Despite these concerns, the more stringent export requirements associated with the horticultural GVC have resulted in significant investments in efficiency and productivity in the sector: Kenya is often referred to as a country that has been able to transform the challenges of adhering to standards in production into opportunities (Henson and Jaffe, 2006). The case study of Kenya and the broader implications highlighted by its experience are discussed in more detail in the following section.

3.1 Upgrading producers to meet standards⁵ in Kenya

GlobalGAP, previously known as EurepGAP, is an example of a private voluntary initiative agreed by retailers so as to ‘reassure their consumers about the environmental impact of farming, and engender a responsible approach to worker health and safety as well as animal welfare’.⁶ The code of practice was initially launched in 1996 by a group of 11 British and Dutch retailers with the objective of creating a single private sector standard for ensuring the food safety and quality of fruit and vegetables from seed to farm gate.⁷

Although the standard helps to avoid multiple audits of standards required by buyers through providing a standardised monitoring of these standards, it also goes beyond mandatory market access requirements. Although some of the standards included within GlobalGAP may be defined as being private voluntary initiatives, they have effectively become a prerequisite for market access and inclusion within the GVCs that supply retailers in the UK and Netherlands (the market structure of which exhibits oligopolistic tendencies). Most European buyers of agricultural products now demand evidence of certification as a prerequisite for doing business. Thus GlobalGAP has a major influence on how horticulture GVCs are structured, including in Kenya.

3.1.1 Initial donor interventions

There are two options for certification. Option 1 is more stringent and requires compliance with all control points. Most large-scale growers opt for this. Most small-scale growers take the second option, which is less stringent, but requires quality management systems (QMSs) to be put in place (see IIED and NRI, 2008). Most donor efforts have been devoted to certifying smallholders organised as groups under GlobalGAP Option 2 (group certification). Under this option, farmers have to develop their own technical teams and QMSs.

The IIED and NRI (2008) estimated that on average £1,000 (\$1,970) was required per small-scale grower to ensure compliance, a major investment that would have meant the exclusion of many producers who were unable to cover such high costs. However, in the cases they analysed these costs were spread over stakeholders: 36% borne by small-scale growers, 44% by exporters and 20% by external agencies (donors). The IIED and NRI (2008) also found that the recurrent costs associated with compliance were on average £175 (\$345) per annum, with 14% paid by the growers themselves and the remainder by exporters. The most challenging criterion in the GlobalGAP implementation process was reported to be the record-keeping requirements associated with the demand for the traceability of produce and chemical application.

Non-recurrent costs, however, vary according to the size of farms and number of employees, etc. For example, Henson and Jaffe (2006) estimated non-recurring costs to be in the region of \$450–510 for outgrowers (with 15–20 acres) who supply exporters and

⁵ This section is adapted in parts from Ellis and Keane (2008).

⁶ The protocol defines the elements of good agricultural practices and includes standards for integrated crop management; integrated pest control; quality management systems; hazard analysis and critical control points; worker health, safety and welfare; environmental pollution; and conservation management.

⁷ See Ellis and Keane (2008) for further information.

\$75,000–\$100,000 for integrated producer/exporters (with 1,000–1,800 acres). These costs vary from less than 4% of annual sales for producer/exporters to 6–11% for smaller producers. Although initial investments may be substantial, they may be recuperated over time through the ability to access a higher-value market. According to survey results, Asfaw (2008) points out that the initial costs of investment by individual farmers may be paid off within three years with donor support and finance or seven years without.

Despite this, UNCTAD (2008) notes that certification remains an immense challenge for most producers in SSA, requiring investments at both the macro and farm levels. Even with donor interventions, the ability of some producers to remain within the horticultural GVC particularly in Kenya has been rather limited. For example, based on case study and survey data, IIED and NRI (2008) point out that between 2003 and 2006, 60% of Kenyan growers were dropped from compliance schemes owing to problems with implementation. Of those able to attain certification, 15% were subsequently dropped by their exporter because the costs of maintaining their certification was not matched by the level of income obtained.

Many Kenyan exporters have significantly reduced their involvement with small-scale growers since the introduction of GlobalGAP in mid-2003. This is because recurrent costs remain high relative to average smallholder margins. The results of a survey by Asfaw et al. (2007) of adopters of EurepGAP and non-adopters ‘empirically demonstrates that resource poor farmers with limited access to information and services hardly comply with the food safety standards’. The sustainability of donor interventions to subsidise certification processes has therefore been called into question.

3.1.2 Successes and continued challenges

The sustainability of donor interventions in the sector should be analysed in two ways: firstly, in relation to the continued inclusion and participation of some producers within the horticultural GVC and, secondly, in relation to the potential spillover effects that may result from participation in this GVC, even if this participation is not sustained over time. Donor assistance in meeting the standard has delivered benefits for some producers, such as training and infrastructure development. Some of the benefits reported by the IIED and NRI (2008) for African smallholders include the following:

- the continued ability to profit from preferential market access
- non-financial benefits, such as improved field hygiene, better knowledge about pesticide use and improved farm management capabilities
- learning about good agricultural practice
- transferring this knowledge to family farms.

However, what is clear is that the benefits of GlobalGAP certification for producers depend on the institutional context, and the extent to which private and public actors collaborate in the development of producer organisations so as to reduce transaction costs and enhance potential spillover effects. Although compliance with the standard enables the effective management of the risks associated with the spread of plant/animal pests and the incidence of microbial pathogens or contaminants (see UNCTAD, 2008), and although this learning may have long-term benefits, the ability to embed such knowledge in institutions – and therefore enhance institutional memory and national knowledge systems – requires collaboration between private and public sector actors.

An alternative approach for donors, therefore, could be to focus on strengthening public organisations so that capacity is built to both undertake certification processes and reduce transaction costs. The ability of producers to reduce recurrent costs is a means through which smallholders continue to be included within the horticultural GVC. This may be achieved through the strengthening of producer organisations, including those comprising private firms collectively attempting to address, for example, coordination failures. It is in this sense that Henson and Jaffee (2006) view standards as catalysts for development if

compliance is viewed as a strategic move. The World Bank in its *World Development Report 2007* also finds this.

Notwithstanding these propositions, however, it is important to note that even when producers have been upgraded and comply with the standards, and Kenyan producer organisations are accredited to undertake certification and audit firms, this is not always recognised by buyers in end markets in the EU. These more recent challenges are discussed in the following sections, where recent shifts in donor and government interventions in the sector are also highlighted. Before doing this, however, an overview is first provided of the cut-flower value chain in Kenya as a sub-sector of horticultural production.

3.2 Structure of the cut-flower GVC

This analysis is based on the results of fieldwork and a number of key-informant interviews undertaken in and around Nairobi between September and October 2012. Three types of cut-flower firms were identified that vary in size, ownership and the functions they undertake. These include:

- Type 1: small firms
- Type 2: medium-sized firms
- Type 3: large multinational enterprises that specifically grow for auction.

Although a number of clusters of cut-flower production are in operation, these can be broken down in terms of the major hubs and their ownership structure:

- **Lake Naivasha** consists of approximately 35% domestic Kenyan farmers; the other 65% are Dutch and other foreign growers (Israeli and Indian). In this area the size of farms is estimated to be large.
- **Thika:** 70–80% Kenyan growers, the rest foreign. The area consists of rather more medium-sized growers.
- **Nakuru (and other):** mostly Kenyan small-scale growers; farms are relatively small (approximately 5–10 ha).

Most of the cut flowers produced in Kenya are destined for auction houses in the Netherlands (65%), while others supply retailers in other EU markets, notably the UK.⁸ An estimated 97% of total flower exports are from the largest firms, most of which are owned by foreign investors (Bolo, 2008). It has not been possible to verify this figure (which could be based on value or volume) during fieldwork and firm-level interviews. However, what is clear is that the sector is dominated by a few large farms that exclusively produce high-value outputs such as flowers. Medium-sized firms may produce some types of cut flowers, including ornamental flowers; they may also supply both auction houses and supermarkets, while the largest firms predominantly supply auction houses. Moreover, such firms may export both cut flowers and other types of horticultural produce such as vegetables.

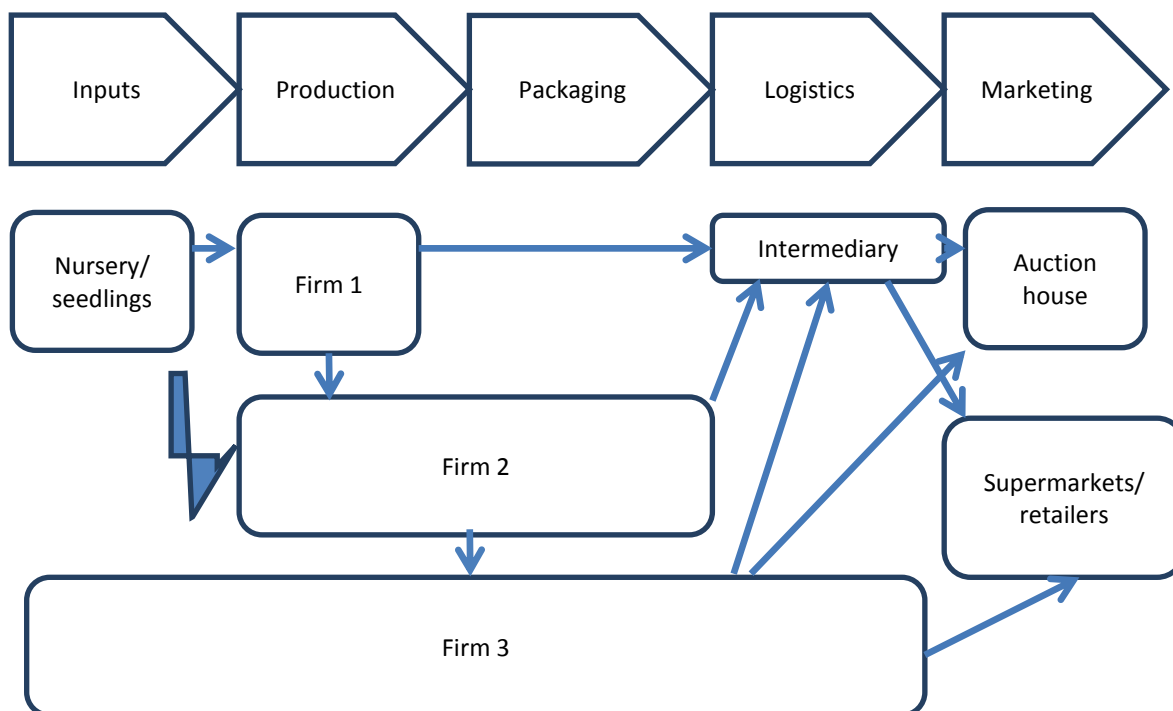
It is estimated that capital investment in flower production requires at least \$50,000 per hectare in addition to access to marketing networks (Bolo, 2008). These requirements have subsequently confined most small-scale growers to summer flowers that can be grown outdoors and which do not require the heavy investments in greenhouses needed for roses, the major flower exported.⁹

⁸ According to estimates by the Kenya Flower Council (KFC).

⁹ The current stock of investment in the horticulture sector is in the region of 650-750 billion Ksh (\$7.3–8.4 billion) according to estimates by the Horticultural Crops Development Authority.

Figure 1 presents a stylised overview of the cut-flower value chain in Kenya. Given some of the similarities that are apparent between how the cut-flower GVC operates and the garment sector in terms of the functions undertaken, we have used a similar overview to that developed by Gereffi and Frederick (2012). This is because, as is the case in the garment GVC, there is a clear division across firms in terms of the functions they undertake and therefore in terms of their functional capabilities. Figure 1 identifies the relative position of the three types of firms identified in the cut-flower GVC and provides an overview of the functions they undertake. Table 3 then discusses these in more detail.

Figure 1: Cut-flower value chain in Kenya



Source: Fieldwork and key informant interviews

Table 3: Functional capabilities of cut-flower firms

Functional capabilities	Description of activities
Firm 1: sub-contractor/assembler Product: foliage/summer flowers/roses Supplier tier: marginal supplier	Small Indian/African firms are integrated into the cut-flower GVC through acting as sub-contractors to larger firms (Type 2) or intermediaries based either in Kenya or overseas markets (predominantly in the Netherlands or UK). This is a form of sub-contracting in which Firm 1 is responsible for the supply of the product up to its final destination (f.o.b.), exporters or Type-2 firms. In general, Firm 1s are relied on to provide products on an as-and-when basis and may have more than one buyer and end market, as shown in Figure 1. In some cases inputs may be supplied by Firm 2s to Firm 1s, depending on the sub-contracts and end product specified.
Firm 2: package contractor/assembler Product: roses and/or foliage/summer flowers Supplier tier: preferred supplier; may sub-contract Firm 2: package	Medium-sized firms tend to rely on their intermediaries based either in Kenya or overseas markets to supply end markets. However, they have greater functional capabilities compared to Firm 1s, both growing and packaging to specification. They may also have their own nurseries and use these to supply other firms with plant varieties. These firms tend to have set annual contracts with their buyers for specific volumes. They may, however, also develop more informal linkages with Type-3 firms and supply on an as-and-when basis; similarly, they may in turn sub-contract Firm 1s so as to fulfil their buyers' requirements. Generally, Firm 2s operate on an f.o.b. basis and are responsible for the supply of the product up to

<p>contractor/assembler</p> <p>Product: roses and or foliage/summer flowers (bouquets)</p> <p>Supplier tier: preferred supplier and may sub-contract; or niche supplier</p>	<p>its final destination. This is where, for the quoted price, goods are delivered on board a ship or to another carrier, via an intermediary, at no cost to the buyer.</p> <p>Firm 2s may be either preferred suppliers to their buyers or they may be niche suppliers. For example, Dutch auction houses typically require a steady supply of high-volume and high-quality roses. In comparison, retailers may require specific products, such as bouquets, that require both roses and summer flowers/foilage. Some firms may supply both markets or specialise in the supply of one rather than the other. These differences are specified in Figure 1.</p>
<p>Firm 3: full-package provider</p> <p>Product: roses</p> <p>Supplier tier: strategic supplier or niche supplier</p>	<p>Large multinational enterprises typically not only have their own nurseries integrated within their supply chains, but they also tend to be vertically integrated, taking care of production, packaging and logistics as c.i.f. suppliers. This means the price invoiced or quoted by Firm 3s includes insurance and all other charges up to the named port of destination or named place (c.i.p.) in the country of destination such as a warehouse.</p> <p>A full-package supplier carries out all the steps involved in production. This includes the selection, purchasing and production of materials; the completion of production; and the delivery of the finished product to the buyer – predominantly Dutch auction houses, but this may also include supermarkets/retailers, as indicated in Figure 1. Firm 3s may sub-contract Firm 2s in order to fulfil their buyers' requirements.</p>

Source: Fieldwork and key-informant interviews

The number of firms in operation has reportedly been stable since around 2006.¹⁰ However, there is some evidence of accumulation processes being under way that are changing the structure of the industry. For example, the smallest firms (Type-1 firms) are increasingly being bought out by medium-sized firms (Type-2 firms) as some consolidation across nodes of production takes place. A number of more medium-sized suppliers have developed new flexible contractual arrangements, including with some of the largest cut-flower farms in Kenya (two of which recently merged).

Because of continued inconclusive negotiations for the EPA with the EU, there are reports of relocation by some of the larger growers (Type-3 firms) to countries such as Ethiopia (which will continue to receive a trade preference in the EU market even if it does not sign and ratify an EPA with the EU, because it is classified as a least-developed country). There may be other reasons, however, related to the competitiveness challenges posed by movements in exchange rates. As previously mentioned, investment by Israeli and Dutch flower growers in the sector was initially attracted to Kenya in the 1990s due to its preferential access to the EU market relative to other countries. The strategy adopted by some Dutch growers to begin production in Ethiopia forms part of a diversification strategy: to increase the number of suppliers and reduce both risks and Kenya's market power. It may also be reflective of increasing competition on profit margins and the need to seek out lowest-cost production locations.

Where large firms have left, other large firms in Kenya have typically taken over, which has meant that production has become increasingly concentrated among the largest and best-connected firms (in relation to end markets).¹¹ These processes to some extent mean that a new period of consolidation in the sector seems to be under way, while at the same time the Kenyan government is becoming more involved in the sector. The following sections describe the response of donors and governments to these shifts in more detail.

¹⁰ This has also been the case with exports of cut flowers, which have recovered since a reduction in demand immediately after the global financial crisis.

¹¹ Historically, the horticultural sector has always been a relatively tightly knit community of a select number of large-scale growers, many with strong contacts in industry in end markets. In terms of the evolution of the industry, a number of the largest firms/farms around Lake Navaisha were previously owned by former Kenyan presidents (Kenyatta and Moi), who took over the most productive land left by colonialists.

3.3 Shifts in donor interventions

The results of firm-level interviews and a review of current major donor activities, notably those undertaken by the Netherlands and UK, respectively, suggest a change in donor interventions in the sector:

- firstly, towards supporting the inclusion of medium-sized enterprises rather than smaller ones (since the lessons from interventions made to date are that these may be more sustainable if targeted at medium-sized enterprises)
- secondly, towards promoting private sector development more broadly
- thirdly, towards addressing more generic measures and non-tariff barriers at borders through adopting a corridor approach and establishing one-stop border posts.

The vacuum left by donors in the provision of support for smaller firms is increasingly being filled by the public sector: the Kenyan government has geared up efforts to ensure the inclusion of smaller producers. However, this process goes beyond simply certifying certification procedures – for which new challenges have been encountered – to include the promotion of cluster development and the better organisation of smaller producers.

3.4 Shifts in governance

There has been an increase in efforts to provide agricultural extension services to different regions across Kenya; this includes the provision of services provided by Kenya's Horticultural Crops Development Authority (HCDA) across all provinces. The HCDA was established in 1967 and grants licences to buyers and sellers of horticultural products. More recently it has begun to provide support to growers and traders so that they do not need to resort to arbitration. It does this through, for example, witnessing contract signing. It therefore tries to foster relationships between small-scale growers and medium-sized firms in terms of adhering to best practice.

Although all buyers and sellers in Kenya must be registered with the HCDA, not all growers are registered with producer organisations such as the KFC or the Fresh Produce and Exporters Association of Kenya. Both organisations are private initiatives designed to increase the lobbying power of the industry and improve coordination among firms in terms of learning about and sharing best practice, including in relation to certification issues. Both are self-regulating bodies.¹² Their members pay fees for industry representation, which includes market access issues.

Government intervention in the sector is likely to increase in the future due to the implementation of the Horticultural Bill, which is considered by most industry representatives to be a long time coming – given the more than 20 years of the industry's development without an explicit policy. As part of this bill, a horticultural development fund will be created. The HCDA will manage part of this fund, in addition to other public and private partners. The objective is to extend the HCDA's coverage so that it has a representative body in each province of Kenya.

The lack of policy on the horticultural sector despite its relative importance in generating employment and foreign exchange is posited as being a result of the hypersensitivity of the industry (which is also very powerful) to government intervention. The increased focus of the government on the horticultural sector has to some extent been driven by external events, which are now also being brought to the fore by firms. These include Kenya's severe current account imbalance; the uncertainty surrounding EPA negotiations with the

¹² The chief executive of the KFC is also the managing director of one of the largest cut-flower firms in Kenya (Findlays).

EU; and the concerns raised by some industry representatives regarding loss of competitiveness, which is particularly notable, given initiatives launched by the Ethiopian government to promote the development of the country's cut-flower sector, including attracting Kenyan investment.

In the absence of an explicit government policy specifically designed for the cut-flower sector, the KFC has developed its own regulations and guidelines for the sector.¹³ The KFC is also an accredited certifier of a number of private voluntary standards. The new policy embodied in the Horticultural Bill is viewed positively by the KFC as providing some leverage in terms of forcing the government to act to better support the sector. There are a total of approximately 120 cut-flower growers in the sector, of which around 70 are members of the KFC. Although the KFC does not represent all registered growers, it accounts for around 60–70% of the volume of exports from the sector. Its members employ 90,000 individuals directly and around 500,000 indirectly in other types of services provision.

The reorganisation of the sector as a result of mergers and acquisitions has led to new concerns being raised by workers, including in relation to increases in workloads without commensurate increases in pay. The Horticultural Bill will include a minimum level for wages in the sector and provide for a wages council to effectively review levels in the sector. The inclusion of this is expected to mitigate claims made against the sector in relation to wage levels, particularly for entry-level workers, which are considered inadequate relative to the cost of living.

Although prompted by structural changes within the sector, the introduction of these new policy measures is also being brought about by changes in governance structures more generally within the current administration. There has been limited capacity to implement trade policy in Kenya effectively during recent years (see Were et al., 2010). The current ongoing governance reforms are two-fold. Firstly, they entail the devolution of power. Secondly, they also mean constitutional reform and the creation of an independent judiciary, etc. This is expected to result in the creation of a much more formidable civil service with the governance capabilities to both design and implement an effective trade strategy. This is particularly important, given ongoing trade policy challenges related to EPA negotiations and more recent upgrading challenges.

3.5 Development of labourers' capabilities

In order to assess the microeconomic benefits for producers and labourers of entry into and participation in the cut-flower GVC, it is necessary to distinguish between direct effects, such as increases in wage-earning opportunities, and indirect effects, which can relate to the knowledge obtained from participating in high-value agriculture that may subsequently be applied elsewhere and shared with others. It is this latter effect that is much more difficult to assess and evaluate, but may still be substantial.

3.5.1 Direct benefits

Table 4 presents the results of key-informant interviews undertaken with production managers and farm workers with regard to relative wages for entry-level positions within the cut-flower GVC for labourers on the field and in the packing house. The names of the firms interviewed have been removed, but types have been assigned to them according to those outlined in Figure 1. The entry-level positions in the cut-flower GVC include the harvesting of cut flowers and their grading. Employers typically require at least Form 4 certification from labourers at this entry level, which is a high-school-leaving certification. However, this requirement is not absolute and often entry can be as a result of a personal recommendation, past experience or through successfully passing a probationary period.

¹³ The KFC was created in 1996.

Generally, entry-level wages for these positions have a similar remuneration across the types of firms interviewed, being in the region of 6,000–13,000 Ksh (\$67–146).¹⁴

Table 4: Relative returns for labourers in Type-2 and -3 firms

Firm type	Size	Average volume of production	Entry-level remuneration
Type 2: 100% Kenyan; supplies intermediary that then supplies Dutch auction houses/UK retailers	120 ha; 600 workers	10,000 stems per day	8,500–13,000 Ksh (\$95–146) per month for harvesters and graders
Type 3: 100% foreign direct investment (FDI); supplying Dutch auction houses	40 ha; 950 employees	N/A	6,000–12,000 Ksh (\$67–135) per month for harvesters and graders
Type 3: 100% FDI, supplying Netherlands auction houses directly	150 ha; 4,500 employees, of which 1,000 seasonal	Approximately 200,000 rose stems per day	6,500–9,300 Ksh (\$73–77) per month for harvesters and graders
Type 3: 100% FDI (Dutch); direct sales with auction house; verbal contracts	450 employees	75 million stems per annum	12,000–15,000 Ksh (\$135–168) per month for harvesters and graders

It is difficult to clearly assess how these wage rates compare to other sources of employment. The last labour force survey in Kenya was undertaken in 1998/1999 as part of the Integrated Labour Force Survey, a nationally representative survey. Although, as discussed by Andalón and Pagés (2008), Kenya has minimum wage legislation in place, it is not enforced: the categories of employment largely correspond to the colonial era and the system has not been substantially updated since then.¹⁵

The minimum wage was increased by 12.5% in 2011 in order to keep pace with soaring fuel and food prices and at that time was estimated to be in the region of 8,364–10,606 Ksh (\$94–\$119) a month (see Ombok, 2011).¹⁶ The range of wages paid for entry-level workers would therefore seem to correspond more or less to other modern sources of formal employment. The extent to which wages in the sector have kept pace with recent food price increases and the cost of living more generally is rather more questionable. However, a lack of information on the cost of living hinders this analysis: the last Living Standards Survey was undertaken in 2005/2006. It has been estimated by workers in the field that approximately 12,500 Ksh (\$140) is required per month to meet the cost of living.

Despite this, the direct benefits of extensions of formal employment opportunities, which also include sickness pay, maternity leave, and in some cases subsidised shelter and subsistence, are irrefutable. It is also notable that entry-level positions such as harvesters and graders are often taken up by both women and men, either straight from graduation from high school or after having obtained other relevant experience. The barriers to entry to such positions would therefore appear to be low.

3.5.2 Indirect benefits

Beyond the direct benefits of formal employment opportunities, other learning-by-doing and spillover effects may result from workers' participation in the cut-flower GVC. Based on the results of firm-level interviews, it would seem that most workers also have their own farms at home (which may be in the vicinity or further afield). The results of focus-group

¹⁴ US dollar equivalents were calculated on 2 July 2013 and rounded.

¹⁵ The minimum wage rate also varies according to the geographical district.

¹⁶ The Central Organisation of Trade Unions, Kenya's main labour-union federation, which has demanded a 60% increase, warned before the increase was announced that it may call a nationwide strike if the minimum wage was not raised by a sufficient margin.

interviews undertaken suggest that the most important transferrable skills are related to pesticide and fertiliser use; the development of social skills related to team work; and all-round administrative skills, including note taking and record keeping.

Generally, cut-flower production is organised through plots of a given number of hectares (± 30 ha); these are then overseen by harvesters (within a range of ± 8 – 11 per ha); a supervisor or production manager; other staff, including sprayers of pesticides; and scouts who identify pests, etc. Supervisors and production managers ensure that activities are undertaken for a fixed production unit; meet contractual demands; and remain within budget in terms of fertilisers, chemicals and the use of labour. Table 5 summarises the skills required/obtained across these positions, based on the results of focus-group interviews.

Table 5: Skills required across employment opportunities in the cut-flower GVC

Type of labourer	Wage	Functions undertaken	Skills required	Skills obtained
Harvester	6,000–12,000 Ksh (\$67–135)	Overseeing production units and ensuring that production meets buyers' specifications	Form 4 certificate or other experience	Health and safety; integrated pest management; pesticide use; other social, organisational skills
Grader	6,000–12,000 Ksh (\$67–135)	Overseeing harvesting of cut flowers, their grading and potentially packaging; ensuring that these meet buyers' specifications	Form 4 certificate or other experience	Health and safety; integrated pest management; pesticide use; other social, organisational skills
Sprayer	12,000+ Ksh (\$135+)	Ensuring that production units are adequately sprayed with pesticide/fertiliser	Technical training on pesticides/chemical use in addition to Form 4 certificate	Health and safety; integrated pest management; pesticide use; other social, organisational skills
Scout	12,000+ Ksh (\$135+)	Ensuring that production units are adequately sprayed/harvested; any emergent pest/disease incidences are addressed	Technical training on pesticides/chemical use in addition to Form 4 certificate	Health and safety; integrated pest management; pesticide use; other social, organisational skills
Supervisor	$\pm 20,000$ Ksh (\$224)	Ensuring that individual production units meet buyers' specifications	Relevant experience, including technical and on-the-job training; Form 4 certificate	Managerial skills
Foreman	35,000–100,000 Ksh (\$393–1,122)	Ensuring that collectively production units meet buyers' specifications		Managerial skills; may have some input regarding contracts
Production manager	Ranges reported: $\pm 35,000$ – $60,000$ Ksh (\$393–673) per month; $200,000$ – $2,000,000$ Ksh (\$2,245–22,447) per month	Ensuring that all production is able to meet buyers' specifications.		Managerial skills with staff internal to the organisation and externally with buyers; may negotiate contracts/enter into verbal contracts

Although access to entry-level positions has been discussed as having relatively low barriers to entry, movement up into managerial roles is more dependent on having the prerequisite qualifications (at least Form 4 school-leaving certification), in addition to relevant on-the-

job training, including in terms of integrated pest management. Entry into all positions would of course be dependent on staff turnover and firm growth. Concerns were raised by some workers regarding inequality across wages and entry into some of the more senior management positions. Often the most senior managers in firms would be foreign and with close links to buyers, e.g. Dutch. In this case it seems that the nationality of the ownership of firms was less important than the nationality of more senior managers and their links with buyers. This was particularly the case where contracts were agreed on a verbal as opposed to on an annual basis.

3.6 Overcoming other upgrading challenges: testing governance structures?

One limitation of interventions in the sector to date is that they have still not adequately addressed asymmetries in the trading relations that exist between producers and buyers within the cut-flower GVC. One example is the fact that the certification processes undertaken by the KFC for quality standards are still not mutually recognised as equivalent to the dominant standard used in auction houses in the Netherlands. This means that producers in Kenya still have to cover the costs of audits undertaken by Dutch certifiers in addition to those undertaken by the KFC. The resultant effect is an increase in costs for exporters, which reduces their relative competitiveness vis-à-vis Dutch producers and can also affect whether producers are certified or not.

A situation could therefore be said to be arising whereby donor efforts to reduce the costs of certification and overcome other non-tariff barriers that prevent traders from accessing markets are being undertaken without due consideration of buyers' actual requirements. These more recent challenges related to the effective participation of producers within GVCs show how these lie outside the direct control of governments.

A question therefore arises as to how the KFC can achieve mutual recognition by Dutch auction houses, which effectively operate as a private members' club. The most that the Kenyan government can do is to try to facilitate this process. This could provide a new role for AfT to assist in creating space for dialogue between producers and buyers, and would also require the creation of more effective public-private dialogue mechanisms.

3.7 Obtaining a more secure supplier position?

The evidence from stakeholder interviews and market-share analysis suggests that only the largest group of firms (Type-3 firms) have managed to move from being solely contractors towards a position of directly supplying buyers and retailers. In both the UK and Dutch markets Kenya has been able to increase its market share for cut flowers. The increase has been much more pronounced in the Dutch market compared to the UK market: Kenyan growers accounted for 47% of supply to the Dutch market in 2010 and 44% in 2011 (the latest year for which data are available), as presented in Table 6. This increase in market share has been accompanied by an increase in unit values, which suggests that over time Kenyan firms may have also been upgrading their position, e.g. selling higher-value products; this has also been accompanied by an increase in market share.

Table 6: Kenya's market share in Dutch and UK cut-flower markets

Year	Netherlands			UK		
	World (\$ '000)	Kenya (\$ '000)	Kenyan share	World (\$ '000)	Kenya (\$ '000)	Kenyan share
2000	424,589	92,541	21.8%	542,297	34,738	6.4%
2001	414,620	98,842	23.8%	592,152	45,997	7.8%
2002	440,177	116,954	26.6%	799,913	53,098	6.6%
2003	477,504	150,643	31.5%	910,105	58,214	6.4%
2004	497,672	178,058	35.8%	978,245	84,433	8.6%
2005	535,558	205,849	38.4%	957,371	94,377	9.9%
2006	590,737	246,812	41.8%	1,004,890	99,621	9.9%
2007	672,374	275,808	41.0%	1,133,862	104,541	9.2%
2008	821,100	337,324	41.1%	1,056,847	132,813	12.6%
2009	711,073	300,933	42.3%	877,690	112,782	12.8%
2010	634,123	295,811	46.6%	935,360	85,985	9.2%
2011	750,498	329,893	44.0%	1,006,189	94,275	9.4%

Source: UN Comtrade database, accessed 4 January 2013

Notes: Data reported by the Netherlands/UK, based on UN Comtrade product code 0603(cut flowers and flower buds).

As Kaplinsky and Readman (2005) and Kaplinsky et al. (2009) point out, the use of unit values and market shares combined provides an indicator of the relative upgrading performance of firms. The logic for this is, as Kaplinsky et al. (2009) discuss, is that firms engaging in successful product innovation, whether minor alterations or more substantial changes in product design and performance, can expect to receive relatively higher prices for their output. However, because higher prices may also reflect inefficiencies in production, suggesting a decline in innovative performance, this suggests that an indicator of cost competitiveness is also needed, and for this reason market shares are used.

Although the combined results of analysis of unit values and market shares may be viewed positively, a note of caution is urged within this discussion, since although some firms may have been able to obtain a more secure supplier position, they have been identified as those belonging to the Type-3 category, as indicated in Figure 1. The ability of *all* firms to therefore obtain a more secure supplier position would therefore appear to be rather limited.

Overall, it could be said that there is some evidence of some Kenyan firms moving towards a position of a full-package supplier (as defined in Figure 1). However, this is not the case for the small and medium-sized firms identified in Figure 1. These are the ones that may also face increased costs in the Dutch market because of the inability of the KFC to obtain mutual recognition of the standards its producers adhere to and those demanded in Dutch auction houses, because they are not directly owned and have rather more indirect relations with buyers in their end markets. This barrier to entry could hinder growth for this category of firms; moreover, it could ensure that the productive structure in Kenya remains relatively polarised between very large growers and small growers, with medium-sized firms either reducing in size or being consolidated into larger firms (although much more evidence is needed to substantiate this hypothesis).

4 Conclusions

This paper has shown how the evolution of the cut-flower GVC has affected producers' participation in and engagement with this type of trade, which operates in terms of a hierarchical structure of governance with highly consolidated marketing and retailing nodes. The paper has argued that some of the more recent challenges for some types of producers require a greater consideration of power asymmetries among firms.

In a globalising world where GVCs are increasingly important, the ability to shift goods in and out is essential to a country's competitiveness, and therefore infrastructure and low tariffs matter. Yet the cut-flower industry also faces a set of non-tariff barriers, such as the need to satisfy stringent private sector standards in Dutch auction houses. We can therefore see a situation arising where donor efforts to reduce the costs of certification and overcome other non-tariff barriers that can prevent traders from accessing external markets are being undertaken without necessarily considering the need also to influence the private relations that exist among firms operating within GVCs. The reasons for this are rather unclear.

A question arises, therefore, as to how the KFC can achieve the mutual recognition of standards by Dutch auction houses (which effectively operate as a private members' club). In effect, these auction houses can set whatever standards they want and so it is up to the KFC to reach an agreement with them. This could provide a new role for AfT. Such an approach might help not only to resolve some of the governance issues that exist between firms and buyers, but also to ensure that such firms are better able to influence the external governance structures within which they trade. Although the Kenyan cut-flower GVC has been in operation for a considerable time, as has been shown in this paper, only some types of firms have been able to obtain a more secure supplier position over time.

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