European Journal of Business and Management
ISSN 2222-1905 (Paper) ISSN 2222-2839 (Online)
Vol.6, No.33, 2014

Codes of Conduct and Marketing Strategies in Kenya's Horticultural Sector

Isaac Maina Kariuki
Department of Agricultural Economics and Business Management, Egerton University, P.O. Box 536-20115 Egerton, Kenya
*Email of corresponding author: waki_gaga@yahoo.de

Abstract
The global demand for product quality and safety in Western European markets has motivated rapid growth of production and marketing codes of conduct between business partners. However, though the Kenya Horticultural Crops Development Authority's code of conduct on contractual guidelines has promoted business to farm business (B2B) relationships between exporters and smallholders, the relationships have received little empirical analysis. This paper uses case analysis based on strategic marketing framework to examine the B2B's purpose, target and competitive, growth, promotion, distribution, and pricing strategies. The analysis reveals that the B2B strategies are based on supply chain governance constructs: written and verbal contracts. The purpose of the contracts is to manage procurement of high quality and safe produce which in itself is contingent on the European Union market served. On targets, written contracts seem efficient with organized producers and verbal contracts with independent producers. As competitive edges, written contracts are orientated toward differentiation strategy and verbal contracts, low-cost strategy. Growth in written contracts is through market penetration and diversification in verbal contracts. However, sharp differences exist on distributional, promotional and pricing strategies.
Keywords: code of conduct, contracts, marketing strategies, horticulture, Kenya

1. Introduction

Since the beginning of the 1990s issues of agricultural sustainability, food safety and quality have dominated global trade in fruits and vegetables. This has been motivated partly by food scares that locked the European market (e.g. Bovine Spongiform Encephalopathy (BSE), Dioxin etc), and the legislations on food safety in the United Kingdom (UK) and France which passed more food safety responsibility to the private sector players (European Commission, 2000). As a result supermarkets established their own codes of conduct, implemented traceability and quality meta-systems (e.g. Hazard Analysis and Critical Control Points (HACCP)) to reassure consumers of the quality and safety of products sourced and distributed through their chains (Henson and Caswell, 1999). The established standards factored on upstream suppliers (i.e. growers, input suppliers etc) through business to business certification schemes (e.g. EurepGAP[1]) focussing more attention on product quality and safety issues by way of applying good agricultural practices, observing employment and corporate social responsibility values (Jaffee and Masakure, 2005). Consequently, code of conducts became an avenue to embrace agricultural sustainability concept (World Commission on Environment and Development (WCED), 1987). Notable for instance is that firms in the industrial and manufacturing sectors are actively involved in codes of conduct (World Bank (2002).

Codes of conduct varies from the protection of the environment, economic issues like employment and fair prices, to socio-cultural factors like gender and sanitation (WCED, 1987). Internationally, there are independent social codes (e.g. Ethical Trading Initiative (ETI)), company codes (International Standards Organization (ISO) 9000) or sectoral codes (e.g. EurepGAP) (Barrientos and Dolan, 2003). Within the framework of these codes of conduct are national ones designed to reflect the social and economic environment of respective trade participants in their own countries. For example, Kenya Flower Council (KFC) has developed a code for cut flower producers and exporters and Fresh Produce Exporters Association of Kenya (FPEAK) has one for fruit and vegetables participants.

Industry wide, Kenya's Horticultural Crops Development Authority (HCDA) developed a code of conduct covering among others good business practices between exporters and suppliers, guidelines for good agricultural practices (e.g. use, application and control of pesticides), and traceability (HCDA, 1995). Under HCDA's code the number of exporters has grown, the volumes and value of exports increased and international market changes have been adopted at the production and marketing level. For instance, studies by Dolan et al., (1999) and Japan

[1] Since 7th September 2007 EurepGAP is now GlobalGAP which reflects its expanding international role in establishing Good Agricultural Practices.

Bank for International Cooperation (JBIC) (2003) indicated between 151 and 200 licensed fresh produce exporters with 50 annual operators and 150 sporadically entering and exiting the industry during the October-April peak season. However, the fresh produce export business is highly concentrated and subsequently supplies from smallholders shrinking. For example, by the end of the 1990s, over 75% of all Kenyan fresh produce exports were being supplied to EU supermarkets by seven top firms and procurement from smallholders had decreased from a high of 18% in 1998 to a low of 11% in 2001 (Dolan and Humphrey, 2000). In terms of national contribution, Central Bureau of Statistics (CBS) (2009) shows that horticulture exports of cut flowers, fruits and vegetables contributed 23% of the total export earnings a sizeable 13% of the agricultural gross domestic product.

Barrientos and Dolan (2003) opine that codes of conduct though based on production and quality management systems aim at enhancing the marketing potential of horticultural exports in the European Union (EU). Therefore, this paper explores how the HCDA-Code of Conduct on contractual guidelines (hereafter referred to as CoC) is implemented between exporters and smallholders' farm businesses in French beans marketing. Recognizing that export marketing requires a contractual farming arrangement; exporters provide the immediate markets and smallholders, farm business suppliers and consequently, a business to business (B2B) exchange is conceptualized. Contracts are either written or verbal depending on the EU market served, size, and objective of exporters and smallholders. Using the CoC, clues for the purpose, targeted suppliers and derived competitive, growth, promotion, distribution and pricing strategies for each contractual regime are highlighted. The purpose of contracting, competitive and growth strategies may be founded on the global demand for quality and safe agricultural products in developed countries. The major motivators are the need for consistent, reliable and consumer-driven products and the changing regulatory and marketing environments in established and emerging markets (Jaffee, 2003). Therefore contracting smallholders may be a priori to ease access to quality and safe supplies to meet demand in Western European markets. On competitive strategies, an exporter seeks to position own business in the ever changing marketing environment dictated by consumers' tastes and preferences (Burton et al., 2001). Due to evolving regulations on trade and commerce, an exporter might grow by venturing into new market niches or deepen their product offers to existing consumers. Promotion strategies emanate from the representation of an exporter and the relationship with smallholders in relation to product exchange at the farm level. Procurement of French beans requires elaborate arrangements to ensure reliability of supplies throughout the season and to avoid produce diversion to part time exporters who seek to fill-in orders (Dolan and Humphrey, 2000). Since supplies come from numerous smallholders, product identification and the need to share information on prices, markets, new methods of farming, and food safety and quality standards is critical to check on product quality and safety violations. Therefore, distribution strategies arise because French beans are perishable in nature, require early harvesting and subsequently quick transport of post-harvest to export exit points in Nairobi which is 120kms away from the study region, Mwea Tebere. Additionally, scattered small farms over a wide growing area and small outputs from individual smallholders make produce assembly essential (Neven and Reardon, 2004). Finally, pricing defines the expected profitability of engaging in the contractual farming arrangement subject to output restrictions (Eaton and Shepherd, 2001). The price offered communicates the value placed on farm produce and the competitiveness of an exporter. Economically, it may reflect the extent of buyer or seller power in marketing. Nevertheless, the farm level price may be tempered by locality differences (e.g. good roads), an exporter's target market in the EU and the promotion strategies utilized.

2. The conditioning regulatory environment and HCDA's code of conduct

The HCDA code of conduct is established under the Export Order of 1995 (HCDA, 1995). The code was designed at a time when the EU, the principle market for Kenyan horticulture was experiencing regulatory and market changes. For instance,, the EU directive on pesticide residues, food hygiene and harmonized framework on pesticides and the UK Food Safety Act became pertinent issues in the production, handling and distribution of all exports destined for the EU in the early 1990s (Jaffee and Masakure, 2005). The latter years of 1990 were marked by EU wide monitoring program on Maximum Pesticide Residual Levels (EU-MRL) and the formation of private food quality schemes (e.g. British Retailers Consortium Standard, EurepGAP, Ethical Trading Initiative etc), which would later become key quality and safety standards in the Kenyan market (*ibid*). Later, the gradual dominance of supermarkets in the EU and decline of wholesale markets as key importers of horticultural exports from Kenya and development of supermarkets' product labels increased (Dolan and Humphrey, 2000). Additionally, competition on prices started dwindling in favour of competition based on quality (Jaffee, 2003).

The Export Order of 1995 defines the CoC is an agreement between the "buyer" of fresh horticultural produce and the "seller" or grower of the produce. Buyers are either exporters and/or processors of fresh horticultural produce and sellers, either individual growers, or schemes which have been developed to benefit groups of small landholders in the horticultural production business. The main aims and objectives of the CoC include 1) to act

as a memorandum of understanding between the buyer and the seller of fresh horticultural produce, 2) to serve as a guideline for the buyer and the seller in order to conduct good business practices which will be mutually beneficial and help promote the well being of the horticultural industry in Kenya, and 3) to act as a guideline or framework for development of a legally binding contract to be executed by the buyer and the seller. We premise that a contract (3rd object) is more pertinent in consolidating buyer-seller's level of understanding (2nd object) and good business practices, mutual benefit and success of the horticultural industry in Kenya (3rd object). By emphasizing on use of contracts when procuring horticultural produce from smallholdings, the CoC seeks to draw from the benefits of: a) reduced transaction costs of not renegotiating contracts with specific exporters every end of season, b) access to stable and reliable supplies, and c) favourable environment for information sharing on prices, market demand and new methods of farming. Since the fruits and vegetables' value chain focuses on quality, hygiene and safety, contracts ensure institutionalization of on-farm training and monitoring frameworks on such matters. This is plausible because smallholders' basic knowledge on and interpretation of codified information on product quality, hygiene and safety is limited and uncertain. Contracts also mitigate the hold-up problem associated with specific assets like packing houses and cooling plants for exporters, and grading sheds for organized groups.

2.1 **Salient elements of the CoC**

Initially, farmers should be organized into well managed groups through registration with the relevant government Ministry. Organized producers benefit exporters with economies of scale in terms of total farm size which is critical in implementing integrated crop and pest management, quality management systems, certification and traceability (Okello and Swinton, 2007). There is also ease in the provision of reasonable extension services at reduced costs per farmer which minimizes monitoring and administrative costs. Additionally, organized producers have the potential for efficient market access through reduced costs of crop assembly, information sharing and product grading (Narrod et al., 2009).

Secondly, smallholders need to be trained on safe and effective use of pesticides to acquire requisite competence to farm high quality, hygienic and safe produce. This is based on the official EU standards relating to fixing of maximum levels for pesticide residues in and on fruit and vegetables (Commission of European Communities, 2000). Training smallholders on reduction of use of banned or restricted and increased use of classified pesticides and observation of pre-harvest spraying intervals is critical in minimizing pesticide residues in farm produce. Additionally, training on personal hygiene and safe disposal of pesticides materials reduces possible microbiological contamination of post-harvest produce and environmental conservation of soils and water ways. Crop and environmental protection, and personal hygiene are mandatory critical control points in the certification process to KenyaGAP/GlobalGAP standard (Graffham et al., 2007).

Thirdly, smallholders should have proper record keeping which is founded on the need for traceability contained in European Communities regulation 178/2002 (Commission of European Communities, 2002). Traceability is an indispensable part of any market for process credence attributes or content attributes that are difficult or costly to measure (Golan *et al.,* 2004). Essentially, producers are required to ensure that all farming activities directed toward the production of the marketed produce from land preparation to post harvest are documented. This includes among others type of pesticides, time of use, number of times sprayed, time crop was planted, type of seeds used, source of seeds, fertilizers and pesticides. Traceability improves supply management, and facilitates trace-back for purposes of food safety and quality by minimizing the production and distribution of unsafe or poor quality products and consequently minimizing the potential for bad publicity, liability and recalls (Golan *et al.,* 2004). For instance, there may be self-testing or official testing for pesticide residues in government laboratories to identify and ascertain produce's compliance with set residue levels.

3. The analytical approach

In the analytical process, we focus on the CoC as the basis for co-opting smallholders in strategic business partnerships with exporters through establishment of farm-level B2B supply management. The purpose is to map the possible contribution in the success of the Kenyan horticulture industry. The paper uses a case analysis approach as explained in Eisenhardt (1989) and Yin (2004) to ask how the salient features of the CoC are manifested at the farm level. Further, as in Ingenbleek and Meulenberg (2006) strategic marketing concepts are used to carry out a case examination of exporters' strategies when procuring supplies from smallholders with respect to the purpose of relational contracting, target market, competitive, growth, promotion, distribution and pricing strategies.

3.1 **Focus of Analysis**

The CoC specifies requirements that should be met by the buyer, the seller and jointly. Following the CoC's

preamble, exporters and outgrower groups should engage in the execution of a contract before conducting business (HCDA, 1995). We focus on a contract as the basis of exporter-farmer B2B supply management framework. Here, we relax the preamble to accommodate market dynamics by suggesting that farm level B2B relations between exporters and smallholders might be conducted with outgrower groups or independent producers under a written or verbal contract. A written contract is identified through a signed document. Because of export market complexities (e.g. market knowledge, coded product quality information etc) exporters are assumed to choose the governance structure and the smallholders to engage. Further, the CoC stipulates that a contract must include specific terms and conditions of payment, responsibilities for production, handling and collection of produce, and any other essential elements which will create a clear understanding of the obligations of both the buyer and the seller (see table 1). This study considers the specific terms and conditions as foundation for exporters' strategies. For instance a contract's condition of payment is viewed as a pricing strategy and handling and collection of produce a distribution strategy. Consequently, the features used in exporters-smallholders B2B relations might help to deduce exporters' purpose, target market, competitive, growth, promotion, distribution and pricing strategies.

Using the abridged contract guidelines in table 1, we define the purpose, target market, competitive, growth, promotion, distribution and pricing strategies. The table shows that there is emphasis on quality and quantity, record keeping, support and training, good agricultural practices, produce rejection, contract duration and payment mechanism etc.

Table 1: Selected HCDA Code of Conduct's Contract Guidelines

Contract feature	Description of requirements
Quality and quantity	Package weight, prices, minimum collectable quantity, quality levels based on Kenya Bureau of Standards (KBS), National Research Institute (NRI) manual and specific importers etc
Inputs	Supply of certified seeds, fertilizers/pesticides, conditions for purchase/sale of inputs
Generally accepted production principles	Use /application of approved pesticides and recommended fertilizers per manufacturers' label, random produce testing for pesticides
Record keeping	Seed/herbicide/pesticides (used, treatments, date, rates) weather (irrigation dates, quantities): harvesting (dates)
Support and training	Group administration, production, handling, grading, collaboration with Ministry of Agriculture (MOA)
Harvesting	Use of clean containers, protection of produce from heat and direct sunlight, maintenance of hygienic conditions
Grading	Inspection and grading of produce, when, where documentation of collection/delivery, when title of goods change
Packaging	Supply of packaging materials, acceptable conditions of the package on collection, condition and quantity of produce, grade and type of produce, placement and orientation within a container
Collection	Time and year, conditions for non-collection, purchase of produce within specified time, 24hrs produce retention after specified time at buyer's expense, tolerance of +/- 10% due to shortages and excesses.
Middlemen	No transactions with middlemen/intermediaries involving produce on contract
Multiple contracts	No multiple contracts with same seller, multiple contracts allowed if there are no unscrupulous business practices
Rejected produce	Point of rejection, conditions for the return of rejected produce, means of disposal, accepted deliveries not returnable
Payment mechanism	Acceptable payment terms, mechanism of safe and timely transfer of funds
Penalties	Compensation for failure to abide with the laid down regulations of the contract
Contract duration	Duration and maturity of contract
Contract termination	Written notice, reasonable period-full production or marketing cycle of produce

NB: A complete version of the HCDA-CoC is available at www.hcda.or.ke.
Source: Horticultural Crops Development Authority, 2014

On contracts, producers may not use middlemen and buyers have to give a written notice on the intent to terminate a contract. This suggests preference for direct linkage to markets and use of enforceable written contracts. The stipulated features in the CoC are used in addition to the features that are essential in creating clear understanding of the obligations of participants. The latter include seller obligations like the ability to use, apply and control pesticides, competence in record keeping and organized production. Further, buyer obligations

might include provision of extension services, packaging materials, inspection and grading, and quality of produce. Jointly, sellers and buyers have the obligation to implement a trace-back system. We recognize that, these being guidelines only, exporters might have variations in the stipulated and essential features at the farm level. For example, one exporter might engage independent producers, another producer groups and another both. Therefore, the focus is on the type of contract used and the attendant and dominant contractual features.

3.2 **Case analysis framework**

The case analysis borrows from Porter (1980), Ansoff (1984), Andreasen and Kotler (2003) and Armstrong (2006). According to Porter (1980) a competitive firm may pursue low-cost, differentiation or segmentation strategy. Ansoff (1984) identifies market penetration, product development, market development and diversification as typical growth strategies for firms. Additionally, Andreasen and Kotler (2003) argue that firms design missions, goals and competitive strategies based on their target markets, competitive position, growth and marketing mix elements. Further, Armstrong (2006) contends that a strength, weakness, opportunity and threats (SWOT) analysis provides a framework for identifying competitive and growth opportunities. These concepts might be more profound in B2B relationships between exporters and smallholders for two reasons. One, the EU markets, Jaffee (2003) posits require exporters to have closer links with importers, supermarkets or wholesalers, investments in food and information technology and reliable suppliers from the farm level. Two, Burton et al., (2001) contend that consumer tastes and preferences drive EU markets dynamism with quality and safety attributes dominating demand. Consequently therefore, the export market, competitiveness (ability to invest and use technology) and source of supplies could potentially dictate an exporter's mission and goals. This suggests that given the same environment large exporters with high capital base might have a different mission and goals compared to small exporters with low capital base and hence follow different strategies. Likewise, an exporter serving high care market chains (e.g. supermarkets) would follow a different distribution strategy compared with exporters targeting low value markets (e.g. wholesale). Additionally, an exporter of high care products might pursue an aggressive product differentiation due to high demand and profitability compared to an exporter of low value products where differentiation may be less profitable.

Following Ansoff (1984) and Andreasen and Kotler (2003) frameworks, it is argued that the purpose, target market, competitive, growth, promotion, distribution and pricing strategies pursued by an exporter replicate at the smallholders' farm level when choosing why and how to coordinate and govern B2B relationships. This means that an exporter's size and the targeted EU outlet (i.e. supermarket or wholesale) determines the mode of supply governance adopted at the farm level and subsequently, the competitive, growth, promotion, distribution, and pricing strategies used. Therefore, given buyer power, an exporter chooses producers to contract (independent/organized/both), the contractual type (verbal/written/both) and determines specific features to guide strategies (e.g. the price and timing, payment mode and timing, product quality and safety measures, produce assembly and grading, packaging and produce identification etc). For example, as in Porter (1980) exporters competing as low-cost marketers could use verbal contracts and spot cash pricing to procure from independent producers to reduce excessive hold-up hazards. On the other hand, exporters competing through differentiation might use written contracts and forward pricing to procure from organized producers despite the high opportunity costs. Consequently, each exporter pursues a unique portfolio of strategies.

However, the uniqueness of the portfolio of strategies may be influenced by what Eaton and Shepherd, (2001) refer to as farmers' and exporters' critical considerations that could be used to forge strategic or tactical pillars for an export company when contracting. Further, predicated on the critical considerations in Eaton and Shepherd (2001), strength, weakness, opportunity and threats (SWOT) analysis (Armstrong, 2006) is used to reveal strategic expectations. We first consider farming experience, farm size, fertility of farms and community considerations (Eaton and Shepherd, 2001). Farming experience connotes production expertise and reduced monitoring costs meaning that exporters would more likely absorb high opportunity cost in written contracts by engaging experienced farmers. The farm size reflects high outputs, potential for increased production capacity and economies of scale when implementing costly quality and safety standards like KenyaGAP/GlobalGAP. Therefore, exporters would risk hold-up problems in written contracts by transacting with large farmers. Fertile farms could potentially reduce use of high levels of fertilizers and pesticides and hence cost of production. In addition, as community considerations organized producers enhance collective regulation, critical supply markets and management of pooled land resources into one single unit. Consolidation reduces monitoring costs, and eases administration of production credit, inputs and crop assembly. Jointly, fertile farms and community organizations might endear use of a written contract as cost reduction and efficient management centres respectively.

Further, consider an exporter's resources, relationship intensity, supply reliability demands, quality and payment

incentives, level of control required and capital specificity (Eaton and Shepherd, 2001). Exporters with a stable capital base might adopt the more risky written contracts by designing incentive-specific features. A highly intensive relationship with smallholders signifies mutual sharing of hold-up problems in written contracts. Additionally, where demand for supply reliability is high, a mechanism that locks partners into an annual or multi-seasonal relationship could more likely exist under a written contract. Further, given quality incentives (e.g. use and control of farm inputs), monitoring detailed requirements might be more manageable under a written contract. Finally, payment incentives and the level of relation-specific capital indicate need for a governance mechanism that minimizes shared risks. For instance, co-ownership of produce sorting and packing sheds guards investments against being rendered un-operational by locking competitors out. On payment incentives, clearly specified terms under a written contract could opt smallholders as residual claimants of the exported produce price.

4. Study area, data sources and description

The primary data come from a 2006 survey of 249 French beans smallholders of Mwea Tebere. Farmers were randomly selected from a collection of 36 villages based on a beans crop on the farm. Using a short structured questionnaire farmers were interviewed on type of contracts used and marketing practices. French beans are produced mainly for export which attracts export market actors and a sizeable participation by local supermarkets (Weatherspoon and Reardon, 2003). Producer groups are common in the study area especially due to mandatory quality management systems required for KenyaGAP/GlobalGAP certification (Graffham et al., 2007; Kariuki et al., 2012). Most EU retailers ascribe to GlobalGAP. Independent producers exist due to demand for off-peak supplies or as suppliers to less strict quality standard markets (Ouma, 2010). There are supportive horticultural infrastructure for all year-round production and marketing such as Embu-Nairobi highway leading to JKIA, irrigation waters from rivers Nyamindi and Thiba and National Irrigation Board's water canals, horticultural handling facilities and informal market reciprocity contracts (Obare and Kariuki, 2003). Secondary data has been obtained from internet resources of HCDA, KFC, FPEAK, Liaison Committee on Europe Africa Caribbean and Pacific countries (COLEACP), GlobalGAP and export firms.

The abridged CoC in table 1 has been used to match the survey findings. When disaggregated by exporters, farm organization and exporter affiliations in table 2, essential characteristics of the whole sample can be observed.

Table 2: Distribution of producers by farm organization, chain governance and affiliation

	Farm organization		Chain governance		Chain affiliation	
Buyer	Independent producers	Group producers	Verbal agreement	Written agreement	FPEAK	COLEACP
1	4	0	4	0	Y	Y
2	1	0	0	1	Y	Y
3	9	0	9	0	N	N
4	4	0	4	0	Y	N
5	6	0	6	0	Y	Y
6	79	0	78	1	Y	N
7	14	29	39	4	Y	Y
8	7	1	7	1	Y	Y
9	1	60	1	60	Y	N
10	24	10	22	12	Y	Y
Total	149	100	170	79		

NB: N==No, Y==Yes
Source: Mwea Tebere French beans survey, April-June 2006

The data has 10 exporters procuring smallholders' supplies, 100 smallholders are in organized producer groups and 149 are independent producers. One hundred and seventy farmers use verbal contracts and 79, written contracts. The data has one exporter using written contracts, four using verbal contracts and five using both contracts to transact with farmers. On source of supplies, 6 exporters use independent producers and 4 exporters use both independent and organized producers. Of the ten exporters 9 are FPEAK members, 6 are COLEACP members and one has neither membership. There is indication that verbal contracts dominate exporter-smallholders business relations in horticultural trade and use of written contracts is limited. The reasonable use of both contracts could be explained by duality of strict and less strict quality outlets in Western European markets. The data also suggests that procuring from independent producers is the key entry point in beans marketing. However, with demand for farm reorganizations to mitigate product quality, hygiene and safety concerns in Western European markets, supplies from organized producers are increasingly gaining importance

(Waweru, 2006). Membership to umbrella and supportive organizations seems critical in export marketing perhaps for bargaining and advocacy reasons.

5. Results and discussions

The results of the case analysis are presented in table 3. The first column of the table shows the derived purpose, target market, competitive, growth, promotion, distribution and pricing strategies conditional on written and verbal contracts. The rows define the dominant feature differentiating written and verbal contracts and identifying the strategies in the case analysis. The results are presented based on the dominant feature within the contracts.

Table 3: Case analysis results

Strategic strata	Written contract	Verbal contract
Purpose of contract	Govern supplies, improve quality and safety of export beans.	Govern supplies, improve quality and safety of export beans.
Target	Organized producers (89.87), Independent producers (10.13)	Independent producers (82.94), Organized producers (17.06)
Competitive strategy	Differentiation and segmentation: sourcing from organized and independent producers using written and verbal contracts	Differentiation, segmentation and low-cost: sourcing from independent producers only using verbal and written contracts.
Growth strategy	Market penetration: full training on GAPP: use and application of pesticides, hygiene, post harvest care and book keeping	Diversification: considerable training on GAPP: use and application of pesticides (80), hygiene (81.76), post harvest care (28.24) and book keeping (41.76)
Distribution strategy	Crate, grading by harvesters, grading on designated site, crop collected off-farm (96.2), collection by buyer's agent, crop title change next market day (73.42), crop rejected next market day (86.08), crop rejection reason given (92.41), no compensation	Crate, grading by harvesters (78.82), grading on designated site (93.53), crop collected off-farm (56.47), collection by buyer's agent (95.29), crop title change on market day (54.71), crop rejected next market day (61.18), crop rejection reason given (86.47), no compensation
Promotion strategy	Farm code (39.24), group name (89.87), grade, date (79.75), farmer name, extension, direct linkage (81.01), consistent engagement	Farm code (35.29), no group name (82.94), grade, date (61.18), farmer name (76.47), no extension (64.12), intermediary linkage (61.18), consistent engagement (55.88)
Pricing strategy	Sales receipt, variable price, payment by buyer's agent, lagged payments, price buyer-given, price communicated to individual farmer, price communicated by buyer's agent (60.76), Pricing timing at planting (82.28), Payment violations (68.35)	No sales receipt (67.06), variable price (87.06), payment by buyer's agent, lagged (52.35), price buyer-given, price communicated to individual farmer, price communicated by buyer's agent (80), pricing timing at harvesting (86.47), Payment violations (85.29)

NB: The figures in () are % of producers accessing that CoC requirement. Lack of % means that all the producers have access to that requirement
Source: Mwea Tebere French beans survey, April-June 2006

5.1 **Purpose**

The contracts aim to facilitate the flow of quality, hygienic and safe supplies of French beans from smallholders to the export markets. Additionally, the contracts aim to strengthen trade exchanges between exporters and smallholders in export marketing.

5.2 **Target**

Buyers either emphasize on procuring from organized smallholders or independent producers. About ninety percent of smallholders in organized groups use written contracts. Written contracts are targeted at organized producers. These contracts seek to tap the economies of scale in administration and enforcement costs that are possible through organized production. For instance, per unit administrative and managerial costs of implementing ICPM, and traceability could be low in organized groups than for individual producers. This is likely because organized producers may effectively enforce an exporter's regulations through group norms and values thus reducing costs of monitoring production and quality violations. This suggests that written contracts differentiate organized from independent producers in a homogeneous market. Written contracts might also

mean need for high quality, safe, reliable and consistent supplies throughout the year.

Buyers using verbal contracts procure from approximately 83% of independent smallholders in the sample. Verbal contracts target independent producers as key suppliers. An important characteristic of independent producers is that they are numerous and widely dispersed in the growing region. Therefore, verbal contracts seem to capitalize on the homogeneity of French beans and grade and hence the contractual enforcement problems in such a market. Further, verbal contracts net a wider supplies base and benefits of the dynamics of market supply and demand. It may be inferred that verbal contracts mainly target producers who are not in organized groups either due to choice, government bureaucracy or lack of critical mass. Another possibility is that verbally engaged producers are suppliers of export markets that are not strict on productivist methods (e.g. traceability), or markets that serve short term on-season orders.

5.3 **Competitive strategies**

Buyers pursue cost leadership and segmentation, and differentiation and segmentation to compete in the market. Exporters 7, 8, 9 and 10 compete through cost leadership and segmentation by procuring beans from organized and independent producers using written and verbal contracts respectively or both (see table 2). Using written contracts with organized producers provides high volume of controlled, consistent and reliable supplies at reduced per unit costs. Additionally, they are more likely to farm quality, hygienic and safe produce and observe uniform grading, handling and traceability demanded in the respective EU consumer markets. In donor supported development programs, organized groups are key compliance organizations for international standards (e.g. GlobalGAP, ETI etc) for smallholders (Natural Resources Institute, 2003; Narrod et al. 2009). Conversely, procuring from independent producers using verbal contracts allows buyers to benefit from the forces of market supply and demand that might generate quasi-rents. For instance, they could be used to fill-in orders when supply from organized producers is insufficient to meet demand. This competitive strategy may be construed to balance the procurement base for targeted consumer markets to diversify market risks. This could be achieved as shown in Jaffee (2003) and Ouma (2010) by segregating produce to supply a given market segment e.g. produce from organized producers could be sold to high quality discerning markets and that from independent producers diverted to less quality discerning markets. Exporters 1, 2, 3, 4, 5, and 6 pursue differentiation and segmentation. In effect, they specialize by procuring supplies from independent producers using verbal and written contracts. This strategy endows exporters with guided marketing focus whether serving high care category supermarket consumers or less strict wholesale markets. This could potentially consolidate and sustain uniform suppliers.

5.4 **Growth strategies**

The findings show that growth is either through market penetration or diversification. Procurement from smallholders using written contracts depict a market penetration strategy where exporters specialize on smallholders with full training on the generally accepted production practices (GAPP). The main purpose is to sustain and expand access into high end Western European consumer markets. GAPPs (i.e. crop and personal hygiene, post-harvest crop care and record keeping) qualify compliance with product quality and safety standards through control and minimization of health risks associated with pesticides residues and microbiological contaminations of marketed produce. It may be imputed that producers trained on GAPP gain competences on welfare issues, environmental conservation, product hygiene and safety which are marketing qualities in Western European markets.

On the contrary, 80% and approximately 82% of smallholders using verbal contracts have training on use of pesticides and hygiene respectively but fewer have training on post-harvest crop care and record keeping. This shows considerable demand for crop and personal hygiene practices by exporters that might be serving markets that are strict and less strict on GAPP regulations such as Western European retailers and local supermarkets respectively. Therefore, growth seems to be through diversification. Despite low investments on GAPP, there is indication that independent smallholders could still access the EU market through exporters targeting dual markets. Arguably, verbal contracts are the most likely export market entry point for new entrants, part time or marginalized smallholders with small farm sizes and low investment capabilities. However, despite independent smallholders' potential for continued participation in export markets, the increased harmonization of standards by EU buyers might render their market access unsustainable.

5.5 **Promotion strategies**

The results from the case analysis show buyers use varied promotion strategies notably linkage to market, provision of extension services and frequency of trade during the season. Eighty one per cent of smallholders using written contracts are directly linked to markets by buyer as outlined in the CoC. Conversely, 61.2% of smallholders in verbal contracts are linked to markets through intermediaries. On one hand, direct linkage offers

an exporter the opportunity to closely interact with suppliers which builds trust and mutual dependence as in personal selling. On the other hand, linkage through intermediaries typifies the problem of organizing numerous small farmers into an orderly marketing system where product, input and credit market failures persist. This could be viewed as a weak case of franchising. In weak market structures, the role of intermediaries is critical especially if they have competitive advantage in assembling produce and transportation (Gabre-Madhin, 2001).

Another promotional tool is provision of extension services. All smallholders using written contracts receive extension visits during the production season but 64% of smallholders using verbal contracts do not receive extension. This suggests that in written contracts exporters endear themselves to smallholders by providing technical, material or informational assistance and monitoring crop production akin to customer relations services. Low extension services in verbal contracts are not unlikely since servicing numerous independent producers generates enormous training, administrative and monitoring costs.

The frequency of trading with smallholders during the season is another promotion strategy. In written contracts, all smallholders have consistent trade exchanges meaning that exporters and producers have a full time repeated and all season contact. This might be predicated on exporters' need for consistency and reliability of supplies while asserting credibility and reputation. Fifty six per cent of smallholders using verbal contracts have consistent trade exchanges. The fact that verbal contracts operate much in the open market system where trade exchanges are weak could explain why some smallholders have intermittent contact. The result is that buyers/suppliers are predisposed to hazards of shifting suppliers/buyers depending on demand and supply in a given region.

5.6 **Distribution strategies**

Exporters have varied distributional tactics: crop assembly, grading, crop title, quality check and traceability. More than 96% of smallholders using written contracts use a designated grading shed to assemble beans compared to 56.5% of those using verbal contracts. As a distribution tactic this resembles a mono-distribution channel in written contracts and a multiple distribution channel in verbal contracts given that about 43.5% of smallholders use farm level grading sheds. Centralized crop assembly reduces per unit transportation costs and standardizes grades while decentralizing assembly diversifies quality risks. Further, buyers' agents handle produce from all smallholders in written contracts while buyers' agents handle produce from 96% of those in verbal contracts. This finding shows that crop assembly is mainly the responsibility of intermediaries.

On grading, all produce from smallholders using written contracts is graded by harvesters at a designated grading shed. In verbal contracts, approximately 79% and 94% of smallholders use the services of harvesters and grade at a designated shed respectively. Use of harvesters and a designated shed are strategic options. In written contracts where differentiation seems to be the key competitive strategy, strict use of harvesters to grade at a designated shed ensures uniformity of grades and minimizes quality and safety failures because of supervised post-farm produce hygiene. If low cost strategy is pursued minimal use of on-farm sheds and considerable use of company employees during grading are dominant.

Another distribution tactic is the timing of the change of crop title. Crop title for more than 72% of smallholders using written contracts changes the following market day. Conversely, crop title changes on the market day for more than 54% of smallholders using verbal contracts. There is indication of pronounced tactical delay of product acceptance in written contracts possibly to hedge on quality and safety measures in the marketing channel. In verbal contracts there is a near balance of immediate ownership and tactical delay perhaps as a mechanism to spread marketing risks.

On quality checks, over 86% of smallholders using written contracts have crop rejects reported the following market day and more than 92% received reasons for crop rejection. Approximately 61% of smallholders in verbal contracts have crop rejects reported the following market day and slightly more than 86% know reasons for crop rejection. The findings suggest more secondary grading of beans to achieve desired quality for export markets for those in written than verbal contracts. However, opportunistic disposal of unsold beans from previous deliveries cannot be overruled for transparency behind rejection returns lacks since farmers are not represented during secondary sorting in Nairobi. The findings also show that information for rejections is widely available suggesting that disclosure of reasons for crop rejection might be intended to minimize channel conflict. Arguably, buyers do not insure producers against distribution inefficiencies on their part.

Produce traceback system is another distribution strategy which includes packaging and identification of grades, producer/group and farm. In both contracts, plastic crates are the standard package for transporting beans from

the farm to Nairobi for processing, cutting, freezing, pre-packaging or canning ready for export. A crate's distributional advantages include ample space to pack beans, possibility of stacking during transportation and transparency of the grade, color and freshness of beans. Crates also reduce chances of unfair marketing practices such as over-packing of beans at the farm level aimed at getting extra beans during repackaging in Nairobi. On identification, all smallholders using written contracts strictly use own name and grade but only grades are identifiable among all smallholders using verbal contracts. Not surprising, about 90% of smallholders in written contracts use producer group's name and 80% also use the produce collection date compared to 77% using own name and 61% using produce collection date for those in verbal contracts. Farm identification in both contracts is low. If interpreted as branding, smallholders using written contracts are more differentiated and traceable. In both contracts, there is indication that exporters implement a least cost traceability system.

5.7 **Pricing strategies**

The pricing strategy consists of price formation, communication and timing, payment mode, receipting and compensation. Irrespective of contractual arrangement, prices are buyer given, buyers' agents pay for deliveries and prices are communicated to individual farmers. This has several implications. As price takers smallholders wield no bargaining power. Communicating price to individual farmers widens price differentials among farmers either in a given producer group, among those selling to the same buyer or those supplying the same grade. On use of agents to pay farmers exposure to unfair pricing practices such as falsified low prices increases. Collectively, this pricing approach might be intentionally strategic to reduce transaction costs and generate quasi-rents.

Uniquely, prices given to all smallholders using written contracts vary during the season, payments are lagged and crop deliveries are receipted. This suggests that prices are based on market demand and supply, buyers spread price risks through residual claimancy and receipting solidifies future exchanges (see Hueth, 1999 for examples). Though not conclusive, written contracts seem to be hinged on differentiation. Conversely, price offers in verbal contracts vary for 87%, payments are lagged for 52.4% and sales receipts are not issued for 67.1% of smallholders respectively. This depicts pricing diversity perhaps to reduce procurement costs by exploiting market supply and demand dynamics and less paper work. The overall finding seems to suggest dominance of low cost strategy in verbal contracts.

On timing of price announcement, 82% of smallholders in written contracts know expected prices during planting while more than 87% in verbal contracts know prices during harvesting. Further, agents communicate prices for more than 60% of smallholders in written contracts compared to 80% in verbal contracts. Buyers using written contracts seem to specialize in forward pricing perhaps to spur production but use spot cash pricing in verbal contracts possibly to exploit market supply and demand. Agency is more pronounced in verbal contracts.

Violation of payments and lack of a compensation scheme are the other pricing strategies. More than 68% of smallholders in written contracts and slightly above 85% in verbal contracts report violation of payments and there is no compensation scheme for all smallholders in both contracts if buyers fail to honour price arrangements. The possible explanation to widespread payment violation might be the strict communication of prices to individual farmers and substantial control of payments by exporters' agents which hinder cooperative bargaining on payment complaints. These constraints expose smallholders to exploitation. Another reason could be that exporters renege on agreed payments to adjust their prices to reflect prevailing market conditions such as fluctuated export prices, demand and competition at the farm level.

6. Summary and conclusions

This paper uses strategic management approach to examine how B2B relationships between exporters and smallholders shape the purpose, target market, distribution, promotion, pricing, competitive and growth strategies when procuring smallholders' horticultural supplies. A case analysis based on written and verbal contracts is presented using data from a survey of 249 French beans producers.

The case analysis indicates that the use of written or verbal contracts is mainly to procure high quality and safe produce from smallholders. Written contracts target organized producers and verbal contracts, independent producers. Differentiation, segmentation and low-cost strategies are the main competitive edges used by exporters in which written and verbal contracts are independently or jointly used to capture organized and independent producers. Exporters using written contracts are market penetrators emphasizing growth into Western European markets through complete training on GAPP. Those using verbal contracts are diversification strategists requiring reasonable but not strict training on GAPP. In both contracts, plastic crates packaging is the only common distribution strategy. Surprisingly, both contracts uniquely lack a compensation scheme. On

promotion strategy farm produce for those in written contracts is completely identifiable by grade and producer's name, farmers access extension services and business exchanges are consistent. The grade is the only complete identification feature in verbal contracts. The pricing strategy in both contracts is common in that price is buyer-given, communicated to individual farmers and payments are made by buyers' agents. While prices vary, payments are lagged and supplies are receipted in written contracts, a portfolio of prices, payments and receipting regimes is maintained in verbal contracts.

The case findings imply that with the increased awareness of food quality and safety by EU consumers and regulations on traceability of farm produce use of written or verbal contracts in B2B relations with smallholders is justifiable. This will co-opt smallholders as individual producers or collective marketing institutions (e.g. farmer groups/ associations/ cooperatives etc) to mitigate product quality and distribution failure. Further, given the duality of export markets in terms of strict and less strict demand for GAPP, market opportunities for produce from smallholders exist. Additionally, to sustain market access, quality and safety requirements and profitability more emphasis on distribution, promotion and pricing strategies is needed.

Acknowledgements
The survey was funded by German Academic Exchange Service (DAAD) and facilitated by Egerton University (Kenya) and Kiel University (Germany).

References
Andreasen, A. R. & Kotler, P. (2003), "Strategic marketing for non-profit organizations", Upper Saddle River, NJ: Prentice Hall.
Ansoff, H. I. (1984), "Implanting Strategic Management", London: Prentice Hall.
Armstrong, M. (2006), "A handbook of Human Resource Management Practice", London: Kogan Page.
Barrientos, S. & Dolan, C. (2003), "A gendered value chain approach to codes of conduct in African Horticulture", *World Development,* 31(9), 1511-1526.
Central Bureau of Statistics. (2009), "Economic Survey", Ministry of Planning and National Development. Nairobi, Kenya.
Burton, M., Rigby, D., Young, T. & James, S. (2001), "Consumer attitudes to genetically modified organisms in food in the UK", *European Review of Agricultural Economics*, 28(4), 479–498.
Commission of European Communities. (2000), "Commission Directive 2000/42/EC of 22 June 2000 on the fixing of maximum levels of pesticide residue in and on cereals, foodstuffs of animal origin and certain products of plant origin, including fruits and vegetables respectively", *Official Journal of the European Union*, 158.
Commission of European Communities. (2002), "Regulation EC No. 178/2002 of the European Parliament and of the Council of the 28th January 2002 laying down the general principles and requirements of food law, establishing the European Food Safety Authority and laying down procedures in matters of food safety", *Official Journal of the European Union*, 31.
Dolan, C. & Humphrey, J. (2000), "Governance and Trade in Fresh Vegetables: The impact of UK supermarkets on the African Horticulture Industry", *Journal of Development Studies,* 37(2), 147-176.
Dolan, C., Humphrey, J. & Harris-Pascal, C. (1999), "Horticultural commodity chains: The impact of the UK market on the African Fresh Vegetable Industry", IDS Working Paper No. 96. Institute for Development Studies. Sussex, UK.
Eaton, C. & Shepherd, A. (2001), "Contract Farming: Partnerships for growth", Food and Agriculture Organization of the United Nations, Rome.
Eisenhardt, K. M. (1989), "Building theories from case study research", *Academy of Management Review*, 10, 803-813.
European Commission. (2000), "White Paper on Food Safety", Brussels: European Commission
Gabre-Madhin, E. (2001), "The role of intermediaries in enhancing market efficiency in the Ethiopian grain market", *Agricultural Economics*, 25, 311-320.
Golan, E., Krissoff, B., Kuchler, F., Calvin, L., Nelson, K. & Price, P. (2004), "Traceability in the U.S. food supply: economic theory and industry studies", Agricultural economic report no. 830, United States Department of Agriculture, Economic Research Service.
Henson, S. & Caswell, J. (1999), "Food safety regulation: an overview of contemporary issues", *Food Policy*, 24, 589-603.
Graffham, A., Karehu, E. & MacGregor, J. (2007), "Impact of EUREPGAP on access to EU retail markets by small-scale growers of fruits and vegetables in Kenya", *Fresh Insights* no. 6. Horticultural Crops Development Authority. (1995), "Code of Conduct. Appendix 3: Legal Notice No. 231 (EXPORT) Order 1995", Available at http://www.hcda.or.ke
Hueth, B. (1999), "Incentive Instruments in Fruit and Vegetable Contracts: Input Control, Monitoring,

Measuring and Price Risk", *Review of Agricultural Economics*, 21(2), 374-390.
Ingenbleek, P. & Meulenberg, M. T. G. (2006), "The battle between "good" and "better": A strategic Marketing Perspective on codes of conduct for sustainable agriculture", *Agribusiness*, 22(4), 451-473.
Jaffee, S. (2003), "From challenge to opportunity: transforming Kenyan fresh vegetable trade in the context of emerging food safety and other standards", Agricultural and Rural Development Working Paper 2, The World Bank, Washington, DC.
Jaffee, S. & Masakure, O. (2005), "Strategic use of private standards to enhance international competitiveness: Vegetable exports from Kenya and elsewhere", *Food Policy*, 30, 316-333.
Japan Bank for International Cooperation. (2003), "A survey of horticultural produce handling facilities project in Kenya", Available at www.jbic.go.jp
Kariuki, I. M., Loy, J-P. & Herzfeld, T. (2012), **"**Farmgate private standards and price premium: Evidence from the GlobalGAP scheme in Kenya's French beans marketing", *Agribusiness*, Volume 28(1), 42-53.
Narrod, C., Roy, D., Okello, J., Avendaño, B., Rich, K. & Thorat, A. (2009), "Public-private partnerships and collective action in high value fruit and vegetable supply chains", *Food Policy*, 34, 8-15.
Natural Resources Institute. (2003), "Focus on horticulture: Exacting standards. In: the New Agriculturalist", Natural Resources Institute. Kent, UK.
Neven, D. & Reardon, T. (2004), "The rise of Kenyan supermarkets and the evolution of their horticulture product procurement systems", *Development Policy Review*, 22(6), 669-699.
Obare, G. A. & Kariuki, I. M. (2003), "Production and productivity effects of informal contract farming in Kenya's smallholder horticultural sub-sector", *Eastern African Journal of Rural Development,* 19(1), 13-24.
Okello, J. J. & Swinton, M. S. (2007), "Compliance with international food safety standards in Kenya's Green bean industry: Comparison of a small- and a large-scale farm producing for export", *Review of Agricultural Economics*, 29(2), 269-285.
Ouma, S. (2010), "Global standards, local realities: Private agrifood governance and the restructuring of the Kenyan horticulture industry", *Economic Geography*, 86(2), 197-222.
Porter, M. E. (1980), "Competitive strategy: Techniques for analyzing industries and competitors", New York: The Free Press.
Waweru, A. (2006), "Testing a generic quality management system for smallholder farmers in Kenya", Available at http://www2.globalgap.org/pcspecials.html
Weatherspoon, D. D. & Reardon, T. (2003), "The rise of supermarkets in Africa: Implications for agrifood systems and the rural poor", *Development Policy Review* 21, 333–55.
World Bank. (2002), "World development report 2003: Sustainable development in a dynamic world", Washington, DC:
World Commission on Environment and Development. (1987), "Our Common Future", Oxford: Oxford University Press.
Yin, R. K. (2004), "Case study research: Design and Methods", Thousand Oaks, CA: Sage

Dr. Isaac Maina Kariuki, born in Mwea Tebere, Kirinyaga, Kenya in 1971 holds a Bachelor of Agribusiness Management degree (1995, Egerton University, Egerton, Kenya), Certificate in Food, Agricultural and Environmental Policy (2003, The Royal Veterinary and Agricultural University, Copenhagen, Denmark), MSc in Agricultural Economics (2004, Egerton University, Egerton, Kenya), and PhD in Agricultural Economics (2012, Christian-Albrechts-University of Kiel, Kiel, Germany). The main research interests include supply chain governance, market analysis, price discovery and economics of smallholding farm business.

The IISTE is a pioneer in the Open-Access hosting service and academic event management. The aim of the firm is Accelerating Global Knowledge Sharing.

More information about the firm can be found on the homepage:
http://www.iiste.org

CALL FOR JOURNAL PAPERS

There are more than 30 peer-reviewed academic journals hosted under the hosting platform.

Prospective authors of journals can find the submission instruction on the following page: http://www.iiste.org/journals/ All the journals articles are available online to the readers all over the world without financial, legal, or technical barriers other than those inseparable from gaining access to the internet itself. Paper version of the journals is also available upon request of readers and authors.

MORE RESOURCES

Book publication information: http://www.iiste.org/book/

IISTE Knowledge Sharing Partners

EBSCO, Index Copernicus, Ulrich's Periodicals Directory, JournalTOCS, PKP Open Archives Harvester, Bielefeld Academic Search Engine, Elektronische Zeitschriftenbibliothek EZB, Open J-Gate, OCLC WorldCat, Universe Digtial Library , NewJour, Google Scholar