South Africa's Agricultural Commodity Markets

Understanding the rules of the game in five commodity markets with the intention of creating opportunities for emerging farmers

Executive summary

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The national imperative of agrarian reform, as is intended in South Africa, has multiple aims but commodity markets - that is the nexus of transactions, institutions, people and actions that link the production and consumption of agricultural goods - are central to these aims and agrarian reform will not succeed unless better access to commodity markets is ensured for emerging farmers.

Of the R 1,198 billion[1] worth of agricultural turnover passing through markets in the 2001/2002 financial year, less than 0.7% was generated by black farmers. Emerging black farmers urgently require greater and more sustainable access to commodity markets in order to sell the goods they produce and convert their surpluses into capital that can be used to stimulate production. Market access will not, however, automatically alleviate the poverty of poor, rural producers. Increasing market access for agricultural producers in developing countries over the past 15 years has tended to result in food price decreases and enhanced the welfare of consumers rather than producers (DfID, 2003). In some instances market access has proven damaging to the livelihoods of the poor.

Empirical experiences have forced a review of the neo-classical understanding, which depicted markets as an abstraction; the aggregation of arms-length transactions between large numbers of atomistic, consenting transacting parties at an exogenously determined price that benefited both parties mutually. Relative bargaining power, politics, contingency options and differences in the quality of the transacted product played no role in the final agreement. The neo-classical understanding underpinned the notion of markets' ability to allocate opportunities to the poor and led to the indiscriminate advance of markets in attempts to alleviate poverty.

New understandings emphasise the fact that markets, in the neo-classical sense, always fail FOOTNOTE and that when they do the distribution of benefits in market transactions is determined by the "rules of the game": that is the institutional, social, political, historical, geographical, gender and legal dynamics governing market access and the sustainability of that access.

South Africa's Agricultural Marketing Act (1996) dismantled the existing State-managed marketing infrastructure that had linked co-operatives, agri-processors, marketing boards and marketing agents within the exclusively white "Organised Agricultural" network. The new Act and the ensuing deregulation of agricultural marketing was intended to promote free and open agricultural commodity markets and facilitate access for new black producers. The new marketing environment is more competitive and has promoted efficiency, it has also reduced the commercial agriculture burden on the fiscus (Poonyth *et al*, 2001), but the percentage of food income accruing to farmers over the same period has fallen dramatically as food is increasingly processed, packaged, stored, advertised and transported (Clay, 2004). Currently agriculture provides 3% of the country's R1.3 trillion Gross Domestic Product.

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[1] "American" billion = $1*10^9$

The vegetable market: The vegetable market is unregulated and technically open to all producers. The fluid and uncertain nature of the market has led retailers to enter contracts with large growers at the beginning of the season so as to ensure a specific range of vegetables in accordance with predetermined schedules. These arrangements have seen a declining role for municipal markets and make it difficult for small, new producers to gain access to the major supermarkets. In spite of these arrangements, opportunities for the supply of small quantities of produce to a range of outlets do exist. SPAR, Lombardi Foods, the traders at municipal markets, restaurants, corner shops and hawkers all procure some of their goods opportunistically on an informal spot-market basis from small scale producers. The key in accessing these opportunities is to win the trust of purchasers by demonstrating the ability to produce quality vegetables consistently and to deliver them on time.

Emerging producers are also well placed to supply the burgeoning informal settlement food market, where onions, cabbages, potatoes and squash are a staple and real incomes are increasing.

Organic certification provides a means by which emerging producers can distinguish themselves from the mainstream and reduce the competition for their produce.

The preferential access to water afforded to new producers under the National Water Resource Strategy (2003), National Water Act (1998) provides emerging farmers that have representation on the Catchment Management Agencies with a powerful bargaining chip in collaborations with existing commercial vegetable farmers seeking additional water resources.

Wine market: The wine industry has experienced a period of growth following 1994, particularly in the export market, which doubled between 1997 and 2002 (SAWIS 2003). Since 1992 producer income has bucked the commodity market trend and outstripped production costs.

The wine market is highly regulated and dominated by capital intensive estates and cellars. In theory it is possible for emerging growers to cultivate high quality grapes on small tracts of land and deliver these to co-operative cellars. In practice resource poor producers struggle to muster the ZAR 75,000 hectare (excluding land) required to establish vineyards and find it difficult to penetrate the affluent and culturally tight-knit wine marketing networks.

The combination of black economic empowerment labels, political pressure, more effective deployment of the South African Wine Industry Trust (SAWIT) and Wine of South Africa (WoSA) funds and opportunities in labelling, transport, contract vineyard maintenance and other support industries provide a means by which emerging producers are able to gain a share of the ZAR 14.6 billion a year that constitutes the national industry.

New developments in the marketing of "fairtrade" wine from South Africa enhance the potential for collaboration between aspiring and incumbent wine producers. Driving these opportunities is the political pressure on an industry that has large investments sunk in fixed capital and has conspicuously little to show in the way of meaningful racial transformation. In spite of this pressure and associated vulnerability, joint ventures in the industry will not automatically or necessarily prove equitable. Rather the vulnerability of heavily-invested, conspicuously affluent and white incumbents provides aspiring market entrants with the potential to secure more equitable portion of benefits in such partnerships.

Critical to any emerging farmer initiative – whether a joint venture or individual enterprise – is the selection of the correct cultivar. The markets for Pinotage and Columbar, for example, are saturated while demand for good quality Merlot, Cabernet Sauvignon and Shiraz is under-supplied. The grape prices for these cultivars reflect their relative supply and demand.

Rooibos tea market: Rooibos is endemic to the West Coast of South Africa and as such producers in this region are exclusively able to supply the rapidly expanding national and international health tea market. The volumes of rooibos tea produced in South Africa have increased 400% since 1998 and now exceed 500 tons per year.

Production and processing of rooibos tea is not expensive but the establishment of a reputable label and international marketing outlets requires 5 years of time and is both difficult and expensive.

Currently seven South African companies have incurred the expense associated with developing processing facilities, branding labels and nurturing market connections. Having made this investment these companies are now actively trying to procure throughput so as to capture market share and cover their overheads. The scramble for product places producers in a relatively strong position and has allowed them to sell their tea. The relative supply shortages have seen the price of dry tea increase from R 2.50/ kg to R 15.00/ kg since 1997. Additional market premia and access is provided for producers of certified organic tea and producers of "green" rooibos tea.

The Fairtrade Foundation (and Transfair in the USA) has, for the past 18 months, procured rooibos tea from South Africa. Fairtrade certification has proven a successful means of adding value to emerging farmer rooibos harvests and should be pursued via the Fairtrade Labelling Organisation in Bonn.

Sheep and goat market: Opportunities in the sheep and goat markets are of a similar nature. Both markets are currently well placed to increase their national and international share. Typically emerging producers sell their produce to speculators who overcome the transport barrier and courier produce to the major cities. Returns per livestock unit via this marketing channel are, on average, less than those received via formal co-operative abattoirs especially when the value of hides and tripe is imputed. There are, however, legitimate cultural, quality related and practical reasons why emerging farmers choose the speculator market for their produce.

In spite of the effectiveness of the emerging farmer-speculator relationship in providing an outlet, emerging stock producers remain price receivers and an over-reliance on speculators renders them vulnerable to downward price pressure. Collective bargaining, increased mobility via contracted or hired transport and the credible threat of marketing produce via a competitor could enhance the bargaining power of emerging stock farmers and result in higher prices.

International demand for Northern Cape sheep meat and goat meat in general, in conjunction with increased requirements to account for health and hygiene measures (especially from the export market) has required co-operative abattoirs to invest in additional infrastructure. As with tea exporters, the onus is on these abattoirs to cover their investment by out-competing neighbouring abattoirs and procuring additional throughput. The oligopolistic competition between co-operative abattoirs conveys some bargaining power to producers. Emerging producers – where they are able to confront the cultural barriers – are particularly well placed, given that co-operative abattoirs are under pressure to demonstrate their commitment to black economic empowerment. There is a role for negotiating agents to exert this pressure constructively, to confront the mis-trust on both sides of the transaction and to ensure due prices are paid. The success of these efforts is enhanced where emerging farmers have established bargaining collectives.

The precedent set by the wool-growers' initiative in the Eastern Cape is illustrative of what can be achieved when market leaders, acting out of enlightened self-interest and in concert with supporting agencies and government, seek to include emerging farmers in the formal supply chain.

Summary: The challenge, as identified by this study, is not for emerging farmers to distance themselves from existing commodity markets, or establish parallel markets – although the credible threat of acting in this way might be important. Rather the challenge for emerging producers is to equip themselves with the requisite capacity to deploy the bargaining power at their disposal so as to secure their rightful share of South Africa's existing commodity markets and to contribute to the competitiveness of South Africa's rural industries. Understanding and emphasising the attributes that impart bargaining power within a given situation is essential to this process.

Broadly there is scope for action at three levels:

1. The international trade regime still imposes a huge cost on the livelihoods of poor South Africans. Globally, liberalising trade in agricultural markets has more potential to alleviate poverty than liberalisation in any other sector. In order to lobby effectively on international trade platforms, South African delegates need to be aware of the impact of their trade policy; the onus is on emerging farmer groups to articulate this impact and bring it to the attention of politicians.

2. At the national level, efforts launched by the Department of Trade and Industry and the Department of Agriculture to tackle food monopsonies, market exclusion and infrastructural impediments to markets need to be strengthened. The increasingly powerful role of supermarkets is cause for particular concern. Whilst lower food prices contain advantages for all consumers, procuring this food should be conducted in a manner that promotes and does not impede access for small-scale producers. Similarly, action is required to bring the agricultural institutions that are financed from the fiscus – cooperatives, DoA extension and veterinary services, SAWIT, WoSA, DTI - and private marketing companies created on the back of State financed marketing boards such as Rooibos PTY Ltd, to account in terms of what they are doing to promote the national imperative of better market access for emerging farmers.

3. At the local level it is important that efforts to settle emerging farmers on land take cognisance of market opportunities as a point of departure in their planning exercises. The goal of market access should always be concomitant with efforts to ensure that emerging farmers benefit from accessing markets. There a number of things that emerging farmers and their support agencies can do to improve the bargaining position. Collective action, the development of alternative outlets, political negotiations, the Fairtrade Foundation, better information, identifying and exploiting weaknesses in the value-chain, capitalising on black economic empowerment sentiment and legislation and collective transport solutions provide means by which market access could be promoted and sustained.

The over-arching implication for SPP-like institutions is that the market place – and the marketing of agricultural produce – should not be out of bounds for rights-based, activist NGOs aiming to assist emerging black farmers. On the contrary, there is an explicit need to develop an understanding of the market and bring value-based negotiation, lobbying, institution building, support and information dissemination into market transactions.