Global Donor Platform
for Rural Development

# Platform Policy Brief

No. 2 | October 2008

Platform Policy Briefs are designed to inform and guide members in the delivery of assistance in agriculture and rural development.

They should be seen in conjunction with the Joint Donor Concept on Rural Development [www.donorplatform.org/content/view/104/149/].

## The Future of Smallholder Agriculture


## SUMMARY

The majority of the world's poor live in rural areas. So, developing the small farms on which many of them live not only contributes to overall growth and development, but also improves the welfare of many of the poor. In the early stages of development, small farms are often more efficient than large farms. Smallholder development also promises to be more equitable, and to generate greater local multipliers. Plus, since females tend to be disproportionately engaged in small-scale farming, it can help to correct gender imbalances. As the green revolution in Asia showed, the potential of smallholder development can be realised. But conditions have changed. Now smallholders face higher transaction costs and have to cope with the fact that agricultural research is biased towards large-scale production. This raises new challenges in small farm development. On the other hand, higher prices of staple foods present opportunities for farmers.

### Political economy

Although much of the policy is well understood, making the case for donor funding for smallholders is a major challenge. Subsidies are a case in point: they can be justified if 'smart' and limited in duration, but they can be costly and difficult to remove. Increasing democracy, greater scope for participation in policy debates and increasing decentralisation leads to more support for small farms. However, the links are far from automatic. Forums that encourage government, private enterprise, farmer representatives and civil society to discuss issues need to be strengthened further.

### Aid instruments

Policy for smallholders is as much about facilitation, co-ordination and flexibility as it is about programming spending on public goods. Currently favoured instruments for delivering aid (general budget support or sector-wide programmes) need to recognise this and provide the resources, forums and time necessary. Most importantly, we must pay more attention to learning from experience and building programmes incrementally, rather than trying to produce a complete blueprint at the outset.


### POLICY RECOMMENDATIONS:

**'Stepping up'**

- **Get the basics in place:** Ensure a stable macro-economy; provide public goods like rural roads, rural education and health care, agricultural research and extension; and develop rural financial systems and 'good rural governance';
- Encourage smallholders to **focus on demand and improve marketing systems;**
- **Generate institutional innovation** in providing **inputs and services.**

**'Stepping out'**

- Encourage the **rural non-farm economy,** including investment in public goods such as roads, power supplies, telecommunications, improved rural financial systems and education;
- Facilitate **migration.**

**'Hanging in'**

- Provide **technical advice;**
- Set up systems for **payments for environmental services;**
- Introduce and strengthen **risk mitigation and** social protection.

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# BACKGROUND

## The case for small farms

Most farms in the developing world are small, especially in the majority of African and Asian countries, where 75% or more of farms measure two hectares or less (Nagayets, 2005). Small farms are home to two-thirds of the three billion people living in the rural areas of developing countries. Since the poor are concentrated in rural areas, it is not surprising that half of the world's under-nourished and most of those in absolute poverty live on small farms (Hunger Task Force, 2003; IFAD, 2001). Developing small farms not only contributes to overall growth and development, but also directly improves the welfare of the poor.
As the green revolution in Asia showed, this twin potential can be realised. Yet governments and donors are sometimes sceptical about small-scale farming since in the OECD countries small farms are now relatively unimportant. Agricultural growth, however, is almost always a necessary step to overall development[1]. In the early stages of development, small farms may be as or more efficient than larger holdings, while providing jobs and livelihoods for many of the rural poor and creating broad-based growth.

The idea of small farms being efficient may surprise those who expect economies of scale in production. But, as Table 1 shows, smallholdings have important advantages over large farms when it comes to operations on the farm – particularly with regard to supervising labour. Large farms, on the other hand, have advantages when it comes to dealing with agents off the farm – in selling produce, and obtaining credit, inputs and information, etc.

## Changes & challenges

Smallholder development has in the past fulfilled its promise[2]. But despite this positive past experience, some observers (Maxwell, 2003; Ellis, 2005) worry that change has dimmed the prospects for smallholder development. Africa today, comments Ellis, is not like Asia in the 1960s at the start of the green revolution.

Changed thinking on policy that stresses the prime role of the private sector in production precludes the sort of wide-ranging government intervention in markets that characterised most Asian green revolutions. This leaves smallholders facing higher transaction costs in markets.

In particular, supply chains are increasingly being organised by supermarkets, especially in middle income and rapidly growing economies. Their demands for quality, uniformity, timely delivery and, above all, for certification and traceability, threaten to exclude small farmers – leaving them to sell their produce, effectively at a discount, in secondary channels with no premium[3].

In addition, an increasing share of agricultural research is carried out by private concerns, which may bias innovations to the needs of larger scale, fully commercial farmers rather than to those of semi-subsistence smallholders. Innovations in production may be more demanding of capital and education than before, putting smallholders at a disadvantage.

Smallholder development today may thus be more challenging than in the recent past. However, new opportunities have arisen as well.

The rise in food prices in 2007/08 (the largest increase seen in more than 30 years) may

### Table 1. Transaction-cost advantages of small and large farms

| Small farms | Large farms |
|---|---|
| Supervision of household labour | Managing skilled labour |
| | Knowledge of markets, techniques |
| Knowledge of conditions on the farm | Purchasing inputs |
| | Obtaining finance |
| | Selling produce |
| Self-provisioning with food from the farm | Registering land |
| | Assuring traceability and quality of produce |
| | Managing risks |

[1] World Bank, 2008.

[2] As seen, for example, in the late 19th century with cocoa farmers in Ghana, in the 1960s with Kenyan coffee and tea growers, and in the 1970s with Thai farmers producing rice, cassava, kenaf, sugar cane and maize, with Costa Rican coffee farmers, and with Indian rice farmers.

[3] Much depends on whether supermarkets can obtain supplies from large farmers in bulk. If they can, they probably will. Otherwise, they may have to deal with smallholders, and indeed help them meet standards. If the foods in question have 'credence' attributes that cannot be determined by inspecting the produce, such as the use of pesticides or child labour, then certification costs for many small farms can be prohibitive.
The rate of expansion of supermarkets is, however, uneven. When incomes and urbanisation are rising rapidly – as, for example, in East Asia – supermarkets multiply. But such conditions are precisely those under which smallholders who cannot meet the produce standards have the opportunity to work in non-farm jobs. So supermarkets may be less of a threat to livelihoods than thought. (See Reardon & Berdegué, 2002; Traill, 2006.)

not last, but world prices of staple foods may still be expected to be 20–40% higher in real terms than they were in 2005. The higher prices should present farmers with more incentives to produce. The higher prices expected for fertiliser and fuels will offset this, but may give a boost to techniques such as conservation farming that economise on fossil fuel inputs. Governments, alarmed by the price spike, can be expected to give renewed attention to agriculture, in an attempt to increase national self-sufficiency in staples, and to build up stocks.

All of this is potentially good news for smallholders, although in some cases they may be threatened by unscrupulous land grabbing by large-scale investors. This said, however, the entry of more private capital into agriculture could still be to the advantage of smallholders, if corporations seeking extra supplies enter into contracts with smallholders and provide inputs in advance.

# POLICY

## Three options for small-scale farmers

Smallholders are a diverse group. Even when land tenure is relatively equitable, substantial differences in access to land, capital and equipment can arise amongst smallholders and according to gender. At one end of the spectrum are households, typically with two to four hectares of land, able to produce their own staple food and to regularly market a surplus. For these producers, farming offers possibilities for escaping poverty. At the other end of the spectrum, however, are households that have half a hectare or less, produce only part of their household food needs, and can rarely sell more than trivial amounts of produce. They usually depend on off-farm income to survive.

Three options for smallholders thus present themselves (Dorward et al., 2005):

- **'Stepping up'** – investing in farming to raise productivity and output;
- **'Stepping out'** – spending more time on non-farm activities, including migration. In time the farm land may be sold or let out, or may become a part-time or weekend farm; and,
- **'Hanging in'** – remaining on the land and producing staple foods to meet part of household needs, but depending on other activities as well[4].

These categories are not exclusive: some households will be able to follow mixed strategies, with different members engaged in farming, off-farm enterprises and migration.

### Stepping up

For those stepping up, three sets of policies are indicated, as follows:

**1.** Get the basics in place: ensure a stable macro-economy; provide public goods gender-consciously (rural roads, rural education and health care, and agricultural research and extension); and develop rural financial systems that offer not just credit but also ways of saving, insuring and transmitting money. These basic needs are well known. Less appreciated is what might be termed 'good rural governance' which is gender-responsive and is ensuring the rule of law in the countryside, and supporting forums and upholding mechanisms for resolving disputes, especially over land (which may be more important than formal titling). Also included in this list should be making public interventions in food and credit markets as transparent and predictable as possible to reduce uncertainty.

**2.** Encourage smallholders to focus on demand and improve marketing systems: This may involve upgrading transport infrastructure and systems, providing credit to traders and processors, and forming farmer associations for bulk marketing. Producer organisations may also serve to procure inputs, to arrange credit, and to represent farmer interests to policy-makers. In a world where governments provide less direct support to farmers, such intermediaries can be critical in helping smallholders deal with markets. In the past, however, such associations have fallen prey to political appropriation and mismanagement. To avoid this, their capacity needs to be developed, and their scope needs careful consideration[5].

Large swings in market prices, between seasons and years, may be problematic. Variation can be reduced by improving private marketing systems through, for example, providing incentives to invest in storage.

**3.** Institutional innovation in providing inputs and services: Recent experience shows only too clearly that markets for inputs, credit and technical advice – however liberalised – often fail in rural areas. Behind these problems lies a lack of information and assurance on the intentions and character of different parties in the supply chain. The dangers of opportunism, especially when some know more than others or have more market power, are considerable.

Institutional innovations (such as contract farming, certification, group lending, and building producer organisations) are needed to overcome these failures. But who will take the

[4] These three categories correspond broadly to the 'rural worlds' (RW ) typology adopted by the OECD Povnet. Those households 'stepping up' form part of RW 2 (traditional agricultural households and enterprises); those 'stepping out' come from RW 3 and RW 4 (subsistence agricultural households and micro-enterprises, and landless rural households and micro-enterprises); and those 'hanging in' belong to RW 5 (chronically poor rural households, many of which are nolonger economically active). How many are in the different categories? The answer varies by circumstances, above all by the degree of market access and the natural resources available. Surveys from Eastern and Southern Africa, for example, show that no more than the upper 25% of rural households have more than the 2 hectares of land that can be considered the minimum needed for specialised farming (Jayne et al., 2001).

[5] Such key issues include whether the organisation seeks vertical integration by taking on supply chain functions (such as transport to market, storage, processing, input supply, etc.) or whether the aim is horizontal co-ordination of farmers and joint negotiation with other intermediaries involved in the provision of inputs, finance, transport and marketing. Size matters: farmer organisations can fail if they become too large with too diverse a membership, if they pursue too many objectives, and if activities become so complicated that members can no longer exercise effective control over leaders and paid employees. What works will vary by context and over time as experience and capacity is built.

initiative? Private actors have the incentives and in some cases will find solutions. In other cases mutual uncertainty and lack of trust stymies initiative, so the state needs to act æ by providing guarantees and assurances. Given that problems are usually specific to the context, finding solutions means tailoring principles to particular circumstances in a learning process.

Yet state agencies may be unfamiliar with this role, ill-equipped to perform it, or lacking in the incentives needed to encourage them to do so. Greater engagement of public agencies with private companies, non-governmental organisations, and farmer associations can facilitate the search for solutions, create incentives, and indeed foster public accountability.

### Stepping out

For those stepping out, policies to encourage the rural non-farm economy or facilitate migration are priorities. Some of the key policies for the former are the same as those needed for smallholder development – namely, investment in roads, power supplies, telecommunications, improved rural financial systems, education, etc.

Moreover, given the importance of multipliers from agricultural development to the non-farm economy (largely through consumption as farmers spend their increased incomes) agricultural development may be necessary for success in the non-farm economy. Thus, the ability to 'step out' or 'hang in' may depend in part on the ability of others to 'step up'. Governments are not keen on facilitating migration, fearing that metropolitan centres will receive more migrants than there are jobs or be unable to provide services for them. But migration can be a vital source of remittances for rural areas. Important destinations can include secondary cities and market centres that are often growing faster than major cities. Providing would-be migrants with information, protecting their rights as citizens when they reach their destinations, and improving systems to send home remittances can all help to ensure that migration is a positive experience. Stimulating the growth of small farms (see Platform Policy Brief no. 1) can help provide attractive destinations for migrants, closer to their origins than distant cities.

### Hanging in

For those hanging-in, provision of technical advice on ways of growing more food crops with technology appropriate to resource-poor households is critical. An example is conservation farming that can economise on the amount of inputs used, minimise the need for draught power, and reduce crop losses caused by dry spells. A future possibility may be payments for environmental services, including carbon sequestration, within some farming systems.

In addition, households 'hanging in' are usually highly vulnerable to all manner of hazards – from drought to illness to accidents. They need policies to underwrite their livelihoods and prevent destitution through social protection and risk mitigation.

## Gender dimensions

What about the particular needs of female smallholders? In many cases, women are de facto the main managers of the farm, especially for food crops. The right and ability to access, own and control productive resources is critical for them. The following three points are particularly important.

- Access and ownership rights to land: While women often manage and work the land, the rights to it may actually be invested in a male head of household. When he dies, widows and other female dependants may be deprived of land because it passes to a male relative. The issue has become all the more pertinent in Eastern and Southern Africa as HIV/AIDS leads to the deaths of male heads of household in middle age.
- Saving labour: Women typically have to shoulder the bulk of household maintenance and child care in addition to their work in the fields. Innovations and facilities that save time and raise productivity are thus a high priority. Some may well be off-farm: saving time in collecting water and fuelwood are valuable examples, given how long these tasks can take. In the fields, labour-saving innovations are also important. Female farmers often adopt parts of technical packages that require little extra work, such as seed and fertiliser, but reject those requiring more labour, such as intensive weeding.
- Access to credit and technical information: Female farmers usually have little or no access to credit or technical information. Yet, women are often reported to be better re-payers of loans in micro-finance schemes. Gender-conscious extension services with gender-specific approaches and more female extension workers do redress some disparities.

## The political economy

Much of the policy agenda is well known, yet the priorities reflected in public spending can be very different. Finding ways to make the case for agriculture and smallholders remains a challenge [6].

Subsidies on credit and inputs, and prices supported above market levels, are sensitive points. Subsidies can allow smallholders to experiment and learn the use of new inputs, to obtain credit, and to redistribute income to a rural population that is usually poorer than the urban. But they can have high opportunity costs. Indian subsidies on fertiliser, electricity and irrigation have risen to cost 15% of all public spending – more than is spent on education (Mullen et al., 2005) [7].

Moreover, subsidies typically benefit large-scale farmers more than smallholders, since the former use more inputs and sell more produce. Once in place, subsidies often become bellwethers of political intentions and are difficult to remove. Where there are compelling reasons to subsidise, 'smart' subsidies that closely target the poor, that are time-bound, and that do not prevent the development of markets, should be the preferred option.

Meanwhile, we are now seeing trends towards greater democracy, more scope for participation in policy debates and increasing decentralisation. These may lead to policies that support small farms, but the links are far from automatic. Indeed, these trends could increase the incentives for populist measures that distribute, rather than invest, public resources.

Some advances have been seen when forums involving government, private enterprise and farmer representatives have been set up to discuss issues. In Tanzania, for example, a national forum has allowed diverse actors to consider how to raise the quality of cotton being delivered to gins (Poulton et al., 2004).

## Policy and the new architecture of aid

Policy for smallholder development and reduced rural poverty needs to consider the following points.

- Agriculture is primarily a private-sector activity. Governments cannot control it. All they can do is enable and encourage it and provide the public goods required.

- Public support for agriculture is undertaken across several ministries and departments. The ministry of agriculture may invest in research and extension, but rural roads, power supplies, schools and health services, as well as an enabling environment (including the rule of law and a suitable fiscal system), will be put in place by other agencies.

- Given agriculture's reliance on natural resources, which vary from place to place and from season to season, appropriate measures need to be tailored by region and context and adjusted over time.

The hallmarks of small farm policy are thus facilitation, co-ordination and flexibility. They involve measures that seek to use public efforts to liberate the energies and resources of farmers, businesses and civil organisations in the supply chain. Part of this involves programming significant spending on public goods – rural roads and agricultural extension and research, for example. But an equally important part concerns fostering institutions that will remedy market failures and encourage collective action wherever individual efforts are insufficient.

The new architecture of aid, as seen in budget support and sector-wide approaches, needs to recognise this and provide resources for facilitation, forums for co-ordination, and time for flexible responses. Smallholder development requires more than the programming of spending.

Above all, donors and their partners must pay attention to learning from experience and building programmes incrementally, rather than trying to produce a complete blueprint from the outset.

[6] In the past, major increases in support for farming in developing countries have come when national crises have arisen, as, for example in India in 1965–66.

[7] In nine Latin American countries from 1985 to 2000, more than 54% of all public spending on rural development went on private goods and transfers (De Ferranti et al., 2005).

This brief was prepared by Steve Wiggins of Overseas Development Institute (ODI) with support of Shenggen Fan of International Food Policy Research Institute (IFPRI)
with funding from USAid.

Editorial production: Mushtaq Ahmed (CIDA), Christoph Langenkamp and Daniel Gerecke (Secretariat of the Global Donor Platform).

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## SOURCES OF ADDITIONAL INFORMATION

A Research Workshop on The Future of Small Farms, organised by IFPRI, Imperial College London, and the Overseas Development Institute, was held in June 2005. The papers presented can be found at:

http://www.ifpri.org/events/seminars/2005/20050626SmallFarms.htm

A Discussion Paper based on a literature review and the deliberations of this workshop is also available:

Hazell, P., C. Poulton, S. Wiggins and A. Dorward. 2007. The Future of Small Farms for Poverty Reduction and Growth. 2020 Discussion Paper no. 42. Washington, D.C.: IFPRI. http://www.ifpri.org/2020/dp/vp42.asp