

POLICY BRIEF

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Sustainable finance for sustainable agriculture and fisheries

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Context

A resilient business is a business that is able to generate enough profits to buffer for bad times and to invest in the future. However, farming businesses have been undergoing substantial cost-price squeezes, due to rising costs and falling output prices. They have either been compensated for such income losses through direct payments from the EU's Common Agricultural Policy (CAP) or they have adapted or disappeared. Since 1992, the CAP has gradually shifted from a paradigm of government-led market regulation (through the use of minimum guaranteed prices, import tariffs and export subsidies) to a paradigm of market-orientation, in which private actors take up responsibility of responding adequately to market signals and of organising for resilience. Currently, the CAP is in a transition phase in which farmers receive direct payments, some market intervention is still possible and risk management schemes are still subsidised.

At the same time, the EU stimulates farmers to **differentiate** their produce through geographical indications, quality labels, organic certification and short supply chains, thus supplying niche markets. However, most producers still supply bulk markets in which they have a weak bargaining position, as they are exposed to strong competition. The policy response so far has been to stimulate producer organisations (**horizontal cooperation**) and branch organisations (**vertical coordination**), regulate unfair trading practices and enhance market transparency. The question remains whether this response is sufficient to improve producers' market orientation and financial situation.

SUFISA

The H2020 project SUFISA has been focusing on **institutional arrangements** (IAs) in general and supply chain arrangements (SCAs) in particular across 22 European agriculture, aquaculture and fisheries cases.¹ IAs are combinations of horizontal cooperation, vertical coordination and public intervention in dealing with market issues. Horizontal cooperation entails a collaboration among producers that are located at the same level



of the supply chain to capture scale economies and build up countervailing power. Vertical coordination entails a collaboration between producers and other supply chain actors downstream or upstream to share information and optimise chain-wide costs.

SUFISA's main policy recommendation is that a framework should be created in order for vertical coordination, horizontal cooperation and public intervention to work in an efficient, synergetic and inclusive way, and contribute to sustainable development.

SUFISA results confirm that market conditions dominate producer thinking and discourse, with low price levels and high market volatility as the most frequently cited conditions.² Stimulating both horizontal cooperation and vertical coordination has been identified in SUFISA's scenario exercises³ as no-regret options, that is, options that should be pursued no matter how the future evolves. However, there is not a single IA that solves all problem: there is no silver bullet solution. Moreover, according to SUFISA results individual producer and marketing strategies still dominate despite efforts to stimulate cooperation.

Efficiency

Efficiency means reaching the objective of producer resilience at the lowest cost to society, that is, by using policy instruments that do not distort market outcomes, that do not crowd out private initiatives and that are adapted to the diversity and heterogeneity in producers' external and internal conditions.⁴ SUFISA identified five sources of **heterogeneity**:

- **Product type:** high product perishability and long production cycles increase producers' rigidity and thus their demand for tighter vertical coordination
- **Firm characteristics:** rigidity is higher for more specialised producers whose demand for vertical coordination is higher, while larger producers may have better bargaining power and thus lower demand for horizontal cooperation
- **Producers' preferences and characteristics:** producers who are less risk averse and are more entrepreneurial require different IAs than risk-averse and production-oriented farmers and fishers
- **Market situation:** number and type of buyers influence the supply of IAs, but bargaining positions also depend on whether production is scarce (sellers' market) or abundant (buyers' market)
- **Institutional context:** trust and institutional stability foster the development of stable IAs.

Synergy

To be successful in the marketplace in the light of increased product differentiation and competition requires a shift in thinking and acting from antagonistic to collaborative supply chain relationships.

Antagonistic relationships are based on a win-lose model and may lead to power asymmetries and potential hold-ups from both ends of the chain. Producer organisations form an independent market benchmark, particularly where spot markets become thinner due to increasing contractualisation. Supply chain actors may collaborate in branch organisations to agree on acceptable business practices. Increased countervailing power held by producer organisations may increase prices paid to producers, but increase prices paid by consumers.

Collaborative supply chain relationships are based on a win-win model aiming at chain-wide improvements and even a win-win-win model with increased societal benefits resulting from better value for money for consumers and higher sustainability performance. Ideally, producer organisations are involved in vertical coordination, but this may be hindered by too antagonistic ways of thinking.

Inclusion

Interesting IAs may not be available to all producers, due to the lack of an appropriate institutional framework, trust and/or supply chain actors interested in collaborative relationships. Further, producers may need additional skills and capital to participate, which may be a barrier to entry for some. It is also likely that processors and retailers will limit collaboration to a small group of producers to limit transaction costs. Therefore, government should build and strengthen enabling frameworks for IAs to emerge, last and be beneficial for all supply chain actors, which implies also strengthening producers' skill base and participation rate.

Sustainability

IAs need to be sustainable, that is, last in the long run, but they also need to contribute to sustainability to underpin product differentiation on the one hand but also to contribute to various sustainable development goals on the other. SUFISA results suggest that, overall, IAs' contribution to sustainability is still limited.⁵ However, market-based compensation for sustainability will be a key factor for producers to invest in sustainability. For this, environmental actions and indicators need to be integrated in producer data collection in order to be able to monitor progress and calculate integrated sustainability indicators.⁶

Role of government

The role of government is complex, having to balance between societal welfare on the one hand and protection of producers on the other. Increased



requirements from society with respect to sustainability are translated into public regulation and lead to higher costs for producers, but these are counterbalanced by institutional mechanisms that aim to reduce these new costs or compensate for them. The emergence of new IAs calls for a rethinking of public policy, as is already evident in the regulation of producer organisations, branch organisations, unfair trading practices, etc. More specifically, IAs may induce thinner and hence more volatile spot markets, which may increase risk for producers not benefiting from contracts. Further, producers may face adjustment costs resulting from the investment in very specific assets when entering IAs. Finally, government needs to help in overcoming the lack of trust and solidarity and in building producer capacity related to marketing and distribution.

We recommend that CAP strategic plans drafted in the framework of the CAP post 2020 legislative proposal should evaluate the efficiency, synergy, inclusion and sustainability of policies related to IAs.

All deliverables and more information can be found at the SUFISA website: www.sufisa.eu. Project results are summarised in commodity- and country-specific extended summaries (<https://www.sufisa.eu/publications/>), policy briefs (<https://www.sufisa.eu/policybriefs/>) and a booklet (https://www.sufisa.eu/wp-content/uploads/2019/03/sufisa_booklet.pdf).

Notes

¹ See <https://www.sufisa.eu/publications/> for a detailed description of cases and Maye et al. (2018) <https://www.sufisa.eu/wp-content/uploads/2018/11/D2.3-comparative-report.pdf> for a comparative overview. The SUFISA conceptual framework can be found in Grando et al. (2019) <https://www.sufisa.eu/wp-content/uploads/2019/04/D1.2-Refined-conceptual-framework.pdf>

² See Vigani et al. (2018) <https://www.sufisa.eu/wp-content/uploads/2018/11/D2.4-producer-survey-report.pdf> for survey based results

³ See Aubert et al. (2019) D4.2 <https://www.sufisa.eu/wp-content/uploads/2019/07/Deliverable-4.2.pdf> and Aubert et al. (2019) D4.4 <https://www.sufisa.eu/wp-content/uploads/2019/07/Deliverable-4.4.pdf>

⁴ For a detailed and comparative overview of these conditions, refer to Maye et al. (2018) <https://www.sufisa.eu/wp-content/uploads/2018/11/D2.3-comparative-report.pdf>.

⁵ See Vigani et al. (2018) <https://www.sufisa.eu/wp-content/uploads/2018/11/D2.4-producer-survey-report.pdf> for survey results across cases and Creemers and Van Passel (2018) https://www.sufisa.eu/wp-content/uploads/2018/09/D_3.4.pdf for more in-depth analysis of results in the dairy and sugarbeet sectors.

⁶ Refer to Moretti and Van Passel (2018) https://www.sufisa.eu/wp-content/uploads/2018/09/D_3.5.pdf for an application of the sustainable value approach using FADN data.