Quality Standards in International Tea Markets
Challenges and Consequences for Smallholders and Tea Processors in Developing Countries

Research Proposal (outline)

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Background and Objectives

While tea traded internationally needs to comply with mandatory standards (e.g. EU's food safety and labelling regulations), quality standards imposed by major private companies in key markets have increasingly important implications for export of tea products from developing countries. The aim of the proposed project is to explore how quality standards in different end-markets affect terms and conditions for market access for developing countries' tea products. This aim is pursued by a comparative analysis of the tea supply chains originating in Indian and Tanzania and going into the European and developing Asian markets.

The role of quality standards in shaping access to international tea markets should be understood in relation to two new tendencies. Firstly, in a context of overall slow growth of tea consumption, notably in traditional tea importing countries in Europe, product differentiation and conformity to new generations of quality requirements represent an important source for large tea manufacturers to stimulate demand and maintain their market position (Oxfam, 2002). New strategies aimed at adding value and market more differentiated tea products include development of products such as decaffeinated and flavoured tea (tea blended with fruit, spices, or herbs), branded tea, instant tea and promotion of tea with geographical indicators. Meanwhile, there has been a constant deterioration and adaptation in the quality of tea and many tea qualities have become interchangeable and bought according to prices. This is partly because of new trends in blending and the development of crush, tear and curl (CTC) tea used for tea bags. Major tea manufacturers have become decreasingly dependent on particular quality attributes of tea coming from specific origins, as they are able to compensate for changes in tea type by blending with other teas (Asian Development Bank, 2004; SOMO, 2006). Thus, (global) tea manufacturers are competing to maintain market share, and the emphasis is on the one hand on the supply of relatively low quality bulk tea for blending and on the other hand on 'niche market' with premium priced, high quality products and this has increased the value of such tea. According to Oxfam (2002: 37), branded leaf tea may command a price six times higher than bulk tea for blending, and price spreads between high and low quality tea seem to have increased recently due to increased production worldwide and demand for higher quality tea (SOMO, 2006; Technical Centre for Agricultural and Rural Cooperation ACP-EU, 2005).

A second (related) tendency is that private vertical coordination systems are growing as a response to consumer demand for quality and safety (ibid.). The tea supply chain has become shorter and more dominated by a small number of large brand manufacturers, who are active in re-shaping the functional division of labour along the supply chain and strongly influences price movements at tea auctions in producing countries and demand for certain qualities of tea (Gibbon, 2006). Several of the leading brand manufacturers are vertically integrated into tea estates and packing and also upstream into shipping and transport and, although auctions currently account for the largest proportion of tea trade in major producing countries, tea is increasingly sold through direct sales agreements between packers and producers as packers are bypassing auctions and dealing direct with producers (IPAR, 2001; SOMO, 2006; Neilson et al., 2006).[1]

However, as Gibbon (2006) notes, while the rise of new generations of product differentiation and chain restructuring is fairly well-documented in the European markets[2], little is known about product and quality requirements in emerging markets such as developing Asia and the former Soviet Union. Import demand in developing Asia as a share of total world import of tea has increased from 5.9 per cent in 1993/95 to 13.5 per cent in 2003/5 (Gibbon, 2006: 8) and Asia (including Japan) is currently the largest importer of tea followed, by Europe, Africa and the Russian Federation (SOMO, 2006: 15). On the basis of analysing average unit prices for tea above or below world unit prices in developing Asian, Gibbon (2006) suggests that that consumer preferences in developing Asia might be for tea products that is minimally differentiated or not differentiated at all.[3] On the other hand however, according to the same study[4], average unit prices for commodity-dependent developing countries' exports of tea into developing Asia was +7.7 per cent above average price of all imports in the market in 2003/05 (ibid.: 11). Although not directly comparable, the average unit price for black tea exports from Tanzania and India into the EU in 2001/03 was respectively 37.4 per cent and 10.5 per cent below the average unit value price of all imports of back tea in Europe (FAO, 2005a). Gibbon (2006) accordingly suggests that tea products might not be at the same quality disadvantage in developing Asian markets as they are in European ones. However, as mentioned above, there is a general lack of empirical studies on the issue of bifurcated global demand.

With concerns about adverse international price trends[5] and uncertain market prospects for export of tea products, tea manufacturers and policy-makers in developing countries are looking to further advances in tea production, improvement in quality and differentiate their products in order to access quality-conscious markets as well as development of trade marks and protection of geographical indicators as means to foster economic growth and diversification (Tea Board India & UPASI, 2004; FAO, 2005a; FAO, 1999; Asian Development Bank, 2004; Simbua, 2006). While tea estates and larger producers are able to certify their production against quality standards, authenticity of origin, or trade marks (e.g. 'Darjeeling tea'), smallholders and small-medium sized processors (brought leaf factories) tend to face significant difficulties. In any case, quality improvement and safeguarding the reputation of a national crop or a regional trade mark requires a significant degree of horizontal coordination between players in the (national) market system. As pointed out by Poulton et al. (2004) and Larsen (2004), the most critical challenge to be overcome is free-riding by factories seeking to avoid making their contribution to things like quality control

[1] About 80 per cent of total tea trade is marketed through tea auctions (2005). The market share of direct sale arrangements is restricted by law in some of the major tea producing countries (SOMO, 2006).
[2] For a review of the tea market see for instance SOMO (2006), Oxfam (2002), and Technical Centre for Agricultural and Rural Cooperation ACP-EU (2005).
[3] The average unit price (in per cent) above or below world unit import price in developing Asia was -7.8 in 1993/95 and -26.5 per cent in 2003/05 (Gibbon, 2006: 10)
[4] The study analysed developments of trade (volume and value) for 17 agro-commodities over the past decade. Commodity-dependent developing countries (CDDC) is defined as developing countries whose average annual exports for the period 1993-95 to 2003/05 were more than 50 per cent dependent on non-oil commodities. The study covered around 70 CDDCs in 1993-95 and around 55 in 2003-05. The largest single concentration of CDDCs is in Africa (Gibbon, 2006: 4).
[5] Note however, that a recent study conducted by FAO on value chains indicate that, of the 27 agricultural commodities, tea showed the second lowest variability in prices (2 per cent decline) compared with for instance 39 per cent for cocoa and 38 per cent for coffee (FAO, 2005b).

but then still competing for the resulting crop output. Furthermore, assurance of quality (e.g. variety, origin or grade) requires some kind of vertical coordination between producers and processors. However, the cost of monitoring, organising and operating smallholder contract farming or outgrower schemes (e.g. screening smallholders, distributing inputs, monitoring their use over the season), increase considerably in a competitive market system.

Against this background, the main objectives of the proposed study are firstly, to examine the scope and nature of salient quality standards in European and Developing Asian markets and how quality is financially rewarded in these markets. Secondly, to analyse the distributional effects of conformity to quality standards amongst developing countries and different groups of actions within a country. Thirdly, to identify what national and local institutional conditions are important in achieving improved conformity with quality standards.

The proposed study is part of a wider research programme ('Standards and Agro-Food Exports (SAFE): Identifying Challenges and Outcomes for Developing Countries') involving the Danish Institute of International Studies (DIIS) and the Department of Agricultural Economics and Agribusiness at Sokoine University of Agriculture (SUA) in Tanzania, running from 2005 to 2009. This programme has research and capacity building components and focuses on costs and benefits of conformity to food safety, quality, organic, sustainability, labour and social standards. The programme includes studies on fishery products, organic produce, tea and cut flowers from Tanzania and selected comparative countries (Kenya, South Africa, Uganda, Vietnam, and India) to northern countries.

Research Questions

This study addresses three groups of research questions:

1) Questions concerning quality standards in the global tea market

- What are the salient quality standards in the European and developing Asian markets and in what ways do quality requirements deviate between these markets?
- What are the reward structures of conforming to quality standards in these markets and market segments (supermarkets, wholesale markets etc.)?
- What is the relationship (if any) of demand and supply of teas to these markets and what role do auction centres have in this distribution?
- What role do auction centres play in terms of the arbitration of quality and quality control?

2) Questions concerning the distributional (in terms of entry barriers) and organisational effects of quality standards on the supply chains

- What levels of participation in export markets have been achieved? What are the main end-market destinations? What end-market segments (supermarkets, wholesale markets etc) are they destined for? Through which market channels (direct sales, sales through auction)?
- What is the extent of conformity to salient quality standards in export markets? Who are the exporters/processors that conform to these standards and how did they conform?
- What are the firm-level challenges of conforming to international quality standards? In what ways do these vary by firm scale; by market channel and by end-market destination?

- What are the farm-level costs and benefits of conforming to quality standards? How do these relate to farm scale and to marketing channel? What types of contracts are typically present with regard to transactions between farmers and factories (e.g. the extent to which contracts are interlocking)?

3) Questions concerning the institutional pre-conditions for improved conformity with quality standards

- What national and local institutional arrangements are in place for ensuring quality standard requirements in international markets?
- What role do public and private sector initiatives play in achieving improved conformity with standards?
- What sector level organisation and conditions are necessary for these institutional forms to operate efficiently? (e.g. levels of competition and horizontal coordination)
- What are the preconditions under which effective coordinating mechanism arise for the supply of public goods?

The reminder of this outline presents research methods with regard to the Indian study and an outline of practicalities related to the project.

Research Methods

The core of the fieldwork will be conducted in India (2007) and Tanzania (2008), but part of the research on the nature of salient quality requirements and how quality is financially rewarded in different end-markets (question 1 above) will be carried out by documentary search on selected quality standards and statistical data on average unit import prices in the European and Asian markets (time-series by tea categories). Equally important, interviews will be carried out in Europe and possibly in Asia with representatives from importers of tea products.

In India it is proposed to carry out fieldwork in four main parts. The first part will involve interviews conducted with companies engaged in exporting tea from India (blenders, packers, distributors, and retailers) in order to obtain information in relation to question 1 and (part of) question 2 above. Efforts will be made to interview all proprietors or managers of companies engaged in exporting tea from southern India in order to access information on quality standards and reward structures in different end-markets and market segments as well as the organisational aspects of export companies' successful compliance (or lack thereof) with quality requirements in end-markets. In addition, interviews will be conducted with brokers and professional tea testers at the main public auction centres in southern India: Coonoor, Coimbatore, and Cochin (south Indian teas are mainly exported to the Russian Federation and Asian markets but also to markets in Europe) and the auction centre in Calcutta (mainly to markets in Europe and America).

The second stage will involve a sample of the Bought Leaf Factories (BLF) present in the Western Ghats. The sampling frame will comprise parameters on size of factory (market share / sales level), marketing channel (auction / direct sale) and end-market destination (if possible). It is planned to make an initial identification of a number of the factories (BLF) in close collaboration with key informants in the area (e.g. with representatives from United Planters Association of Southern India (UPASI) and/or officials at the auction centres in the area concerned and/or packers/blenders).

The third part will involve a survey of smallholder tea farmers based on their marketing channel and stratified by size of landholding. It is assumed that ownership-related assets (e.g. possession of land) influence smallholders' ability to comply with more demanding quality requirements as well as their ability to become engaged in contract farming and/or direct sale arrangements with the BLF. Therefore, it is intended to conduct a survey of smallholder tea farmers selling their produce directly to the BLF (interlocked transaction via so-called Self-Help Groups or contract farming) and a survey of smallholder tea farmers selling their produce to buying agents (spot-market transaction). The final stratification criteria and number of smallholders to be interviewed in each case will be determined *in situ* in collaboration with key informants in the area (e.g. the BLF concerned and/or UPASI).

In both cases, costs of activities related to production and sale of tea will be measured including costs of labour input (family and/or hired labour) into land preparation, weeding, pruning, fertilizer and herbicides application, plucking, transport and marketing (measured in man-days) and costs of variable inputs such as fertiliser, herbicides and tools.

Finally, the role of public/private sector initiatives in promoting and monitoring quality standards conformity will be examined by conducting interviews with representatives of key institutions including the United Planters' Association of Southern India; the Tea Research Institute; National Tea Research Foundation; the Indian Tea Association; and the Tea Board India as well as by addressing the same phenomenon to respondents in the different segments of the supply chain during the course of the fieldwork in India. Indicators of the coordinating aspects of the supply of public goods will include:

- Types of coordination through:
    - Associations with decision-making powers and/or industrial boards
    - Major actors in the sector taking decisions informally amongst themselves
- Procedures for implementing decisions agreed and kinds of mechanisms developed to enforce agreements
- The extent and nature of public goods made available (e.g. quality control, testing methods, certification, investment in agricultural research).

It is thought that the bulk of fieldwork will be undertaking in the Western Ghats in Southern India (3 months), followed by 3-4 weeks fieldwork in Calcutta, in the form of interviews with companies (brokers, blenders, wholesalers, retailers) engaged in export of tea products as well as interviews with respondents at the auction centre in Calcutta. All interviews will be carried out by the author, possible with a research assistant who will help with introduction to key individuals and institutions in the study area, and with language translation.

Practicalities

Research cooperation
The project will be based at the Department of Geography and Geology, University of Copenhagen and linked to the SAFE research programme at the Danish Institute for International Studies, coordinated by S. Ponte. In India, the project will be carried out through corporation with the Institute for Social and Economic Change at the University of Bangalore (Prof. K.V. Raju and Dr. Lenin Babu) and in Tanzania through affiliation with the Department of Agricultural Economics and Agribusiness at Sokoine University of Agriculture (Dr. E. Lazaro).

Timing and Duration
Fieldwork in India is scheduled to take place between March and July 2007. The Indian sub-project will be written-up in the second half of 2007. In addition, fieldwork in Europe (conducting interviews with representatives from major stakeholders in the market) is planned to take place following fieldwork in India. Fieldwork in Tanzania is planned to take place in early 2008, though the actual timing will be determined later, followed by writing-up and publication in the second half of 2008. The project as a whole will be written-up and finalized in the first half of 2009.

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