

# The effect of the international financial and economic crisis on the fruit and vegetables sector in developing countries

## Summary

The financial and economic crisis has already had a significant negative impact on export levels, profit margins and employment in the fruit and vegetables sector in developing countries. Exports from developing countries (DCs) are under pressure, especially from importers in Europe using their market power to cut prices. However, the sector is also suffering from declining demand for more expensive varieties of tropical fruit and vegetables, off-season products and recently introduced varieties. The decreased demand for products produced outside the European growing season may face further pressure from European consumers and their growing awareness of the carbon footprint of these products. Some export companies, furthermore, notably those with a focus on the UK market, have been hit by exchange rate fluctuations. Local markets are only a partial substitute for export markets due to their limited size or the limited alignment between the products on offer and local demand in terms of price and quality.

As production prices are not going down, margins are under pressure. However, the effects on employment appear to be limited so far. The longer-term effect of the crisis on employment will depend on the composition of exports (which products), the structure of production (perennial crops or one-year crops) and the target destinations selected by exporters and their countries (e.g., the West European market is performing better than the North American and East European markets).

Obtaining credit is among the most pressing issues facing companies in DCs, especially small producers. Respondents to the questionnaire indicate that since the onset of the crisis obtaining credit for working capital, investments and export financing has become more difficult. Access to credit for working capital poses the greatest difficulties, but financial institutions have also become increasingly reluctant to provide investment capital or to finance trade. European buyers are unable and/or unwilling to completely fill this gap. Many exporters of fruit and vegetables are therefore struggling with liquidity problems.

According to the CBI experts and several BSOs approached for this survey, investing in quality, certification, logistics and market entry activities is vital to retaining existing buyers and/or finding new ones. Export companies, they suggest, must focus on their core competencies and follow a long-term strategy centred on innovation and cooperation. Also, both exporters and BSOs should seek to increase awareness among buyers of the potential and products of their countries. Specific opportunities may exist for cheaper alternatives for exclusive fruit and vegetable varieties already being marketed in the EU.

## Introduction

Exporters in the fruit and vegetables sector, like many others, are worried about the effects of the credit crisis. Insurance firms are nervously reviewing credits. Exporters fear lower revenues for their products; the pressure on exotics and/or luxury products, especially, is high. Although short-term turnover statistics in most West European countries do not suggest a severe downturn, the concerns are real. In Great Britain and Ireland, for instance, consumers have become distinctly more price-conscious.

This report offers an overview of the impact the financial crisis is having on fruit and vegetables exporters in DCs and the consequences for European imports from these countries.

## Approach

### 1. Online questionnaires

The following parties were asked to fill out sector-specific online questionnaires: BSOs, exporters in developing countries, European buyers importing from these countries, European associations.

This online questionnaire was held between February 23 and March 2, 2009, and yielded the following response:

**Table I Response to online questionnaire, fruit and vegetables sector**

	Partner countries	Other CBI client countries	EU	Total
<b>Exporters</b>	48	10		58
<b>BSOs</b>	20	4		24
<b>EU buyers</b>			7	7
<b>Associations</b>			8	8
<b>Total</b>	<b>68</b>	<b>14</b>	<b>15</b>	<b>97</b>

### 2. Interviews

A number of representatives of these groups were approached for in-depth interviews. In the interviews, these players were asked questions about the impact of the crisis, specific institutional and private needs, opportunities, and the different levels at which they seek assistance in promoting exports. A total of 20 interviews were conducted: 9 with exporters, 4 with BSOs and 4 with importers; the CBI experts and Programme Manager were also interviewed.

As far as possible, the information drawn from the questionnaires and interviews has been supplemented with additional market information.

## 1 Consequences for Companies

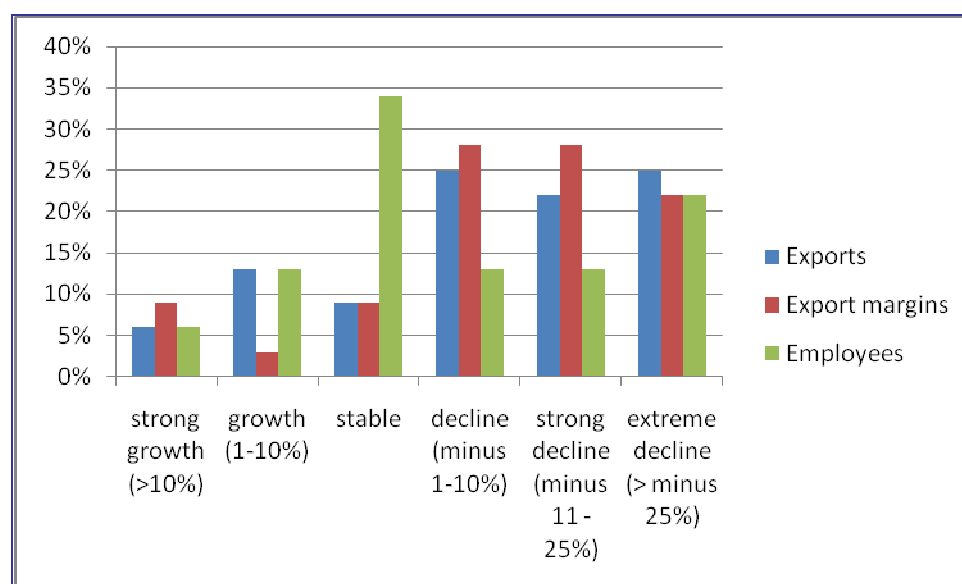
In these early stages, in which the first results of the crisis are slowly coming into view, it is difficult to present a detailed picture of the consequences of the crisis for the fruit and vegetables sector. Statistics and trade data are not yet available. Also, production in this sector is highly seasonal: for many products and countries it is not yet clear what this year's harvest will bring and how markets will respond. However, on the basis of input from the questionnaires and interviews, an attempt has been made to outline the effects of the economic crisis as accurately as possible.

### 1.1 Consequences in Developing countries

#### Expectations

From the questionnaires and interviews it appears that most exporters expect negative export developments. Until now there is no clear indication of this in the market, however. More than half of the exporters approached for this survey expect severe or very severe export decreases. The emphasis here is on export value, as European importers are using the crisis and their strong market position to negotiate lower supply prices. However, their own sales prices are also under considerable pressure.

**Figure 1.1 What fruit and vegetables exporters expect for 2009**



The BSOs confirm this prognosis, although most of them are slightly milder in their forecasts. Both the respondents anticipating strong growth and those anticipating a steep decline are fewer in number than the exporters with similar expectations. However, a few BSOs do anticipate a very sharp decline in exports, especially for sectors depending on a limited number of importers or buyer markets, such as Uganda.

**Table 1.1 What BSOs in the fruit and vegetables sector expect for 2009**

	Exports		Margins		Employees	
Strong growth (>10%)	0	0%	0	0%	0	0%
Growth (1-10%)	3	18%	2	12%	1	6%
Stable	3	18%	3	18%	5	29%
Decline (minus 1-10%)	6	35%	6	35%	8	47%
Steep decline (minus 11 - 25%)	3	18%	5	29%	1	6%
Extreme decline (>minus 25%)	2	12%	1	6%	2	12%

The economic crisis has contributed to a considerable devaluation of certain currencies, notably the pound sterling. The euro exchange rate, as compared to the US dollar, has also gone down, dragging down the value of exports from DCs whose currencies are linked to the US dollar. Devaluation of the pound sterling has had a particularly negative influence on DCs whose exports are heavily UK-oriented.

Export margins are under severe pressure. Prices are dropping and exporters observe that their European buyers have become more price-conscious and tougher negotiators. Exporters and BSOs also note that European firms are less inclined to develop long-term trade relations. Instead, their orders are becoming smaller in volume, which in a fresh produce sector is very bad for producer margins. Many producers and BSOs also report that production costs are rising – or at least that the cost of raw materials, labour and transportation is going down at a lower rate than are export prices.

Employment in the fruit and vegetables sector has thus far remained reasonably stable. The main explanation for this is that most producers hire day labourers and employ personnel on a 'project basis'. The effect on out-growers<sup>1</sup> is difficult to assess, though it is probable that employment in this segment is already decreasing. The effects are likely to vary from one sub-sector to another. Companies that have invested in perennial species are likely to have a longer-term vision and will therefore try to retain their staff for as long as possible. If the crisis does not subside within a reasonable period of time, this segment will suffer intensely, however, as it lacks the flexibility to adapt production. Producers of species

<sup>1</sup> The term 'outgrower scheme' is often reserved for schemes in which the agri-business has considerable control over the smallholder production process, providing a large number of services, such as input credits, tillage, spraying and harvesting. The smallholder provides land and labour in return for this comprehensive extension/input package (NRI, 2003 - <http://www.nri.org/projects/NRET/SPCDR/Chapter3/services-3-4-2-1.htm>).

with a shorter growth period have more room for flexibility in production, choice of species and employment levels.

## The Key Problems

Exporters and BSOs list the following key problems facing fruit and vegetables exporters:

- Payments are being delayed and possibilities for trade financing are limited.
- Prices in several product groups are under severe pressure.
- Demand for some products is declining, especially luxury tropical fruit and vegetables, off-season fruit and vegetables and recently introduced varieties.
- Insufficient demand on local markets or mismatching between local demand and supply means domestic markets are a poor alternative for exporters.
- Order volumes are diminishing, as many European buyers who previously ordered in bulk are avoiding risk by placing more frequent, but smaller orders.
- The drop in oil prices has not yet led to price drops for transport or agricultural products, such as fertiliser and seeds. In some countries, in fact, prices have gone up due to exchange rates. Labour and packaging costs are also fairly rigid. On the upside, decreasing demand for air transport has induced some airlines to offer cheaper rates (e.g. Martinair from Ecuador).

### Declining demand

As a result of declining European demand for fruit and unsold Brazilian grape supplies, South African grapes are being sold for 2 to 3 euros less than last year, says Levan Biljon of Dole. "Worries about economic conditions in Europe are causing many exporters to ship larger volumes of grapes to the Middle east and beyond. Those markets have started to feel the pressure much earlier than usual." ([www.DeGroentenFruit.nl](http://www.DeGroentenFruit.nl))

Both of the CBI experts as well as the CBI's Programme Manager for this sector expect a decline in exports, but say it is difficult to predict how steep the decline will be. Dutch trade journal 'Groente en Fruit' suggests that European fruit and vegetables sales have dropped by 5 to 10%.

## Regional Differences

As stated previously, it is difficult at this stage to accurately predict the effects of the crisis on developing countries. The interviewees approached for this survey – citing recent information – do not see significant regional differences. They do note that such differences may occur, resulting from the fact that different regions depend on different export markets and to varying degrees. Africa, for instance, depends heavily on the West European market. With turnover in Europe showing less decline than in the USA, the impact of the crisis in Africa may be limited. Many products from Southeast Europe are geared to East European markets, where the crisis is expected to have a major impact. The same applies to South and Central American producers, who tend to focus largely on the North American market.

## Differences per Product (Group)

BSOs often have a clear view of the development of specific products. Their most important conclusion is that more expensive exotic fruit and vegetable products produced during Europe's off-season will be hit by the crisis. European concerns about the high carbon footprint<sup>2</sup> of off-season fruit, meanwhile, are increasing.

Within the tropical fruit segment, the crisis is especially damaging exports of mangoes, pineapples, nuts, special banana varieties and other special or recently introduced products, such as physalis, passion fruit, jackfruit and kumquat. Among the non-tropical fruit products, strawberries and table grapes are suffering most. The most vulnerable vegetables, according to the BSOs approached for this survey, are luxury products such as mini veggies, avocados, sugar snaps, snow peas, fine (or Kenya) beans, artichokes, bell peppers (or capsicums) and cherry tomatoes.

Some BSOs, however, expect growth for these products – proof of the uncertainty dominating the sector. Sector experts in DCs are at a loss as to how the sector will develop. Products considered to have potential include melons, sweet potatoes, limes, lemons, pomegranates and peaches.

<sup>2</sup> The carbon footprint is a way of gauging the influence of human activities on the environment in terms of the amount of greenhouse gases (carbon dioxide) measured. The footprint is a means of visualising the contribution made by people and organisations to the greenhouse effect. A large proportion of the overall carbon footprint is produced in DCs by transportation activities; cross-continental air transport of products is a particularly important contributor. The trade focus in recent years on upscaling, production relocation and greater efficiency will gradually shift towards a focus on the CO<sub>2</sub> emissions involved in marketing a product.

## CSR and Sustainable Production

Most of the BSOs believe the crisis will influence the corporate social responsibility (CSR) policies and sustainable production processes of exporters negatively or not at all. The BSOs state that the additional cost involved in many CSR-related measures will have a negative influence. One sector expert counters that these BSOs fail to see CSR and sustainability as a means for exporters to distinguish themselves in a difficult period. CSR, he says, can be used as a marketing argument to convince European importers. As described below, sustainability remains an important issue for European consumers.

The sector experts note that long-term contracts are becoming scarce. Increasingly, European retailers are buying on spot. If price competition increases, CSR may disappear into the background for exporters. Particularly sustainability business process measures involving additional cost will be put off. Fair Trade and certified organic products will still be in demand, but growth in this segment will slow down and the market may even shrink.

### 1.2 Consequences in the EU

Many of the developments described above are confirmed in the European market. From interviews with European buyers it appears that many of them have adopted a more critical attitude towards advance payments, whereas the restricted access to capital in DCs is forcing them to finance production. These developments are hindering trade and may have a negative effect on future supply from DCs as exporters are forced out of business. Many European buyers are quite concerned about this.

Consumer purchasing is expected to shift from more expensive, luxury products to more 'basic' products. The replacement of Kenya's haricots verts, or fine beans, by other bean varieties is an example of this 'downtrading'.

In the fruit sector this shift will be even more dramatic, with the more expensive 'exotics' facing decreasing demand. Recently introduced fruit varieties, such as dragon fruit and star fruit, may also be avoided by European consumers. The introduction of other new fruit and vegetable varieties is likely to come to a standstill.

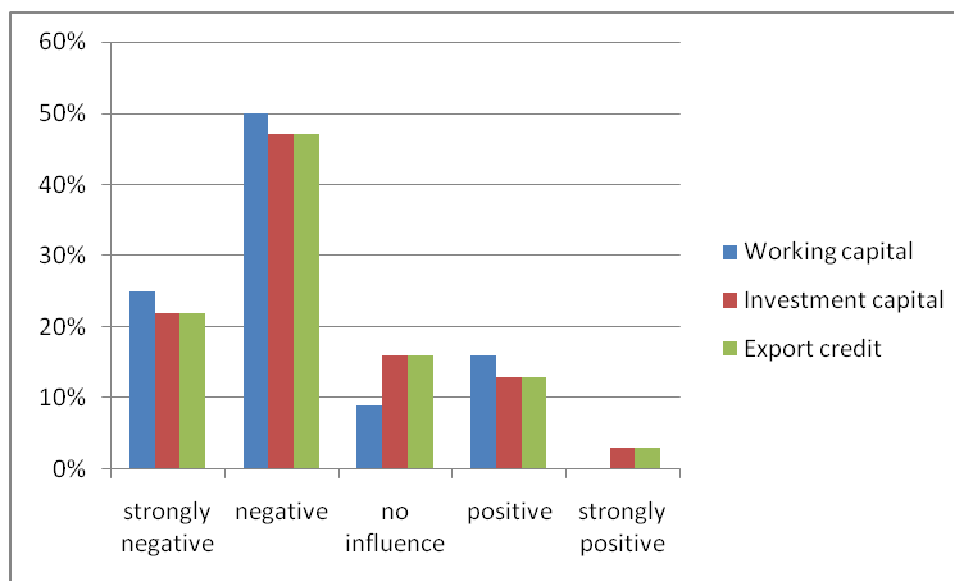
Sales of 'basic' products – citrus fruits, apples, pears – will not show immediate growth, but will at least be more stable. Much depends on how European retailers market these products.

The concern among European consumers about the carbon footprint of the food they eat also remains an important factor. Currently, transport by air is having a very negative impact on margins due to the drop in selling prices. In the future the social acceptance of air transport is likely to decrease and investments in alternative modes of transport will be necessary.

## 2 Credit

Exporters are worried that the credit-worthiness of their buyers will decrease. Insurance companies are reviewing credits and setting stricter demands. As a consequence, more and more suppliers are asking for advance payments, which is slowing down trade. The sector is already suffering from this development and the situation is likely to get worse.

Limited access to credit is causing a lot of trouble among exporters. The crisis has especially impacted their access to working capital.

**Figure 2.1 Consequences for access to export credit**

The BSOs largely have the same view on this issue. A relatively larger number of BSOs say the crisis will hardly affect access to credit, but none of them expect the credit position of fruit and vegetable producers to be affected positively. Some of the developments mentioned by the respondents are described below.

#### **Working Capital**

- Rising costs and decreasing prices have put pressure on profit margins, negatively impacting the availability of working capital.
- Regional differences do exist: in Africa, attracting capital was already difficult before the crisis and working capital was often drawn from other sources, such as family capital or company revenues; the impact in Africa, therefore, is limited (if not the need for capital).

#### **Investment Capital**

- In order to comply with EU rules and regulations regarding food safety, companies must invest in changes in production and logistics and in obtaining the necessary certificates. The availability of investment credit has worsened, however, as have the conditions under which it is offered (securities, own capital, business plan requirements etc.).

#### **Export financing**

- Banks are reluctant to grant export credits and guarantees. Here, too, conditions vary from one country to another. In some countries, such as Egypt, export credit is still considered by financial institutions to be a lucrative form of investing.

Remarkably, Egypt's exporters say the crisis is positively impacting business – thanks to the availability of various government investment instruments offering support to producers of fruit and vegetables. This is a good illustration of the value the government attaches to this sector, but also of the trade facilitation and incentives that can be generated with the right investment tools.

Financial problems vary from one company to the next, often depending on those companies' relations with buyers. In the fruit and vegetables sector it is not uncommon for importers to offer cash flow services to their regular suppliers in the form of, say, delivery down payments and deposits. Such financial allowances provided DC exporters by European importers can help solve the problem of export financing. According to one of the experts interviewed for this survey, Dutch importers have plenty of resources to offer this kind of assistance. However, the importers add that there is a need for a system of guarantees, as they too face rising costs and an increasingly noticeable credit pinch.



### 3 Opportunities

Most of the exporters do not see any significant opportunities arising from the crisis. A few of them do, however:

- If the crisis forces some producers out of business, there will be more room for their competitors. The crisis will purge the sector of companies offering poor quality or failing to deliver on their promises.
- By improving products and process efficiency, producers can strengthen their ties with European customers, while cutting production costs at the same time.
- The crisis will push down farm land prices, while some companies will be sold. Producers with sufficient capital will thus be able to expand.

The CBI experts and Programme Manager agree that the crisis has not given rise to clear new opportunities. They do note that market changes will boost interest in cheaper alternatives to exclusive products.

More than half of the BSOs believe the crisis will present new opportunities to companies responding in the right way.

- Within certain product groups, the BSOs say, there is room for development. Pomegranate sales, for example, are expected to show steady growth, while the 'back to basics' tendency among consumers offers opportunities for basic fruit and vegetable varieties, such as citrus fruits.
- Demand for cheaper fruit and vegetable varieties may place certain producers from DCs in the foreground as they can produce these at lower prices than their European competitors.
- Companies will be encouraged to diversify their sales markets, which may contribute to the future stability of this sector in developing countries.
- HACCP, GlobalGap and other certification schemes are important means for producers to distinguish themselves on the European market.
- Certain countries already enjoy a competitive advantage, which they could reinforce. BSOs in Ghana, for instance, believe decreasing transport costs and their relative nearness to Europe can make it easier for Ghanaian exporters to access European markets if they seize the opportunity to proactively seek new buyers.
- All round, the feeling exists that a proactive attitude may well help producers find new buyers in Europe – albeit at the expense of existing suppliers.

Strengthening ties with European partners and obtaining access to credit are generally considered important keys to capitalising on opportunities and surviving the crisis. Both of the experts interviewed for this survey say it is essential that export companies build on their core activities and stick to a clear, long-term strategy. Collaboration with other players is also gaining importance.

### 4 Needs

Surviving the crisis calls for a more strategic and professional business administration. Only then will companies succeed in adapting to the changing economic situation before it is too late. Import duties and strict phyto-sanitary regulations are a major obstacle for exporters from DCs, besides the immediate effects of the crisis; the crisis has heightened the impact of these factors. Requirements regarding quality, traceability and certification will be taken more and more seriously. Exporters need coaching to cope with these requirements and thus to gain access to European markets or to improve their position there.

Several problem areas emerge from the questionnaires and interviews with exporters and BSOs. Some of these can be found in Table 4.1.

**Table 4.1 The needs of exporters and BSOs in developing countries**

• Decreasing prices	• The exchange rate of the euro
• Restricted access to credit	• Declining demand for luxury/ exotic fruit and vegetables
• Rising raw material prices	• Irregular and delayed payments by customers
• High production costs	• Smaller export margins
• High storage and distribution costs	• Limited availability of accurate market information

The needs perceived by exporters and BSOs are directly related to these problems. Exporters are primarily in search of financial support and services to improve their liquidity. Solutions include deposits and advance financing by European importers aimed at limiting shortages of working capital and export financing. There is also a need for new and more solid relationships between exporters and their European buyers. Another top priority among exporters is to broaden their export markets, for instance by visiting trade fairs and launching new market entry activities.

Economic conditions are rapidly changing as a result of the crisis, making it difficult for exporters to make strategic decisions. They need applicable, specific and up-to-date market information to gain better market access and to respond effectively to developments in the European fruit and vegetables market. Much of the information available on the Internet is either outdated or too general. The information provided by the CBI is valued positively, however, crisis conditions calls for more frequent updates dealing with the specific implications of the crisis for specific product groups.

All too often, local BSOs and other organisations in DCs are unable to meet this information need. In fact, the BSOs are in need of information themselves. They also attach significant value to improved marketing and promotion of their companies and products and the qualities of their countries as producers of fruit and vegetables.

Maintaining export prices and a general export orientation is of vital importance to exporters. Failure in these areas may threaten future production quality and quantity, while also damaging the market shares, business contacts, trade relations and image these companies and countries may have acquired. Buffers could be created at sector or country level to absorb temporary export drops. Guarantee schemes with regard to advance financing of production by importers may also help secure the continuity of the sector. Holding on to market share by heavily investing in customer retention is also vital at this time.

Transport costs are gaining importance in international competition, because of their large share in total costs. Declining volumes may leave exporters with fewer options and therefore higher costs. Increased attention for the ecological aspects of transport and production, meanwhile, are raising interest in alternative solutions, such as improved cooling facilities aimed at pushing back sell-by dates and thus making transport by sea a viable option.

This survey was compiled for CBI by ProFound – Advisers In Development

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