Regoverning Markets
small-scale producers in modern agrifood markets

Information Sheet April 2007

Kenya

Trends in growth of modern retail and wholesale chains and related agribusiness

The actors along agribusiness supply chains in Kenya comprise of producers, brokers, processors, wholesalers, retailers and exporters. In regard to retail level, the main formal retailers for **fresh fruit and vegetables** are supermarkets and groceries. Leading supermarkets include Nakumatt, Uchumi, Tusker Mattress, Ukwala and Safeways. Uchumi has extended its network to Kampala, Uganda, where it is competing with Shoprite of South Africa. In line with the growing global internationalization of food retailing, there are foreign multinational supermarkets in Kenya such as Woolworths of South Africa. Although Woolworths in other countries stock food items, the three branches in Kenya specialize in clothing and kitchen equipment or items. Another foreign supermarket, Metro Cash and Carry had branches in the country but closed recently. Groceries in Nairobi include Westlands Green Grocers, Zucchini Vegetable Shop and Corner shop. In addition to supermarkets and groceries, other key buyers of fresh fruit and vegetables, dairy products and meat including poultry are hospitals, hotel chains and fast food chains. The main fast food chains in Kenya are Steers, Kengeles and Innscor Kenya Ltd including also Pizza Inn, Chicken Inn, Nandos, Creamy Inn, Bakers Inn and On the Run. Steers and Innscor Kenya are franchises with headquarters in South Africa.

In the informal or traditional channel, large retail markets for fresh fruit and vegetables in Nairobi are City park, Gikomba, Kangemi, Kiserian and Githurai. In wholesaling, the main wholesalers of fresh fruit and vegetables include Mugoya and Fresh 'n' Juici. In addition there is a large wholesale market, Wakulima, in Nairobi. The main brokers of fresh fruit and vegetables are associated with this wholesale market. The hygiene conditions of the wholesale market have improved following a thorough clean-up and renovation in 2005. There is adoption of quantity standards for instance in potatoes. The hawking of fresh fruit and vegetables at the streets of Nairobi was banned by the local government in 2006.

Key points

- There are market changes taking place in sub-sectors of fruit and vegetables and meat, including poultry at national, regional and international levels
- The key drivers of market changes are consumer "pull", policy "push", urbanization, commercial opportunity, food standards, foreign investment, tourism, changing urban habits, environmental awareness and social welfare
- Key demands and issues of the dynamic markets are consistent supply, quality standards, freshness, hygiene, quantity, variety, reliability, traceability, safety, sanitary and phytosanitary standards and maximum residue levels
- The standards set by local private sector and the international markets are more or less the same, an indication that the formally clear distinction between the local and export markets is becoming blurred
- High value markets tend to procure from medium or large-scale farmers or from organised small-scale farmers thereby minimizing transaction costs
- For small-scale farmers to meet the conditions of the high value dynamic markets, they require technology, financial capital, human capital and organization

In regard to exports, **key exporters of horticultural crops** include Homegrown (Kenya) Ltd, Kenya Horticultural Exporters, Sher Agencies, Vegpro (Kenya) Ltd, Wilham (Kenya) Ltd, East African Growers, Oserean development company Ltd, Sunripe Ltd, Frigoken Ltd and Everest enterprises. Most of these exporters are producers-cum-processors. Some exporters do sub-contract small-scale farmers through out-grower

This series of Information Sheets provides a summary of market changes taking place at national level within key high value agrifood commodity chains. The intention is to serve as a point for public sector, donor and private sector discussions with particular focus on securing and improving income among the rural poor through their participation in new and dynamic markets.

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arrangements. Most of the produce is exported to Europe while imports are usually sourced from South Africa, Italy, East Africa, Egypt and Ethiopia.

Small-scale farmers account for about 56% of the total **milk** production thereby dominating dairy production in Kenya (SDP, 2004). The sub-sector supports more than 600,000 small-scale dairy farmers. About 60% of total milk production is produced in the highlands from exotic and crossbred dairy cattle. Milk marketing is undertaken through the formal and the informal market. The informal channels (hawkers and kiosk/vibanda) handle 62% of raw-milk sold in urban areas (Tegemeo, 2005). There has been growth in processing of dairy products accelerated by a policy change. Before 1992, the government controlled milk prices and supported the co-operative movement through direct assistance and subsidized services. The main channel of milk then was from producers to dairy cooperatives to a monopoly processor, Kenya Cooperative Creameries (KCC), to wholesalers and retailers and then to consumers. The implementation of liberalization policy in 1990s created opportunity for other entrants and there was sudden inflow of processors, brokers and hawkers in the supply chain. The processors include: multinationals; owned by large-scale farmers; co-owned between small-scale farmers and private investors; or owned by organized small-scale farmers alone. Their location is both urban as well as in rural high potential areas. There are about 30 licensed and operational milk processors. The leading ones and those with a capacity of at least 100,000 litres per day are Brookside dairy ltd, Githunguri dairy cooperative, New KCC, Limuru milk processors, Meru central FCU ltd and Spin knit dairy ltd.

Pertaining to the **meat** sub-sector, there are several large scale slaughterhouses in Nairobi (Njiru and Dagoretti) and in Mombasa among other large towns. The slaughterhouses receive most of their animals from Arid and Semi Arid Lands (ASAL) such as Mandera, Isiolo, Garissa and Wajir usually through ranchers where animals are temporarily taken for fattening. The main market of meat and meat products from the slaughterhouses are the low and medium cadres in urban areas (towns and cities) and sometimes institutions. The main processors of meat targeted for high value markets such as supermarkets, airports, export, big hotels and fast food chains are Kenya Meat Commission (KMC), Alpha fine foods, Meatons, Kenchic (specialized in poultry), Farmers choice, Keainvest holdings ltd, Hurlingham butchers and Dam View. In the international arena, the most important importers of Kenyan live animals and meat are Libya and Egypt in North Africa, and Middle East countries including Bahrain, Jordan, Iran, Oman, Qatar, United Arabs Emirates (UAE), Saudi Arabia and Yemen. Another major importer is Mauritius.

The **key drivers of market changes** taking place in the sub-sectors of fruit, vegetables, meat, and dairy products are consumer "pull", policy "push" (including liberalization, regionalization and globalization), urbanization, commercial opportunity, food standards, foreign investment, environmental awareness, changing urban habits, tourism and social welfare. Considering the world scenario in the context of urbanization, the twentieth century witnessed a rapid population growth. The global proportion of urban population increased from a mere 13% in 1900 to 29% in 1950 and reached 49% in 2005 (UN, 2005b). Kenya urban population has also continued to increase with 1999 census estimating it at 19.3% (Republic of Kenya, 2001).

The key drivers of market changes have caused the spread of dynamic modern retailers, wholesalers and food processing businesses. There has been increased concentration of supermarkets and agri-food processors in the country. Supermarkets are continuously emerging as key outlets for fresh fruit, vegetables, meat and dairy products. The sale of fresh fruit and vegetables in supermarkets is increasing and slowly spreading out of Nairobi's middle- and upper-class areas into poorer areas and rural towns. In 2004, there were 204 supermarket outlets in Kenya and there were 11 hypermarkets (Neven and Reardon, 2004) up from 200 and 10 supermarkets and hypermarkets respectively in 2000 (Stamoulis, 2003). Nevertheless, despite the growth in concentration of the formal channels, fresh fruit and vegetables are still mainly (93%) marketed through traditional channels rather than the modern system.

The **key demands and issues of modern market chains** in Kenya revolve around issues to do with consistent supply, quality standards, freshness, hygiene, quantity, variety and reliability. An increasing characteristic of the dynamic markets is semi-prepared (e.g. French beans, carrots and baby corn), quantity standardization (e.g. in potatoes) and pre-packs (e.g. apples and passion fruits). Due to increased nutritional awareness among the urban dwellers, concomitantly the demand for fresh fruit and vegetables has increased. In selecting suppliers, supermarkets, hotels, groceries and hospitals consider factors such as level of trust, traceability, feasibility, prices, proximity, reliability and potential for production in terms of quantity and quality. They are biased to procuring from large and medium sized growers because they have irrigation facilities to allow for year round production, mobile phones to access market information and means of transport to save on transaction costs, and a bank account to allow for payment through bank transfers. Participation of small-scale farmers alone is seen only with commodities that are not required in large quantities such as dhania, cauliflower, turnips and beetroot.

On **livestock**, the suppliers that qualify to sell to sophisticated abattoirs such as KMC may be individual livestock producers, organized groups of farmers, established livestock traders, or ranchers. However, they must fulfil some conditions such as branding of animals, certification evidencing free from trans-boundary diseases, authentication of vaccination records, clinically examined for mucosal diseases (e.g. foot and mouth) at the point of loading, movement permit, supply on order or agreed schedule, no objection certificate, supply at least 10 heads of cattle or canter-load in case of sheep and goats, transport not on foot unless through designated stock routes and animals be treated 30 days before delivery.

The meat sold in the high value markets such as supermarkets are characterised by some degree of value addition through the cut, processing and packaging. Common forms to which meat is sold in supermarkets are meatballs, minced meat, samosa, fresh prime cuts and canned beef. The products are hygienically packaged to satisfy the consumers' preference. This too increases the appeal for the products.

On **dairy**, the leading processor is KCC with a capacity of at least one million litres per day. KCC is currently offering the highest milk prices (18% above market rates) but at the same time it is demanding the highest quality of milk from farmers. Some of the standard measures of milk quality are alcohol test, density and butter fat content. While the alcohol used in alcohol-test by other processors has concentration of 68-72%, KCC recently raised this to 80%. This was done so as to conform to quality guidelines issued by East African Community (EAC). Adherence to the standards consequently promotes access to KCC products in the regional and international markets. To achieve and sustain these standards, farmers would have to improve on animal husbandry as well as improve the handling and storage of milk before delivery to processors.

In regard to **poultry**, high value markets are airports (airline catering), supermarkets and big hotels. The markets demand processed poultry and hence the need to have processing machines, cold rooms and add value. Traceability is very crucial in poultry targeted for the high value markets especially with the scare of Avian flu in 2005 across many continents including Africa. The airport market demands the highest quality of chicken where the main quality parameters are bio-security (prefer disease free chicken), antibiotics level at time of sale (prefer chicken free from antibiotics), age (prefer 35–40 days old chicken) and taste. Airports demand frozen pasteurized eggs. Poultry processing facilities require high capital investments hence are not affordable to small-scale farmers unless through innovative approaches. Organized farmers are however succeeding in penetrating high value markets, for instance, the Makueni farmers group is processing and selling chicken to Nakumatt.

Alongside the market changes characterizing the fresh fruit and vegetables, dairy, meat and poultry sub-sectors, the **supply side is increasingly adjusting** in terms of adoption of good agricultural practices, increased investment in systems such as irrigation and refrigeration, increased professionalism, more green houses and increased distribution of information, educational and communication materials. Most retailers have upgraded their premises with air conditioning, better lighting and display. The high value markets are increasingly sourcing directly from producers as opposed to middlemen thereby enhancing traceability and quality through shortened supply chain that also promote freshness of the produce. The range of products available in the formal (supermarkets and groceries) markets has also increased. There is a growing preference of organically grown products as opposed to those conventionally grown. In the poultry sub-sector, the safety and traceability factors have led to a shift in production systems to secure lucrative markets; farmers are shifting from free range to intensive systems of production. Good records showing details such as feeds, drugs, vaccines, source of chicks and technical support received, which characterize intensive systems, are increasingly required.

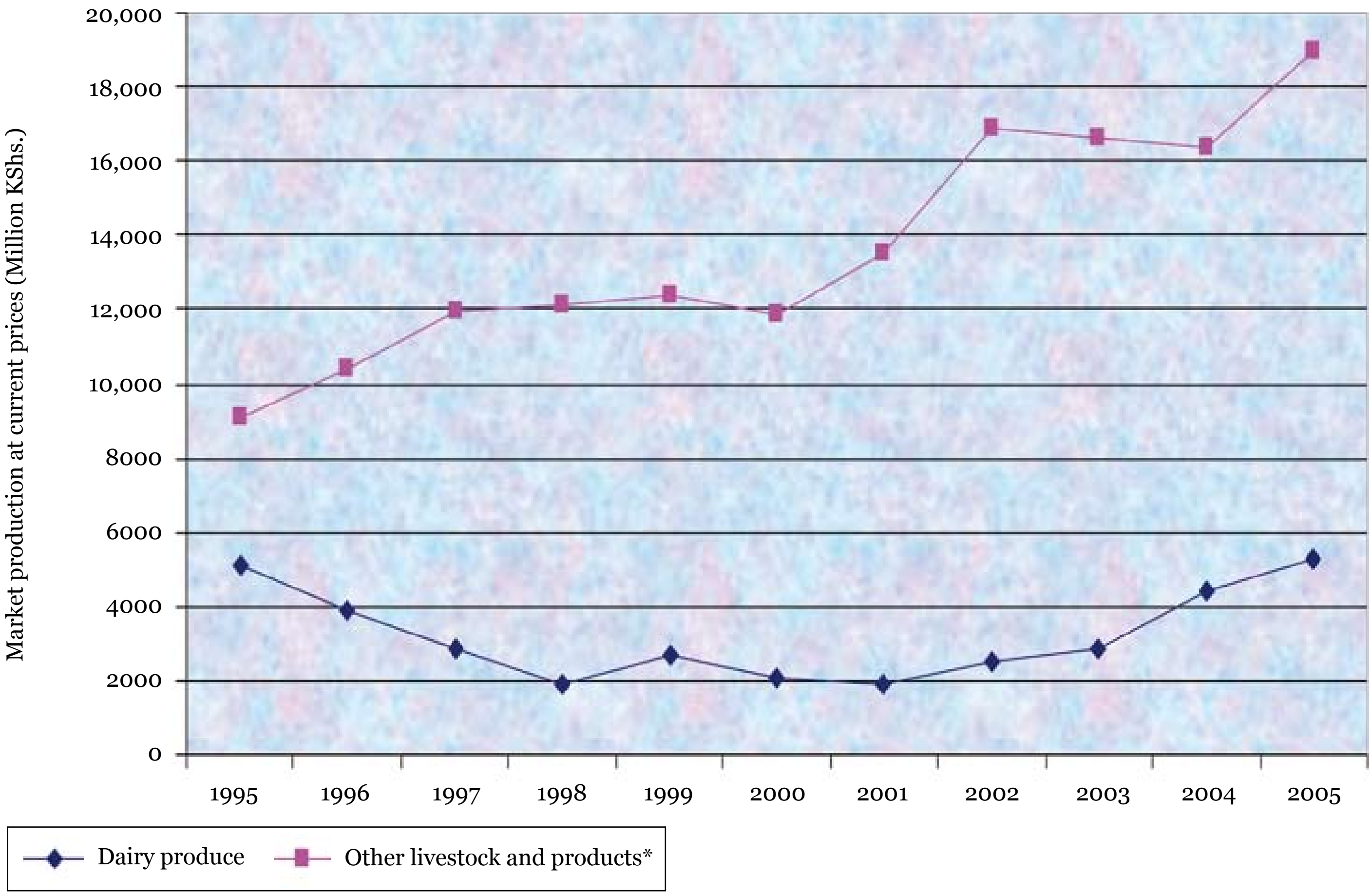
Regional and International Markets and Linkages with National Channels

Horticultural crops have become Kenya's main agricultural export. The export boom in vegetables and flower has been dominated by foreign affiliates' production. Horticulture exports have grown rapidly in recent years, exceeding coffee exports in 1999 and tea in 2003. Cut flowers represent the largest share of volume (46%), followed by fruit (37%) and vegetables (17%). Sales are in most part to Europe, accounting for 95% of fresh produce exports. Horticulture has increasingly continued to be one of the major foreign exchange earners in the Kenyan economy contributing 23% of total export earnings in 2005 (Economic survey, 2006). There was a general increase in exports during the decade, 1995 to 2005. The quantity of exported fruit increased by 34% from 13.9 million kg in 1995 to 18.5 million kg in 2005. On the other hand the quantity of exported vegetables increased by 122% from 28.5 million kg in 1995 to 63.4 million kg in 2005. In 1992, nearly 75% of fresh fruit and vegetables shipped from Kenya was from small-scale farmers. However, by 1998, 40% of the produce was grown on farms owned or leased directly by importers in the developed countries; another 42% was produced by large commercial farms while small-scale farmers produced a meagre 18% (Oli, 2005). This is an indication that the dynamic international markets (mainly supermarkets in Europe) are favouring commercial farmers that are able to swiftly adjust to their quantity and quality standards.

Kenya being a member of the EAC and the Common Market for Eastern and Southern Africa (COMESA), has witnessed increased flow of products to and from the member countries. For instance most apples, grapes, and oranges to leading supermarkets in Kenya such as Uchumi, Nakumatt and Tusker Mattress are sourced from South Africa. Anecdotal sources indicate that South Africa is able to supply fresh fruits and vegetables throughout the year even if the production is seasonal due to its advanced technology as compared to Kenya and its neighbours. South Africa has refrigeration facilities, which can store some produce for the entire year. In the international context, Kenya being a member of African, Caribbean and Pacific States (ACP) gets assistance in the form of training and information on markets and technology. Projects like those of the Centre for Promotion of Imports from developing countries (CBI) of the Netherlands have benefited both the small-scale farmers and the exporters.

In regard to the **dairy** sub-sector, the value of marketed dairy produce has shown a positive trend since 2001 (Figure 1). According to Economic Survey 2006, the exports of dairy products more than doubled from 3,150 metric tonnes valued at Ksh 196 million in 2004 to 6,557 metric tonnes valued at Ksh 351 million in 2005. The quantity of processed milk increased by 18.7% from 192,830 thousand litres in 2004 to 228,800 thousand litres in 2005 (Economic survey, 2006).

Likewise, the output of cheese, butter, ice cream, sausages, pork, mutton and goat meat all rose. The main factors behind the growth of meat and dairy industry include: the increasing role of KCC in processing milk, favourable weather conditions in some major milk producing areas, and expansion of the regional market for Kenyan dairy products.



Sources: Economic survey, various years. *Other livestock and products comprise of cattle and calves, chicken and eggs, and others.

Figure 1 Marketed Livestock and Livestock Products in Kenya

In relation to dry milk powders, there are two categories whole milk powder and skim milk powder. Dry milk powder in general accounts for 44% of Kenya's total volume and value of milk imports, which include also milk cream, infant milk, butter and raw milk. Dry milk powder is a substitute product to raw liquid milk produced and marketed domestically. Over the period 1995 to 2002, imports of dry milk powders were lowest in 1996 at about 0.8 million tonnes, rose to a high of about 3.8 million tonnes in 1999 and decreased again to a low of 0.9 million tonnes in 2002 (FAO, 2007). In the absence of domestic stocks of dry milk powders, imports are required to meet domestic requirements during and soon after the dry periods. Another factor behind the surge is the consequence of the implementation of liberalization policies.

On **poultry**, over the period 1995-2004, the annual import of chicken meat has been below 200 tonnes however this saw an abrupt rise to 560 tonnes in 2005.

The key demands and issues of regional and international trade or export markets especially in regard to **fresh fruit and vegetables** include the need for traceability, quality, safety, sanitary and phytosanitary standards and maximum residue levels. At the regional level, plans are underway to harmonize the agricultural standards. For fresh fruit and vegetables, the exporting to Europe demands adherence to Euro-Retailer Produce Working Group Good Agricultural Practices (EurepGAP) requirements, these being private standards set by member retailers in Europe.

The regional and international market for **meat** also has some specific demands and issues. Meat for export from Kenya must have been derived from animals slaughtered in an approved abattoir, designated for export and under regular veterinary supervision, fully eviscerated and deboned, chilled for 24 hours and at least pH <6.0, processed to ensure destruction of Foot and Mouth Disease (FMD) and Rinderpest viruses, and must come from disease-free zones.

The regional and international markets have **spillovers and linkages with national commodity market channels**. Some of the exporters of fresh fruit and vegetables such as Sunripe and East African Growers also supply to the local high value markets such as supermarkets. This implies flow into local markets of products grown as per EurepGAP standards. Therefore, although the EurepGAP requirements target the export market, there are some positive spillover effects on the local market, especially the supermarkets where exporters sometimes supply the high-quality products. The local consumers therefore also get access to products of EurepGAP standards. Institutions sometimes procure either directly or through brokers some of the high-quality products produced under EurepGAP demands. Some of the quality standards set by EurepGAP and those set by the local private sector, including supermarkets, hotels and hospitals, are more or less the same, an indication that the formally clear distinction between the local and export markets is becoming blurred.

Implications of Market Changes to Procurement Practice and Models of Innovation that Enhance Inclusion of Small-Scale Producers in Dynamic Markets

The market changes have had implications on the procurement practices of supermarket chains as well as hotel chains, fast food chains and other institutions. Apart from products that have a one-day shelf life that are delivered directly to the retail branches, the procurement of the other products is usually centralized or through distribution centres. Further, apart from products required in small quantities such as Asian vegetables that are bought from individual small-scale farmers directly, the rest are bought from medium or large-scale farmers or from organised small-scale farmer groups. The organisation of small-scale farmers and linkage to the market is sometimes facilitated by support agencies such as Farm Concern International (See Box 1), Horticultural Crops Development Agency (HCDA), Horticultural Development Centre (HDC), Kenya Agricultural Research Institute (KARI) and Kenya National Federation of Agricultural Producers (KENFAP). The modern procurement system characterising the high value markets normally bypass the brokers and other middlemen thereby reducing transaction cost and minimising the deterioration of product quality. Unlike supermarkets, fast foods do not sell fruit although they sell juices. Procurement by fast food chains varies from one to the other, for instance, Innscor Kenya ltd sources its vegetables from a preferred supplier (a family business - Western green grocer), Steers sources from a broker while Kengeles sources from green grocers and traditional markets in the vicinity of their local branches. The suppliers of meat to the fast food chains are KMC, Alpha fine foods ltd and Dam View while the sources of poultry are Kenchic, Alpha fine foods and supermarkets.

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Box 1 Innovation Linking Small-scale Farmers of African Indigenous Vegetables to High Value Markets in Kenya

Small-scale producers of indigenous African vegetables were usually excluded from the chain supplying lucrative outlets largely because they could not satisfy the stringent conditions characterizing the markets. The main standards particularly by supermarkets were that the indigenous vegetable units (bunches) supplied to them be: clean, fresh, neat, not attacked by insects, appropriate length (between 12 and 18 inches), right quantity (about 600gm per unit), harvested before they flower or develop seeds and the supply has to be consistent. The majority of the small-scale farmers practiced subsistence farming and brokers exploited the few that marketed the indigenous vegetables. However, through the innovation of collective action by farmers coupled with support from an NGO, Farm Concern International, and efforts by government, they managed to turn around the situation and qualified as preferred suppliers to leading supermarkets in Kenya. They managed to by-pass the brokers thereby reducing the chain actors to farmers, transporters and supermarkets.

The innovation comprised of (a) formation of marketing groups (each with about 25 members) by farmers under facilitation of an NGO, (b) training of farmers, market research and market linkage by the NGO, (c) provision of technical support, and (d) sensitizing the community on nutritive value of indigenous vegetables by the Ministry of Agriculture, Home Economics Department. By transforming from subsistence production to farming as a business, farmers formed business support groups that were successful due to factors such as: good governance; an ingrained culture of farming; commitment; access to technical advice; integration into necessary support services; regular and predictable incomes; transparency and accountability; support and backstopping by an agency.

The farmers successively satisfied the conditions of the high value markets hence benefiting from high prices and by-passed the middlemen and merchants altogether. The higher prices in the high value markets compensated for the higher production and post-harvest costs that characterize commercial farming rather than subsistence. On average the farmers in the innovation made 55% more margins than farmers selling through other outlets. For sustained inclusion of small-scale farmers in the high value chain, it is important to maintain training on good agricultural practices and requirements of the dynamic markets including quality and quantity standards, as well as continue to promote collective marketing.

Public sector policy and role

Some of the market changes have emanated from Government's efforts through national strategies and policies. The Kenyan Government's Economic plans are stipulated in its Economic Recovery Strategy for Wealth and Employment Creation (ERSWEC). According to the strategy, the agriculture sector is the growth sector, which is most likely to play a central role in reducing poverty and increasing food security. Within the livestock sub-sector, the Government proposes to increase investments in animal health services with the objective of preventing disease outbreaks and improving the quality of services.

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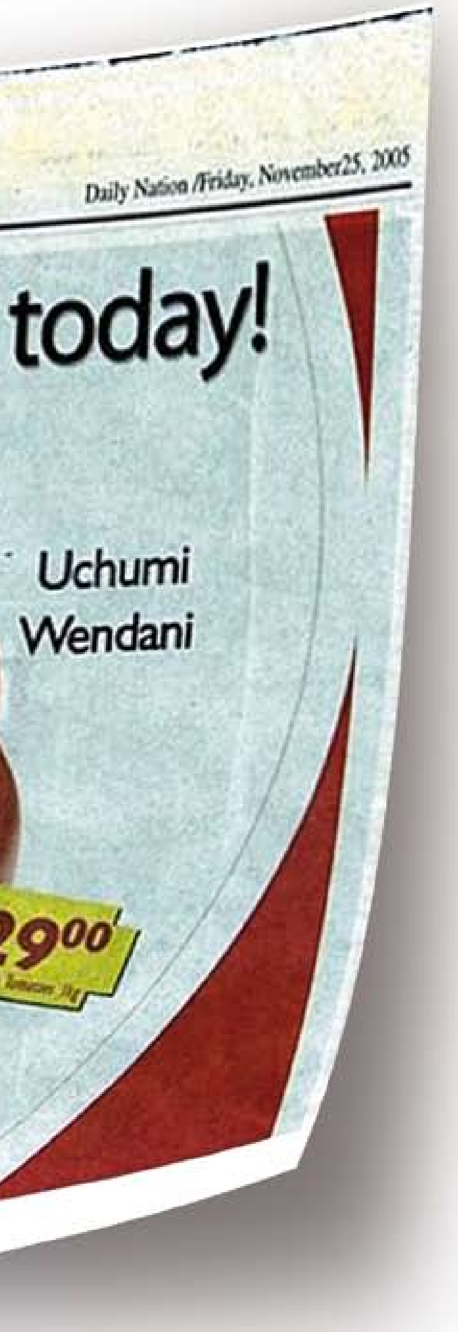
Additionally, the Government intends to improve marketing possibilities and expand access to water services and other rural infrastructure. It is also the intention of the Government to provide adequate security especially in the ASAL's, which periodically are areas of conflict amongst communities competing for resources. According to Strategy for Revitalizing Agriculture, ASAL's potential is not effectively utilized due to the low productivity of the production system, poor infrastructure for marketing of livestock and delivery of services amongst others.

Foreign Direct Investment (FDI) regulations and regional policy are also linked to the market changes. The three main factors that promote FDI in Kenya are people, market access and opportunities (UN, 2005a). The Kenyan workforce has been described as skilled, hardworking and enterprising. Investing in Kenya provides investors with access to EAC since 2005 when the region became a customs union. Next steps in the integration process include setting up a common market by December 2007, adoption of regional currency by September 2009, and achievement of a political federation by 2013. Kenya is also a member of COMESA. EAC and COMESA markets have circa 100 million and 385 million consumers respectively (ibid). As a member of the ACP, Kenya exports have privileged access to European Union and to United States under the provision of the African Growth and Opportunity Act (AGOA). Kenya has ideally well suited climate and soil in some parts of the country. These create opportunities for further development of agricultural produce including for export. Kenya offers several investment incentives including; allowance on plant machinery, building and equipment; carrying forward losses to be offset against future taxable profits, and remission from custom duties (KIA, 2005). To drive investment up in Kenya and with the goal of



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making the country a destination of choice for investors, the Government has suggested setting up an independent vetting unit in Treasury to harmonise the issuing of business licences.

The level of public sector funding for agricultural research and technology has seen a decline from US$1000m in 1994 (based on 1993 international dollar) to US$78m in 2000. This may impact negatively on the competitive position of the sector.

Emerging Implications for the Small-Scale Producer and Potential Opportunities for Public and Donor Intervention

For small-scale producers to meet the conditions of the high value dynamic markets, they require technology, financial capital, human capital and organization.

Support to collective marketing If small-scale farmers were to promote and sustain their inclusion in the local dynamic chains, they ought to satisfy the conditions demanded by the markets. Given their meagre resources however, they may not succeed in doing so unless they pool the resources together and market their product as a group. For instance, a farmer with three heads of cattle would not qualify to market through KMC but if he is joined by a few other farmers they could satisfy the criteria of the ten minimum heads required to sell through this channel. Pooling meagre resources may enable farmers to accumulate funds for capital investments. Collective marketing would benefit farmers through reduced cost from economies of scale and would improve their bargaining power. By organising themselves into groups such as cooperatives or producer organisations, the farmers can obtain credit facilities to enable them to purchase technologies necessarily to successfully adhere to the stringent quality and safety standards demanded by the dynamic markets. They can also benefit from information, training and start-up funds provided by public and private sector development initiatives.

Support to ensure EurepGap compliance In order for farmers to continue participating in the fresh fruit and vegetable export markets especially in Europe, they ought to adhere to EurepGAP guidelines. To sustain access to the markets, small-scale farmers would be required to market as a group registered by Government; construct farm structures as specified in EurepGAP standards; ensure traceability by keeping proper records of all farm activities; follow GAP including observe harvesting hygiene and appropriate produce handling; keep records of complaints and corrective actions taken; and be EurepGAP certified.

Capacity building and market information Public and private sectors and NGOs could promote small-scale producers' access to the dynamic markets by continuously providing information and training on the new requirements and standards demanded by the dynamic markets. Farmers that are unable to meet the quality and quantity standards demanded by the markets are excluded from the chain. Training on scheduled production and advice on which crop to grow and timing along the year are important in enhancing year round supply and in avoiding loss due to over supply. It is essential to enhance the capacity of farmers including building a market intelligence capacity and designing marketing strategies as well as providing support to strategic alliances with market entrepreneurs and consumer groups.

Access to infrastructure and technology The donor community and government could support small-scale farmers' access to the dynamic markets by initiating and supporting projects that promote access to water, which is essential in enhancing all year round production and supply especially of vegetables. Support to research and development and dissemination of productivity-enhancing technologies to boost small-scale producers' ability to attain volumes required by the dynamic markets is a prerequisite. Further disease control programmes including de-worming, vaccines and selective breeding as well as support for the rehabilitation of holding grounds would promote the selling of safe and clean animals and meat.

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For further information contact

Protase Echessah
Regional Advisor
Resource Centre for Rural Development (RRD)
Embassy of Sweden
Nairobi
Kenya
T +254 20 4234000/33
protase.echessah@foreign.ministry.se

Bill Vorley
Regoverning Markets Team Leader
International Institute for Environment and Development (IIED)
3 Endsleigh Street
London WC1H 0DD
UK
T +44 (0)20 7388 2117
bill.vorley@iied.org

About the authors

James K. Nyoro is the Director of Tegemeo Institute of Egerton University, Kenya. Email: jnyoro@tegemeo.org

Isaac K. Ngugi is a Research Fellow with Tegemeo Institute of Egerton University, Kenya. egerton@tegemeo.org

About the series editor

Felicity Proctor is the outreach leader for the Regoverning Markets Programme and a Visiting Fellow at IIED, UK. felicity.proctor@iied.org

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