Bridging the Gaps in the Kaong Subsector

Ivan Idrovo and Marian Boquiren
SDCAAsia

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The United States Agency for Development’s (USAID) Microenterprise Development Division has been funding programs in microfinance and business development services (BDS) through the Implementation Grant Program (IGP) since 1995. As of 30th September 2004, over 90 grants have been approved for a total life-of-project funding greater than 100 million dollars. The current IGP-BDS grantees are an impressive group of organizations and projects that: cover almost every geographic region, consist of numerous value chains, use various approaches, and contain enormous potential to make a positive impact. These programs present an important learning opportunity on how to improve the design, implementation, and impact of BDS programs.

The USAID Microenterprise Development Division, in an effort to establish a participatory learning process, initiated a learning network for the IGP-BDS grantees. The SEEP Network, a non-profit organization in Washington, DC, is the secretariat for the IGP-BDS Learning Network. The SEEP Network provides resources for the IGP-BDS grantees to conduct technical exchanges, hold virtual discussions, organize an annual meeting, and learn about different approaches and tools that are being used in the various IGP-BDS grant programs. In addition, The SEEP Network generates opportunities for: peer exchanges, collaborative case studies, and conference participation for IGP-BDS Learning Network participants.

The goal of the IGP-BDS Learning Network is to be an excellent technical resource for the participants of the IGP-BDS Learning Network, furthering their program and organization objectives. Through the IGP-BDS Learning Network, lessons on sound practices will be captured and disseminated to the wider microenterprise development industry.

The IGP-BDS Learning Network was officially launched during a meeting organized by The SEEP Network and held in New Delhi, India in December 2003. This Learning Network identified the following three learning themes, which frame the common challenges of the IGP-BDS Learning Network participants, and are aligned with the market development goals of the IGP-BDS grants.

1. How to effectively manage the market facilitation role and tasks across a range of market settings and market problems.
2. How to build win/win business relationships between MSEs and other key market players.
3. How to effectively stimulate demand for business services.

Each IGP-BDS grant operates on a performance basis, tracking progress against targets established at the outset of the grant. The semi annual reports also provide qualitative narratives that link programmatic performance to the overarching IGP-BDS Learning Network’s agenda. The agenda aims to understand how to harness the power of increased MSE participation in growing markets to achieve positive and lasting development outcomes.

Six IGP-BDS Learning Network case studies have resulted from the first two learning themes. These cases were written against a set of guidelines adopted by the IGP-BDS Learning Network. These six case studies have initiated a process of learning linked to useful and practical outcomes. In the near future, the IGP-BDS Learning Network plans to: develop diagnostic tools that manage and track performance, document learning against current and future learning themes, and distill lessons on the links between better practice and performance.

- Marshall Bear, IGP-BDS Learning Network Facilitator
- Jimmy Harris, Deputy Director, The SEEP Network
- Jennifer Hansel, Program Associate, The SEEP Network

SDCAsia (formerly Swiss Contact Philippines) is working to help small-scale processors of fruit and vegetable products in Mindanao enter higher value markets by establishing commercial linkages with established processors and vendors. SDC is working with processor and wholesalers to stimulate demand for Mindanao-processed products through trade fairs and market information in the metro Manila area and is working to differentiate the newer products with innovative marketing approaches (e.g., using clean and hygienic processing practices as a marketing tool). SDC is facilitating sustainable market access and upgrading services by embedding these services within commercial transactions between small scale farmers and processors. SDC is also strengthening horticulture cluster in Mindanao utilizing mentoring and networking tools.
The Market Context

Indigenous Kaong Semi-Processors

The indigenous communities of Davao del Sur are made up of various tribes, the majority of which are Bagobos. The Bagobos are a proud people with a strong social structure that has enabled them to blend well with the main political body of the Philippines while retaining many indigenous customs, beliefs, and values.

Many Bagobos have suffered dislocation due to the loss of ancestral lands and the effects of communist and Muslim insurgencies which are more pronounced in Mindanao than in other parts of the country. These semi-processors are generally located in uplands, accessible only by trail. Non-farm income, such as kaong semi-processing, is crucial to Bagobo households because it helps smooth the flow of income over the crop production cycle and spreads income risk. Ownership of trees such as the sugar palm, usually through group property rights, represents a high share of Bagobo capital assets. Harvesting and selling of another person’s kaong is considered stealing and proper fines must be paid. When households are in dire need of money trees can be used as collateral or even pawned.

Harvesting of kaong is usually done by male members of the household, which entails climbing up the palm and cutting off bunches of fruit. In the past, women primarily performed the semi-processing, which involves cleaning, boiling of the nut, pitting, and soaking of pitted seeds in water. (please see attached value chain). At present, male household members have also become active in semi-processing. When the SDCAsia program started, there were only about 40 households in the business of kaong processing. At present (September 2004) there are 250 households, which derive, on average, 40 percent of their monthly income from kaong processing.

The Kaong Market

The main features of the kaong fruit market, as seen from the perspective of the upland communities of Davao del Sur, are summarized in Annex 2.

SDCAsia Project

The goal of the SDCAsia program is to increase the income-earning capacity of resource-poor entrepreneurs in Davao del Sur by facilitating their access to bigger, more lucrative markets for semi-processed kaong fruit. Given the characteristics of the Bagobo communities and the environment in which they operate, the project team, in consultation with various community-based stakeholders, adopted a strategy to:
strengthen the semi-processing activities of Bagobo communities rather than immediately move up the value chain and produce end–products, and

build on the traditional trading system, meaning that semi-processors do not deal directly with Manila- and Davao-based processors, but rather, with community-based market intermediaries.

The team assessed that it would require more time to fully develop the capacity of semi-processors to produce end-products than semi-processed fruit. The investments required for end-products were, moreover, beyond the capacity of both the semi-processors and the community-based traders. The focus on semi-processed products served to increase the income levels or, at least, sustain the economic activity of the indigenous communities.

The decision to work via intermediaries was based on the latter’s experience in dealing with relatively bigger enterprises and “city people,” basic minimum infrastructure, and transaction costs that were either low and/or could be spread among other cash crops carried by the intermediaries.

Principal Market Relationships

The project team identified the following market relationships to be most crucial in bringing resource-poor enterprises to the mainstream market:

- relationships between kaong semi-processors and community-based intermediaries; and
- relationships between community-based intermediaries and the buying agents of processors.

Facilitating More Equitable Market Relationships

Drilling Down

Market research and gathering feedback play an important role in facilitating the development of win-win relationships in the kaong market. The analysis and use of market data gains value as information feeds into the development process, which increases confidence and decreases risk. The primary tools being used in market research are (a) use of secondary market info; (b) key informant interviews, and (c) informal group discussions.

Information gathering involves understanding:

- the nature of the kaong market and value chain and how semi-processors are currently served by them
- market structure, players, and their dynamics vis-à-vis the market position of the semi-processors
- the indigenous culture and trading system, including governance.

Recently, SDCAsia identified a good market for kaong vinegar, an end-product suitable to the capabilities of the Bagobo communities. Product development is in progress and the product is being market tested locally. The building of trading/marketing networks is ongoing.
Based on the information gathered, the project team implemented the following steps:

- Identified and selected market channels and links that would provide opportunities for indigenous communities to penetrate the mainstream market and get larger share of the value within the chain
- Identified critical constraints and opportunities of selected market channels/links, as well as requirements or standards that should be met
- Assessed skills and know-how required by indigenous communities to be able to meet requirements and how these can be accessed by indigenous communities
- Matched requirements to the resources, objectives, and existing activities of the relevant market players
- Selected entry points and champions—an initial core set of market players with whom the SDCAsia program could work.

The team discussed the feedback of different market players with the players themselves, seeking to identify win-win solutions to problems. At this point in the project, the various parties preferred that SDCAsia play the role of mediator to resolve dissatisfaction, new issues, and constraints in market relationships.

**Strengthening Market Linkages**

Support for market linkages is provided primarily to (a) expand markets of the different links in the kaong value chain, (b) ensure a continuous flow of orders to the Bagobo communities, (c) provide the impetus for the various players to work closely with each other, and (d) encourage the upgrading and optimization of the value chain by triggering market demand. Project interventions are currently directed towards traders and processors.

The SDCAsia program actively brokered the first supplier agreement between the community enterprise and the processor to show the viability of partnerships, overcome historical distrust, and spark the first significant orders (and thus motivate business development training, which the majority of processors had never undergone). The delivery of specific services such as production processes training and quality control by the processor was also included in the partnership agreement.

Making the first marketing agreement work meant that the project team had to accept responsibilities passed on to it by both parties (e.g., ensuring delivery and payment), which included filling the skills gaps of relevant parties. This phase of the project gave the team the opportunity to learn more about kaong trade, although it felt that its role of filling up weaknesses of both parties was unsuitable for sustainable operations.

Although the project successfully achieved its short-term objective of improving semi-processing skills and higher prices for semi-processed kaong, it became evident that the capacity of kaong processors to deliver business development services (BDS) to communities was insufficient to improve the market position of the semi-processors. Linkage and close partnership with a mainstream business can jumpstart the development process, reduce the costs of bringing the products to the markets and act as a catalyst in improving the efficiency of the supply chain (at the community level). But linkages alone and the BDS provided by buyers are not enough to bring enterprises into the mainstream market. Often times the main prerequisite for a subcontracting agreement is for potential subcontractors to have a certain acceptable performance level. As such, the project team found it necessary to: a) develop a range of services with market requirements as the starting point that will address the gaps; and b) build the indigenous capacity to provide and deliver the BDS by themselves, particularly those that relate to skills that affect improvements in the community level supply chain, and consequently, enable them to meet market requirements.

In addition to skills constraints, the project suddenly faced stagnant markets in Mindanao (the principal market of the processor) due to bombings in Davao City and nearby provinces. With the unstable peace and order activities, commerce significantly slowed down. Fortunately, the project was already in discussion with a Manila distributor which facilitated continuous sales for the Davao processor and consequently the indigenous communities.

The project then shifted to concentrate on building up a BDS system in the Babogo communities and, consequently, strengthen their market position. The BDS system builds on existing trade/marketing structure to facilitate the flow of BDS to all players in the community supply chain. Under the system, marketing intermediaries at every level are tapped and trained to handle typical technical and business concerns of microenterprises. In the kaong communities, for instance, the contractors provide market-based quality specifications as well as share some technical and market info to the central buying agent in the community. The central buying agent
then shares these with the pool of trainors\(^2\) from the cooperative. The cooperative organizes the training for the microenterprises (members and non-members) and also operates the common service cum marketing facilities. Training sessions are conducted both in the common service facilities center and in the place of the barangay assemblers. The sessions also became forums to discuss and find solutions to common concerns and potential market opportunities. Coaching and mentoring services and quality control services are provided by the barangay assemblers\(^3\) to their group of suppliers and the transportation group. In other words, the BDS delivery system follows the flow of the products. Knowledge and skills upgrading forms of BDS and marketing service are paid via mark-ups while tangible services (e.g., use of common service facilities, raw materials) are paid in cash with various payment schemes.

The project team also adopted a passive role in brokering transactions. Market development activities thus focused on promoting product quality and food safety by making buyers aware of the positive changes implemented by communities, providing opportunities (formal and informal) for the different players to interact with each other and supporting the participation of processors to marketing events.

To date, the shift in activities appears to be working well. Linkages induced by market forces are becoming more spontaneous. More buyers are coming to the kaong market in Davao del Sur, including buyers from Manila. The main role of the program is now to track the progress of orders and negotiations between buyers and the communities, including discussions of new issues and constraints. Processors provide the program with feedback on their transactions, which is used as the basis for capacity building for the intermediaries. Intermediaries also discuss the problems they have encountered with the project team, which provides them assistance in defining solutions and developing new opportunities.

Market relationships facilitated by the SDCAsia project have not yet reached the point where the different parties can discuss relationship issues and constraints openly with each other. However, a certain degree of openness has been established.

The entry of more buyers both from Davao and Manila has provided the Bagobo communities more choices, and hence, more power in the market. Community intermediaries must now learn to use this power in a positive way, i.e., to create long-term, win-win transactions, ethical trading relationships, customer loyalty, and customer retention.

Competitive forces (i.e., additional buyers) are enabling traders to offer better terms and conditions to semi-processors, as well as to upgrade their role and function (e.g., pick-up of products at buying stations, packaging materials, market info, assistance in opening bank accounts, etc.), thus improving the efficiency of the supply chain. Similarly, processors or their buying agents are offering relatively better prices to traders, as well as added services (e.g., assistance in opening bank accounts, cash payments, pick-up of products at buying stations, etc.). It has been observed that trader loyalty is stronger to processors who offer additional services.

**Strengthening Supply-chain Governance**

Many of the trust issues between traders and semi-processors can be traced to the lack of product standards. At the beginning of the project, for instance, pricing was said to be set arbitrarily. Processors claimed that products produced by the Bagobo communities were of poor quality and required additional re-processing. The main problem was that quality standards were subjective. At the start of the program, the Bagobo communities believed that they were producing products of acceptable quality, a position which, based on local norms, could be considered correct. To address many trust and transparency issues as well as to facilitate the development of product differentiation the project team facilitated the strengthening of supply-chain governance by:

- strengthening horizontal linkages (identifying and facilitating commitment to common objectives)
- establishing process and product quality standards. The standards and norms were set by key players in the community that were trained by specialists, with input from buyers.
- promoting the benefits of meeting quality standards among the different players. This campaign was primarily directed at barangay assemblers since they are the nearest to suppliers in terms of location and influence.

\(^2\) Consist of fruit processors and barangay assemblers

\(^3\) They collect the semi-processed kaong from their group of suppliers and deliver these to the cooperative
strengthening the capacity of marketing intermediaries in good manufacturing processes and quality-control processes

developing and ensuring the access of different players to BDS services that enable them to match market requirements with quality standards

promoting compliance with product standards via marketing intermediaries at various levels. This process depended to a great extent on a strong “chain leader” in the community (i.e., a community-based buying agent who was well-respected by the semi-processors). The explicit acceptance of the chain leader was very important in facilitating supply chain collaboration.

The effectiveness of collaboration among supply chain actors at the community level, as well as their consequent collective adherence to product standards depends on shared goals and mutual interests. The program therefore offered organizational development support and conducted social marketing campaigns. However, the best trigger for closer collaboration and cooperation has been the pursuit of markets outside the locality.

At present, a clear concept of good-quality product vis-à-vis an unacceptable product (“rejects”) is recognized by buyers and semi-processors. The traders and the Bagobo communities have started to realize the rewards of managing performance and quality along their supply chain. As one trader puts it, 90 percent of the time traders only accept and pay for clean seeds that have been pre-processed well. Sometimes, however, the buyer relents and accepts discolored, poor-quality kaong in consideration of the farmers’ effort. “It would be uncharitable to turn them away after they have carried kilos and kilos of seeds on their back or head for hours,” the trader explained. “I just tell them how to do it better and make sure they understand that next time, I won’t accept poor-quality seeds.”

The trader added that she also requires farmers who bring their kaong to the buying stations to attend “good manufacturing practices” (GMP) training, especially when their kaong are substandard. One time, almost half of the 100 kilos she collected at one buying station were of poor quality. She immediately tasked community-based trainers to conduct a GMP training there. After some time, the GMP sessions bore fruit. The percentage of substandard kaong was eventually reduced to 5 kilos, or about 5 percent, of the total kaong collected.

Lessons Learned

The SDCAsia project offers the following lessons learned:

- The best way to convince mainstream businesses to work with indigenous communities and microenterprises is to present proof that production systems and practices, including product quality and volume, have improved. As soon as the Bagobo communities became known for high-quality, semi-processed products and the capacity to produce required volumes of consistent quality, contractors began to approach the communities without much facilitation on the part of the project team.

- Market relationships must offer tangible benefits to all involved, thus creating an incentive for continued participation and maintenance.

- Facilitating supply-chain governance and continuous dialogue among all parties ensures that mutual objectives of the supply alliance are met and that no one member attempts to benefit at the expense of the others. Third-party facilitation during the formative stages of relationships helps build trust by ensuring that information pertinent to the parties involved is exchanged.

- Facilitating win-win relationships entails in-depth understanding of the nature of the value chain and markets important to resource-poor enterprises, their structure, the different stakeholders involved, their institutions, their dynamics, and the way in which the poor are currently served by these markets.

- It is important to facilitate the process of building market relationships and not engage in core market activities. The facilitator of the project should not be viewed as the “ever-ready savior” of these relationships. However, the facilitator must be flexible and should help the parties find solutions to the problems that arise.
Annex 1:
Moving Kaong from the Mountains to the Cities
## Annex 2:
### Key Features of the Kaong Fruit Market of Davao del Sur

<table>
<thead>
<tr>
<th>Baseline situation</th>
<th>Current situation (September 2004)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Villagers' social networks and access to markets are historically limited to the</td>
<td>Four different market channels have been reached by the project's target groups: local traders,</td>
</tr>
<tr>
<td>town &quot;public market.&quot;</td>
<td>buying agents, Davao-based processors, and Manila exporters.</td>
</tr>
<tr>
<td>According to processors, the quality of semi-processed kaong was very poor and</td>
<td>Semi-processed kaong from the indigenous Davao del Sur communities is acknowledged to be of very</td>
</tr>
<tr>
<td>its sale price was thus low.</td>
<td>good quality by industry players.</td>
</tr>
<tr>
<td>According to semi-processors, product quality was acceptable based on traditional</td>
<td></td>
</tr>
<tr>
<td>local norms.</td>
<td></td>
</tr>
<tr>
<td>The only kaong processor based in Davao del Sur bought from villages on an</td>
<td>Buyers consist of agent-distributors and processors from Davao, nearby cities in Mindanao, and</td>
</tr>
<tr>
<td>intermittent basis (including peak season).</td>
<td>Manila.</td>
</tr>
<tr>
<td>Representatives of Davao-based processors sourced semi-processed kaong only when</td>
<td></td>
</tr>
<tr>
<td>they were desperate for supply.</td>
<td></td>
</tr>
<tr>
<td>Community traders[^4] and buying agents engaged in semi-processed kaong trading</td>
<td>In 2004, production and trading of semi-processed kaong continued even during the supposedly</td>
</tr>
<tr>
<td>only during the peak season.</td>
<td>lean months due to orders from processors. (These orders were destined for export markets and</td>
</tr>
<tr>
<td></td>
<td>institutional buyers, such as restaurants and hotels.)</td>
</tr>
<tr>
<td>The raw kaong nut was a more established traded product. Semi-processed kaong was</td>
<td>Semi-processors and community trading intermediaries now speak in terms of kilos and tons.</td>
</tr>
<tr>
<td>traded in small volumes. This period is now referred to as the &quot;Caltex years&quot;</td>
<td>A Manila-based exporter purchases 10 to 15 tons of kaong every two weeks through a buying agent.</td>
</tr>
<tr>
<td>because semi-processed kaong was purchased in quantities of Caltex containers, not by weight.</td>
<td>Local processors buy an average of 10 tons per month.</td>
</tr>
<tr>
<td>The buying price of semi-processed kaong ranged from US$0.09 to US$0.15 per kilo.</td>
<td>The buying price of semi-processed kaong now ranges from US$0.18 to US$0.26 per kilo.</td>
</tr>
</tbody>
</table>

[^4]: Community traders are also microenterprises. They are the intermediaries between the community of suppliers and the buyer (usually located outside of the locality). They collect the semi-processed kaong and sell these to the city-based buyers.
## Annex 3:
### Baseline, Current, and Future Relationships in the Kaong Market

<table>
<thead>
<tr>
<th>Relationship between Semi-Processors and Community-Based Traders</th>
<th>Relationship between Community-Based Traders and Processors and/or Buying Agents</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Baseline</strong></td>
<td><strong>Current</strong></td>
</tr>
<tr>
<td><strong>Supplier and Buyer Selection/Procurement</strong></td>
<td><strong>Supplier and Buyer Selection/Procurement</strong></td>
</tr>
<tr>
<td>Spot selling and purchasing.</td>
<td>Some semblance of long-term relationships. Each trader has an informal network of suppliers. Traders absorb deliveries and outputs of regular suppliers.</td>
</tr>
<tr>
<td>No prior commitment or orders, but some informal guarantee of future business. Some degree of recognition of past transactions/relationships.</td>
<td>Verbal orders and volume commitments relayed from main buying agent to barangay buying station to semi-processors. However, buying stations and semi-processors still prone to a “better offer gets the supply” attitude.</td>
</tr>
<tr>
<td>Price and payment terms are the main determinants of buyer and seller selection. Information on traders who offer higher prices spreads rapidly within the community.</td>
<td>Preferred suppliers/buyers. Semi-processors manifest higher degree of loyalty to traders who help them improve their skills, offer facilities/infrastructure near their residence, etc.</td>
</tr>
<tr>
<td>Flexible, subjective pricing and payment terms.</td>
<td>Product quality is already an additional consideration to price.</td>
</tr>
<tr>
<td><strong>Relationship between Semi-Processors and Community-Based Traders</strong></td>
<td><strong>Relationship between Community-Based Traders and Processors and/or Buying Agents</strong></td>
</tr>
<tr>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td><strong>Information Sharing/Transparency</strong></td>
<td><strong>Baseline</strong></td>
</tr>
<tr>
<td>Some degree of information sharing on price, cost, and demand from traders, but mostly for the benefit of traders. Information sometimes distorted to serve their interests.</td>
<td>Information shared with respect to demand, both current and potential. Suppliers and traders aware of standards. Purchasing and pricing decisions almost always based on agreed standards.</td>
</tr>
<tr>
<td>Prices vis-à-vis standards are set arbitrarily and accepted by microenterprises in exchange for immediate cash.</td>
<td></td>
</tr>
<tr>
<td><strong>Quality Control/Inspection</strong></td>
<td><strong>Baseline</strong></td>
</tr>
<tr>
<td>Focus on weight or counting number of Caltex containers.</td>
<td>Quality control at buying station. Improved understanding and acceptance of standards among semi-processors. Final weighing at buying station.</td>
</tr>
</tbody>
</table>
## Relationship between Semi-Processors and Community-Based Traders

<table>
<thead>
<tr>
<th>Value-added services/Collaboration and cooperation</th>
<th>Baseline</th>
<th>Current</th>
<th>Future</th>
</tr>
</thead>
<tbody>
<tr>
<td>Some learning and skills transfer, but knowledge limited to local norms and traders.</td>
<td>Close monitoring of production and logistics, as well as final product at delivery. Training and mentoring services by community-based traders to solve production problems. Buying stations set up to reduce transportation costs. Interdependence and partnership. Both parties mutually exploit cost, quality, technical, and/or marketing advantages via collaboration.</td>
<td>Almost non-existent. Some assistance to improve product quality and trader operations. Most buyers purchase products at buying station, allowing traders to maintain decent profit margin. Greater respect now given to weaker party. Some processors feel that there is still a lack of trust on the part of traders, despite significant orders in recent months. Processors also sense a lack of ethics, which makes them hesitant to significantly invest in supplier development.</td>
<td>Partnerships are based on a long-term commitment to cooperate and thus achieve mutually acceptable outcomes.</td>
</tr>
</tbody>
</table>

## Basis of competition/ Market offer

| Price. Abundant supply. | Supply of semi-processed kaong is growing. Quality and price are the most important indicators. | All parties able to transact business under better conditions. Business transacted primarily via differentiation factors other than price. Price and supply availability. | Bagobo communities becoming known for top-quality products. Economies of scale and lower transaction costs are being realized. Quality, cost efficiency, price, dependability, and reliability. Socially responsible trading practices. |