COMMERCIALISING AND PROFESSIONALISING THE MANAGEMENT OF DAIRY HUBS

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Kenya Markets Trust (KMT) is a Kenyan not-for-profit organisation that specialises in market transformation. We work to stimulate inclusive and resilient growth that will lead to a step-change in the livelihoods of millions of Kenyans. We take a long-term approach, staying true to our vision while adapting to the forces that are shaping the markets we operate within such as climate change and access to emergent technologies.

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The dairy sector in Kenya comprises more than 1.8 million smallholder dairy farmers. Developments in the sector span over a period of 90 years and have undergone various evolutionary stages.

The value of Kenya’s dairy industry is estimated at USD 1.4 billion based on the amount of milk marketed with more than two million households believed to be involved at the production level of the value chain, many of whom are rural poor. For these households, dairy is the leading source of agricultural income contributing to over 20% of household income.

The sector comprises of two value chains; formal and informal. The informal market controls an estimated 80% of total milk sold, while formal market accounts for about 20%.

Despite the disparity in size, working with the formal sector offers the greatest opportunities for sustainable value-creating enterprise development.

Currently, milk demand is estimated at about 4.5 billion litres and is expected to increase to 12 billion litres by 2030. Local consumption is expected to grow by at least 2-3% per year driven by population growth, coupled with urbanisation and improvements in household incomes.

There are, however, feasible opportunities to raise smallholder incomes from dairy farming. These include opportunities to sustainably increase farmers’ incomes by boosting milk yield; if more dairy farmers use high quality hay, artificial insemination and veterinary services, yields will rise.

Further, dairy farmers can also stabilise their incomes by raising milk production at times of the year when the general market production levels are very low. Increased demand for milk presents another opportunity for smallholder farmers.
Introduction

There is a growing unmet demand for processed milk and milk products both locally and internationally. Leading Kenyan processors have begun exporting their products and this has created a huge opportunity to sustainably raise farmers’ incomes by increasing their milk yields and quality.

However, there remain systemic constraints related to interconnectivity of various service markets feeding into dairy as well as how the process of formalisation is evolving.

With this, there is a need to work with dairy hubs to improve their effectiveness and efficiency in business operations. Major focus being on business practices that have particular implications to farmers.

Systemic Constraints

Different actors across the dairy sector continue to face key challenges along the value chain including; high cost of production, low adoption of appropriate dairy production technologies, lack of access to markets, poor infrastructure, poor milk quality, and lack of a sufficiently strong market player to regulate and enforce behavior change.

At the cooperative and dairy hubs level, constraints more prominent are to do with poor governance, lack of customer loyalty, and lack of proper management tools for efficient service delivery to the farmers.

On the other hand, smallholder farmers in the dairy sector continue to face challenges of limited access to correct and reliable animal inputs, which in turn lowers production capacity and subsequently their income. Since the farmers are not consistent with the capacities produced for the markets, they are unable to attract competitive prices for their milk.
**Intervention**

In September 2016, KMT and PKF entered a partnership aimed at developing key dairy intervention areas with a view to achieve systemic change in Kenya’s dairy sector. This was to be done through commercialising and professionalising the management of dairy hubs.

The aim of the project was to unlock dairy hub’s potential by transforming them into thriving businesses that offer affordable quality services and better prices to their farmers.

PKF developed a hub management package that sought to unlock the potential of dairy hubs and eventually that of smallholder dairy farmers. The strategy started with a recognition that there have been numerous investments in the dairy sector over the past years, particularly through support from donor funded projects. To a great extent, these investments have been successful in growing demand, increasing production and improving the position of smallholders.

However, the investments have not been as effective in shifting and aligning investments to drive formalisation from within the industry. Specifically, the level of investments from processors to capture informal milk production continues to be inadequate.

In the view of these challenges and constraints, PKF designed interventions targeted at facilitating dairy hub access to alternative and direct milk markets.

**The broad strategy of the partnership was categorised in broad areas of:**

- Developing a farmer loyalty program that includes co-ownership and setting up preferred business models and other services that improve farmers’ livelihood;

- Supporting dairy hub linkages for business expansion and alternative marketing including financial inclusion for debt and equity financing;

- Capacity building hub managers as part of existing strategies to provide guidance on the development of physical structures, relationships with farmers, information and technology to support sale of safe and quality milk; and

- Developing policies and procedures leading to business scale up.
When PKF started implementation, three business models were developed and adopted. Six dairy hubs were engaged after taking them through a rigorous selection criterion.

The models selected were:

**Farmer-led model:**
under this model farmers were to invest in all milk handling equipment and infrastructure and market their milk to the final consumer.

**Investor-led model:**
in this model an independent business entrepreneur was to invest in processing equipment and enters into contract with farmers for supply of milk.

**Mixed/Co-ownership model:**
this model entailed farmers and entrepreneurs developing a business model where both are shareholders depending on capital contributions.
**Results**

The project generated phenomenal results and great gains for the farmers.

For Miharati Dairy Hub in Nyandarua County under the *farmer-led model*, within the engagement with PKF conducted a SWOT analysis which identified poor governance as the greatest impediment towards growth. To address governance and other issues identified PKF facilitated the hub to come up with a five-year strategic plan and developed action plan. To expand production and supplement milk collected from farmers the hub entered into contract with traders who delivers milk to them and after they pasteurize it, they sell direct to their market.

This dairy hub has increased their production capacity from 8,000 litres in 2016 to 22,000 litres per day as at August 2019. Further the hub mobilised farmers recruitment and increased its membership from 3,000 farmers in 2016 to 5,800 farmers as at August 2019.

As a result of improved governance and existence of management tools like strategic plan, the hub attracted funding from GIZ and partnered with Safaricom. In this partnership they were able to develop a mobile base application to manage milk collection and payment. In this application the milk collection clerk keys in farmers information at collection point which is received in the system at the office. All collection records for individual farmers are accumulated in the system which linked is to payment through mobile money and bank transfers.

With an aim of boosting the quality of milk collected, the dairy hub with facilitation from PKF organized and rolled out a farmers training on modern milk handling procedures. The quality was further maintained by purchasing an automated weighing scale which made the collection process effective and farmers experienced reduced wastage, as a result the dairy hub reported to have reduced rejection rates by 5% from around 7% in 2015. Currently only about 2% of farmers’ milk is rejected.
Gakundu dairy hub in Embu County which was facilitated to test the Investor Led Model, yielded great results as well. In 2015 the hub was facing challenges in governance and farmers management. PKF offered technical assistance to the hub and facilitated selection and employed a functional board of directors. The new management was also taken through organizational capacity building. Subsequently through PKFs facilitation, the hub entered into contract with Lattana Dairy Cooperative (processor) in collecting and pasteurizing farmers’ milk. Farmers were able to receive better prices for their milk from the new partnership between Gakundu Dairy Hub and the processor. One of the farmers reported that the price has increased to Kes. 34 per litre as compared to 2015 when the highest they could get was Kes. 28 per litre. PKF facilitated the dairy hub with mobilization and recruitment of farmers, currently the dairy hub has a total of 2000 farmers as compared to 2015 when they were less than 200 farmers.

With the intention of boosting farmers’ production and bearing in mind the limited capacity of farmers to access feed, in December 2017, the hub partnered with Sidai Agrovet to offer inputs to the farmers on credit, this meant that farmers can access feed and other inputs like drugs and minerals on credit from the agrovet, then the hub pays Sidai on the inputs supplied and deducts from the farmers monthly payment through a checkoff system. Most of the farmers appreciate this partnership as it has enabled them to sustain high production capacities. Further to sustaining high production farmers have increased their production, one farmer reported to have doubled daily production from 8 litres per cow in 2015 to 15 litres per cow. This increase was attributed to the sustained access to the inputs.

As reported by the dairy hub farmers loyalty has increased, this was validated by the level of satisfaction expressed by the farmers, who appreciated that the payment process has greatly improved as they are able to receive their payment at the 16th day of each month, this was in reference to times before the processor entered into contract with the hub farmers could go close to 3 months without receiving their pay. This will greatly improve their participation in the markets. Further to this the processor provides credit facilities and advance payment to the farmers on request, the amount is paid back through a checkoff system from the farmers monthly payment. Most farmers as well appreciate this service as it opens opportunities for them to grow production and improve their living standards.
At Kibugu Dairy Hub in Embu County, which PKF engaged to pilot the Mixed/Co-ownership model, this hub was engaged in late 2017 at a time the hub was really struggling with governance issues and mistrust between the farmers and the hub officials. At this time some officials had acquired a loan facility secretly without consulting the members as it was stipulated in the bi-laws. This occurrence had affected the stability of the hub as the farmers couldn’t receive their payment notwithstanding that they constantly supplied their milk. PKF facilitated the hub to institute a functional management and board of directors through continuous capacity building and checks. When the new management took over in June 2018, farmer recruitment was mobilized and commenced immediately and by August 2019 they had increased their farmers to 300 from 20 farmers in 2017.

With improvement in governance the hub procured a mobile based app to manage milk handling. The app is loaded on transporters mobile phones, once they collect milk and weigh from the farmers the volume is recorded on the app under the farmers details and received in the central database by the collection manager. At the point of collection, a receipt is printed for the farmer indicating the volume collected at every point and cumulative collection for the month per farmer. From this system there is increased farmer loyalty since every farmer is able to track their records. There is also increased transparency by use of this mobile based app in management of farmers payment. The mobile application is linked to the farmers telephone numbers and on regular basis they received updates on volume collected cumulatively, total to be paid at the end of month and any deduction that might be applicable. On special occasion the farmers are updated on change of prices.
Challenges

• Access to stable markets and competitive prices remains unachievable for the dairy hubs, regardless of improved processes and unwavering farmer loyalty the hubs are not able to always attract good prices from processors, at times the prices are very unpredictable and fluctuates from high to low, ranging between Kes. 28-34 per litre. This puts the hubs in a position where they can’t offer good and competitive prices to their farmers.

• Despite the project having facilitated settlement of governance issues, it remains an obstacle to smooth operation of the hubs. This is worsened by both insiders and outsiders who have vested interest without farmers welfare.

• The dairy hubs expressed concern of monopoly from the big processors, due to their high processing capacity, these processors sometimes collect direct from the farmers at relative high prices and this affects farmers loyalty.

Recommendations and Opportunities for Scale Up

There needs to be proper policies in place to manage the dairy value chain, this can be achieved by empowering Kenya Dairy Board as this will increase their points of leverage.

County governments should take interest in the work done by dairy farmers, there is minimal support from the county. This can be achieved by for instance factoring the dairy hubs in the County development plans.

There is a big gap in financing for the dairy sector as both dairy hubs and farmers require linkages to financial institutions where they can access credit facilities to grow their businesses and unlock some potential areas like value addition and production of diversified products.

Conclusion

Dairy hubs have a great potential to grow the dairy sector and increase small holder dairy farmers’ participation to formal markets, this will grow the sector, but this can only be reality if the hubs are managed professionally. Unwavering farmer loyalty is key to the success of the dairy hubs as well. There is weak enabling policy environment in the dairy value chain, and this calls for policy makers to consider empowering bodies like Kenya Dairy board so that both dairy hubs and farmers interests are taken care of and are regulated. Growth in the sector calls for participation of both County and National governments in order to cushion the small holder dairy farmer.
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