FARMWORKER PARTICIPATION SCHEMES: CONDITIONS FOR SUCCESS

Philip Nel
Development Bank of Southern Africa

Johan van Rooyen
Director, School of Agriculture and Rural Development, University of Pretoria

Simphiwe Ngqangweni
Research Assistant : School of Agriculture and Rural Development, University of Pketoria

Farm worker participation schemes which give access to farm assets must be viewed in the context of agrarian reform. For South Africa this implies a possible strategy to support land reform programmes. This paper summarises factors which might impact on successful implementation of the model.

PLAASWERKER DEELNAME SKEMAS: VEREISTES VIR SUKSESVOLLE TOEPASSING
Plaaswerker deelnemingskemas in die landbou wat toegang tot boerderybates bied, mag 'n model wees vir agrariese en grondhervorming. Die referaat gee 'n opsomming van faktore wat suksesvolle implementering van die model mag beïnvloed.

1. Introduction

Various models to address land reform in South Africa have been proposed, covering small farmer settlement schemes, communal farming models, contract farming, land rental models, agri-village schemes and a number of variants of participation schemes on privately owned farms between the present owner and farm workers (Van Zyl *et al*, 1994). These participation models however are focussed on more than land distribution per sé as they provide access to farming assets. If the scope is extended from land reform to agrarian reform each of the proposed models will likely be appropriate in a specific set of circumstances.

This paper concentrates on the contexualization and possible application of farm worker participation models[1] as a strategy for agrarian reform[2]. Reference is given to practical considerations for successful implementation in the South African environment. Two models are discussed, viz. the equity participation scheme and the share block model.

2. International perspectives: participation through partnership and joint ventures as instruments for agrarian reform

Joint ventures and partnership arrangements have been common to institutionalise reform in the international plantation sector during the past few decades (Glover, 1984; Sajhau & on Muralt, 1989; Tiffen & Mortimore, 1990). These arrangements have resulted in attempts by transnational corporations (TNCs) to integrate peasants, small growers and workers into the modern agrarian sectors. Attempts have mainly been in the form of public support for contracting smallholders and settlement of outgrowers around nucleus or core farming estates. One of the most successful contract arrangements is the Kenyan Tea Development Authority (KTDA), created in 1964 by the government of Kenya with the support of the Commonwealth Development Corporation (CDC), with finance from the World Bank, OPEC, and the former EEC (Currie & Ray, 1986; Swainson, 1986; Kirk, 1987). Under this system local farmers supply produce while an agri-business firm retains responsibility for technical assistance and marketing. The KTDA arrangement has served to introduce small farmers into more intensive commercial farming and thereby developing them to be financially economically independent. This and other joint ventures also in countries like Swaziland (*cf* Williams, 1985; Levin, 1988) and Indonesia have become vehicles for agrarian reform through broadening access to previous deprived groups, to assets and support systems. Particular land tenure arrangements evolved as response to such access. In South Africa the sugar production schemes are examples where small farmers are accommodated as outgrowers.

Joint ventures and partnership arrangements to accommodate new farmers and farm workers in agricultural enterprise should clearly be viewed in a broader context than land reform per sé. A major reason for this being the importance of providing access to business activities, working assets and appropriate contractural and managerial arrangements in addition to land tenure. Commercial farming in South Africa clearly provides scope for such arrangements.

3. Rationale for participation schemes

Participation models provide participation opportunities for economic empowerment of a particularly disadvantaged group i.e. the farm worker. Primary goals of a new agrarian structure in South Africa would not only be to normalise the distribution of land in society but also to increase rural incomes and access to rural employment opportunities for a growing rural population. It would appear, that, in general, smaller agricultural units and increased agricultural intensification is required (Van Zyl, 1994). Notwithstanding this, it is also likely, however, that large farms will remain a predominant feature in South Africa. With this in mind, it appears logical to seek ways of increasing rural livelihoods and access to land on large scale farms through access and new ownership relations as part of an overall rural restructuring effort (McKenzie, 1993). The participation model proposes the rearrangement of ownership to include the farm workers and thus involve them in the mainstream economy (McKenzie *et al*, 1993).

Models involving the private sector are presently investigated by a task team of the Department of Land Affairs. Fundamentally these models produce a pact between labour, technological and managerial skills whereby the owners of the skills stand to gain or lose, based on performance. Success in a market economy is more likely in a model where the profit motive is applicable to all the production factors rather than a model where the owner of technical and managerial skill is remunerated at a fixed rate (e.g. such as where support on technology and management is provided through a government department or parastatal).

Participation schemes is expected to have benefits for all partners in the project through synergy, and also to the economy at large (Van Rooyen *et al*, 1994), as summarised in the following paragraphs:

3.1 Advantages to the worker

- expected improvement in income;
- greater expected security of employment;
- opportunity to build a capital base for an own venture or future needs. Comments from participants in an equity participation scheme indicated that the scheme resulted in farm workers now attending to long term financial planning in which the future use of a capital base include establishing an own farming operation, provision for tertiary education of children and a financially secure retirement (Muller & Witbooi, 1994);
- lower risk in the initial phase of entry into commercial farming through the skills support of the present land owner and management structure being continuously available;
- high quality technical and managerial support at no additional cost;
- new learning opportunities through exposure to a range of skills wider than that acquired as worker, and
- known partner;

3.2 Advantages to the present owner

- expected improvement in productivity. Indications are that the impact on productivity was underestimated in the first participation models to be implemented;
- greater expected stability in the labour force (lower expected turnover and increased loyalty);
- release of capital for alternative investment;
- known partners; and
- a means to contribute to the RDP through sound business decision.

3.3 Advantages to society

- a model to achieve redistribution goals;

- leveraging of government funds. Public funds used in support of participation schemes are required in the initial set up phase and leverages private sector sources to reach a large number of beneficiaries;

- no recurrent cost to the state as private sector is mobilised to supply technical and managerial support and extension services;

- achieve empowerment of new entrants at a lower cost (both recurrent and capital) than settlement schemes;

- in equity participation schemes, the debt burden of agriculture remains constant in comparison with new settlement, which will likely incur debt as a greater multiple of net farm income than is the national average.

3.4 Participation schemes : A long term involvement

Present land owners might regard the participation scheme as an unwieldy mechanism which requires inordinate commitment and accommodation. A decision of the present land owner to embark on a participation scheme, must be made in full knowledge that a long term relationship, difficult to undo, is being proposed. As a result of the long term nature of the participation scheme, safeguards and guarantees are included in the joint venture agreement for both the farm worker participant and the present owner, in order to maintain the nature and spirit of the joint venture. This is specifically required to ensure the sustainability with regard to succession of ownership of the present owners' share.

The process required to facilitate economic empowerment during preparation and negotiation of the participation scheme is by nature more intensive than what takes place in a farm sale between the present owner and an empowered and informed buyer. It is unlikely that a participation scheme can be launched with success as a quick sale.

Joint ventures with farm workers are thus not suitable for a farm owner with a short term motive. Requirement for protection of farm worker rights built into legal agreements and the intensive empowerment process will most likely deter inappropriate candidates.

4. Two models

4.1 The equity participation scheme

Sharing of ownership through equity participation schemes, have advantages of broadening the ownership base in a farming operation, where the intention is to maintain the business as a single operating entity. Share holding can not, however, be related to individual underlying assets and the model is thus not suitable for facilitating emergence of the individual farmer. An advantage, however, is that individual business risk of the new participant is spread over the entire operation. Equity participation schemes as a model are furthermore equally applicable to new ventures as well as existing operations. A typical equity scheme can be represented as in Figure 1.

The structure and ownership of an equity participation scheme is sufficiently flexible to accommodate project specific requirements, e.g. different percentage ownership of the operating and land holding entities, distinction between productive areas and residential areas, existing fully developed farms or new ventures. Where an intermediary organisation is required to hold the interest in the operating and landholding bodies (e.g. if the number of participating workers exceeds what can be accommodated in a private company) special provision has to be made for a market to allow for change in the participant register

4.2 Share block schemes

In instances where a goal of the joint venture is to relate profit to individual performance and / or to target sole ownership by the new entrant as a future phase, identification of individual participants with a demarcated unit is required. A share block company is a possible vehicle for this purpose as profit on an individual unit can be identified with ease and individual units are marketable, thus allowing sale of units between farm workers, or by the present owner to the new partner. Launching of a share

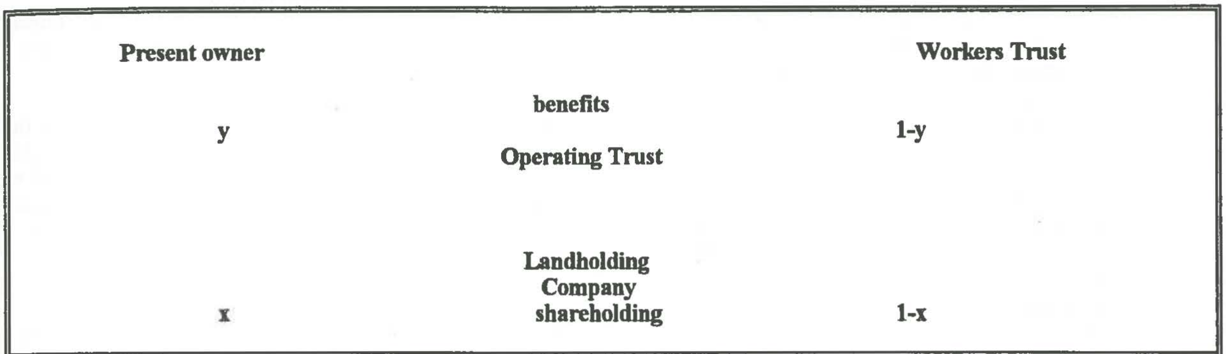

Figure 1: Schematic representation of an equity participation model

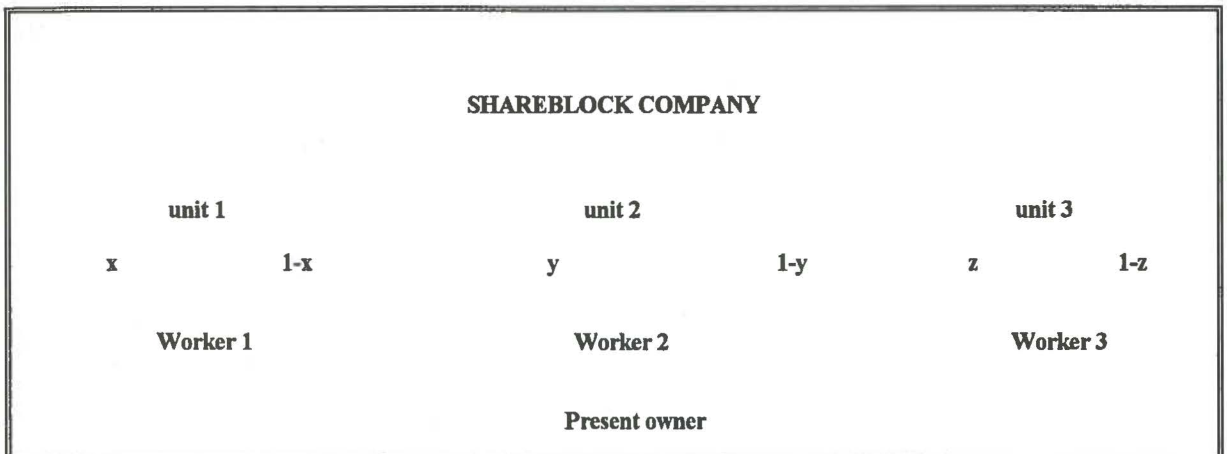

Figure 2: Schematic representation of a shareblock participation model

block scheme wil, however, require approval for subdivision of agricultural land.

A share block scheme is schematically represented in Figure 2.

A disadvantage of the share block scheme, (particularly with permanent crops) is that the individual participant is exposed to business risk greater than that of the share block area as a whole and thus greater than the risk exposure of the present owner. A mechanism to diversify risk might be considered, e.g. partially pooled marketing between the individual units or hedging through agreement with the present owner.

5. Process and transaction cost: DBSA experience

The operational involvement with various project proposals for equity participation and other farm worker models undertaken by DBSA, highlighted the importance of the **process** by which the empowerment takes place and focused on involving the target participants to take part or otherwise. Their contribution to formulation of the model furthermore ensures ownership of the proposal, the latter regarded as essential to obtain the improvement in productivity which is the motivating factor for the present owner to embark on such venture. An inclusive process will more likely yield a project which embodies empowerment juxtaposed against a turnkey proposal to the target participants based on skilful financial and technical modelling.

5.1 Process steps

A proposed process for equity schemes (case for owner identified project) is set out below.

Step 1: Owner identifies, prepares proposal (ie. offer to sell).
cost : owner

Step 2: Enquiry at financial agency and/or development agency.
cost : owner

Step 3: Development agency/financial institution establish likelihood of success based on:
- seller's motive;
- existing social relationships;
- financial criteria; and
- negotiability of offer.

cost : development/financial institution

Step 4: Owner makes formal offer to workers, preferably with development agency/financial agency present.
cost : owner/development institution

Step 5: Development agency:
- clarifies required institutional arrangements for project preparation;

- confirms farm worker organisation;
- assist farm workers in appointment of support agent through agreement on grant budget for process and transaction cost.

cost : development agency (direct or through grant budget)

Step 6: Workers with support agent consider seller's proposal/prepares counter offer/negotiates consensus model/seeks appropriate financing and submit final proposal to financiers (ie. undertakes full project preparation).
cost : grant budget

Step 7: Approval of loan/grant financing by financial institutions/ government/parastatals.

Step 8: Formalisation of approved project model (ie. deed of sale, registrations, transfers loan agreements, etc).
cost : pro rata workers (grant budget) & owner

Step 9: After care and monitoring, ie. support to workers maintained until skilled w.r.t input into management of the venture and management of worker's holding entity. (Grant support for this purpose considered only up to the stage where cash inflow from the project can service the requirement, eg. on phasing out basis).
cost : workers (initially with grant budget)

5.2 Process support

In the Whitehall project, an equity participation scheme in the Western Cape, the support to the workers and coordination of the project, was initially done in an ad hoc manner, by various agencies. A worker support agent was appointed after the investment decision by development/financial institutions.

It is proposed that future projects be handled through appointment of a support agent at the earliest possible stage in order that the buyer can take full responsibility for the process (ie. the full project agent function). In the Whitehall case, a significant portion of the worker mobilisation and project preparation was done ("free of charge") by DBSA and IDT staff, a luxury which is unlikely to be available in future. The appointment of a principle agent with budgetary provision for subcontracting of required skills and costs at various stages is proposed.

5.3 Costs and funding of project planning and equity acquisition

The total budget for process and transaction costs should be compiled on a milestone basis to be released upon progress.

The workers' share of process and transaction costs for co-operation projects, could be partly or fully recovered from the **planning grant** on land reform projects, presently available for the pilot land reform projects by Department of Land Affairs.

A norm for process and transaction cost can not yet be given with only the experience on Whitehall as guideline. The total process and transaction cost of Whitehall was however less than 5% of the purchase price.

Although the experience gained at Whitehall will result in greater efficiency of process in future, it is also true that the process and transaction cost is not proportional to the project cost, specifically as the required worker interaction is not a function of the project value.

The present **"land acquisition"** grant of R15 000 from the Department of Land Affairs could furthermore be available to farm worker to purchase equity and leverage loans if so wished. In the Whitehall case this grant would have contributed substantially to the affordability of the scheme.

6. Key issues for success

A number of key issues were identified through the DBSA projects for successful implementation of a participation scheme. However, the extent to which the issues impact on a participation scheme need still to be studied and verified.

These issues are complemented by those identified through the investigation of case studies by Nqgangweni Van Rooyen (1995). (Also see Van Rooyen *et al*, 1994).

6.1 Seller's motive

A joint venture with farm workers should be based on credible economic motive, i.e. gain to the present owner through expected improvement in productivity and stable internal environment of the farming business.

Joint venture schemes are not a mechanism for easy access to subsidised capital or a last resort to retain part ownership in an illiquid or insolvent business, i.e. no "catchnet for meritous bankruptcies".

6.2 Existing social and business relationships

In the ideal case, a participation scheme is a logical progression from an existing sound relationship between farm owner and farm worker. Joint ventures will unlikely succeed as a tool to heal ill relationships on the farm, as the scheme aims at:

- economic empowerment through creating access to wealth; and
- empowerment in the work place with respect to a newly aligned relationship.

6.3 The empowerment process

Due attention should be given to the process by which the farm worker is introduced to a joint venture .

The transaction required to launch a participation scheme is in principle a normal sale in the market. This implies obtaining agreement on the sale between a willing buyer and a willing seller. A number of issues are raised by this approach viz. :

- willing buyer implies wilful and informed decision. In order to enable the farm workers (uninformed buyer) to make an informed choice and to negotiate on equal footing with the land owner (informed seller), a buyers' support agent is required with the brief to advise the farm workers with respect to all facets of the proposal;
- willing buyer in a participation scheme furthermore implies a collective decision. However, choice by the individual farm worker to take part or remain outside the scheme should be provided for. This issue relates

to the nature of the empowerment strived for with the scheme. If all farm workers are required to take part, or participants are selected, the entrepreneurial decision to be exposed to risk for possible gain, is lost and the scheme reverts to a service benefit. A different approach for equity participation schemes and share block/sectional title schemes will be required. In equity participation schemes there is no limit to the number of participants. The proposal can be put to the workers collectively, with the individual decision to take part delayed until the project proposal has been finalised. In share block schemes, the number of individual units available, places a limit on the number of participants. In such instance a selection will have to be made. Involvement of the target group (from which the selection will be made) in drawing up the selection criteria, provides the opportunity to exercise a choice.

- fair treatment of both the participant and non-participant with respect to risk-reward relationship should be strived for. A mechanism to allow choice on participation by the individual farm worker should be structured such that the participant is exposed to a risk-reward relationship relative to the non-participant. An example of a mechanism is to include as service benefit, a fixed annual bonus (e.g. 13th cheque) with participants forfeiting the right to the bonus in favour of an expected dividend;

- buyer implies payment. Although an attempt is made to structure participation schemes such that they are essentially self financing, the farm worker opting for participation should contribute towards the purchase price. This further provides equitable treatment of the non-participant in that the participant do not get a windfall gain. The forfeiture of bonus (or other mechanisms) also serves the purpose of payment for asset purchased;

- earliest possible involvement of the workers in the process. An often heard response by project proposers (and by support agencies) to early involvement, is to finalise the proposal with respect to approval of financial support and sources thereof, prior to involvement of the farm workers lest creating false expectations. This seems somewhat paternalistic. Life consists of a series of expectations on a daily basis. Some met, others spurned. Involvement with the process of appraising the offer to sell will have benefit to the farm workers even if the project proves unviable.

- Involvement need to be through a neutral agent, i.e. not the present owner or owners' nominee, in order to maintain unbiased consultation, to promote empowerment and to remove the proposal from the concept of a service benefit; and

- farm worker input into institutional arrangements. This aspect is relevant with particular reference to the rules governing participation relative to labour turnover. The workers themselves should agree on the level of participation by each individual in the workers' share of the joint venture. A "market" has to be created through which workers can realise capital appreciation upon termination of service and through which new employees are allowed to buy in at the appreciated value.

A turnkey offer based on sound and innovative financial engineering and technical and institutional modeling is no guarantee for a successful venture. Involvement with the process to ensure ownership is likely to make the venture succeed.

6.4 Financial viability

In cases where the market value of the farming concern is higher than the productive value (the rule rather than the exception) it can be argued that the present owner should sell at a discount to market value. This is justified through the expected increase in productivity and lower risk of the joint venture, with concomitant expectation of increased net income. The lower selling price eases the financing of the access of farm workers to a participation scheme relative to outright purchase of privately owned land for settlement.

The farm workers generally have little own capital to significantly contribute towards the purchase price of their share of the joint venture. This leaves a gap between the value of the loans that can be raised and the selling price of the farming venture, requiring assistance to make the willing buyer also an able buyer. Proposals that a "land acquisition" grant to rural families be made by government and that such grant may be applied to obtain a share in a farming venture, was discussed at the Land Reform Conference held at the end of August 1995, and will hopefully be available in the near future. In an equity participation scheme co-financed by the Development Bank of Southern Africa, Standard Bank of South Africa and the Independent Development Trust, a nil per cent interest loan was obtained from the IDT as proxy for a possible capital grant.

Figure 3 is a schematic representation of the relationship of the agreed selling price to the loan value, the market value and the pre- and post project productive values An added advantage of financing the gap between the loan value and the selling price of a participation scheme with a grant, is that the participant workers can receive a dividend at an early stage. An early dividend is of importance, as it is unlikely to generate enthusiasm for a proposal in which the farm worker participants can only expect a cash return at a distant date.

6.5 Loan security

Loans taken up by the workers requires security in the form of mortgages on the farm and if still insufficient, bonding of moveable assets. The value of security required will in cases exceed the pro-rata workers' share of the fixed and moveable assets. The present owner might thus be placed in a position of not being able to have the full benefit of the pro rata share of assets to pledge as security for ventures outside the participation scheme. The latter is furthermore likely to be precluded in a joint venture as a mechanism to protect the joint venture in the initial stage.

6.6 Percentage participation.

No norms have yet been developed for an appropriate percentage share holding by the workers in a participation scheme. Projects implemented and being considered ranges from a 50:50 joint venture to proposals, to less than 20% equity held by the workers. What constitutes a meaningful shareholding is open for debate, but a 50:50 joint venture requires less additional protection to be written into the joint venture agreement than is the case for a minority holding by the workers

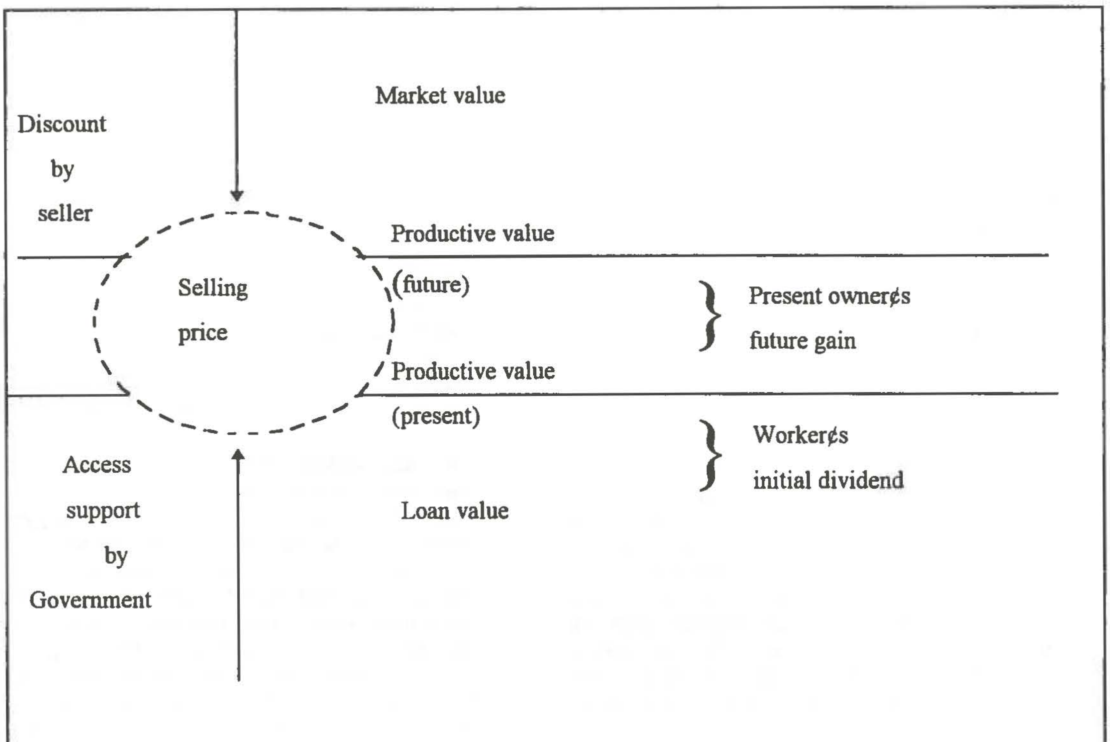

Figure 3: Schematic representation of agreed selling price

6.7 Number of participants.

This issue relates to the applicability of the model in various types of farming, with first indications that equity participation models are valid for capital intensive agriculture with a high labour demand. No norm has yet been developed but a norm for the minimum number of participants might be required to avoid the farcical situation where one worker elects to participate in an equity scheme. A norm for share block schemes relates to the number of units within the share block company and thus a target income per participant.

7. Agrarian reform policies

Agrarian reform policy objectives should aim at equitable development and fundamental issues of productivity food security, entitlements, and safety-net for the rural poor. This is partly where the question of growth with equity comes into play. While a class of new entrants into farming are empowered through these participation models to achieve prosperity, there is a potential danger that the position ofthe rural poorest may be neclected. The equity position is therefore not clear. However, participation schemes can satisfactorily contribute to rural welfare as part of a programme where opportunities, wealth and employment are equitable distributed.

8. Conclusions

The partnership and joint venture type of agricultural schemes holds considerable potential for rural development and agrarian reform if it can facilitate the integration of peasants and the rural dwellers into the national economy. The KTDA scheme in Kenya and the sugar schemes in South Africa are considered as "models" of smallholder development. The concept can be extended to commercial farming ventures in general. Schemes should be based on clear policy objectives from the macro-level (policy-making level) and business related deals at the micro level.

In South Africa participation schemes between the present owner and farm workers on an existing farming venture or an expansion of farming operations are clearly models which should be considered as vehicle for achieving agrarian reform on private owned commercial farm land with synergistic benefit for both parties. It is however important that only sound bussiness opportunities should be considered for such models.

Success of the ventures might also be dependent upon will requirethe availability of a capital access grant from government, a process of involvement and capacity development of the farm workers to establish a sense of ownership and preparedness on the part of the present owner to discount future expected increase in income, in a selling price and continued participation as partner cum mentor.

Notes

1. Whereby a joint venture is entered into between the present land owner and the farm worker.

2. Simply defined as a process in which land tenure reform, if required, is accompanied by redirection and reshaping of other institutions to insure that support services go to the beneficiaries of reform (Thiesenhusen, 1989 : 7).

References

CURRIE, K. & RAY, L. (1986). On the class location of contract farmers in the Kenyan economy. Economy and Society, Vol 15: 445-475.

GLOVER, D.J. (1984). Contract farming and smallholder outgrower schemes in less developed countries. World Development, Vol 12(11): 1143-57.

KIRK, C. (1987). Contracting out : plantations, smallholders and transnational enterprise. IDS Bulletin, Vol 18(2): 45-51.

LEVIN, R. (1988). Contract farming in Swaziland : Peasant differentiation and the constraints of land tenure. African Studies, Vol 47(2):101-120.

MCKENZIE, C.C, VAN ROOYEN, C.J. & MATSETELA, T. (1993). Options for land reform and potential funding mechanisms. Paper presented at the South African Fertilizer Society Conference, Durban.

MCKENZIE, C.C. (1993). Farm worker equity model : Mechanism to broaden the ownership base in agriculture. Paper delivered at the LAPC Land Options Conference, 12 to 15 August 1993.

MULLER, J. & WITBOOI, J. (1994). Employees of Whitehall Farm, Elgin. Personal communication.

NGQANGWENI, S. & VAN ROOYEN, J. (1995). Equity sharing as a (unique) option for local agrarian reform experience : The perceptions of farm workers. Agrekon, Vol 34:221-225.

SAJHAU, J.P. & VON MURALT, J. (1987). Plantations and plantation workers. Geneva: International Labour Office (ILO).

STILWELL, W.J. (1995). Options for private sector initiatives in the land reform programme. Discussion document prepared for the Department of Land Affairs, August 1995.

SWAINSON, N. (1986). Public policy in the development of export crops: Pineapples and tea in Kenya. IDS Bulletin, Vol 7(1):39-46.

THIESENHUSEN, W.C. (ed) (1980). Searching for agrarian reform in Latin America. Boston: Unwin Hyman.

TIFFEN, M. & MORTIMORE, M. (1990). Theory and practice in plantation agriculture : An economic review. London: Overseas Development Institute (ODI).

VAN ROOYEN, J.; NEL, P. & VAN SCHALKWYK, H. (1995). Boerdery organisasievorme vir die toekoms: moontlikhede vir plaaswerkersaandeelhouding. Paper at a North West Province Farmers' Day.

VAN ZYL, J. (1994). Farm size efficiency, food security and market-assisted rural land reform in South Africa. Agrekon, Vol 33:156-164

VAN ZYL, J., VAN ROOYEN, C.J., KIRSTEN, J & VAN SCHALKWYK, H (1993). Land reform in South Africa : Options to consider for the future. Journal of International Development.

WIESE, C. (1995). Opening address, Western Cape Agriculture Union Congress.

WILLIAMS, S. (1985). Commonwealth Development Corporation : A sugar production and settlement scheme in Swaziland. In: S. Williams and R. Karen (eds). Agribusiness and the small-scale farmer : A dynamic partnership for development. Boulder : Westview.