BENEFITS FROM THE FORMALISATION OF THE RAW MILK TRADE IN KENYA

Transformation of the Dairy Sector—SITE Case Study

The critical role played by the informal sector in Kenya’s economy is underscored in the Vision 2030 strategy and its transformation recognized as being key for growth. The informal sector is strongly dominant in the dairy industry perhaps more than many other economic sectors yet, over the years, little attention to mainstream and support it has been given, rather, barriers of different kinds have been erected or sustained. This paper highlights two initiatives which have seeded a transformation of the sector through market system interventions and application of a rights approach to poverty reduction.

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<td>BDS</td>
<td>Business Development Services</td>
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<td>BSMDP</td>
<td>Business Services Markets Development Programme</td>
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<td>DFID</td>
<td>Department for International development</td>
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<td>DTA</td>
<td>Dairy Traders Association</td>
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<td>KDB</td>
<td>Kenya Dairy Board</td>
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<td>KSHS</td>
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<td>ILSD</td>
<td>Improving Livelihoods in the Small Holder Dairy Sector</td>
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<td>MoLD</td>
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Acknowledgement

SITE is pleased to share a summary of our experiences and lessons learnt during the implementation of two of our projects in the dairy sector. We acknowledge DFID for providing the funding for the work through the Business Service Markets Project, BSMDP for the IQAM project; and the Civil Society Challenge Fund, CSCF, which supported the ILSD project. We also acknowledge our partners in ILSD, Traidcraft Exchange. The success of these initiatives was possible through the efforts and determination of thousands of small scale milk traders and the producers who they work with and the enterprising service providers who pioneered a new era in this area of work. The pragmatic approach demonstrated by the Kenya Dairy Board team through re-engineering of how policies are practiced on the ground is highly appreciated. We also appreciate the dedicated SITE staff team lead by Judith Kithinji for ensuring the success of these projects. The preparation of this paper was inspired by our interaction with Mr. William Grant of DAI whose encouragement is highly appreciated.

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1.0 Introduction

Setting the Scene

The dairy sector in Kenya is a very important source of income to large numbers of small and medium farmers, tens of thousands of traders and is one of the most rapidly growing food consumption items in the country. In 2008, an estimated 750,000 small producers sold approximately 30 billion Kshs. of milk. Between 2003 and 2010, the dairy sector in Kenya has seen tremendous growth, with a 50% increase in total quantity of marketed milk. This has been driven in a large part by the surging economy and increased purchasing power of the Kenyan consumer, but has also been the result of ongoing transformation of the sector that has allowed the supply side of the industry to better serve the needs of the consumers.

DFID has played a significant role in the development and transformation of the sector. Beginning with its work on smallholder dairy farmers from the 1990’s, it gained significant knowledge of the inner working of, and the challenges within, the sector. Starting in 2001, DFID carried out deeper analysis on the structure of the dairy sector (ECI 2001) which highlighted the main drivers of the sector as the nature of consumer demand driven by price, product quality and preferences, and, utilization patterns and the critical role being played by the informal sector in meeting the demand of the consumers. Starting in 2003, DFID began implementing a major dairy component under the Business Services Market Development Programme (BDMDP) which worked simultaneously at all functional levels of the value chain (see figure 1 on the next page) to address farmer productivity, processing and marketing challenges. BSMDP placed great emphasis on the role and importance of the informal marketing channels that delivered the raw milk that was most desired by the consumers, accounting for 80 percent of all marketed milk. This had been identified in the 2001 subsector study as the most critical component for growth of the subsector, in particular the regulatory aspects. As this trade was officially illegal and the regulatory environment posed a serious threat to the industry that could cut off the larger majority of small producers from the end market if regulations on marketing raw milk were strictly applied and deny the low income earners in urban areas a much needed source of nutrition especially for the under-five children, since other milk supplies are beyond their purchasing abilities. This is the first time that formal development effort was deliberately targeted on the dominant market players in the dairy sector.

The rest of this case study focuses on how DFID funded, BSMDP, IQAM, project tackled the sticky issues around legalizing the trade of raw milk over a six year period, and documenting the benefits this has derived. The work is ongoing but is an excellent example of how a structured market facilitation approach can bring together the key actors, identify and address the critical constraints using market driven services and sustainable institutions, and drive the transformation and formalization of a previously opaque and informal industry. The benefits from this formalization are felt by all the actors – producers have better markets, traders have better

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**KDB: FOR MALIZATION OF THE INDUSTRY STEMING FROM TRAINING ON QUALITY**

**Certification of Trainers**
- Approval of training courses
- Increased consultation
- National Dairy Regulators Consultative Forum
- Regional Regulators Forums
- Formation of District Stakeholders Committees
- Branding of KDB Quality
- Increased confidence
- Improved income for KDB- Sales of licenses, increased cess collection
- Improved systems
- M&E system for KDB to track the actors

**Service market**
- Laboratory testing

**Service markets for Information transmission through**
- Media Programmes
- Livestock [breeders show

**Enabling Environment**

- Markets
- Retailing
- Wholesaling
- Transporting
- Processing
- Pasteurizing
- Cooling
- Collection / Bulking
- Production
- Input / Feed

**Service Market**
- Milk Dispensers
- Hawker Distribution network

**Service Market:**
- Training of traders, transporters, milk bars

**Development of Service Hubs**

**Service Markets:**
- Supply of commercial dairies
- Transport to the collection centers
- Bulking and chilling of product

**Service Markets:**
- Distribution of semen
- Marketing of AI services
- Agrovet for feed and medicines

*Figure 1: BSMDP Dairy Value Chain Interventions*
businesses, and consumers get better quality and cheaper prices, and the sector regulators have better grasp of the work of the dominant players.

The BSMDP Programme and Legitimizing the Informal Sector

Although the informal raw milk channel was officially illegal in 2004, sanctions against it were unevenly enforced. It serviced urban markets dominated by millions of consumers with low purchasing power which provided market for most smallholder farmers. The inconsistency in regulation needed to be addressed because it left thousands of traders effectively working illegally and open to harassment and rent-seeking by officials. This rent-seeking was common particularly affecting milk transporters and mobile retailers and provided disincentives to investment. In order to tackle the fears and real health concerns inherent in unregulated milk sales, however, concerns about the sales would have to be addressed and a consensus built to support legalization of the raw milk chain.

To respond to the concerns of the KDB, BSMDP developed the improving Quality Assurance in Milk Marketing (IQAM) subproject in conjunction with SITE Enterprise Promotion (SITE), to address the capacity of the traders to handle milk safely. From November 2004 until 2008, SITE initiated a series of activities through IQAM I and IQAM II projects to enhance the food safety of traded milk, working closely with the KDB and reduce overall losses in the enterprises. By developing a quality assurance training programme that met the requirements of the KDB and developing a cadre of accredited trainers to train the milk traders (business service providers), KDB initiated a programme to license the traders. This provided the foundation for the industry regulators to officially recognize the trade of raw milk in May 2007. While the statute legalizing the trade of raw milk has not yet been officially enacted into law, the KDB has been regulating the sector as if the statute were in effect.

The BSMDP used market-driven activities to develop the service providers to improve the competency of the traders and the quality of the milk being traded in the raw milk channels. KDB provided incentives to traders to get licensed—with well defined requirements for licensing. Further, for a certain category of traders, KDB branded the enterprise, which raised the value and competitiveness of their product, and provided protection from hassles by other regulators. The regulator then created four new sets of licenses (producer/trader license, hawkers license, transporter’s license, and milk bar license) to make these traders legal. The regulator’s agreement required all traders to be trained by the accredited trainers before they could obtain a license. As of 2008, SITE had trained 90 trainers (SPs), of whom 46 were fully engaged in offering training, and had trained about 5,000 traders toward certification. Of these, about 2,000 traders had been certified, with the rest in process (DAI 2008). The ongoing commercial services being provided by the trainers, who are contracted directly by the traders, continue to serve as a key component of the regulator’s certification and licensing programme.

However, simply convincing the regulator to recognize the raw milk traders proved insufficient as the other regulators did not necessarily know about the changes in regulation practices. Therefore, the programme subsequently helped the regulator to work with the traders to obtain concurrence from the Ministry of Health (public health department), the local authorities, and the police in understanding the policy shifts and recognize the traders.

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The challenges facing the raw milk market were not only reflected at the regulatory level, but higher levels of public policy formulation. In order to inform/educate and extend dialogue with the wider decision makers, the programme identified the public sector especially the Ministries of Livestock development, Cooperatives development respectively. In order to reach them, Regional and District dairy regulator forums were created to increase consultations between the actors and to discuss and address issues arising from the licensing of the traders and the services they provide to small scale milk producers and consumers. KDB also needed effective monitoring system to allow them to track and record the development of the traders through the service providers. SITE helped KDB to develop and operationalise this system.

Though the issue of the trade of raw milk had been under discussion for years, the critical link to the BSMDP was the latter’s direct engagement with the regulator. The BSMDP's IQAM project succeeded in getting the regulator to understand the market issues facing the the raw milk segment of the dairy subsector and their potential impact on consumers and smallholders, demonstrating to the regulator that training could address the health risks and issues that were of concern and resolve them.

The legalization of the raw milk channel began leading to increased formalization of the marketing channel, securing the acceptability of this market to producers and consumers alike while reducing transaction costs as product flows to market. These benefits have led to greater regulation of a formerly unregulated sector, giving the KDB a better view of what is happening in the sector. The statistics in 2008 were already showing that it was leading to more profitable business for the traders, stimulating investment by the traders in upgrading their equipment, skills and the quality of their services and important increases in traded milk. Another significant impact was the centralization of the raw milk sector as a legitimate and integral component of the future of Kenya’s dairy sector development, worthy of consideration by other actors, especially at inter-ministerial level in their development strategies.

2.0 The Development of The Dairy Traders' Association

Overview

Following these early successes, the leading licensed dairy traders approached SITE to assist them organize themselves for collective actions. They wanted a vehicle to enhance the status of the licensed dairy traders in their negotiations with the regulator, as well as to improve their ability to deliver services to their members, and build...
a positive image of the raw milk sector which was generally unfairly regarded especially among the ‘elite’. Though they were operating in a more regulated environment, they were still not universally protected, especially since many traders were still working in the same old ways still let the police and health authorities to continue to hassle them. There was a clear imbalance between the traders and the formal sector and formal agencies like the police and health departments and the traders needed greater organization to gain formal recognition. There were still negative perceptions about traders and a poor image for their sector. The traders wanted to be recognized and work together.

The work of SITE through the BSMDP IQAM had introduced a consensus building for regulating the raw milk sector based on an engagement with the regulators, and the positioning of independent service providers who support the traders to comply with requirements and build better milk trading businesses. However, for long-term change and growth in the sector, there was a missing element—the direct participation of the traders in dialogue and future policy negotiation and representation in emerging policy discourse. This is critical in balancing power in the value chain. The self-organisation of the traders was going to add this critical element in the transformation.

In 2008, SITE and Traidcraft Exchange received funding from the DFID Civil Society Challenge Fund to implement the Improving Livelihoods of Smallholder Dairy (ILSD) Project. The work under ILSD has solidified the early progress started under BSMDP and greatly strengthened the ability of the dairy traders to fight for their rights. SITE has engaged by mobilizing traders in key production and high market areas. They started a consultation process and developed a self-organisation rationalization (small groups, regional associations and finally a national umbrella). The focus of the early work has been on organizational development using the four pillars toolkit depicted in figure 2 (below).

The four pillars are based on a rights framework focusing on building the capacity of the traders to organize themselves, function effectively to represent members and focus on services that promote the growth and security of the traders businesses. SITE provided on-going support to the sector and associations, driven by strategic outcomes at enterprise, raw milk sector and business environment levels.

**Current Status of the DTA (as of June 2010)**

The traders are organized in 68 groups of traders based on geography and category. This is the first contact and service point for the traders with each other. These groups then form regional branches of the Dairy Traders Association. There are 10 regional branches, registered as Associations in their own right—these are in Kisumu, Eldoret, Kericho, Nakuru, Naivasha, Mt Kenya Region and greater Nairobi. The 10 regional branches then formed a national umbrella, the National Dairy Traders Association, DTA registered in April 2009.

The DTA membership now totals 4200 traders out of a total estimated 28,000 traders in Kenya. But their numbers are growing steadily by 200 traders per month as more traders are licensed and they understand the value of the services offered by the DTA. SITE put in place an effective monitoring system at DTA to track the registration and the sales of their members, since they are also the point of licensing and the collection of the cess for the KDB. This allows for better tracking of the changes in the industry.

These members market 504,000 Litres/day, or roughly 18% of all marketed raw milk in Kenya. These traders purchase from over 101,000 producers, and actually pay higher prices to the producers (22-26 ksh/l) than the formal sector (17-23ksh/l), totaling to payments of more than Kshs. 12m to producers each day. The dairy trade is also being seen as a viable business alternative for young Kenyans, as the age of traders at entry is 19 to 22 years.
Changes Emanating from the Organizational Development of the DTA

There has been a wide variety of changes within the sector due to the involvement of the DTA. These will be viewed at different levels in the following sections: relation between the traders and the regulators; self-regulation being imposed by the DTA; growth at the enterprise level by the traders; increased services being provided to the traders; influence on the policy environment; impact on producers; the impact on consumers; and the market system as a whole.

Working with Regulators
The association(s) has changed not only how the regulators view the sector, but also how they work with the traders. The DTA is able to provide greater clarity of regulatory requirements to its members and boosts the incentives for their compliance. It has established dialogue between the traders and the regulators, which allows the traders to argue against unfair treatment by officials, but also allows the KDB to interact more directly with the traders, making it easier for them to reach out and regulate the traders.

One of the benefits for both the KDB and the traders is creating a point of leverage for licensing and health inspection. These are reducing the costs to both the KDB and the traders, providing more incentives to formalize. In Kisumu, traders can register at the DTA branch, reducing their costs associated with getting licensed from 800 ksh to 20 kshs. In Eastern, there is a one stop service. In Miwani, the health department organizes the health inspection on site at the branch, making it faster and easier for the traders to get their health certificates.

The most important change from the perspective of the traders is that they now have a ‘big-voice’ and can speak through one channel - in the past, the public sector always argued about the inability to deal with thousands of small businesses, compared to a handful of other private sector actors in the sector. DTA has legitimately provided a representative of the raw milk traders and this has opened opportunities for the raw milk to be put squarely on the table at top level of policy and sector discourses. The Association is virtually represented in all the major discussions on regulations, policy and other debates on the sector. The sector policy and draft Bills, as well as the draft Master Plan clearly include the raw milk sector and DTA is well able to articulate the interest of the traders. This is introducing a power balance that will greatly influence future sector development agenda.

Self Regulation
The DTA is also in the process of increasing their self-regulation of the industry. They have instituted a traders’ Code of Conduct, which is enforced at the cluster level. If traders are caught not respecting the code of conduct, especially around quality issues, they are subject to fines by the Association. This has led to significant changes in practice by the members, eliminating adulteration of the milk, leading to better quality and stabilization of trade that can be tracked.

Growth of Trading Enterprises
The DTA monitoring system, developed with SITE’s help, tracks numerous indicators that demonstrate the improvement of the dairy traders as businesses. There has been a documented 54% increase in milk volume traded by DTA members; over the last 12 months average dairy sales in litres have increase from 1550 to 2789 in Kisuuru; 1273 to 2713 in Nakuru; and 2296 to 2451 in Kirinyaga. Embu and greater Nairobi are also dealing in much larger volumes.

Many of the enterprises are upgrading their operations, moving from bicycles to motor cycles, Tuk-tuks and pick-ups. Many mobile vendors are now opening milk bars (since they are legal). There is increased processing of liquid milk to mala and yoghurt, innovative business/food solutions especially for youth and urban labour force. Finally, many of the traders are now investing in new equipment – milk steel cans, storage tanks, etc.

Services to members
The DTA offers (or facilitates) access to a wide range of services. It is organizing business training courses to be delivered by private trainers to the traders. It is providing protection during harassment (interface with the officials to resolve disputes), and access to service providers especially for quality improvement and processing (mala and yoghurt).

There has also been an increase in financial services including welfare and table banking. For example Kshs 1.42m loaned every week from current savings by members (at 10% for the week) in one cluster/group. The DTA is establishing links with banks/FSI e.g. Faulu and Equity in Nakuru and Kirinyaga. Financial services opportunities running into millions of shillings is slowly budding.

Producers
Benefits to the producers include more reliable buyers and better prices (as shown above). There is an increase in the use and reliability of informal credit systems (supplier or buyer credit), and greater access to information through the associations/groups.

Consumers
From the consumers’ side, there is easier access to affordable quality milk – stabilized at Kshs. 30-40 per liter delivered at the door as opposed to 60-70 ksh at the store. They are able to purchase their preferred produce (whole milk) in the amount they want, buying quantities they need – from 300ml to 50 liters. They also have a personal relationship with the suppliers, allowing them set up credit arrangements where they are paying on a weekly basis.

Other Changes in the Value Chain
In addition, there are a host of side benefits to this arrangement that led to more efficiency in the value chain, enhancing benefits to the traders and to the consumers. Traders now have greater confidence in their enterprises, so there has been a rapid change of self-image. There is growing consumer confidence and respect by others, now that food safety being assured. There are increased and affordable services to the sector emerging (training, certification, processing, etc). In addition, because of the formalization, there is greater demand for better marketing conditions and there is investment in new milk marketing points (MMPs) which were initially funded by DFID but now through MESPT/Danida, as well as investment by traders and producers in milk chilling hubs.
Some immediate benefits lie in efficiencies from bulking and marketing. For example, the producers serving the Kipkelion milk hub contracted sales of 5,000 litres/day to a cluster of milk bar operators of Kisumu DTA, which is more cost effective and profitable for all involved. In the Miwani MMP traders are pooling transport to the market saving time and money while Nairobi traders that are collecting in Nyandarua are also pooling transport, lowering their costs and allowing use of specialized containers.

During ‘milk glut’ in early 2010, when the formal dairy processors reduced their purchases, the DTA members increased their sales significantly, picking up much of the milk made available by the reduced demand by the formal sector. Their ability to seek out isolated small producers also allows more farmers to access markets.

4.0 Conclusions

The formalization of the raw milk channel in the dairy subsector is in process and is leading to significant benefits to the entire value chain. The progress has derived from an informed and practical regulator, which understands the issues confronting the sector and is working to upgrade the participants, working in conjunction with supporting institutions that understand the dynamics driving the subsector. SITE’s work has demonstrated that it is possible to organize an opaque and fragmented informal sector into a more structured set of actors who see the benefits from formalization, and develop sustainable systems to further promote that formalization. The ability to effectively organize the sector to work with the key actors who will benefit from that organization has led to deeper systemic changes in the dairy value chain. This has introduced a power balancing in the sector that will influence future policy work and investment by key actors.

A critical element in the whole process has been the understanding that the markets and consumers drive the sector. When dealing with a commodity, the products offered must conform to what the consumer wants to purchase. Trying to deny the consumer what they want will just drive the supply underground. But establishing conditions that meet the regulator’s needs and can respond to the consumers’ desires can provide a framework for the regulator to create a transparent sector that can be tracked, engaged, studied and upgraded. This creates a win-win situation that;

- For the regulator, they have increased their ease of access to the traders. It has generated more revenue for the KDB by increasing the cess and levies they can collect, while facilitating (reducing the cost of) their collection. It has increased the quality assurance of the milk that is being handled, and promotes a realistic engagement by the traders since they are dealing with the dominant player in the sector.

- From the traders’ perspective, they have a more formalized sector within which to work. They are able to engage more effectively and concretely with the regulator to protect their rights. They are able to demonstrate their willingness to upgrade and to respond to the conditions that the KDB has established, in return for less hassle and lower transaction costs. By organizing, the traders are able to access better services to upgrade their skills and quality, while creating a better environment within which to operate, stimulating investment in their businesses.

- For the farmers, especially the very small scale farmers, they have an expanding and reliable market for their produce, stimulating further investments. The ‘embedded services provided by growing traders/buyers of their milk is expanding the scope of benefits they accrue from their farm enterprise and increasing incomes they derive from their labour.

The sum of these factors has been a demonstrated increase in the overall quantity of marketed milk through the informal sector and a greater acceptance by the regulator as they continue to steadily upgrade the quality of the supply and improve benefits to the consumers.