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## VALUE ADDITION ON KENYAN TEAS: EFFECTS ON INTERNATIONAL MARKET SUSTAINABILITY AND COMPETITIVENESS

**ESTHER WANJIRU MAINA**  
**ASST. LECTURER**  
**SCHOOL OF BUSINESS KARATINA UNIVERSITY**  
**KARATINA**

### ABSTRACT

*Tea is exported in bulk, denying farmers better income consistent with the value of their crop. The tea is used for blending with other teas for taste, aroma, colour and density, thereby losing its unique identity. Tea in its traditional form as brewed beverage is undergoing change in the context of changes in consumer preferences and lifestyles and increasing competition from other beverages in the global market. Value addition is today being driven by consumer choice and this is encouraging Kenyan tea firms to look into new ways to add value to their teas. Packing tea into tea bags in many forms has become popular because of convenience and it can be considered as an effective form of value addition. Selection of environmentally friendly packing materials, which are bio-degradable, recyclable and re-usable, has become a favorable factor. Flavoring of tea using natural mixtures of spices, herbs and extracts in liquid or granulate form has become very popular in most of the market segments of specialty teas. Strong artificial flavors are also used widely to flavor conventional teas. Carbonated drinks Ready to drink teas have great potential in both the local and export markets. Ready to drink teas can substitute popular carbonated drinks in the market based on awareness of the beneficial health factors, the ready to drink teas will soon become a popular market product. This gives the Kenyan Teas international competitiveness in the global markets. This paper explores the benefits of the value addition and diversification on smallholder return on investment and market diversification for tea product sustainability for international competitiveness. The paper is supported by field data obtained from small-holder tea farmers sampled from Nyeri County in Central Kenya and secondary data from the tea sector stakeholders. The paper indicates that the Kenya tea industry is at crossroads and the country's status as an exporter of bulk CTC black tea needs to be changed to an exporter of value added teas. The paper recommends strategies for enhancing Value addition to the advantage and benefit of the smallholder tea enterprise and the sustainability of the Kenyan tea competitiveness.*

### KEYWORDS

Value added Teas; International Market; Return to small holder tea farmer; Small holder tea enterprise sustainability; Competitiveness.

### 1. INTRODUCTION

According to *Economic Survey, Kenya National Bureau of Statistics (2011)*, Kenya is currently the world's third largest producer of tea after India and China but the leading exporter of black tea. Kenya's tea industry is well developed and is among the country's leading foreign exchange earners and contributes about 20% of the Kenya's total export earnings.

Since 2009, the Tea industry was the highest foreign exchange earner raking in Kshs 92 billion in 2010. Kenya's major markets for tea in 2010 included Pakistan, Egypt, United Kingdom, Afghanistan, Sudan, Russia Federation and Yemen. The top four countries alone accounts for about 66% of total exports and this shows a high concentration of markets. Kenya's tea exports are mainly constituted by black CTC (crush tear and curl) teas in bulk and exports of value added teas are still very low KTDA, Annual Report, (2013).

### 2. BACKGROUND OF THE STUDY

The tea industry plays a key role in the agriculture sector and the economy at large with tea output contributing about 11% of the agriculture sector's contribution to Gross Domestic Product (GDP) of the country. In addition, the industry supports directly and indirectly approximately 5 million people making it one of the leading sources of livelihood in Kenya. However, the tea industry has been faced with various challenges including: high cost of production, poor infrastructure, low level of value addition and product diversification, inadequate research, development and extension services and declining global tea prices. (Economic Survey, Kenya National Bureau of Statistics, 2011).

At present the world tea market is rapidly growing with emerging customer needs. This demands the importance of a change from bulk tea exports to value added tea products to meet the customer's emerging and changing needs in an increasingly competitive beverage market. Firms failing to address the competitive forces by developing their marketing strategies as well as add value to their products will lose out to competitors. Since the inception of tea industry in Kenya, tea exports are in the form black CTC tea and exported bulk. Low prices, loss of income and the discrepancy in the prices between export prices and retail prices are the results of the bulk export of tea. Value added tea export will increase Kenya's export income and competitiveness of the tea industry.

The tea industry has made major strides in tea variety improvement, development of appropriate soil and plant nutrition management technologies, good agricultural and tea manufacturing practices, pests and disease identification and management techniques, development of extension materials and sensitization on importance of tea branding among others. These technologies have contributed to making Kenya attain the highest tea productivity in the world. Despite these advances, Kenya has continued to be a producer of processed tea at primary level with very little product differentiation and value addition. This has constrained growth in profitability, prices of the Tea and competitiveness in the international market (Tea Research Foundation of Kenya: 2010 – 2015 Strategic Plan).

A study carried out by the Kenya Tea Research in 2010 indicated that Kenya is currently the world's third largest producer of tea after India and China but the leading exporter of black tea. The major markets for Kenyan teas included Pakistan, Egypt, United Kingdom, Afghanistan, Sudan, Russia Federation and Yemen; The top four countries alone accounts for about 66% of total exports and this shows a high concentration of markets.

Kenya has more than 110,000 hectares of land devoted to tea and Tea is grown in the highland areas with adequate rainfall and low temperatures. Tea is a major foreign exchange earner, and the main source for 17 to 20 percent of Kenya's total export revenue. Small-scale farmers grow more than 80 per cent of it while the rest is by large-scale producers. Small-scale farmers market their produce through the umbrella Kenya Tea Development Authority (KTDA), who is in charge of collection, processing and selling of processed leaves. Large-scale producers of Kenyan tea include Brooke Bond, George Williamson, Eastern Produce and African Highlands. Unlike small-scale farmers, large-scale growers are responsible for processing and marketing of their own crop. (Tea Board of Kenya Strategic Plan 2008-2012)

Currently, Kenya produces and exports over 96% of the tea as black teas. The tea is sold to the world market in bulk and hence is largely used for blending lower quality teas from other countries. Consequently, it fetches low prices and therefore depressed revenue for tea growers in particular and low foreign exchange for the country in general. The Kenyan teas have been positioned the best in the world tea Market which has been rapidly growing with newly emerging customer needs. Although Kenyan tea industry had been mainly focused on bulk tea from the beginning to now, the tea sector is being diversified into value added trends with some value added strategies in terms of new product levels, value features, branding and packaging too. But again, the major international tea competitors such as Sri Lanka, China, India, Indonesia, Vietnam and Argentina are also aggressively following that value added strategies to penetrate and capture the potential markets. With this, Kenyan Tea manufacturers' needs to value add their teas as an effective and competitive strategy for having sustainable marketing results.



### 3. STATEMENT OF THE PROBLEM

Owino (2012) defines value addition in the context of tea denotes the processing of tea produced or bought in bulk form (mostly at the tea auction or at the factory) into products that are sold at the retail level in consumer-ready packets through product modification and diversification to create more value for the product. This is achieved through product branding, packaging and flavoring.

Tea in its traditional form as brewed beverage is undergoing change in the context of changes in consumer preferences and lifestyles and increasing competition from other beverages in the global market (Kelegema, 2010). Kenyan tea remains largely unknown in the international market with the exported bulk used to blend other teas, then packed using different brands. The tea industry wants a policy on value addition so that local brands can find pride of place internationally. Tea is exported in bulk, denying farmers better income consistent with the value of their crop. The tea is used for blending with other teas for taste, aroma, colour and density, thereby losing its unique identity. As a result, the Kenya tea industry is at crossroads and the country's status as an exporter of bulk CTC black tea needs to be changed to an exporter of value added teas. This would result to the future viability of the tea industry in the global market.

Despite the impressive successes that the Kenya tea Industry has registered in the past, there are varied challenges along the value chain which the sector is facing and would need to evaluate ways of reengineering itself into more improved ways of production, processing and marketing to sustain competitiveness and profitable investments. The challenges range from increased cost of production, processing, electricity bills, stagnant earnings due to export of tea in bulk form, low level of product diversification among others. Kenya is predominantly a black CTC tea producer, with black CTC teas forming about 99% of the total production. (Market Research and Information, KTDA, 2013)

The need for value addition of the tea has become more necessary than before as a solution to the myriad challenges and problems facing the tea industry as mentioned earlier on. Value added teas are tea exported as small packets and bags; and also herbal tea, flavoured tea and green tea instead of black Tea. Value addition to Kenyan Teas would not only provide the consumers world-wide with pure Kenyan branded teas, blended at source but would as well make the teas internationally competitive. Like other producing countries, Kenya can capture more value in the tea supply chain by diversifying into value-added production. A strategic approach is to diversify and add value to the tea products for the domestic and international markets. This lack of diversity of customers places Kenya in a precarious position, where a drop in demand from any one of these countries could have a major impact on revenues from Kenyan tea exports. Kenya risks losing major key tea markets, if it does not combine bulk and value addition in the production of tea.

Value addition is today being driven by consumer choice and this is encouraging Kenyan tea firms to look into new ways to add value to their teas. Packing tea into tea bags in many forms has become popular because of convenience and it can be considered as an effective form of value addition. Selection of environmentally friendly packing materials, which are bio-degradable, recyclable and re-usable, has become a favorable factor. Flavouring of tea using natural mixtures of spices, herbs and extracts in liquid or granulate form has become very popular in most of the market segments of specialty teas. Strong artificial flavours are also used widely to flavour conventional teas. Carbonated drinks Ready to drink teas have great potential in both the local and export markets. Ready to drink teas can substitute popular carbonated drinks in the market based on awareness of the beneficial health factors, the ready to drink teas will soon become a popular market product. This gives the Kenyan Teas international competitiveness in the global markets. A major factor that is driving countries to look into value addition is a drop in global prices for bulk teas in recent years. It is for this reason that the researcher would be interested in carrying out a study on factors influencing Value Addition of Kenyan Teas for international competitiveness.

### 4. OBJECTIVES OF THE STUDY

#### GENERAL OBJECTIVE

The general objective of the study is to investigate the factors influencing value addition on Kenyan Teas for International Competitiveness in the global market.

#### SPECIFIC OBJECTIVES

1. To find out whether product differentiation influences value addition of Kenyan teas for international competitiveness.
2. To establish the effect of repacking on value addition of Kenyan Teas for international competitiveness.
3. To determine the effect branding on value addition of Kenyan Teas for international competitiveness
4. To find out the effect of flavoring on value addition of Kenyan Teas for international competitiveness

### 5. METHODOLOGY

This adopted mainly the secondary data collection method to gather pertinent and relevant information to support the study. The primary method was also used where interviews was conducted to tea farmers and other tea stakeholders followed focused group discussions to gather their knowledge and experiences on tea value addition in accordance with the requirements constitution of Kenya. The secondary data was obtained from the tea industry reports, newspaper articles, industry website and other relevant literature on the tea industry. Reference was made on the Tea Industry the Tea Amendment Act (Cap 343) (2010) of the Laws of Kenya, National Tea Policy of (2013) and the Strategic Plans of Tea Board of Kenya, KTDA Tea Research Institute of 2013.

### 6. JUSTIFICATION OF THE STUDY

Although the volume of value added tea sales has been increasing, there is still need for promotion to increase sales by creating product diversity, increasing the profitability, and providing job opportunities for Kenyans doing value addition rather than foreigners, and finally achieve the goal of industrialization as envisioned in the Vision 2030.

The need for value addition of the tea has become more necessary than before to provide the consumers world-wide with pure Kenyan branded teas, blended at source.

Like other producing countries, Kenya can capture more value in the tea supply chain by diversifying into value-added production. Value added teas is tea exported as small packets and bags; and also herbal tea, flavoured tea and green tea instead of black Tea.

The Country also needs to promote more the origin of teas from a particular region and then marketing the teas with a clear indication of their origin. The Tea Board of Kenya recently launched the Mark of Origin. For the promotion of the exporting of value added Tea, it is recommended that Kenya considers providing incentives like other competitors (especially Sri Lanka) do to the producers and packers of teas through duty free imports of flavours and packing equipment and materials and also placing all factories under the special economic zones. This paper acts as an important benchmark for future solutions existing and emanating problems of Agricultural products.

### 7. SIGNIFICANCE OF THE STUDY

The findings of the study help in assessment of the tea sector practices by the Government, tea manufacturers and other stakeholders. The findings further identify gaps in understanding, product differentiation, repacking, branding, and flavoring being value addition strategies to gain international competitiveness in the global market. It may help the policy makers and the Government through the Ministry of Agriculture to develop policy frameworks that take into account the diverse needs of the stakeholders in the tea industry and further add value to the managers and other employees of the manufacturing companies by creating insights on environmental changes revolving around the tea industry as well as contribute immensely to the existing literature in that field so that academicians could use it as a basis for further research.

### 8. TEA VALUE ADDITION

#### TEA VALUE ADDITION SITUATION IN KENYA

The level of tea value addition in Kenya is relatively low for both local and international markets consequent to which the country has not optimized its earnings from tea. Compared to other countries who have actively embraced value-addition such as Sri Lanka, Kenya tea earnings from exports have been slightly less. In

2010 for example, Kenya earned USD 1.23 billion from exports of 362 million kgs of its own tea as well as re-exports of 79 million kgs of other origin teas, while Sri Lanka earned USD 1.37 billion from its export of 314 million kgs owing to higher prices and more valued added shipments. Even though Kenya exported 29% more tea in quantity terms than Sri Lanka, the country earned 10% less in value terms (Tea Board, 2013). Statistically as presented by the Tea Board (2012), in 2010 Kenya produced 339 million kgs of tea. 20 Million Kgs (5%) was sold in value added form in the local market; 38.6 million kgs (10%) was sold to the international market in value added form. This translates to 58.6 million kgs (15%) of total Kenya tea production being sold in value added form both locally and internationally. This justifies the reason why the entire tea industry in Kenya need to fully concentrate and invest heavily on value addition as a strategy to boost the sales and expand the market share both locally and internationally.

#### **BARRIERS TO TEA VALUE ADDITION IN KENYA**

The following were noted to be the existing impediments to tea value addition in Kenya:-

- Competition from established traders/firms in consuming countries, particularly multinational corporations, with well established brands and long consumer royalty, vast resources to promote their brands and fight new challengers, well developed distribution networks and huge investments in tea packing plants in consuming countries.
- Tariff escalation and non-tariff restrictions on imports in some of the markets particularly the ones that have the potential for value-added tea products. Amongst the value added teas, instant tea attracts the highest duty. The import duty on instant teas ranges from 5% to 75% with the highest duty of 75% being levied in Iraq, 70% in Algeria and 60% in Egypt.
- Limited fiscal and monetary incentives and where provided such as TREO scheme (Tax Remission for Export Office), they are ineffective and not favorable to promote tea value addition.
- High levies on tea packaging materials for local consumption. Local tea packers pay a 25% duty on packaging materials and 16% VAT.
- High cost of equipment required for tea value addition.
- Tea for domestic consumption unlike other food products attracts VAT. Within the East African Community member states, Kenya is the only country that levies VAT on tea and this makes its tea uncompetitive within and outside the region. VAT is, therefore, treated as an additional cost of production by packers.

#### **RECOMMENDED TEA VALUE ADDITION STRATEGIES IN KENYA**

##### **• MARKET AND PRODUCT DEVELOPMENT SUPPORT BY THE GOVERNMENT**

The Tea Industry has continued to change the marketing pattern and strategies to other sectors such as the European, North American, Japanese and other sectors which are keen in importing tea in value added form to try and balance between tea exported out in bulk and value added form. The Government has also offered additional budgetary support for market development in emerging markets which are especially inclined to value added product. The Government of Kenya through the Ministry of Agriculture has attempted to address the value addition gap by proposing a value addition strategy through which it will offer support to entrepreneurs who would like to pursue value addition services. The proposed facilities will have a provision of tasting, blending and packaging of tea in accordance with trader specifications and consumer requirements.

##### **• ENHANCEMENT OF THE KENYA TEA BRAND**

In 2009, the Ministry of Agriculture through the Tea Board of Kenya launched a Mark of Origin for Kenyan Tea. This is a branding initiative that will encourage trading in 100% Kenya tea and ensure that Kenya tea does not lose identity once exported. Legal reforms are also underway to entrench the value addition regime. The Tea Act (2011) under review of the regulations is underway to create an enabling environment for value addition. The Act has given the Ministry of Agriculture through Tea Board of Kenya mandate for promotion and monitoring of tea trade hence supporting value addition initiatives.

##### **• COMPLIANCE WITH CONSUMER REQUIREMENTS**

Most tea factories and enterprises in Kenya have undergone various international certifications such as Fair Trade and Rain Forest Alliance Certifications which is applied to the packaging and production which have consequently increased the competitiveness for Kenya tea worldwide and especially in Value Added Markets.

## **9. CONCLUSION**

Despite the fact that tea is the leading cash crop in Kenya, Kenya has continued to be a producer of processed tea at primary level with very little product differentiation and value addition. This has constrained growth in profitability. Attractive and durable packaging is the main marketing tool to increase the market share of the company this is lacking in the current situation where tea is packaged in the traditional non attractive packs making as compared to other substitute competitive products such as drinking chocolate, coffee, sodas and water.

Kenya will realize better returns through higher prices and increased foreign exchange earnings through Tea Value Addition. Value addition will also increase employment opportunities, and enhance industrialization and greater technological development and thereby contribute significantly to the realization of Vision 2030.

## **10. RECOMMENDATION**

The tea industry stakeholders need to concert their efforts at all levels to enhance and embrace Tea Value Addition initiatives in order to make the tea industry more profitable, competitive, rewarding and sustainable.

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