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Farming, Entrepreneurship, and Market Access: Evidence from Chilean Wine Grapes

This paper studies the decision of farmers to become high-quality producers. In recent decades there has been a change in consumer preferences in the world towards high-quality products. This has provided opportunities but also presented challenges for small-holder farmers (Reardon and Berdegué, 2002; Anderson, 2004). For example, in developing countries credit is usually rationed because of lack of collateral (Eswaran and Kotwal, 1986). This paper provides evidence that lack of credit limits producer access to high-quality markets.

In the Chilean wine-grape market we observe a bifurcation of farmer types. “Quasi-subsistence” farmers produce traditional wine-grape varieties and complement their subsistence income with cash coming from wine-grape sale. On the other hand, we observe “entrepreneurial” farmers who produce classic varieties that have the potential to produce high-quality wines.¹

We use the entrepreneurial-choice literature to represent the decision of farmers to become high-quality producers. This literature studies the decision of individuals to become self-employed, as opposed to wage workers, and take on risky projects (e.g., Evans and Jovanovic, 1989; Blanchflower and Oswald, 1990; Buera, 2009; Quadrini, 2009). Its main prediction is that liquidity constraints bind and that capital is essential for starting and remaining in self-employment. We hypothesize that the choice of farmers of switching from quasi-subsistence farming to high-quality production depends on their assets. The entrepreneurial-choice literature also acknowledges the importance of entrepreneurial ability by indicating that the more able individuals should enter into entrepreneurship. In addition, we consider the possibility that the contracts that farmers have with specific wineries may also affect this decision.

To test these predictions, we run a regression of the probability of being a high-quality producer on wealth, access to credit, ability, and buyer heterogeneity, using data from 184 wine-grape farmers in Chile. We measure high-quality production through the crop-management practice of thinning wine grapes. In our empirical approach we first, explore the data as one sample and conduct linear regression. Second, given that the variables representing wealth could be endogenous, we instrument for them and use two-stage least squares. Third, we conduct a threshold test to detect potential non-linearities in the sample with respect to farm size (one of our wealth measures). Finally, given that this threshold results to be significant, we conduct threshold regression to explore the probability of thinning above and below the threshold.

The findings for the full sample indicate that in order to become high-quality producers, farmers need to be wealthy, have high cultivation ability, and need to contract with buyers that are interested in high-quality production. Further, we explore the effect of wealth in the split sample. We find that for the sample above the threshold, farmers who are classified as “high ability,” who invested in classic varieties, and who have high soil quality, all seem to increase the likelihood of thinning. Moreover, we use different measures of credit and find that getting a loan for investment or for production costs in the previous contract increases

¹We refer to “traditional” as those varieties that were introduced with conquerors in the 1500’s, such as País, and to “classic,” as those varieties that were introduced later, in the 1800’s, such as Cabernet sauvignon.
the likelihood of thinning in the sample above the threshold.

Although the positive effect of personal wealth on starting or participating in self-employment is well documented, we are not aware of previous work that views the transition from low- to high-quality supplier through the lens of entrepreneurship. We find that this framework provides strong explanatory power. In addition to liquidity constraints, grower ability and buyer heterogeneity are also important determinants of entrepreneurship.

References


