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# CLIMATE, SHOCKS, WEATHER AND MAIZE INTENSIFICATION DECISIONS IN RURAL KENYA

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# Climate, Shocks, Weather and Maize Intensification Decisions in Rural Kenya

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## *Abstract*

*We explore how climate, climate risk and weather affect maize intensification among smallholders in Kenya. We find that they all play an important role in maize intensification choice. The economic implications of this choice are also analyzed. We find that the share of maize area planted to hybrid seeds contributes positively to expected crop income, without increasing exposure to income variability or downside risk. The promotion of maize intensification is potentially a valuable adaptation strategy to support the well-being of smallholder farmers.*

Keywords: Climate Change, Maize, Smallholder farmer, Vulnerability, Kenya

JEL Codes: D81, O13, Q12, Q18

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## 1. Introduction

Farmers in Africa are among the most vulnerable to climate change. On the African continent, multiple stresses occur at multiple scales; African smallholder farmers, who are among the world's poorest, have limited capacity for adaptation (Boko et al., 2007). Kenya is heavily exposed to changing climatic patterns, with serious repercussions for the well-being of farming households (Oremo, 2013). Many areas of the country have registered rising seasonal mean temperatures over the last 50 years. Regional climate model studies suggest drying over most parts of Kenya in August and September, although climate impacts are likely to be unevenly distributed across the country (Niang et al., 2014).

Smallholder farm families pursue various adaptive strategies to cope with climate change, but intensification of production - e.g. increased use of hybrid seed and mineral fertilizer - is not generally considered to be one of them. Since the Green Revolution in Asia, researchers have debated whether the yields of improved varieties and hybrids are higher but also more variable, exposing poor farmers to greater risk (e.g., Anderson and Hazell, 1989). In general, empirical evidence on this point depends on the counterfactual (which varieties/hybrids are compared) and the geographical scale of analysis. In the major agricultural regions of Kenya, farm families depend on maize as a food staple and ready source of cash. Maize growers have high adoption rates and a history of growing maize hybrids with and without fertilizer (Mathenge et al., 2014). They have limited access to credit and no access to insurance, so they have a strong incentive to plant seed that reduces the variance of yields and limits their exposure to downside risk. Preliminary research by Jones et al. (2012), who considered several of the major maize-growing agro-ecologies, suggested that use of hybrids in maize production not only enhanced mean yields but also reduced downside risk, with no significant effect on yield variance.

Smallholder agricultural production in rainfed agriculture, like that found in Kenya, relies on environmental production conditions that are “exogenously” determined - largely outside the control of farm families (Sherlund et al., 2002). Yet, climate and soil characteristics are rarely incorporated into micro-economic analysis of crop and variety choice. Mutiso (1996) showed that farmers in southeastern Kenya follow local knowledge systems when choosing the time to prepare land and plant. Other agronomic factors also guide planting decisions, especially in areas with sparse rainfall (Sacks et al., 2010). Thus, it is important to account not only for

environmental conditions, including climate and soil quality, but also for factors influencing farm management choices and adaptation options, such as human capital (labor supply and quality), financial and physical capital (assets, access to credit, farm size and tenure).

We address two research questions in this paper. First, we ask how climatic shocks, weather and climate change affect smallholder decisions to *intensify* maize production. We measure intensification as the share of maize area per farm allocated to hybrid seeds. While controlling for relevant covariates as noted above, we differentiate and test the separate effects of climatic shocks, climate and weather on hybrid area shares. *Climate shocks* refer to the number of times during the previous decade that each village experienced a serious drought. The term *climatology* refers to climate normals. Climate normals are measured as the average weather condition over a 30-year period (1971-2010). *Weather* indicates the rainfall and temperature registered during the main rainfall season of the corresponding data collection year.

Second, we ask whether and how allocating a higher share of maize area in hybrid seeds per farm affects the vulnerability of smallholder incomes, expressed in terms of expected crop income, crop income variability and downside risk. Maize is the primary staple food grown by all smallholder farmers in the sample, across a wide range of livelihood types and farming systems. Mathenge et al. (2014) report that maize accounts for about 28% of gross farm output in the small-scale farm sector and that outside the semi-arid areas, 98% of households grow maize. Tegemeo Institute data, used by Mathenge et al. (2014) and here, show that the share of crop income in household income averages 45%, varying only between 44% and 48% over the years of the survey.

With reference to the portfolio theory of decision-making, we address the second question by using Antle's (1983) method of moments. Our econometric strategy reflects the structure of our data-generating process and conceptual frame. We apply our model to four waves of panel data collected in the major agricultural regions of Kenya, controlling for time-invariant heterogeneity by applying the Mundlak-Chamberlain procedure. We are interested in examining both the maize intensification decision and the relationship of maize intensification to income vulnerability in our two-stage econometric modeling. We also consider the potential endogeneity of input choices in crop income outcomes.

We contribute to the existing literature in several directions. First, from a methodological

perspective, we differentiate the roles of climatology, climate shock and weather on input choices in a micro-economic context. Second, we explore the intensification of staple food production through the dimension of hybrid seed. The Boserupian hypothesis (Boserup, 1975) suggests that population pressures on a declining environmental base generate incentives for intensifying food production. In a volatile environmental context, input intensification could aggravate smallholder vulnerability. We test this hypothesis.

Third, in the second stage of the estimation procedure we include, along with intensification variables, climatology, climate shocks and weather as explanatory factors, gauging the impact on crop income and risk across agro-regional zones. The inclusion of both climate and weather variables allows us to capture the full extent of underlying adaptation decisions (Bezabih et al., 2014). Thus, our work contributes to illuminating an ongoing debate concerning the appropriate measurement methods in adaptation studies.

Finally, we include detailed information on environmental production conditions, such as climate and soil characteristics at village level, and separate main and short season rainfall, which varies across Kenya's agro-regional zones, within years. Sherlund et al. (2002) have demonstrated the potential bias in production models of failing to control for soil quality. In terms of measurement techniques, we utilize the most advanced drought index available (SPEI). The SPEI is a multiscalar drought index that accounts for the fact that the impact of rainfall on the growing cycle of a plant depends on the extent to which water can be retained by the soil.

## **2. Theoretical basis**

A leading paradigm in models of seed-fertilizer adoption since the Green Revolution has been the portfolio theory of investment attributed to Markowitz (1952), articulated by Just and Zilberman (1983) in terms of trade-offs between the mean and variance of yield distributions where the choice variable was the crop area share allocated to new techniques (here, hybrid seed) with higher mean yields as compared to more traditional farmers' techniques (local maize, no mineral fertilizer).

However, the approach has been far less commonly applied in the analysis of natural resource management. We apply it in the context of intensification choices made under climate change and extend it to include skewness effects, following Antle's method of moments (1983).

Recent research has demonstrated the importance of the third moment in analyzing of climate-related risk in agricultural production (Koundouri et al., 2006; Di Falco and Chavas, 2009).

Notably, we assume that a farm family will maximize the following function:

$$\max_{\alpha_t} \alpha_t (E_t R_{t+1} - R_{f,t+1}) - \frac{k_1}{2} \alpha_t^2 \sigma_t^2 + \frac{k_2}{3} \alpha_t^3 \gamma_t \quad (1)$$

Where the family chooses to allocate the maize area share of  $\alpha_t$  to the riskier hybrid seeds at time  $t$  and the other terms are defined as it follows:  $R_{t+1}$  is the return to hybrid maize, from time  $t$  to time  $t+1$ ;  $R_{f,t+1}$  is the return to local maize, from time  $t$  to time  $t+1$ ;  $E_t R_{t+1}$  is the conditional mean (conditional on the farmer's information at time  $t$ , thus they are written with  $t$  subscript) of the maize area planted with hybrid seeds and  $\sigma_t^2$  is the conditional variance of the maize area planted with hybrid seeds.

The terms  $k_1$  and  $k_2$  are coefficients representing farmers' risk aversion to yield variance and skewness respectively. Higher terms  $k_1$  and  $k_2$  indicate more conservative farmers which hold less hybrid seeds.

We extend the standard mean variance model by adding skewness, defined as:

$$\gamma_t = E \left( \frac{X - \mu}{\sigma} \right)^3 = \frac{\mu^3}{\sigma^3} \quad (1)$$

Given the definition of  $\alpha_t$  we can re-define the overall variance of (maize) yields as:  $\sigma_{pt}^2 = \alpha_t^2 \sigma_t^2$ . Similarly, we define the skewness as:  $\gamma_{pt}^2 = \alpha_t^3 \gamma_t$ . The return on the input mix (the seeds portfolio) is a linear combination of the simple returns of the riskier and less risky inputs. By definition, the input that generates higher means (in this case, the intensifying input, hybrid seeds) also generates greater variance. One of the factors that can contribute to increasing the vulnerability of modern agricultural production systems is the utilization of a narrow range of genetic material in plant breeding, so that the different varieties grown by farmers are in fact closely related; another is the slow turnover of modern varieties in farmers' fields, although we have no evidence of such a situation in Kenya (Smale and Olwande, 2014).

We assume that the benchmark input set has sufficiently low risk, so that the solution of the problems is almost identical to the standard mean-variance model with a riskless asset. The

farm family prefers a high mean and low variance of returns on the mix. As in the standard mean variance model we assume that the farm family maximizes a linear combination of mean and variance of returns from inputs, with a positive weight on the mean and a negative weight on the variance. The farm family is averse to results skewed in a specific direction ( $\gamma_t < 0$ ).

By solving the first order condition of Equation (1) we can find the optimal share of maize land to be farmed with the riskier input set.

$$E_t(R_{t+1} - R_{f,t+1}) - k_1\alpha_t\sigma_t^2 + k_2\alpha_t^2\gamma_t = 0 \quad (2)$$

Defining:

$$\Delta = E_t R_{t+1} - R_{f,t+1}; \quad x = \frac{\Delta}{k_1\sigma_t^2}; \quad y = \frac{k_2\gamma_t}{\Delta}$$

The solution of the maximization problem can be also written as:

$$\alpha_t = \min\left(\alpha_t = \frac{1 - \sqrt{1 - 4xy}}{2xy}, \quad 1\right) \quad (3)$$

In cases where the yield skewness plays a small effect, an approximate solution, up to the first order in  $\gamma$ , is:

$$\alpha_t = \frac{\Delta}{k_1\sigma_t^2} + \frac{\gamma_t\Delta^2k_2}{k_1^3\sigma_t^6} + \dots 0(\gamma_t^2) \quad (4)$$

Where  $\frac{\Delta}{k_1\sigma_t^2} > \frac{|\gamma_t|\Delta^2k_2}{k_1^3\sigma_t^6}$  and higher orders are expected to be negligible, because of the way we defined the approximation.

Equation (4) indicates the share of (maize) land for which the farmer is willing to rely on from his riskier inputs (hybrid seeds). This share is equal to the risk premium divided by the conditional variance times a coefficient representing the risk aversion of the farm family plus a term capturing aversion to negative outcomes of the distribution of skewness. By including skewness in the model we can approximate downside risk exposure. Increased skewness of yield (income) implies lower exposure to downside risk. Downside risk refers to the probability of non-positive crop income for a smallholder farming family, which are potentially disastrous (Di Falco

and Chavas, 2009). Reducing downside decreases the asymmetry of the yield (income) distribution by shifting it toward higher outcomes, holding both means and variance constant (Menezes et al., 1980; Di Falco and Chavas, 2009). We can view the short-term decision of a farming family as intending to avert negative outcomes or yield fluctuations in a specific direction.

Figure 1 illustrates the result of the farmer’s maximization problem presented in Equation (4). The figure shows the optimal share of (maize) land planted to intensified inputs, for given ranges of variance, skewness and expected returns. Figure 1 has some interesting features: first, we notice that for high values of the variance term  $\sigma_t^2$  the distribution of yield’s skewness does not matter in defining the share of land allocated to the risky inputs  $\alpha_t$ , as indicated by the almost vertical boundaries lines for values corresponding to  $\alpha_t=0.1$  to  $\alpha_t=0.4$ . However, as variance decreases or expected crop income increase (i.e., we move on the right along the horizontal axis), the distribution of yields’ skewness (captured by  $\gamma_t$ ) becomes increasingly relevant in determining the family’s allocation to the risky input, up to a point where the variance is very low and only extremely adverse distributions of outcomes matter.

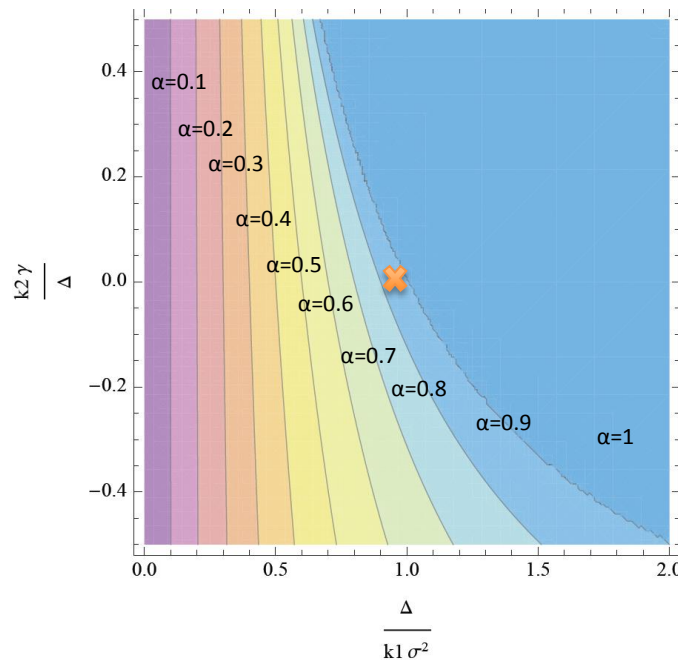


Figure 1: Optimal (maize) land partition

For example we can consider an initial land allocation between risky and less risky input combinations defined by the red cross in the graph, where 90% of the area is allocated to



intensified inputs and 10% to other input set. We assume that the distribution of skewness equals to zero and the ratio  $\frac{\Delta}{k_1\sigma_t^2}$  equals to almost 1.1 for this input choice.

If skewness raises to high enough positive outcomes, holding the variance constant will cause the share  $\alpha_t$  to rise to 1. However, as the distribution of skewness assumes negative outcomes (and the farm family fears crop failure) the share of cropland allocated to the intensified input decreases. Under downside risk aversion farm families are adversely affected by down side risk (e.g. risk of negative crop income). We expect that a downside-averse decision maker will invest in adaptation strategies to reduce such risk (Menezes et al., 1980; Antle, 1983 and 1987; Di Falco and Chavas, 2009). Our research interest in capturing how inputs contribute to the skewness of the crop income distribution is greatest when variance is neither too low (and there is very little risk associated with the second moment of the distribution of crop income) nor extremely high.

The precise shape of the cutting lines in Figure 1 depends on the values range attributed to the expected yields, their variance and skewness. These are determined by the type of crops grown and local environmental conditions. Figure 1 provides intuition concerning why, under some conditions, the third moment of the distribution of agricultural yields does not seem to be a key determinant of farmer input choices while some literature found it to be crucial (Koundouri et al., 2006; Di Falco and Chavas, 2009; Groom et al., 2008; Di Falco and Veronesi, 2014). For example, skewness and variance effects might be very different across a country like Kenya, which is characterized by the presence of various agro-regional zones. Notably, hybrid seed would be preferred in areas where the marginal productivity is higher.

### **3. Empirical approach**

#### *3.1 Data sources*

We draw on three comprehensive data sources in our analysis. The first source is household survey data collected by Egerton University's Tegemeo Institute of Agricultural Policy and Development with technical support from Michigan State University in four rounds (2000, 2004, 2007, 2010). Argwings-Kodhek (1999) provides a detailed description of the sample design implemented in consultation with the Kenya National Bureau of Statistics (KNBS). Survey

instruments are available online ([www.tegemeo.org](http://www.tegemeo.org)). All non-urban divisions in the selected districts were assigned to one or more agro-regional zones based on agronomic information from secondary data. The panel dataset comprises eight agro-regional zones. Within each division, villages and households in that order were randomly selected. The sample excluded large farms with over 50 acres and two pastoral areas. The final dataset used in this study contains detailed farm-level data from 1,243 agricultural households in 22 districts. Certain village-level covariates, such as population density and agro-regional zones, are included in these data and our analysis.

Second, we associate climate variables developed from the monthly average maximum, minimum and average temperature and monthly cumulative precipitation for 107 villages across Kenya from 1971. These climate data is from the Climatic Research Unit (CRU) CRU TS3.21 dataset (Harris et al., 2014). We compile climate data to match the main and short season, taking into account local differences in the length and timing of these two seasons. These data were used to calculate the SPEI Index. The SPEI Index is a multiscalar drought index that accounts for the fact that the impact of rainfall on the growing cycle of a plant depends on the extent to which water can be retained by the soil. This in turn depends on the characteristics of the soil and on the extent to which sunshine induces evaporation (Harari and La Ferrara, 2014). The indicator, developed by Vicente-Serrano et al. (2010), considers the joint effects of precipitation, potential evapotranspiration (PET) and temperature in determining droughts.

The SPEI index is an extension of the widely used Standardized Precipitation Index (SPI) (McKee et al., 1993), and can be used for determining the onset, duration and magnitude of drought conditions with respect to normal local conditions. Increasingly, the SPEI index is considered as an improved measure over similar indexes previously used (e.g. the SPI, which is based on the rainfall only, and on the assumption that temperature and potential evapotranspiration have negligible variability compared to precipitation, or the Palmer Drought Severity Index (PDSI) (Palmer, 1965), which is based on the soil water balance equation on a fixed temporal scale (between 9 and 12 months)) because it provides a better measure of the effective amount of moisture received by the soil (Vicente-Serrano et al., 2010; Harari and La Ferrara, 2014). We employ a 3 months SPEI Index (SPEI3), determined for the last month of the main rainfall season and comprising also the two preceding months, taking into account differences between agro-climatic zones in establishing the reference month.

Third, we draw on soils data at the village scale from the Harmonized World Soil Database, a partnership between the Food and Agriculture Organization (FAO) and the European Soil Bureau Network (FAO, IIASA, ISRIC, ISSCAS, JRC, 2012).

### 3.2. Estimation strategy

Our analysis is conducted in two stages. In the first stage, we analyze the determinants of maize intensification, paying particular attention to the role of past climatic shocks (captured by the SPEI3 index), access to market (captured by population density) and the price per kg of fertilizer used on dry maize from hybrid seeds during the main rainfall season<sup>1</sup>. Second, we probe how maize intensification, along with climate and weather, affect farmers' welfare under uncertainty, taking into account the heterogeneity in agro-regional conditions within Kenya. In this second step, we model the production technology as a stochastic production function, assessing its probability distribution using the sequential estimation procedure (Antle 1983; Kim and Chavas, 2003). The dependent variables in the second step of the estimation procedure are expected crop income, variance and skewness of crop income.

We test and control for the potential endogeneity of maize intensification decisions by estimating two-stage least squares. This is a robust estimation method that provides a standard starting point for applying instrumental variables (Angrist and Krueger, 2001). In the first stage of the estimation procedure, we use the frequency of climatic shocks, the logarithm of population density at village level and the price of fertilizer as instrumental variables for the decision on maize intensification. For identification purposes, some of the variables in the equation determining maize intensification (Equation 5) can be excluded from the crop income and risk equations (Equation 6).

In the first stage of our estimation we represent the optimal strategy undertaken by the representative farm household by Equation (5):

$$\alpha_{it} = \alpha (x_{it}^h, x_r^s, x_{rt}^v, x_{ikt}^p, x_{it}^f, x_{rt}^{CR}, x_{rk}^c, x_{rkt}^w, Z_a; \gamma) + \varepsilon_{it} \quad (5)$$

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<sup>1</sup> By dry maize, we refer to maize grown and harvested dry, rather than green. Price averaged over types, of which the dominant type for hybrid maize was Diammonium Phosphate (DAP).

The subscripts  $it$  denotes the  $i^{th}$  farm household in year  $t$ , while the subscript  $r$  is used for village-level observations and  $k$  indexes the rainfall seasons. Terms  $\gamma$  and  $\lambda$  are vectors of parameters, and  $\varepsilon_{it}$  is the household-specific random error term. The dependent variable  $\alpha_{it}$  is a continuous variable indicating the share of land planted with hybrid seeds of dry maize.

### 3.3 Explanatory variables

Definitions for each variable are presented in Table 1. Descriptive statistics of the variables used in this study are presented in Table 2.

Vectors  $x_{it}^h$ ,  $x_{it}^f$ , include household and other farm characteristics respectively. The human capital resources of the household are measured as the number of adult men in the household with a secondary education, which is highly correlated with women's education. Financial capital is measured in terms of livestock wealth, access to credit at the village level, and salaries and remittances, which provide liquidity that is uncorrelated with crop income. Farm physical capital is represented by scale of land cultivated, with a dummy variable indicating ownership by deed.

Vector  $x_{ikt}^p$  includes the farm price for fertilizer applied to maize from hybrid seed purchased during the main rainfall season,<sup>2</sup> while the vector  $x_{rt}^s$  includes soil quality information at village level. Vector  $x_{rt}^v$  includes the logarithm of population density at village level.

Of special interest is vector  $x_{rt}^{CR}$ , capturing how climatic risk affects intensification decisions. This vector includes a climate risk proxy stemming from the SPEI3 index, determined for the last month of the main rainfall season, taking into account differences between agro-climatic zones in establishing the reference month. Notably, we include the number of times during the previous decade that the value of the SPEI3 was lower than -1.65. This value indicates the exposure of the village to serious drought stress. The SPEI3 drought index expresses the incidence of past droughts (climatic shocks) as determinants of input choices. Vectors  $x_{rt}^c$ ,  $x_{it}^w$  include climate and weather information. Vector  $Z_a$  contains agro-regional zones fixed effects. We include them in the analysis, as we believe that being in a specific agro-regional zone affects significantly the farm management decisions. For examples, the way farmers adapt to

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<sup>2</sup> If the household did not buy fertilizer for this crop during the main rainfall season, the village's average is used.

climate change might differ significantly depending if the farm is located in a zone with bimodal or unimodal rainfall regime.

The role of variable  $\alpha_{it}$ , representing farmers decisions on the intensification of production, enters the second stage of our estimation strategy via the predictions from the system of equations (1). Through this second step, we investigate how intensification affect farmers' expected crop income under risk.

In order to capture the full extent of risk exposure we assess the impact of intensification strategies on the distribution of expected crop income (Equation 6a), its variance (Equation 6b) and skewness (Equation 6c). To do this, we follow Antle's moment-based approach to specify the stochastic structure of the model.

Accordingly, the estimated relationship between crop income risk equations, climatic variables, maize intensification decisions and other covariates is given by:

$$\ln y_{it} = \alpha + \beta_w w_{rkt} + \beta_c c_{rk} + \mu x_{i,t} + \varphi s_r + \vartheta \hat{\alpha}_{it} + \xi Z_a + \varepsilon_{it} \quad (6a)$$

$$\hat{\varepsilon}_{it}^2 = \alpha + \beta_w w_{rkt} + \beta_c c_{rk} + \mu x_{i,t} + \varphi s_r + \vartheta \hat{\alpha}_{it} + \xi Z_a + \check{\varepsilon}_{it} \quad (6b)$$

$$\hat{\varepsilon}_{it}^3 = \alpha + \beta_w w_{rkt} + \beta_c c_{rk} + \mu x_{i,t} + \varphi s_r + \vartheta \hat{\alpha}_{it} + \xi Z_a + \tilde{\varepsilon}_{it} \quad (6c)$$

The subscripts  $i$ ,  $t$ ,  $r$  and  $k$  are defined as in Equation 5. The dependent variable  $\ln y_{it}$ , denotes the logarithm of crop income for the  $i^{th}$  farm household at year  $t$ .<sup>3</sup> We incorporate both weather and climate measures as determinants of farm-level crop income and risk, as presented in Equation 6. Therefore,  $w_{rkt}$  is a vector of weather variables: temperatures (minimum and maximum) and precipitations (monthly cumulated) in year  $t$ , while  $c_{rk}$  is a vector of climate normals for the mean temperature and cumulated rainfall. Both vectors refer to village  $r$ , for the main rainfall season ( $k=1$ ). Vector  $x_{it}$  includes socioeconomic and physical farm characteristic variables at time  $t$ . Vector  $s_r$  contains soil quality variables, available at village's level.  $Z_a$  is a set of agro-

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<sup>3</sup> In order to treat the zero values in the sample, which would result into a reduction of the sample size, we add the constant 1 to each variable before taking the natural logarithm i.e.:  $\ln(\text{variable}) = \ln[1 + (\text{variable})]$ . By doing this we ensure that the logarithms will all exist.

regional zone fixed effects. These dummy variables can capture exogenous variables that vary by agro-regional zone but have not been measured.

The coefficients  $\beta_w, \beta_c, \mu, \varphi, \vartheta$  and  $\xi$  represent the vectors of parameter estimates for each associated vector of variables and  $\varepsilon_{it}$  is the error term. The composite error term is composed of a normally distributed random error term,  $u_{it} \sim N(0, \sigma_u^2)$ , and an unobserved household specific time invariant component ( $q_i$ ), as it follows:

$$\varepsilon_{it} = q_i + u_{it} \tag{7}$$

Similarly,  $\check{\varepsilon}_{it}$  and  $\tilde{\varepsilon}_{it}$  are the composite error terms for the variance Equation (6b) and the downside risk Equation (6c) respectively, and have the same distribution properties of  $\varepsilon_{it}$ .

The panel structure of our dataset necessitates the use of a fixed effect estimator that permits the time-variant regressors to be correlated with the time-invariant component of the error term, while assuming that these regressors are uncorrelated with the idiosyncratic error. This estimation provides consistent parameters even if there is correlation between the independent variables and time invariant unobserved heterogeneity, such as soil quality. The estimation of an instrumental variables model with fixed effect methodology would allow us to test and control for potential endogeneity caused by a correlation between decisions regarding intensification and vulnerability outcomes. However, standard fixed effect models rely on data transformation that removes the individual effect.

We have previously discussed the importance to include in our framework variables that are in their nature time-invariant regressors, such as climatology and soil quality variables. One way to include time-invariant variables while addressing endogeneity is to estimate a random effects model while controlling for unobserved heterogeneity using the Mundlak-Chamberlain approach (referred to as the pseudo-fixed effects model). Following Mundlak (1978) and Chamberlain (1982 and 1984) the right-hand side of our regression equation includes the mean value of the time varying explanatory variables. This approach relies on the assumption that unobserved effects are linearly correlated with explanatory variables. Thus the unobserved household specific time invariant component in Equation (7) can be specified as:

$$q_i = \zeta \bar{x} + v_i$$

where  $\bar{x}$  is the mean of the time-varying explanatory variables within each farm household (cluster mean),  $\zeta$  is the corresponding vector coefficient, and  $v_i$  is a random error unrelated to the  $\bar{x}$ 's. The vector  $\zeta$  will be equal to zero if the observed explanatory variables are uncorrelated with the random effects. The use of the Mundlak-Chamberlain device also addresses the problem of selection and endogeneity bias where these are due to time-invariant unobserved factors, such as household heterogeneity (Wooldridge, 2002). If we failed to control for these factors, we would not obtain consistent parameter estimates. Moreover, estimation of parameters  $\zeta$  allows us to test for the relevance and strength of the fixed effects via an F test, performed for the endogenous variable.

#### **4. Results**

First-stage regression results for the potentially endogenous variable are reported in Table 3. Frequent past climatic shocks, as manifested by drought incidence, reduce the maize area share per farm allocated to hybrid seeds. Looking at the weather variables, extreme temperature influences maize intensification. Maximum temperature has a negative (insignificant) impact on intensification of production at an increasing rate (significant), while minimum temperatures have the opposite signs with the same significance. Higher rainfall has a significant, positive correlation with hybrid seed use, at a decreasing rate. Farmers in areas where the weather is more favorable tend to allocate more maize area to hybrid seeds; temperatures are lower in the areas with the highest historical adoption rates.

Population density has positive correlation with maize intensification, consistent with the Boserupian hypothesis. The presence of educated men in the household has a positive impact on the adoption of maize hybrid seeds, since education provides access to information, services and communication, as well as the potential to utilize these more effectively.

Fertilizer price has the expected negative sign but is not statistically significant determinant of maize area shares planted to hybrid seed. Other research in Kenya has suggested that Kenyan farmers tend to apply non-optimal quantities of mineral fertilizers. Ogada et al. (2010) found that most Kenyan farm households apply insufficient quantities of mineral fertilizers; Sheahan (2011) and Marenja and Barrett (2009), found the opposite. Our empirical model does not enable us to draw conclusions regarding the quantitative response of fertilizer

application rates on maize to price variation, but only regarding the jointness of use of mineral fertilizers and hybrid seed. In about 90% of the plots in our dataset where maize hybrid seeds are planted during the main rainfall season, mineral fertilizers were also applied.<sup>4</sup> Also using the Tegemeo dataset, Smale et al. (2015) found a strongly significant, and expected negative sign between nitrogen nutrient kgs per ha of maize and the fertilizer price.

Wealthier farm families are more likely to plant larger share of their land with hybrids. There is no statistically significant evidence that those farmers living in villages with less binding expenditure constraint are planting larger land shares with hybrid seeds. Credit is not provided directly for maize production in Kenya, but farmers who obtain credit for other purposes may also be more likely to plant hybrids (such as tea growers in the highlands). A larger land endowment is negatively associated with the land share allocated to maize hybrid seed planted, suggesting that larger land owner might allocate larger land share to other crops, such as cash crops, instead of staple crops. Soil quality strongly affects intensification decisions.

Table 4 reports the results for the second stage regressions. We address the issue of instruments' relevance using an F test of the joint significance of the excluded instruments, reported at the bottom of Table 3. The F statistic is greater than 10. This result indicates the strength of the chosen instruments (Staiger and Stock, 1997). The choice of instruments seems appropriate and we turn to discussing our main regression results.

Column (1) reports the impact of intensification of production on expected crop income. Consistent with previous research, larger shares of maize area allocated to hybrid seed per farm tends to positively affects expected crop income (Jones et al., 2012; Mathenge et al. 2014). To capture the full extent of how these management decisions determine risk exposure we also report both the farm-specific, variance function (column 2) and the skewness function (column 3) for crop income. We find no evidence that larger share of land allocated to dry maize hybrid seeds (intensification) increases risk (consistent with Jones et al. 2012), either in terms of variance or skewness of the distribution of crop income. Share of maize area allocated to hybrids has no significant impact on either the variance or the skewness of the crop income. Thus,

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<sup>4</sup> The remaining 10% observations has missing values regarding the application of mineral fertilizers in the plot, thus we cannot exclude that the percentage of plot farmed with hybrid seeds where mineral fertilizers was applied is even higher.



planting a greater area with maize hybrid seed planted contribute positively to mean crop income, with no statistically significant impact on the other risk equations.

In general, long-term impacts are larger than short terms one, a result also found in Bezabih et al., (2014). Looking at weather, the squared temperature and precipitation coefficients are generally significant. This finding implies that the model is nonlinear. The fact that the squared terms are positive or negative reveals that seasonal effects are convex or concave, respectively. The maximum diurnal temperature correlates negatively to expected crop income, whereas higher minimum temperature is beneficial, up to a maximum of 16.6°C. Furthermore, higher diurnal temperature are associated with crop failure. Several agronomic studies confirm that maize reacts differently to maximum and minimum temperature (Harrison et al., 2011). Rainfall during the current main rain season has a bell-shaped relationship with crop income. Looking at the crop income equation (column 1) we also notice that the coefficients associated to temperatures are much larger than the coefficients associated to rainfall. This result confirms those of Kabubo-Mariara and Karanja (2007), who concluded that in Kenya the temperature component of global warming is much more important than precipitation. Interestingly, weather has an impact on the third moment of the distribution of crop income, but not climate.

The impacts of climate normals on expected crop income are very similar, generally larger but not statistically significant. An increase in rainfall climatologies enhances the risk associated to the variance of the distribution of agricultural yields, as well as the risk of crop failure. This result is probably related to the fact that most of the agriculture in the country (and in our sample) is rainfed and depends strongly on the quantity and distribution of rainfall across space and time. An increase in mean temperature climatologies does not have a statistically significant impact on the expected mean and the variance of crop income but it impacts higher moments of the distribution of crop income, with a positive impact of the skewness of crop income, up to 25.7°C.

Soil quality is an important determinant of farm crop income. Higher values associated to the gravel variable indicate higher percentage of materials in the soil that are larger than 2mm. In areas where this type of soil is predominant, farming is more difficult and plant life is sparser. Notably, the higher the value associated to gravel soil, the lower the ability of the soil to retain moisture, and the lower the presence of mineral nutrients. Henceforth, the negative coefficient

associated to this variable complies with our expectations. pH is a measure for the acidity and alkalinity of the soil, measured in concentration levels ( $-\log(H^+)$ ). pH between 5.5. and 7.2 (acid to neutral soil) offers the best growing conditions, and the mean value of the sample is in this range. Higher pH (associated to alkaline soils) is negatively correlated with crop income. Furthermore, farmers in Kenya tend to apply DAP as main fertilizer type on dry maize from hybrid seeds, when they need to increase the soil pH. This application might however also increase acidity of the land over the medium-long term.

Farm size, as expected, plays an important, positive role in determining crop income, as does the value of livestock assets. Higher shares of remittances and other salaries in the total household income negatively affect crop income, probably because farmers with outside options in terms of income diversification have lower incentives to take management and investment decisions to improve maize farming conditions.

Whether the family has a deed title over the land it operates is not statistically significant on expected crop income. However, the associated coefficient is negative, indicating that land tenure insecurity could be detrimental to crop income. Since the ratification of the new constitution in Kenya, land tenure and entitlement has been a prominent concern. This finding suggests that land certification could be an effective policy instrument to buffer against climate anomalies.

## **5. Conclusions and implications**

In this paper, we have analyzed two major research questions. First, we have explored how climatology, weather, and climate shocks, other factors held constant, affect maize intensification. Second, we have tested whether maize intensification affects the vulnerability of smallholder farmers to crop income variability and downside risk, in the presence of these factors. We have defined maize intensification as the maize area share per farm allocated to hybrid seed (much of which is fertilized). Drawing from and extending the portfolio theory of investment choice, we estimated a two-stage model to identify the determinants of input use and assess the effects of input use on the mean, variance and skewness of crop income among smallholder farmers in Kenya. We focus on maize production, considering the importance of this crop not only as a food staple but also an income source for in Kenya. In order to include time-

invariant variables such as soils and agro-regional fixed effects, while addressing endogeneity, we estimate a random effects model while controlling for unobserved heterogeneity using the Mundlak-Chamberlain approach (referred to as the pseudo-fixed effects model). We extend the portfolio investment approach previously applied to the analysis of input use decisions by incorporating and differentiating the effects of weather, climate change and climatic shocks.

Our approach enables us first to demonstrate that maize intensification is strongly affected by weather, climate shocks and climatology, in addition to commonly cited, household-farm characteristics such as education, wealth, access to credit and off-farm earnings. Next, we find that maize intensification has a positive effect on expected crop income but has no significant effect on the crop income variability or downside risk. Moreover, relying on a higher scale of hybrid seed use, which is negatively associated with persistent climatic shocks, is not enough to reduce statistically significantly the likelihood that crop income falls below a given threshold (downside risk). Importantly, cropping system decisions are related to longer-term investment choices, while decisions on specific hybrid types are rather annual decisions.

Thus, maize intensification is not in and of itself an effective strategy in the face of climate change and climate shocks. Further, our results suggest that farmers are not adapting optimally to climate change. Suboptimal choices might reflect multiple market failures, such as credit constraints, poor access to input and output markets, information asymmetries and commitment failures.

In addition to these major findings, our empirical analysis confirms the need to agro-regional zones and soil quality variables in micro-economic models of input use and adaptation strategies. Omission of these factors could cause biased estimates of included coefficients. Regression results support the Boserupian theory that rising population density provides incentives for the shift toward more intensive farming systems. Finally, we find trade-offs between nonfarm employment and crop income, indicating changing dynamics of income in rural communities as Kenya urbanizes. Our findings lead us to recommend that the Government of Kenya play an active role in encouraging smallholder adaptation to changing climate patterns and climate shocks. In Kenya, multiple market failures include poor or non-existent insurance, so that farmers use other risk-coping mechanisms, which can be weak (Fafchamps, 1992; Kurosaki and Fafchamps, 2002). Safety nets typically provide only limited support (Dercon and Krishnan,

2000; Dercon, 2004), while off-farm, non-covariant income is limited in more remote rural areas. In this context, smallholder maize growers need other incentives than the use of hybrid seed as a strategy to buffer against downside risk. Not only do smallholders need continued improvement of access to well-adapted hybrid seed and other inputs through decentralized, competitive markets but also effective, widely-diffused market information services and other insurance mechanisms. Promoting knowledge formation among farmers concerning weather, climate, production and post-harvest handling, and other adaptation strategies, would be beneficial.

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**Table 1: Variables Definitions**

Variable	Description
<b><u>Farm specific variables (Source: Tegemeo)</u></b>	
Crop income	Value of crop production minus input and land preparation costs (labor and seeds costs excluded).
Price fertilizer (kes)	Farm price fertilizer for dry maize from purchased hybrids. If the household did not buy fertilizer for this crop category, the village's average is used.
Educated men	No of adult men with secondary education
Livestock assets (KES)	Total nominal value (KES) of livestock assets
Credit village	Proportion of village households that received credit, by year
Salaries & remittances	Share of salaries and remittance earnings in total household income
Land	total household land area (ha)
Land title deed	=1 if land owned with no title deed, 0 otherwise
<b><u>Village-specific climate characteristics (Source: CRU TS3.21)</u></b>	
SPEI3 Index	3 months Standardized Precipitation-Evapotranspiration Index (SPEI3) for the last month of the main rainfall season (January, July or August, depending on the division and agro-regional zone to which each village belongs) and the two preceding months. We calculated the SPEI index manually, using the R routines developed by Vicente Serrano et al. (2010). SPEI index for each location is based on monthly precipitation and rainfall at village level, downloaded from the CRU TS3.21 dataset (Harris et al., 2014) for the period 1971-2012.
Droughts_165	Number of times in the last decade <sup>#</sup> the value of the spei3 was <-1.65 in the last month of the main rainfall season.
Temperature max (°C)*	Monthly average maximum air temperature (°C) during the major rainfall season
Temperature min (°C)*	Monthly average minimum air temperature (°C) during the major rainfall season
Temperature average (°C)*	Monthly average average air temperature (°C) during the major rainfall season

Rainfall (mm/mo)*	Cumulated rainfall (mm/mo) during the major rainfall season
Temperature average climatologies*	Average air temperature (°C) 1971-2010 during the major rainfall season
Rainfall climatologies (mm/mo)*	Cumulated rainfall (mm/mo) 1971-2010 during the major rainfall season

**Village-specific soil characteristics (Source: World Soil database)**

AWC_mm	Available water storage capacity class of the soil unit, measured in mm/m
Ph top soil (-log(H+))	pH measured in a soil-water solution. It is a measure for the acidity/alkalinity of the soil
Gravel top soil (% vol)	Volume % gravel (materials in a soil larger than 2mm) in the topsoil (i.e. 0-30 cm) (% vol)

**Village level socio economic variables & Agro-ecological Zones**

Population density	Village population density (cap/km <sup>2</sup> )
Agro-regional zone	HPMZ high potential maize zone (26.6%); CHI central highlands (19.4%), WLO western lowlands (12%); WTR western transitional (11.7%); ELO eastern lowlands (11.3%); WHI western highlands (10.3%); CLO coastal lowlands (5.9%); MRS marginal rain shadow (2.7%). Percentages indicate the frequency of farms in our sample in each agro-regional zone.

\*We take into account the relevant cropping season: e.g. for villages in the Rift Valley, the reference period is March (year-1) to (August year-1). # Reference Decades: 1989-1999 for 2000; 1993-2003 for 2004; 1996-2006 for 2007; 1999-2009 for 2010.

**Table 2: Descriptive Statistics**

<b>Variables</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
<b><u>Farm-specific variables</u></b>				
Crop income	87,911	142,264	0	3,883,123
Hybrid seeds (maize land share)	0.338	0.323	0	1
Price Fertilizer (kes)	37.08	18.03	0.32	700
Educated men	0.89	0.98	0	10
Livestock assets (kes)	81,366	217,682	0	8,679,900
Credit village	0.47	0.30	0	1
Salaries & remittances income share	0.18	0.24	0	1
Land	5.80	8.72	0	157
No land title deed dummy	0.36	0.48	0	1
<b><u>Village-specific climatic variables</u></b>				
Temperature max (°C)	26.56	3.63	19.12	33.47
Temperature min (°C)	14.04	3.76	7.5	23.95
Temperature average (°C)	20.27	3.62	13.3	28.67
Rainfall (mm/mo)	708.75	209.29	145	1154.1
Temperature average climatologies (°C)	19.57	3.69	13.61	27.89
Rainfall climatologies (mm/mo)	708.95	186.32	184.58	946.44
SPEI3 Index	-0.18	1.01	-2.28	2.24
Droughts_165	0.74	0.72	0	2
<b><u>Village-specific soil characteristics</u></b>				
AWC_mm	149.42	3.77	125	150
Gravel top soil (%vol)	1.25	4.09	0	28
Ph top soil (-log(H+))	5.75	1.04	4.5	8.9
<b><u>Village-specific socio economic variables</u></b>				
Population Density	363.47	214.88	16.43	1,245.11



**Table 3: Estimation results – First Stage regressions**

	share acreage under purchased hybrids	
<b>Droughts_165</b>	-0.0565***	[0.0085]
<b>ln population density</b>	0.3544***	[0.0536]
<b>ln fertilizers price</b>	-0.0167	[0.0103]
Temperature max	-0.2031	[0.1486]
Temperature max squared	0.0059**	[0.0028]
Temperature min	0.0583	[0.0648]
Temperature min squared	-0.0042**	[0.0021]
Rainfall	0.0004*	[0.0002]
Rainfall squared	-2.67e-07**	[1.40e-07]
Temperature average climatologies	-8.3840***	[1.1118]
Temperature average climatologies squared	0.1509***	[0.0234]
Rainfall climatologies	-0.0133***	[0.0037]
Rainfall climatologies squared	7.98e-06***	[2.26e-06]
AWC_mm	0.0008	[0.0030]
Ph top soil	0.0895***	[0.0116]
Gravel top soil	0.0089***	[0.0019]
ln livestock assets	0.0060*	[0.0031]
ln credit village	0.0459	[0.0324]
no land title dee dummy	-0.0049	[0.0092]
ln educated men	0.0267**	[0.0119]
ln salaries & remittances income share	0.0561	[0.0347]
ln land	-0.0465***	[0.0126]
	agro-regional FE	yes
F test of excluded instruments		F(5, 4043)=31.19
Observations		4,085

*Notes:* pseudo-fixed effect estimation. Robust standard errors in brackets.

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

**Table 4: Estimation results – Second Stage regressions (Pseudo Fixed Effects Estimation)**

	(1)	Crop Income	(2)	Variance	(3)	Skewness
share acreage under purchased hybrids	0.9634***	[0.2562]	-0.6262	[0.4717]	2.0910	[2.5907]
Temperature max	-3.2067***	[0.4628]	0.8606	[0.9954]	-13.1331*	[7.966]
Temperature max squared	0.0613***	[0.0091]	-0.0149	[0.0190]	0.2522*	[0.1524]
Temperature min	1.9460***	[0.2054]	-0.4286	[0.4601]	5.2394	[3.6946]
Temperature min squared	-0.0643***	[0.0071]	0.0130	[0.0146]	-0.1719	[0.1156]
Rainfall	0.0067***	[0.0006]	-0.0003	[0.0007]	0.0031	[0.0049]
Rainfall squared	-4.34e-06***	[3.85e-07]	-1.63e-08	[4.49e-07]	-1.85e-06	[3.11e-06]
Temperature average climatologies	0.6627	[3.6340]	-19.9585	[18.377]	229.85***	[78.62]
Temperature average climatologies sq.	0.0180	[0.0781]	0.3690	[0.3646]	-4.469***	[1.471]
Rainfall climatologies	-0.0061	[0.0069]	0.0350*	[0.0180]	-0.242***	[0.084]
Rainfall climatologies sq.	0.0000	[0.0000]	-0.00003*	[0.00001]	0.0002**	[0.0001]
AWC_mm	-0.0012	[0.0135]	0.0603**	[0.0274]	-0.0089	[0.1249]
Ph top soil	-0.4419***	[0.0450]	0.0858	[0.0679]	0.0062	[0.3619]
Gravel top soil	-0.0451***	[0.0085]	-0.0064	[0.0167]	-0.0825	[0.0694]
In livestock assets	0.0451***	[0.0097]	-0.0264	[0.0169]	0.1870	[0.1392]
In credit village	0.3183***	[0.1017]	0.3672*	[0.1896]	-2.0105*	[1.0878]
no land title dee dummy	-0.0394	[0.0276]	-0.0741**	[0.0303]	0.2420	[0.2118]
In educated men	0.0198	[0.0391]	0.0608	[0.0582]	0.1322	[0.4226]
In salaries & remittances income share	-1.0470***	[0.1439]	0.5477	[0.4623]	-5.0775	[4.0287]
In land	0.4653***	[0.0469]	0.1219	[0.0775]	-0.5191	[0.5811]
Constant	5.53	[8.37]	-62.80*	[37.19]	493.7***	[161.5]
Agro-regional FE		Yes		Yes		Yes
Observations		4,085		4,085		4,085
Number of hhid		1,166		1,166		1,166

*Notes:* Pseudo-Fixed effect estimation. Robust standard errors in brackets. \*\*\* p<0.01, \*\* p<0.05, \* p<0.1.

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