

MARKET SYSTEMS DEVELOPMENT - FACILITATION TACTICS LEARNING SERIES

Financing Mechanisms Series: BUYER CHECK-OFF as a financing strategy

Designed by EcoVentures International 2016

Let's explore a financial mechanisms for improving Farmer Productivity that is particularly applicable across many countries and market systems:

Buyer Check-off

Buyer's Challenge: Larger buyers often need to lock in supply and ensure they are going to get a minimal level of quality and quantity, or a specific variety.

The buyer may, for example, have a contract with a unique end market that can pay a higher price if certain quality and volume requirements can be achieved.

Buyers tend to struggle to meet the quantity and quality needs from the open market

But ... what if buyers provide seeds or other specific inputs to farmers?

... then they can reduce the risk of non-compliance on quality.

So ... the buyer accesses quality seeds and a fertilizer blend that is important to achieve quality.

The buyer meets with farming communities (that they have long, established agreements with) to explain the new opportunity.

Hmmm?

How does a buyer check-off system work?

Firstly, let's look at how the buyer might explain the concept to farmers if they use a credit-based version of the buyer check-off system.

Credit-based buyer check-off system

The buyer discusses the process of providing input on credit where farmers pay off the debt via crop.

The buyer and farmers agree on the terms, including the cost of the inputs and the buying process at harvest.

Great! We've agreed on a floor price at planting!

Or we could have agreed on a process for negotiating and setting the price and agreeing on other terms (such as quality).

The buyer provides inputs to farmers that are on contract or who agree to the scheme or have proven their commitment.

The farmers use the input, grow the crop, and deliver the crop to the buyer.

The buyer grades and weighs the crop/product ...

... keeps part of proceeds to repay the credit, giving remainder to the farmer.

What are interesting variations of a buyer check-off system applied in practice?

Farmers could agree to a community assurance scheme to give the buyer confidence they will get repaid in crop.

Or ... the buyer could up a farmer management system.

I can track individual farmer performance (as part of my preferred supplier program) and farmer pre-purchases!

Buyers could also set up criteria for selecting high performing farmers for additional investment/support.

Preferred Supplier Program

Quality: _____

Volumes: _____

Adherence to agreements: _____

Hmm?

How is this financing mechanism useful to buyers and farmers?

Buyers can lock in supply and ensure the quality/variety required

Farmers can minimize risk of holding cash (since the deal is a bartered deal) and have easier access to quality inputs.

For the market system this can create a foundation of trust and minimize market risks for both the buyer and farmers.

To be effective, buyer-farmer relationships need to be strong, with buyers investing in building relationships with their farmer suppliers.

Are there any risks in a buyer-check off mechanism?

This type of mechanism can concentrate risks with one market actor (the buyer), making the overall system more fragile.

This type of mechanism tends to work only when the channel is tightly closed, and there are limited options for farmers to grow other crops.

We operate in a monopoly or there are no other buyers because of limited end market contracts.

If farmers have access to other buyers or they can easily shift to another crop these mechanisms tend to be highly risky.

To counter these risks, there needs to be a foundation of trust between buyer and farmers ...

Preferred Supplier Program

Quality: _____
 Volumes: _____
 Adherence to agree...

... and buyers need to institute management practices that limit their exposure to farmers that cannot perform effectively, or will not commit to and adhere to agreements.

What does a buyer check-off system look like that does not involve credit but rather uses a pre-pay approach?

The buyer sets up a pre-payment mechanism that includes a discount for all farmers who pay for their inputs through the buyer.

DISCOUNT!

The buyer gives their farmer suppliers the option to participate in a rolling check-off process. ...

Rolling check-off?!

... for each coming season the participating farmers sell crop to the buyer

Check-off System:

Farmer: _____
 Crops sold: _____
 Pre-paid next inputs: Yes No

... the buyer uses portion of their crop proceeds to pre-buy discounted inputs for the next season...

Why do some buyers consider using a buyer check-off system that does not involve credit?

A non-credit version can lower the costs by limiting the need for credit.



The lower cost savings should be passed onto the farmers!



By moving away from credit, the buyer substantially reduces their risk, as well as reducing risks throughout the whole market system.

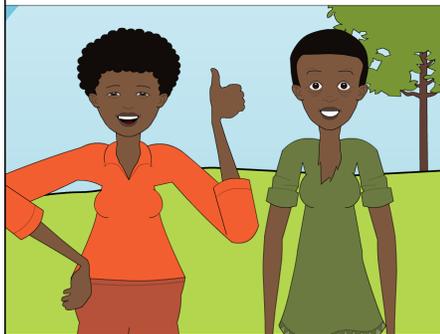
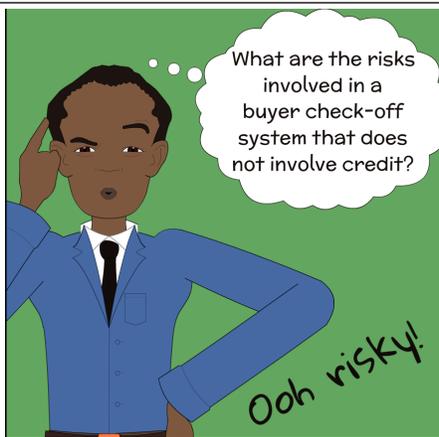
The buyer should pass on part of the benefits from reducing the risk to the farmer via additional discounts.

There is improved cash flow management at buyer and farmer level.



Yay!

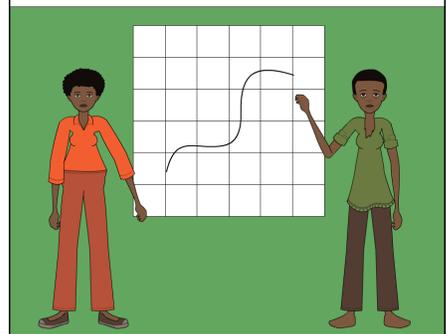
Reduced relationship pressure between buyer and farmer should mean a more robust outgrower/buying scheme.

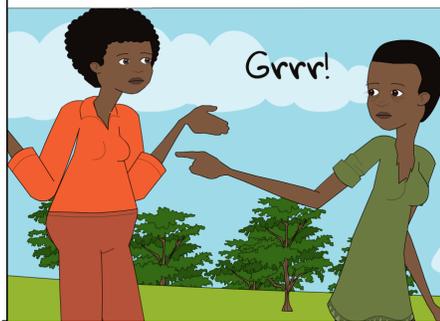
What are the risks involved in a buyer check-off system that does not involve credit?

Ooh risky!

The primary risk is the level of trust between the farmer and the buyer. These mechanisms require trust to be viable.



Misuse or poor cashflow management by the buyer could create substantial disputes and increase the levels of distrust throughout the system.



Grrr!

Buyer's inventory management could be highly stressed once she begins pre-selling inputs, which can increase the levels of distrust.



Ineffective, inappropriate or improperly applied inputs that do not provide a return to the farmer ...

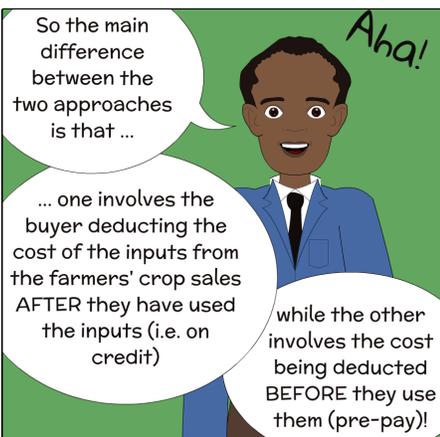


... are likely to create disputes increasing the fragility of the buyer-to-farmer relationship.

So the main difference between the two approaches is that ...

... one involves the buyer deducting the cost of the inputs from the farmers' crop sales AFTER they have used the inputs (i.e. on credit)

... while the other involves the cost being deducted BEFORE they use them (pre-pay)!



Aha!

Yes!

There is a huge potential to help buyers to set up a buyer check-off systems in many different sectors.



Could this work in your contexts?

