Business Innovation Facility

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Inclusive business in practice – Case studies from the Business Innovation Facility portfolio

ACI Agribusiness: Designing and testing an integrated contract farming model in Bangladesh

This report is one of a series of 'deep dive' case studies that seeks to understand inclusive business in practice. The series explores contrasting inclusive businesses, all of which have been supported by the Business Innovation Facility.

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Foreword: An introduction from the authors

When we visited Rajbari farmers in July 2013, before the project's summer tomato harvest, farmers were excited by the potential of the contract farming model to generate additional income. *"We can make more money with the same amount of work,"* exclaimed one farmer. The farmers were also relieved that they no longer needed to worry about finding a buyer for their crops.

However, as it turned out, there were also downside risks for the farmers, including the potential for financial duress due to crop loss. While the bulk of the fieldwork and analysis for this case study was done in July-August 2013, it has necessarily been updated through interaction with the ACI and BIF team since. At the time of the final editing of this case study, the impacts of the poor harvest were being addressed by the partner organisations in the hope that the pilot has no long-term negative consequences. It is certainly a clear example of the ups and downs of pilot projects, and the production risk that underlies all agricultural models, however carefully constructed they are.

ACI acknowledges that there are a number of adjustments that still need to be made, so that future iterations of its contract farming operating model are successful. Like many new inclusive business models, it is a work in progress. This case study provides insights into that journey, and reveals wider lessons for other companies developing inclusive business models, particularly in agriculture. We hope you find it as interesting as we did.

Acknowledgements

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Table of Acronyms

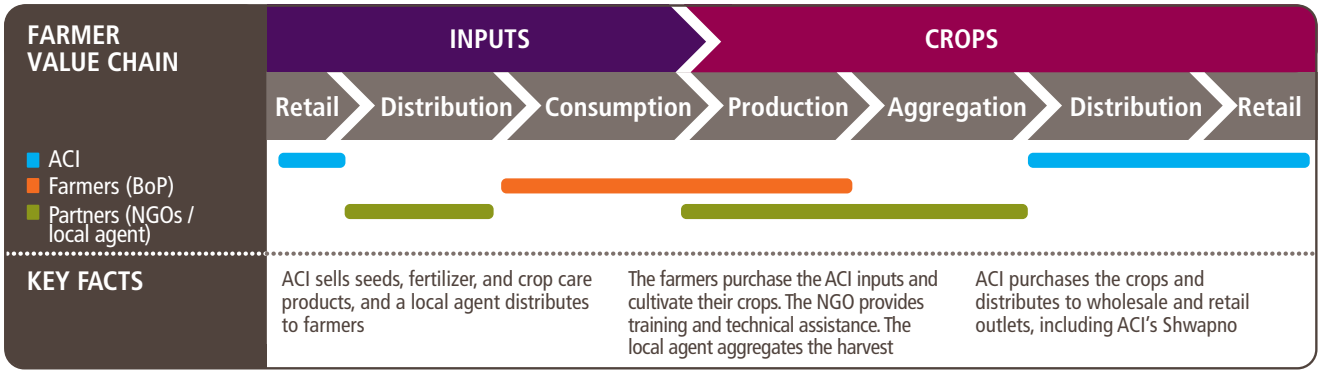
BDT	Bangladeshi Taka
BoP	Base of Pyramid
NGO	Non-governmental Organisation
RCL	Renaissance Consultants, Ltd.
SBU	Strategic Business Unit

Executive summary

Dhaka-based Advanced Chemical Industries (ACI) Limited is a leading corporate in Bangladesh with a vision to improve the quality of the life of people through responsible application of knowledge, skill and technology. The company's Agribusiness division launched a contract farming initiative in 2012 that seeks to expand its customer base, increase brand recognition, facilitate intra-company collaboration, and improve supply chain stability for its retail outlet, Shwapno.

ACI has a number of business units engaging in different aspects of agriculture and with their own field force or sales agents who, for example, sell seeds, provide crop care services, or source produce for retail. The contract farming initiative emerged from an agreement across the business units to trial an approach that was innovative in two respects: it would be an integrated approach across business units in their engagement with farmers; and it would be a contract farming approach that offered marginalised farmers the opportunity to access quality inputs and higher returns. The next step was a detailed analysis of different contract farming options available, for which the Business Innovation Facility provided support. An intermediary model was chosen in which an NGO acts as an intermediary between ACI and the farmers.

Figure 1: *Overview of ACI Agribusiness Integrated Contract Farming Project*



The ACI operating model is noteworthy among the many other contract farming models, in that ACI is both supplying the inputs and also purchasing the crop yield. It does so through an intermediary that distributes the inputs to the farmer at the beginning of the growing season, and then aggregates the produce and sells it to ACI Cropex, once the crops are harvested. Farmers receive financing for the inputs, under the assumption that the loans will be paid once farmers sell their harvest. ACI's contracts with the farmers guarantee a market for their produce at a fair price, reducing the risk of loan default. The company's other intermediary partner, an NGO, provides the farmers with technical assistance on how to grow the crop and maximise their yields.

In 2013, a pilot project growing summer tomatoes took place in Rajbari, a district in central Bangladesh. A local microfinance organisation (MFI), provided financing to the farmers to purchase inputs, and expectations were high for improved yields, revenues and profits. However, inclement weather and disease decimated the crops and the pilot harvest was not a success.

This set back did not prevent ACI from wanting to continue developing the contract farming model, which is strategically important to the company. Beyond the potential for increased revenues in the future, the model improves internal collaboration within ACI, increases brand recognition for its products, expands the market for agricultural inputs and helps to secure its supply chains. ACI plans to continue with the development of the model in future seasons once the company feels that the operating model has been appropriately adjusted to address the shortcomings discovered during the pilot.

Although the initial pilot failed, it yielded valuable lessons that ACI will build on going forward. These include the need for improved communication, both within the company to build stronger buy-in internally, and between the company and its intermediary partners and farmers, so that roles and expectations are more clearly defined and good agricultural management practice is ensured. The pilot also revealed the need to better manage risk for the low-income farmers who were initially left financially vulnerable when the crops failed. Increased training and the use of more proven crop varieties will help, but additional steps may need to be taken.

Figure 2: *Summary of ACI Agribusiness Integrated Contract Farming Project impacts*

ACI Agribusiness Integrated Contract Farming Project

Country: Bangladesh
Sector: Agriculture
Product: Summer tomatoes
BoP: Smallholder farmers

Inclusive business model:

Providing financing, inputs, training and guaranteed crop purchases to farmers aimed at reducing overall costs and increasing yields. BIF support to determine the appropriate contract farming operating model and monitoring and evaluation support.

Market opportunity:

- Increased brand recognition for ACI farm inputs
- Secure supply chain of produce for Shwapno retail outlets
- Improve collaboration between ACI divisions

Commercial results:

- The pilot did not demonstrate the commercial viability of the contract farming model due to crop loss
- The model will be further refined based upon lessons learned in the pilot

Development impacts:

- Benefits of guaranteed harvest purchase and overall reduced cost were not realised
- Crop loss left farmers initially exposed to risk of loan default; post-harvest arrangements made to protect farmers from financial loss

Future plans:

- Generate $500,000 revenue and ROI equal to 14% within 3 years
- Expand into new varieties and implement changes to farming methodologies (e.g. organics)
- Integrate online market exchange platform to increase transparency

Website: www.aci-bd.com/agrobusiness.php

Note on figures used:

Currency: Financial figures that were provided in Bangladeshi Taka are expressed in USD, based on an exchange rate of Tk79/$1.

Base of Pyramid: Numbers of people reached at the base of the pyramid represent those directly engaged as suppliers, entrepreneurs or consumers, and are not multiplied by household size to represent 'lives touched'.

1 The inclusive business in brief

> **ACI Agribusiness, part of a leading corporate in Bangladesh, is piloting an integrated contract farming model that aims to improve the yields and profits of low-income farmers.**

> **The company relies on its partner intermediaries to provide inputs and training to the farmers, and to aggregate and sell their harvest for fair market prices.**

1.1 What is the inclusive business?

Advanced Chemical Industries (ACI) Limited, a large Dhaka-based corporate, was formed in 1992 with the mission to enrich "the quality of life [in Bangladesh] through responsible application of knowledge, skills and technology." Over the past two decades, ACI has established itself as one of the largest conglomerates in Bangladesh, and in 2012, the company achieved net turnover of approximately $282 million and gross profit of $73 million.

ACI is organised into four distinct business divisions, with Agribusiness comprising six sub-units (Figure 3). While most of the agribusiness units focus on selling inputs for agriculture, the Cropex unit (ACI shorthand for "Crop Exchange") serves a market-linkage function: buying crops from farmers and selling to wholesalers and retailers, including ACI's retail subsidiary, Shwapno.

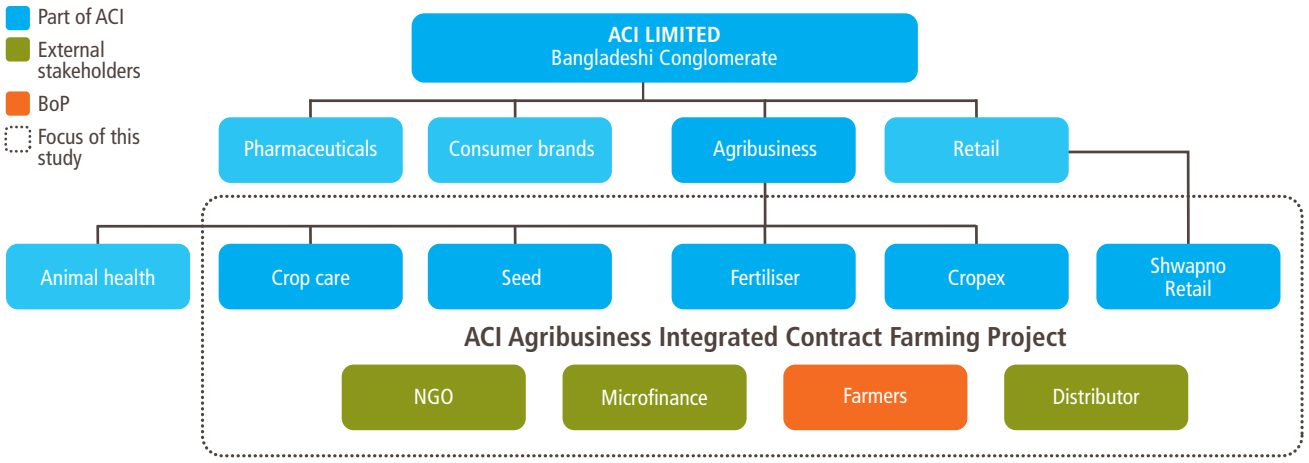
The inclusive business that is the focus of this case study is an integrated contract farming model, one of multiple contract farming initiatives within ACI Agribusiness. It was piloted in Rajbari, a district in central Bangladesh located approximately 100 kilometers west of Dhaka. Although ACI has had previous contract farming arrangements, this one is distinctive both in its approach to straddle the agribusiness divisions, as well as in its fair pricing approach with farmers.

Table 1: *Overview of the ACI Agribusiness Integrated Contract Farming Project*

ACI Agribusiness Integrated Contract Farming key facts	
Name	ACI Agribusiness Integrated Contract Farming Project
Sector	Agriculture and Food
Country	Bangladesh
Product/ Service	Contract farming project with smallholder farmers in Bangladesh that provides guaranteed purchases, quality inputs, and training
Relationship with lead company	The project is one small initiative of ACI Limited, one of the largest conglomerates in Bangladesh

During the pilot, ACI Agribusiness worked with an international NGO, to identify a group of marginal or land-less farmers willing to participate in the pilot project. A microfinance organisation provided capital for the farmers to rent land and equipment and purchase seed from ACI and hormones and other inputs from ACI Fertiliser. ACI provided the seeds for new summer varieties of tomato, and ACI Seed and the NGO provided training and oversight to the farmers throughout the growing cycle. Post harvest, a local agent would then aggregate the farmers' yields and ensure product quality, and then sell the crops to ACI Cropex. ACI Cropex would either sell the crops to a wholesaler or retail outlet, such as Shwapno.

Figure 3: *Focus of this report: ACI Agribusiness Integrated Contract Farming Project*



1.2 How is the business commercial, inclusive and innovative?

How is the business commercial?

The contract farming pilot is part of ACI's larger strategy of expanding markets and increasing sales. During the initial planning phase of the project, it was estimated that within three years the project would generate approximately $500,000 in revenue per year, growing to $1.25 million in revenue within five years with the expansion into new varieties and geographies. Other commercial benefits expected include improved collaboration across Agribusiness Strategic Business Units (SBUs), increased brand recognition for ACI inputs and a greater ability to meet the supply chain requirements of its retail outlets.

How is the business inclusive?

The contract farming project aims to improve the yields and profits of low-income farmers. Benefits delivered by the model include a guaranteed purchase of the harvest at fair market prices (Box 1), reduced overall costs through transportation efficiencies, and financing for land, farming equipment and agri inputs. ACI and its partners also provide training and technical support to the farmers throughout the entire process – from pre-planting to harvest. Within three years, ACI hopes to reach 5,000 farmers through the initiative.

A fair price for produce

Many contract farming agreements establish a fixed price at which the crops will be purchased from the farmers. Under the terms of the pilot project, Cropex agreed to purchase the crops from the farmers at the prevailing market rate on the day of the purchase. This was felt to be the lowest risk option for both farmers and ACI, as the price for summer tomatoes is always high due to their scarcity during the pilot's harvest season.

Box 1

How is the business innovative?

Contract farming is common in many parts of the world, but it is still unusual in Bangladesh. ACI's innovative approach involves both providing inputs and buying outputs from farmers. It also relies on a variety of partners whose complementary strengths allow the company to provide an end-to-end solution to smallholders. The initiative also provides an innovative product offering, giving farmers the opportunity to grow new higher-value crop varieties and access other quality inputs that would otherwise be inaccessible to them.

The shade structure covering the tomato plants

2 The story behind the ACI Agribusiness Integrated Contract Farming Project

> **ACI developed the contract farming model to improve collaboration within its Agribusiness divisions, expand its sales, and increase its brand recognition.**

> **Although the initial pilot did not succeed due to weather difficulties, lessons learned are being integrated into the company's next attempts.**

2.1 Commercial drivers

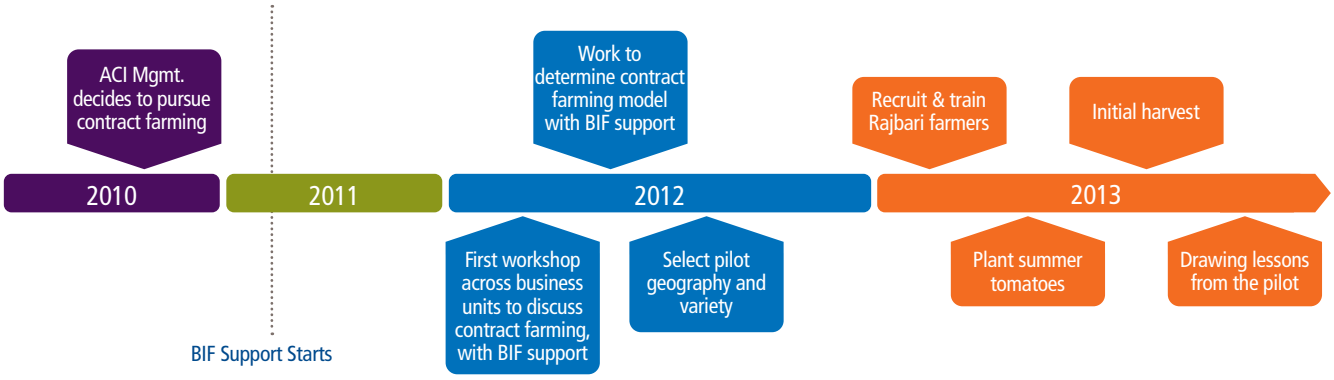
ACI's management team determined that the ACI Agribusiness Integrated Contract Farming Project would deliver the following four commercial benefits to the business:

- **Financial:** More than 95 per cent of the revenue of $500,000, estimated for Year 3, is expected to come from the resale of crop yields to wholesale and retail outlets. The remaining portion of the sales would be generated from inputs sold to the farmers – from ACI Seed, Fertiliser and Crop Care – and training and ongoing support from ACI Agribusiness. The pre-tax profit margin of the project was expected to be 15 per cent.
- **Increased brand recognition:** Through implementation of a successful contract farming model, ACI Agribusiness hopes that farmers recognise ACI to be of the highest quality, encouraging them to seek out ACI for future farming input requirements.
- **Secure supply chain for Shwapno retail outlets:** The contract farming initiative is a means for Shwapno to improve supply chain stability. It is Shwapno's hope that ACI Agribusiness will be able to monitor both the quantity and the quality of the crops throughout the growing season to ensure that end product meets Shwapno's high-quality standards.
- **Improved collaboration within ACI:** ACI management are continuously seeking out ways to increase collaboration between the ACI Agribusiness Strategic Business Units – Seed, Fertiliser, Crop Care, Motors, Animal Health and Cropex. A contract farming model that involves multiple subgroups in a commercially sustainable relationship can help to foster collaboration and increase linkages across ACI Agribusiness, leading to increased efficiencies within the company.

2.2 Timeline

Late in 2010, ACI management decided to pursue a new contract farming model. During strategic planning sessions, the ACI management team believed it was in the best interest for the future of Agribusiness to improve collaboration efforts between the various sub-segments. It was determined that contract farming was the most suitable means for achieving this goal.

Figure 4: Timeline of ACI Agribusiness Integrated Contract Farming Project



Although there was internal support for the contract farming project, ACI did not have the internal expertise to develop the appropriate operating model. Additionally, such a small project did not have the financial resources to hire outside consultants. It was for these reasons that ACI applied for BIF support (Box 3).

BIF support in brief

In early 2010, BIF began to support ACI's development of its integrated contract farmer model. It facilitated a workshop with ACI agribusiness units that revealed the extent to which the organisation's SBUs were 'siloed' – and better collaboration could be established. This started the process of sharing information and building a vision of a coordinated engagement with farmers.

Following the initial workshop, the project was approved for more substantive support, during which support was provided to determine the appropriate contract farming operating model. The engagement also included the development of more advanced financial projections and methodologies for collecting key performance indicators (KPIs) for financial, operational, and developmental metrics.

Box 3

Support from BIF helped ACI to determine the most appropriate model. ACI decided to pilot an "intermediary" model – a contract farming model where an NGO acts as an intermediary between ACI and the farmers. An NGO partner was chosen through a competitive bidding process, and Cropex was given primary responsibility for leading the initiative.

Rajbari was selected for the pilot location because of an existing relationship between the NGO and the district's farmers. Determining the most suitable crop for the pilot was more challenging. Several varieties were proposed, including winter tomatoes, cauliflower, cucumbers, and mangoes. Summer tomatoes were eventually chosen, because Shwapno had a desire to sell domestically grown summer tomatoes in its stores.

The NGO recruited more than 100 farmers and, working in conjunction with the MFI and ACI Seed, Fertiliser and Crop Care, trained the farmers on proper cultivation techniques. The 'train the trainer' methodology was used, where additional training was given to the lead farmers, who in turned trained the farmers in the group.

Planting was initially delayed because of intense rain in June, and more than half of the farmers dropped out of the program primarily due to financial concerns. Ongoing weather difficulties delayed the harvest as well, and 90 per cent of the plants were affected by virus. In the end, only 200-280kg of tomatoes were harvested. It appears that the problem started at the initial stage when the late transplantation made the seedbed muddy, and farmers did not construct a plastic tunnel while raising their seedlings, as they were advised to do by ACI Seed.

ACI and its partners are now undertaking an exercise to learn from the pilot so that ACI can improve the business model in its next attempts. This was the first time the farmers in Rajbari attempted the delicate techniques required for cultivating summer tomatoes and hence need closer guidance. No farmers should suffer long-term losses as a result of the pilot, as ACI and the other partners in the pilot are planning to cover their operating costs and compensate them for having not had a summer crop on the land that they used for the summer tomatoes.

2.3 Management culture

After the management team's decision to pursue contract farming as a means for improving collaboration, the project was primarily overseen by Mr. M. Saifullah, the Head of Strategy for ACI Agribusiness. Mr. Saifullah and his team were the driving force behind "getting the contract farming project off the ground." They were responsible for applying for BIF support, and they worked nearly full-time with the BIF consultants to develop the appropriate operating model. Today, the various Agribusiness units carry out the majority of the Rajbari project's workload, but the strategy team continues to spend 10-30 per cent of their time on the initiative.

While ACI is doing inclusive business within each of its Agribusiness units since inception, the company is also proud of its two-decade long tradition of promoting corporate social responsibility (CSR) initiatives. In 2003, ACI was the first Bangladeshi company to adopt the United Nations' Principles of Global Compact, which "enforces basic human rights and accepted labor practices and environmental standards in all business activities." Today, there are only 15 other companies in Bangladesh who have formally adopted these principles[1]. In the Agribusiness sector, "ACI has undertaken extensive programs to educate farmers all over rural Bangladesh in Appropriate Agricultural Practices, regularly holding a range of technical trainings and field demonstrations."

[1] Global Compact Network Bangladesh, Accessed August 2013. http://ungcbangladesh.org/index.php?NoParameter&Theme=default&Script=resources

2.4 Market Context

Competition

As a conglomerate, there are several markets in which ACI competes. The markets relevant to the Cropex contract farming initiative include:

- **Farm inputs:** ACI is engaged in the sale of seed, fertilisers, crop protection products, and agricultural machineries primarily to distributors. According to the Bangladesh Seed Grower, Dealer & Merchants Association, "there are more than 100 companies involved [in seed production] and over 5000 registered seed dealers operating across the country." The competition for fertiliser manufacturing and distribution is equally as fragmented within the country.
- **Crop exchanges:** Served by ACI Cropex, this marketplace matches suppliers (farmers) with buyers – wholesalers, retailers, or directly to individuals. The primary competitors for Cropex are physical market places, which range in size and capacity from larger regional aggregation points to smaller village marketplaces.
- **Retail outlets:** Served by ACI's retail division, Shwapno, this market is defined by a number of different grocery store chains within Bangladesh. Shwapno considers Agora and Meena Bazaar to be its two biggest competitors. According to Shwapno, as Bangladeshi consumers become more sophisticated, they are also seeking out high-quality food products that are both safe and affordable. Shwapno is trying to capitalise on these customer requirements through its engagement with the contract farming project.

Contract farming in Bangladesh

Although contract farming exists within Bangladesh, it is generally limited in terms of size and scope. According to BIF, "contract farming is not completely new to Bangladesh, but it remains a selective rather than common practice[2]." Domestically, contract farming is primarily used for atypical crops and poultry. For example, in Mymensingh District, approximately 50 farmers grow oyster mushrooms, which are primarily supplied to restaurants and hotels. In this case, the trader purchases the produce from the farmers at a fixed price, which is negotiated prior to the harvest. In another example, Bombay Sweets, a Bangladeshi snack food manufacturer, has undertaken a small-scale contract farming project with farmers in Habiganj District to secure its supply of potatoes and peanuts.

Bangladesh faces the common challenges associated with contract farming but also has a unique set of obstacles that need to be addressed in order for contract farming to become a fully established practice. The primary challenges include:

- **Environmental conditions:** Bangladesh is subjected to unpredictable weather patterns (including flooding and cyclones), suffers from poor irrigation, and high-levels of chemicals are often found in the soil.
- **Poor infrastructure:** The power supply is insecure and there is limited access to cold storage for produce.
- **Limited government support:** There is currently no contract farming governing body, there are limited funds to support these initiatives, and crop insurance does not exist as it does in other locations around the world.

***Table 2:** Summary of influencing factors*

Internal factors	
Company strategy	Desire to facilitate collaboration within Agribusiness; increased brand awareness (both inputs and consumer products)
External factors	
Macro-economic conditions	Increasing need for end-to-end supply chain visibility
Evolving market opportunities	Increased consumer demand for safe, high-quality produce; blossoming demand for organic produce from high-end customers

[2] 'Project Resource: Sustainable contract farming initiative', *BIF*, 2013. http://api.ning.com/files/Yt9-0kiWPzlkCid5Je9cVG4tw3TNnu2de09LcWjQTdhp79qsuUzEka6*rd0WpxiEkxPfvvhdOzzU2rZj*kEkwwag506-GnLw/ProjectResource_Sustainablecontractfarminginitiative_nov12.pdf

3 How does the inclusive business model work?

> **ACI has chosen an 'intermediary' contract farming model, whereby NGOs and other organisations serve as intermediaries between the ACI and the farmers along the value chain.**

> **As the Rajbari pilot demonstrates, key risks remain for both ACI and its farmers. These challenges will be addressed in upcoming iterations of the model.**

3.1 Overview of the value chain and business model

The ACI operating model is noteworthy among the many other contract farming models in that ACI is both supplying the inputs and also purchasing the crop yield. The value chain includes both supply and consumption of agri inputs plus production and distribution of crops. Farmers are consumers of the inputs and producers of the crops. ACI is active at either end of the value chain, while external partners are responsible for direct engagement with farmers, both on distribution of inputs, and in supporting production and aggregation of inputs.

Another key element of ACI's contract farming model is the critical role that an NGO plays. After ACI and the NGO have determined the appropriate crop requirements and negotiated the buyback terms with the farmers, ACI supplies the farmers with appropriate inputs, including seeds, fertiliser and crop care products. The NGO then works with the farmers throughout the growing period by providing field training and technical assistance. Following the harvest, ACI Cropex will purchase the crops from the farmers and transport the produce to the wholesale or retail buyer.

A typical house for the farmers participating in the pilot

Meeting with the local agent

Figure 5: *Value chain of ACI Agribusiness Integrated Contract Farming Project*

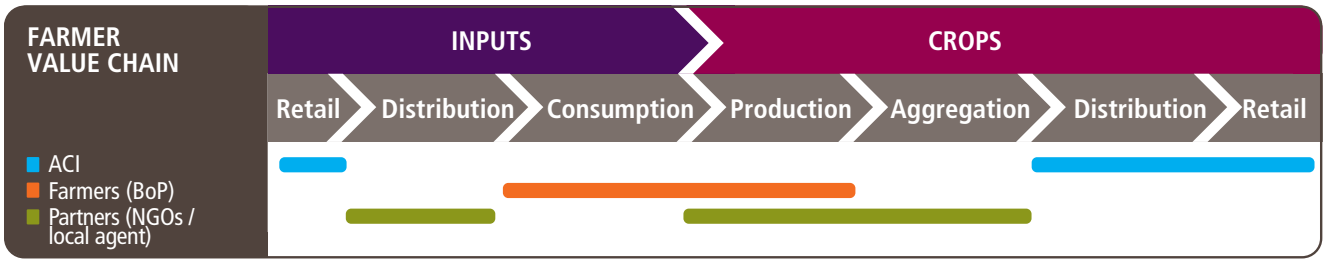
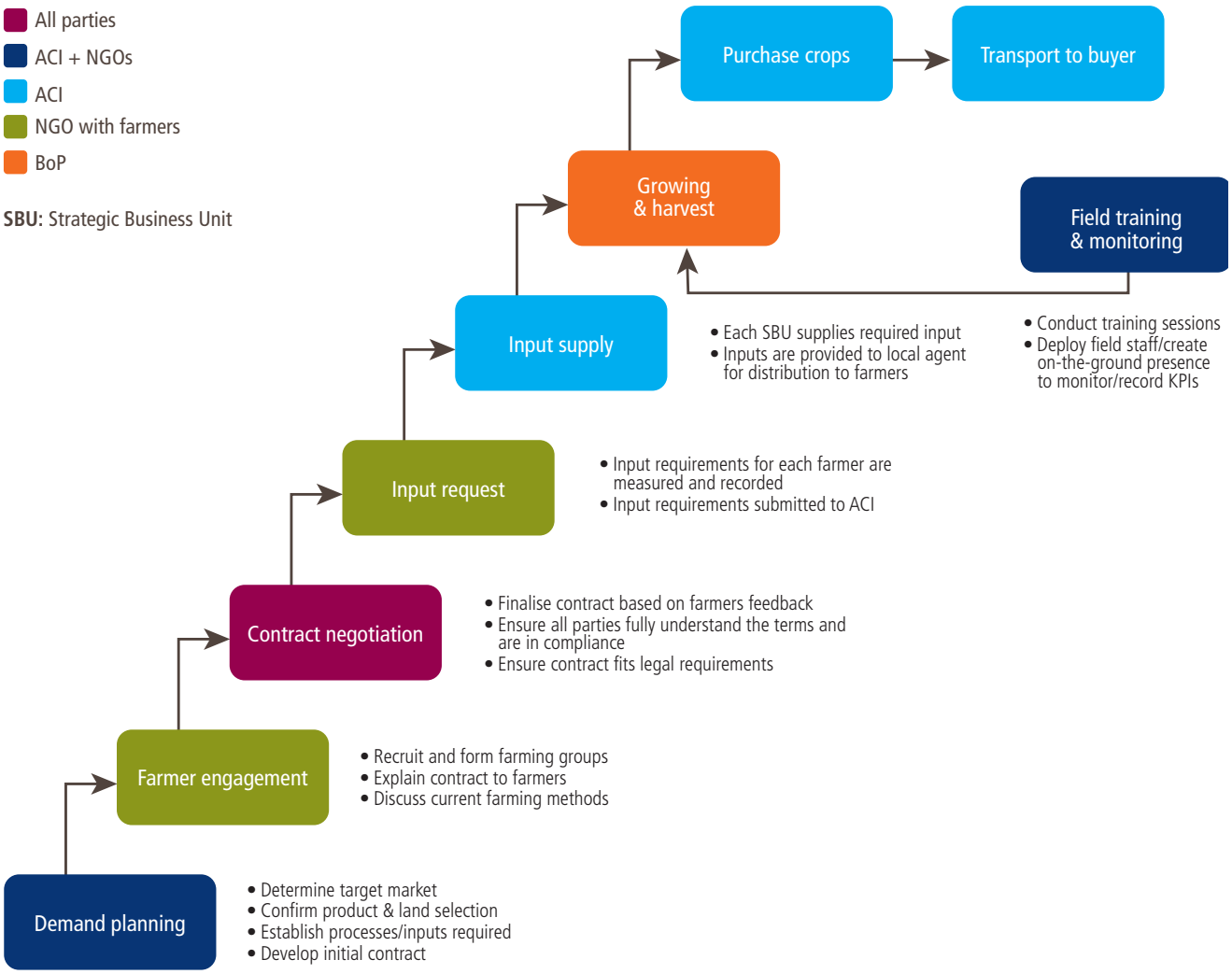


Figure 6: Agribusiness Integrated Contract Farming Project business model



3.2 Evolution of the model

With support from BIF, ACI looked carefully at a range of contract farming models. These models were derived from a study of contract farming models across a number of developing counties and contexts. ACI chose what they refer to as the 'intermediary' model (Box 4) because this appeared to be the best fit with ACI's capacity and experience.

What is an 'intermediary' model?

BIF characterised the 'intermediary' model as follows:

- Involves a sponsor or middleman who provides linkage between farmers and the company
- Contracts are generally established between the company, intermediary (NGO, farmer groups, collectors) and farmers
- Used most often for staple food crops such as potatoes, rice and mangos

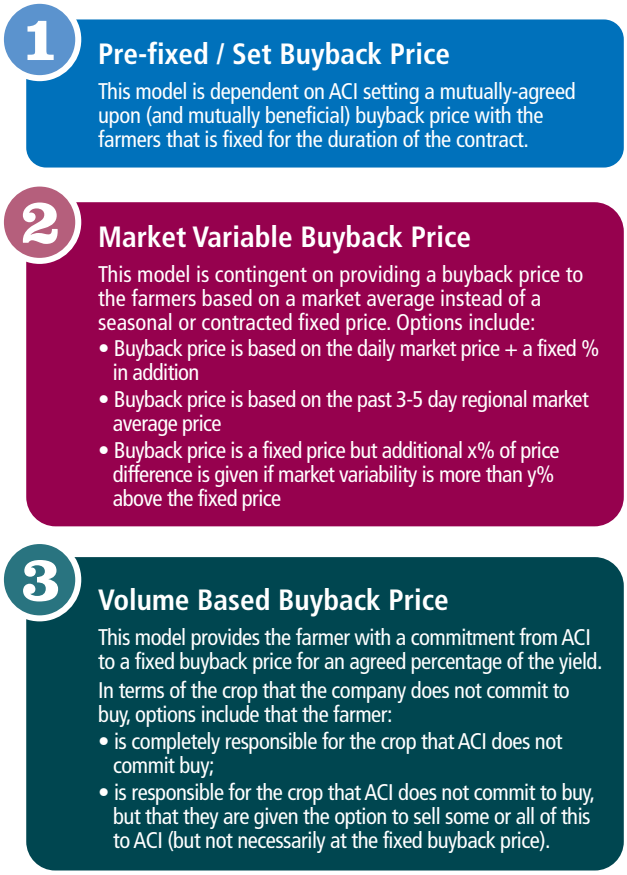
Box 4

They felt this model was most suitable for ACI because the company has the inputs required to grow fresh produce but does not have the resources or presence on the ground to organise local farmers. This excludes a contract farming business model where the company can have a high level of day-to-day contact with farmers, such as a nucleus estate or out-grower model. ACI was thought to require an intermediary that currently has established relationships with farmers to provide this level of contact and support.

With this model ACI can still control the level of inputs used and the production processes, which would not be possible in a less formal model. There also appeared to be potential for future scalability, by removing the intermediary once the model is established and transitioning to a centralised model.

A second area that the company had to decide on was the mechanism by which they buy back crops (Figure 7). The market variable buyback option was assessed as being the lowest risk for both farmers and ACI. Farmers would also perceive this to be 'fair' as it clearly links to the prevailing market price at the time the crop is produced.

Figure 7: Buyback options for ACI



The originally conceived business model was implemented to plan in Rajbari, but the problems that affected the pilot will no doubt lead to further evolution of the business model.

3.3 Challenges and risks

The intermediary model does have its risks for the company, as was indicative in what seems to have gone wrong in the pilot at Rajbari. These risks include:

- Danger of company losing control of its production base
- Technical policies and management inputs can become diluted and production distorted
- Harder to ensure quality control of product.

A common critique of contract farming is that it can also place small farmers, who are often not well placed to absorb shocks, at risk. In the pilot of the ACI model, the benefits of a guaranteed harvest purchase and reduced overall costs achieved by working with ACI were not realised by the farmers because of the very poor harvest.

More than half of the farmers took advantage of the low interest microloans and they were primarily earmarked for purchasing ACI's more expensive inputs. However, there was a misunderstanding between the farmers, the MFI and ACI, which has led to some displeasure with the terms of the agreement. It became apparent during the field visit that the farmers who took out the loans were under the impression that if the harvest did not succeed, their loan obligations would be lifted. However, this was not the case, and the farmers were in fact expected to repay their loans regardless of the outcome. This is particularly distressing for the farmers because crop yields fell far short of expectations. Once the extent of harvest failure was apparent, ACI and partners stepped in to remedy the situation.

Although many individuals within ACI think that there is little downside risk to the company engaging in this project, one comment from the Seed business manager indicates that there is some trepidation with the new business model. Even before the harvest failed in the pilot, managers were concerned that a poor harvest would be incorrectly attributed to ACI seeds and fertiliser. According to Dr. Md. Shafiqul Aktar, Business Manager for ACI Seed, "Farmers always blame the seeds, even if it was the weather or they did not follow the correct steps."

Now that the harvest has not been successful, there is a fear that the current farmer participants will cease to use ACI products in the future, and, even worse, spread a negative reputation about the products to other farming communities. ACI is working hard with its partners to address these concerns, but it is an example of the risks that companies encounter when seeking to engage low-income producers.

Table 3: Key risks associated with ACI Agribusiness Integrated Contract Farming Project

Key risks	Mitigating activity
Farmer may end up in debt if they can't repay the credit used for seed and other farm inputs	• Improve the supervision of farmers so that they are able to achieve the expected yields and financial returns
Negative reputation of ACI inputs due to poor harvest	• Actively oversee the farmers during the cultivation period to ensure proper procedures are followed • Obtain feedback from farmers following the harvest to discuss what went well and what could be improved in the next round of the contract farming
Shwapno misses summer tomato sales targets	• Procurement of near similar varieties from open market instantly

4 Commercial results

> **ACI projects a pre-tax profit margin of 15 per cent, and a three-year Return on Investment of 14 per cent.**

> **Although the pilot failed to reach its goals, management is still committed to developing a viable contract farming model.**

Commercial viability

In May 2012, during the initial planning phase of the project, it was estimated that within three years the project would generate approximately $500,000 in revenue per year, growing to $1.25 million in revenue within five years with the expansion into new varieties and geographies. The pre-tax profit margin of the project was expected to be 15 per cent.

The internal investment requirements for the first three years of the project were expected to be less than $20,000 annually, thereby generating a Return on Investment (ROI) equal to 14 per cent, the minimum acceptable return for ACI to move forward with any new project – whether or not it is considered "inclusive."

Actual results

As a result of the technical difficulties experienced, the pilot did not demonstrate the commercial viability of the contract farming model for ACI.

Mr. M. Saifullah, the Head of Strategy for ACI Agribusiness, has suggested that financial performance is only a secondary concern for the project. The primary objective is to understand the appropriate contract farming operating model, and he believes that the pilot is helping ACI Agribusiness move closer in that direction. ACI is wholly committed to building a sustainable contract farming model.

Table 4 sets out the current position with regard to the commercial results that ACI is still targeting.

Table 4: *Summary of commercial results*

Commercial returns	Financial	Strategic
Company objective	• Revenue of $500,000 within three years • 14% ROI (minimum requirement for any ACI project)	• Improve collaboration across Agribusiness SBUs • Increase brand recognition for ACI inputs • Meet Shwapno supply chain requirements
Progress to date	• Initial harvest and financial results from pilot negative	• Better collaboration between Agribusiness SBUs • Valuable lessons learned in terms of developing the operating model
Trajectory going forward	• Can still hit financial targets when the operating model is improved	• Develop next iteration of the contract farming operating model • Expand into new geographies / farming communities with new varieties • Integrate online market exchange platform
Key challenges	• Fast enough sales growth	• Clearly defined project leadership • Improved liness of communication • Monitoring and troubleshooting

5 Development impacts

> **ACI aims to reach 5,000 base of the pyramid farmers and their families within three years.**

> **Farmers benefit from better inputs, improved techniques, and increased access to markets, potentially resulting in significantly higher yields and revenue.**

5.1 Direct impacts at the base of the pyramid

Table 5: Summary BoP impacts

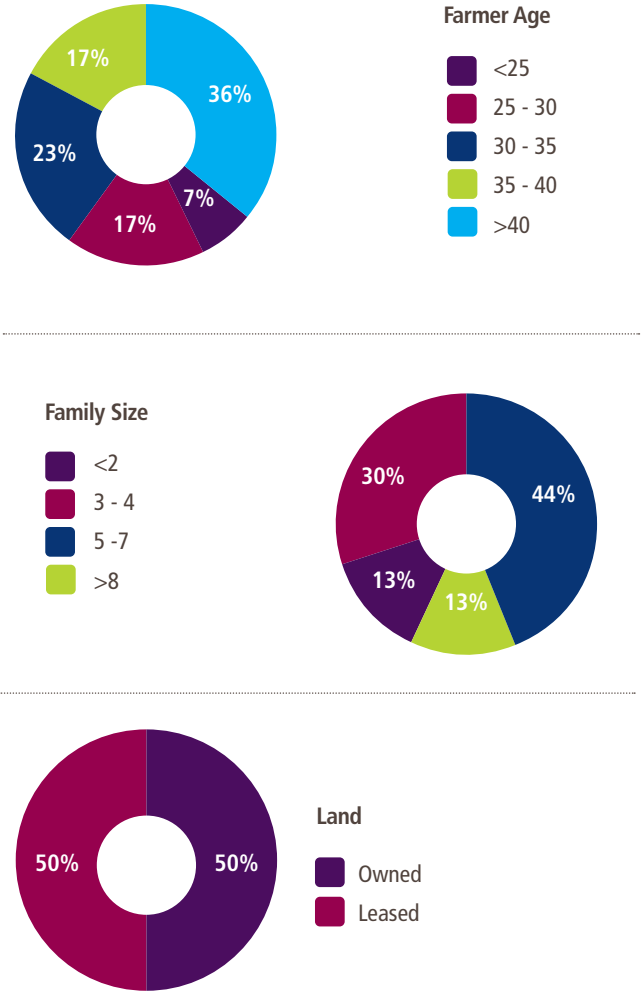
BoP impacts	To date
Number of farmers engaged to Q3 2013	Approximately 50 farmers in the pilot
Trajectory for number of farmers impacted	5,000 farmers within three years
% who are/ will be women	No women were included in the pilot; future involvement depends on farmer / crop selection
Characteristics of farmers	• Rural farmers with wide-range of poverty likelihoods • Three-quarters have >5 family members • Up to 63% fall below the PPI's poverty income threshold for Bangladesh
How they can benefit	• Higher profitability from summer tomatoes • Financing makes purchase of inputs less risky • Improved farmer education • Homestead gardening – the family can get involved
Losses suffered in first pilot	• ACI and other partners have agreed that the farmers will be compensated such that they suffer no long term losses from the pilot

Who is benefitting?

The base of the pyramid (BoP) in the context of the ACI Agribusiness contract farming project is currently limited to the 50 farmers participating in the pilot and their families. All of the pilot farmers were male. These individuals live in Rajbari District, which is located approximately 100 km west of Dhaka, and the local economy is almost entirely centered on agriculture and raising livestock. In July 2013, a month before harvest, the authors conducted a focus group session in Rajbari to better understand the characteristics of the farmers. The 30 farmers who attended revealed the following:

- The farmers (both present and absent) are members of four larger farmer groups, each consisting of approximately 25 farmers
- In the past, these farmers have grown tomatoes (winter varieties only), jute, rice, onions, legumes, cauliflower, and other vegetables – but no summer tomatoes
- More than half of the farmers are aged 35 years or older and 57 per cent of their families have five or more family members
- 50 per cent of the farmers do not have their own land and rely on leased land
- Farmers rely primarily on rainfall for farming water requirements.

Figure 8: Demographics of Rajbari farmer focus group session (July 2013)



Additionally, 10 farmers were asked to complete a survey to measure their Progress Out of Poverty Index (PPI) Score (Annex 2), which indicated varying degrees of the likelihood for poverty within the community. The basic amenities that these farmers owned were also varied: some owned televisions, while others did not; some homes were comprised of a single room, while others had three or more; but almost everyone owned a mobile phone. Seven of the 10 were more than 50 per cent likely to fall below the $2.50 per person per day international poverty line, while only two of the ten fell below the $1.25 line.

ACI employed the NGO and the MFI to recruit farmers to participate in the pilot. The Rajbari farmers were an acceptable choice because they were generally considered smallholder farmers, and they were eager to participate when they learned of the potential for high profits from summer tomatoes.

How do people benefit?

Low-income farmers were expected to benefit from the pilot in a number of ways:

- **Guaranteed purchase of the harvest:** Through the contract farming buyback scheme, ACI Cropex guarantees that they will purchase crops from the farmers at the fair market price, reducing the farmers' costs and risks associated with finding a buyer.
- **Reducing overall costs:** Although some costs increased for the farmers in the pilot – such as the cost of high-quality ACI inputs and the shade structure required for summer tomatoes – overall costs were expected to decrease primarily due to the elimination of the high-cost of transportation.
- **Financing for land, farming equipment and inputs:** The MFI provided low-interest loans for farmers to rent land and equipment and purchase ACI inputs. ACI provided further credit to farmers who did not qualify for the loans.
- **Improved farmer education:** ACI, in partnership with the NGO and MFI, provided training and technical support to the farmers throughout the entire process – from pre-planting to harvest.

At the time of the field visit farmers described being thrilled by the profitability prospects that summer tomatoes offer. Had the harvest been as expected (and as ACI have achieved in similar areas of Bangladesh in controlled conditions) they could have earned up to ten times more revenue per decimal of land, as compared to winter tomato varieties .

***Table 6:** How do BoP farmers gain?*

Dimension of Significance	Relevance	How it applies
Income	√√√ (potentially)	The Rajbari farmers were eager to participate in the summer tomato harvest because of the crop's higher market value – they could obtain 10x more revenue from the same amount of land.
Security	Marketing √√√ Production √	ACI has guaranteed that they will purchase the crops post-harvest at the fair market price. However, the farmers are still vulnerable to crop loss and the associated risks – e.g. inability to payback higher input costs.
Choices	√√	By participating in the program farmers add a new summer crop to their agricultural portfolio and get access to more advanced farming equipment, techniques, and training which gives them more options for the future.

The actual harvest for the pilot tomato crop was very poor (Section 2.2). More than half of the farmers took advantage of the low interest microloans and as described in the 'challenges and risks' section above, without intervention from the pilot partners would be at risk of long-term indebtedness.

The post-harvest survey team visited 38 farmers, noting that "Most of their crops were destroyed so now most of them are working as day laborers. The MFI and local agent are still asking for their money which the farmers are not able to pay right now. As the season isn't over yet, the farmers can't do anything with their land until next season. So they are really passing through a tough time now."

The survey revealed that the farmers spent on average $140 (Tk 11,000)[3] on seed, fertiliser and other chemicals, and construction materials to protect the plants. Ten of the farmers had also spent money leasing land, and all but five had paid labour to do some of the work. Around one fifth of this was with money borrowed from the MFI, and farmers also owed money to ACI (via the local agent) for the fertiliser and seed. The survey data is forming the basis of the ongoing efforts by partners to cover the losses incurred by the farmers in the pilot.

[3] Note on exchange rate: Financial figures that were provided in Bangladeshi Taka are expressed in USD, based on an exchange rate of Tk79/$1.

In spite of these setbacks, ACI is eager to scale up the contract farming project once the company feels that the operating model has been appropriately adjusted to address the shortcomings discovered during the pilot. ACI is also looking to expand into additional crops, such as cucumbers, mangoes and cauliflower. Within three years, ACI hopes to further expand its reach to 5,000 farmers.

5.2 Environmental impacts

An essential aspect of the technical training that both ACI and the NGO provide is sustainable agricultural practices and the application of optimised agricultural inputs. Application of well-balanced inputs helps to maintain the organic content of the soil and enhances soil health in the long run. During the focus group session in July 2013, the farmers resoundingly indicated that they are using less fertiliser than before, although the cost per kg is higher (which is indicative of having used lower quality fertilisers in the past).

Additionally, sustainable agricultural practices can significantly reduce the amount of fertilisers which wash away into the rivers, eventually emitting greenhouse gases such as carbon dioxide and nitrogen dioxide into the atmosphere. Although the environmental impacts have not empirically been measured at this point, it is likely that these improved farming practices have contributed to the lowering of both air and water pollution.

5.3 Potential for systematic impacts

The Bangladeshi government is keen to promote more contract farming initiatives within the country. ACI is looking to share its contract farming lessons learned with the government once the operating model has been refined and successfully implemented. With supportive government policies and an inclusive business blueprint for success, other companies may enter the market and help scale the benefits.

A pest on one of the tomato plants

6 Future outlook and lessons learned

6.1 Future outlook and potential for scale

According to ACI Agribusiness, there is a "100 per cent chance" that the company will continue scaling up the contract farming line of business. It is continuing its relationship with the pilot farmers for the next growing season, and building off the lessons learned from the last. Other near-term opportunities for the model's growth include:

- **Expanding into new varieties and implementing changes to farming methodology:** ACI intends to expand into new varieties as a next step in scaling up the contract farming project. Shwapno is also beginning to see more demand for organic produce from its customers, and there are discussions about how the contract farming initiative can fulfill those supply requirements.
- **Integrating online market exchange platform into contract farming:** Within the next six months, Cropex is planning to roll out a new online market exchange platform, and the business unit anticipates an opportunity to integrate this platform with the contract farming project. From the demand side, farmers will be able to understand the crops that are most required by retail and wholesale outlets; from the supply side, those outlets will have more accurate information about the availability of produce. The platform will speed the transfer of payments to BoP farmers, and also provide banking autonomy to women, who often face more challenges (and costs) marketing their produce due to cultural constraints.

ACI is a long-established company within Bangladesh, and it has an extensive network of partners throughout the agribusiness value chain. The large size and reach of the company should further help the contract farming model to develop and scale.

6.2 Additionality of BIF support

In 2010, ACI Agribusiness managers determined that contract farming would serve the dual goals of uniting their "siloed" business units and stabilising Shwapno's supply chain requirements. However, it marked a departure from normal business for ACI. ACI did not have the internal expertise to operationalise such a strategy, and management was unwilling to commit scarce financial resources to undertake the necessary study to determine the appropriate contract farming operating model. It was at this point that Mr. M. Saifullah, the Head of Strategy for ACI Agribusiness, decided to apply to the BIF program. BIF's additionality was absolutely necessary for the contract farming project to get underway; it transformed the project from a board room idea to implementation of the recommended contract farming operating model, and to a potential new way of doing business at ACI Agribusiness.

> **"Without BIF's support, this project would not have started."**
>
> **Mr. M. Saifullah,** Head of Strategy for ACI Agribusiness

6.3 Strengths and weaknesses of the model

The intermediary model that ACI has adopted for the contract farming pilot has proven to be both useful and challenging during the contract farming pilot. The operating model was preferred because ACI did not have the ground support staff to work with the small farmers on a daily basis. Additionally, small-scale farmers are not particularly comfortable working directly with a large corporation such as ACI. Given these circumstances, the intermediary model was a logical way forward.

However, the expertise of management added by the NGOs failed to adequately support ACI to monitor progress and troubleshoot when necessary. ACI Cropex and the Agribusiness Strategy team were not notified that more than half of the farmers had dropped out of the program. Had ACI been informed of this, they could have taken more proactive steps to ensure that the farmers felt that their needs were met. The farmers were also not properly monitored about the crop care application of the new tomato crop. If there was a clear flow of communication, the outcomes may have been different.

An additional challenge that management has identified is that the Cropex division does not have the manpower and skill sets to manage the entire project. Although Cropex was intended to be the primary ACI point of contact, other ACI divisions ended up working directly with the NGOs and the farmers. This led to a further breakdown of communication and potentially hindered the success of the project. Mr. M. Saifullah believes that the Agribusiness division should create a team solely dedicated to the contract farming initiative. This team will be in a better position to coordinate activities with Agribusiness's other business units. It is likely that this change will be implemented for the next round of contract farming.

ACI management suggests that the ACI Agribusiness Integrated Contract Farming Project is on an upward trajectory and the initiative will continue into the future. It is highly likely that ACI will expand into new varieties and work with new sets of farmers from different locations within Bangladesh. It is also likely that ACI will make adjustments to the operating model to ensure that the process runs more smoothly going forward. Once the model is adjusted and the project ramps up, management has great expectations that contract farming will turn into a strong performer within ACI Agribusiness.

6.4 Lessons learned

Contract farming is a model more commonly used and frequently discussed in other developing countries. The ACI pilot is likely to be different in at least three ways: (1) it is led by a large corporation, with the divisional structure that entails; (2) the drivers for developing contracts relate to expanded markets for agri inputs, and not only to securing procurement volumes; and (3) it took place in Bangladesh where there is relatively little experience with contract farming. Nevertheless, and bearing the differences in mind, some key lessons emerge from the experience so far, which are useful both for ACI and others developing similar approaches:

- **Use the pilot to test a model not deliver results:** The fact that the crop failed may actually make the pilot more useful for informing future design. When testing a model, risks to low-income stakeholders need to be cushioned.
- **Secure strong central leadership and management buy-in:** When a large organisation undertakes a project that spans multiple business units, strong central leadership is needed to align differing opinions and get everyone on board.
- **Building collaboration across business units takes time and leadership:** The degree of collaboration across ACI business units has progressed considerably since the first workshop two years ago, but has required considerable time and effort from the strategy team.
- **Clearly identify partner roles:** Corporates often need to engage with non-traditional partners, such as NGOs, when piloting a new inclusive business model. Given the differences in expertise, partner roles must be clearly planned with shared expectations and appropriate follow through on both sides.

A farmer and his summer tomato plants

- **Pilot with proven technologies:** The pilot has faced several challenges, from extreme weather conditions to miscommunication between the field and project managers. Choosing to use a new variety of tomato created additional risk that was avoidable.
- **Provide adequate training:** A single day-long classroom-style training session may not be sufficient, particularly for less experienced farmers who may be hesitant to adopt new approaches. Regular and practical training sessions are preferable.
- **Ensure farmers understand the terms:** Irrespective of what is written down, build in a feedback loop to identify what farmers think has been agreed, particularly around their own obligations such as paying loans or selling crops.
- **Monitor closely:** Sufficient monitoring coupled with clear lines of communication are needed to find and troubleshoot small problems before they become big ones.

Annex 1: Case study methodology

Overview

The case studies were conducted using both primary and secondary data.

Primary data was collected during a two-week visit to Bangladesh in July 2013. Primary research consisted of individual meetings with relevant stakeholders – ACI, the NGO, the MFI and Renaissance Consulting. Additionally, a one-day field trip to Rajbari was made that included two focus-group sessions with a group of the pilot farmers and representatives from the local agent. A team member from Accenture Development Partnerships (ADP), who provided support under BIF, was also interviewed on their role in the project.

The following table outlines the various meetings / sessions and the high-level topics covered:

Representative	Topics Covered
ADP – J. Hauser	ADP deliverables
BIF/RCL – P. Huda, J. Debnath	BIF support of project
ACI Strategy – M. Saifullah, A. Raihan	Project background, Rajbari field trip
ACI Cropex – M. Mustafizur	Cropex perspective
ACI Seed – S. Aktar	Seed perspective
ACI Schwapno – A. Kalam	Shwapno perspective
Rajbari farmers (30)	Focus group session lasting 2 hours
Local agent (10)	Focus group session lasting 1 hour
MFI (1)	MFI perspective
NGO (2)	NGO perspective
BIF – C. Ashley	BIF support of project
IDS – E. Wach	Monitoring and evaluation methodology

Secondary data included BIF baseline reports, application forms to BIF, contract farming deliverables, BIF / RCL workshop documents and desk research about poverty levels in Bangladesh. This desk research was conducted during July and August 2013.

Strengths of this case study

- **Transparency:** All stakeholders, particularly ACI, provided unfiltered access to project documentation, and every interviewee was forthcoming and candid during information sessions.

Limitations of this case study

- **Status of the harvest and financial outcome was still unknown in mid 2013 at the time of the field research:** This is by far the biggest limitation, particularly for understanding whether or not the pilot proved that contract farming is commercially viable for ACI. The draft case study has been updated in recent months with new information from ACI and BIF, but no further fieldwork was possible.
- **Missing key performance indicators:** BIF provided rough guidelines for methodologies for capturing key performance indicators (KPIs) related to financial, operational, and developmental metrics. These items were not tracked, and it is unclear if anyone within the ACI organisation was ever tasked with this assignment.
- **Confusion over the repayment of the farmers' loan obligations:** During the focus group session, both the representative from ACI and the author could not identify the source of the confusion about the terms of the loan repayment.

Annex 2: PPI scores and corresponding poverty likelihood for 10 Rajbari farmers

	Farmer	Jafor	Torromalla	Rokit	Najrul	Nadar	Baschu	Gohorul	Liakot	Roslom	Salam
	PPI Score	**24**	**37**	**44**	**56**	**66**	**73**	**79**	**80**	**87**	**87**
Poverty likelihood according to…	National Lower	37.1%	15.0%	12.7%	1.5%	0.4%	0.2%	0.0%	0.0%	0.0%	0.0%
	National Upper 100%	62.7%	36.0%	26.7%	7.1%	4.4%	2.3%	1.2%	0.5%	0.0%	0.0%
	National Upper 150%	96.1%	80.8%	76.1%	42.6%	28.6%	24.6%	21.4%	17.0%	8.3%	8.3%
	National Upper 200%	99.5%	93.6%	91.9%	75.6%	52.5%	51.0%	40.3%	32.0%	24.9%	24.9%
	USAID Extreme	32.7%	13.8%	11.1%	1.8%	10.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	$1.25 2005 PPP*	78.0%	50.3%	40.8%	14.5%	8.7%	5.6%	4.3%	2.7%	0.0%	0.0%
	$1.75 2005 PPP	96.3%	83.6%	79.6%	50.4%	32.2%	31.5%	25.8%	19.7%	10.7%	10.7%
	$2.00 2005 PPP	98.4%	90.7%	87.4%	65.2%	44.5%	42.9%	34.0%	26.7%	14.6%	14.6%
	$2.50 2005 PPP*	99.7%	96.9%	94.9%	84.3%	63.3%	60.4%	50.7%	40.9%	33.3%	33.3%

**The PPI scores show that two of the farmers were likely (above 50% likelihood) to fall below the $1.25 PPP poverty line, and 7 of the 10 were likely (more than 50%) to fall below the $2.50 PPP line.*

Partner profiles

Business Innovation Facility

The Business Innovation Facility supports companies as they develop and implement inclusive businesses. Inclusive business is profitable, core business activity that also expands opportunities for people at the base of the economic pyramid: either as producers, suppliers, employees, distributors, or as consumers of affordable goods and services.

The Business Innovation Facility is a pilot project funded by the UK Department for International Development (DFID). It is managed for DFID by PricewaterhouseCoopers LLP in alliance with the International Business Leaders Forum and Accenture Development Partnerships. It works in collaboration with Imani Development, Intellecap, Renaissance Consultants Ltd, The Convention on Business Integrity and Challenges Consulting.

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For further information and to join the discussion on inclusive business, go to:
Practitioner Hub on Inclusive Business: www.businessinnovationfacility.org

Business Innovation Facility

Institute for Development Studies (IDS)

The Institute of Development Studies (IDS) is a leading global charity for research, teaching and information on international development. Our vision is a world in which poverty does not exist, social justice prevails and economic growth is focused on improving human wellbeing. We believe that research knowledge can drive the change that must happen in order for this vision to be realised. IDS hosts six dynamic research teams, several popular postgraduate courses, and a family of world-class knowledge services. These three spheres are integrated in a unique combination – as a development knowledge hub, IDS is connected into and is a convenor of networks throughout the world.

The Impact and Learning Team (ILT) conducts action research to generate new insights into the ways that evidence is used in decision making in policy and practice, including the generation of multiple types of evidence and knowledge (from evaluation, monitoring, and research), and the behaviours and capabilities of decision makers in using evidence to contribute to organisational, programme and policy changes. The ILT is situated under the Knowledge Services department of IDS, and works collaboratively with the six research teams in the institute as well as external partners.

For more information about the Impact and Learning Team, please visit:
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IDS Institute of Development Studies

Oxford University, Saïd Business School

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For further information please visit: http://www.sbs.ox.ac.uk/

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About this series of case studies

The definition of inclusive business is fairly well known by now – profitable, core business activity that also expands opportunities for people at the base of the economical pyramid (BoP). But what does it look like in practice? That is a harder question to answer. Experience is diverse, much of it early stage, and published reports often err on the side of 'cuddly', not forensic.

This report is one of a series of 'deep dive' case studies that seeks to understand inclusive business in practice. The series explores contrasting inclusive businesses, all of which have been supported by the Business Innovation Facility (BIF). Support from BIF is not cash, but technical input to help overcome challenges, seize momentum, and build a business model that will take the inclusive business to scale and sustainability. The partnership with BIF is, thus, very focused on the practicalities of business models and identifying key milestones in an inclusive business journey.

Over the past three and a half years, BIF has worked with almost 100 companies in five countries. BIF-supported businesses offer rich lessons about the evolution and impact of inclusive business, ranging from working with smallholder mango farmers in Malawi to rural energy solutions in India. Some of this is captured in the monitoring and evaluation (M&E) system. However, the system was designed to be applicable to all projects, not necessarily to capture the richness of the most interesting.

In order to add a deeper understanding of BIF supported inclusive business, BIF, in partnership with the Institute of Development Studies (IDS) of Sussex University and Saïd Business School (SBS) of Oxford University, has generated a set of case studies of inclusive business.

Following a joint framework developed by BIF and IDS, these reports explore what counts as success and what factors have created it. They assess the internal and external context of a company's business model, the 'nuts and bolts' of how the model works, actual or likely commercial returns, emerging impacts on bottom of the pyramid beneficiaries, value added from BIF support, key success factors for scale and lessons relevant for other companies.

We hope that the reports will provide inclusive business practitioners with knowledge and insights on how companies are progressing on their inclusive business journeys – each one distinctive, yet each discovering challenges and solutions that resonate with others.

Caroline Ashley and **Carolin Schramm**, BIF, **Elise Wach**, IDS and **Pamela Hartigan**, SBS

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> ACI Agribusiness: Designing and testing an integrated contract farming model in Bangladesh
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The series was coordinated by Carolin Schramm, and edited by Caroline Ashley. The methodology was developed and shared with authors in collaboration with Noshua Watson and Elise Wach of the Institute of Development Studies. Editing was done by members of the BIF team and by John Paul, independent inclusive business consultant. The series Production Manager was Clare Convey, and design was done by Caroline Holmqvist.

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