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FEASIBILITY STUDY



Barriers, constraints and
recommendations for catalyzing
for-benefit procurement within
the cocoa value chain in Ghana.





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A Closer Look at Ghana's Cocoa Sector



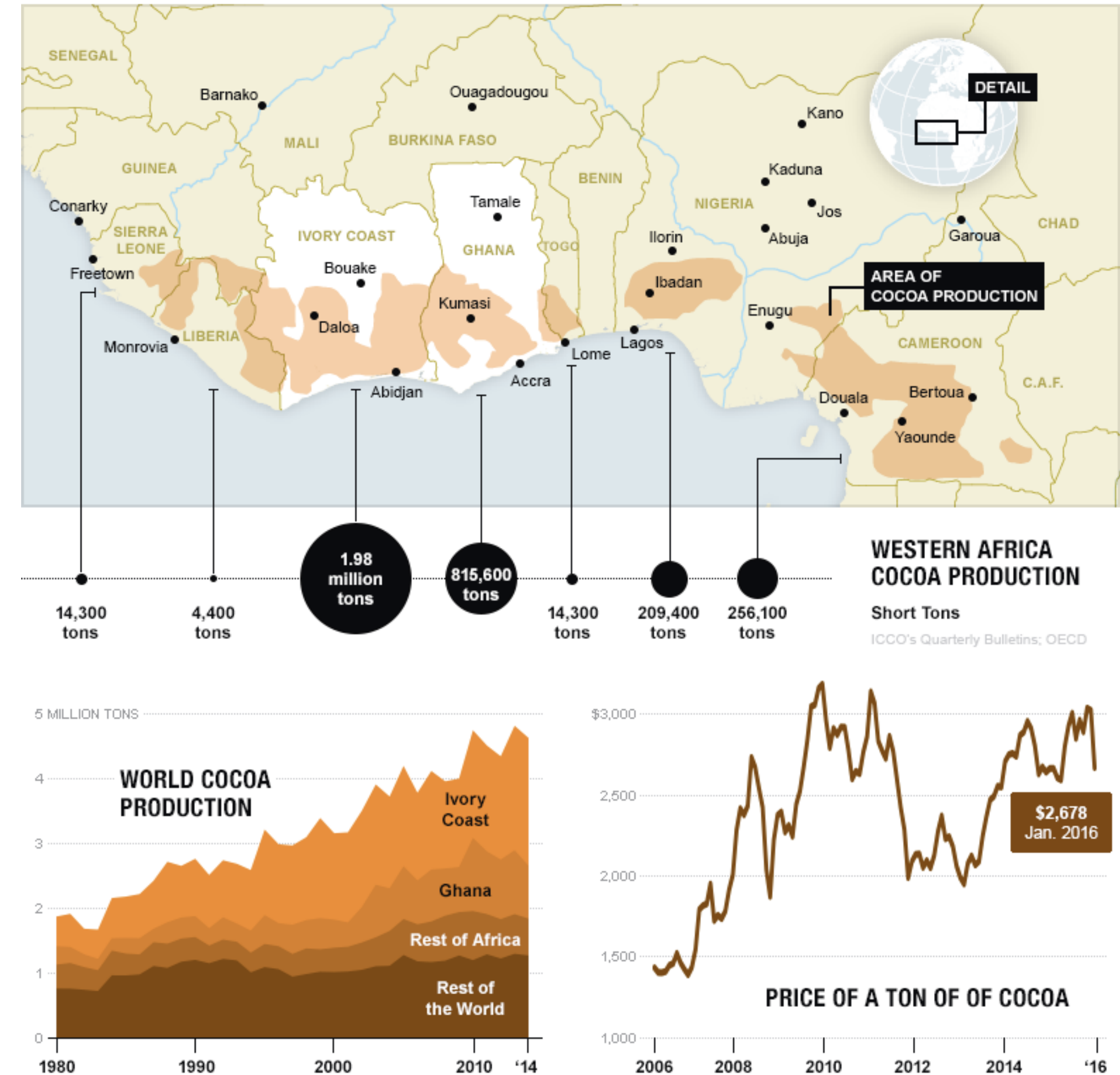
A Closer Look at Ghana's Cocoa Sector

Ghana's economy heavily depends on cocoa exports and the chocolate industry depends on West African cocoa

- Ghana is the second largest cocoa producing country in the world after Cote d'Ivoire
- It is estimated that more than 6 million people, approximately 25% of the population, are involved in the cocoa sector as either farmers, buyers, distributors, processors or retailers.
- Cocoa accounts for approximately 30% of the Ghana's export earnings and is the country's most important agricultural export crop. Around 80% of the cocoa is exported in raw form.

HOT COCOA

As global demand for chocolate continues to rise, so too does production. More than 70% of the world's cocoa comes from Africa. Sixty percent of the total crop is formed in just two countries — Ivory Coast and Ghana. Though the price of the commodity has risen in recent years, farmers in West Africa still live in poverty.



A Closer Look at Ghana's Cocoa Sector

The cocoa value chain is modeled like an hourglass with millions of smallholder farmers at one end and millions of consumers at the other, connected by a handful of companies in the middle where profits are held at the expense of farmers and farmer well-being

It is estimated that in 2013, over half of global cocoa production was traded by just three companies - Barry Callebaut, Cargill and ADM - and that four companies now control more than 60% of the world's cocoa grindings.

This concentration of activities has helped to increase cost efficiency and traceability along the value chain. However, it also enables the big players to exert considerable influence and power within the sector.

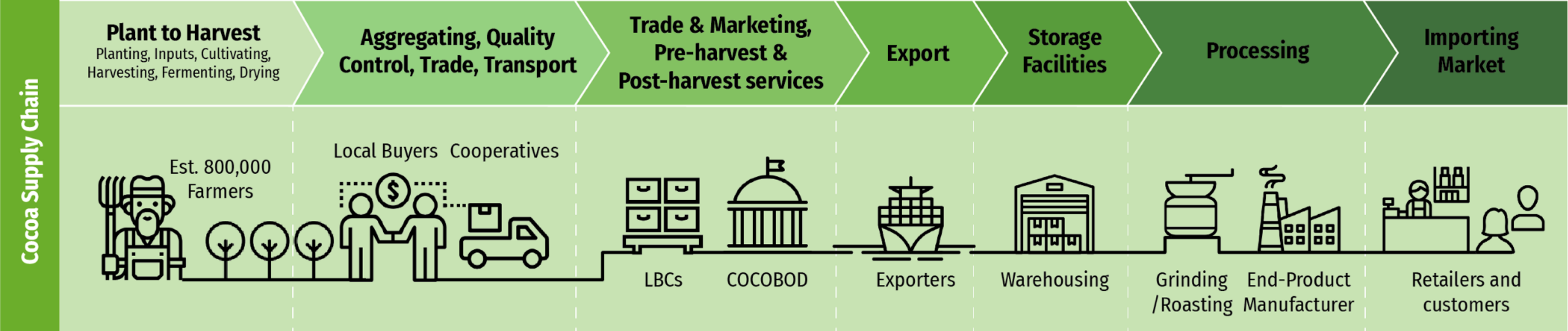
In contrast, cocoa farmers are locked into weak bargaining positions because they individually occupy a minuscule proportion of the value chain. Even when farmers are organized into larger groups, their limited access to resources and services including market information, finance and agricultural inputs places them at a huge disadvantage and renders them extremely vulnerable to fluctuations and shocks in the market.



Stakeholder Map:

Understanding
Challenges Facing
Farmers in Ghana



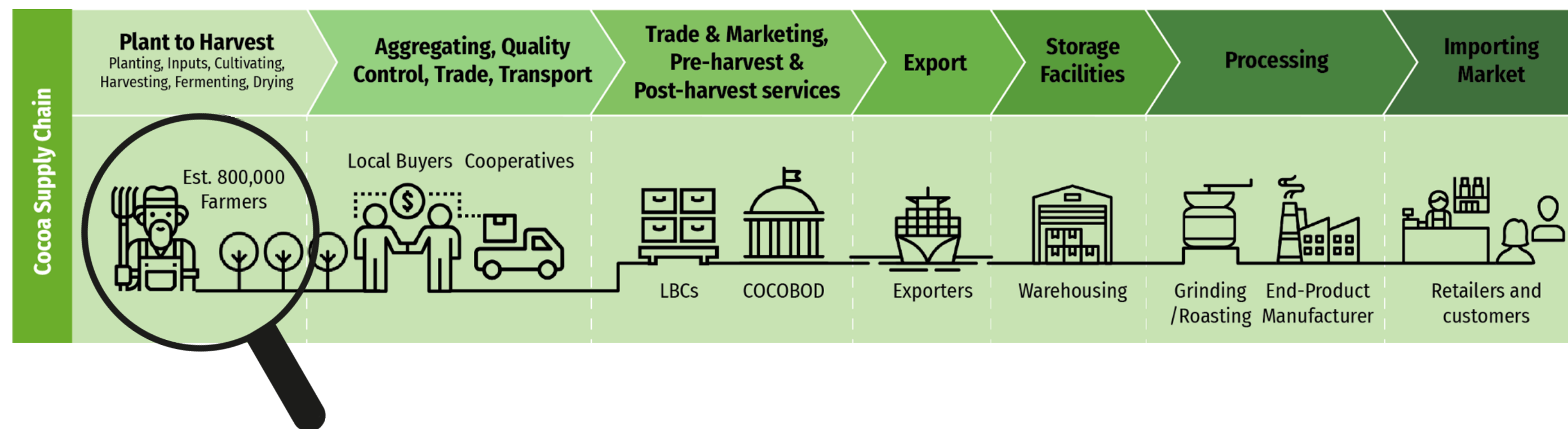


- Farmer income is low
- Widespread black pod disease
- Low yield
- Declining Soil Fertility
- Limited land rights
- Inadequate extension services
- Insufficient replanting of cocoa trees
- Aging population
- Farmer ambition low
- Poor financial management

- Farmers disadvantaged by Purchasing Companies (PCs) via scale adjustment and underpayment
- High sales targets incentivize PC's to squeeze margins with farmers
- Farmers dependent on lending from PC's due to absence of formal credit

- Little transparency over price and budgets
- Corrupt and inefficient distribution services
- Limited private sector engagement to introduce improved inputs and services
- Top down decision making

- Vertical integration has led to few powerful companies exerting much influence over industry
- High barriers to entry for competition
- Lack of transparency in pricing
- Premium prices from certification is inadequate to provide farmers a living wage
- Untimely and inadequate distribution of premium price
- Local processing too cost inefficient to generate meaningful income for country



Low income has resulted in little incentive to grow cocoa and limited ability to increase yields

Aging farmer population

Low incomes has resulted in the **youth leaving cocoa farming** and an aging farmer population that cannot properly weed, prune and apply pesticides.

Farmer yields and income are low and crop disease is widespread

The average cocoa household only earns 52% of the living income for a typical male-headed 6-member household in rural Ghana (\$4,742 per annum).¹ (Royal Tropical Institute (KIT))

Farmer's receiving low price results in their low investment into cocoa production as farmers are unable to hire adequate labor and quality input to maintain soil quality further resulting in widespread black pod disease.

Ghana's COCOBOD estimates that 40 percent of the country's crop needs replanting. COCOBOD, has encouraged farmers to clear away old trees and replant in one part of their land and diversify their crops.

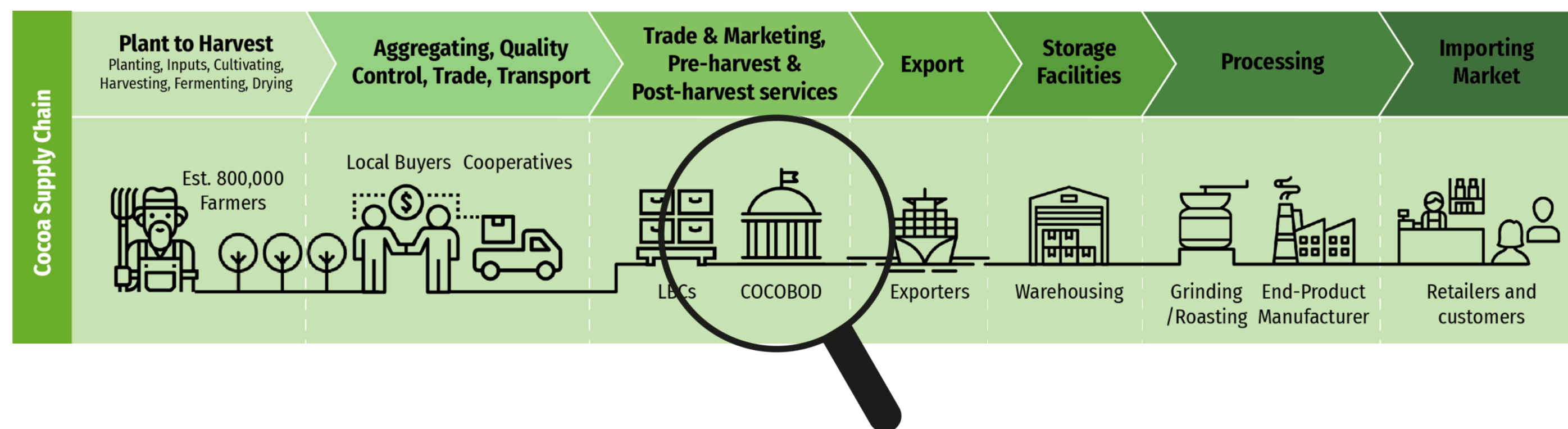
Challenges

Farmers have limited land rights

Under the traditional agreements that govern rural land use, a farmer's land rights are tied to the crops they are growing. Cutting down the cocoa can mean losing your lease. It also takes 3 years for a new tree to produce fruit all of which disincentives crop rehabilitation and better use of land through crop diversification.

Mismanagement of household funds

Poor financial literacy and limited access to credit means that farmers do not properly manage the profits they receive during harvest season when they are well off.



Ghana Cocoa Board acts as the **sole buyer and exporter of cocoa** which protects farmers from price fluctuations

Ghana Cocoaboard (COCOBOD) is a government institution that fixes the national cocoa buying price as a means to protect farmers from fluctuations in the world market price.

For the 2017/2018 season, **the producer price is set at 75% of net FoB (Free on Board) price.** The remaining 25% of the net FoB value is used for cost items such as a buyers' margin, crop finance, haulers cost, storage and shipping, disinfection and grading, inspection and government/COCOBOD revenue.

The use of a 'net' FoB price is somewhat controversial because it implies that certain costs are deducted before allocating a share of the price to the producer. To arrive at the net FoB price, **COCOBOD first deducts an amount from the gross FoB for disease and pest control, fertilizer application (hi-tech), operational input costs, and rehabilitation (nurseries and seedlings).**

The Minister of Finance has the final say in the exact level of the producer price to be paid to farmers; other social and economic pressures especially those related to electioneering and political issues do influence the final level of prices.

Challenges

COCOBOD is not transparent about about prices and budgets potentially resulting in **the inefficient distribution of profits and corrupt practices** that keeps the institution powerful at the expense of farmer livelihoods

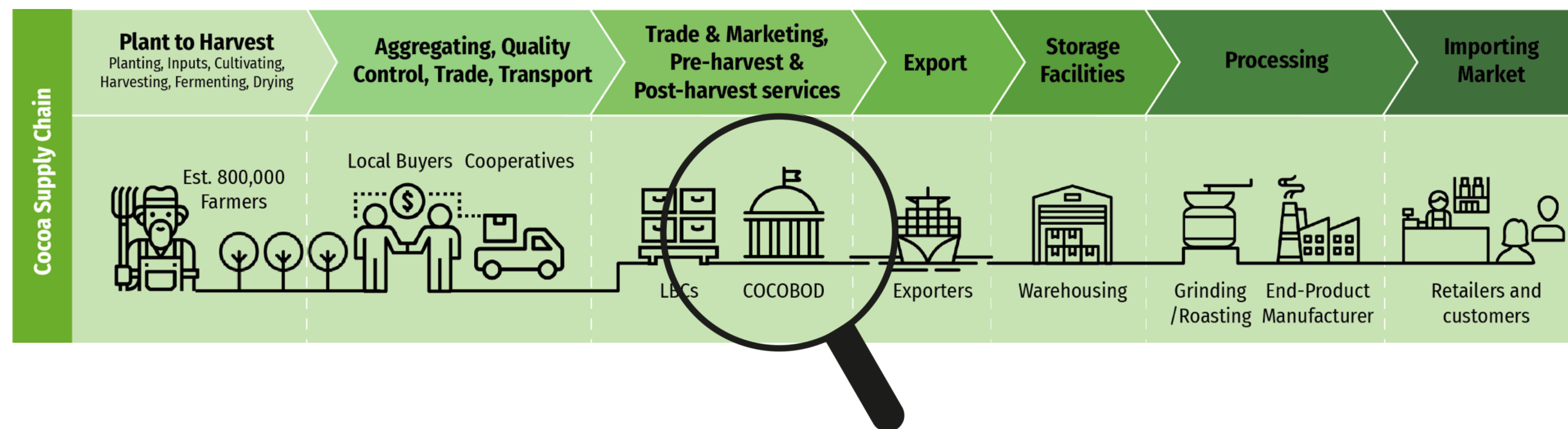
Lack of transparency in sales and price of cocoa

Prices obtained by COCOBOD may differ considerably from global prices because of advanced sales. **COCOBOD is not transparent** about the sales of cocoa beans and prices obtained.

Lack of transparency in budget of COCOBOD services

While producer prices and costs of other services are announced at the beginning of the season, **the rationale for and details of the budget for carrying out industry activities are not published**—even though this budget affects the size and scope of COCOBOD's services to farmers.

Top down decision making
Low participation of cocoa farmers in decision-making in policy formulation (including price fixing) and monitoring.



COCOBOD distributes all inputs and services to farmers

COCOBOD implements a distribution program for fertilizer, agro-chemicals and planting materials. Cocoa planting materials (pods and seedlings) are supplied through its Seed Production Division (SPD) and Cocoa Health and Extension Division (CHED) to farmers. Additionally, COCOBOD procures fertilizer and agrochemicals and distributes them to the farmers under its Cocoa High-Tech Program.

There are no systems in place to ensure that services of COCOBOD are distributed equitably. Supplies that often fall short of demand make equitable distribution even more difficult.

Challenges

Farmers are taxed on the gross FOB price for services but COCOBOD's distribution is inefficient, unequal and limits innovation from the private sector

Unequal distribution of services

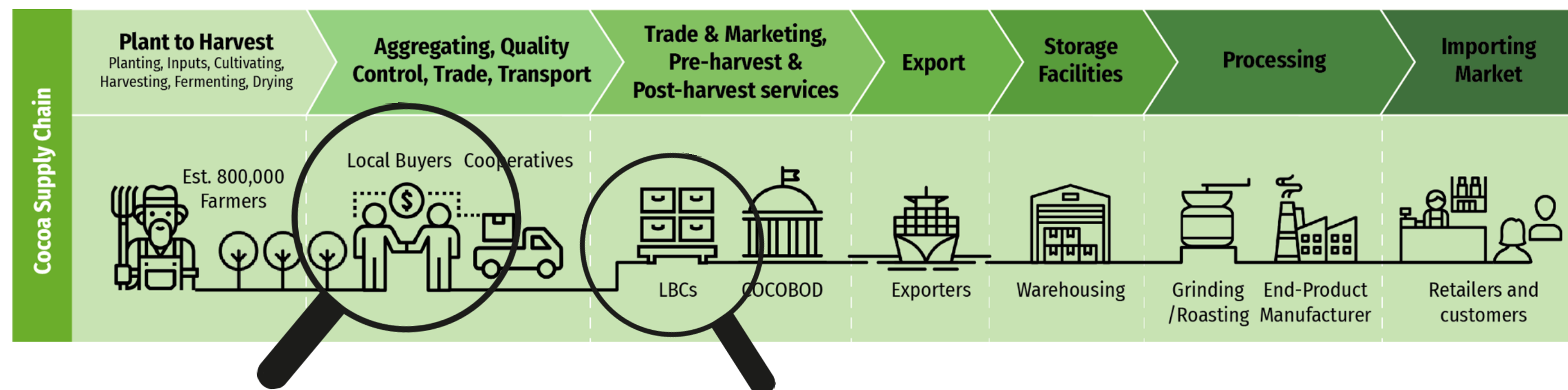
Even though the distribution, as communicated within the public domain, creates an impression that these inputs are supplied for free, in reality farmers pay for them through the so-called "Industry Costs" that COCOBOD levies when setting the price at which they purchase the cocoa from farmers ('net' FOB price). While all farmers effectively pay for cocoa inputs, only selected farmers receive them as the input distribution system is highly politicized, erratic and often corrupt, and in some cases COCOBOD inputs have been illegally exported to neighboring countries.

Lack of transparency

Little transparency on the budget of service delivery has meant farmers accept poor quality and inadequate inputs and services from the government, believing it to be good enough as free and subsidized when in reality they pay for it through the reduced price of cocoa they receive.

Limited access to quality inputs

The seed system in Ghana is still largely dependent on public support (with minimal private sector participation), and the seed value-chain (from the production of breeder seed, foundation seed, its multiplication, and the production and distribution of certified seed) has inherent cost inefficiencies that invariably affect the competitiveness of the domestic seed industry. Furthermore, with the limited development of the private sector in this important area, access to good quality seed among smallholder farmers remains a major issue.



Farmers sell their cocoa to purchasing clerks who are hired on a commission basis by private licensed buying companies

Farmers sell their cocoa beans to a number of Private Licensed Buying Companies (LBC) in the cocoa communities through a local buyer called a purchasing clerk. LBCs act as competitors to the state-owned Produce Buying Company (PBC) (i.e. COCOBOD), which provides buying services for which they receive a fixed margin of the ‘Free on Board’ (FoB) price.

LBCs and their purchasing clerks who purchase, weigh and grade cocoa are not allowed to pay less than the producer price, and do not compete on price (although some pay slightly more for conventional cocoa). LBC’s receive a buyers’ margin (almost 8% of net FoB), and PCs are paid on commission basis. The higher the volume PCs buy from farmers, the more they earn. This is a financial incentive for PCs to build a good business relation with the farmers.

Challenges

Farmers believe **purchasing clerks cheat them of a fair price but are also dependent on them for loans** in the absence of formal credit institutions.

Corruption

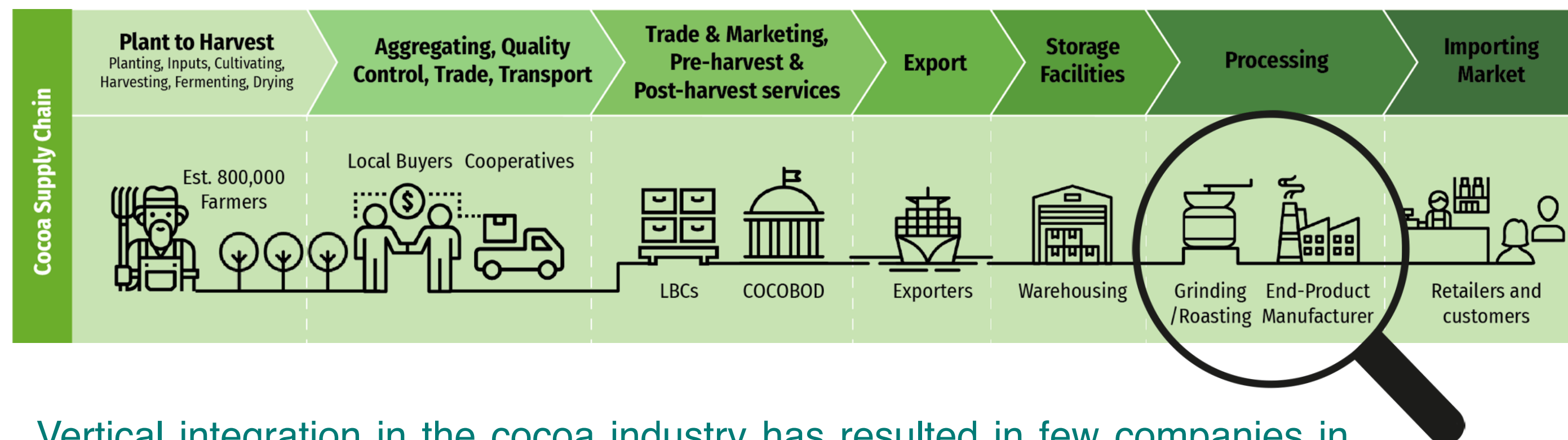
In a study of the relationship between farmers and PCs by the Cocoa Research Institute of Ghana farmers believe that they are being **cheated continually by PCs via scale adjustment and under-payment**. Farmers reported that when they arrive with their cocoa to the shed held by the PCs, the scale was adjusted downwards sometimes by as much as 15kg. They contended that most PCs hire laborers to re-dry their cocoa beans or hire security guards whom they pay a cut of the money they saved from scale adjustments.

Weak governance structures and high sale targets

There is the general perception amongst farmers that the abuses by PCs are due in part to pressure from their superiors (the District Officers were often cited by farmers). **Farmers believe that District Officers of LBCs demand bags of cocoa from PCs who in turn steal from them.**

Farmers lack access to credit

The absence of institutional credit for farmers has created a space for **PC’s in many cocoa communities to become the financial pillar to the community providing soft and ‘hard’ loans to farmers** to meet critical pressing needs such as payment of ward school fees, funerals, hospitalization and farm maintenance. However, many **farmers feel PCs exploit them through various schemes** including mortgaging their farms for loans, refusing to pay for cocoa delivered to them, cheating on bonus payment or provision of hard loans (with very high interest rate).



Vertical integration in the cocoa industry has resulted in few companies in the cocoa industry having large amounts of control across the value chain

The global cocoa industry has also experienced significant vertical integration as companies have expanded their activities from sourcing beans to producing chocolate products. Only a few companies remain that have operations in only one segment of the value chain. The increased consolidation has permitted the attainment of economies of scale and contributed to improving efficiency in the industry, cost and otherwise. It has also meant a few companies have substantial influence over the industry - Mondelez, Mars and Nestlé control more than 40% of global chocolate market share.

Such behavior increases the bargaining power of big and integrated players to the detriment of small actors, and farmers are entrenched in a low bargaining position, which reduces them to “price takers.” The cost savings resulting from improved efficiency in the sector are rarely passed onto farmers.

Certification initiatives by large companies were started to provide consumers with assurances that the cocoa in their products is being produced under ethical working conditions and the price premium charged to buyers is passed onto farmers.

Local processing companies have also been incentivized to keep money in Ghana and receive 20% discount on light crop beans.

Challenges

Few companies have large influence over the cocoa industry resulting in **farmers having little bargaining power** over the price they receive and **high barriers to entry in the industry** to change the sector to support farmers.

Lack of transparency in pricing

Price determination in both Ghana and Côte d'Ivoire is largely done behind closed doors with the power resting mostly with governments and companies. Cocoa producers have little to no voice in the determination of the price that they receive for their cocoa. Farmers are not consulted about what the price of cocoa should be, and are completely uninformed about the process to determine it.

Untimely and inadequate distribution of certification premiums

In surveys with cocoa farmers in Côte d'Ivoire, nearly a quarter of the farmers interviewed had no prior knowledge to the costs and standards associated with certification before becoming certified. Farmer interviews in Ghana revealed many complaints with premiums being distributed late, which has hindered their ability to purchase inputs like chemicals and fertilizer for the following season, particularly since they lack access to credit.

High barriers to entry limit competition

These companies' economies of scale as well as the huge capital needed for starting business in the market is the main obstacle for new companies to enter the cocoa industry and put pressure on companies to change practices. Efforts to produce locally are not that profitable since most of the value in chocolate comes from marketing and branding not from local grinding and processing. The capital investment required to create one job grinding cocoa in Ivory Coast could create over 300 jobs processing cashew nuts. (World Bank 2012).

Value Case:

For-Benefit Opportunity in the
Cocoa Value Chain



The For-Benefit Opportunity: Alignment with Industry Priorities

The Importance of For-Benefits in the Cocoa Ecosystem

Cocoa companies have chosen priority areas to focus on, given specific opportunities for a positive impact in their supply chains.

The four major priority areas that recur across many of the sustainability strategies of cocoa industry leaders and collaborative efforts are:

1. Achieving **sustainable livelihoods for farmers**, including living incomes
2. **Eliminating child labor** and promoting the rights of children
3. Advancing **economic opportunities for women and underemployed youth**
4. Halting or mitigating **deforestation**



Opportunity for Innovation: Emerging Focus on For-Benefit Enterprises in Cocoa Value Chains

- The complexity of challenges facing cocoa farmers will require new ideas and systemic solutions. Many of the challenges discussed in the earlier section lend themselves to entrepreneurial solutions that could lead to lasting and meaningful impact.
- This is why **a growing number of cocoa industry players are taking an interest in working with for-benefit enterprises**, to inject their business with new, sustainable approaches to achieving social and environmental impact.
- Over the last two decades, for-benefits have gained traction as a new way to build companies, innovate within sectors, and create access and entry points for underserved communities.



Value Case for Corporate Supply Chains: For-Benefit Opportunity in Cocoa

Value Case Opportunity	Cocoa Value Chain Elements to Consider
Corporate Values	<ul style="list-style-type: none"> For-benefit suppliers' primacy of purpose (social and/or environmental mission integral to the business model) would strongly align with the company's corporate values and mission.
Environmental Impact	<ul style="list-style-type: none"> For-benefit partners like <u>supply chain mapping companies</u> could help mitigate cocoa related deforestation by ensuring greater visibility of and accountability for environmental performance of suppliers down the value chain.
Social Benefits	<ul style="list-style-type: none"> Sourcing from for-benefit cooperatives with a primacy of social purpose (e.g. ABOCFA) could benefit farmers by increasing incomes, reducing the need for child labour and help <u>farmers secure their land rights</u>.
New Employment Opportunities	<ul style="list-style-type: none"> For-benefit companies in local cocoa processing can have the <u>potential of creating jobs in West Africa</u>. This expands job opportunities to new segments along the value chain.
Sustainability	<ul style="list-style-type: none"> Sourcing from a for-benefit supplier can help support corporate sustainability goals around environmental efficiency. Working with for-benefits strengthens capacity for long-term sustainable farming techniques to drive future revenue
Revenue Opportunity	<ul style="list-style-type: none"> For-benefits that support farmers with re-planting healthy cocoa trees could generate greater yields and revenue.
Cost Potential	<ul style="list-style-type: none"> For-benefits locally processing could result in reduced export costs of processed cocoa.
Brand and Reputation	<ul style="list-style-type: none"> Strong brand value due to social mission and social/environmental impact of for-benefit businesses in supply chain would result in higher customer loyalty and employee retention. Increased transparency - an important issue for consumers - as a result of for-benefit reporting, helps build trust in your product.
Challenges and Risk	<ul style="list-style-type: none"> For-benefit companies in supply chain are structured to be resilient in changing conditions (training & support, increase fertility of the land in long-term); Prevent the use of child / forced labor which reduces risks to company.

Case Studies





ABOCFA

Organic-Fairtrade Cocoa from Ghana

- Started with the guiding mission of environmental stewardship, achieving 100% organic cocoa from farmers in 2009, ABOCFA is a cooperative of cocoa farmers.
- Consists of 700 farmers in 13 hamlets. ABOCFA is currently maxed out on membership, with a waitlist for those wishing to join.
- Added Fair Trade certification in 2011.
- Vision is to be a leader in the supply of quality Organic – Fairtrade cocoa beans whose members have improved livelihood and are resilient.

For-Benefit Characteristics:

- Organizational structure is democratic with all members voting on governance structure, accountability and management.
- Premiums are pooled with 50% having been voted on to go directly back to farmers in cash distributions and the remainder used on the certification fees, core organization costs, the training, agriculture support and community services.



Impact:

- Provide farmers support through training, pruning and spraying of trees to keep quality consistent and decrease burden on members. ABOCFA takes an active role in marketing and engaging with purchasers in order to guarantee their cocoa is secured for the premium.
- Partners such as **Tony's Chocolonely** are able to secure 100% traceability (a key marketing and mission tenant for the company) and a reliable high-quality source of Fair Trade cocoa.



- Divine Chocolate was launched in 1998, born from Kuapa Kokoo, now the largest cocoa cooperative in Ghana.
- Kuapa Kokoo is a Fairtrade-certified cocoa farmer organization in Ghana that owns 45% of Divine Chocolate's shares. The cooperative currently has over 100,000 registered members.
- Divine's chocolate bars are carried at Whole Foods, The Co-Op, and WHSmith, among other global retailers.

For-Benefit Characteristics:

- Founding purpose is "to help farmers gain a share of the wealth they are helping to create, putting them higher up the value chain." In doing so, this creates a supply chain that shares value more equitably and serves as an example of a viable model for how to secure the sustainable future of cocoa and cocoa farming.
- Certified B Corp.



Impact:

- Divine provides Kuapa Kokoo a guaranteed minimum Fairtrade price of US \$1,600 per ton, protecting farmers from the volatility of the market.
- An additional premium of US \$150 per ton is invested in improvements to the farmers' living standards and farming productivity.
- 2% the price of Divine bars goes towards 'producer support and development', which Kuapa Kokoo spends on farmer education, maintaining the values and vision of the cooperative as it grows.



- Founded in 2015 as Landmapp, Meridia provides services to digitally map land boundaries and validate legal documents to help secure ownership of land for cocoa farmers.
- For an average of USD \$100-120 (of which 70% are official fees paid for signing and legalization), Meridia provides the farmer with a customary land rights document.
- Expanded operations to Indonesia and Malawi, where it is working with Unilever and Sainbury's supply chain traceability.

For-Benefit Characteristics:

- Mission driven company, driving their growth. Meridia's mission is to make the equitable distribution and use of land accessible to all.
- For cocoa farmers in Ghana, land ownership is one of the most important path to prosperity. Clear access to land offers everyday sustenance *and* long-term economic perspective.



Impact:

- Mapped 104,900 hectares, documented 13,510 parcels documented and impacted 101,120 people.
- Sixty-six per cent of Meridia's customers indicated that their quality of life improved after obtaining documentation. With tenure security, farmers have proven willing to invest in the maintenance of their farms and explore better farming methods because they now consider the farm truly their property.



- Since 1985, Maquita has promoted productive, commercial and association enterprises, including AgroMaquita.
- They work with craft groups and small farmers around Ecuador, helping with production, design and marketing of their products.
- AgroMaquita specifically supports farmers and acts as an exporter of cocoa beans and semi-processed cocoa products.
- Founded by a group of Christian church communities to combat rising poverty and inflation.

For-Benefit Characteristics:

- Mission is to bring together small food and craft producers in order to increase their strength in relation to the national and international market.
- Its governance and organizational system is 100% democratic and participatory.
- Fairtrade and organic certified.



Impact:

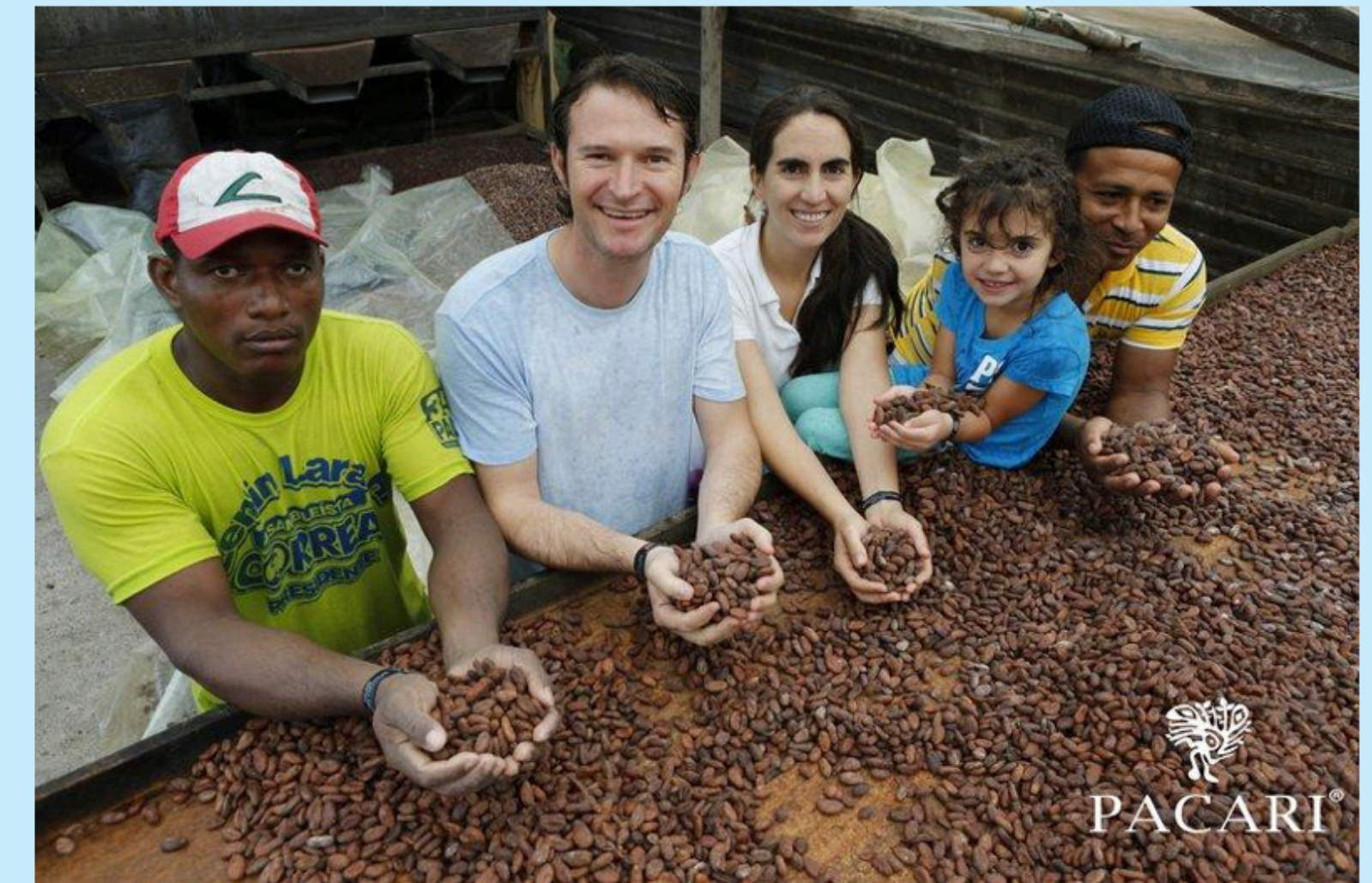
- Over 500,000 active participants, 45% are women.
- AgroMaquita pays 8 to 15% above the price to farmers by other exporters.
- Provides training to farmers on innovative production techniques, post-harvest management and farm management, including accounting and business planning.



- Pacari Chocolate was founded in 2002, as a family-owned company, dedicated to making the highest quality organic chocolate from Ecuador.
- The first single-origin organic chocolate made entirely in Ecuador.
- 2013 overall gold winner at the International Chocolate Awards.
- Works directly with small-scale traditional cacao growers, not plantations.

For-Benefit Characteristics:

- Pacari “believes that business, especially in a developing country like ours has a duty to support healthy and environmentally sound production.”
- Sourced and developed to preserving the native Arriba Nacional cacao.
- Fair trade, Biodynamic certified, Kosher, and Certified Organic



Impact:

- Provided traditional growers direct and active participation in the Ecuadorian cocoa industry.
- Provides small producer financing to form associations, buy technology and support certification costs.
- Works with 3,500 families through 7 farmer associations.

Recommendations



For-Benefit Procurement: Build an Ecosystem of For-Benefit Partners

- For-benefit enterprises represent a sustainable path forward for the cocoa industry as large cocoa companies seek to **prevent or overcome environmental and social challenges** while still generating a profit.
- Building up the for-benefit ecosystem will be imperative to **aligning with cocoa companies' priorities around social and environmental sustainability**, while also gaining the most value from their supply chains.
- This can be achieved through a focus on creating a better **network of and enabling environment for the growth of for-benefit enterprises** that can support or be directly embedded into cocoa supply chains.





Engage Government to Ensure Conducive Policy Environment for For-Benefit Enterprises to Grow

Challenge:

- In Ghana, there is momentum in the policy environment to support social entrepreneurs and for-benefit enterprises to help them overcome typical start-up challenges, including:
 - lack of training for entrepreneurs;
 - navigating government regulations;
 - access to funding.

Recommendation:

- Strengthening the West African for-benefit enterprise landscape will require **support for promising individual for-benefit businesses** that can serve as role models and proof points for other stakeholders.
- It will also require **investments in the ecosystem itself**, with programs that address the needs of entrepreneurs at different stages, the availability of **flexible forms of capital**, and **support for policies that enable local entrepreneurs to succeed**, whether by reducing barriers for registrations, certification and permits that companies need, or avoiding subsidy programs (especially in cocoa - e.g. fertilizers and seeds) that create disadvantages for commercial business models.



Build and Cultivate the Marketplace for For-Benefits to be Identified and Supported

Challenge:

- For-benefits struggle to respond to sourcing opportunities from large cocoa sector actors, and require help to meet procurement opportunities.
- In turn, large cocoa sector actors often themselves are unaware of innovative services and products are being offered by smaller for-benefit enterprises.

Recommendation:

- Sector players can utilize regional for-benefit incubators like Ghana Climate Innovation Center and Growth Mosaic to identify for-benefits. They can also work with these incubators to finance pitch competitions and provide investments as prizes.
- This helps larger cocoa companies gain greater visibility in the innovation pipelines for companies that could positively disrupt the cocoa supply chain.
- It also serves to grow for-benefit supply chain options in the future and creates connections early as these companies grow.



Ensure Financing Takes into Account a For-Benefit Organization's Primacy of Purpose

Challenge:

- Many for-benefit businesses struggle to grow because their guiding principles require local and motivated regional leads to ensure the social mission does not come second to revenue generation.
- For-benefit businesses also struggle to meet expectations of traditional investors because they know that rapid growth cannot come at the expense of the primary purpose and mission of the organization.

Recommendation:

- Companies and investors need to respect the social mission of for-benefit businesses when committing investments and create appropriate impact-oriented performance metrics, aligning with their own desired social and environmental impacts.
- Funding these companies directly or supporting connections to flexible, appropriate sources of funding and impact investors who are genuinely committed in supporting entrepreneurs with both social and financial goals is critical to grow for-benefit impact and innovation.



Recognize and incentivize for-benefit businesses as critical partners for increased supply chain health and sustained impact

Recommendation:

- A healthy for-benefit ecosystem is key to being able to replicate impact along the entire cocoa supply chain. Cocoa sector actors can:
 1. Encourage government to implement policy that formally recognizes for-benefits;
 2. Support networks and associations to boost shared learnings, networking, and camaraderie around for-benefits;
 3. Facilitate hack-a-thons and other events with accelerators and incubators to encourage new for-benefits to break through into the cocoa sector and design innovative models to overcome challenges in the cocoa industry.
- Consider priority impact areas alongside cost and other traditional procurement factors when selecting certain suppliers in the cocoa value chain. This can encourage current for-profit vendors to move towards for-benefit status and will increase for-benefit businesses' competitiveness as they are achieving multiple outcomes.