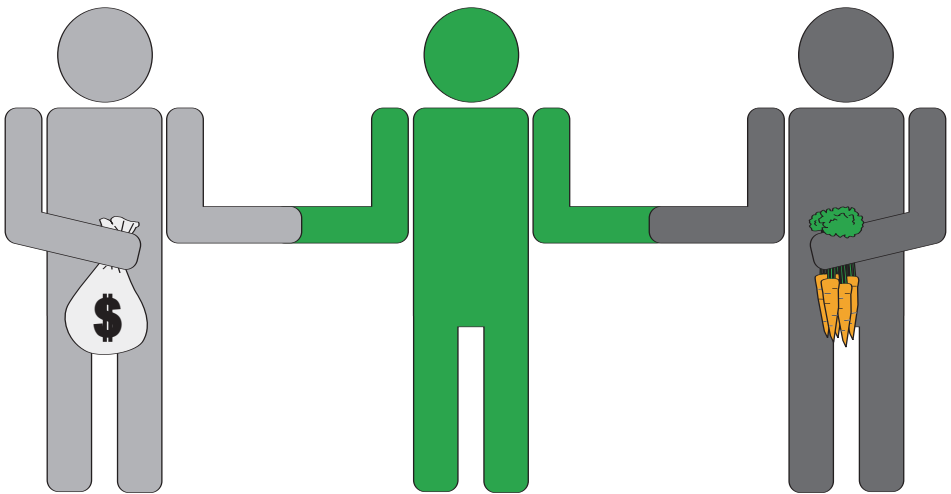




SWEDISH COOPERATIVE CENTRE

Farmers' Organization's Guide to setting up a Small Scale

# BROKERAGE



in Southern Africa

H. G. Lutz







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## *Foreword*

Lack of access to remunerative markets and high transaction cost are two of the biggest problems faced by small-scale farmers in Southern Africa. Individual marketing of products results in high cost for identifying the market and high transport cost. Very often, small-scale farmers take the easy way out, selling their produce to local traders. Lack of market information and negotiation skills result in most small-scale farmers selling their products at below market price, exacerbating the already severe lack of capital.

Farmers' Organizations in the region are suffering to achieve financial sustainability of their activities. Few organizations can sustain their activities on incomes from member subscriptions alone. Additional incomes from services offered to members are therefore needed. Levies or service charges on marketing facilitation activities are among the options. However, most organizations have failed to develop effective mechanisms for collecting such service fees.

SCC contributes to the solutions to this problem in many ways, whereof one is assessing the possibilities for farmers' organizations to identify and operate profitable businesses. The businesses identified should utilize lots of what farmers' organizations generally have relatively much of and little of the assets that are mostly in deficit. One such business is a small scale brokerage, which is the subject for this Guide.

A brokerage takes advantage of superior access to information (in this case market information) to minimize

transaction costs for sellers as well as buyers, and charges a fee for that service. In essence, this is the same service that a trader offers, but a trader never links the seller to the buyer. Instead, a trader takes over ownership of the goods, and then in turn becomes a seller herself. A brokerage therefore is associated with relatively lower risks than trading.

Further information on SCC ROSA's support to Farmer's Organizations is available on [www.sccrosa.org](http://www.sccrosa.org).

On behalf of SCC I would like to express the deepest felt gratitude to Anne Chisanga and Joseph Dzanja, who authored the lions' share of the guide; Mariam Mapila, Benito Eliasi, and Ian Goggin whose help was crucial in the production; and countless others, whose names do not appear here but who nevertheless have been invaluable in the process. Thank you.

H. G. Lutz  
Editor and co-author





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# Introduction to Brokerage

Smallholder farmers often have difficulties accessing reliable markets for their commodities. This problem is more prevalent in developing countries, especially those of the Sub-Saharan Africa where most farmers are not organized and illiteracy levels are high. Individual farmers have difficulty identifying buyers for their commodities, let alone engaging in effective business negotiations. Organization among farmers has mostly taken such forms as farmers associations, cooperatives and clubs. Management of these organizations has often proved difficult, as they have failed to attract significant membership. Members' needs for such organizations have therefore not been adequately met.

One of the possible ways of solving the marketing problems faced by farmers is to identify a mechanism through which they can be linked to potential buyers. A brokerage is one such mechanism, and the possibility of establishing a low cost Brokerage is the subject of this guide.

The first issues to tackle are: Who is a broker?; What does she do?; How does she get started?; How is a brokerage different from other trading businesses?

A broker is an agent for trade, connecting buyer and seller without at any time taking over ownership of the goods being traded. Brokers are market-makers: they bring buyers and sellers together and facilitate transactions. Brokers play a frequent role in 'business-to-business' and 'business-to-consumer'. To achieve these roles, brokers must be professional negotiators for them to link the parties involved and to make sure that the parties are happy with the brokerage.

The broker utilizes superior access to information (in this case market information) to minimize transaction costs for sellers as well as buyers, and charges a fee for that service. In most circumstances a broker is a third party to an agreement to purchase a commodity. The item being bought and sold is neither owned nor controlled by the broker, who simply acts as an intermediary and is normally paid on completion of an agreement. The broker has to have good market information to help her serve her clients better. She has to make sure that the buyer and/or the seller actually find it profitable to pay her for the service.

All businesses consider information a strategic resource that is essential to help them stay on top of changes in the market, new ideas, competition and other operations of their business. A broker has to track down and locate the specific information a business, organization or client needs. If you engage in this business, your task is to find, organize, analyze and use the information to serve your customers.

## **Differences between a Broker and a Trader**

It is important to point out from the outset that brokerage is related but not similar to a Trading Business. In essence, both a broker and a trader interact with commodity sellers and buyers. The difference is that a trader never links the seller to the buyer. Instead, a trader takes over ownership of the goods, and then in turn becomes a seller herself. The trader does not have to have access to a buyer and a seller at the same time, nor does she have to be entirely sure where to find the buyer if she finds a good seller. She only has to know that there is a profit to be made. On the other hand, trading involves the use of (often substantial amounts) money to buy, store and transport goods, and it involves a fair amount of risk. In contrast, brokering does not involve taking title to the goods involved in the transactions and therefore considerably lowers risks.

### *Major differences between a Broker and a Trader:*

A trader buys the goods and sells them elsewhere (usually at a profit). A broker does not engage in buying and selling of the goods under transaction. Instead she helps in linking the sellers and buyers of goods to facilitate the transaction.

A trader (by paying money for the goods) takes title to the ownership of the goods. A broker never takes title to the goods under transactions.

A trader needs substantial cash to buy, store, process and transport the goods in her business. In contrast, brokers use a minimum of cash.

## **Functions of a brokerage**

### *Deal Negotiations*

A broker helps to facilitate the negotiating process. Buyers and sellers have to agree on the terms of exchange before the transaction can take place. Negotiating for terms of transaction can be an emotionally charged affair since each party wants to reap more from the transaction. One therefore will benefit greatly from a third party who can handle all aspects of the transaction. A broker is in a better position to speak more candidly to each party involved in the transaction than they could manage on their own.

A broker acts as a coordinator in facilitating purchases and/or sales. She does this by providing information to both buyers and sellers about who is buying and selling a specific commodity. This coordinating role is only achievable if the broker accesses market information from whatever source deemed reliable.

This function can be difficult if farmers are not organized, and therefore calls for formation of farmers' groups. The elected leaders of these groups should be the ones in constant touch with the broker. It is these leaders that should constitute the association's executive at district level. At this level, they should be able to consolidate orders of inputs required by their members and produce quantities available in their respective areas. This information should be relayed to the broker for onward transmission.

Brokerage is even more necessary for the already existing farmers' organizations because, as said earlier, most of these organizations have difficulties identifying markets for their

commodities. They do not have adequate information about the requirements of the major agribusiness buyers, quality and quantity needs and pricing information. Relevant market information is also expensive to collect, and thus many organizations do not have time or resources to identify commodity markets. Brokerages therefore significantly reduce the transaction costs for the farmers.

### *Reduction of Transaction Costs*

Brokers help reduce costs that are associated with the product or commodity transactions. Every commodity exchange function is associated with costs that have to be borne by both buyers and sellers. Farmers have to look for markets for their commodities /products. Most major commodity buyers are located in the cities and towns while production is done in remote rural areas. In search for buyers, they may have to travel long distances, and negotiations for a deal may likewise take too long to reach. In the process, farmers have to take multiple trips and thus spend money on transportation and other related costs.

Buyers likewise have to spend time and other resources in search of the commodities of the right quantities and quality. Sometimes goods delivered may prove to be defective and the transaction may fall through despite costs incurred by both parties. Due to power imbalances between buyers and sellers, farmers may face unscrupulous buyers or traders who may take advantage of their (farmers') ignorance of the market conditions to buy the commodities at prices far below the optimum levels. These costs incurred during and as a result of the transactions are known as Transaction

Costs. The higher the transactions costs, the lower the returns to the commodity producers and buyers.

A broker helps to untangle any complicated administrative procedures. An experienced broker will know the most efficient way to acquire all the necessary permits and licenses. For example, for farmers to export some agricultural commodities they may need special permits and the procedures to get the permits may be long. A broker can help assist the farmers to get the same permits quickly.

### *Bulking*

Brokers facilitate Bulk Buying. Most smallholder farmers produce commodities in small quantities while most buyers (like large Agri-businesses) buy in bulk. Bulk buying has the advantage of minimizing the cost of sourcing the required commodities since the buyers do not have to move from one point to the other collecting small quantities of goods from individual farmers. Instead the broker is the one who can organize the farmers to assemble their goods at one central and accessible point from where the buyers can collect the goods. The other advantage with this arrangement is that the broker also makes sure that the goods assembled meet the required quality standards.

### *Transport arrangements*

Most smallholder farmers don't have capacity to transport their goods at individual level unless they link up with other farmers to pool their financial resources together and hire a vehicle. Transport may be required when the buyer specifies that the goods be delivered to her place. The broker in this case

may link the farmers to a reliable transporter with reasonable prices. The broker must keep a database of transporters from which she can recommend to farmers depending on the nature of the goods to be transported. For example, a group of farmers who have 40 metric tons of maize in stock may have difficulties identifying a good transporter to their identified buyer. The local transporters may be prohibitively expensive. A broker could in that case assist the farmers in identifying a reliable transporter with reasonable prices. In so doing the broker has provided services to both parties – the transporter and the farmers. Brokerage fees can be charged on the total value of goods transported, the value of the transportation revenues or any other agreed-upon remuneration procedure. As long as the farmers realize that by using the brokerage service they will save money –even though they have to pay a commission- they will certainly use the broker.

*Facilitation of the establishment of formalized agreements and contracts*

A broker should also coordinate the preparation and negotiation of commodity buying/selling contracts between buyers and sellers. This is needed much more in a situation where one party does not agree with some parts of the contract or does not understand the implication of the contract to the transactions. Commodity buying and selling contracts are usually simple and therefore easy to understand. In some cases, however, smallholder farmers may not adequately understand the implication of the contract to their farming businesses. A broker can bring the potential buyers and sellers together for negotiation until both parties are comfortable with the terms of the contract,

and she can be of assistance in learning how a contract can be enforced. Please refer to the SCC ROSA material on Contract Negotiations on this matter.

### *Information Supply*

Information flow to and from the farmer is very vital for production and marketing decisions. Farmers are exploited because they lack relevant market information that can assist them make accurate business decisions. Traders take advantage of this ignorance and may press to buy their produce at lower than optimum prices. This is what mainly ruins their businesses. Information is a very powerful asset for a brokerage.

A broker however can not disburse all the information she has – if she did, the business would not survive. She has to disburse only the information that will generate business. Such information includes information related to prices and quantities demanded. It is not advisable for her to provide information about the buyers- otherwise the farmers will make direct linkage to the buyers.

Dissemination of information can be done in several ways. Some people may come direct to the broker's office and get it. The broker may also use the media houses like radio stations and newspapers, publications which can be sold or given out free. This information may also be displayed at the broker's office on bill and display boards. Meetings can be convened where messages can be relayed. This method is good because clarifications can be made right there. Potential buyers and sellers can just be placing their

information with the broker. They may as well invite the broker to their meetings where she can collect the information.

### **Characteristics of a Good Broker**

Customers will always want to use a broker who has good reputation as regards meeting their needs. Brokers must therefore possess desirable attributes that would enable them to attract new customers and retain existing ones. The following are some of the major important attributes that a broker needs to have:

*Negotiation Skills:* A broker must be a good negotiator because she must bring two different parties (buyers and sellers) together and assist them in creating deals that benefit all parties involved.

*Availability:* The broker must be available, even if it is just on her mobile, so that all parties immediately can clear queries that arise.

*Knowledge:* The broker must be equipped with adequate knowledge about the technical skills to run the brokerage because customers (both buyers and sellers want to engage a broker that can provide advice on various issues to do with product markets.

*Trustworthiness:* The broker must be someone that customers believe they can put their trust in because they will be working with him or her quite closely in the future. She must have credibility and bring across to the customers a sense

that she is reliable and can assist to secure a good business at the best price in the shortest amount of time.

*Easy to Get Along With:* The broker must be approachable and easy to talk to. Clients should feel comfortable to visit the office anytime and be assured that their needs will be addressed. Such character will result into a very warm relationship between the brokerage and the clients.

*Credentials:* The broker should be somebody who is highly recommended as a reliable and honest person. Sometimes such credentials stem from a personal track record, as when someone has been visible in society for some time, showing she can be trusted. More often, however, credentials come with positions or titles, and are connected to some organization or another. In the case of a small scale brokerage in an agricultural setting, member based farmers' organizations tend to be credible indeed. The broker must also be licensed or approved to do business under the regulations in the state in which the brokerage is run.

### **Potential Challenges of a brokerage**

A brokerage has its unique challenges. It is therefore important that aspiring brokers must know these potential challenges. As has been pointed out earlier brokers bring buyers and sellers together and facilitate transactions. In this way, a broker is called to the task of finding and holding the middle ground, and then that of transforming all parties involved into a commitment to the transaction. To find and hold the middle ground takes a sense of mission and strength of character. To create a win-win situation for all, takes tenacity and a level of

integrity which must be above suspicion. It is therefore necessary that a broker understand the likely challenges that may be encountered in her business. The following are some of the possible challenges that a broker may face:

*Power Imbalance*

A transaction takes two parties, i.e. the buyers and the sellers. If one party does not have adequate capacity to negotiate effectively for the transaction there is power imbalance and in certain cases this situation leads to lack of mutual understanding and respect and the deal can fall through. A broker is supposed to take a balancing role so that the two parties can understand each other until the transaction takes place. Commodity exchange can sometimes be an emotional activity since both sides want to win. This is a challenge that every broker must be prepared to face.

*Absence of Sincerity and Integrity*

Sincerity and integrity are the lynch pins of a successful brokerage. The character of sincerity and integrity is important for all the parties involved in a transaction, (i.e., the buyers, sellers and the broker herself). Some unscrupulous buyers may not be willing to pay for the commodities delivered. Some sellers may sell stolen goods or they may deliberately under pack their commodities. For example instead of packing 50kg bags of tobacco, they may pack 45kg or even put stones or sand at the bottom of the bale/bag to cheat the buyers. Some Brokers may hide behind some farmers to pose as commodity sellers. In this way they wouldn't want to follow the rules. If buyers discover this scam they may be put off and a broker may lose her

business. A broker must therefore investigate thoroughly the sort of people she is dealing with; keeping in mind that once involved in a corruption scandal the brokerage will lose its good image.

### *Identity Problems*

Some major buyers of commodities are so much used to buying from particular sources. They may therefore find it difficult to accept the brokerage role of the broker. It takes time and a lot of effort to convince buyers and sellers that they would benefit by using a broker and yet they have to pay for the brokerage services. This payment was never there before. Some of the clients may argue that the whole issue is their business and that a third party is not needed. They may even go on to lay down various excuses so as to put obstacles in the way of the broker. They may give the following excuses:

- It is no business of the third party
- The third party cannot know enough about our business
- The third party does not have the feel and idiom for our policies
- The third party has nothing at stake and does not have to live with the result of a broken contract.

The broker must therefore be an effective negotiator to motivate both buyers and sellers towards using her brokerage.

### *Cultural Attitudes*

Sometimes cultural attitudes or traditions pose severe obstacles for establishment of successful Businesses. For example, some communities do not trust professionals that have grown up in the same communities. They would rather deal with strangers. In such societies, and of course in all other societies, it is of paramount importance for the broker to cultivate good public relations with the clients by reaching out to them to sell the business and thus dispel the air of mistrust.

### *Incentive Structure*

In a brokerage, it is of uttermost importance that the broker is motivated to do business, and as much business as possible. In a one-person private company brokerage this is not a problem, as the owner of the company will get all the proceedings from the business, and hence has an income that is directly and only dependent on the turnover. However, as soon as the broker has to share the profit with another party, problems arise.

## **The Position of a Broker in the Marketing Chain**

The sequence of stages involved in transferring produce from the farm to the consumer is generally referred to as a marketing chain. The buyer could be as close to the producer as the same village. All transfers involve marketing activities in some form or other. All activities involve costs. At the simplest level the cost involved may just be the time taken by a farmer to walk to a nearby market and stay there until all her vegetables are sold. At the most complex level a product may be stored for lengthy periods, transported long

distances and processed several times before reaching the form in which it is finally sold.

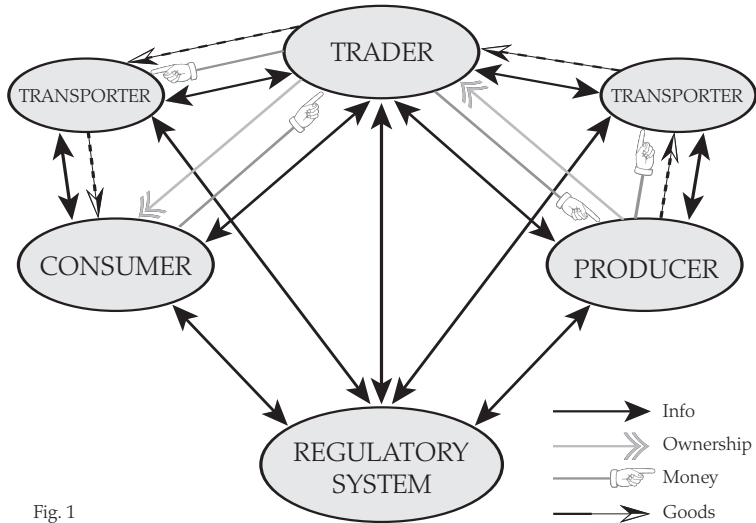


Fig. 1

In an ordinary market chain, all players need to establish contact, make transactions and sustain relations with a large number of other players. The number of relations usually grows with the number of transactions, as the players change over time. These activities are time consuming, difficult and costly.

## BROKERAGE

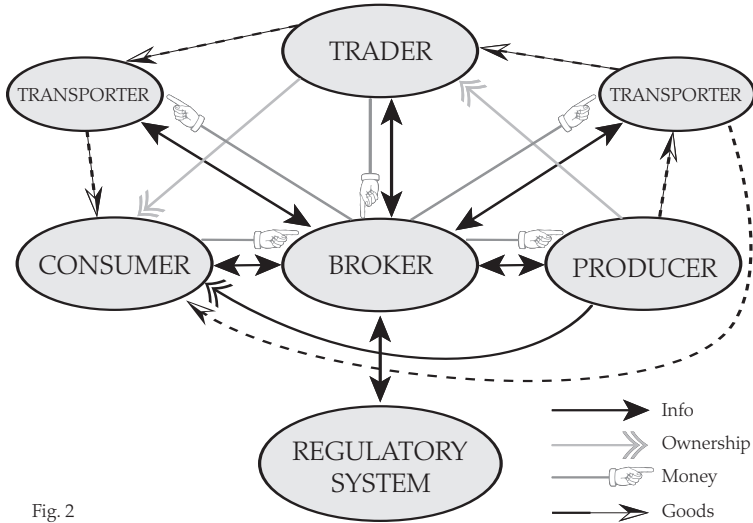


Fig. 2

*A broker eliminates many of the relations, cutting the number of contacts and transactions necessary, thus minimizing time invested and total costs in the chain. The brokerage's function of linking together parties in the Agricultural sector that are otherwise separated is a most important side-effect.*



# Assets

As has been discussed, a brokerage's most important asset is market information. However, there are lots of other assets that are immensely important. A brokerage is totally dependent on good relationships and mutual trust between the broker and the customers (commodity buyers and sellers). Some of the necessary assets are Intangibles, whereas others are Tangibles.

It is important to keep in mind that farmers can sell their produce, and commodity buyers can find their required commodities, without going through a broker. If these sellers and buyers are to seek brokerage services, they must be convinced that such services will not compromise their business values. A broker must therefore have an attractive character that could build and preserve mutual trust between him or her and the customers. Customers can not deal with a broker who is corrupt and who does not honor her obligations. A broker must be trustworthy and above reproach in her business dealings. Her business must adequately serve the needs of the customers to ensure that customers are satisfied, and the brokerage itself must have adequate assets to serve its customers.

An Agricultural Processor in the city will have difficulties trusting a broker who is not contactable. Customer satis-

faction builds trust between the broker and her customers, thus enabling customers to deal with a broker without any reservation. This trust is an intangible asset. It can not be touched or seen, but it is there at both personal level and institutional level and adds a lot of value to the business. However, the phone line and the fax machine that make communication possible are tangible assets. Tangible assets alone can not attract brokerage customers, though they support the activities of the brokerage.

### **Information You Need**

Market Information is one of the strategic resources of brokerage and is essential to help the business stay on top of changes, new concepts, competition and other operations of the business. A commodity broker must have a systematic way of collecting relevant market information. This information must be updated regularly to make sure that all market changes are captured. A broker can hardly provide professional advice to her clients if relevant information is not available or if wrong information is given to the clients. The question is 'what kind of information should a commodity broker have'?

The following types of information should be collected, analyzed and safely stored by the brokerage:

- **Product/ Commodity Information:** This is information associated with particular products or commodities. Such information includes:
- Types of commodities or products produced in various regions of the country.

- Production volumes in each region (both current and past volumes). Past volumes can be used to check the trend of commodity production volumes over time and this trend can also be used to predict future production quantities.
- Prices of each type of commodity (both current and past prices).
- Local major commodity buyers. Information related to all major commodity buyers must be collected as well. The buyers could be Commodity processors like Maize Meal processors whose major raw material is maize. Information for commodity buyers should include their physical addresses, telephone and fax numbers, names of contact persons, type and quality of commodities which they buy, average quantities which they buy.
- Export markets: Information related to export markets should include all commodities required by international buyers and their quality standards. Information also related to export documentation should be collected. For example, phytosanitary certificates are required if one is to export crop products. Information related to procedures to be followed to acquire export documentation should also be collected.
- Producer information: Information in this case should include number of individual producers or producer organizations in different regions, including the types of commodities which they produce and the quantities

thereof. Contact details of major commodity producers should also be collected and stored.

- Economic information: This information should include export and import taxes, interest rates, exchange rates and any other information which may affect farming business.
- Sources of farm Inputs and equipment: The broker should have information on sources of farm inputs and equipment and prices of such materials, contact details of all suppliers and types of equipment which the suppliers stock.
- Transporter information: Information related to all relevant commodity transporters should be collected.

### *Sources of Information*

A broker must be resourceful to make sure that she gathers as much relevant information as possible. The broker should make sure that she gets the information timely so that it reaches the users timely as well. Information can be collected from a number of sources:

- The private sector. Large Commodity Processors who normally buy agricultural commodities can be a good source of information. These companies can provide information about the type, quantity and quality of commodities which they use and even the time they will need the commodities. Other private institutions include private schools, colleges and hospitals.

- Public sector. The public sector is also one of the major sources of information. In Malawi for example, The Government, through the Ministry of Agriculture has a well-defined market information system by which commodity price information is supplied to the general public for various parts of the country. They do this in news papers and radios. A broker can use the information to update her database.
- Print and electronic media: Newspaper, radios and television provide a lot of valuable information which a broker can use. Buyers advertise tenders for the supply of specific commodities and sellers likewise do advertise what they have for sale. A broker must be diligent in collecting, analyzing and storing this information for use in her office.
- Non Governmental Organizations (NGOs). Some of the NGOs work with farming groups in seed multiplication projects. Such NGOs do have information about the production quantities available in the farming groups involved.
- Internet. The internet is a gateway to a wide variety of valuable information for an agricultural commodity broker. The internet can provide information about the international commodity markets, quality and quantity specifications; sources of agricultural inputs
- Export promotion agencies. Most countries have export promotion agencies. These agencies do keep a lot of information about the available international markets for

exportable products. A broker can access such information for use in her brokerage

- Local and international agricultural trade fairs. Trade fairs, whether local or international provide an opportunity for a broker to interact directly with sellers and buyers. A broker can collect a lot of information for use in her brokerage.
- Individual farmers or groups. The farmers themselves can provide information about the nature of agricultural commodities which they have in stock.

### **People you need**

Human resource is one of the strategic resources in a brokerage. A brokerage must have personnel that are skilled enough to undertake various brokerage functions. The following are the key tasks that must be performed in a brokerage office:

- Organizing meetings between buyers and sellers
- Facilitation of negotiation between buyers and sellers
- Facilitation of contract writing
- Updating information database
- Collecting, analyzing and filing market and any other relevant information

- Maintaining books of accounts and financial administration
- Typing all correspondence between the brokerage office and the customers
- Office cleaning
- Preparation of bid forms

For a low cost brokerage establishment, one professional broker is adequate. The broker has to carry out all the activities listed above. She has to set up the office for the brokerage by making sure that an office building is either rented or built and all office equipment and furniture is available. She is then responsible for the overall management of the brokerage office. As a manager she has to organize and coordinate all brokerage activities and that all resources are used efficiently. She must have brokerage skills since she must take a lead in facilitating negotiations between commodity buyers and sellers. She must be resourceful and able to interpret market data, news and relevant reports for she has to help organize a well defined information database for the brokerage.

### **Things You Need**

Every business establishment has its own assets. The nature and number of assets depends on the activities of the business. A brokerage has its own relevant assets. The assets are divided into three groups as follows: Office Building; Office Equipment; Transportation;

### *Office Building*

A low cost brokerage can operate from rented buildings which may be available in town centers. If one has adequate financial resources to construct an office, one must make sure that the office is simply constructed, with adequate rooms for all members of staff and a separate room for meetings with clients.

Some brokers operate from their homes. They do so to avoid rental costs. One problem with this arrangement however is that the house may not be strategically located for business operations. Another problem associated with homestead operations is that professional activities can be confused with household activities, which can discourage customers. For example, clients can be put off when the broker has to attend children crying for her attention. It would mean that the client would not have adequate time to attend to her clients. A brokerage office must be located where clients can easily reach, and a signpost must be mounted to direct all customers who want brokerage services.

### *Office Furniture*

It is necessary to start with simple and inexpensive furniture. The furniture should however be enough to enable brokerage activities run smoothly. The following are some of the suggested pieces of furniture in a brokerage office:

- *File Cabinets:* This type of furniture is good for storage of information. A broker collects various types of information and this information must be stored systematically in files or folders. Each type of information may be stored in its

own file and the files can be labeled for ease of retrieval of such type of information when needed. One file cabinet is enough for the start for the business.

- *Book Shelves:* Good for storing information, such as information books (relevant to brokerage), magazines or files.
- *Office Desks and chairs:* For a low cost brokerage establishment, simple office desks and chairs that do not need a lot of money to buy are a desirable option. When buying such equipment for members of staff, visitors' chairs must also be included. A brokerage usually receives a lot of visitors who come to seek various kinds of information and brokerage services.

### *Communication and Information Equipment*

Telephones and fax: An ordinary telephone and a fax should be installed. Mobile phones are also necessary to allow the Brokers to be easily contactable even when they are out of office. Communication assures the customers that the broker is reliable and can serve them anytime.

Computer with auxiliary equipment: A brokerage operating in a modern environment may make good use of a computer. It will be used for typing, collection of data (internet), organizing of data, storing of data and general communication (email).

Typewriter: Should the broker operate in a setting that does not necessarily demand a computer, or has a very strained budget, a typewriter will have to do.

## **Transportation**

For a new brokerage, a motorcycle is appropriate facilitate mobility. A motor vehicle could be bought later when the business picks up.

## **Cash Requirements**

The value of all the recommended assets can differ from one country or region to another. It is however estimated that in a normal situation these assets should not be more than USD 2000 to USD 3000. This figure can be lower if the broker can buy from second hand sources. If the broker decides to construct her own office building of simple design, the total startup cost will increase but should not exceed USD 5000. The broker has to undertake a feasibility study to establish the appropriate investment level.

## **Farmers Organizations as Owners of the Brokerage**

The relationship between the brokerage and farmers' organizations is crucial, as it will determine the management style of the brokerage. If the brokerage is to operate on sound business principles it is recommended that the brokerage be legally separated from the owners –who in this case are the farmers organizations. Legal separation between the business and the owners ensures independence in the management of the business and thus gives the managers the space and flexibility to exercise their management skills for the good of the business without any intrusion by the owners.

To achieve this legal separation the business has to be registered as a limited liability company. In this type of business the owners' liabilities are limited to the investment they make in the business. The business owners (also known

as shareholders) are not obligated to deal with the company's debts or lawsuits because the business is expected to deal with its own problems. If the business is sued in the court of law it normally does not affect the shareholders.

In a limited liability company the shareholders are represented by the Board of Directors. These directors portray the interests of the shareholders and have to be freely elected by the farmers' organizations themselves. The Board of Directors has the following responsibilities:

- Generally accepted accounting principles are followed and that financial control is maintained.
- Legal obligation in terms of payment of taxes, social benefits and other fees are paid according to the law of the country.
- Hiring and firing of staff and other staff related issues.
- It is the responsibility of the board of directors to ensure that the organization complies with the brokerage Code of Conduct.
- The board must exercise leadership, enterprise, integrity and sound judgment in directing the enterprise so as to achieve continuing prosperity for the enterprise.
- The board should determine and implement the brokerage's purpose, values and strategy to achieve its purpose.

- The board should ensure that procedures and practices are in place that protect the brokerage's assets and reputation.
- The board should allow every director to play a full and constructive role in its affairs while ensuring that no one person or block of persons has unfettered powers.
- The board must identify key risk areas and key performance indicators of the brokerage in order for it to generate social-economic benefit so as to enhance stakeholder value in the long term. This should be conducted within the context of recognizing wider societal interests and other circumstances affecting the circumstances in which the organization fulfils its 'mandate' to operate.

For the board to carry out its functions efficiently and effectively:

- The board must meet regularly. How regularly or at what intervals the board meets is a matter for each board to decide, having regard to the enterprise's own circumstances. It is however recommended that a board should meet at least once a quarter.
- Individual directors on the board should devote sufficient time to their responsibilities.
- The board should regularly assess its performance and effectiveness as a whole and that of individual directors, including the employed broker.

## **Staffing, Job Descriptions and Required Skills**

Small scale brokers have to handle all the day-to-day operations of brokerages, performing a number of different jobs with a wide range of responsibilities. The job involves ensuring that their company's customers receive an adequate level of service or help with their questions and concerns. These customers may be individual farmers, their representatives or commodity buying companies, and the nature of their service needs can vary considerably. Such officers interact with customers to provide information in response to inquiries about products or services and to handle and resolve complaints. They communicate with customers through a variety of means; by telephone, e-mail, fax, regular mail correspondence, or in person. Some customer service representatives handle general questions and complaints, whereas others specialize in a particular area. The officer plans and schedules meetings and appointments; organize and maintain paper and electronic files. Brokers may contact customers, and inform them of any market changes. Some of these jobs are more clerical and require only a high school certificate for a small scale Brokerage. The amount of information generated by brokerages grows rapidly. It is necessary to classify, store, retrieve, and update this information. In many small offices additional responsibilities, such as entering data, performing word processing, sorting mail, and operating copying or fax machines, will also have to be handled by the only employee.

The broker should collect, analyze, interpret, type and file information and correspondence. She also has to do all office cleaning and preparation of bid and trading forms as well maintaining all books of accounts. She must also handle

general questions and complaints from clients. She has to plan and schedule meetings and appointments; organize and maintain paper and electronic files.

Incoming material should be examined and coded; numerically, alphabetically, or by subject matter, as appropriate. The paper forms, letters, receipts, or reports must be stored or entered into file cabinets and other storage devices. In order for records to be useful, they must be up to date and accurate. It is important that new information is added to files in a timely manner and that outdated file materials are discarded or transferred to inactive storage. Files should also be checked at regular intervals to make sure that all items are correctly sequenced and placed, as this minimizes the changes that material goes missing. As an organization's needs for information change, the filing system must be changed accordingly.

When records are requested, it is important that said information can be located, and that it is straightforward to determine whether it should be given to the person requesting it. This may be done manually or with the aid of information technology. If necessary, copies of records could be made and distributed. In addition, it is important to keep track of materials removed from the files, to ensure that borrowed files are returned.

The professional broker could be someone with a diploma or graduate with specialist agricultural marketing skills. However, the interpersonal skills, negotiation skills and reputation are incredibly important assets for a broker, and

someone with a combination of these characteristics and a strong business mind will be the perfect candidate, with or without academic background.

### *Salary and incentive system*

Small scale brokers are mostly one person businesses. The reasons for this are plenty, but there is no doubt that one of them is incentive structures. In most businesses the owners have rather good opportunities to monitor employees' performance, for example using inventory as a measuring rod. In a brokerage, however, this is far more difficult. An employed broker will often face situations where she closes deals worth large sums of money and charges a substantial commission, but the actual part of the sum charged that ends up in the broker's pockets is small. If a brokerage shall have any opportunity of becoming successful, this incentive problem must be dealt with in the most efficient way possible.

The most common solution is a bonus system, whereby the broker's salary is tied to the performance, combined with a large amount of "exclusivity", components we will deal with separately.

#### *1. Incentive salary*

In a brokerage, it is of uttermost importance that the broker is motivated to do business, and as much business as possible. In one person private company brokerage this is not a problem, as the owner of the company will get all the proceedings from the business, and therefore has an income that is directly dependent on the turnover. However, an employee does not necessarily have that reason to perform.

Should a broker have a fixed salary, she would not really have any reason to close any deals at all, or at least not many. It is therefore important that the employed broker has a salary that is related to the amount of business that is made. To make it attractive to be employed, this can be combined with a fixed part, resulting in a total wage that is part fixed, part profit dependent. The fixed wage should be low, pushing the broker to perform. The bonus should be calculated in a way that gives an expected total salary that is at least at par with what the broker could expect holding another position. There are however good reasons to apply some kind of 'exponential' bonus system, rewarding the broker higher and higher bonuses the higher the turnover is.

**Example:**

*If we assume that*

- A person competent to fit the position as broker could make 300 USD/month in another firm
- The "other costs" incurred average 300 USD/month
- We charge a 5% commission on trade
- The broker will get a 100 USD/month fixed salary

*The result must be that:*

We expect to trade, on average, more than 12,000 USD/month. This is derived by dividing the brokers expected salary plus other costs (600 USD) by the percentage of the turnover that is income for the brokerage (5%). Should we not manage to

trade this amount, the brokerage is not sustainable, as the broker would make more in another position. Now, of course we would also want to make some profit from the business, and we might have to pay taxes on that profit. Let's say that we, on average, expect to broker contracts worth 15,000 USD/month. It would then be sufficient to give the broker a bonus of 1.3% ( $200/15,000$ ) to make sure that she, on average, makes as much when employed by us as when holding another position. This would give us a gross profit of 150 USD ( $15,000 \times 0.05 - 100 - 200 - 300$ ). However, the element of insecurity attached to a bonus based system is often perceived as such a big potential "cost" to the employee that it is necessary to "overcompensate" to keep everybody happy. A bonus of 1.5% at the expected turnover would give the broker an expected salary of 325 USD, slightly higher than she would get somewhere else.

However, we would of course want the broker to be really eager to trade ever bigger volumes. This can (potentially) be achieved by employing a bonus system where the bonus level itself is tied to the turnover. In this example, the bonus 1.5%, which is what we would want to pay the average broker an average month, could be expressed as: "the broker gets a one percent commission for every 10,000 USD traded". Now assume that the broker manages to trade 30,000 USD. That would then mean that she gets a 3% bonus, amounting to 900 USD, plus the fixed salary 100 USD, totaling 1000 USD! Not bad. At the same time, such extreme performance gives us an income of 1,700 USD ( $30,000 \times 0.05 - 900 - 100 - 300$ ), which is even better! On a bad

month, the broker manages to trade only 5,000 USD, resulting in a meager 0.5% bonus, and a total salary of 125 USD, whereas we, as owners, make a loss...

The numbers in the example are fictive, and should not be used for anything other than describing the idea.

## *2. Exclusivity*

A brokerage of the kind we are discussing here makes use of several assets to operate profitably, whereof information and trust are the most prominent. A broker working in a company owned by farmers, through a farmers' organization, can supply both these essentials in a way that few other structures can. Hence, a broker would find it most challenging to manage to trade even a fraction of the same amount on her own. This must be emphasized and made very clear, not only at the outset of the venture, but repeatedly throughout operations. The broker must be constantly made aware that the position she has must not be abused, and that abuse would remove the very foundation she has for her business. It should also be stressed that the profit that the organization makes is by no means "unfair", even though the broker is the one concluding the deals. As the organizations' work is what creates the assets and the environment in which the brokerage operates, it is but a fair share of the profits.

One way of visualizing the exclusivity is investigating what "private" brokers make, and make comparisons with what

the employed broker makes. Such comparisons work well not only as motivators, but also serve the purpose of ensuring that the bonus levels are correct (not too low and also not too high) and to show shareholders (members) what their business is good for.



# Starting and Managing a Brokerage

## **Feasibility Study of a Brokerage**

A brokerage is a commercial entity. As a business, it must operate profitably for it to grow. A business feasibility study should be the first step towards the establishment of the business so as to see if the business idea makes sense. The process of investigating to see if a business can work, i.e. to see if it is feasible, is what is known as a Business Feasibility Study.

Functions of a feasibility study:

- It clearly displays the key elements of the business idea, so that one understands all the steps that are needed to bring it to life.
- It convinces other people (e.g. investors and/or financiers) to support the idea with their money and expertise.

A feasibility study has three major components:

- Market Research
- Technical Analysis
- Financial Analysis

### *Market research*

Market Research refers to the gathering, analysis, storage and retrieval of market information to aid in decision making. Market research is usually required to enable one to investigate market conditions. The following are the key questions, which should be answered in the marketing analysis:

- What is the current demand for your proposed brokerage services? That is, the type of consumers or customers that you are targeting with the product. You need to estimate the number of customers that you think will most likely use your services. For example, a broker must know the number of commodity buyers and sellers that have interest to deal with him.
- What competition exists in this market?
- Are there other brokers in the proposed business area? How many competitors are there?
- What is their estimated share of the market?
- What are their strengths and weaknesses of the competitors

- Who are their main customers?
- If other brokerages failed, why?
- What brokerage commissions and bidding fees will be acceptable to the clients?

### *Technical Analysis*

The technical requirements of the brokerage must also be thoroughly investigated. It is essential to plan ahead in order to make the best use of people, materials, machines and equipment for the proposed business. Technical planning helps one to:

- think ahead about the business to prevent problems arising during operation.
- avoid 'bottlenecks' in the process or running out of essential raw materials.
- know if the business will make profits in the future.
- get the necessary information for bank loans, suppliers' credits

The following is therefore a checklist of technical issues that should be looked into when carrying out a feasibility study:

- What sort of office design, furniture and equipment is needed in a brokerage? Where will such assets be sourced from and at what cost?

- Should office be rented or a new office should be constructed. In either case, at what cost?
- Is the proposed location of the business suitable in terms of accessibility by customers?
- Are services (fuel, water, electricity and telecommunication) available and affordable? What will it take to have these services connected?
- What caliber of staff (if needed) should be recruited? What skills are required for various operations? Check if these skills are locally available and at what cost.
- Legal issues like business registration, licensing requirements must also be investigated.

### *Financial Aspects*

Costs are incurred when starting and managing a business. The following questions are helpful when investigating financial requirements of the business:

- How much money is required to start the business?
- How much money should we borrow?
- Where can we get financial assistance?

If some money has to be borrowed from financial institutions, then the following issues must be investigated adequately:

- What is the loan for?
- How much do I actually need to borrow? Calculate the amount carefully; borrowing too much will cause higher repayments costs.
- Will I have to contribute something towards the loan? Lenders will often ask for at least 10% contribution from the borrower.
- What will be the interest rate that I will have to pay?
- How long will I have to repay the loan?
- Are there any other costs connected with the loan?
- Will I have to give some collateral?
- How much will I need to pay each month?
- Will I have to start repaying the loan straight away?
- Do I have a good business plan to back up my loan application?
- Will I earn enough money to pay the loan back?
- Which is the best place to borrow the money?
- Will I be expected to do anything else other than repaying the loan?

- What will happen if I do not repay the loan?
- Who can help me to answer all these questions?

When all the market aspects, technical issues and financial requirements of the brokerage have been investigated, one must now be able to answer the question, 'Is the brokerage idea making sense'? If the answer is yes, then one can proceed to prepare a business plan.

## **The Business Plan**

### *What is a Business Plan?*

A business plan is a document that serves as a guide that helps one to successfully start and run a business. Simply put, a business plan describes how business will be done.

As explained earlier, a feasibility study indicates that your business idea is sound. It assesses the potential of a business in terms of its required market, production technology and other technical aspects of the business, including finances. The business plan, however, continues the analysis at a deeper and more complex level, building on the foundation created by the feasibility study.

Advantages of a business plan:

- Essential when one needs a loan to get started. Most financial institutions demand that a business plan should be presented when one wants to get a business loan.
- Convinces other potential investors to invest in an enterprise. A broker for example, can use a business plan to

convince the other professional brokers that her business idea is sound so that they should invest with him.

- Helps one to successfully assess the strengths, weaknesses, opportunities and risks and the realistic steps that can be taken between your ideas and their realization.

You will find a suggested structure for a business plan at the end of this publication. Making use of it will pay off !

### *Fees and Commissions*

All businesses need a steady flow of income for them to grow. Income for a brokerage comes from commissions and bidding fees. Commission is usually charged as a percentage on the value of the transaction. There is no hard and fast rule on this; brokers may take a fee from either the seller or the buyer and in some cases both parties will pay the broker. Small scale brokers sometimes charge commissions as high as 10% to 15%. This is sometimes necessary when the broker has very high costs resulting from very low brokered amounts per deal, and corresponding high transaction costs. However, such high commissions are not in the farming community's best interest. A well functioning brokerage should be profitable at commissions between 1% and 2%, and this should definitely be the aim for a brokerage run by a farmer's organization.

Brokers also make money through bidding fees. A bidder (i.e. a seller or buyer who wants to sell or buy commodities through the broker respectively) is expected to pay some bidding fees for engaging the broker. Usually there are some

bidding forms (see example appended) which the client has to fill specifying their personal particulars and the quantity and quality of goods and the expected prices at which they can buy or sell the goods. Should one fill a number of forms for different commodities, they are expected to pay for all the forms separately.

The difference between the commission and the bidding fees is that the commission is only paid when a transaction is concluded, i.e. when goods have been bought while bidding fees are paid before the transaction takes place.

When a bid form is filled the broker has to start looking for a partner as soon as possible. A bid form is a form in which buyers and sellers of a particular commodity fill when they come to the brokerage office. The form has space where the seller or her representative indicates contact details, the commodity which is available, quantity, quality, packaging, unit price, total value of the commodity, validity period of offer delivery arrangements and payment terms. When a buyer fills in the form, she has to fill the same details regarding the commodities which she intends to buy. The bidding fee is paid as soon as the buyer or seller fills the form. It now remains with the broker to search for partners to the transaction.

The two parties are then brought together to negotiate for better terms with the broker facilitating the negotiations. The broker has to clarify issues if not understood very well. When the two parties finally agree on the deal, they both fill what is known as a trading form. A trading form is similar to the

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bid form, except that it has spaces for the two parties to fill together on the same form. All required details about the agree-upon commodity are indicated on the trading form (see appendix 2). Brokers may also bargain on behalf of the farmer if she is not able on her own but this is not encouraged. When the two parties agree, the broker follows the deliveries and payment to make sure agreed quantities are delivered and payment done as agreed. In most cases payment is made through the broker and the broker deducts her commissions in accordance with the agreed upon terms.



# Profitability Analysis under Different Scenarios

From the brokerage structure suggested (assets and required skills), profitability analysis has been done based on three different economic scenarios. The scenarios are based on the value of assets. A Profit and Loss Account for each scenario has been prepared to show the degree of profitability for the business.

## *Scenario One*

The setting is as follows: A group of 500 farmers have different types of commodities. The commodities include maize, rice, groundnuts and Soya beans.

Maize:	150,000kg
Rice:	85,000kg
Groundnuts:	100,000kg
Soya beans:	120,000kg

The farmers do not have a reliable market for the maize; as

such they are incurring a lot of storage costs each. They therefore decide to go and seek help from a broker who is located at their District's Headquarters. The name of the Broker is Commodities Brokers. The groups would like the broker to help identify good buyers who can buy the goods at competitive prices and in bulk. The broker then facilitates transactions between the group of farmers and commodity buying companies located in one of the cities.

The following are the assumptions to the Profitability Analysis:

- The agreed prices between the buyers and farmers are  
0.24 USD per kg for maize  
0.95 USD per kg for rice  
0.75 USD per kg for groundnuts  
0.25 USD per kg for soya beans
- Brokerage Commission is 10% of the value of the transaction
- Bidding fee for both buyers and sellers is 5.00 USD per bid
- The broker operates from rented offices and she pays 24.00 USD per month
- There are 100 deals made, i.e. 25 deals per commodity.
- The transporter charges 100 USD per metric ton and the broker gets a 10% commission

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- The broker has no loans to service
- Broker's salary is 100 USD/month fixed, plus a 15% bonus on total commissions.

### *A. Profit and Loss Account for Commodities Brokers as at end of year 2005.*

<b>Gross Revenues</b>	<b>USD</b>
<b>I</b> Brokerage Commission for maize (10% of value of goods)	3,600
Brokerage Commission for rice (10% of value of goods)	8,075
Brokerage Commission for groundnuts (10% of value of goods)	7,500
Brokerage Commission for soya beans (10% of value of goods)	3,000
Total Commission from Commodity Brokerage	22,175
Total Commission from transport deal	4,500
<b>II</b> Bidding Fees (100 deals, each with two parties, at 5 USD each)	1000
Total Revenues	27,675
<b>III</b> Direct Costs	5,500
Gross Profit	22,175

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IV Administrative Costs	
Salaries	5,200
V Rentals	288
Utilities	150
Vehicle Running Costs (motorcycle)	176
Total administrative Costs	5,814
Operational Profit (profit before Depreciation and Interest)	16,361
Depreciation	250
Interest	0
Profit before Tax	16,111
Tax (30%)	4,833
Net Profit	11,278
Net Profit margin (%)	41%
Return on Investment (ROI) ([net profit]/[total costs])	100%

**I:** The figure is computed by multiplying the unit selling price of 0.24 USD by the total tonnage of 50,000 kg.

**II:** The figure is computed by multiplying the bidding fee of 5 USD by 200 transactions. There are four crops, thus 100 transactions for sellers and 100 transactions for buyers

**III:** Direct cost include all costs directly connected to

particular transactions, such as stationery, communication, wage labour etc

IV: Administrative costs include transportation costs, rentals, salaries, utilities for one year etc.

V: This is computed by multiplying the monthly rental of 24USD by 12 to get the annual rental cost

*Scenario Two*

Setting: The 1500 farmers in a rural district have several commodities, including maize, rice, groundnuts and soya beans, for sale.

Maize:	300,000kg
Rice:	170,000kg
Groundnuts:	200,000kg
Soya beans:	240,000kg

The farmers do not have a reliable market for the maize; as such they are incurring a lot of storage costs each. They therefore decide to go and seek help from a broker who is located at their District’s Headquarters. The name of the Broker is Commodities Brokers. The groups would like the broker to help identify good buyers who can buy the goods at competitive prices and in bulk. The broker then facilitates transactions between the group of farmers and commodity buying companies located in one of the cities.

The following are the assumptions to the Profitability Analysis:

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- The agreed prices between the buyers and farmers are  
0.20 USD per kg for maize  
0.90 USD per kg for rice  
0.60 USD per kg for groundnuts  
0.20 USD per kg for soya beans.
- Brokerage Commission is 5% of the value of the transaction
- Bidding fee for both buyers and sellers is 5.00 USD per bid
- There are 100 deals made, i.e. 25 deals per commodity.
- The transporter charges 100 USD per metric ton and the broker gets a 10% commission
- The broker operates from own new offices and that she borrowed money (1,200 USD) for building her office from a financial institution at 30% interest rate. There are no rentals because the business is running from own offices.
- Broker's salary is 100 USD/month fixed, plus a 15% bonus on total commissions

*Profit and Loss Account for Commodities Brokers as at end of year 2005.*

<b>Gross Revenues</b>	<b>USD</b>
I Brokerage Commission for maize (5% of value of goods)	3,000
Brokerage Commission for rice	

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(5% of value of goods)	7,650
Brokerage Commission for groundnuts (5% of value of goods)	6,000
Brokerage Commission for soya beans (5% of value of goods)	2,400
Total Commission from Commodity Brokerage	19,050
Total Commission from transport deal	4,500
<b>II Bidding Fees (200 deals at 5 USD each)</b>	1000
Total Revenues	24,550
<b>III Direct Costs</b>	5,500
Gross Profit	19,050
Administrative Costs	
<b>V Salaries</b>	4,732
Rentals	0
Utilities	150
Vehicle Running Costs (motorcycle)	176
Total administrative Costs	5,058
Operational Profit (profit before Depreciation and Interest)	13,992
Depreciation	250
Interest	315
Profit before Tax	13,427
Tax (30%)	4,028

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Net Profit	9,399
Net Profit margin (%)	38%
Return on Investment (ROI) ([net profit]/[total costs])	89%

**I:** The figure is computed by multiplying the unit selling price of by the tonnage.

**II:** The figure is computed by multiplying the bidding fee of 5 USD by 200 transactions. There are four crops, thus 100 transactions for sellers and 100 transactions for buyers

**III:** Direct cost include all costs directly connected to particular transactions, such as stationery, communication, wage lab our etc

**V:** This is computed by multiplying the total commission by the bonus rate and adding that to the fixed salary  $((19,050+4500) \times 0.15 + 12 \times 100)$

### *Scenario Three*

Setting: The 4000 farmers in a rural district have several commodities, including maize, rice, groundnuts and soya-beans, for sale.

Maize:	250,000kg
Groundnuts:	250,000kg
Soya beans:	1,000,000kg

The farmers do not have a reliable market for the maize; as such they are incurring a lot of storage costs each. They

therefore decide to go and seek help from a broker who is located at their District's Headquarters. The name of the Broker is Commodities Brokers. The groups would like the broker to help identify good buyers who can buy the goods at competitive prices and in bulk. The broker then facilitates transactions between the group of farmers and commodity buying companies located in one of the cities.

The following are the assumptions to the Profitability Analysis:

- The agreed prices between the buyers and farmers are  
0.25 USD per kg for maize  
0.70 USD per kg for Groundnuts  
0.30 USD per kg for Soya beans.
- Brokerage Commission is 2% of the value of the transaction
- Bidding fee for both buyers and sellers is 5.00 USD per bid
- There are 25 deals made per commodity
- The transporter charges 100 USD per metric ton and the broker gets a 7% commission
- The broker operates from own new offices and that she borrowed money (1,200 USD) for building her office from a financial institution at 30% interest rate. There are no rentals because the business is running from own offices.

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- She borrowed money (2,000 USD) for buying a second hand Vehicle (One Ton Pick-Up) from a financial institution at 30% interest rate.
- Broker's salary is 100 USD/month fixed, plus a 15% bonus on total commissions.

### *Profit and Loss Account for Commodities Brokers as at end of year*

<b>Gross Revenues</b>	<b>USD</b>
Brokerage Commission for maize (2% of value of goods)	1,250
Brokerage Commission for groundnuts (2% of value of goods)	3,500
Brokerage Commission for soya beans (2% of value of goods)	6,000
Total Commission from Commodity Brokerage	10,750
Total Commission from transport deal	2,000
Bidding Fees (75 deals at 5 USD each x 2)	750
Total Revenues	13,500
Direct Costs	5,500
Gross Profit	8,000
Administrative Costs	
Salaries	3,113
Rentals	0

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Utilities	150
Vehicle Running Costs (Pickup)	750
Total administrative Costs	4,013
Operational Profit (profit before Depreciation and Interest)	3,987
Depreciation	656
Interest	840
Profit before Tax	2,491
Tax (30%)	747
Net Profit	1,744
Net Profit margin (%)	13%
Return on Investment (ROI) ([net profit]/[total costs])	18%



# Case studies

## **Case Study of brokerage, from Market Information Gathering to Sale of Commodities**

Chiwere Association has produced 100 ton of CG7 groundnuts and is looking for a market for the commodity. Previously, private traders used to come to their area to buy groundnuts but at as low as MK35 (0.28 USD) per kg. At that price farmers were not making any profit. They were selling to the private traders out of desperation.

One of the farmers gets informed that the traders actually resell the groundnuts to some large commodity processing companies in the cities at as high as MK100 (0.8 USD) per kg. Frustration among the farmers grows as they realize that the private traders are grossly exploiting them. The farmers then collectively decide not to sell to any private traders. The problem however is that they do not have adequate information about the large companies in the information in terms of the ground nut quantities they can buy, when, of what varieties and how the commodity can be transported to the cities.

If the farmers have to hire transportation to deliver the groundnuts to the cities, they have to be prepared to pay a substantial amount of money. The only transporter they know charges exorbitantly for short distances – How much

more with a distance of 250 km to Lilongwe City? The farmers therefore realize that they have several major challenges: they need money to send their representatives to the cities to identify the potential buyers, negotiate for better terms and hire transportation for the delivery of the commodities. They also know that such negotiations will not take one day, but several days and that means more money is required. Besides, they do not seem to have good negotiators who can ably influence the experienced commercial managers for the large commodity buying companies.

The farmers then hear that a commodity broker, located in a nearby town has managed to help other associations find a good market. They also learn that the broker has a list of companies that can bring their own trucks to carry the commodities – so the farmers will not have to incur too much transportation costs. Each farmer will simply have to carry the commodity to a central place from where the buyer will collect the commodity. The farmers further learn that the broker charges brokerage fees and commission for her services. They however decide to engage the broker to link them to a competitive buyer.

The farmers' representative fills a brokerage form, detailing the name of the association, contact details, the type of commodity available, quantity and their expected selling price (0.95 USD per kg) for the groundnuts. They then pay USD 4.00 as bidding fees. The broker then contacts potential buyers and she selects one who indicates the willingness to buy all the groundnuts and will collect the commodities

herself. A meeting is then set where the farmers representative, the broker and the buyer meet to discuss the terms of the transaction. The farmers' representative brings with him a sample of the groundnuts available for the buyer to examine.

Negotiation for the transaction begins. The buyer indicates that she can only buy at 0.50 USD per kg) while the farmers stick to the bidding price. The broker then comes in to facilitate the negotiations until both parties settle at 0.75 USD kg per kg. The buyer is happy and so are the farmers. This is much better than US\$0.28 per kg offered by the private traders. Besides, they will not have to incur significant transportation costs. It is a good deal!! The parties then sign a contract where each party commits themselves to the agreed terms of the transaction. The terms include the price, the required quality, date when all groundnuts will be available at one central point and the payment terms. Payment will be done through the broker. The broker will get her commission at 10% of the total value of the groundnuts.

### **A typical brokerage's operations over a year**

A commodity broker must plan her activities thoroughly. Activities for a commodity brokerage span across the whole year. The following is a case study for a brokerage, managed by Ms. Samuel.

Ms. Samuel is operating a brokerage situated at the district headquarters. She has been in the business for five years now. She deals with both inputs and outputs in her business. She does business with individual farmers and buyers as

well as organizations. Most farmers market their products through her business because they are able to make profits other than through traders.

The brokerage is located in an area where harvesting of crops starts in the month of April. The brokerage has its financial year starting from January to December every year. As the business financial year is closing in December, Ms. Samuel also has to plan for the next financial year. She has produced a cash flow budget for the next year so that she can plan in advance the allocation of money to all envisaged activities.

In January most of the crops are still in the field and harvesting will commence in April. Ms. Samuel goes around the district between January and April, visiting farmers and farmers' organizations to estimate production quantities for various crops in order to get prepared. She then records all the information in her files.

She also contacts all the prospective buyers, mainly the major agribusiness processors in the cities and town, including some public institutions such as universities, hospitals and schools. These institutions buy food commodities in bulk every year. The broker collects valuable information from these institutions such as the types of commodities required, quantities, quality requirements, expected time of delivery, mode of transportation and expected buying prices.

Having done that, she then contacts various transporters

who have been doing business with her for sometime. She gets their transport costs to various destinations. She updates the list removing those who are out of the business and includes those who have joined the transportation business. All the information from the potential buyers and transporters is properly and systematically recorded and stored in her office.

During and after harvesting time, she visits farmers again to make sure that the commodities wanted by the buyers are available and enough quantities to meet the demand. Where in one area quantities do not meet the demand, she goes to another area to make sure the quantities add up to the required. She convinces the farmers not to sell to traders because there is a market already identified. She also finds out what prices they want to sell at.

In May, she is in constant touch with all players (buyers and sellers) to get an update of activities. In June, buyers start inquiring about the availability of commodities they want to buy. She advises them to visit her office to fill the bid form so that she can link them with the sellers. Ms. Samuel then facilitates all transactions between the farmers and the buyers. She charges 15% of the value of each transaction and 5 USD for each bid from filled.

As harvesting is going on, farmers are also busy with winter cropping. Their commodities will be ready for sale in four months time, meaning that she starts looking for a market for the winter crops in August. At the same time the farmers need agricultural inputs for the winter cropping. She collects

information on types and quantities of inputs demanded by the farmers and then goes to negotiate with input suppliers for better prices. The broker links the two parties and she gets her commission by charging 10% on the price of each bag of input delivered. The farmers realize that the input prices are far much lower than the normal market prices since they are buying at wholesale prices. Though they have to pay the commission, the farmers discover that the total cost is still lower than what they could have incurred without the brokerage.

She arranges with a reliable transporter to deliver the fertilizers to the farmers, on which she charges the transporter 10% commission on the value of the transaction.

As September approaches, the new rainy season is already approaching and producers are looking for more inputs (fertilizer and seed). She has a database of input suppliers but also goes around checking availability and prices, which she communicates to the farmers and advises them on where they can purchase at reasonable prices. She contacts organizations which buy seed and links them to producers with good quality seed at reasonable prices as well.

In December, the brokerage office should now consider summarizing all the financial transactions from the whole year to determine the profitability of the year. An auditor should be hired to audit the books of accounts. Planning for the next growing season should also start.

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## Appendix 1: BID FORM / CONTRACT OF AGENCY

Date: \_\_\_\_\_ Time: \_\_\_\_\_

Firm Name: \_\_\_\_\_

Contact Person: \_\_\_\_\_

P.O. Box: \_\_\_\_\_

Street & Building: \_\_\_\_\_

City/Town: \_\_\_\_\_

Telephone: \_\_\_\_\_

Fax: \_\_\_\_\_

E-mail: \_\_\_\_\_

Country: \_\_\_\_\_

To Buy or Sell<sup>3</sup>: \_\_\_\_\_

Commodity: \_\_\_\_\_

Quantity: \_\_\_\_\_

Price Asking / Expecting<sup>4</sup>: \_\_\_\_\_

Where is the Commodity Available: \_\_\_\_\_

Specify Grade: \_\_\_\_\_

Other Details: \_\_\_\_\_

This contract shall be valid until such time as terminated in writing, or a deal is accordingly concluded.

Name and signature of broker \_\_\_\_\_

Name and signature of bidder \_\_\_\_\_

<sup>3</sup> A buyer indicates 'to buy' and a seller indicates 'to sell'

<sup>4</sup> A buyer indicates her asking price and a seller indicates her expected price

**Appendix 2: Example of Trade Form**

ITEM	SELLER	BUYER
Company / organization		
Name of Representative		
Signature of Representative		
Post Office Box		
Physical Address		
Phone		
Fax		
Email		
<b>Commodity</b>		
Name		
Quantity		
Quality		
Packaging		
Unit Price		
Total Value		
Validity		
Delivery		
Payment		
Other Items		
Stamp and Signature		

## **Appendix 3: Business plan format**

### **(I) Executive Summary**

Short description of your business.

Explain what your business is all about.

It must capture their interest and convince them that you can really successfully run the business.

### **(II) Background**

Business Location: Explain the location of your business and why it is located there.

### **(III) Specifics of the business**

Explain your experience in that type of business

Demonstrate that you have all the facts clearly established.

This includes the possible problems that may be encountered and how you will solve them.

Do not forget the basics – your name, ownership details, management of the company and proposed start up date.

### **(IV) Outline of the business operations**

Explain the production process; describe the product, its packaging, storage and distribution.

Explain the expected volume of production.

Compile a list of machines and other equipment, their sources and why you have chosen such type of equipment.

Include details of sources of your raw materials.

### **(V) Information about staff plus staff plan**

Explain legal status of the business- whether sole proprietorship, partnership or a limited liability company.

If staff is to be employed, indicate the anticipated jobs and the person profiles of people suitable.

Describe staffing /management structure

Include an outline of pay rates, bonuses and other incentives. You may also need to explain how these benefits compare with those of the competitors.

Plans for staff training must also be indicated.

### **(VI) Marketing Plan**

This is a very important section of a business plan and it should include the results of market studies that you have done.

Describe the product or service in terms of its specific benefits; ability to meet customers needs and its advantages over products from competitors.

Explain what you have found out about the status of the market, i.e. describe the expected customers, their needs and expectations (especially of quality and price) that they are willing to accept. How big is your market?

Nature and extent of competition? List each competitor and her price, strengths and weaknesses.

Estimate the total market size and value and the market share you expect to capture within a specified time period.

Indicate the expected price(s) of your product(s).

Advantages of your product over the competitors

Proposed method of sales, after sale product guarantees and advertising and promotional activities.

### **(VII) Costs**

Start up costs must be clearly indicated. All items that will be required must be listed including their costs. Determine the total cost of the business.

Then list the details of the expected variable production costs at the scale of production that is required to meet the anticipated market share. Such costs include:

Raw materials e.g feed, chemicals, breeding animals in dairy farming

Veterinary drugs

Direct labor, e.g. wages for milkers

List and calculate the operating costs, such as:

Utility bills

Rentals

Staff costs

Repairs and maintenance

### **(VIII) Sources of finance**

Finance can come from savings, gifts, loans and the income generated from the business.

### **(IX) Calculate your expected monthly income (revenues)**

### **(X) Risk analysis**

Business risk refers to any unforeseen occurrence that could badly affect our business. For example, cattle theft (a dairy farmer could lose all his/her dairy animals through theft). She may have to insure her animals against theft.

List the key risks that will affect the plan, along with an explanation of how the organization intends to deal with these risks. In relation to financial risks, show how the financial projections will be affected according to the different risks that are described.

## BROKERAGE





The Swedish Cooperative Centre (SCC) has a long history of supporting farmers' organizations around the world. We take pride in partnering with organizations representative of the farming societies, providing important services to what is often a majority of the population.

This material is one in a series of SCC publications aiming at contributing to enabling farmers and their organizations to engage more effectively in marketing activities. It focuses on providing a practical guide to how a small scale brokerage can be set up, explaining what signifies a broker and how a small scale broker operates.

*Lennart Hjalmarson*

CEO Swedish Cooperative Centre



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