

**MARKET RESEARCH  
for agroprocessors**



For further copies of this publication  
and for information on FAO's activities  
related to agricultural marketing  
please contact:

Agricultural Marketing Group  
Agricultural Support Systems Division  
Food and Agriculture Organization of the United Nations  
Viale delle Terme di Caracalla  
00100 Rome, Italy

FAX: (39) 0657056850

E-mail: [AGS-Registry@fao.org](mailto:AGS-Registry@fao.org)

Web Site: <http://www.fao.org/ag/ags/agsm/marketin.htm>

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3

Marketing Extension Guide

# MARKET RESEARCH for agroprocessors

by  
Andrew W. Shepherd

Agricultural Support Systems Division

FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS  
Rome 2003

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# Preface

Before any agroprocessing venture is started, or before an existing venture decides to expand its product line, an understanding of the market for the planned products is essential. Companies and individual processors need to feel confident that people will accept and want to buy their products. They need to be sure that they can sell what they produce at prices that give them a good profit. They need to have a realistic idea of the quantities they can sell and be sure that the facilities they build and the equipment they buy are suitable for those quantities, being neither far too large nor too small. They need to know where they can sell their products and how best to distribute them to consumers. Last, but not least, they need to be certain that the raw materials, other ingredients and packaging they require will be available when needed, at a price that permits profitable processing and marketing.

This guide describes, in fairly simple terms, the market research that agroprocessors can carry out, and some of the ways of doing such research. Market research can never guarantee success but it can certainly increase the likelihood that the new business will turn out to be profitable. It can identify at an early stage those processing ideas that are unlikely to lead to profitable operations.

The guide is addressed to entrepreneurs and companies who are planning to develop or expand medium-sized agroprocessing businesses. It is also intended to be used by banks who need to understand the potential market before lending for agroprocessing; by consulting firms and individuals offering market research services in developing countries and by government agencies and policy-makers interested in developing the agroprocessing sector. Extension workers and non-governmental organizations (NGOs) who are supporting individuals and groups planning to set up small rural processing ventures could also use parts of this guide.

# Contents

Preface .....	iii
Acknowledgements .....	vii
1 Why do we need market research? .....	1
2 How much can be sold, where and when? .....	13
3 Researching consumer attitudes to your products .....	27
4 How can your product be made attractive to consumers? .....	43
5 How should your product be distributed? .....	57
6 How should you promote your product? .....	71
7 Are your agroprocessing plans feasible? .....	79
8 Will your business be profitable, and at what prices? .....	91
Annex 1 – Questions for market research .....	107
Annex 2 – A consumer questionnaire .....	111
Further reading .....	113

# Figures

1	Estimating totals consumed .....	21
2	Example of a tasting survey form .....	39
3	Example of a price survey form .....	47
4	Margins and mark-ups .....	67
5	Simple profit and loss account calculation .....	95
6	Cash flow analysis .....	98

# Boxes

1	Types of processed agricultural products .....	5
2	Product, price, place and promotion .....	6
3	The business-planning sequence .....	9

# Acknowledgements

Working under FAO's Volunteer Programme, Martin Hilmi provided invaluable assistance by reviewing existing literature on this topic and proposing a detailed outline for the guide. Stephen F. Jones was kind enough to search out his unpublished 1983 dissertation on Marketing Research for the Agricultural and Food Sectors in Developing Countries, which proved very helpful, as did an unpublished Business Plan for Small-Scale Agro-Industries by Morton Satin. Much use was made of several of the books listed in the Annex on "Further reading." Particular appreciation is due to the various publications on food processing by Peter Fellows and to Ian Crawford's work for FAO on Marketing Research and Information Systems (FAO Marketing and Agribusiness Text No. 4).

Messrs Fellows, Hilmi and Jones all provided valuable comments on an early draft of this guide, as did Roberto Cuevas-García, John Dixon, Michael Griffin, Miranda Jabati, Yoram Levtov, Alexandra Röttger, Edward Seidler and Pieter Ypma. Francesca Cabré Aguilar patiently revised numerous drafts. Tom Laughlin conceived the Marketing Extension Guide series and was responsible for the design of this guide. Last, but not least, many thanks to "Yuss" for the cartoons.



# **1 Why do we need market research?**

*Main points in Chapter 1*  
**Why do we need market research?**

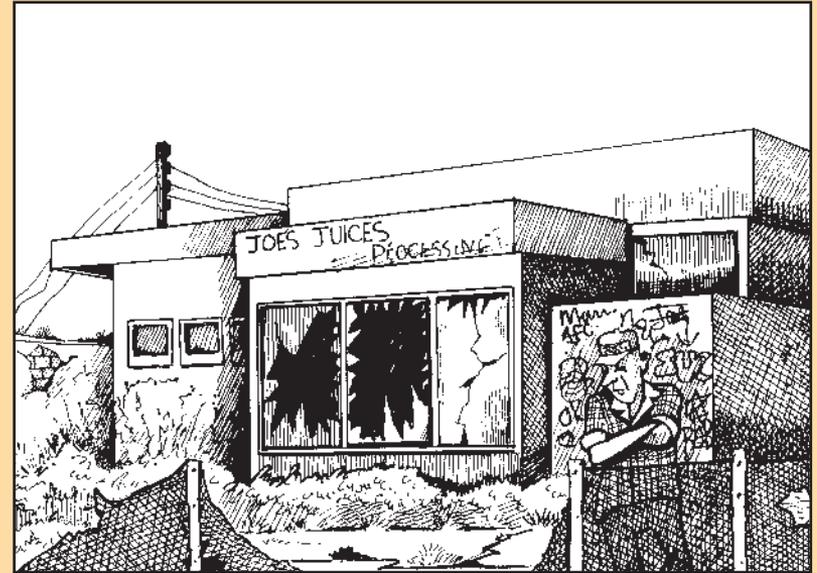
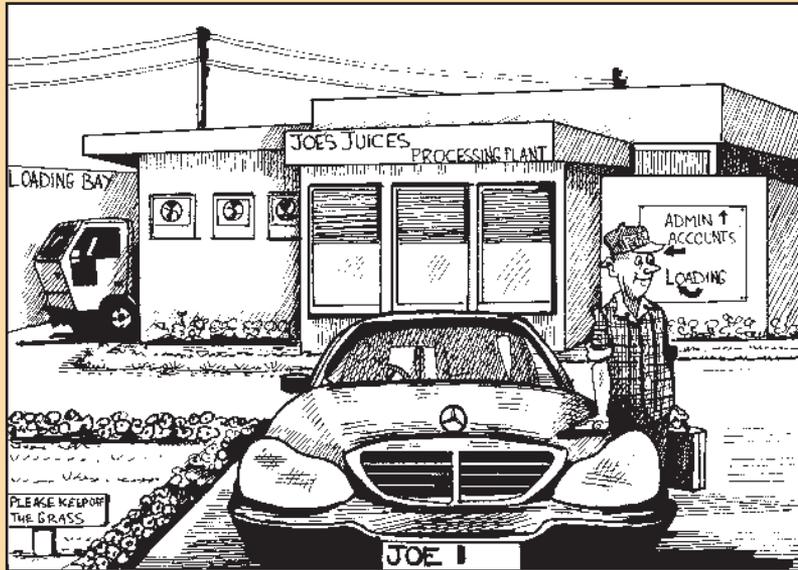
*Agroprocessing ventures are often unsuccessful.  
Lack of market research can be one reason for this.  
The chapter looks at what is meant by “market”  
and what is market research.*

*Agroprocessors need market research to ...*

- *identify the right opportunities for processing;*
- *be confident they can cover their costs;*
- *be confident they can sell their products  
at a profitable price;*
- *make sure that consumers will accept  
the product and the packaging;*
- *identify potential problems.*

*The chapter concludes  
with brief summaries of Chapters 2 – 8.*

*Market research  
can sometimes make the difference  
between this ...*



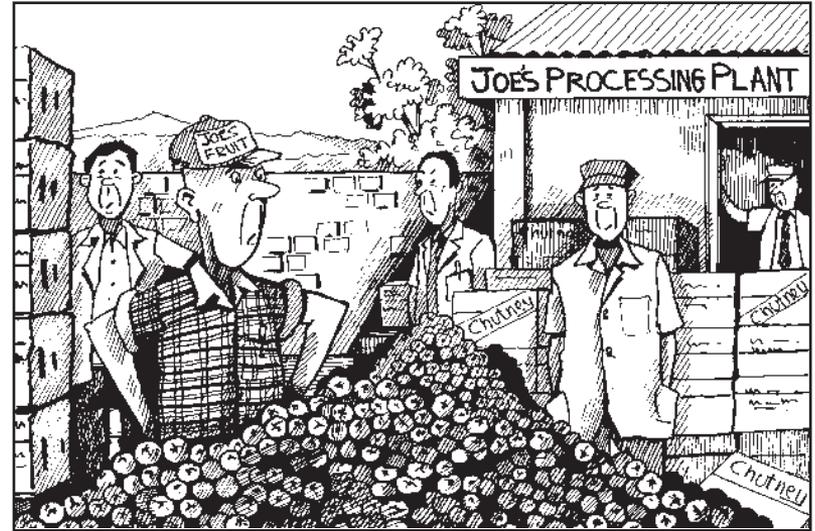
*... and this!*

*Processing must be based on market demand ...  
... not just on the availability of raw materials.*

## INTRODUCTION

Why is it that agroprocessing ventures are often unsuccessful? Processing developments often fail to take into account the simple fact that the processed product has to be sold. Activities are started because they are technically possible, because they are “in fashion” in other countries and, perhaps, because there are abundant raw materials. The fact that people have to buy the finished product and that ways of selling and distributing it have to be developed often receives only limited attention. The result can be a shiny new factory, which loses money because it cannot sell enough of the processed product. Such “white elephants”<sup>1</sup> are to be found in every country.

Individual entrepreneurs (businessmen or women) or private companies are perhaps less likely to make such a mistake because they are investing their own money in the processing facility. More likely to fail are facilities established by groups or cooperatives, with the support of outside bodies such as government departments, NGOs or donors. The private sector usually begins with the question: “can we make money by making this product and, if so, how much?” An important way of finding out



the answer is to do market research. Outside bodies, on the other hand, frequently start with the question: “what can we do to help people in this area?” Such a question rarely leads to a detailed investigation of the market.

Market research is essential before beginning any venture of this type. Without market research there is a risk that consumers do not need or want the product, or do not like it or the way it is packaged and presented. There is a danger that retailers do not want to sell the product. There is the possibility that the price the processor wants to charge is too high for consumers to afford.

<sup>1</sup> White elephants were considered to be sacred. The Kings of Siam (Thailand) used to reward opponents with white elephants which, as it was not permitted to put them to work, were extremely expensive to keep.

Research is also required to ensure that the agroprocessing can be carried out efficiently and, hence, profitably. Are raw materials available when required and at an affordable price? Are other ingredients and packaging materials easily available? Will problems be experienced with constructing and equipping the factory?

Any one of these and many other potential problems is enough to result in the failure of an agroprocessor. The

purpose of this guide is therefore to help entrepreneurs, companies, cooperatives, NGOs and others to better understand the market for the products they plan to produce. In this way it is hoped that agroprocessing will become more profitable. Researching export markets is not considered here. Companies should usually have a solid foundation on the domestic market before thinking about exporting. It must also be stressed that market research is not a “one off” activity to be done at the planning stage.

### *Box 1*

#### **Types of processed agricultural products**

##### **DAIRY AND ANIMAL PRODUCTS**

milk, sour milk, cheeses, yoghurt, butter,  
ghee or samn (clarified butter), ice cream,  
sausages, dried meat,  
eggs, smoked meat and fish

##### **FRUIT PRODUCTS**

carbonated drinks, juices, cordials, jams, jellies,  
sun or solar-dried fruit,  
fruit pulps, fruit leathers, ice lollipops,  
fried banana chips, chutneys, candied or glacé fruit  
bottled or canned fruits

##### **VEGETABLE PRODUCTS**

chutneys, pickles, snack foods, tomato paste, garlic  
paste, tomato ketchup (catsup) and other sauces  
canned or bottled vegetables

##### **GRAIN PRODUCTS**

bread (including from special flours such as  
millet or sorghum), meals and weaning foods,  
biscuits, cakes, puffed grains (e.g. popcorn), pasta

##### **ROOT CROP AND TUBER PRODUCTS**

crisps or chips made from potatoes,  
cassava, taro, etc.

##### **MISCELLANEOUS PRODUCTS**

wine (e.g. palm wine), toddy,  
sugars (e.g. gur in India), candies, honey,  
dried herbs and spices,  
cooking oils from nuts or oilseeds, tea,  
peanut butter, tree syrups, dried nuts  
and other nut products,  
fermented sauces (fish, soya), soya milk

Agroprocessors should monitor their markets as an ongoing activity. Market conditions can change overnight and processors need to be aware of such changes.

The emphasis of this guide is on research that processors can carry out themselves. However, many countries have specialist market research consultants and companies. Companies or organizations planning large processing investments would be well-advised to use such specialists. This guide can then be used to help processors identify the type of research they require.<sup>2</sup>

### **What is a market?**

For the purposes of this guide a “market” is firstly defined as the characteristics of consumers’ demand (i.e. what they want) for a product. This definition also includes the requirements of those involved in supplying that consumer demand, such as retail shops and their wholesalers. Secondly, the term “market” also embraces the actions of competitors, such as how they set their prices, organize their distribution and decide on promotion. Understanding competitors is just as important as understanding consumers.

One of the most important aspects of demand is clearly the quantity of a product that consumers want to buy. But when we talk about demand and the “market” we consider many other factors, such as those outlined in Box 2.

<sup>2</sup> see Fellows, P.J. and Axtell, B. (eds) pages 64-68 for a discussion of the benefits of doing research oneself or hiring outside consultants.

### *Box 2*

#### **Product, price, place and promotion**

##### **PRODUCT**

the taste and other attributes of the product that consumers prefer;  
the quantities, packaging and sizes consumers buy;  
the appearance, including labels;  
the brand name

##### **PRICE**

competitors’ wholesale and retail prices;  
competitors’ price response to a new product;  
price variations according to location and type of consumer;  
methods of setting prices

##### **PLACE**

where and how to sell the product;  
advantages of different types of distributor;  
how distributors can be supplied;  
distributors’ requirements in terms of quantity, delivery and price; the costs involved in the various distribution options

##### **PROMOTION**

the advertising required;  
other promotional tools that are used, such as free samples;  
costs involved with various types of promotion

A “market” as discussed in this book is, as noted above, a set of characteristics of demand and supply, not a physical location. For small ventures such a “market” can be local, for larger ones, national. To avoid confusion, when we are talking about physical market locations we will refer to “marketplace” or “wholesale” and “retail” markets.

### **What is market research?**

Market research is the process of investigating a market in order to find out the sales prospects for a product and how to achieve success with it. Put another way, it is the set of activities necessary to obtain the information required about the market that we have listed above. At the simplest level such research may just involve talking to people in the same village to find out what they want to buy and what they can afford to buy. At the most complex level large organizations may carry out person-to-person or telephone interviews with thousands of potential consumers. However, both activities have the same aim: to make sure that a product can be sold and that it can be sold profitably. Market research activities that will be considered in this guide include:

- consumer questionnaires;
- tasting tests, to see if people accept the product, or which tastes they prefer;
- interviews with retailers and wholesalers.

### **Why do agroprocessors need market research?**

Processing facilities can be costly to establish. Individual entrepreneurs may put all of their life savings into setting up a small factory. Banks may lend large sums of money to new ventures, or to existing ventures to enable them to expand their operations. Governments, donors or NGOs may similarly lend or give grants of large amounts. With so much at stake, no one wants the processor to fail.

Yet, as we have noted, rural processing ventures frequently do fail. Why? Some of the reasons can be:

- failure to identify the right processing opportunities;
- high fixed costs;
- high selling price or, alternatively, the low selling price of competitors;
- product and packaging quality;
- failure to identify potential problems.

***Failure to identify the right opportunities for processing.*** As noted at the beginning of this chapter, processing activities are often started because there are plenty of raw materials. They are rarely started because of detailed market research that has identified particular opportunities. This could lead to a company failing to identify the most profitable products it could produce. For example, it may decide to process pineapple juice because pineapples are abundant, and fail to notice that orange juice processing could be much more profitable.

**High fixed costs.** As discussed in more detail in Chapter 8, a factory needs to achieve a certain minimum throughput in order to make products at a price consumers can afford. Processing facilities have a number of *fixed costs and overheads*, such as the cost of the building and the cost of the processing equipment. The more products that are produced, the lower the fixed cost per unit. On the other hand, the *variable costs*, such as the cost of the raw materials, increase in proportion to how much is processed. The profitability of a factory depends on its ability to minimize the fixed costs per unit produced. When production is significantly less than the capacity of the factory then fixed costs per unit will rise to unacceptable levels and the factory will have to close down. Two reasons why fixed costs per unit may be too high are:

- demand for the product is much less than the capacity of the factory. If good market research is done from the beginning it should be possible to plan the processing venture so that its size matches the likely demand;
- supply of raw material of the right quality and price is much less than the possible throughput of the factory. If, for instance, crop production is seasonal and lasts for three months, what will the factory do for the rest of the year? Initial research of processing feasibility doesn't just involve studying the market for the product: it also involves making sure that there will be enough raw material to keep the factory operating at close to capacity.

**High selling price.** Large factories, if they are efficient, can benefit from “economies of scale”. This means that by producing big quantities they can share their fixed costs over a large number of products. Larger factories can often buy sophisticated processing equipment that can make the product at a lower unit price than can the equipment that small businesses can afford. The result of these economies of scale is that larger companies can frequently sell their products for much less than can small processors.

The price at which an agroprocessor will be able to sell the product and make a profit has to be known before the investment in the factory is made. In too many cases in the past, agroprocessing companies have expected too high a return, setting their prices more on the basis of wishful thinking or guesswork than on a serious analysis of the market.

**Product and packaging quality.** The agroprocessor may find that its products are not liked by consumers, particularly when compared with other brands of the same product that can be purchased in local shops. There could be many reasons for this: the available raw material (e.g. fruit for fruit juice) may be of bad quality or the wrong variety; other inputs (e.g. flavourings) may be of a different type to those to which consumers are used; the processor may have technical problems. And even if the product tastes fine consumers may still not buy it because they don't like the packaging. Perhaps they are used to buying fruit juice in cartons of 0.25 litres and don't want to buy it

in plastic containers of 2 litres. Perhaps the labelling does not look very good, making consumers suspect that if the processor cannot get the labels right there may also be something wrong with the product. Again, before large investments are made the acceptability of the taste and appearance of the product has to be confirmed.

***Failure to identify potential problems.*** Even if an agroprocessor is producing a tasty and attractive product

problems may still be experienced. Perhaps the local retail shops don't want to sell it. They may argue that they already have three brands of fruit juice on their shelves and don't want any more. Perhaps they buy all of their supplies from one wholesaling company, which gives them weekly deliveries, and they can't be bothered to buy directly from any other company, even if it is local. Alternatively, the shops may be happy to sell the product but will only do so if they can pay for it two months after it has been delivered.

### *Box 3*

#### **The business-planning sequence**

Although this guide is mainly intended to cover the topic of market research, it inevitably also touches on more general aspects of developing an agroprocessing business, such as carrying out a detailed feasibility study. Market research is an essential input into such a feasibility study and into the preparation of a business plan. The usual business-planning sequence is summarized below:

##### **1 MARKET RESEARCH**

- assessment of information needs;
- market research to obtain this information;
- research of existing sources;
- primary research with wholesalers, retailers and other major buyers;
- primary research involving questions to consumers;
- consumer tasting panels.

##### **2 MARKETING PLAN**

setting out the actions required, that is the "4 Ps" - Product, Price, Place and Promotion.

##### **3 PRODUCTION PLAN**

describing and quantifying the inputs required for the business to produce the product(s), including the raw materials, the capital requirements such as factory, machinery and equipment, and labour requirements.

##### **4 FINANCIAL PLAN**

- cash-flow forecast;
- profit-and-loss account forecast;
- break-even analysis;
- sources of finance.

### ***MARKET RESEARCH HINT***

***Arrange for research results to be written down even if you are only carrying out a small study***

*Presenting research results in an organized way makes it easier to evaluate the findings of the research and enables you to easily identify inconsistencies or contradictions that require further research. The structure of a report, which does not have to be very long, will vary according to the product and market and the amount of detail required. A suggested format is:*

- *Brief background and description of proposed product.*
- *Existing products and consumer attitudes to those products. Strengths and weaknesses of competitors.*
- *Existing market size in target area, by type of outlet, by product, by container or package size, etc. with estimates of the potential market for new product(s).*
- *Important characteristics of the market, such as price, quality and packaging, and your ability to compete.*
- *Consumer response to tasting panels.*
- *Distribution methods recommended for your product and costs of distribution.*
- *Promotional techniques used by competitors. Promotional tools preferred by the distribution chain.*
- *Conclusions regarding suitability of your product for the market, with recommendations of the best ways to price, promote and distribute it.*

If the agroprocessor has to pay farmers in cash for their fruit, but only gets paid two months after delivering the juice to retailers, it may well experience cash-flow problems (see Chap. 8).

There may also be production problems. The effect of seasonal raw material supply has already been noted, but difficulties may be experienced in obtaining other essential inputs and poor cash flow may make paying for them difficult in the short term. Pricing of the product may

also jeopardise a factory's success. Failure to consider at an early stage the price at which a product can be sold may lead to a factory being unable to make a profit at the prices consumers are prepared to pay.

The items above are just a few examples of the difficulties that agroprocessors are likely to face if they do not carry out market research. The amount of research required will, of course, vary according to the size of the venture and the area the venture sees as the potential

market. Someone planning a bakery in a village will clearly need to do less research than someone planning to sell fruit juice to a city. But they will still need to do some market research.

Market research can never guarantee success nor totally eliminate risk. It can, however, reduce risk. The costs of carrying out market research are relatively small compared to the potential costs of not doing any, which can be the loss of an entire investment. Market research should not, however, be seen just as a way of minimizing problems. Good research can identify new products that can be produced profitably. It can help agroprocessors to reduce costs by avoiding expenditure (e.g. on packaging characteristics that consumers do not demand or on unnecessary labelling). It can help the processor improve the taste or appearance of products so that more consumers want to buy them. It can help a company to work out how and where to sell its products in the most efficient manner and at the best price. It can help make decisions about whether advertising or promotion is necessary and how this should be done. Finally, market research is an important input into decisions about the price at which the processor should sell the product.

## THIS GUIDE

*Chapter 2* looks in detail at ways of assessing how much of a product can be sold. This involves identifying the quantities of similar products already being sold and assessing the extent to which consumer demand is being supplied. Is demand seasonal? Who are the potential buyers? Could everyone be expected to buy the new product or only more affluent consumers? If the market is already well supplied what will the agroprocessing venture have to do to make sure its products are purchased? Is it wise to produce a new brand of a well-supplied product?

*Chapter 3* looks at how to investigate consumer attitudes about products it is planned to produce. It also considers how to test consumer reaction to the taste and appearance of new products and how to assess whether consumers would buy them in preference to similar products already available.

*Chapter 4* reviews the research necessary to find out how the product should be presented to consumers. What type of product do consumers want? What quality? What package size(s) is required? What type and quality of packaging? Are labels necessary, both to make the product attractive to consumers, and for legal reasons? Would the use of a “brand name” be a good idea?

*Chapter 5* covers researching methods of distributing the product. Where are the best places to sell it (e.g. supermarkets, shops, retail markets)? How should the product be transported and delivered (e.g. in cardboard boxes)? How do costs vary according to location of sale? How often should deliveries be made? What are the business terms of the potential distributors? When do they pay, and how promptly?

*Chapter 6* considers how products should be promoted and advertised. Do competing products do any promotion or advertising? What type of promotion is most appropriate for the product, the distributors and the consumers? What are the costs involved?

*Chapter 7* reviews production feasibility and production and marketing costs. Will processing equipment, raw materials and other inputs (e.g. water, electricity, packaging) be available and has the cost been identified?

*Chapter 8* looks at simple ways of calculating whether a venture will be able to make a profit or not. It also pays attention to ways of setting prices. The processing venture needs to make sure that it can get the ex-factory price it needs. At what retail price does the product need to be sold to achieve this ex-factory price, that is, what are the costs between the factory and the consumer? What pricing options are available for the venture? Can it charge more than it really needs to? Should it charge

less in order to attract customers? How does it price different sizes?

The chapters and the activities you need to carry out are presented here as a sequence. This is to facilitate presentation of the various types of issue. In reality, of course, many of the market research activities outlined here (particularly those of Chapters 2, 4, 5 and 6) are carried out at the same time. When researchers visit shopkeepers they will want to cover the points raised in all four chapters. Annex 1 presents a checklist of questions to help them do this.

**2 How much can be sold, where and when?**

*Main points in Chapter 2*  
**How much can be sold, where and when?**

*Agroprocessors need to be able to work out the size of the potential market, identify that part of the market that they can supply and find out who their competitors will be. The chapter advises on ...*

- *surveying potential retailers and wholesalers;*
- *working out how much of a product can be sold;*
- *identifying the market for similar products;*
- *finding out the existing supply and the different market “segments”;*
- *learning about seasonality of demand.*

*Retailers and wholesalers are often happy  
to collaborate with your research.*



*Use a checklist  
so you don't forget any questions.*

## THE POTENTIAL MARKET AREA

You need to develop realistic expectations about where you can sell your products. You should not be too ambitious and should not plan to go further afield than is necessary to sell your output, as this will increase costs. Some of the things that need to be considered when identifying potential locations to sell are:

- *how perishable is the product?* Milk, for example, is very perishable in hot climates. Transport to distant cities has to be in refrigerated trucks. A small dairy may be attracted by better prices in the towns but may find it has insufficient milk to use the trucks to full capacity, so pushing its costs up;
- *who consumes the product?* Many consumers have very little money. They may not often be able to afford processed items such as pasteurized and packaged fruit juices, cheese, dried fruit or snack foods. Thus your potential market may, depending on your product, be limited to the richer parts of urban areas. Processed food consumption is also likely to vary from one ethnic group to another. Religion can be another important determinant of consumption patterns;
- *what is the competition?* It is vital to consider the competing products. Can you produce products that can compete in taste and appearance with those that are manufactured by large commercial companies or

even imported? If not, you will have to sell your products where the commercial products are not available. For example, large companies may sell their products only through supermarkets in large towns. Such items may not be available in smaller shops, particularly if they are perishable. Thus you may be advised to concentrate on selling in small shops and in villages rather than in town supermarkets.

- *what transport is available?* This is a very important question. You need to be certain that you will always have transport available. Many small and medium ventures will not find it to be viable to own and operate their own truck and they will therefore be dependent on transport services. Are those services reliable? Where do they go? How often? How much do they cost? Are they suitable for food products? What are their terms and conditions? These questions need to be answered before potential sales locations can be investigated.

## SURVEYING POTENTIAL OUTLETS

Once the potential sales area has been identified, the next step is to consider how the product should reach consumers. Very small-scale processors who are centrally located in a village or small town may feel that they can

sell directly to consumers from a small shop next to their factory (e.g. a small dairy). Alternatively, the local retail marketplace may be a suitable outlet for some types of product. In most cases, however, retail shops are likely to present the best opportunity for reaching consumers. Once you have decided to sell to retail shops, you also need to

decide whether to sell direct to the retailers or through wholesalers, if such wholesalers exist (these options are discussed in more detail in Chapter 5). You could also consider selling to government institutions such as schools and hospitals and, depending on your product, to hotels, restaurants, or fast-food suppliers.

**MARKET RESEARCH HINT**  
**Gathering information about demand  
and quantities sold**

*It is clearly not practicable to stand inside or outside a shop all day to count how much of a product consumers are purchasing. In order to get the information you need you have to interview the shopkeeper, supermarket manager or wholesaler. In doing so, you need to be aware that:*

- *Shopkeepers are often very busy. When they understand the reason for the interview and how it can benefit them, they are normally happy to help, but they have to give priority to serving customers and other matters connected with their daily business. You must recognize that you are asking a favour of the shopkeeper and you must therefore be prepared to wait until the shopkeeper has some spare time. The interview is likely to be interrupted on several occasions. Try to select a time when the shop is unlikely to be busy.*
- *Shopkeepers are always suspicious of people who visit to ask questions. Therefore, a good interviewer does not start asking questions straight away. In many*

*societies it is obligatory when people meet to spend some time on social pleasantries. Even where this is not part of the culture it is a good idea to take time to explain in detail the purpose of the interview and to assure the shopkeepers that the information they give will be kept confidential. You should ask sensitive questions at the end of the interviews when the shopkeepers have come to trust you.*

- *Make the people you interview feel that you are interested in what they have to say because they are the “experts.” Be careful to use language they can understand and are familiar with.*
- *You should encourage shopkeepers to talk freely about their business. Prompt more detailed replies to your questions with follow-up questions such as, “could you please tell me more?” or “why is that?” or “why don’t you do that?” and be ready to write down the answers.*

## Asking questions

When the possible outlets for your products have been identified the next step is to carry out a detailed survey of those outlets. Depending on the type of product and the number of potential outlets identified, you may plan to visit all shops in the area. However, larger processors that are planning to sell over a wide area will have to take a sample of shops. No hard and fast rule can be made about the minimum number of shops to sample, but it is important to ensure coverage of all types (e.g. supermarket, high street shop, corner shop in urban area, village shop). If possible, when there are only a few supermarkets all should be contacted, as they will almost certainly be the largest distributors and sampling of a small number could cause major inaccuracies.

It is also important to know how many shops of each type there are in the area, so that the information obtained from the sampled shops can be used to make an estimate of the total market size (see Figure 1). Preferably, their location should be marked on a map to help you sample shops from different areas. Such a map will also be of assistance later when you begin to promote your products and plan delivery routes. Sampling of consumers is discussed in Chapter 3. Similar techniques can be applied when sampling retailers.

## HOW MUCH OF THE PRODUCT CAN BE SOLD?

In order to estimate potential sales, your surveys should try to find out:

- what quantities of the product are already being sold in the area?
- what quantities of similar products are being sold, and at what prices? Are there any that people may stop buying in order to buy your product?
- is the existing supply of competing products adequate to meet the demand, or is there a shortage? If there is a shortage, are there any known plans by other suppliers to increase their supply?
- does the market have different segments according to the type and quality of the product or according to the type of consumer? Is the potential market limited to some types of buyers?
- is demand seasonal? This is important. If demand is highly seasonal, for example, during a religious festival, shops will not want to take delivery until just before the festival. You will then have to store the product for long periods, so adding to your costs.

### Total quantities being sold

At the simplest level, if you are planning to produce just for your local village you need to ask questions of local shopkeepers and also talk to consumers. For example, if

a village has no bakery there may be a good opportunity to open one. The first step of the market research process is to find out how much bread is already being sold locally. In this case it would be important to know what type of bread is sold. Is it fresh bread from a bakery in a nearby village or town, or commercially baked, wrapped bread from the city? If the latter, would people buy fresh bread instead, or do they prefer wrapped bread because it lasts longer? Do people want a fresher version of wrapped bread, or do they prefer more traditional styles?

Similarly, there may be scope to open a small dairy and a survey of shops can be done to find out how much long-life (UHT), condensed or evaporated milk and milk powder is sold. However, it cannot be assumed that a dairy can replace all UHT sales with fresh milk sales. People may prefer UHT milk because it lasts longer. In Tonga, in the South Pacific, there was a reluctance to buy fresh milk from the country's first dairy because, after becoming used to long-life milk, people found the taste of the real thing to be too strong. In the Middle East milk powder is used for making sweets and desserts, so a liquid milk supplier cannot assume that the total milk market is for liquid milk.

People tend to have unreliable memories. Also, when shopkeepers sell a wide range of products they cannot be expected to know off the top of their heads exactly how much of each they sell. You could therefore ask larger shopkeepers to check their records. These could be delivery notes from the supplier or receipts from visits to

***MARKET RESEARCH HINT***  
***Visits to shops should also include***  
***an evaluation of their suitability***  
***to sell your products***

*When you visit retailers to carry out market research you should be using the opportunity not just to get information but also to decide whether you want your products to be sold in their shops. As a consumer, would you find the shop a pleasant place to make purchases? Is the display attractive? Would your product be displayed in a satisfactory way? Does the shop have the right facilities for your product (e.g. a display refrigerator)? Do the people working in the shop give a good impression? Is the shop clean and likely to handle your product in an hygienic way? Does the shop look like a dynamic, expanding business, or like one that is about to close down?*

a wholesaler. If possible, you should ask the shopkeeper to provide information about quantities purchased over the previous twelve months.

In practice, however, shopkeepers may be unwilling or unable to provide such information. Checking records may take up too much of their time, or they may simply consider the information confidential. Try making estimates of their sales in a more subtle way. For example, you could ask them how much they sold in the previous month and then

get them to say whether that month was an average one for sales, or not. Then try to find out in which months sales are normally higher and in which months they are less, and by how much.

It is also useful if you can get retailers to give you a general idea about trends in sales. Have annual sales of the products you are interested in been increasing or declining? Have particular brands been increasing their share of the market and, if so, why?

A calculation such as that in Figure 1 can then be done. It is important to get information on quantities sold for all size units. You need to know not only that the shopkeeper sold 3 000 litres of packaged fruit juice last year but also how much of that total was in one-litre containers, how much in half-litre containers, etc.

#### ***MARKET RESEARCH HINT***

##### ***Plan your schedule of interviews carefully***

*Make sure that you allow enough time to travel from shop to shop and sufficient time to look round the shop (if it is a large one) before talking to the owner or manager. Shops are not always open every day, or for all of the day. Try to find out in advance when they are open. Look also at the neighbourhood of each shop to try to get an idea of its customers.*

It is important to first find out whether, for the product being researched, the shop or supermarket deals directly with producers or importers or whether it buys through wholesalers. Some very small retailers in villages may even get their supplies from larger retailers in nearby towns. In some major cities wholesalers may have large warehouses, which retailers visit to get their supplies. In other cases the wholesalers may deliver to retailers. Where retailers buy only from wholesalers then detailed interviews should certainly be held with those wholesalers. Wholesalers may have trouble in providing accurate information about sales to a particular area and will probably not be prepared to give information about sales to individual shops. Such information should be regarded as confidential and should be obtained from the shops themselves. Information from wholesalers about quantities sold is therefore likely to be of most use to larger agroprocessors who are planning to supply large areas of a country.

While interviews with those selling the products are usually the best way of getting information about the size of the market, there may be some instances when useful information already exists in published form. This will apply particularly to ventures that are planning to supply an entire country, for example, in the case of small island states such as in the Caribbean or Pacific. In these countries, import statistics may give a useful indication of total market size, particularly where there are no local producers. However, it is always wise to be cautious about official statistics.

*Figure 1*  
**Estimating totals consumed**

Assume that the researchers interview the following samples of shops:

- Five** out of the **five** supermarkets in the area;
- Five** out of the **twenty** urban shops;
- Ten** out of the **fifty** village shops.

Then, on the basis of the information obtained from the sampled shops, the following calculations can be made ...

... for one-litre containers of fruit juice

<i>Shop type</i>	<i>Total sales in sampled shops</i>	<i>Multiplier</i>	<i>Estimated total sales</i>
Supermarket	35 000 litres	1.0	35 000 litres
Urban shop	12 000 litres	4.0 (20÷5)	48 000 litres
Village shop	9 000 litres	5.0 (50÷10)	45 000 litres
Total			128 000 litres

... for half-litre containers of fruit juice

<i>Shop type</i>	<i>Total sales in sampled shops</i>	<i>Multiplier</i>	<i>Estimated total sales</i>
Supermarket	17 000 litres	1.0	17 000 litres
Urban shop	7 000 litres	4.0 (20÷5)	28 000 litres
Village shop	6 000 litres	5.0 (50÷10)	30 000 litres
Total			75 000 litres

Customs and Excise categories are often fairly broad and may include products other than those you are interested in. Furthermore, the accuracy of import statistics is frequently questioned in many countries. Official statistics on national production of a wide range of products may also be available. These should also be used with some caution, and should certainly be supplemented by interviews with shopkeepers. In some cases manufacturers' or trade associations may exist for the products you are interested in, and they can often provide useful information.

### **The market for similar products**

Many processed food products cannot be considered "essential" and many are not purchased regularly. Snack foods, sweets or candies, soft drinks, ice cream, etc. are not vital to people's diets and are often only purchased when people have some spare money. What they buy will depend on a variety of factors such as what is available in the shop, what they have eaten and enjoyed before or what advertising they may have seen. In many cases a purchase may be made on a "whim." Sometimes, if you ask someone when they walk out of the shop why they bought a particular product they may have no real explanation. They may just say that they "felt like buying it at the time."

In many cases, therefore, you need to try to identify the total demand for a wider range of products than just the products you can supply. For example:

- potato chip (crisp) producers need to examine the entire market for all snack foods, and not just the market for potato chips;
- orange juice producers need to review the market for all fruit juices, and not just orange juice;
- ice lollipop producers need to consider the entire ice cream market and not just the lollipop market;
- sausage producers need to take into account the total market for meat and meat products;
- tomato sauce producers need to look at the market for all sauces, and not just that of tomato.

It will, of course, not be possible for a sausage producer to persuade people to eat only sausages and no other meat. However, if market research indicates that existing sales of sausages are very low, that will not always mean that additional sausages cannot be sold. Persuading people to eat sausages instead of other meat for just one meal a month may be more than enough for a profitable sausage-making business.

In carrying out interviews with shopkeepers, therefore, you need to get information both on existing sales of the product you plan to produce and about sales of other products that could be substituted by your product.

### **The existing supply**

There is a big difference between a market for packaged fruit juice where annual sales are 120 000 litres and those sales correspond to what people want to buy, and a market

where annual sales are 120 000 litres but where the shops are always in short supply and 200 000 litres could be sold if adequate supplies were available. You therefore need to check the shelves of shops to make sure that they have stocks on display, and also confirm with shopkeepers that supplies are always available.

If there is a shortage of supply, you should try to find out from the shopkeepers the reasons for this. There could be several explanations. For example, on a small island imported supplies may arrive by boat just once every two weeks and run out after the first week. In other cases, there may be a shortage of the raw material or of imported packaging. How do the existing suppliers explain the shortage to the shopkeepers? Has there always been a shortage, or is it just a temporary problem? If there has been a shortage for some time, are the shopkeepers aware of plans by the existing suppliers to increase production? Clearly, if the demand for a product is not met by the supply and other producers or importers are not planning to increase supply then there may be good potential for a new processor. If, on the other hand, an existing supplier is just about to complete a new factory, which will double that company's production, then a new processor may face considerable problems.

### **Market segmentation**

This refers to the types of products and the types of customers who buy them. It is very important that market researchers take market segmentation into consideration.

If this is not done there is a great risk of overestimating the market size. In the case of orange juice, for example, there are in many countries several different products available in the shops:

1. 100 percent natural fruit juice;
2. A combination of 100 percent natural fruit juice and reconstituted juice;
3. Reconstituted juice in cartons, bottles, jars or cans;
4. Frozen, concentrated orange juice;
5. Concentrated juice in cans or bottles.

Each of the above is likely to appeal to a different type of consumer. The richest consumers, who like and can afford "fresh" products, can be expected to prefer Nos. 1 or 2. The poorest consumers may buy only No. 5, in part because this may be the only fruit-juice product available in villages and poor districts of towns and in part because it is all they can afford. Thus, when surveying the market size, you need to break down the total market into different categories. You also need to find out which categories of product are sold in which areas and in which shops. Careful research will ensure that the market for your product is not overestimated and will also avoid mistakes being made later, such as trying to sell expensive "fresh" juice in inappropriate areas.

### **Seasonality**

It is not enough to know that 120 000 tons of fruit juice are sold every year. You also need to know if that represents

**MARKET RESEARCH HINT**  
***Prepare checklists of questions to be asked  
prior to research visits***

*The possibility of research mistakes can be reduced by making sure that you have prepared checklists of questions before interviewing shopkeepers and/or wholesalers. An example of such a checklist is given in Annex 1. You should try to include in the checklist all the questions you need to ask. However, new questions may emerge while you are talking to shopkeepers, so you should leave space for additional questions and their answers to be inserted.*

10 000 tons a month or if in some months 15 000 tons are sold and in others 5 000 tons. Where consumer demand is seasonal so will be the purchases of shopkeepers. When consumer demand is low retailers will not want to buy products that they cannot sell. When demand is high they will want to be sure that you can supply enough. Ask retailers about seasonality and try to verify the information they provide by asking if they have monthly sales figures.

You will need to decide whether to adjust the throughput of your factory to reflect the seasonal demand. This will normally depend on the perishability of the product.

24 Canned foods, for example, should cause no problems

as they have a long “shelf life”<sup>3</sup> and can easily be stored. Dairy and some meat products, juices and even some snack foods, on the other hand, have relatively short shelf lives. Another important consideration is the ability of your venture to finance stocks. If you are manufacturing products but not selling them because demand is seasonal then you will be spending money on the raw materials and on the workers in your factory, but not receiving money from their sale. You may need to get a bank loan to finance the stocks (see cash flow calculations in Chapter 8): alternatively you may decide to reduce or even temporarily stop production.

Seasonal demand for a few products can be fairly obvious. In countries that have pronounced seasons you can usually expect that sales of ice cream will be much higher in summer than in winter. People are also likely to drink more juices and other drinks in the summer. But there may be seasonal trends that are less immediately obvious; for example, consumption of products by children may depend on whether they are on holiday or at school. In Thailand 25 percent of milk is consumed by schoolchildren at school. Milk consumption tends to go down during school holidays.

In developing countries people in rural areas usually have more money available at harvest time and less when

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<sup>3</sup> “Shelf life” is the amount of time a product can be kept without spoilage or loss of safety and quality and can still be sold. Most food products now have a “sell by” or a “use by” date, after which time they should not be sold.

school fees have to be paid. Many countries require workers to be paid a 13<sup>th</sup> month's salary and some even a 14<sup>th</sup> month. This additional money can also influence how much of a product people buy. You therefore need to question shopkeepers very closely about seasonality and try to get as much information as possible about their weekly or monthly deliveries. Where there seems to have

### ***A WORD OF WARNING***

*When you develop a new product that proves very popular, others will inevitably copy it. You must therefore consider the possible impact of others starting to produce similar products. This could affect your sales and the price you can charge.*

*Similarly, where there are existing suppliers of the products you plan to produce, you will need to consider their likely reaction to your competition. If they are big national companies and you are planning just to supply a small local area, they will probably not worry. But if you are aiming to take a significant share of a national or provincial market your competitors may respond in ways that make it difficult for you to succeed. For example, they may increase their expenditure on promotion and advertising. They may temporarily lower their prices. Such actions may have a significant impact on the quantities you can sell and the prices you can charge.*

been a period when they didn't buy very much you need to find out why. Was it just because they had ordered too much before, or was it because they knew that demand would be low? In some cases seasonality of demand can be very pronounced. This is normally when products are mainly consumed during particular festivals.

Of course, it is not only demand that can be seasonal. Raw material supply for agroprocessors is also likely to be seasonal. If you are planning to produce a perishable product with raw material that is only available for a short period, and that period corresponds with a period when demand is low, then you clearly need to reconsider your plans. For example, one possibility would be to use the available raw materials to produce something with a longer shelf life.

### **REACHING CONCLUSIONS**

Carrying out the research outlined above can help you to decide whether or not there is a potential market for the type of product you plan to produce and whether it appears practical for you to supply that market.

You should now have a good idea of:

- the total market for your product in the geographical area you can supply and whether demand is fully satisfied by existing suppliers;
- the quantities of each package size that are sold;
- the periods when demand is high and the times when demand is low;
- the potential market if you can persuade consumers to buy your product rather than something different (e.g. chili sauce rather than tomato sauce).
- the types of product similar to yours that are sold and when, where and to whom they are sold.

You can then reach some basic conclusions, such as:

- the total packaged orange juice market is around 100 000 litres and I was planning to produce just 5 000 litres a year. I should not have too much trouble taking just five percent of the market;
- the total packaged fruit juice market is 100 000 litres a year but only 20 000 litres is orange juice. I plan to produce 5 000 litres. Is my product good enough to take 25 percent of the market?

- the total annual market is around 10 000 packets, but I was planning to manufacture 20 000. Clearly I have to rethink my plans;
- no one is selling chips made from taro, but the snack food market is around 200 000 bags a year, so I should be able to sell 10 000 bags of taro chips if I can make a good product;
- no one is selling fruit leathers. I may be able to persuade children who buy lollipops, chocolate bars, etc. to buy my fruit leathers occasionally, but I am not sure;
- I was planning to process cheese, but it looks as if demand for cheese is very low. However, several shopkeepers indicated that they would like to sell yoghurt but cannot find a supplier. Can I make yoghurt?

If your initial research convinces you that there is a potential market for your product, then half the battle is over. But much more information is required before you can be really confident of success. Will people accept your product? Will you be able to present the product as customers want to buy it, and at the right price? Will shopkeepers sell it? What advertising will you have to do? Issues such as these will be considered in the next chapters.

### **3 Researching consumer attitudes to your products**

*Main points in Chapter 3*  
**Researching consumer attitudes to your products**

*Before beginning commercial production  
you must be sure that consumers will want to buy your products.*

*The chapter reviews ...*

- *how to carry out a survey and interview consumers to find out what they buy, where and when;*
- *designing questionnaires for consumer surveys;*
- *organizing and carrying out tasting tests on consumer preferences about tastes, smell, texture, etc.;*
- *surveying consumer reaction to packaging and labelling.*



*It is important to test people's reactions to your products before going into full-scale production.*

## INTRODUCTION

As we have seen in Chapter 2 and will discuss again in the following chapters, much market information can be obtained from observing the existing situation in shops and asking questions of retailers and wholesalers. However, this type of research will be wasted if, when you come to sell your products, people do not buy them. Before you invest in a factory you must be sure that people will want to buy what you are going to produce, and that they will keep on buying it. To achieve this confidence it is desirable to both carry out surveys of consumers and to arrange for potential consumers to taste your products and give their opinions.

## CONSUMER SURVEYS

Consumer surveys are used to find out:

- *who buys certain products and where they buy them.* You need to decide where you are going to sell your products. Some products may be purchased by almost everyone in every type of shop. Others, however, may only be purchased by more affluent people who tend to live in certain areas of towns. In that case you want to make sure your products are sold in shops in those areas. As noted in Chapter 2, you can get much of this information from interviews with retailers, but interviewing consumers can enable you to double check the information obtained;
- *what people think of competing products.* What do they think about products that will compete with yours? What is good about them; what is not so good? What do people think about the packaging? How important is the price in people's decisions to buy a product? Do attitudes to various characteristics of products vary according to people's incomes, where they live and where they shop?
- *how people buy competing products.* What size do they prefer? Do they make regular purchases or just buy the products for special occasions? If the latter, when? This is important information to enable you to plan your production and delivery schedule. For

example, in the case of a fairly perishable product such as yoghurt, if people buy yoghurt to consume at the weekend you will want to supply shops on Thursday or Friday, not on Monday morning. Some products may be mainly purchased for holidays and religious festivals and you will need to organize your deliveries to meet those periods of high demand.

Consumer questionnaires are mainly used when the type of product to be sold is already well-established on the market. If people have never tasted nor used the type of product you plan to produce then it will be difficult for them to answer questions about it. For a product with which most people are familiar, such as juice or jam, it is a relatively easy matter to ask questions and get useful information.

### **Carrying out a survey**

Before you carry out a survey of potential customers you need to decide who to survey and how you are going to carry out the survey. If you decide to use questionnaires, then you also have to design the questionnaire so that it will provide you with the information you need.

In developed countries interviews by telephone are widely used. However, this is rarely appropriate for developing countries. Normally you have to interview potential customers in person, either individually or as members of a group. For small and medium-sized processors individual interviews are probably easier, as

organizing to get groups of people together can be rather difficult. Here we shall concentrate on individual interviews, although you could consider inviting groups of people to meetings, at which you could discuss their attitudes to the products you plan to compete with. You could also use such groups to discuss possible “brand” names for your products (see Chapter 6).

It is clearly not possible to interview all potential customers. For that reason you will have to take a sample. The question of sampling is fairly complex and the subject of much debate among market research professionals. For fairly small organizations it is necessary only to observe a few basic rules:<sup>4</sup>

- carry out interviews in a relevant location;
- carry out interviews in a systematic way;
- use simple sampling techniques;
- limit interviews to potential customers;
- stratify;
- minimize the cost.

***Carry out interviews in a relevant location.*** If you have no idea about where you will be able to sell your product then you may need to carry out a random survey of the entire population in a particular area. However, if you are

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<sup>4</sup> Large companies who wish to understand the topic in more depth may wish to refer to Chapter 7 “Sampling in marketing research” in FAO, 1997 (see “Further reading”).

planning to sell your product through supermarkets it may be a good idea to carry out interviews of people as they walk out of a supermarket.

**Make sure you carry out interviews in a systematic way.** Standing in the street or at a marketplace and talking to people you see there may produce biased results. For example, if the interviewer is a man he may choose to interview the most attractive women; conversely, a woman may choose to interview the most handsome men. Neither approach is likely to give you an accurate view of people's ideas about the product you plan to produce. You need to decide in advance how you will choose the people you interview, using simple sampling techniques.

**Use simple sampling techniques.** The simplest method is to interview a percentage of people in a structured way. For example, if you decide to interview ten percent of all people leaving a supermarket on a particular day then you could interview the first to leave, the eleventh, the twenty-first, the thirty-first, etc. This removes the possible bias caused by the interviewer choosing to interview someone just because they look nice or because they look friendly and willing to cooperate. However, a problem with this method is that it is difficult to interview someone and count people leaving a store at the same time, so you may have to employ two interviewers.

**Limit interviews to potential customers.** You should concentrate your interviews on the people you feel are



*Systematic interviewing, such as asking questions of every tenth person ...*



*... avoids the risk of the interviewers picking the most attractive people to interview!.*

most likely to buy your products. For example, it is probable that most purchases of iced lollies are by children (you should confirm your ideas about potential customers by talking to shopkeepers first) or by parents for their children. It is more useful to interview children, either alone or with their parents, as they leave the shop. Even more obviously, children are unlikely to buy beer, so there is little point in interviewing them about beer. In the above examples, therefore, you could survey every tenth child about iced lollies, or every tenth adult about beer.

**Stratify.** Let's suppose that you interview every tenth child leaving a supermarket in order to ask questions about iced lollies. At the end of the day you find you have interviewed fifteen girls and five boys. There may be reasons for this, unrelated to iced lollies. For example, the shop may be close to a girls' school or parents may be more likely to ask their daughters to do shopping for them (girls may go to the shop to buy other things). However, a sample of fifteen girls and five boys may not be representative of all children shopping in all shops where you could sell your lollies. You can overcome this problem by taking a stratified sample in which you plan to interview ten girls and ten boys. You start out by interviewing every tenth child until you have spoken to ten girls. After that you interview just boys. Other ways of stratifying include age and income. For example, you could further stratify the sample of children by planning to interview five boys and five girls under eleven years old and five of each over eleven years old.

**Minimize the cost.** The amount of consumer research you can do is, of course, related to the expected size of your business. The number of interviews you need to do will depend on how large an area you intend to supply and on the amount of money and time you think you can afford to spend on interviews. You will have to do more interviews if your product is something that is not purchased by everyone than if it is a product that everyone buys. For example, if you interview 50 people you may find that almost all eat bread but that only ten eat yoghurt. After a time, you will discover that you are not getting much, if any, useful information from additional interviews and it is time to stop. Interviewing people in a public place is more cost-effective than visiting them in their home, although if you need to ask a lot of questions home interviews may be more appropriate (people are unlikely to want to stand in the street answering your questions for more than a few minutes). Random sampling of people according to their addresses is expensive because of the costs of going from one home to another. You could concentrate interviews in a few randomly selected areas (i.e. cluster sampling)<sup>5</sup> or just carry out interviews in those parts of town where you think you will be able to sell your product.

<sup>5</sup> see FAO, 1997 page 74

## Designing questionnaires<sup>6</sup>

Questionnaires should be designed in such a way that the information obtained from each interview can be compared and much of it can be put in the form of tables of data. If you are planning a small business and will do the interviews yourself you still need a structure for the interview. If you are going to employ people to ask questions you should give them a very clear questionnaire with instructions to ask every question exactly as written. The questionnaire should be clear and easy to understand and as brief as possible. Apart from a few polite opening comments it should not contain questions that will not be of use to you in planning your business. In planning the questionnaire you need to:

- decide on the information required (see above);
- decide who you want to interview (see above);
- decide on the questions and their wording;
- put the questions into a sensible order;
- check the length of the questionnaire;
- pre-test the questionnaire.

Types of questions that can be used include:

- opening questions;
- closed questions;
- multiple-choice questions;
- scale questions;
- open-ended questions;
- combination multiple-choice and open-ended questions.

*Opening questions.* These are polite introductory questions to put the person being interviewed at ease. For example ...

*“I am doing a survey about the fruit juices that people like to buy. Do you mind helping me by answering a few questions?”*

*Closed questions.* These questions have “yes” or “no” as answers and can be used to establish basic facts. For example ...

*“Do you drink orange juice?”*

*Multiple-choice questions.* These require the person being interviewed to choose one answer from a list of possible answers you have pre-selected. For example, a number of answers are possible for the question ...

*“How often do you buy orange juice?”*

among these are ...

- more than once a week
- about once a week
- once or twice a month
- less than once a month

or you may ask ...

“Which orange juice do you like best?”

- ABC juice
- XYZ juice
- Joe’s juice

*Scale questions.* These are a type of multiple-choice question where the person being interviewed can give answers from a scale of possibilities, such as ...

- |                          |                          |                                     |                          |                          |
|--------------------------|--------------------------|-------------------------------------|--------------------------|--------------------------|
| horrible                 | bad                      | OK                                  | good                     | fantastic                |
| <input type="checkbox"/> | <input type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

You could also ask people to rate the importance of a feature of your product. For example ...

“Sugar content in fruit juice is to me”:

- |                          |                                     |                          |                          |                          |
|--------------------------|-------------------------------------|--------------------------|--------------------------|--------------------------|
| extremely important      | very important                      | important                | not very important       | not important            |
| <input type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

Other approaches include ...

“ABC Juice is”

- |                          |                          |                          |                                     |                          |
|--------------------------|--------------------------|--------------------------|-------------------------------------|--------------------------|
| excellent                | very good                | good                     | fair                                | poor                     |
| <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> |

or ...

“ABC Juice is better than Joe’s Juice”

- |                          |                          |                            |                                     |                          |
|--------------------------|--------------------------|----------------------------|-------------------------------------|--------------------------|
| strongly agree           | agree                    | neither agree nor disagree | disagree                            | strongly disagree        |
| <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/>   | <input checked="" type="checkbox"/> | <input type="checkbox"/> |

**Note:** The advantage of multiple-choice questions is that they simplify the statistical analysis of the questionnaire. The disadvantage is that they force people to give answers they may really not want to give. For example, in response to the question about which juice is preferred some people may want to say, “I like ABC juice and Joe’s juice the same but XYZ juice is awful.” (In this case the problem could be avoided by changing the question to “which of the following juices do you like?”, although, of course, the information obtained will not be exactly the same.)

*Open-ended questions.* These are questions where the interviewer writes down the answer the respondent provides. It is difficult to do any statistical analysis of the answers to such questions but they can provide useful information, for example by revealing issues that had not been thought about before.

*Combination multiple-choice and open-ended questions.* These are like multiple-choice questions but have a blank space for a reply not foreseen when the questionnaire was designed. For example, answers other than those listed are possible for the question ...

*“What is the main reason you buy ABC juice?”*

- the taste
- the price
- the packaging
- company reputation
- others *my children like it*

The questionnaire needs to follow a logical sequence. For example, you need to establish that people do, indeed, buy fruit juice, before asking them what types of juice they buy. The following sequence is logical ...

1. Do you drink fruit juice?
2. Which brand of fruit juice do you normally drink?
3. What do you like about this brand?
4. What would make you consider buying a different brand?

... whereas the next sequence is not logical and is cumbersome ...

1. What would make you consider buying a different brand of fruit juice to the one you already buy?
2. What do you like about the brand you drink?
3. What brand do you normally drink?

Once you have designed a questionnaire, you need to first try it out with a few people. Do they understand the questions? Can they answer them without any difficulties? Are they willing to wait standing up for the time it takes to answer the questions? After this test you should amend the questionnaire, if necessary, before doing a further test in a market or outside a shop.

**Note:** An example of a consumer questionnaire is given in Annex 2.

## TASTING TESTS

### When to have your products tasted

It is a good idea to carry out consumer surveys before you organize tasting. The surveys may tell you a lot about what people expect from a product, allowing you to change your product's formulation to meet their preferences.

The need for tasting surveys will depend on the products you plan to market. Foods that taste more or less the same everywhere require little or no advance tasting, but foods that depend on the formulation and on different ingredients do.

Some points to consider are:

- if you plan to open a dairy you should not need to have people taste your milk, as long as they are already familiar with the taste of fresh milk.<sup>7</sup> But if you plan to produce products such as cheeses and yoghurts you should certainly seek consumer opinion of these;
- some products may seem the same but are not. The flavour of honey, for example, depends very much on the flowers from which the bees obtain pollen. Consumers may like one type of honey very much but dislike the honey produced by your bees. Mass-produced honey often has a very bland taste and if consumers have become used to this they may not like honey with a strong flavour;
- in the case of eggs, consumers may be used to eggs from battery-farmed chickens. These often have fairly weak-looking yolks, with no strong taste. Eggs from free-range chickens can have very yellow yolks with a much more pronounced taste that consumers may, initially at least, not like very much;
- products that require significant processing can vary noticeably from producer to producer. For juices, jams, sauces, chutneys, snack foods, sausages, beer, etc. you will certainly need to test your products before making expensive investments.

## **Organizing tasting tests**

Unless you already have a processing facility and are just planning to add another product to your range, the products you prepare for tasting purposes will probably have to be made in your experimental kitchen, if you already have one, or in someone's home. For this reason they will not taste exactly the same as they will when you begin commercial processing. You should therefore try to create a situation in the experimental kitchen as close as possible to commercial production. For example, if you think that the fruit you will be using will take two days to reach you from the farmers, don't use freshly picked fruit for your trials. If your factory will eventually use large caterers' packs of sugar, make sure that this sugar is the same as that used in your experimental products. Use cooking utensils of the same metal as those you will use in your factory. There are many factors that can influence the taste of processed foods.

The tasting survey you organize will depend on the products you are planning to produce. For example, if you are going to make jam this is a product with which most people are already familiar. You can then ask them to compare your jam with other jams that they already buy (see Figure 2). On the other hand, if you are planning to produce a product that is unknown in your area you will need to find out not only whether people like the product but also whether they would buy it.

<sup>7</sup> but see the story in Chapter 2 page 19

When organizing tastings there are several important things to take into account:

- the people who do the tasting may not be entirely truthful when asked for their comments on your products. If they are friends they may not want to hurt your feelings by telling you the products taste awful. Even if they are strangers, they may still want to please you by saying your products taste nice. Ways of overcoming such problems include:
  1. Have people compare your product with another that is already available. If you are organizing a tasting of jam, for example, you could buy another jam and get the tasters to compare it with your jam. You should put the jams on similar plates and number them 1 and 2 or A and B so that only you know which jam is which. It is good if you can organize more than one tasting session as this will give you a chance to change the numbers to reduce the danger of bias (some people may think that Jam No. 1 is meant to be the best); You could also compare your jam with different jams each time. Experience suggests that many people have difficulty in evaluating more than two samples at the same time so it may not be a good idea to give your tasters three or four jams to taste.<sup>8</sup>

2. Ask people to fill in a questionnaire to give their comments on the product (if the tasters are unable to read and write you can employ people to ask the questions and write down the answers). Such questionnaires can give tasters the opportunity not only to say whether they like the product or not, but also to make comments on it. Thus one question may be simply, “how much do you like this product?” If the tasters are trying to please you they may respond, “very much.” But answers to further questions may indicate that they don’t like it very much at all. You could ask, “how would you improve this product?” This may result in people who said they liked your product also giving many suggestions for improvement. Additionally, you could identify specific characteristics of the product and get the opinions of the tasters on each, for example “is this product too sweet, about right, or not sweet enough?” This type of question can be used for new products that people do not presently consume. It can also be used for products that are already in the shops, such as jam, after you have done a comparative tasting as described above.

- it is not just the taste that determines whether people like a product. In the case of jam, for example, the ease with which it can be spread on bread may be important. Colour and texture are also important. If relevant to your product you should ask questions about these features;

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<sup>8</sup> See Coetzee, H., 2001 for an interesting article on the testing of new food products on illiterate and semi-literate consumers.

*Figure 2*  
**Example of a tasting survey form\***

<i>For the following characteristics please put a tick under the better jam</i>	<i>Jam A</i>	<i>Jam B</i>
Taste		
Thickness		
Fruit content		
Colour		
<i>Please give 2 ticks to the jam you liked more and 1 to the jam you liked less</i>		
<i>Please put 1 tick under the jam(s) you would consider buying and a cross under the jam(s) you would not buy</i>		

\*although this form shows a survey for jams,  
any product can be substituted

- as far as possible, tastings should accurately reflect the way in which people normally consume a product. For example, if people normally eat jam on bread, make sure that you have available a supply of the bread they would probably use. Clearly, however, this will not always be possible. If you are having people taste tomato ketchup it is not really feasible to cook everyone a meal to create the sort of situation in which they would normally use ketchup;
- the people who buy a product may not be the ones who consume it. This particularly applies to items mainly consumed by children, such as sweets and candies. So if you are planning to make this sort of product you will have to organize tasting surveys for children, not for their parents. Be aware, however, that just because children like something a lot doesn't mean that their parents will buy it. They may, for example, think that a product is too sweet and not good for their children's teeth;
- your samples should be as fresh as possible. Do not prepare them too far in advance;
- when organizing tasting surveys you should keep things as simple as possible. Too many people tasting your products at the same time will cause confusion and may lead to questionnaires being filled in inaccurately. People who have completed the tasting should be kept away from those who are waiting to taste, otherwise they may influence their opinions. Tasters should be told not to make comments when tasting and to only express an

**MARKET RESEARCH HINT**  
*Give traders the opportunity to taste your products*

*When visiting wholesalers and retailers it is useful to take samples of your product. Traders usually have a good idea of what appeals to consumers and can advise on whether your product would be appreciated in their area.*

- opinion when filling out the questionnaire or being interviewed by you or your staff;
- hygiene is an important consideration and, depending on the product, you should make sure you have supplied enough spoons, knives and forks, as appropriate, so that each person can use a clean one. Where you are doing a comparative tasting of two or more products then each person will need the same number of spoons or forks as items being tasted, both for reasons of hygiene and to prevent contamination of the taste of one product by another. For comparative tastings you should provide water in disposable cups so people can wash out their mouths between each tasting.

## Consumer reaction to packaging and labelling

Tasting surveys should come at an early stage in the development of your business, as there is little point in making further investments if people do not like your products. At this stage you are unlikely to have decided on the packaging and almost certainly will not have designed a label. However, you could ask tasters one or two questions about packaging to help in your planning. Where there are alternative types of packaging you could ask, “in what type of packaging would you prefer to buy this product?” In the case of fruit juices, for example, the possible answers could be plastic bottles, glass bottles, cartons or cans.

After you have decided to go ahead and make the product, you need to finalize plans for the packaging and label (see Chapter 4). When you have chosen the type of packaging you want to use and have a draft design of a label, you could consider doing a further consumer survey to find out whether people like your plans. If possible, you should give people two or more alternatives to choose from, rather than simply asking them whether they like your proposal or not. You could also have samples of competitors’ packaging and ask people to compare these with your prototype.

## REACHING CONCLUSIONS

Interviewing consumers and carrying out tasting surveys should give you a good idea of:

- whether people are satisfied or unsatisfied with the existing brands on the market;
- the reaction of potential consumers to the idea of a new brand being available;
- whether there are different market segments and, if so, which locations buy which products;
- whether people like your product or whether you will have to change the recipe.

You can then reach conclusions, such as:

- nearly everyone likes my new jam. People say that the existing brands are not very good, so I should have no trouble making sales;
- most consumers say that price is the most important factor in their decision to buy snack foods. Everyone likes my new chips but the price I may have to charge could be too high. I will need to concentrate my sales on the more affluent areas, and I may not be able to sell as many as I had hoped;
- people didn’t like my pineapple juice very much. It may be that I didn’t use enough sugar, but perhaps the

pineapples are not suitable for juicing. I will have to spend more time developing the product.

When you have decided that people will want to buy your new product, you then need to turn your attention to getting detailed information about the market, as described in the next chapter.

**4 How can your product be made attractive to consumers?**

*Main points in Chapter 4*

**How can your product be made attractive to consumers?**

*A product can taste wonderful but few people will buy it if it is too expensive, in the wrong packaging or unsuitable sizes, or if the labels are unattractive or uninformative.*

*This stage of the market research process involves ...*

- *checking on the size units and prices of competing products, according to location;*
- *identifying quality weaknesses of the competition;*
- *examining the containers used for competing products, in relation to the types of containers you can supply;*
- *learning from the labelling used by competitors and finding out legal obligations regarding label contents;*
- *considering the use of a brand name.*



*It is important to understand the quality of competing products,  
and where your product fits into the quality range.*

## FURTHER INFORMATION REQUIRED

Your research has confirmed that there is a good market for the type of product you plan to make, and you feel you should have no trouble selling what you produce. When you test your product on potential consumers they seem to like it. However, before you can be sure that your new business will be a success there are a lot more questions that require answers. The first question is: “even if people like the product, will they buy it when it is in the shops?” To answer this you need to look at the following:

- can you compete on price with other products?
- can you compete on quality?
- what sizes are sold on the market?
- what packaging and containers do shopkeepers and consumers want and can you supply these?
- what labels are needed and what information do you need to put on the labels to both satisfy consumers and satisfy the law?
- are you going to give your product a “brand name?”

### Price competition

Figure 3 gives an example of a survey form which could be used to compile basic information about products available in a region, their sizes and their prices. Using such a form you can obtain a lot of information, which can be checked with shopkeepers. Also, if you do not

**MARKET RESEARCH HINT**  
*Before interviewing shopkeepers  
it is always a good idea to have a quick look  
at what is on the shelves  
of the shop you are visiting.*

*You can get a considerable amount of information by looking at the shelves of the shops you visit for interviews. Advance research of this type will make you appear knowledgeable when meeting with shopkeepers and this may improve the quality of information you get from them. Also, there is no purpose in wasting the time of shopkeepers by asking them questions that you can answer for yourself by spending a little time looking at their shelves.*

*Look out for the sizes and prices of competing products, and the packaging and labels used. You need to be aware of the way in which other suppliers are distributing their products. For example, as we noted in Chapter 2, some high-quality products may only be available in shops serving richer areas.*

understand the reasons for some of the answers this research gives you, you can ask shopkeepers if they can explain. For example, you may find that one shop stocks only small sizes while another sells only large containers. The shopkeepers may explain that this is because one

*Figure 3*

**Example of a price survey form**

<i>Product</i>	<i>Village shop 1</i>	<i>Supermarket</i>	<i>Village shop 2</i>	<i>Town shop</i>	<i>Suburban shop</i>
ABC Orange Juice 1 litre	\$1.30	\$1.20	\$1.40	\$1.25	n.a.
ABC Orange Juice 0.25 litre	\$0.40	\$0.35	\$0.45	\$0.40	n.a.
Joe's Fresh Orange Juice 2 litres	n.a.	\$3.30	n.a.	\$3.60	\$3.75
Joe's Fresh Orange Juice 1 litre	n.a.	\$1.75	n.a.	\$1.90	\$1.95
Jane's Orange Juice 1 litre	n.a.	\$1.25	\$1.40	n.a.	\$1.30
Jane's Orange Juice 0.25 litre	n.a.	\$0.35	\$0.45	\$0.45	\$0.40

n.a. = not available

shop is close to a school and mainly sells drinks or snacks to schoolchildren, while the other shop mainly sells family packs.

As noted in Chapter 3, it would be useful, when testing your product with consumers, to give them a similar product to taste at the same time, not telling them which one is yours. This will give you an idea both of what consumers think about your product and how they compare it with other products already available. If, for example, the tasting test shows that consumers think yours tastes best or is better in any other way, then you may be able to price it near the top of the price range, although you may need to charge lower prices at the beginning to encourage people to try your product (see Chapter 8 for comments on pricing techniques). But however good your product is, and however much it costs to make, you will only be able to charge what people are prepared to pay for it. If your product is clearly better than any other similar product, don't make the mistake of thinking that you can charge much more for it. Most consumers have only limited amounts of money to spend on non-essential items and, even if they recognize the quality of your product, will probably not want to, nor be able to, pay much extra for it.

If the processed product you plan to produce is not being sold in your area then you need to look at the prices of similar products. Again, avoid thinking that you can charge much more because yours is a superior product.

48 For example, if you are planning to produce cassava chips

then the price you can charge for those will be closely related to the price of potato chips and you need to survey shops to find out the prices of potato chips and similar snack foods.

Once you have an idea of the prices at which competing products are sold, you then need to find out from shopkeepers how much of that price the producer or importer receives, and how much the shopkeeper keeps (the "margin"). Try to get as much information about this as possible as pricing arrangements will almost certainly vary from store to store and, possibly, from brand to brand. Factors influencing the shopkeeper's margin are discussed in Chapter 5.

After you have found out from shopkeepers how much they are paying other suppliers, you need to ask two very important questions. These are:

1. "If I wanted to sell my product to you for X dollars,<sup>9</sup> how much would you sell it for in your shop(s)?"

and

2. "If I wanted you to sell my product for Y dollars, how much would you pay me?"

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<sup>9</sup> The \$ sign and the word "dollar" are used throughout this guide to refer to money in general, and not to any particular national currency.

This information is very important to help you work out whether you can run a profitable business (see Chapter 8). If you need to sell your product for X dollars to make a profit, you have to be sure that people will want to buy it at the price the shops will charge. Don't assume that the shop will want to apply the same mark-up to your product as it does to other brands. The shopkeeper may feel that he or she already stocks sufficient brands of that product and will only agree to stock yours in return for a larger mark-up. This may push the retail price up above the price of Y dollars that similar products are selling for. If you want your product to sell in shops for Y dollars then you may have to sell it to shops for prices less than those you require to make a profit (see also, "Pricing, margins and mark-ups" in Chapter 5).

### **Competing on quality**

Shopkeepers, particularly those running larger shops, usually have a good idea of what their customers want in terms of quality. Customers will not hesitate to tell them if they do not like a product and will sometimes ask them to stock a different brand that they have purchased elsewhere. Ask shopkeepers what they think of the quality of the products they are selling and whether there is a gap in their range that you could supply. For example, village shops may tell you that they only sell concentrated orange juice because juice in cartons or plastic bottles is too expensive for their customers. They may suggest that they could certainly sell juice in bottles if it were not too

expensive. Shopkeepers in urban suburbs may say that customers complain about the quality of the juice they sell and they could sell fresh juice if someone produced it.

You should also ask shopkeepers about the relationship between price and quality. Which of their existing brands sells best? Is this because the price is low, because the product is seen as offering good value for money, or both? If you plan to sell your product at the same price as this popular brand then you may have problems.

### **Sizes available on the market**

It is very important that you fully research the size units competing products are being sold in. You will probably have to sell your products in similar units because:

- that is what people are used to buying;
- packaging is usually only available for those sizes and it is extremely costly to ask a packaging manufacturer to produce an unusual size just for your business. Only the largest companies can afford to do this.

As we noted earlier, processed foods are often sold in two or three sizes. A small size may be used for individual purchases, when people want to consume the product when they are away from home, and a large size is sold for use in the home. Snack foods, sweets or candies, juices, yoghurts, and ice cream are examples of this. The smaller the pack, the higher is the cost of packaging and handling

per unit of product. Thus the retail price per litre of a small pack of fruit juice will almost always be more than the retail price per litre of a large container. Where two different sizes are available you will have to find out from the shops their interest in stocking a new brand of both sizes. A shop may feel that it could sell extra quantities of the small size but not the large size, for example.

Some types of packaging may give agroprocessors the opportunity to vary the weights inside. A snack food bag may normally be used for 50 g of the product, but there is often room to increase this to 60 g or even 70 g. Similarly, it could be possible to reduce the contents to 40 g.

#### ***MARKET RESEARCH HINT***

***Check size information carefully and continue to check it after you start manufacturing***

*Other companies may change the sizes they provide at any time. Such changes are often done in order to avoid putting the price up. For example, a company may sell 50 g chocolate bars for 50 cents. At this price it may have trouble making a profit and want to put the price up to 55 cents. However, if it puts the price up:*

- *people may buy less and buy competitors' chocolate bars instead;*
- *it is less convenient for shops to give change for 55 cents than for 50 cents;*
- *vending machines will have to be reprogrammed. Indeed, they may only accept 50-cent coins;*

- *schoolchildren may be given 50 cents a day pocket money by their parents and would not be able to buy the product if it went up to 55 cents;*
- *supermarkets will have to change display prices.*

*As a short-term alternative, the manufacturer may decide to reduce the size of the chocolate bar to 45 g. Few customers are likely to notice and the price remains the same while giving the manufacturer more profit. This practice is sometimes followed even when customers are certain to notice. For example, in order to keep the price of a pack of cigarettes in a vending machine unchanged, manufacturers have been known to take one or two cigarettes out of each pack.*

However, if you vary the contents of a package, you need to pay attention to the following:

- if the package is half empty consumers will probably feel that they are being cheated. If your competitors use smaller bags but fill them up, consumers will almost certainly buy their product, even if the weight of the contents is exactly the same. Manufacturers are very conscious of not wanting to appear to be cheating consumers. Where a product is likely to settle down in the box or container after being packed (corn flakes for example) it is common for the manufacturers to put a note on the packet such as “box may not be full due to settling”;
- every time you change the weight of the contents you will have to reprint the label to indicate the new weight.

### **Type and quality of packaging and containers**

Your packaging will have to protect and preserve the product. Beyond that, your decision about what type of packaging to use should be based on research among consumers, retailers and wholesalers, as well as on what type of packaging is available to you. If, for example, you are proposing to compete with imported products that use sophisticated packaging you may find that such packaging is not available in your country and that it would be prohibitively expensive to import. Will retailers be prepared to sell your product with less-sophisticated packaging? Will consumers want to buy it? Try to find out why particular types of containers or packages are used. For example, if

clear glass jars or bottles are used, is this because people like to see the product? Would you have trouble selling your product if it was in dark glass, which is normally only used for products that need protecting from the light?

You need to check on the different types of containers that are used and discuss with retailers the types of packaging they prefer and the reasons why. Retailers may want items that can be easily stacked on their shelves and may thus prefer biscuits or snack foods in boxes rather than bags.

Packaging serves three basic functions:

- it protects and helps preserve the product;
- it provides a convenient way to handle and transport the product;
- the package can be used to promote and provide information about the product.

***Product protection.*** Packaging protects a product by maximizing its shelf life. Detailed information on this topic is available elsewhere.<sup>10</sup>

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<sup>10</sup> see, for example, Fellows, P.J. and Axtell, B., “Appropriate food packaging”. (full details in “Further reading.”)

Packaging can protect products from the following types of problem:

- contamination by bacteria;
- surface mould (e.g. in the case of jams);
- contamination by dirt and other impurities;
- physical damage;
- damage from moisture, air and, in some cases, light (e.g. oils);
- evaporation;
- loss of carbonation (e.g. in the case of fizzy drinks).

**Handling and transporting the product.** While many products are still transported and sold unpacked, there is an increasing trend for packaging to be used. This is partly to provide greater protection, for the reasons outlined above, but it is also to provide greater convenience in handling, both for the shopkeeper and the consumer. The growth of supermarkets has been an important factor: supermarkets reduce costs by having relatively few staff and relying on the customers to serve themselves. This requires that most products are sold in packages. In Europe in 1960 it was still common for biscuits, for example, to be sold loose. That has died out and in Europe only a few processed products, such as dried fruits, are now occasionally sold in loose form.

**Promotion and information.** Packaging can be printed or it can have labels fixed to it. Attractive packaging will make people interested in your products. Boring packaging

with handwritten or badly printed labels will make it very difficult to sell the products. The type of packaging used can also be an important selling point. A good-quality container suggests that the contents are of high quality. Poor-quality packaging suggests that the contents are not particularly good, even if that is not the case. Indeed, poor-quality packaging is a common cause of business failure. You have, of course, to decide whether the additional cost of using high-quality packaging, and the higher prices you have to charge, will be compensated for by increased sales.

When visiting shops you need to look closely at the packaging used by your competitors or potential competitors. One of the important things to consider is the “sell-by” date that processors are increasingly putting on their products and which, in some countries, is already a legal requirement. This is used to reassure consumers that they are not buying old stock. It also protects the manufacturer should retailers sell old stock that has safety or quality problems. In such a situation the manufacturer can deny responsibility because the product was sold after its “sell-by” date.

The duration of the “sell-by” date is also very important for retailers. They will usually prefer to stock the brand that has the longest shelf life as this reduces the risk of not being able to sell a product before it passes its “sell-by” date. If your competitors’ products have a shelf life of three months you need to use a manufacturing process and



*An attractive label design featuring a panel of information for the customer.*



*Note that the label provides detailed information about the ingredients*

**Assist the retailer.** In developed countries it is virtually impossible to market a product these days without using a bar code. This code, which is either incorporated in the label or affixed to the side of the package, is used by supermarkets to simplify the check-out process and to assist with stock control (it tells them how many of each item they have sold, so they know when to reorder). Depending on your country you may find that if you want to sell through supermarkets you also need to provide a bar code.<sup>11</sup>

**Provide advice on using the product.** Consumers may need to be told how to use products that are not particularly well known (e.g. different herbs or spices). Manufacturers often include recipes on packets in order to encourage people to experiment with new ways of using their products.

### Brand name

Even if you are a very small producer you should give your product a brand name. A simple label with the word “Jam” will not be very helpful in the long term. If people like your jam they will want to buy it again. To do this, they need to be able ask the shopkeeper for it. Trying to buy jam by saying “well, the label was white and it had the word Jam written on it and it was in a jar and it really tasted good with lots of strawberries...” may work if the

<sup>11</sup> Information about national organizations administering bar codes can be obtained from EAN International at: <http://www.ean-int.org/index800.html>

consumer goes back to the same shop, but will be useless anywhere else. It's far easier if the consumer can ask for the product by name, for example, "do you have Joe's Strawberry Jam?"

Furthermore, if you are producing a wide range of items, people who are impressed with your jam may want

*People who like one of your products  
are likely to try others as well ...*



to try your other products. You need to have a brand name so that people will know, for example, that the mango juice they see in a shop is made by the same processor who makes great jam. This recognition will be helped further if your labels are all designed in the same way. You could put a picture on the label and use an attractive design for the brand name.



*... a distinctive brand name and label  
will help to identify them.*



## REACHING CONCLUSIONS

The market research outlined in this chapter should have enabled you to answer a number of important questions about the market, such as:

- the price at which you need to sell your products in order to compete with other brands already on the market;
- the importance of price and quality in different locations;
- the different sizes in which other brands are sold, and in which you will probably have to sell your products;
- packaging requirements and the packaging used by other brands with which you will compete.

Following this and earlier research you should be able to reach some basic conclusions about how to present your product to the market, such as:

- price is very important with jam purchases and people will not be willing to pay more for my jam than other brands. Based on the present market prices, the maximum retail price for my jam should be \$1.00;
- most yoghurt sales are in small pots. I had been planning to sell my yoghurt in family-size pots but this will really limit my potential sales;

- all snack foods on the market are imported. The quality of the packaging is better than I can buy locally but if I import my packaging it would be too expensive. I need to do some trials to see what consumers think of the packaging that is available.

By now you should have a good idea of the structure of the market and how your products could fit in. The next stage is to work out how to distribute them.

**5 How should your product be distributed?**

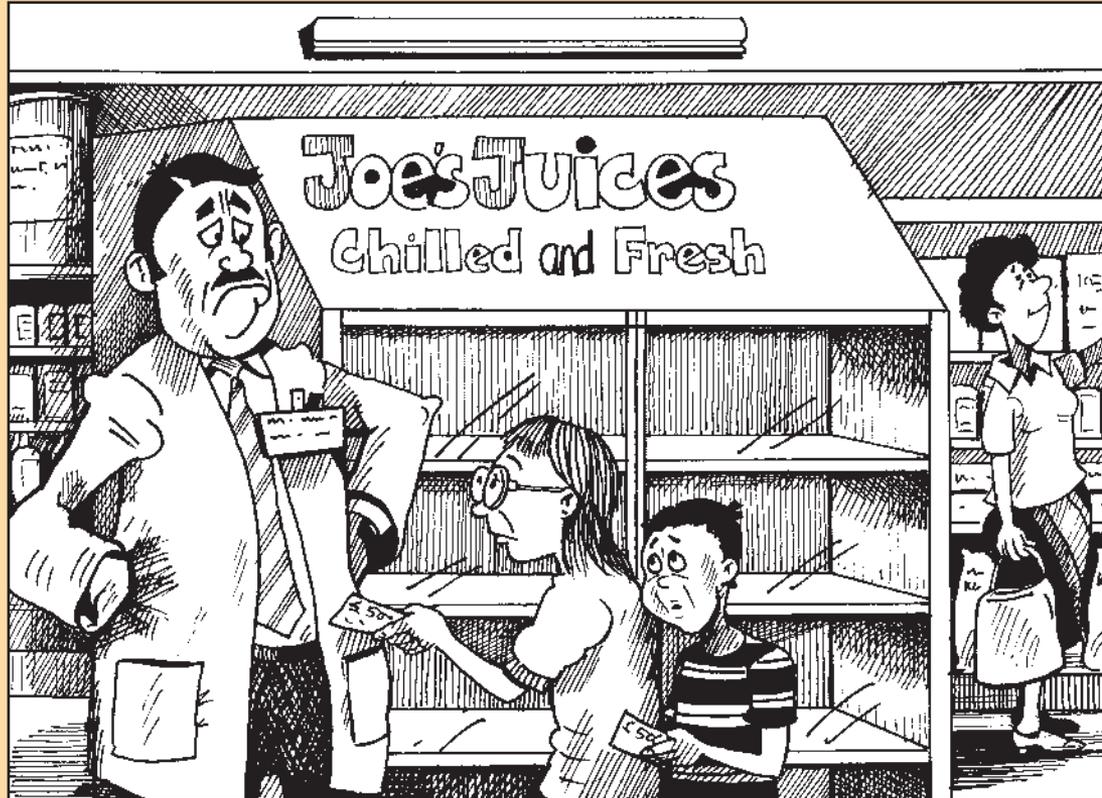
*Main points in Chapter 5*  
**How should your product be distributed?**

*Agroprocessors have a number of options for distributing their products.  
Market research can identify the most appropriate.  
Distribution can be ...*

- *direct to consumers, which may be a suitable option for smaller processors covering small areas;*
- *to all suitable retailers in an area;*
- *to supermarkets, if they find the product acceptable and sufficient quantities can be delivered;*
- *to wholesalers, suitable for larger processors;*
- *to institutions and the catering trade.*

*Factors to be considered in deciding  
on the marketing channel(s) to use include ...*

- *quantities processed and quantities required by distributors;*
- *transport arrangements;*
- *margins and mark-ups;*
- *payment arrangements.*



*When deciding on which retailers to supply,  
you must be sure that you can keep  
their shelves stocked at all times*

## POSSIBLE DISTRIBUTION CHANNELS

By now you should have covered the issues related to the product and to the potential consumers. You have surveyed the market size and consumer tastes and identified those categories of consumer likely to buy your products. You have decided on the packaging and unit sizes. You have chosen a brand name and identified what needs to be printed on the packets or labels. You have found out what prices competitors' products are being sold at to consumers and what the shops are paying for them. With this information you have concluded that you may be able to sell your products profitably. However, you still need to consider how the items you produce are to get from your processing facility to the consumer. This requires further research. Possible distribution channels are selling:

- directly to consumers;
- to retailers;
- to supermarkets;
- to wholesalers;
- to institutions and the catering trade.

### **Selling directly to consumers**

This can be done from a small shop, usually attached to the processing facility, or at the local retail market. It is usually only an option for very small-scale processors although, in some countries, medium and large-scale producers do sell

directly to consumers by using mail order or teams of door-to-door salespeople. The advantages of selling directly are:

- you can keep the full retail selling price and do not have to pay the margins of wholesalers and retailers;
- in other retail shops your products will just sit on the shelves waiting for someone to buy them, but in your own shop you can actively “promote” your products;
- you may not have to provide packaging for some types of product;
- you have few transport problems;
- you can talk to your customers and find out what they think about your products. They may even suggest ways in which you can improve them.

On the other hand, if you are going to sell directly to consumers you will:

- have to do it yourself, in which case the time you have to spend selling is not available to you for processing. This limits how much you can produce and your ability to expand your business; or
- have to employ someone to sell for you. Unless you are confident of selling a large number of products in a shop or market, for example if your shop is on a busy main road, this may cost you much more than paying the margins of the shopkeepers;
- have trouble expanding your business, as selling in just one or two locations limits the total quantities you can sell.

## **Selling to retailers**

The advantages of using shops to sell your products include:

- you can sell greater quantities because your products are on sale in many more locations than if you were doing your own marketing;
- you can devote most of your time to processing, which is what you are best at.

Offsetting these benefits are the facts that you do not receive all of the retail selling price and that you have to organize transport of your products to the retailers and ensure that they do not run out of stock.

## **Selling to supermarkets**

Supermarkets are a particular type of retailer. Some are independent companies with just one or two shops. These can be considered as large retailers and you can usually distribute to them as you would to other retailers. However, supermarkets are often part of a large chain. Selling products through such chains can cause considerable problems for small and medium-sized processors.

Reasons include:

- supermarket chains are often reluctant to sell other than popular, well-advertised brands and, occasionally, their “own brands”. They give priority to brands with a high turnover;

- chains often require their suppliers to supply all their shops and may specify minimum quantities, which can be difficult for smaller processors;
- chains may require deliveries to a central warehouse, which may be a long way from the processing factory;
- chains can sometimes be very slow to pay!

## **Selling to wholesalers**

In your discussions with retailers you need to find out whether there are wholesalers operating in your area and, if so, who they are. You can then contact the wholesalers to find out which areas they supply and to obtain other important information, as discussed below. The advantage of working with a wholesaler is that you usually only have to make one delivery to one location. For example, you may be able to make a delivery to a wholesaler once a week, for which you could hire a vehicle and driver for a few hours. Supplying lots of individual retailers who are spread out over a large area may mean that you have to operate your own vehicle every day, which can be costly. Another advantage is that wholesalers visit, or are visited by, a large number of retailers and are thus able to give your products much greater exposure and sell them over a wider area than you could do on your own.

The disadvantages of using wholesalers are that they may require large minimum quantities that may be difficult for you to supply. Also, of course, they need to make a profit from their activities and need to take a margin. This further reduces the share of the retail selling price available to you.

*Your sales need not only be through shops.  
Restaurants and fast food restaurants  
may also be possible outlets for your products.*



### **Selling to institutions and the catering trade**

For ventures that are neither very small nor large enough to finance an expensive promotion campaign, selling to institutions can be an attractive option. Institutions, such as schools, hospitals, prisons and military bases, can be supplied under fixed agreements which permit you to know in advance how much you will sell. Also, if you can supply institutions you do not have to worry about promotion. One drawback is that governments are often very slow to pay their bills. However, you should certainly visit all the

institutions in your area to see if they are interested in your products.

Similarly, you should survey restaurants and fast food outlets to identify their requirements for processed foods. The questions you need to ask are very similar to those you would ask retailers.

### **DECIDING ON THE CHANNEL OR CHANNELS**

This should be discussed carefully with retailers and wholesalers. Combining some limited direct sales with sales to retailers should cause few problems. For example, for a small dairy it should be possible to sell milk and dairy products directly to consumers in your village as well as supplying retail shops in neighbouring villages. Combining sales to both retailers and wholesalers may be possible, but it may also cause problems. In some cases, for example, very large supermarkets may not want to deal with wholesalers and will expect you to deliver direct to their shop(s) or warehouses. Even small shops may prefer to get all their supplies from one wholesale source, in preference to dealing with individual small suppliers. Where there is more than one wholesaler in an area, each may demand sole distribution rights for that area. This means that for one of them to agree to stock your products you

have to agree not to supply retailers and other wholesalers. No wholesaler will want to do business with you if you also want to supply retailers directly, unless you have a clear agreement from the beginning about which retailers you can supply.

During your discussions with wholesalers and larger retailers you need to find out what conditions they will attach to selling your products, as discussed below. On the basis of this information and an understanding of the mark-ups that particular retailers and wholesalers require, you can begin to work out which channel, or combination of channels, is likely to suit you best in terms of maximizing the sales you can make at prices that will be profitable.

## DELIVERING YOUR PRODUCTS

Wholesalers and retailers may not have much storage space available. Very small retailers, for example, may only have the space they use for selling to consumers, with no additional storage room. In such circumstances they will not be happy to sell your product if you only want to deliver once a month, as they have nowhere to keep it. Also, they probably have problems in paying for a month's supply in one go. They may ask for weekly deliveries or, if you insist

### ***MARKET RESEARCH HINT*** ***Identify the quantities that you can deliver to retailers at any one time***

*As well as estimating the total market size for the items you plan to produce (see Chapter 2) you also need to work out how many of your products you can sell to individual retailers at any one time. Find out from the retailers how frequently they receive deliveries from your potential competitors (daily, weekly, fortnightly, monthly, etc.) and the total quantities they buy each time. Assume, also, that when retailers agree to sell your products they will, at least in the short run, continue to sell the brands they are already selling.*

*To get some idea of the likely size of your sales to a retailer divide the total quantities purchased by the retailer by the number of existing suppliers plus one (i.e. you). Unless your company is large enough to do advertising, or your products are significantly cheaper or you give additional margins to the retailer, this is likely to be the maximum that you could sell at the beginning. The result of your calculation should enable you to work out which size of retailer would be able to take quantities that are viable for you to deliver or whether it would be better to supply retailers through wholesalers.*

on delivering once a month, require you to offer them credit for that period, so increasing your costs.

When you are delivering non-perishable items to small retailers in urban areas you can agree to sell them quantities that reflect what they sold in the previous week. For example, if a small retailer normally takes two cartons of your potato chips but didn't sell many in the previous week, you, or your salesperson, can deliver one carton instead. This clearly doesn't apply to rural areas as you may drive 20 km to a shop, only to find out that it wants nothing! When your products are perishable, particularly when you have to make deliveries on a daily basis (e.g.



*Many shops can only take small quantities at a time ...  
... be careful not to oversupply them.*

milk), you want to be sure that you can sell everything you produce. You need to discuss with retailers their willingness to take delivery of an agreed quantity every day. Without such an arrangement you could face big problems in disposing of the surplus.

If your research makes you believe that it would be uneconomic to supply small shops directly, or if you find that small shopkeepers buy all their supplies from wholesalers, then you have to look at the delivery requirements of larger stores and/or wholesalers. It is important to note that **supermarkets do not like to have empty shelves and wholesalers do not like to tell their retail customers that they are unable to supply a particular item.** You need to be sure that you can supply the minimum quantities that they require. If you start delivering to a supermarket or to a wholesaler and are unable to continue to supply the agreed quantities, then those buyers are unlikely to want to buy from you again. If you later increase your production capacity so that you can meet their minimum quantity requirements you will have a lot of trouble persuading them that you are reliable.

Supermarkets and wholesalers do not like having “old” stock even if it is not past its “sell-by” date. Thus, for some more perishable products they may insist that every time retailers make a delivery they take away any unsold stock, even if it has not reached its “sell-by” date. This can mean a considerable cost for agroprocessors. Under these circumstances you will need to be careful that you only

supply such companies with quantities they are likely to be able to sell.

### **Shipment or distribution containers**

By “shipment or distribution containers” we refer here not to the packs or containers that go on the retailers’ shelves (see Chapter 4) but to the packaging in which those containers are delivered. You need to find out what sizes of carton, sack, bag, barrel, etc. your competitors are using and whether the wholesalers and retailers are happy with these. Remember that the containers you use should not be too large, particularly if you plan to supply small shops, or wholesalers who sell to small shops. In northern Iraq, for example, one factory ran into problems because it was supplying retailers with cartons containing 15 cans of tomato paste. Competing factories were all supplying six cans per carton.

In deciding on the size of the containers to use, you need to refer to your estimates of the quantities different types of retailers are likely to order (see above). Wholesalers usually prefer to deliver to retailers in the packaging that the producers provide. Therefore, the number of units you provide per carton, etc. must be consistent with the quantities retailers are going to want to buy at any one time. For example, very small retailers who sell eight or nine cans of pineapple every week will probably want to buy either one or two cartons containing six cans every week. They will not want to buy a carton containing 36 cans.

### **Transporting your products**

Having decided to where you want to deliver your products and having learned of the requirements of those you hope will buy from you, you now need to identify your transport requirements. As noted above, if you think you will have to supply a large number of small retailers with daily or weekly deliveries, you may need to buy and operate your own vehicle. On the other hand, if you intend to supply just a few large shops or one or two wholesalers you may be able to make arrangements with a local transporter to deliver your products once a week.

It is important to make a detailed study of your transport costs. Although supplying small retailers may be your preferred method of distribution you may find that the costs of supplying small quantities to some or, indeed, all small retailers are so high that the prices you have to charge will mean consumers will not want to buy your product.

In your discussions with wholesalers and/or large shops you should find out at what times they accept delivery. Some, for example, may only receive goods between certain hours or on certain days. You also need to identify the delivery procedures. Does the wholesaler assist with the unloading or does the company expect you or your transporter to unload everything?

Once you have all this information then you can approach transporters in your area to find out whether they can provide the service you require at the times you

require it. You can also get some idea of the likely costs. Transport for food products must be sanitary, covered and preferably only used for food products.

## **PRICING, MARGINS AND MARK-UPS**

This subject requires detailed discussion with potential customers. The ways in which you can work out your selling price are discussed in Chapter 8. However, at this stage of your research you need to find out from wholesalers and retailers what their approaches to pricing and margins are. You need to get as much information as possible about the prices that wholesalers and retailers presently pay for those brands that would compete with your planned products, and the mark-ups they apply. You need to discuss whether they would pay the same prices and apply the same mark-ups for your products or whether they would expect to pay less and charge higher mark-ups because they would be taking a risk by stocking new products. Figure 4 illustrates the concept of margins and mark-ups.

The price that wholesalers and retailers are prepared to pay and the mark-ups they require are likely to depend on several factors.

Some of these are:

- speed with which the product is sold;
- quantities that can be sold;
- range of products to be stocked;
- the strength of the manufacturer;
- the strength of the retailer.

### **Speed with which the product is sold**

If businesses expect to stock products for a long time before selling all of them, then they require higher mark-ups. Low mark-ups are required for products shopkeepers are sure they can sell quickly (e.g. carbonated drinks). The more often shopkeepers can buy and sell, the more profit they can make.

### **Quantities that can be sold**

Wholesalers and retailers often accept a lower mark-up for products that can be sold in large quantities. This may be a condition imposed on them by the manufacturer, but they may also find that lowering the price can increase overall sales and, hence, their revenue.

### **Range of products to be stocked**

The range of products is a factor contributing to the speed with which they are sold. Shoe or clothing retailers, for example, have to stock a large number of items so they have available the style and size that everyone wants. They therefore expect higher mark-ups.

*Figure 4*  
**Margins and mark-ups**

	<i>price</i>	<i>% of retail price</i>	<i>margin (%)</i>	<i>mark-up (%)</i>
Ex-factory price	75	62.5		
Wholesale selling price	90	75.0	12.5	20.0
Retail selling price	120	100.0	25.0	33.3

From the above it can be seen that the “margin” is calculated with reference to the final selling price. It is the percentage of the retail selling price retained at each stage of the marketing chain. The “mark-up,” on the other hand, is calculated with reference to the buying and selling prices at each stage of the marketing chain. It is the percentage difference between the price a company pays for a product and the price it sells it at. Thus, in the example above, the retail margin is  $[(120-90) \div 120] \times 100$  or 25 percent, while the retail mark-up is  $[(120-90) \div 90] \times 100$ , or 33 percent. The concept of “margin” is useful when you are looking at the profitability of your business. However, in dealing with shopkeepers you will nearly always be discussing their “mark-ups,” i.e. by how much they want to increase the price when selling your product.

### **The strength of the manufacturer**

Larger companies, particularly those with well-advertised and well-known brands, can often negotiate very favourable arrangements with distributors. Some brands are so famous that shopkeepers have no alternative but to sell them if they want to attract customers. In this situation the manufacturers can often dictate the maximum retail selling price, and hence the mark-up, although in some countries this practice is illegal. Small agroprocessors, on the other hand, are in a position of some weakness when negotiating with distributors, particularly when there are several other suppliers of the same product.

### **The strength of the retailer**

Large supermarket chains are extremely powerful in many countries. They sell a high proportion of foodstuffs and are able to buy from manufacturers at very favourable prices. As a result they can retail the products at prices much lower than can smaller retail shops **and** charge profitable mark-ups. Even in rural towns, a large supermarket is in an extremely powerful buying position in dealing with a local agroprocessor, because of the quantities it can purchase.

## **TERMS AND CONDITIONS OF PAYMENT**

This is an extremely important subject. Payment terms and conditions can make the difference between profitability and bankruptcy, particularly in countries with high inflation or high interest rates. If you have to wait for payment from the businesses that you supply you may:

- have to delay payment to your suppliers, for example the farmers or wholesalers who sell you the raw materials;
- have to borrow money from the bank to pay your suppliers and staff; or
- have to use your own money to pay your suppliers and staff when it could be in the bank earning interest.

All over the world companies that are basically profitable occasionally run into “cash flow” or “liquidity” problems. This means that what they must pay out to their suppliers is not being matched in the short run by what they are receiving from their customers (if it is not matched in the long run they will, of course, go bankrupt). This is discussed in more detail in Chapter 8.

Small retailers may pay in cash when you deliver to them. Larger shops, supermarkets and wholesalers, on the other hand, almost certainly will not. They normally expect you to post them an invoice and undertake to pay

within a certain period. In some cases this period can be up to 90 days. You need to clarify with these businesses the exact length of credit they require. It is also a good idea to check with existing suppliers to wholesalers or shops in order to find out whether those businesses do in fact pay within the agreed period. When a company is very slow in paying there is little you can do about it. You can stop supplying the company but taking legal action will often cost more than the sum you are owed.



## REACHING CONCLUSIONS

You should now have a good idea of the channels that are likely to be the most profitable for you. Such information should include:

- the advantages of selling direct to consumers compared with through distributors;
- the benefits of supplying retailers direct compared with wholesalers;
- the advantages of selling to caterers, small retail shops or to large supermarkets;
- how to deliver products, when and in what quantities;
- pricing and payment arrangements.

You can then make some informed conclusions, such as:

- the quantities of orange juice I shall produce will be too small for wholesalers and the local supermarket chain to handle. I shall have to concentrate on supplying small local retailers and one or two restaurants and fast food shops;
- I can deliver my weekly production of tomato sauce to the wholesaler in one morning, using a hired truck. Delivering to retailers will take five days a week. I need to calculate whether the cost of delivering to retailers is greater than the margin I will have to give the wholesaler.
- I can produce sufficient jam to supply my local supermarket chain. Although this company will pay less than smaller retailers, I can deliver to all its shops on one day in a week and my costs will be much less. The local wholesaler requires larger quantities than I can supply.



**6 How should you promote your product?**

*Main points in Chapter 6*  
**How should you promote your product?**

*However good the product, it is unlikely to sell itself.  
Advertising and promotion are required.  
The chapter discusses researching ...*

- *types of promotion, including advertising, point-of-sale displays, free samples and price reductions;*
- *promotion carried out by competitors;*
- *how competitors advertise their products;*
- *what arrangements are usually made with distributors for in-store and other promotions.*



*A promotional presentation, such as a point-of-sale display, will help identify your products to consumers.*

## PLANNING PROMOTION

You should be thinking about how to promote your product a long time before you start producing it. Your visits to shops and interviews with shopkeepers and wholesalers will give you an opportunity to find out what sort of promotion your potential competitors are doing and what sort of promotion you could organize with shopkeepers.

### Types of promotion

The word “promotion” covers a range of activities to make people aware of, and want to buy, your products. Examples of techniques that are used around the world include the following:

- advertising;
- point-of-sale displays;
- free samples;
- word-of-mouth;
- coupons;
- tokens;
- special prices;
- free publicity.

**Advertising.** This can be on radio or television, in newspapers or magazines, on posters and billboards, or by using leaflets handed out in the street or delivered to homes. For small agroprocessors, television and national

newspapers are not realistic options, but other approaches could be used. In many countries the number of rural radio stations is expanding rapidly, and these may offer the possibility of relatively low-cost advertising.



*A design suitable for a poster or a leaflet hand-out can be reduced in size for a newspaper or magazine advertisement.*

**Point-of-sale displays.** These are special displays of a product or range of products inside a shop. In addition to the products being on their usual shelves, they are displayed at other locations, often, in the case of supermarkets, near the check-out area. A printed cardboard display stand could be used, possibly with posters and banners, which can be displayed around the shop.

**Free samples.** This technique is particularly useful for new products. People may be reluctant to try something new when they see it in a shop, without having first tasted it. In developed markets companies often deliver small samples of their new product to every household in a country. Agroprocessors could consider handing out samples at shops for people to taste when they are going in. This would have to be done in conjunction with a good point-of-sale display.

**Word-of-mouth.** For small processors this can often be very effective. You can organize parties and gatherings at your home or at the homes of employees and friends, in order to taste your products. If people like them they will, in turn, tell their friends about them.

**Coupons.** Manufacturers sometimes include coupons on their packaging. These can be used by consumers to get a reduced price on their next purchase. Coupons can also be included on leaflets. The use of coupons does, of course, require the cooperation of shopkeepers,

*Free samples can be an important way of drawing attention to your product.*



for whom collecting the coupons and returning them to the manufacturer for reimbursement can mean a lot of additional work.

**Tokens.** Another technique is to include a small token on each packet or container. When people collect a specified number of tokens they can take them to the shop or return them to the manufacturer to receive a gift. Again, such promotions often require the cooperation of the shopkeeper.

**Special prices.** Reducing prices can be used as a short-term promotional technique. However, it is not enough just to cut your prices and have your product on sale for less – you have to tell people you are doing so. Thus price reductions have to be used together with other promotional techniques, such as advertising, and in-store displays.

**Free publicity.** Local newspapers and radio stations often look for local news items. They may be very pleased to do an article about your new factory. Make sure you don't approach the media before your product is on sale. An article in the newspaper that "Joe is going to open a juice factory in six months" will not do you much good and may alert potential competitors. An article such as "*Joe's Juices go on sale today*" will, on the other hand, be valuable free publicity, particularly if you can get the reporter to name some of the shops where your product is on sale.

These are examples of promotion to consumers. However, you also need to promote your products to retailers. Perhaps the best way of doing this is to convince them that your promotion activities for consumers will result in very good sales, so they will make money by selling your products. Another way is to offer special discounts for your first sales to a particular retailer (see Chapter 8). Free samples can also be used to attract the interest of shopkeepers in stocking your products (see Box 4). Gifts, such as pens or key rings, with the name and logo of your company on them can also be used. Many countries have specialist companies that supply such gifts.

### Promoting cassava chips in Tonga

The author of this guide once worked in the South Pacific island nation of Tonga. An FAO project assisted with the establishment of a food processing plant that, among other processed products, developed very tasty chicken-flavoured cassava chips. Promotion on the main island of Tongatapu was carried out by visiting all of the numerous small shops or kiosks on the island to give the shopkeepers two free packs of the chips, together with a leaflet telling them where they could buy the chips in wholesale quantities, and the prices.

Most promotional activities have a cost. Smaller agroprocessors may find that they just do not have the financial resources to do many of the activities outlined above. They may have to rely on free publicity through word-of-mouth or stories in the local media. Even very large companies have to balance carefully the cost of promotion against the likely benefits in terms of increased sales at profitable prices.

### What type of promotion is being done?

During your research, visit as many shops as possible, even if you do not interview all the shopkeepers. You should look closely at the techniques used for promotion by all manufacturers, particularly those who will be your competitors.

Look to see what is on display in the shops, such as:

- posters;
- leaflets;
- banners;
- point-of-sale displays;
- special price offers.

You should ask shopkeepers what types of promotion they have been involved with, and why. If small shops have one or two posters on display, for example, it would be useful to find out why they are displaying those posters in preference to others. Which promotions do shopkeepers feel to have been the most successful, and why?

### **Messages of your competitors' advertisements**

You need to consider not only how your competitors promote but also what features of their products they highlight in their advertisements, and which features of your product you would like to highlight. Examples of the type of language used include:

- healthy and nutritious;
- luxurious;
- smooth tasting;
- easy to use;
- full of fruit;
- 100 percent natural;
- a product for the élite;
- good or best value.

### **Arrangements for promotions**

You need to understand the agreements made between the manufacturers and wholesalers and/or retailers. For example, if products are offered to consumers at special prices, does the manufacturer expect retailers to reduce their margins for the duration of the promotion? What conditions do larger retailers attach to the use of point-of-sale displays? What financial and other agreements need to be reached to hand out samples inside or outside shops? Is the processor expected to provide the staff to hand out the samples, or is this arranged by the store?

Your discussions with shopkeepers should be aimed not only at finding out the types of promotion that are carried out but also the likely cost of such promotions to

#### ***A WORD OF WARNING***

*Do not promote your product before you have sufficient quantities ready for sale. This is a common mistake of processors and it means that:*

- 1. Consumers will be frustrated when they cannot find the product in the shop.*
- 2. Retailers will be annoyed that they are out of stock.*
- 3. When you do, finally, have enough to sell you will have to do more promotion.*

you. For example, when special price offers are made, by how much is the price normally reduced? How long do in-store promotions with free samples usually last, and how much is it likely to cost you to provide enough samples?



## **REACHING CONCLUSIONS**

Your research should have given you a good idea of the types of promotion carried out in your area both in general and for the types of product you plan to produce in particular. You can then reach conclusions such as:

- promotional activities are rare in my area. However, I shall have to do something to make sure people learn about my new yoghurt. The best method is probably to print some colourful posters, which I can ask the retailers to display;
- all the other carbonated drink producers do lots of advertising. To compete with them I shall have to do radio advertisements and provide banners and posters to the retailers;
- I cannot afford to advertise my honey. But the new FM radio station is always looking for news stories. I shall visit them with some samples of my honey and information about where people can buy it.

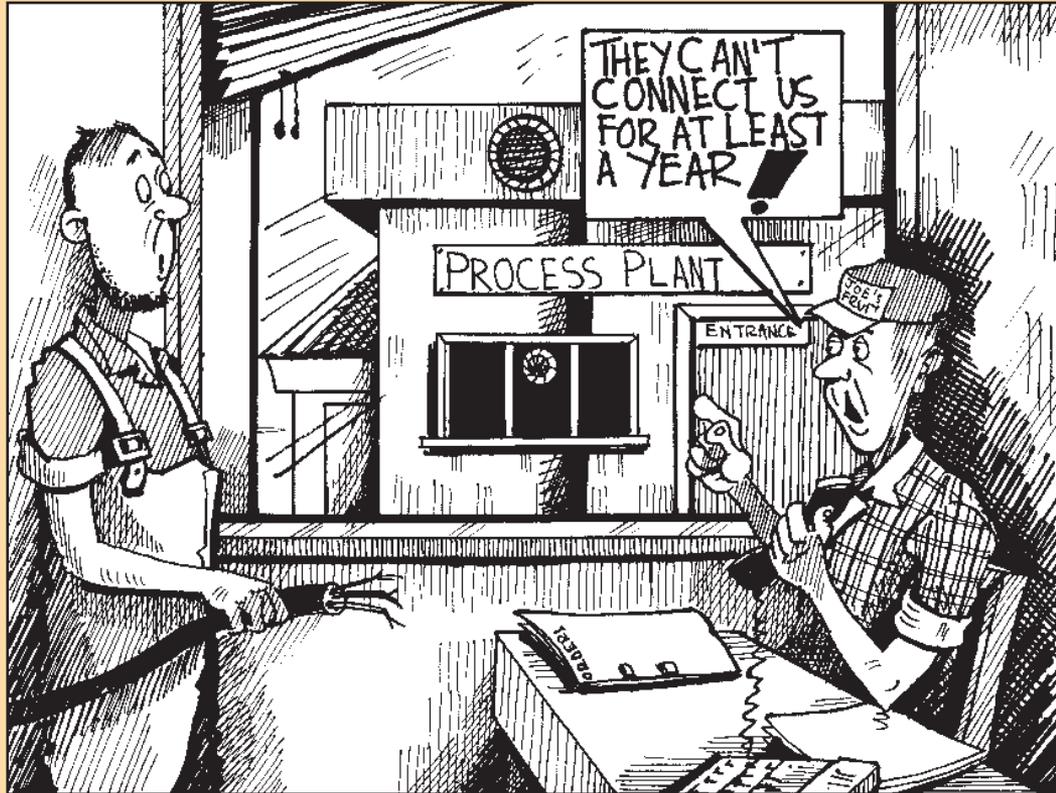
**7 Are your agroprocessing plans feasible?**

*Main points in Chapter 7*  
**Are your agroprocessing plans feasible?**

*Prior to making expensive investments  
agroprocessors need to research not only the market  
but also all aspects of their production process.  
The chapter briefly reviews ...*

- *identifying the raw material supply;*
- *production location and product quality;*
- *buying costs;*
- *price and price seasonality;*
- *research sources and costs of other processing inputs;*
- *identifying sources and costs of packaging and label design and production;*
- *deciding on the equipment to be used;*
- *researching suppliers and cost of equipment;*
- *organizing factory rental or construction, and utility supplies;*
- *clarifying labour requirements, costs and availability;*
- *planning distribution arrangements.*

*Delays in completing a factory  
can make the difference between success and failure.*



*Inputs and utility supply need to be researched  
before investments are made.*



## CAN YOU MANUFACTURE?

By now you have completed your market research and have a good idea about the potential markets for your products and the prices at which you can sell them. Before being able to calculate whether you can supply those markets profitably (see Chapter 8) you need to do a different kind of research. You must examine whether it is possible to manufacture your products on a commercial scale and what the costs of this will be. This research is just as important as the market research described in the earlier chapters and involves looking at the supply and cost of everything you require for the manufacturing process.

Some of the items that must be considered include the following:

- raw materials;
- other processing inputs;
- packaging and labelling requirements;
- equipment;
- buildings and utilities;
- labour;
- distribution and promotion;
- other requirements and costs.

## Raw materials

A common mistake is for agroprocessing facilities to be constructed because there is a surplus of raw materials. For example, someone might decide to build a tomato-paste factory because farmers are producing too many tomatoes. The opposite also occurs: factories are built when there is insufficient raw material, on the assumption (which is often faulty) that the existence of the factory will encourage farmers to produce. An important issue, which frequently receives inadequate attention, is the subject of seasonality. If tomatoes are only available for three months of the year, what is the factory going to do for the rest of the year? If you make sizeable investments in equipment you will want those investments to be earning you money throughout the year, and not just for a few months.

The importance of the availability of raw materials does, of course, vary according to the size of your processing plant. A very small operation may consider processing activities a part-time operation to be done when supplies of raw materials are available. However, organizations that have a factory, special equipment and permanent staff need to be very concerned about whether they will be able to buy sufficient raw materials. They need to research the availability of fruits and vegetables, milk, meat, poultry, etc. and relate this availability to the size of their planned processing operations. Even if a market for the finished product were available, it would make little sense to buy a

piece of equipment capable of processing one tonne a day if the maximum availability of the raw material was likely to be half a tonne a day.

For the raw materials you want to process you therefore need to research the following:

- the production in your area and the seasonality;
- the existing markets, the location of the farmers and buying costs;
- the prices of the raw materials;
- the quality of raw material that you can obtain;
- price seasonality;
- the scope for farmers to increase production.

**Production and seasonality.** Possible sources of information include the local agricultural extension service and local retail or assembly markets. Local offices of the Ministry of Agriculture may not have detailed information about production levels but should be able to tell you where the most important farmers are to be found. A crop calendar, which shows the seasonality of production, may be available. Larger retail markets may keep records of how much of each product is sold, although this is unlikely. The best way of getting information is probably by talking to the farmers and retailers who are selling in local markets. When are the products you are interested in considered to be abundant and when are there shortages?

**Existing markets, farmer locations and buying costs.**

Where do farmers presently sell their produce? Do traders visit them at their farms or do the farmers visit local markets to sell their products to consumers or to retailers? This is important information. Will you have to visit farmers in their fields to obtain your raw materials or would farmers deliver directly to your factory? What is the location of the farmers presently producing the crops that you need? How often do you need to visit them (some products may require processing almost immediately after harvest) and what are the transport and other buying costs?<sup>12</sup>

**Raw material prices.** Where countries have national or local market information services you can use these to get information about the prices you may have to pay, particularly when they publish annual reports that can give you price trends over several years. If such information is not available, you should use your own knowledge of local market conditions, and supplement this with visits to markets to talk to the farmers and traders. One thing you may need to consider carefully is the impact your purchases could have on the market price. If your processing venture is only going to buy one or two percent of production in your area there is no need to worry. If, on the other hand, you expect to buy something like 20 percent of the crop, your purchases will almost certainly push up the price farmers expect, so increasing your costs.

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<sup>12</sup> See Shepherd, Andrew W., "A guide to marketing costs and how to calculate them".

**Raw material quality.** You will not get a high-quality product if you do not start with a high-quality raw material. When you plan your business you need to have a clear idea of the variety, size and other characteristics of the products you plan to process. You must then make sure that the available raw material matches these characteristics.

**Price seasonality.** Seasonal production results in seasonal prices. At the peak of production prices can be very low; when production goes down prices can rise to much higher levels. You need to work out in advance the likely periods when you can buy produce at prices that are profitable for your venture. This means that you have to carry out detailed calculations of the profitability of your factory's processing operations at different buying and selling price levels (called a "sensitivity analysis" – see Chapter 8). For much of the year there may be no produce available or the price may be so high that you cannot process it profitably. The operations of your factory will depend on how much you can buy when prices are low and on how long you can store it properly before processing, as well as on the range of raw materials you are processing (particularly if they have different seasonal production patterns).

**The scope for farmers to increase production.** Your investigations may lead to the conclusion that, at existing production levels, you may not be able to purchase sufficient quantities of a product for your planned

operations, at prices that will be profitable. One way round this problem may be to work with local farmers, possibly through the extension services, to ensure that they produce adequate quantities. This may require some kind of contractual arrangement with the farmers, as they are unlikely to increase production without a guarantee that they can sell the output. Clearly, very small processors cannot consider such an arrangement, but larger companies may find that it is in their interests to reach agreement with farmers.<sup>13</sup>

### **Other processing inputs**

Agroprocessing requires more than the basic raw materials such as fruits and vegetables. You may need products such as cooking oil, flavourings, vinegar, sugar, salt, citric acid or other preservatives, gelatine, yeasts, pectin and baking powder. While some of these may be easily available in rural areas, others may be more difficult to obtain. Before you start processing you have to identify sources for such inputs and be sure that the inputs will be easily available when you require them. Failure to do this could be disastrous. For example, you may buy a large amount of fruit only to find that you cannot process it because you have run out of sugar. Consumers are often very sensitive to the taste of a product. Once you have developed a product it needs to remain consistent if you

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<sup>13</sup> For more information see, for example, Eaton, C.E. and Shepherd, A.W., "Contract farming – Partnerships for growth," (details in "Further reading").

*Make sure that you have  
a reliable supply of all ingredients.*



*Customers will soon realize  
if you have to change the formulation.*

are to keep the loyalty of your customers. This means that you have to use ingredients of equivalent characteristics and quality. If, for example, you make chips it could be disastrous to change the type of cooking oil and the brand of flavouring that you use, as customers would soon notice. This means that you have to be sure you will not run out of your preferred ingredients.

In addition to identifying sources of processing inputs, you need to find out how much they cost, in order to calculate the viability of your planned production. You should also find out what the payment terms of the suppliers are. Do you have to pay cash? What are the minimum quantities they supply? Do they give discounts for larger quantities?

### **Packaging and labelling requirements**

Your market research should have given you a good idea of the packaging you need and the sizes required. As with other inputs, you need to make sure that these are easily available. In many countries, and in remote areas of all countries, this may not be the case and considerable effort may be necessary to identify potential suppliers. Many smaller countries may have to import glass jars and bottles, plastic containers for yoghurt, and bags suitable for snack foods, for example. In such circumstances you would be taking a big risk to rely on such essential items arriving at the last moment and it is best to ensure that you have them in stock before you start processing your raw materials.

Packaging can be a major cost. In some cases the packaging may cost more than the cost of the raw materials. You therefore have to pay close attention to your packaging purchases. The quality must, of course, be good enough to protect your product but you should not buy a higher quality than you need as this will put up costs. You need to identify all suppliers, learn about the qualities of packaging they can offer, the sizes they can supply and their unit prices for different quantities. You should also check how long it takes them to deliver.

Where you plan to use labels these need to be designed. Many countries have legal requirements regarding the information that should be presented on labels and you need to find out what these are. In the same way as you try out the taste of your products on consumers before finalizing the recipe, you should also test the appearance of your labels with consumers. Labels then have to be printed. Finding a supplier of suitable labels, working out an acceptable design and getting the labels printed can take much longer than you might expect. You must be certain that the labels will be ready before you start to process and, again, you need to know the costs of label purchase, design and printing in advance, as these will form part of the calculations of profitability.

### **Equipment**

Agroprocessors often have to buy specialized processing equipment. This can be difficult to find and, because demand for such equipment is limited, can be very

expensive. Except for the largest countries, much of this type of equipment is not manufactured locally and has to be imported. Costs can be considerable and would-be processors need to have full information about them. In order to work out the profitability of the planned venture it is also useful to have an idea of how long each piece of equipment can be expected to last. This can have a big impact on profitability. A piece of equipment costing \$10 000 and lasting ten years costs \$1 000 a year. If it only lasts five years it costs \$2 000 a year. You also need to estimate the annual servicing, maintenance and running costs.

### **Buildings and utilities**

You will, of course, have to decide on the size and capacity of the equipment to be purchased. You certainly do not want to buy costly equipment that is much bigger than you need. On the other hand you can't afford to buy equipment that is too small. Just one piece of equipment that is too small for your processing line can cause major bottlenecks.

Processing has to be carried out somewhere. Except for the smallest ventures, agroprocessors will have to either build or rent a building or use an existing one that they own. It can be difficult to work out the cost of a new building without a detailed design and, therefore, the annual rent of similar buildings is often used when doing feasibility studies. You need to find out the cost per square meter of renting similar buildings in your area. You also need to

estimate how much it would cost to get a building ready for your operations, such as installing the equipment and connecting the utilities.

Water drainage, electricity, gas for cooking (piped or in cylinders) and telephone, must be available and connections should be easy to arrange with a minimal delay. An adequate supply of water is essential for many types of processing and the quantities that you require may be considerable. You need to be sure that the flow and pressure of water is suitable for your needs. You may need to install water purification equipment. Similarly, in many areas electricity supply is very basic and/or unreliable and you may need to install a small generator. All of these aspects have to be researched and costs identified for the solutions you arrive at.

### **Labour**

How many employees will you require to ensure that your new production line will function at maximum efficiency? You need to give considerable thought to this. You don't want to employ people to sit around doing nothing but, on the other hand, you do want to ensure that your production process won't break down because of inadequate staff.

Are workers of a suitable calibre available in your area? How much does it cost to employ them and what other terms and conditions of employment will you have to meet? Will you have to spend anything on staff training? You also need to look closely at your country's labour regulations.

You may want to employ people on a seasonal basis but in some countries it may be difficult to hire and fire short-term staff. Many countries require the employer to make social service contributions and even pay the employee's tax. Some countries require the employer to pay a "thirteenth" or even a "fourteenth" months salary, and this also has to be included in your calculations.

### **Distribution and promotion**

Earlier chapters looked in detail at the kind of information you need in order to decide what products to sell, where and to whom to sell them, in what quantities and how often. You should also have considered how to promote your products. With this information you should now be able to develop a plan for the distribution of your products to wholesalers, retailers or consumers and a promotion plan. It is then necessary to work out the costs of implementing these two plans and also to make sure that they are consistent with your processing capabilities.

The main distribution cost will be transport. Do you need to buy a vehicle? If so, how much will it cost to buy, run and service? Alternatively, if you plan to hire transport, how many vehicle-days do you need per week or month to carry out your deliveries? How much will that cost?

Chapter 6 discussed the types of promotion that you could consider. You need to work out the costs of advertisements, posters, leaflets, in-store display, free gifts, etc. Contact radio stations and newspapers to find

out their advertising rates. These may vary according to the time of day, as may the type of person listening. Try to find out when the people you expect to buy your product are most likely to be listening. Don't make the mistake of thinking that you only need to do promotion when you introduce your product onto the market. Although this is the time when you want to make the biggest promotional effort, you should consider promotion as an ongoing activity which needs to be done more or less all the time.

If you decide to give out free samples of your products, you need to take account of the cost of this. Such costs could include the cost of packaging, the cost of plastic cups for samples of drinks, and the cost of employing people to hand out samples and leaflets. With regard to the cost of the products you give out for free, this is perhaps better taken into account when you do a feasibility study, as discussed in Chapter 8. For example, if in the first month of your operations you produce 1 000 litres of juice and use 100 litres for free samples, then you are only able to earn revenue on 900 litres.

### **Other requirements and costs**

You need to research all legal requirements associated with running a business in your country. Food processing facilities are normally governed by regulations to ensure hygienic practices, and you will have to observe these. National and local licences may be required for a variety of reasons and their cost needs to be incorporated into your feasibility calculations.

There may also be regulations relating to the product you plan to produce. For example, the alcohol content of beer may be specified by law, as may the fruit and sugar content of jam.

At the start of your operations you may need to identify specialist help with, for example, setting up and operating your factory. Larger companies will require accountants. All such costs need to be worked out in advance and incorporated in your feasibility calculations, as must the cost of the market research you carry out.

Taxation is something that entrepreneurs often overlook until they are presented with a bill that they cannot pay. In addition to Income Tax, many countries have a system of Value Added Tax (VAT). You need to incorporate that in your price calculations and register to pay the tax before you commence operations.

## REACHING CONCLUSIONS

Earlier research indicated that you had a good product that could be marketed successfully. The research in this chapter should have enabled you to identify:

- whether sufficient raw materials will be available, when and at what cost;
- how easy it will be to obtain supplies of processing inputs such as flavourings, preservatives, yeasts and pectin as well as packaging and labels;
- what equipment you need and whether it is easily available, and at what cost;
- whether suitable buildings are available for your factory and whether utilities are easily available.

On the basis of this you should then be able to reach conclusions, such as:

- although apricots and peaches for drying are only available for three months of the year, my fixed costs (see Chapter 8) are low and I should still be able to run a profitable business;
- the equipment I need to produce peach juice is very expensive. Peaches are only available for three months of the year and I will not be able to cover my costs. Are there other juices I could produce from fruits with different seasons?

- I need to buy about 50 percent of the tomatoes produced in my area if I am to have enough for my planned factory. That would put up the price of tomatoes to a level higher than I can afford. I have to consider giving farmers a contract to grow for me;
- there is no suitable building for me to rent for my factory. I may be able to get a bank loan to build a factory but that would increase the financial risk to me if the venture does not succeed. I need to examine the economics very carefully.

**8 Will your business be profitable,  
and at what prices?**

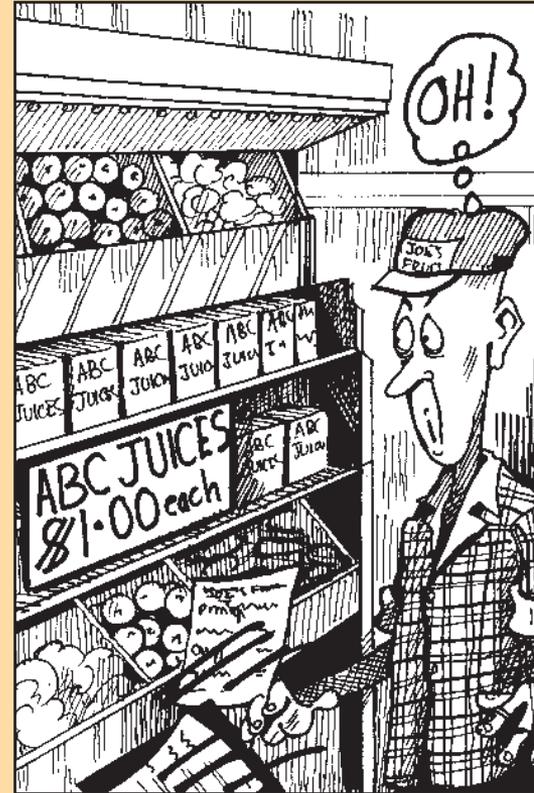
*Main points in Chapter 8*

**Will your business be profitable, and at what prices?**

*Having completed research into the market  
and having considered the availability and cost of all production inputs,  
including equipment and buildings,  
you are now ready to carry out some basic calculations  
and work out what prices to charge.*

*The chapter considers ...*

- *calculating the likely annual profit from your planned processing;*
- *calculating the return to your time and capital;*
- *reviewing your cash flow;*
- *covering your fixed costs;*
- *different ways of setting prices.*



*Before starting a venture  
it is essential to calculate its profitability*

## WILL YOU MAKE A PROFIT?

Throughout the previous chapters this guide has stressed that it is not enough just to identify a potential market for your products. You must be sure that you can supply that market in a way that is profitable for your enterprise. Most products can be sold if their price is low enough. However, if the price is too low you will not make money.

By now, your research should have given you a good idea of the prices your products can be sold for in the shops and the prices that the shopkeepers or wholesale

### *A WORD OF WARNING*

*When calculating the profitability or feasibility of your planned venture you must include the full cost of everything you need in order to process your products, even if some things, such as processing equipment, are subsidized or even provided free of charge by a donor, an NGO or the government. At some stage you will have to replace that equipment and pay the full commercial price for it. Therefore, you need to know from the beginning whether your activity is likely to be commercially profitable or is only profitable because it is being subsidized.*

distributors are prepared to pay you for them. You should also have a clear indication of the costs of the inputs, including the raw material, utility, equipment and packaging costs. With this information you should now be able to make some profitability or feasibility calculations.

Feasibility studies can range from the very basic to the very detailed. As the purpose of this guide is mainly to advise on market research techniques we shall not discuss the more complex types of study. The “Further reading” section at the end of the book gives some sources of more detailed information about carrying out such studies. If you are planning to borrow money from a bank to set up your venture you will need to have detailed discussions with the bank to find out what information it requires in order to make a decision on whether to lend you money.<sup>14</sup>

### **Profitability calculations**

In order to calculate profitability (see Figure 5) you should:

- have calculated the exact quantities of ingredients required to make your product. For example, if you are making pineapple juice, what quantities of pineapples, sugar and other ingredients are required to make a kilogram of juice? Make allowances for wastage. Some

<sup>14</sup> Pages 93-95 of the FAO publication “Guidelines for small-scale fruit and vegetable processors” (see “Further reading”) outline the points that need to be covered in a Business Plan.

*Figure 5*  
**Simple profit and loss account calculation**

<b>Total annual revenues</b>	\$
Estimated revenue from annual sales of fruit juice	
6 000 litres in one litre bottles	
4 000 litres in 0.333 litre cartons	
<hr/>	
TOTAL REVENUE	
minus transport, delivery and payment collection costs	
<hr/>	
<b>(a) net revenues</b>	<input type="text"/>
 <b>Annual costs</b>	 \$
Building and equipment costs:	
Factory cost ÷ 25	
Truck cost ÷ 7	
Other equipment costs ÷ 4	
<hr/>	
TOTAL ANNUAL ASSET COSTS	
Start-up costs ÷ 5	
Maintenance and servicing costs for factory and equipment	
Estimated cost of fruit to produce 10 500 litres of juice	
Estimated cost of other ingredients, including wastage	
Estimated cost of utilities	
Packaging costs:	
Labour costs	
Interest and loan repayment	
Other costs (e.g. licences)	
Taxation provision	
<hr/>	
<b>(b) total annual production costs</b>	<input type="text"/>
Promotional costs including costs of producing free samples	
<hr/>	
<b>(c) total annual costs</b>	<input type="text"/>
 <b>Annual profit</b>	 <b>(a) minus (c)</b>
<hr/>	<input type="text"/>

of the agricultural products you buy will not be suitable for processing. When you peel fruit prior to processing, this can remove much of the weight. You may need to buy 100 kg in order to get 80 kg of processable fruit;

- recognise that some of the processed product will not reach the consumer. It may, for example, get spilled during bottling. In Figure 5 it is assumed that you will need to produce 10 500 litres of fruit juice in order to sell 10 000 litres;
- have an approximate idea of the cost of utilities (gas, electricity, water) used for your processing;
- estimate not only the price paid for ingredients but also the cost of buying them, for example costs of visits to farms;
- give a cost to all ingredients even if you grow some on your own land (the cost should be the price you could get if you sold those ingredients fresh). Otherwise you could end up processing produce that it could be more profitable to sell in the local market or to other processors;
- take into account the different packaging sizes you will be offering and the fact that revenue and costs will vary according to the size;
- take into account miscellaneous costs, such as licences. Disposal of waste material (e.g. fruit peelings) can also be a significant cost;
- build into your calculations the costs of factory buildings and equipment. The easiest way to treat these is simply to divide the cost of the investment by the number of

years you expect it to last. (This should be part of your research – see Chapter 7). Thus you may divide the cost of a building by 25, the cost of a delivery vehicle by seven or the cost of a simple food mixer by three. Also, don't forget that buildings and equipment have servicing, maintenance and insurance costs and these need to be included in your calculations. As you will have probably borrowed money you should not forget to include interest and loan repayments;

- calculate your staffing requirements and the cost of that staff;
- take into account any significant start-up costs, such as technical consultancy services or market research costs. These are unlikely to be repeated every year so it would bias your feasibility calculations to charge these as annual costs for the first year. Consider apportioning such start-up costs over three to five years.

### **Return to time and capital**

Once you have calculated your likely profit, two further calculations are required before you can decide whether it is worthwhile to go ahead with your venture:

1. If you are the owner of the business, then you must calculate the return to your time and that of family members who work without wages. Make a realistic estimate of the number of days you and your family expect to work. Don't forget to include the time spent buying the raw materials and selling the products and

any bookkeeping you have to do, as well as time spent on processing and marketing. Then divide the profit by the number of days. Is this profit per day attractive to you? Could you make more by taking a paid job somewhere? Perhaps the daily rate for a paid job may be less but you could do that throughout the year, whereas your processing business will only keep you occupied for three months. Could you make more by doing a different activity?

2. If you use your own funds to finance the business, is this a wise use of your money? Could you earn more by simply depositing it in the bank? To make this decision you should work out the return to your capital invested. From your calculated profit in Figure 5 subtract the amount of money you could earn from an alternative activity and then calculate the percentage rate of return on your investment, as shown below:

	\$
Estimated profit for one year's operations	9 000
Estimated income from paid job	7 000
Additional benefit from processing	2 000

Capital invested \$10 000  
 Percentage return on capital  
 $[(2\ 000 \div 10\ 000) \times 100] = 20\%$

Don't forget that there are always risks associated with going into business. In order to compensate you for taking these risks the percentage annual return in the long run

should be more than you could earn by putting your money in the bank and the return to your time more than you could get by working elsewhere. In the short run, however, you should be willing to accept lower returns, in expectation that your business will eventually expand and profitability will increase.



### **CASH FLOW**

If it looks like your processing plans will result in a good profit, you are almost ready to proceed. However, you also need to do an analysis of your cash flow. This is to ensure that the cash you plan to put into the business, or that you plan to borrow from the bank, will be enough to meet your needs on a continuing basis. Will you spend all your available cash before you are earning any revenue? Will you be able to pay your bills? Will you be able to buy your ingredients from farmers and other suppliers? If not, you are likely to have problems, even though your earlier calculations have convinced you that the business will be profitable. Poor cash flow is one of the major reasons why companies all over the world run into problems.

**Figure 6**  
**Cash flow analysis**

	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6	Month 7	Month 8	Month 9	Month 10	Month 11	Month 12	Month 13	Month 14
Cash available	10 000	4 000	700	1 100	2 500	2 900	4 300	6 200	10 300	9 700	9 100	8 500	7 900	5 800
Income			4 700	4 700	4 700	4 700	4 700	4 700						
(1) Equipment	4 000													
(2) Fruit		2 000	2 000	2 000	2 000	2 000	2 000							2 000
(3) Staff	200	200	200	200	200	200	200	200	200	200	200	200	200	200
(4) Bottles	1 000		1 000		1 000								1 000	
(5) Ingredients	500	500	500	500	500	500							500	500
(6) Utilities		300	300	300	300	300	300	100	100	100	100	100	100	300
(7) Loan repayment	300	300	300	300	300	300	300	300	300	300	300	300	300	300
<b>Expenses:</b>	<b>6 000</b>	<b>3 300</b>	<b>4 300</b>	<b>3 300</b>	<b>4 300</b>	<b>3 300</b>	<b>2 800</b>	<b>600</b>	<b>600</b>	<b>600</b>	<b>600</b>	<b>600</b>	<b>2 100</b>	<b>3 300</b>
Cash balance	4 000	700	1 100	2 500	2 900	4 300	6 200	10 300	9 700	9 100	8 500	7 900	5 800	2 500

The simple cash flow analysis in Figure 6 assumes that you have borrowed \$10 000 from a bank to put into your business. Repayment starts immediately at \$300 a month. It assumes that you use your own building at no cost, but the equipment you need costs \$4 000 and you must pay for it before it is delivered and installed. Before you can start processing you will have to buy bottles. The minimum quantity that the bottle company will supply will cost \$1 000 and will last you two months. Again, you will have to pay cash. A month's supply of other ingredients will cost \$500. An employee will cost \$200 a month and will need to be recruited for training a month before production starts. You will need to pay \$2 000 a month for fruit\* and your monthly sales revenue is expected to be \$4 700. You estimate that you will be able to buy fruit for six months and you will not be able to store it for more than a few days so you will only be processing for six months.

\* For the sake of simplification we assume in this example that the price of fruit will remain unchanged. This is unlikely to be the case, however.

In doing a cash flow analysis you need to work out:

- when you have to spend money for equipment, raw materials, rent, etc;
- when you have to pay your employees;
- when you are able to begin processing, when you can make your first deliveries, **and when you can expect to be paid**. At the time you carried out your market research, you should have discussed payment terms with potential buyers (see Chapter 5).



*You must pay attention to your cash flow.  
Otherwise, you could run out of money  
to buy raw materials.*

### ***A WORD OF WARNING***

*Although it is important to ensure you do not have cash-flow problems and do not run out of money, you should, at the same time, be careful not to borrow more money than you really need. If too much is borrowed there is a risk of losing all the profit to repay the loan. Consider increasing your contribution as the owner. For larger ventures, consider finding a partner who can put money into the business. Alternatively, consider whether you and your family could increase your inputs in order to reduce costs of employing labour, so lowering your finance requirements.*

*As the owner of the business you may want to take out some of the profits; be careful that you do not take out so much that you run short of cash for the next processing season!*

The cash flow analysis shown in Figure 6 indicates that although you have \$10 000 available and are only spending \$4 000 of this on equipment, you will come dangerously close to running out of money at the end of the second month. If there are any delays in receiving payment from the shops you supply or if the price you get from selling your product is not as much as you expected, you may not have cash to buy enough fruit from farmers. In turn, you will not be able to make enough processed

product, your revenue from sales will go down and you will have to close your new business. In this example, therefore, it would be wise to increase slightly the amount of cash you have available. To get a clearer position of your cash flow at the beginning of operations you could do the projections on a weekly rather than monthly basis

When you are processing fresh produce, you can only do this for as long as you can buy and store that produce. For the rest of the year you will not earn revenue but you will continue to have some costs. You need to have cash available to meet these costs and to prepare for processing in the following year.

### Fixed and variable costs

Some of your costs are fixed. This means that you have to pay them whether you are processing or not. These costs include rent, loan repayments and interest, permanent staff costs (as opposed to temporary employees hired only when you are processing) and fixed utility charges.<sup>15</sup> All other costs are considered variable costs. This means that they change according to how much you produce, how much you pay for your ingredients, the cost of utilities, etc.

As you have to pay the fixed costs no matter how much or how little you produce and sell, you need to be sure that you will sell enough processed product to cover those costs. Consider the following ...

	\$
Revenue from annual sale of 5 000 litres of fruit juice	3 000
<u>Variable costs</u>	<u>2 000</u>
Gross profit	1 000

... this looks like a profitable venture: you are making 50 percent profit on every litre of juice sold.

However, when fixed costs are taken into account the picture can look very different ...

	\$
Revenue from annual sale of 5 000 litres of fruit juice	3 000
<u>Variable costs</u>	<u>2 000</u>
Gross Profit	1 000
<u>Fixed costs</u>	<u>1 200</u>
LOSS	200

... from this it is clear that while you are covering your variable costs very well, you are not producing enough to cover your fixed costs.

<sup>15</sup> Most utility providers charge a nominal monthly fee whether or not you actually use any water, electricity, etc.

If you can double your production and sell the juice at the same price the picture changes ...

	\$
Revenue from annual sale of 10 000 litres of fruit juice	6 000
Variable costs	4 000
<hr/>	
Gross Profit	2 000
Fixed costs	1 200
<hr/>	
NET PROFIT	800

Now you should work out the break-even point for your venture. This is the quantity you need to produce and sell in order to cover your fixed costs. This is calculated as follows ...

$$\text{Fixed Costs} \div \text{Gross Profit per unit of sale}$$

In our example this is ...

$$\$1\,200 \div \$0.20 \text{ (i.e. } \$2\,000 \div 10\,000) \text{ or } 6\,000 \text{ litres}$$

This is the break-even level of production and sales. More than 6 000 litres will give you a profit, less than 6 000 litres and you will make a loss. If you can easily expand production and sales above 6 000 litres then you are likely to run a profitable business. If increasing production much higher than 6 000 litres is likely to cause problems you should reconsider your plans.

The break-even point can also be stated as a percentage. Taking into account the fact that raw materials may only be available for a few months every year, how much could you process and sell in a year? If the maximum you could produce is 20 000 litres, then the break-even percentage is  $6\,000 \div 20\,000$  or 30 percent. The lower this percentage the greater the scope you have for increasing production and making your business more profitable.

## SETTING THE PRICE

The different ways of setting prices include:

- market-based pricing;
- competitive pricing;
- introductory pricing;
- prices for different sizes;
- geographical pricing;
- cost-plus pricing.

## Market-based pricing

This sets prices at the level already found in the market and, of course, can only be used when there are similar products already on sale. You need to look at the competing products with regard to their price and quality. What do your tasting tests tell you about the quality of your product and how it compares with others already available? Using market-based pricing you should aim to set the price of your product at no more, and probably less, than brands of similar quality. Where you are competing with well-established brands marketed by large companies with a big advertising revenue, you almost certainly have to set your prices at a lower level than those brands even if tasting tests indicate that consumers prefer your brand. You should certainly not be charging the same price as brands that you believe are of higher quality because consumers will definitely continue to buy those brands.

## Competitive pricing

Competitive pricing involves setting prices at a lower level than those of your direct competitors. This will, you hope, lead to increased sales. Any price difference must, of course, be large enough to influence consumers' buying decisions as just a small price difference may have no impact on your sales. You need to discuss this with retailers and get their ideas regarding prices that will attract people to buy your product. When you have decided on a competitive price you then need to estimate what impact this will have on your total sales and repeat your profitability calculations using the new figures.

For example, using the fruit juice example on pages 100 and 101, assume that you reduce the price from \$0.60 a litre to \$0.55 a litre and that your sales rise from 10 000 litres to 12 000 litres ...

	\$
Revenue from annual sale of 12 000 litres ( $\$0.55 \times 12\ 000$ )	6 600
Variable costs [ $\$4\ 000 \times (12\ 000 \div 10\ 000)$ ]	4 800
<hr/>	
Gross Profit	1 800
Fixed costs	1 200
<hr/>	
NET PROFIT	600

In this example you have increased your sales by 20 percent, but the lower price means you are worse off. You would have to increase your sales to almost 13 500 litres before you benefit from the price cut. This illustrates the value of doing a sensitivity analysis (see below) and the need to be careful before trying to compete on price. You also need to consider that lowering the price too much may not necessarily make your product more attractive to consumers. People often associate low prices with low quality and if quality is more important to them than price they will not purchase a low-priced product.

## Introductory pricing

This is short-term, competitive pricing for the purposes of introducing your product onto the market. It is very difficult for new products to be accepted by consumers who are

already used to, and enjoy, existing brands. If you pursue a policy of introductory pricing, you may lose or make very little money in the short term, but in the long run this should increase customers' familiarity with your products and eventually increase your sales and your profits.

The next calculation uses the first fruit juice example, with the following assumptions:

- price reduced to \$0.50 per litre in the first three months and thereafter increased to \$0.60;
- sales are 5 000 litres in the first three months and 12 000 litres for the rest of the year.

Then ...

	Jan-Mar \$	Apr-Dec \$	Total \$
Revenue from sale of fruit juice	2 500	7 200	9 700
Variable costs	2 000	4 800	6 800
Gross Profit	500	2 400	2 900
Fixed costs	300	900	1 200
<b>NET PROFIT</b>	200	1 500	1 700

### Prices for different sizes

If you sell juice in one-litre bottles and half-litre bottles, you should not sell the larger bottles for twice the price of the smaller bottles. The larger the container the lower the price per litre (or kg) of contents is the general rule. The smaller container almost certainly costs more than one-half the cost of the larger bottles. Also, the cost per litre of filling the smaller bottles, putting them in boxes and distributing them is much higher than for larger bottles. You will need to work out these costs.

### Geographical pricing

You need to consider whether your product should be sold for the same price everywhere or whether you could vary the price. One reason for varying the price could be the high transport costs you may incur in getting to remote areas. However, another reason could be that consumers are more affluent in some areas than others and you may thus be able to charge a slightly higher price.

### Cost-plus pricing

This pricing technique starts with the calculation of your variable production costs per unit. To this should be added an amount necessary to cover fixed costs at the production level you expect as well as an amount to cover the profit that you want to make. While cost-plus pricing can perhaps be used for a new product that is not presently available in your area, it is not of much value when there are competing products. If you set a price that is too high people will not buy your product.

## UNDERSTANDING THE RISKS

All business ventures involve risks. A wise entrepreneur cannot completely avoid such risks but he or she can develop an understanding of what they are. The best way to do this is to carry out a sensitivity analysis, which tests how sensitive your profits are to price and cost changes.

A sensitivity analysis is done by making different assumptions to those you used in your basic profitability and cash flow calculations. It is best to recalculate on the basis of a set of “*what if?*” questions, such as:

- what if my competitors reduce their prices and I have to sell at prices 10 percent lower than I planned?
- what if the price I have to pay for labour goes up by 10 percent?
- what if the raw material prices are 20 percent more than I expected, and I can only buy 80 percent of what I planned?
- what if sales are 30 percent less than I expect?

All of the above are very possible occurrences. There are further, less likely, risks, but these are also worth considering, particularly in relation to your cash flow.

Examples include:

- what if factory construction is not finished in time for the fruit production season and I have to delay processing for a year?
- what if there is a strike at the bottle factory and I run out of bottles? How will this affect my cash flow?

## REACHING CONCLUSIONS

The issues discussed in this chapter should enable you to:

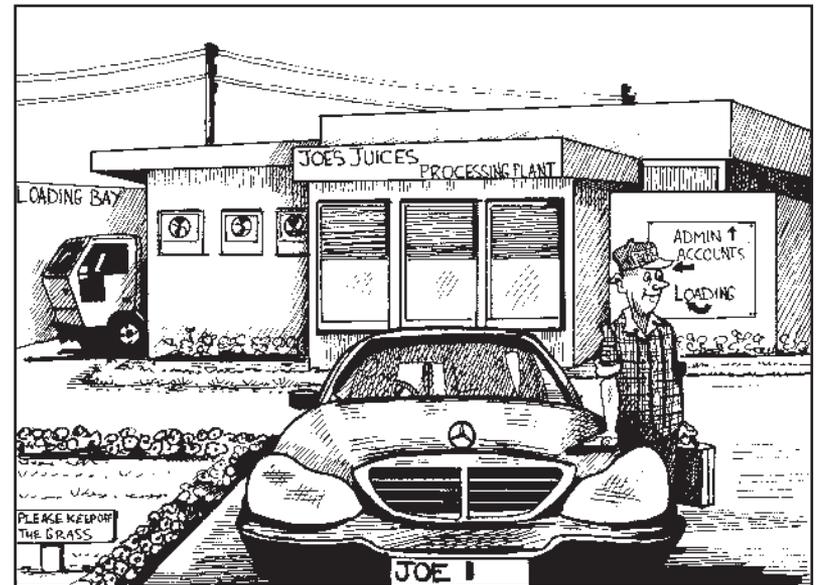
- calculate the likely profitability of your proposed agroprocessing venture, on an annual basis;
- review your financing requirements, to ensure you have adequate cash available to keep the business running (i.e. cash flow);
- work out the return to your time and capital;
- work out how much you need to process, in order to cover your fixed costs;
- decide on the best approach or approaches to price setting;
- consider the risks associated with your plans, by carrying out a sensitivity analysis.

You should then be in a position to reach some conclusions, such as:

- my fruit juice business is likely to be profitable. However, there are a lot of risks that could jeopardise that profitability and I need to consider these carefully;
- everyone likes my jam and retailers are happy to sell it. I am sure that my business will be profitable. However, I may run into cash flow problems because I have to pay for the fruit, the jars, other inputs and the label design and printing a long time before I will be paid for the jam. Perhaps I need to make arrangements with my bank in case I need a loan in a hurry;
- my forecast of yoghurt sales is too close to my break-even point. I can easily produce more but I need to work out ways of increasing my sales first.

You should now be in a position to make a final decision about whether or not to go ahead with your plans.

# Good luck!





## Annex 1

# Questions for market research

### Checklist for shop observations

- What brands of the product are presently sold?
- In what market segments?
- In what size units?
- In what quality?
- What are the prices for each brand and size?
- If similar products are on sale (e.g. if you are planning to sell orange juice – other types of fruit juice; if you are planning to sell potato chips or crisps – other types of snack food) what are the sizes, brands and prices of those?
- Are the shelves full or does the product appear to be in short supply?
- Are any promotions being done for the product you plan to produce or for similar products?
- Is there any advertising for these products?
- What type and quality of packaging is used by other brands?
- What information is provided on the packages or labels?
- What is your overall impression of the shop (including the staff)? Would it be a good place to sell your products?

### Checklist for retailer interviews

*Opening statement.* “I am carrying out a study for the ABC company, which is thinking of producing a new product and selling it in this area through shops such as yours. As you sell this type of product do you mind if I ask you some questions, which will help our company decide whether or not to start producing it and, if so, where to sell it. Any information you give will be treated as confidential and only used to help us make a decision on whether or not to produce and how to market our products. Let me begin by asking ...”

- What products of this type do you sell?
- Approximately what quantities of the product did you sell in the last 12-month period?
- Do you sell more than one brand? If so can you say approximately how much of each brand you sold in the last 12 months?
- How much of the product do you presently have in stock now?
- In the last five years have your sales of this product been increasing or decreasing. If so, by how much? If there is an upwards or downwards trend in the overall total or for particular brands, can you suggest the reasons for this?
- If you sell more than one size, can you say approximately how much of each size you sold in the last 12 months?

- \_\_\_ Do you stock all available sizes? If not, why not?
- \_\_\_ How do you get your supplies of this product? From the producer/importer, a wholesaler(s) (could you name them please?), other retailers? If you use more than one channel, what is your preferred method?
- \_\_\_ Approximately what quantities of similar products (e.g. all snack foods; all fruit juices) did you sell in the last 12 months?
- \_\_\_ Do sales of the product vary according to the time of the year? What are the reasons for this? Can you provide monthly sales figures?
- \_\_\_ Can you get enough of the product, or competing products, or is there sometimes a shortage? If the latter, do your suppliers give you any reasons for this? Is the shortage said by suppliers to be a long-term problem or just temporary?
- \_\_\_ Are you aware of plans by producers or importers of similar products to increase the supply?
- \_\_\_ Would you be interested in stocking a new brand of the product? Under what conditions would you sell a new brand?
- \_\_\_ What do consumers say to you about the existing brands that you sell? Do they ever complain about the quality/packaging, etc. Do you think that a new product could sell well?
- \_\_\_ Which of the brands you sell do people prefer, and why do you think this is (quality, price, product appearance, packaging)?
- \_\_\_ What is the most important consideration for your customers? (price? quality? convenience? size?)
- \_\_\_ What do you pay your existing suppliers at present for each brand, size and quality?
- \_\_\_ At what prices do you sell these products?
- \_\_\_ Do you decide on the selling price or do you follow your suppliers' recommendations? If you decide, how do you calculate your selling price? Do you follow the same mark-up for all products/brands or does the mark-up vary?
- \_\_\_ What mark-up would you apply to a new product?
- \_\_\_ What type of packaging would you prefer for this new product? Why?
- \_\_\_ Do you get complaints from customers about the containers used for other brands?
- \_\_\_ Would customers buy the product in different packaging, such as.....?
- \_\_\_ Do the brands you sell have "sell-by" or "use-by" dates? How long do they last? If so, what do you do with products if the date has expired? Can you return them to your supplier? Under what terms and conditions?
- \_\_\_ What quantities of your existing brands of the product do you take delivery of at any one time? How frequently do you receive deliveries?
- \_\_\_ If you agreed to sell a new brand of this product what are the minimum and maximum quantities of each size and type that you would accept delivery of at any one time?

- \_\_\_ How often would you expect deliveries to be made?
- \_\_\_ In what size of distribution containers (e.g. cardboard boxes) are other brands packed? How many retail packs are supplied in one container? Would you accept containers with less/more retail packs?
- \_\_\_ Do you accept deliveries at all times or only at certain times/on certain days?
- \_\_\_ When do you pay your suppliers? On delivery, at the next delivery, etc? How do you pay (cash, cheque)? If your suppliers give you credit, for how long?
- \_\_\_ In the past year, have any existing brands of the product carried out any form of promotion that you participated in, such as:

- price reductions?
- advertising?
- free samples?
- in-store displays?
- other?

- \_\_\_ If so, please describe the arrangements under which you participated.
- \_\_\_ If the store displays advertisements you might ask ... please explain why you display advertisements for these products and not others?

## Checklist for wholesaler interviews

- ✓ \_\_\_ What area or “territory” do you cover? Are there similar wholesalers covering the same area?
- ✓ \_\_\_ What quantities of the product for each size unit and brand did you sell in the last 12-month period?
- ✓ \_\_\_ How much do you presently have in stock?
- ✓ \_\_\_ In the last five years have your sales of this product been increasing or decreasing. If so, by how much? If there is an upwards or downwards trend in the overall total or for particular brands, can you suggest the reasons for this?
- ✓ \_\_\_ Do you stock all available sizes? If not, why not?
- \_\_\_ What quantities of similar products (e.g. all snack foods; all fruit juices) did you sell in the last 12 months?
- \_\_\_ Can you get enough of the product, or competing products, or is there sometimes a shortage? If the latter, do your suppliers give you any reasons for this? Is the shortage said by suppliers to be a long-term problem or just temporary?
- \_\_\_ Are you aware of plans by any producers or importers of this product to increase the supply?
- \_\_\_ Would you be interested in stocking a new brand of the product? Would you attach any special conditions to selling a new brand?
- \_\_\_ If there is more than one wholesaler in the area you might ask... do you expect to be the only distributor of a particular brand?

- \_\_\_ Do you allow your suppliers to supply some retailers or caterers directly? If so, under what conditions?
  - \_\_\_ What do retailers say to you about the existing brands of the product that you sell? Do they ever complain about the quality/packaging, etc. Do you think that a new product could sell well?
  - \_\_\_ What do you pay your existing suppliers for each brand, size and quality?
  - \_\_\_ At what prices do you sell these products?
  - \_\_\_ Do you decide on the selling price or do you follow your suppliers' recommendations? If you decide, how do you calculate your selling price? Do you follow the same mark-up for all products/brands or does it vary?
  - \_\_\_ What mark-up would you apply to a new product?
  - \_\_\_ If you agreed to sell a new brand what are the minimum and maximum quantities of each size and type that you could accept delivery of at any one time?
  - \_\_\_ How often would you expect deliveries to be made?
  - \_\_\_ In what size of distribution containers are other brands packed? How many retail packs are supplied in one container? Would you accept containers with less/more retail packs?
  - \_\_\_ Do you accept deliveries at all times or only at certain times or on certain days?
- \_\_\_ When do you pay your suppliers? How do you pay (cash, cheque)? Do you expect your suppliers to give you trade credit? If so, for how long?
  - \_\_\_ In the past year, have any existing brands of the product carried out any form of promotion that you participated in. If so, please describe the arrangements under which you participated.

## Annex 2

# A consumer questionnaire

For the purpose of this example, we assume that the agroprocessor is thinking of producing strawberry jam.

1. Good morning. I work for a company that makes jams. Could I ask you some questions about what you think about jams?
2. Do you or your family eat jam?  
 yes  
 no
3. Could you tell me what types of jam you have had in your home in the last 12 months?  
 strawberry jam  
 mango jam  
 pineapple jam  
 orange marmalade  
 others \_\_\_\_\_
4. Who are the main consumers of jam in your home?  
 adults  
 children

5. Approximately how many jars of jam and marmalade have people in your home bought in the last 12 months?

more than 20  
 between 11 and 20  
 between 6 and 10  
 between 3 and 5  
 one or two

6. What size of jam do you normally buy? (show the different sizes to the person being interviewed)
7. Does your family buy jams all through the year or only on special occasions? \_\_\_\_\_  
\_\_\_\_\_
8. Of the jams you purchased, can you remember approximately how many were strawberry jam? \_\_\_\_\_  
\_\_\_\_\_
9. Can you remember the brand of the strawberry jam your family usually purchases? (if people cannot remember give them the names of the available brands to jog their memory)  
\_\_\_\_\_  
\_\_\_\_\_
10. From the words on this line how would you rate the quality and taste of that brand of strawberry jam?

excellent    very good    good    OK    poor

11. What are the two main reasons you buy that brand rather than a different one?

- It's the only one in the shops
- The price is right
- My family prefer this brand
- It spreads very well
- I like the label
- It has the best taste
- Other \_\_\_\_\_

12. What do you think about the colour of the strawberry jam presently available in the shops?

- too bright
- about right
- too dull

13. What do you think about the sweetness of these jams?

- too sweet
- about right
- not sweet enough

14. What do you think about the thickness of these jams?

- too thick
- about right
- too thin

15. If most of the jam your family buys is not strawberry jam, what is the reason for this?

- My family prefers other jams or marmalades
- The strawberry jam in the shops is not very good
- Other \_\_\_\_\_

16. If a new brand of strawberry jam was available in the shops, do you think you would try it?

- yes
- no
- perhaps

17. At which shop do you buy most of your jams? \_\_\_\_\_

18. What are the reasons why you shop there?

- It is near our home or work
- The prices are good
- It is a nice place to shop
- It has a good selection
- Other \_\_\_\_\_

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NOTES

## NOTES

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Desktop publication: George Ellis  
Cover illustration: Emanuela D'Antoni

The following is a list of booklets published in the  
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Viale delle Terme di Caracalla  
00100 Rome, Italy

FAX: (39) 0657056850  
E-mail: [AGS-Registry@fao.org](mailto:AGS-Registry@fao.org)  
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Market research is essential before embarking on any agroprocessing venture. This guide describes, in fairly simple terms, the market research that agroprocessors can carry out, and some of the ways of doing such research. It is addressed to entrepreneurs and companies who are planning to develop or expand medium-sized agroprocessing businesses. It is also intended to be used by banks who need to understand the potential market before lending for agroprocessing, by consulting firms and individuals offering market research services in developing countries and by government agencies and policy-makers interested in developing the agroprocessing sector.