

# WHITE PAPER FAQ

## A Data-Forward Living Income Strategy for Commodity Supply Chains

### 1. What makes the White Paper's approach unique?

The strategy integrates two key methodologies: the Living Income Price (LIP) and the Cost-Yield Efficiency (CYE) Analysis. By using actual data from farmers and cooperatives, the strategy provides a nuanced understanding of production costs and yields, allowing for dynamic price discovery rather than reliance on fixed benchmark prices. Additionally, the strategy emphasizes transparency and the use of open-source tools, promoting broader adoption and collaboration across the supply chain.

### 2. Which methodologies are introduced in the White Paper?

The White Paper introduces two key methodologies:

- **Living Income Price (LIP):** This methodology provides a structured approach for calculating the price per unit of a commodity based on its actual costs of production at various supply chain stages. Farmgate (individual and typical), Cooperative/Producer Organization, and Free-On-Board (FOB).
- **Cost-Yield Efficiency (CYE) Analysis:** is a complementary methodology for detailed assessments of efficiency levels among farmers and producer groups, by considering both costs and yields. This helps identify areas for improvement and develop tailored intervention strategies. Following the publication of this White Paper, an addendum will be released to provide a deeper exploration of the CYE methodology.

### 3. How is the Living Income Price (LIP) calculated?

The LIP is calculated using actual (primary) data on yields and costs at producer, cooperative, and FOB (Freight on Board) levels. It involves detailed steps including data collection on production costs, yield, and other relevant factors, and then applying specific formulas to determine the LIP at different points in the supply chain. A Living Income Benchmark is also a crucial part of the calculation, ensuring that the price reflects the amount needed for a household to achieve a decent standard of living.

### 4. Which methodologies are introduced in the White Paper?

The key differences are:

- **LIP (Living Income Price):** Developed by Heifer International and Fairfood International, it's based on actual (primary) data on yields and costs at producer and cooperative. It is a dynamic price discovery methodology within a supply chain rather than a fixed benchmark.
- **LIRP (Living Income Reference Price):** Developed by Fairtrade International, it calculates the price needed for a typical farmer household with a viable farm size and sustainable productivity level to earn a living income.
- **True Price:** Developed by True Price and Wageningen University & Research, it calculates what the living income gap is per unit of produce and what proportion of that living income gap can be allocated to a certain product. Additionally, it adds the social and environmental costs of a product to the market price, reflecting the true cost of production and consumption.

## 5. What use cases are best suited for the LIP vs. the LIRP vs. True Price?

- **LIP:** Providing transparency on actual production costs, yields and pricing gaps within a supply chain. Results can be used by producers, cooperatives, and businesses to advocate for living income gap-reducing interventions along efficiency and productivity improvements and/or sustainable pricing that reflects actual costs assumed by producers in a given season plus a livelihoods margin. As an alternative to static price indicator, actual production data is used to dynamically assess supply chain performance over time.
- **LIRP:** Establishing a standardized benchmark price for a typical farmer household to be able to earn a living income, based on a viable farm size and sustainable productivity levels. Results can be used by certification bodies to inform procurement standard requirements, by producer organizations and businesses to negotiate contracts and foster responsible trading practices, and guide overall pricing policies that align with living income benchmarks across different regions and commodities.
- **True Price:** True Price's Living Income Module shares a similar use case with the LIP at the producer-level calculation. True Price's Human Capital and Natural Capital modules introduce a unique approach to measuring the social and environmental costs within a value chain. These can be used for advocacy towards consumers or by businesses to inform reduction or remediation of externalities.

## 6. What are the primary components considered in the Farmgate LIP calculation?

The primary components for calculating the Farmgate LIP include:

- Living Income Benchmark
- Adjustments for household size and inflation
- Diversification ratio (revenue-based)
- Production costs
- Farm depreciation costs
- Yield
- Productive farm size

## 7. How does the Farmgate LIP account for income diversification?

The Farmgate LIP accounts for income diversification by incorporating a diversification ratio. This ratio measures how a household's income is distributed across different sources, including non-farming activities. The LIP calculation uses a revenue-based allocation approach to estimate the contribution of the primary commodity to the overall living income, ensuring a comprehensive view of household income sources.

## 8. What is a Cooperative LIP?

The Cooperative Living Income Price (Cooperative LIP) is defined as the price paid for a commodity that adequately covers both the Farmgate LIP for cooperative members and the operational costs associated with cooperative activities and processing capabilities. It helps cooperatives negotiate fair terms and prices, ensuring that the benefits or fair share of the FOB price trickle down fairly, providing a living income for farming households and supporting sustainable business operations. This methodology allows cooperatives to manage their value-added services sustainably, contributing to the long-term formalization and sustainability of their supply chains.

## 9. What are the primary components considered in the Cooperative LIP calculation?

The primary components for calculating the Cooperative LIP include:

- Farmgate LIP (mean or median)
- Commodity weight conversion factor
- Costs of cooperative operations
- Equipment depreciation costs
- Total production of the cooperative

## 10. How does the Cooperative LIP differ from the Farmgate LIP?

The Cooperative LIP includes the Farmgate LIP for cooperative members plus the operational costs associated with cooperative activities and processing capabilities. It helps cooperatives negotiate fair terms and prices with exporters, ensuring fair income distribution throughout the supply chain.

## 11. What is the FOB Living Income Price (FOB LIP)?

The FOB LIP defines the price an exporter sets for a commodity when selling to an importing entity, covering all costs incurred up to the point of shipment. It ensures that exporters can meet the farmgate LIP for farmers and cooperatives while covering value-added services and operational costs.

## 12. What are the primary components considered in the FOB LIP calculation?

The primary components for calculating the FOB LIP include:

- Farmgate LIP (mean or median) or Cooperative LIP
- Product weight conversion factor
- Export costs (actual or estimated)

## 13. What best practices are recommended for data collection?

Best practices for data collection and reporting include:

- Defining a production scenario
- Selecting a representative sample size
- Accurately capturing production and cooperative costs
- Implementing farmer-centric data governance
- Detecting and cleaning data outliers
- Calculating and reporting both mean and median LIPs
- Ensuring consistency in the time frame of data

## **14. What is the role of the Open-Source Toolkit?**

The Toolkit supports stakeholders in applying the LIP and CYE methodologies within their supply chains. It provides resources like data sharing and informed consent contract templates, cost of production data collection surveys, and analysis tools. The toolkit aims to facilitate practical implementation and promote broader adoption of data-driven living income discussions and sustainable practices within commodity supply chains.

## **15. What is the importance of transparency and open-source tools?**

Transparency and open-source tools are crucial for fostering trust, ensuring fair value distribution, and promoting broader adoption of sustainable practices. The authors commit to making specific parameters and tools publicly accessible, encouraging inclusive and informed decision-making among all supply chain stakeholders. This means it can be used by anyone, without the need to involve Heifer International or Fairfood International. Although we'd love to know if you do.

## **16. What is our call to action?**

The call to action encourages stakeholders to utilize verifiable data to support claims about living incomes, invest in both efficiency and price interventions, and join efforts to set new standards for transparency and accountability in global supply chains. It aims to create a sustainable future for all stakeholders, keeping the promise of fair income distribution for producers worldwide.

## **17. Would this not create more confusion in the market, enabling a race to the bottom?**

Heifer and Fairfood's Commodity Living Income Strategy, along with Fairtrade and True Price's approaches, are designed to be complementary rather than competing. Each model provides unique value by serving different needs of achieving living incomes for producers. Rather than causing confusion, these diverse approaches can collectively enhance market understanding and drive informed decision-making. By presenting a unified front with our complementary tools, we can elevate awareness and visibility of gaps within supply chains. This collaboration allows us to build joint strategies and leverage our combined insights, strengthening our ability to advocate for sustainable and fair pricing across different regions and commodities. Instead of a race to the bottom, we aim to create a race towards greater transparency, equity, and sustainability in global supply chains- and perhaps even a race to the top.