Revolutionising finance for agri-value chains

Brussels Development Briefing no. 35

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On 5th March 2014, CTA organised the 35th Brussels Development Briefing on Revolutionising finance for agri-value chains – part of a series of bi-monthly Development Briefings on ACP-EU rural development issues. More than 140 participants discussed key role of finance for value chain development and emphasised the innovations in financial instruments and service.

Revolutionising finance for agri-value chains. The Briefing looked at finance as a key driver for value chain development and discussed the concept of agricultural value chain finance, new opportunities for financiers, and the new context of value chain finance in Africa - including the development of ICTs that support innovative applications. It examined the innovations in financial instruments and services and presented concrete examples of innovative applications on the ground which demonstrate the potential of value chain finance for shaping African agriculture.

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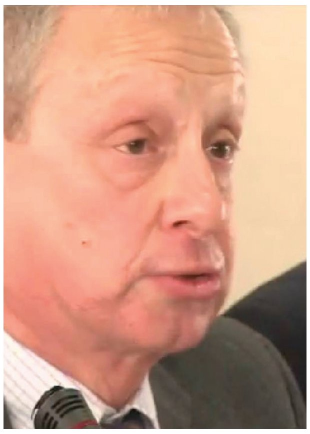
Alhaji Muhammad Mumuni



Denis Salord

Michael Hailu

As an introduction, **Alhaji Muhammad Mumuni, Secretary General of the ACP group of States**, stressed that, for most ACP countries, agriculture remains the second most important sector and forms an instrument for sustainable development and poverty reduction. Nevertheless, some constraints remain persistent, limiting its competitiveness along the value chain. Participation can only be enhanced through financial empowerment. In this regard, agriculture value chain finance offers an opportunity to reduce cost and risk in financing. For financial institutions, value chains finance creates the opportunity to better understand the competitiveness and risk in the agricultural sector.

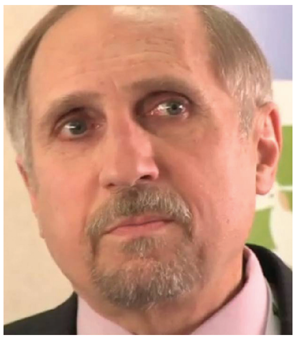
Denis Salord, Head of Unit, Regional Programmes Sub-Saharan Africa & ACP-wide, DG DEVCO, European Commission, underlined the importance of agriculture for the global economy. He explained that the agricultural sector has to deal with more and more demands in the world and that agriculture development is the main priority of ACP-EU cooperation programs. Agriculture is, for most of these countries, the main source of income.

One of the challenges of developing value chains finance is the need for better identification of the funding requirements and the establishment of systems to deal with it.

Since 2004, the EU adopted a plan of action to support commodity farmers. Since 2007 programs have been implemented in order to support the access of small farmers to more adequate funding and one of the keys for success is related to proper supply of market information.

Finally, **Michael Hailu, Director of CTA** stressed the need to focus on mobilising finance for smallholders in ACP countries. Productivity has to increase through better technology and innovation and a massive investment is needed to make this possible. The current lack of access to finance is a critical impediment for most smallholder farmers in developing countries. The CTA has developed an extensive program in support of smallholders including


H.E. Frédéric Assomption Korsaga


Calvin Miller


Lamon Rutten


Saleh Usman Gashua

value chain finance and is currently working with the African credit associations to spread awareness about value chains financing techniques in Africa.

Given the enormous challenge of feeding rapidly growing cities with high quality food, it is essential that all parties develop trust. In addition, governments and central banks should consider what they can do to facilitate arrangements including public-private partnerships.

Panel 1: Finance: a key driver for VC development

The first panel provided an overview of the concept of agricultural value chain finance, the new opportunities for financiers, and the new context of value chain finance in Africa – including the development of ICTs which support innovative applications. It was moderated by **H.E. Frédéric Assomption Korsaga, Ambassador of Burkina Faso**.

Calvin Miller, Group Leader FAO Agribusiness and Finance Group, focused his speech on the concept of agricultural value chain finance and types of value chain business models. He underlined that the increase in food prices has caused concern in many governments and increased interest of investors in agriculture. Integration helps value chain finance and value chain finance helps integration.

The objective is to align finance to deal with the industry's needs and to reduce the associated costs and risks. It is not necessarily to try to change everything through every single farmer. The success of Bolivia demonstrates that it can work if all the drivers are there such as capacity, good governance, accountability and so on.

In summary, value chains finance is not a universal panacea. Moreover, stakeholders have to be careful not to lose sight of the need for diversification of smallholders that are involved in more than one chain. Value chain finance is a comprehensive approach to finance. We can take advantage of the knowledge within the value chain to help improving our processes and so to reach a win-win solution.

Lamon Rutten, Programme Manager, Policies, Markets & ICTs, CTA, stressed the reasons which explain why value chains are a good investment and what is needed support them.

The need to secure supply of commodities and a declining risk capacity have resulted in a push for more investment in value chains. Moreover, as regard to the pull factors, consumers demand proper value chains and capital market investors are looking for new places to put their money. However, serious efforts are required to turn this potential into reality.

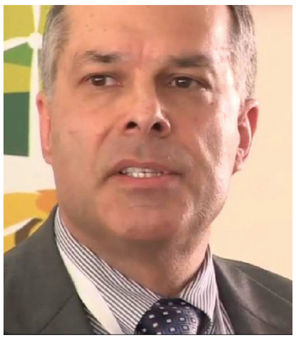
There are two possible options to increase the overall funding in the sector by fifty percent. Either agriculture becomes much more profitable or a dramatic increase in external funding takes place.

Regarding agriculture finance, investors have to deal with two main risks. On the one hand, the ability of farmers to reimburse lenders and on the other hand, the unwillingness to reimburse. If the process goes well, you will have safe and very easy production and so you can continue financing as long as the VC is operating. We need to learn from best practices. It means identifying the necessary skill set and mindsets. Moreover, proactive governments and central banks are needed, as at present, many African central banks do adequately respond to the reality of African economies.

In conclusion, value chains finance is a key tool to get agriculture to meet current challenges but also a great opportunity for banks.

Saleh Usman Gashua, Secretary General of Afraca, focused on how to improve rural and agricultural financial inclusion. Agriculture occupies a top position in the national economies as the sector serves as the key driver of growth, wealth/job creation, food security and poverty reduction. The problem is that the investment in agriculture has been low, with only one percent of commercial lending in Africa going to agriculture in 2010. What really matters is the network. While rural-,


Kanayo Awani


Lee H. Babcock

agricultural- and micro-finance look the same, each of these three sectors has distinguished statistics.

The challenges are numerous. The governments have not achieved the objective, fixed in the Maputo declaration, to dedicate 10% of their budget to agriculture. The participation of the private sector, which is supposed to be the driving force of African agriculture, is still weak and a slow and uneven offer of financial services for agriculture and rural activities by financial institutions can be observed.

With regard to the role of Afraca, one of its key focus areas is capacity building. In this regard, it uses a bottom-up strategy, from institution, to country, and to sub-regional level. In conclusion, lending to the agricultural sector is not easy, despite all the interventions.

Kanayo Awani, Director Trade Finance and Branches of Afreximbank in Egypt, stressed the new opportunities for African Trade finance.

A number of factors have inhibited the flow of financial resources to support activities across the African agriculture value chain. These includes: low public sector investment; high catastrophic risks (climate, etc.); poor state of agriculture related infrastructure; absence of, or inadequate, agricultural insurance market; poorly regulated agriculture sector; dismantling of commodity boards in the 1980s and 1990s; limited knowledge on agriculture production and farm maintenance practices.

With regard to the role of Afreximbank in financing agriculture value chains, the Bank is supporting various programs in different countries such as Cameroon, Cote d'Ivoire, and Nigeria. The Bank's support for the agricultural sector has been growing over the years which could be explained by the emergence of agricultural reforms in a number of African countries. The Bank is not only supporting countries with finance but it also provides access and gives advice as well. One example of a program launched by the Afreximbank is the African Cocoa Initiative which has the objective of providing long-term financing for the creation of processing capacities. The Bank also tries to improve deals and encourages states to issue Cocoa bonds. Ms Awani invited partners to join the Bank in an effort to support the transformation of the agricultural sector in Africa.

Lee H. Babcock, Expert on mobile finance for agriculture, USA, described the strategic benefits and approaches to agricultural mobile finance.

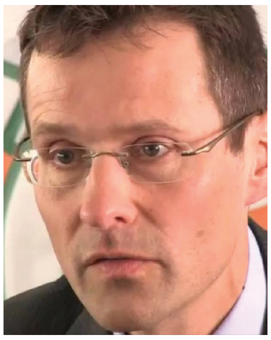
In developing countries, there is a phenomenal penetration of mobile phones. Moreover, investors are looking at expanding into rural areas. So on the one hand, we have farmers with phones and on the other hand, we have massive foreign direct investment. The benefits for smallholder' farmers in having a mobile bank account are numerous: they can send and receive payments in a more secure way by avoiding cash transactions; it increases productivity and provides them with a financial identity.

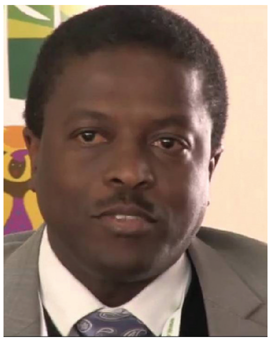
Nevertheless, there are barriers to rolling out agricultural mobile phone platforms such as illiteracy and lack of trust among people. There is a tremendous opportunity to connect the agenda of the private sector with the objectives of agricultural development. There are three steps which have to be followed to overcome these barriers. Firstly, market research into the cash usage behaviour patterns of farmers is needed. Secondly, after gaining visibility, discussions and strategic alliances have to begin to take place. Finally, the integration of mobile finance services into agriculture value chains interventions must take place. On the demand side, awareness promotion and education about the features, and benefits of mobile money towards farmers, are needed. On the supply side, supply has to be stimulated .

The main objective is to create a global ecosystem of agricultural mobile finance service to make value chains more efficient and effective.

The debate focused mostly on women's access to finance. All panellists agree that this issue is very important and that efforts still have to continue. The problem of lack of coordination between


H.E. Brave Ndisale


Hans Bogaard


Hans Balyamujura

all actors and the barriers that undermine the use of ICT were also raised during the debate.

Panel 2: Innovations in financial instruments and services

The second panel, chaired by **H.E. Brave Ndisale, Ambassador of Malawi**, presented concrete examples of more current applications on the ground which demonstrate the potential of value chain finance for shaping African agriculture.

Hans Bogaard, Head of the agribusiness advisory activities, Rabobank, shared practical stories on VC finance. The two examples of leading banks in Tanzania and Zambia are the two big success stories of Rabobank. In Zambia, Rabobank is partnered with Zanaco, the country's leading agriculture bank. Zambia has the advantage that it already has the necessary agricultural infrastructure. On the contrary, in Tanzania, there was a need to adopt VC finance and the challenge is now to move to emerging farmers and less integrated markets.

Agrifinance is the result of a good enabling environment and a good organization. If all factors are well organized, agri finance will come automatically. What is very important with regards to agrifinance, is the segmentation of the market. It is easier to finance large farmers, corporates and traders but it is more challenging to go down to the primary sector. The bank has to understand that each segment requires a different approach.

Agriculture should be seen as a business and, knowledge is key so we need to invest in agrisector knowledge and systems. The focus has to be on payment capacity; collateral and guarantees come after. Then, state owned Agri banks don't work because there is still too much political intervention. Mr Bogaard stated that Rabobank believes in the role commercial banks can play with rural stakeholders in support of agriculture. In that context, the Bank has to work closer with traders and processers and to focus not only on farmers but on the whole VC.

In Uganda, Rabobank is financing the rice sector. ICM, an Australian company, is investing in rice mills. Another good thing is that unions were supported to take stake in mills. There is a three-way agreement, between the rice union, the rice mill and the bank, which has created a change in the value chain. The Bank is financing not only the mill, which is the easiest part, but also the union, the cooperatives and the farmers. It is a complex task because the need for coordination amongst partners.

Hans Balyamujura, Co-Founder and CEO of ZED Group Limited, focused on linking rural entrepreneurs to financial services. On average globally upstream and downstream farming activities account for 78% of the value added in all agricultural value chains. The question is how does the farmer extract the value? Another point is that only about 1- 3% of commercial debts is in agriculture. The bigger challenge is at the bottom of the pyramid. The question is how to link the different chains within the value chain to the main value chain. One of the big issues is the lack of data.

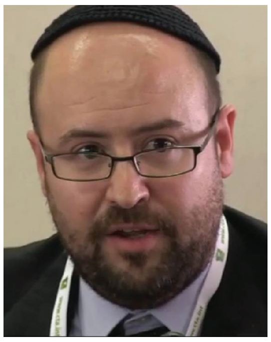
Looking at the new generation of smallholder agribusiness models, we can put at the top the agricultural production and at the bottom the input production. We have also to look at the risks and the technical aspects along the value chain and identify who is the rural entrepreneur. Farmer organisations also play a critical role in terms of helping to structure the process.

The objective is to aggregate the different ecosystems. Quality food products in Tanzania are a good example of an entrepreneur working to create a fully integrated value chain. The Southern African Confederation of Agricultural Unions (SACAU) is playing a leading role to ensure farmer centric models of operation. The challenge is how to get involved in the value chain without owning them.

Value chains finance and the digital environment offer new opportunities but we have not yet seen the capability of what can be generated out of the cell phone.


Priscilla Wambui Muiruri


David Ruchiu


Adam Gross

Currently, Africa is seeing a lot of economic growth. We need to ensure that the interventions take place as close as possible to the bottom of the pyramid, that the link the bottom of the pyramid in ways that are better organized - with accountability and transparency, and creating access to the markets through value chain integration.

Priscilla Wambui Muiruri, Agribusiness Specialist, KAPAP, presented the Kenyan Experience in Agri-value Chain Financing. Agriculture contributes to 26% of the Kenyan GDP and provides 70% of employment in rural areas. Kenya Vision 2030 is the plan of action which was launched in order to become a globally competitive and prosperous country with a high quality of life by 2030. In this regard, the financial sector is expected to play a critical role in mobilising resources and to also try to promote Public Private Partnerships.

It is evident that that all the actors of the value chain are linked together and that they are from public and private sectors and in every chain of the value chains, financial support is needed.

Regarding the financial products in agriculture, Kilimo Biashara (Agribusiness) connects farmers to markets by improving access to credit. There are some partners such as the Equity Bank, which lends its own funds, resulting in benefits such as increased productivity and investment, and has increased the number of farmers accessing funds. It is to be noted that increasingly farmers mobilize their own resources. One example is the Keretai Self Help Group which has increased its production thanks to credit. However, some challenges remain such as irregularity in information sharing on loan disbursements, weak market access linkages and high illiteracy among smallholder farmers.

Technology could play a role in enhancing financial access for farmers. What is needed now is to establish a market intelligence system; demystify loan acquisition procedures and processes through capacity building; to do the promotion of farmers groups ‘own’ savings mobilization and linkages to financial instruments; and also to integrate production, financing and marketing.

David Ruchiu, Africa Director, Farm Concern International, Kenya, described the E-warehouse Initiative. Smallholders farmers are very vulnerable. Agri finance is fundamental but it is not easy because it is difficult to attract investment. We need to focus on mobile phones to attract the agricultural sector and ensure that technology is accessible, and to increase value by facilitating access to financial services.

The data collection system known as “E-warehouse” provides access to all data. E-warehouse increases the value retained by smallholder farmers for their crop by facilitating access to mobile financial services and enhances market access for smallholder farmers. This environment provides data on the value of products during harvest time. So famers should use this new technology to connect information. This technology makes all the process very easy, because payments are easy. Farmers can then sell after the harvest time.

Adam Gross, Investments and Capital Markets Advisor, Nepad Business Foundation, focused on Commodity Exchange Developments. In Africa today, there are about a thousand warehouse systems which basically houses the commodity in a warehouse. The simplest version of exchange is the spot exchange, for the trade of physical commodity. The more sophisticated adaptation is a model from Malawi, for food exchange. The last kind of exchange, which is prevalence in many markets in Europe, is a derivative or future option exchange. It is generally a financial exchange for price risk management. This is the model for the South African Commodity Exchange.

After the harvest time, farmers transport the commodity to a warehouse where it is weighed and graded. A warehouse receipt is then issued, which certifies the quality, the quantity and the location of that commodity. Finally it goes to storage. With the commodity exchange, the farmer has two options: he can sell immediately at the prevailing market price, which is called a spot transaction, or he can access finance. It means that he can keep the commodity in storage, receive finance from a bank and wait until the price goes up. When the price is looking good, he can sell the commodity, pay the storage fee and the warehousing, pay the bank loan and receive cash.

There are many benefits from an exchange which supports key aspects of the value chain finance transaction: pricing, collateral, pledging, valuing, liquidation, performance, risk management and liquidity. So, commodity exchange is not value chains finance but it is an effective institution for managing value chains finance.

Regarding the risks with value chains integration for the farmer, if that VC collapses then the farmer is also a loser for reasons often not related to his or her own activities. A good thing with the commodity exchange is that the farmer can access various different off takers, traders, export markets through the commodity exchange. So commodity exchange (comex) also creates a certain level of flexibility.

Today, in Africa, there are only three exchanges which can be considered fully functional: the Johannesburg Securities Exchange (JSE), South Africa; Agricultural Commodity Exchange of Africa (ACE), Malawi and the Ethiopian Commodity Exchange (ECX), Ethiopia. These examples show that a comex can work in any African context. So we can say that commodity exchanges have been successful in Africa. However, challenges include misalignment with government policy; ensuring that value will be created for all stakeholders (traders, processors and offtakers), standardising the commodity quality, putting too much focus on the trading platform and small national markets, which suggests that a regional market might be better.

The Briefing was concluded by H.E. Brave Ndisale, Ambassador of Malawi, who highlighted that, as demonstrated by the speakers, revolutionising finance for agri-value chains is a reality. Aligning finance to the value chain and the needs of the farmers is very important. It is also important to increase the benefits and revenue of players at the bottom to increase their participation in warehousing and commodity exchange developments. Finally, Mrs Ndisale pointed out that mobile finance offers new opportunities for Africa.

Further information on the web:

- Brussels Briefings: *http://brusselsbriefings.net*
- Reader: *http://tinyurl.com/m83vg9h*
- Report prepared by Isolina Boto, Manager of CTA Brussels Office and Jonathan Pfund, Research Assistant.