PROCEEDINGS

FINANCING AGRICULTURE FORUM 2012

March 28-29, 2012
Kampala, Uganda

THE WORLD BANK

AGRIFIN
Agriculture Finance Support Facility

Centenary Bank

I. INTRODUCTION

On March 28-29, 2012, the Agriculture Finance Support Facility (AgriFin) held its first annual meeting in Uganda, Kampala to promote knowledge exchange and to foster partnerships in agriculture finance. The Financing Agriculture Forum, which was co-sponsored by Centenary Rural Development Bank, brought together over 100 participants from 30 countries. Through plenary sessions and technical presentations, 32 financial institution professionals shared their specific business models and approaches to segmenting markets and developing products on financing agriculture.

II. DAY 1 – MARCH 28, 2012

Ahmadou Moustapha Ndiaye, Country Manager, The World Bank; Fabian Kasi, Managing Director, Centenary Rural Development Bank; Ajai Nair, Program Coordinator, AgriFin, The World Bank; Mark Cackler, Sector Manager, Agriculture & Rural Development Department, The World Bank; Carlos Cuevas, Deputy Director, Financial Services for the Poor, B&M Gates Foundation; and Louis Kasekende, Deputy Governor, Bank of Uganda. On behalf of their respective organizations, the panelists welcomed delegates and stressed the importance of South-South knowledge sharing in agriculture finance, and the significant opportunities for increased agricultural lending by financial institutions that might arise from such learning. They reflected on the economic importance of agriculture to developing countries.

From left to right - Carlos Cuevas, Bill & Melinda Gates Foundation; Mark Cackler, World Bank; Louis Kasekende, Bank of Uganda; Moustapha Ndiaye, World Bank; and Fabian Kasi, Centenary Rural Development Bank

The key message was that tackling poverty globally requires increased investment in agriculture, which relies on improved access to finance. In their remarks, it was noted that the underlying challenge in agriculture finance is finding the appropriate mechanisms for expanding agricultural lending sustainably.

Keynote Address: New World of Agriculture and the Opportunities for Finance

Nancy Barry, Enterprise Solutions to Poverty, USA.

Nancy Barry is a recognized global leader in building enterprise and financial systems for the poor. Drawing from her rich experience in the field she discussed a number of key challenges and opportunities facing agricultural finance, noting in particular new and emerging opportunities for small farmers in the current landscape. A number of developing countries see a new generation of progressive farmers shifting from subsistence farming to producing for markets.


Nancy Barry during the opening remarks

These farmers demand high quality and yield enhancing inputs. This has created an enormous business opportunity for financial institutions to provide farmers with the financial means of acquiring these inputs. This will entail identifying these farmers and designing appropriate financial products for them. Large agribusinesses, agro dealers, and input suppliers are finding efficient ways of working with these progressive farmers and linking them with other players along agriculture value chains. Financial institutions should continue to collaborate with agribusinesses in order to reach bankable clients and deliver services such as insurance, payments, and loan origination points. Given the advanced state of current technologies, financial institutions are now able to leverage 'deep telecom agent distribution systems' in rural areas to reduce the costs of serving clients in remote locales and to offer a diverse set of services.

Business models that rely on tight linkages among supply-chain stakeholders provide the strongest opportunities for lending to farmers through the development of tripartite relationships. Experience shows that relaxed relationships only add increased risk and uncertainty.

In conclusion, three elements in particular are essential to building a sustainable agriculture financing business: (a) lending to farmers with multiple sources of income, who are tightly linked to the market through value chains, (b) collaborating with agro dealers for input supply and advice, and (c) working with aggregators, such as farmer associations.

In the discussion following the keynote address participants reinforced the importance of aggregating smallholder farmers through linkages to reduce transaction costs and to enable banks to reach more bankable clients. The experience of several financial institutions suggests that in the absence of large scale commercial farmers, serving aggregated groups of farmers in developing countries is an effective strategy for managing risk and increasing scale. Participants also noted that many governments in Asia and Africa support programs that aim to improve access to finance for the poor – including farmers. While acknowledging these efforts on the part of governments, these types of programs require active private sector involvement to ensure effectiveness, scale, and ultimately, sustainable access to finance for large numbers of smallholders. Finally, the participants stressed that for an agriculture finance program to succeed, factors such as improved access to extension services, business development, advisory services, and market linkages are essential.

New Approaches in Reaching Smallholder Farmers

Chandula Abeywickrema, Hatton National Bank, Sri Lanka; Vasco Nunes, Banco Oportunidade Moçambique; and Nick Handler, One Acre Fund, Kenya. The panelists discussed their respective institutional models and experiences in serving small farmers. These financial institutions have developed mechanisms that are focused on the aggregation of small farmers for scale, use of value chain linkages to manage risk, financial literacy, and low-cost delivery channels.

Tailoring the repayment and disbursement of loans to the production cycle, ensuring collaboration between loan officers and extension agents in the field, and assessing the quality of inputs when loans are in-kind were noted as critical success factors by Banco Oportunidade Moçambique. One Acre Fund's operation to finance subsistence farmers in Kenya achieved remarkable growth within five years of operation. Nick Handler noted that combining loans, training of staff and clients, low-cost delivery mechanisms, and building multipurpose distribution channels for inputs, finance, and other services have been crucial to the success of One Acre Fund's agriculture finance model.

For Hatton National Bank, which has served farmers for 120 years, having well-qualified field officers with expertise in agriculture, finance, and knowledge transfer has contributed to the positive performance of its agriculture business. The institution's performance has also benefitted from continued linkages in the value chain with corporate partnerships for entering large markets.


Dos Dinn and Chheng Yanith, AMRET, Cambodia

The session highlighted the importance of providing additional non-lending financial services, including savings, life and production insurance, and money transfers when targeting small clients. These services beyond credit generate additional income for the financial institution while assisting smallholders to better manage their businesses. Savings can provide significant benefits by providing a safety net to farmers, as well as being a means of funding inputs and other costs prior to harvest. Farmers need to be educated and encouraged to save through financial literacy programs.

First Agriculture Finance Market Scoping study in Tanzania

Ian Anderson from the Gatsby Charitable Foundation, Kenya, presented results of the first Agriculture Finance Market Scoping (AgFiMS) study in Tanzania. The objective of AgFiMS is to collect, interpret, and disseminate information on the need for financial services among agricultural businesses, and to identify factors that restrict their access to those services. Based on this information, interventions can be designed to overcome the gap. On the demand side, the scoping work identifies commercially viable agribusinesses and financial services that are well-suited to their needs. On the supply side, the scoping work is used to quantify current financial provisions to the agriculture sector. The AgFiMS is a private sector-led survey to segment a bankable market.

The approach in Tanzania uses a set of criteria to identify a commercially viable segment. According to these criteria, farmers who operate on less than 5 hectares and who earn less than US$600 annually are considered too poor for commercial financing. The scoping survey found 519,972 qualifying agriculture businesses, most of which are traders, concentrated in well-developed value chains with working capital and other financial needs. According to AgFiMS, about 29 percent of these agribusinesses are formally banked by SACCOs and MFIs and less than 12 percent are served by commercial banks. The remaining enterprises rely on informal sources of finance, mainly through friends and family.

Those enterprises which are served by formal service providers for the most part make use of payment services and savings products. This reveals a huge gap in terms of credit. This gap offers an opportunity to provide credit to agribusinesses which the banks already reach and know. AgFiMS estimates that the demand for agriculture credit in the Tanzanian market is approximately US$50 million. This approach can be replicated to promote the development of financial markets for agriculture finance in other countries throughout much of Africa. The execution of similar markets segmentation studies in other countries would bring a range of benefits, including inter-country learning, policy benchmarking, and cross-market analysis for international investors and banks.

Opportunities and Challenges in Financing Producer Cooperatives

Presentations by **Arnold Tijdens, Banque Populaire du Rwanda; Mary Achini, Co-operative Bank of Kenya; and Nathaniel Schaffran, Root Capital, Kenya,** examined their individual approaches towards lending to agricultural cooperatives. All of the presenters noted the use of tripartite lending relationships as instrumental in reducing default risk. Tripartite agreements entail repayment to a bank, made by a buyer on receipts of goods from the producer. They also discussed the importance of value chain relationships to ensure repayment, and the need for banks to fully understand the value chain and the industry in order to accurately assess risk. Limited managerial capacity can be a significant barrier to working with such groups.

George M Irungu, Head of Agriculture Credit, Equity Bank Ltd.

Financial institutions generally prefer working with cooperatives that have proven management expertise and are able to provide reliable financial statements and acceptable balance sheets. The advantages of utilizing tripartite arrangements for short-term seasonal financing were recognized as being significant, while longer term lending faces a number of serious challenges. The provision of longer term loans depends on the establishment of long-term relationships between banks and producers – relationships that enable the parties involved to utilize third-party guarantees and to provide finance on reclaimable assets. Banks are likely to find significant value in capacity building by training their staff to understand how cooperatives and value chains work. This understanding of financial management of cooperatives will better qualify bank staff to assess the risks associated with lending to client cooperatives.

New Models for Lending to Emerging Commercial Farmers

Hans Balyamujura, ABSA Bank, South Africa; George M Irungu, Equity Bank Ltd., Kenya; and Patrick Mutenda, Zambia National Commercial Bank (Zanaco) presented their experiences in offering services to emerging commercial farmers. The three banks classified producers based on farm sizes, though this classification varies significantly between banks since what is considered a small producer by one bank may be classified as a large producer by another bank. While product offerings vary between the three, loan repayments in all cases are tailored to the production cycles of the producers. Small-scale producers require comprehensive technical assistance in agricultural production and in business management to enable them to become bankable clients. The three banks in this session are already offering capacity building services to clients, with the cost charged to the client as a way of ensuring sustainability.

III. DAY 2 – MARCH 29, 2012

Transaction, Savings and Payment Services for Agricultural Clients

Michael Andrade, HDFC Bank, India; Hans Balyanujura, ABSA Bank, South Africa; and Agness Jazza, First Merchant Bank, Malawi, discussed their respective experiences relating to the use of technology and other mechanisms to facilitate lending and other financial services. Following the presentations, participants expressed an eagerness to learn more about using innovative, low-cost mechanisms to enable them to offer services to low-value (income? margin?) clients. A growing variety of technologies and models are available to reach agricultural clients in a cost-effective way, including agency banking models, mobile branches, and migration to automated delivery service channels, including ATMs, cell phones, and Smartcards. Because revenues per agricultural client are relatively low and because the clients are dispersed geographically over wide areas, finding cost-effective ways to conduct transactions is an important priority. Client recruitment needs to be reassessed in order for banks to migrate from the traditional recruitment model (recruiting clients individually) to a model by which groups of client are secured en-masse. This effectively minimizes the costs of acquiring new clients. Among the examples that emerged was that of working with processors and buyers to recruit and service their producers. Questions to the panel also related to the success in mobilizing savings from producers.

The panel noted that most smallholder farmers do not save at formal financial institutions, mainly due to high transaction costs and financial illiteracy. Financial institutions are adopting mechanisms to encourage farmers to save. Some banks design savings products to mobilize deposits during seasonal sale and offer loans tied to the savings accounts. Others provide financial literacy training to farmers to raise awareness and promote savings products.

Working Capital Solutions for Agricultural Enterprises

Wilfredo Maldia, Land Bank of the Philippines; Aoua Sawadogo, Reseau des Caisses Populaires Burkina, Burkina Faso; and Abdul Kyanika, Centenary Rural Development Bank, Uganda, explained the working capital loan products they offer to agricultural clients. While each bank utilized a different model (price, product, promotion, and security), they have al achieved significant growth in scale and volume in recent years.

The panel on Working Capital Solutions for Agricutural Enterprieses presenting their experiances

Discussion following the presentations focused on the maximum length of working capital loans, savings mobilization mechanisms, repayment processes, and non-traditional forms of security taken for loans. With the exception of Centenary Rural Development Bank, banks generally classify working capital facilities as being for periods of less than one year, and the loans are primarily used for either trade finance (agricultural processors and traders) or for production cycles (farmers).

For lenders, the challenges of securing savings from agricultural clients result in a gap between loans and deposits. Solutions include savings campaigns, focusing on savings mobilization in non-rural areas, and utilizing third-party funds such as the European Investment Bank and other donors.

Won-Sik Noh, Secretary General, Asia Pacific Rural & Agricultural Credit Association (APRACA)

The banks also noted that repayment cycles are linked to agricultural seasons, with producers due to repay following harvest periods. In addition, there are challenges in taking collateral from agricultural clients, especially in cases where land title is unclear. Solutions proposed to remedy this latter problem ranged from taking charge of non-land assets to the case of Burkina, where security is provided through "mutual security organizations" in which people who lack security contribute to a fund which acts as collateral for the bank.

Investment Financing for Agricultural Enterprises

Chandula Abeywickrema, Hatton National Bank, Sri Lanka; James Mugabi, DFCU Ltd., Uganda; and Nat Robinson, Juhudi Kilimo, Kenya, presented on the topic of financing for longer term investment in agriculture. Hatton National Bank focused on its irrigation financing loan; DFCU on its leasing products and Juhudi Kilimo on longer term loans for smallholders. A major theme throughout the presentations and subsequent discussion related to the prerequisite of lenders having strong relationships with the suppliers of infrastructure equipment, who would use the loans to purchase this equipment. Through these relationships between lenders and equipment suppliers, borrowers can be encouraged to purchase appropriate technologies and quality products, and receive support in installing and maintaining them following the purchase. In this way, banks can significantly raise the probability of the investment producing positive returns and their chances of receiving repayment. Strong supply chain relationships also enabled financing to reach down to the smallholder level, enabling banks to identify stable marketing arrangements for smallholder produce and ensuring tripartite repayment mechanisms, where appropriate.

Opening Up Access to Finance Through Warehouse Receipt Systems

Robert Pascal, NMB, Tanzania; Michael Andrade, HDFC Bank, India; Paul Musoke, Housing Finance Bank, Uganda; and Mamo Mihretu, Ethiopia International Finance Corporation, shared their respective experiences on warehouse receipt financing. NMB works with more than 28 licensed warehouses with a capacity to store coffee, pigeon peas, cashew, maize, paddy, sunflower, and sesame. With a combination of warehouse receipt product- and out grower scheme-based lending, NBM's agriculture portfolio reached about US$73 million in 2011. A strong and reliable market system is fundamental to success in warehouse receipt financing. NMB's experience further shows that large volume is required to ensure the viability of a warehouse receipt financing system. HDFC Bank in India is currently providing warehouse receipt-based loans to over 2,000 customers.

The panel on warehouse receipt financing discussing experiences in Ethiopia, Uganda, Tanzania and India

Of these, about 50 percent are wholesale customers, 40 percent are SMEs and 10 percent are large farmers. As the client distribution shows, HDFC's warehouse receipt financing product is designed for large agriculture enterprises owing to very limited storage by small farmers. In order to take the warehouse receipt financing system down-market and make it attractive to farmers, it is essential to consider investing in warehouse infrastructure closer to farmers and offering additional services at warehouse locations. Integrating the warehouse system into the supply chain and leveraging the facility to offer services to various actors in the supply chain contributes to a viable and successful warehouse receipt financing system.

The Ethiopia IFC-supported warehouse receipt financing program focuses on creating a functioning warehouse receipt-financed market. The program currently supports the provision of short term (2-4 months) working capital loans to farmers against warehouse receipts issued by the Ethiopia Commodity Exchange. As in the case of HDFC in India, the Ethiopian warehouse receipt financing product has limited participation by small farmers. Because of the size of stock that can be stored and the lack of physical access to warehouses, most of the clients are cooperatives, traders, and commercial farmers. A strong market player, such as a commodity exchange, a performance guarantee system, price discovery system, supportive legal framework, and public awareness are critical to a successful warehouse receipt financing system.

Subsequent discussion centered heavily on the limited availability of infrastructure and the lack of professionally managed storage facilities both of which, are in short supply across Africa and Asia. However, facilities do not necessarily need to be perfect, and those with a padlock and limited sets of keys are sufficient to serve as storage locations for collateralized lending, even if they are ineligible for a formalized WRS.

The discussion then moved to regulatory issues, specifically whether WRS can only function where formal laws related to WRS are in place. While most participants concurred that appropriate laws are helpful, it was noted that warehouse-receipt-based lending could, in fact, operate effectively where laws have not yet been enacted, Kenya being a particular example.

What Does It Take To Build A Profitable Agriculture Finance Business Line?

Chandula Abeywickrema, Hatton National Bank, Sri Lanka; Fabian Kasi, Centenary Bank, Uganda; and Robert Pascal, NMB, Tanzania.

This lively session generated a great deal of discussion and debate between panelists and the floor. Topics included the importance of effectively segmenting agricultural clients based on the local market and the needs of the financing institution; the economic and social motivations of banks engaged in lending to agriculture and the need for banks to understand what their motives are for lending to the sector; and the underlying profitability of financing agriculture when undertaken in an effective manner. Other issues that emerged were the importance of public and private partnerships, especially with regard to the public sector (and NGOs) building the capacity of producers and enabling them to become bankable clients; the need for banks to understand agricultural risks and to build these into their client risk assessment practices; the importance of understanding the sector so that banks can identify and work with clients engaged in value chains that demonstrate "tight linkages"; and, finally, the need for banks to develop and design products that are tailored specifically to agricultural segments that support the client in an effective manner.

Forum Highlights

Ajai Nair, AgriFin Program Coordinator, thanked participants for attending the Forum and, most importantly, for contributing their ideas, experiences, and lessons learned relating to agriculture financing.

Ajai Nair, AgriFin Program Coordintor

The Forum concluded with a presentation of the key themes and messages that had emerged during the two days deliberations as follows:

- Improving financing for agriculture is imperative to development and poverty reduction. Vast numbers of the poorest people on the planet are engaged in agriculture, and improving agriculture productivity is vital to reducing poverty. Agriculture productivity, among other services, relies on access to appropriate financial services.
- Linkages are crucial, with banks much better able to service clients who are ingrained in established, well structured value chains.
- Banks should focus on commercially oriented farmers.
- Getting financing to farmers requires aggregation, whether through cooperatives or supply chain intermediaries; directly lending to farmers is possible, but transaction costs are high.
- Traditional security for loans excludes too many producers; banks need to be creative in finding alternative and appropriate assets to accept as security against loans.
- The majority of the challenges faced by banks wishing to lend to agriculture are similar across different regions. As such, the solutions are also similar; demonstrating how information sharing between banks can—and will—reap rewards.
- Producers need support to improve their productivity, and improved productivity is critical in making producers into bankable clients.
- Effective ways need to be found to build the capacity of producers; this will involve public, private, and third-party partnerships.
- Lending to agriculture, when done well, can be a highly profitable business line. Banks committed to generating profit from increased lending to agriculture need to manage credit risk and transaction costs.

IV. Outcomes

The forum has demonstrated the need to have banks share experiences with other banks so that they can learn from each other. South-South learning holds a tremendous potential to significantly increase access to finance, which is critical to improve agricultural productivity in order to meet market demands.


Participants during coffee break

The following were key outcomes from the Financing Agriculture Forum 2012:

- *Improved knowledge on agricultural lending practices*

Based on conference interviews and evaluations, the participants felt they had learned much from their peers about agricultural lending practices. Many participants expressed appreciation in learning about farmer aggregation models and linkages with input dealers and buyers to increase outreach, mitigate risks, and reduce costs. The use of mobile technology and geo-spatial mapping to identify clients was an innovation that some of the participants from Asia would like to incorporate into their business models back home. There was also recognition of the importance of having specialized in-house agricultural lending 'know-how' for developing a viable business line. Participants appreciated the strategies that some financial institutions have employed to develop this expertise.

- *Enhanced networking among agriculture finance practitioners*

Since the challenges faced by banks wishing to lend to agriculture are similar across different regions, the solutions are also similar. This further demonstrates how information sharing between banks can—and will—reap rewards. The forum was designed to maximize South-South collaboration and networking. Throughout the forum, participants demonstrated a strong openness to share knowledge and eagerness to learn from each other. A global network of agriculture finance practitioners was truly in the making.

- *Better understanding of the demand for knowledge products on agriculture finance*

Having hosted the forum, AgriFin walked away with a better understanding of the demand for a wide array of knowledge products and topics on agriculture finance. Participants expressed interest to continue the peer-to-peer learning virtually and to delve more on topics, such as value chain financing, credit scoring, client advisory services to name a few. While participants expressed high satisfaction with the sharing of information about various operational models, they would like to have more sharing of specific tools, like product sheets, training modules, and credit scorecards.

V. Looking Ahead

Most importantly, participants expressed their willingness to continue sharing and learning from their peers. To facilitate this process, AgriFin is creating collaborative channels and tools to enable practitioners from around the world to connect with their peers, share knowledge, tools and experience. Through active contribution and participation from its members, AgriFin seeks to build and share knowledge on agriculture finance with the end goal of improving access to finance for farmers and rural entrepreneurs worldwide. To access all conference presentations and materials, and learn more about AgriFin's program and upcoming events, please visit https://www.agrifinfacility.org.