Panel on Value Chain Finance Draws Large Numbers at SEEP AGM

Washington, D.C. On October 28th, 2005, there was a workshop at the SEEP Network’s Annual General Meeting called Value Chain Finance: How Does This Work in the Field? The three panelists from the Practitioner Learning Program (PLP) in Strategic Alliances for Financial Services and Market Linkages in Rural Areas showcased included: Mr. Bob Fries (ACDI/VOCA), Mr. Ashok Kumar (EDA Rural Systems), and Ms. Tiodita Mori (ACCION).

The main focus of the panel was to show how understanding value chain finance – the financial relationships among different commercial actors in a value chain – can enhance the work of microfinance institutions and market development facilitators or BDS organizations working to increase the incomes of micro and small enterprises.

Mr. Ashok Kumar highlighted how organizations that serve as market development facilitators are instrumental to understanding the financial needs of growers, as well as different commercial actors in the litchi value chain in Muzzafarpur, India. EDA conducted a value chain assessment in August 2005 and included a specific set of questions that focused on financial aspects. By understanding the financial relationships, opportunities and constraints, EDA expects to work with banks and commercial actors in the litchi value chain to increase the flow of finance to growers.

Ms. Tiodita Mori is the Resident Advisor for Accion working at El Comercio, a microfinance institution (MFI) in Paraguay. From the perspective of a financial institution, Ms. Mori highlighted how financial institution can build off the existing financial relationships between commercial actors such as storage providers (i.e. silos) and small farmers. By studying the agricultural value chains such as soya and sesame, El Comercio is able to improve their financial services to small farmers. Ms. Mori explained that by partnering with storage providers, El Comercio has benefited by reducing the cost of crop supervision, reducing the cost for loan recovery and credit supervision and by sharing risk with the storage providers. In the future, El Comercio plans to use their knowledge of value chain finance to develop new products such as insurance, savings, and current account facilities to meet the needs of “unbanked” farmers.

Mr. Bob Fries explained that in order to increase access to finance, it is necessary to look at rural finance that is provided by financial institutions as well as through value chain actors, such as wholesalers, processors, storage providers, traders and input suppliers. It is possible that by linking value chain actors to formal financial institutions more farmers and micro and small enterprises in rural areas will have more access to finance.

American Refugee Committee conducted a value chain analysis in November 2005 in Sierra Leone. Above, a picture taken at their value chain workshop. To learn more, see “Featured Columnist: Ask ARC”

Recommended Reading:

INSIDE this issue:
Peer Assist Phone Calls – A New Way to Stay Connected (p. 2)
Ask ARC: Mary Morgan, Sarah Ward, and Ben Noballo talk about gathering information on value chain finance in Sierra Leone (p.3)
Travel: Take a Journey to India and meet EDA and IDEI (p.4)
Peer Assist Phone Calls Keep PLP Partners Connected Worldwide

To keep PLP partners connected, the PLP program held two Peer Assist Phone Calls in the past quarter. The Peer Assist Phone Call is a knowledge sharing technique that is being used so that PLP partners can share their experiences to date, discuss challenges they are facing in their work, and bounce ideas about potential solutions. Although PLP partners have busy schedules, phone calls are viewed as a good way to exchange information in a time-effective way. For the next round of calls, we are exploring internet calling that will be free using Skype!

So…What Did We Talk About?
Cherie Tan (Caja Nor Peru), Alex Snelgrove (MEDA/IMON), Suresh Subramanian (IDEI) and Bettina Wittlinger (ACCIION/El Comercio) participated in a Peer Assist Phone Call on December 21, 2005. David Knopp (Kenya BDS), Peter Kivolnzi (RMC), Ashok Kumar (EDA) and Sarah Ward (ARC) participated in a Peer Assist Phone Call on January 31, 2006.

Among the many topics discussed, a key topic was how to bring on board different players into a strategic alliance or partnership. Some tips we discussed were:

- **Show potential partners that what you are offering works!** IDEI uses demonstration plots to show how their low-cost irrigation systems works and the benefits of irrigation to economic activities. IDEI is analyzing the economic returns with partner banks so that banks and commercial value chain actors can see for themselves the returns from using low-cost irrigation. Over time, IDEI wants to get banks on board to finance this type of equipment.

- **Be persistent and patient.** Talk to different people, especially decision-makers at the regional, headquarters, and board of directors level in order to get buy-in to form a strategic alliance or partnership. One key lesson so far is that selecting potential partners and getting them on board takes time and patience. For Caja Nor Peru, one commercial player initially did not want to be involved in a risk-sharing scheme to lend to small farmers, but then changed its mind and came on board after several meetings.

- **Show potential partners a win-win situation.** For example, ACCION/El Comercio (Paraguay) was able to partner with silo owners in the soya value chain because silo owners did not have sufficient capital to finance their suppliers. Since silo owners want more supply, El Comercio is in good position to extend finance, enabling small farmers to get access to finance and markets.

- **Take a gradual approach.** MEDA/IMON (Tajikistan) launched a small storage loan so that small farmers can store their own products during the winter months. Currently, the storage capacity is very limited in the area that MEDA/IMON are operating. By starting small, MEDA/IMON hopes to learn more about lending for storage purposes and would like to work with larger storage providers in the next season.

In the Spotlight: MEDA/IMON

_Sogd Region, Tajikistan._ As part of the PLP program, all partners submit bi-monthly diaries. Here is a review of some initial lessons coming from MEDA/IMON.

In doing their value chain analysis, MEDA/IMON learned it is important to be flexible in order to capture new information. In addition, triangulating and using a variety of research techniques, such as interviews, focus group discussions, and stakeholder meetings help to ensure the validity of information gathered. For instance, answer regarding financing varied when asked to different value chain actors. Farmers claimed they only received financing from MFIs but buyers said there were other available credit arrangements.

IMON/MEDA’s first pilot product, a $350 group loan to purchase storage materials, proved extremely successful with all farmers able to take advantage of significant price differentials and able to payback their loans on time. It is exciting that this product will now be expanded to other project regions and crops. However, farmers said that the loan size was not enough and that they would like to store more but need the space to do so. They would also like to make further improvements to their facilities, such as adding wood shelves (which reduces spoilage). Thus, a larger product of approximately $1,500 will be piloted with farmers, allowing them to build and/or expand their existing storage facilities.

The participants in the SEEP PLP in Strategic Alliances for Financial Services and Market Linkages in Rural Areas look forward to seeing if the second, larger product will be as successful as the first and will better meet client demand.
Q: Tell us about your Value Chain Analysis.
We initially conducted a baseline study and supply chain market studies in the districts of Kailahun, Kono and Koindadugu. The individual market studies looked at supply chains and market outlets at the rural level for bananas, cocoa, cassava and groundnuts. We prepared subsector/value chain maps. Then, we reviewed the maps, synthesized information on the production yields, revenue potential, and identified the constraints faced in each subsector. Three main criteria to choose the subsector were identified using the Participatory Rapid Appraisal (PRA) technique of ranking. We felt that the value chain selected should 1) reach large numbers of MSEs from vulnerable populations; 2) lead to a potential increase in income and wealth for micro enterprises; and 3) show potential for value addition. After the ranking exercise, the groundnut subsector was chosen because of the potential market and the potential increase in income for shelled groundnuts was substantial.

Q: What techniques did you use to understand the financial relationships between value chain actors and financial institutions?
We led focus groups in 8 villages over 3 days with 410 farmers. The focus group questions covered how people earned their money, in which months, their expense, when these expenses occurred in a year, what savings mechanisms existed, and if and where they accessed credit. The answers to focus group questions were the quantified and detailed community cash flow maps were prepared. These maps illustrated that credit and savings mechanisms were not sufficient to cover the expenses incurred for agricultural production.

To complement the cash flow maps, semi-structured interviews were conducted with transporters, wholesalers/traders, and local brokers who worked for the wholesaler/traders. These interviews were held all along the chain, from the smaller towns to the capital city.

Q: What did you learn on the financial side?
We discovered that there were no existing relationships between any of the value chain actors and financial institutions (MFIs or banks), but there were some existing informal savings and credit mechanisms. It was clear that these mechanisms were not sufficient for farmers to access the necessary amounts of capital to purchase input supplies. Some farmers have accessed credit from brokers in the past. These brokers set the price for the final product (that they would buy back) at the time of the loan. When farmers sold their product back to the broker, the price was often lower than the market price at the time of harvest. The interest on the loan was discounted from the price as well. Both the project and the farmers identified this as a relationship that could be improved.

Q: How did conducting a value chain analysis (VCA) with a financial services lens benefit your project? What are your next steps?
It allowed us to better focus our resources and efforts. This was particularly important as value chains in Sierra Leone were severely weakened by the 10 years of civil conflict and none have sufficiently recovered. To be effective, we saw that we would have to use the different interventions in harmony to support one chain at many levels. The addition of the financial services lens assured us that, not only would we see the role of credit in the chain, but we would not “re-invent the wheel”. The development of financial services to support shelled groundnuts will be based on the existing systems of seed-banks and village savings and loans (VSLs).

Our next step was to review the proposed interventions with our partners and get their buy-in. This was made simpler by their full involvement in the VCA from the start, so we had the benefit of “preaching to the choir.” We now have champions from each of the international non-governmental organizations that form part of the LINKS project in each area: agriculture, technical assistance, financial services. Their job now is to facilitate and follow-up on the interventions at the different levels.

Q: What would you advise (or not advise) other practitioners in conducting a similar analysis?
Going through the whole process using the financial services lens, rather than adding a survey post-analysis, was valuable. It helped us choose a chain we would be able to strengthen within our timeline and existing programs. As a part of the value chain analysis with the financial services lens, we held cash-flow mapping exercises with the communities and mapped the financial services available in the surrounding towns. This showed us how we could provide technical assistance to strengthen systems with which farmers were already working (seed-banks, VSLs), allowing them to fill an unmet credit need for groundnut input finance. It also showed us that focusing on more traditional trader and transporter credit farther up the chain could provide the necessary boost in input supply. We would also recommend going thought the preliminary review and ranking of the value chains, which led us to choose shelled groundnuts. This process helped us avoid pre-judging, as we might have been tempted to automatically select an export cash crop, like cocoa or coffee. Looking systematically at all the value chains, as well as at our project’s goals and resources, led us to select a local and regional cash crop with a huge unmet demand.
Suresh Subramanian, Chief Operating Officer of International Development Enterprises India (IDEI) says, “It is in the best interest of the farmer or dealer for there to be a variety of financing options available, allowing room for negotiation and more favorable loan conditions.” Providing access to finance to the world’s rural economically poor is a challenging endeavor given the high costs and risk often associated with lending in rural areas. However, two organizations in India, EDA Rural Systems (EDA) and IDEI, are aiming to overcome some of the obstacles the rural poor face in obtaining finance.

EDA and IDEI are developing various financial models that can be grouped into two overall types of strategic alliances. One type of strategic alliance involves financing within the value chain, among different value chain actors, while the other type is financing from outside of the value chain, such as through rural financial institutions or MFIs. Both EDA and IDEI are market development facilitators playing a role in increasing access to finance. EDA has decided to develop the following three models to increase access to finance for litchi farmers:

1. Banks lend to litchi processors, pre-harvest contractors, and wholesalers of litchi fruits, who then lend to litchi growers
2. Banks lend to litchi fruit grower associations
3. Rural credit agents in villages link litchi growers and banks

While EDA is focusing on three financial models for litchi fruit in the Muzzafarpur district in Bihar State, IDEI is looking at five models for farmers to gain finance to purchase drip irrigation for sugarcane and vegetables in Tamil Nadu State. Having a strong strategic partner for a particular financing model, such as a well managed and financially sound sugarcane factory, is key. The five models IDEI is developing all stem from IDEI’s basic model of a drip irrigation dealer extending credit to a farmer. IDEI’s five financial models are the following:

1. Banks lend to farmers with a guarantee from a sugarcane factory
2. Sugarcane factories lend directly to farmer
3. Jaggery plants (a plant that buys lower grade sugarcane to make less processed sugar) partners with dealers to share risk and lend to farmers
4. Banks lend to farmers through self help groups (SHGs) where members take turns taking loans
5. Banks lend to dealers, and the dealers lend to farmers. The dealer is responsible for extending credit as well as recovery.

Lessons are emerging on the advantages and constraints of each financial model as they are being implemented in the field. Look for the up-coming MicroLINKS “Note from the Field” to learn more about EDA and IDEI’s work (www.microlinks.org).