

# ACCESS TO INCLUSIVE AGRIBUSINESS FINANCE

Aspirational issues and priorities for collaboration

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## 1 SUMMARY OF ISSUES

A host of development actors in emerging markets have spent more than 60 years experimenting with approaches to provide farmers with access to financial services. Starting in the 1950s, many governments established agriculture development banks or capitalized commercial banks, both with mandates to lend to smallholders at below-market interest rates. In the 1970s, fuelled by the failures of both directed credit and subsequent laissez-faire policies, micro-finance institutions and some commercial banks began providing microfinance in rural areas. This approach faced challenges too, as most microfinance providers (with the exception of some in Asia) did not ultimately maintain a sustained reach to smallholders. However, a renewed drive at the beginning of the 21st century to connect farmers to financial services has ushered in a new “era of farmer finance”.

Even with these developments, however, the gap between the financial needs of smallholders and the supply of financial services is anticipated to remain significant. Credit provided by informal and formal financial institutions, as well as value chain actors, currently only meets an estimated USD 50 billion of the more than USD 200 billion needed for smallholder finance in the regions of Sub-Saharan Africa, Latin America, and South and Southeast Asia<sup>1</sup>. In addition, agricultural insurance reaches just 10% of smallholders and fewer than 15% have access to a formal savings account. Projected growth of 7% per year from formal institutions and value chain actors will not make a meaningful dent over the next five years.

Changing the trajectory of access to finance for smallholder farmers and SMEs will require a coordinated effort across actors to address today’s most pressing constraints, including:

1. **A gap between farmers’ need and demand for financial products:** At present, farmers’ demand or willingness to pay for formal financial services does not always match their needs. Mistrust of financial institutions is also an influencing factor, as well as farmers’ perceptions of informal options as being better suited to their needs.
2. **Elusive business model returns for financial service providers:** Broadly speaking, the drivers of low returns – well documented by past research – are the high cost of reaching remote customers, the high risk of non-performing loans, and the low revenue generated per customer. Business model innovation is needed to address these complexities.
3. **A mismatch between financial service provider (FSP) capital needs and the type and volume of capital available from investors:** For many FSPs, capital availability is a critical barrier to reaching scale. In addition, available capital often does not meet FSPs’ needs in terms of tenure, currency, or other conditions. Significantly scaling up the sector will require drawing in new and more suitable capital sources and applying new approaches to blending capital.

All actors have a critical role to play in moving the sector towards this new vision of financial inclusion for smallholder farmers. In this new era of farmer finance, a pluralistic, systems-based view of the issues and opportunities needs to be advanced at global, national and local levels.

<sup>1</sup> Initiative for Smallholder Finance and Rural Ag Finance Learning Lab, “*Inflection Point*”, 2016

## 2 ASPIRATIONAL ISSUES FOR A COMMON AGENDA

- Define how the ecosystem of initiatives and actors can better collaborate at a global and national level.
- Establish a stronger evidence base on what models and partnerships work and how they can be further scaled.
- Define how the industry should structure capital and smart subsidy to unlock access to finance, including identifying major gaps for international donors and capital providers.
- Make mainstream how new approaches to product design and technology should be used.

## 3 POTENTIAL RESEARCH AND LEARNING QUESTIONS

### 3.1 Research questions

- How are different networks, alliances and platforms supporting global action around agricultural finance, and what should be done differently around co-ordination and collaboration?
- What are the economics (costs/benefits) of service delivery models that anchor financial and other services for smallholder farmers?
- What evidence exists of the efficacy of different approaches to blended finance and subsidy applied to facilitate access to agricultural finance?
- How can subsidies and blended finance be efficiently deployed where needed to reduce risk and enable smallholder finance?

### 3.2 Learning questions

- What service delivery models and partnership models are working to anchor access to financial services and how sustainable or scalable are they?
- How can the latest advances in technology and product design be mainstreamed to enhance the way in which financial institutions and other organizations provide financial services to smallholder farmers?
- How should different actors within the broader ecosystem collaborate more effectively at a global and national level to drive better access to finance in agricultural value chains?

## 4 POTENTIAL PRIORITY AREAS

Action is needed in all areas of the industry, but particularly around five key themes:

- **Smart subsidy:** With few models achieving commercial scale and sustainability, further work needs to be done on how blended finance and subsidy should be effectively structured to enable finance in agricultural markets.
- **Progressive partnerships and service delivery models:** New evidence and rigor needs to be brought to understanding the economics and effectiveness of different service delivery models and partnership models.
- **Customer centric design:** Ongoing work is needed to advance approaches to designing products that specifically address the needs of smallholder farmers.
- **Use of technology:** Technologies hold immense potential for transforming the costs and risk management approaches used in the provision of financial services. Ongoing research and work needs to be done to push the boundaries of what is possible with these new tools.
- **Capacity development:** Technical, managerial and business know-how of farmers is essential to explain the methods and criteria the banks use to evaluate financial assistance and application to borrowers.



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## 5 ONGOING WORK

**Development banks** are strong actors in promoting the smallholder finance agenda. Development finance institutes like *ADB*, *AfDB*, *IFC*, *IADB* and *bilateral development banks* are increasingly interested in smallholder agriculture as an investment case for their private sector and sovereign operations.

**Commercial banks** can do more but need to know better. Apart from impact investors, commercial banks are also getting increasingly interested in the smallholder agriculture space. However, the sum of their investments is still small, given the limited number of bankable deals, risk perceptions in the sector, and investment procedures that somehow dis-favour smaller deals in the range of USD 3–50 million which are typical for inclusive business models.

**AgDevCo** is a specialist agriculture impact investor that has established a Smallholder Development Unit (SDU).

**AGRA's Financial Inclusion for Smallholder Farmers in Africa Program** works with financial institutions and agriculture value chain actors.

**AgriFin** is a special initiative to increase access to financial services for farmers and agribusinesses and focusses on activities that promote knowledge-sharing and networking among financial institutions globally.

**CGAP** leads a dedicated research and business model development program that focuses on user-centric product design and farmer segmentation.

**The Council on Smallholder Agricultural Finance (CSAF)** is an alliance focused on developing a thriving financial market to serve small and growing agricultural businesses in low- and medium-income countries. It is made up of nine social lenders, including Root Capital, Oikocredit, ResponsAbility, and Triodos.

**EU AgriFi** aims at increasing investment in smallholder agriculture and agribusiness by mobilizing public and private investment, in particular through the provision of risk capital, guarantees or other risk-sharing mechanisms.

**IDH** (the sustainable trade initiative) works on sustainable trade across a variety of commodity markets with a focus on understanding how different service delivery models can underpin provision of financial services for smallholder farmers.

**Initiative for Smallholder Finance (ISF)** is a multi-donor and investor platform for the development of financial services for the smallholder farmer market. With a focus on research and catalysing investment, the ISF has developed a strong knowledge base around the provision of financial services for smallholder farmers. See <http://www.initiativeforsmallholderfinance.org/> for an overview of their industry research.

**MasterCard Foundation Fund for Rural Prosperity** enables businesses to begin or expand financial services in rural areas of Sub-Saharan Africa.

**Propagate** is a coalition of smallholder finance practitioners focused on microfinance institutions, including BRAC, One Acre Fund, and Juhudi Kilimo.

**Rural and Agricultural Finance (RAF) Learning Lab** fosters knowledge creation, sharing and collaboration that leads to better financial solutions for smallholder farmers and other rural clients. Link to the learning agenda: <https://www.raflerning.org/about/agenda>



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## 6 RESOURCES AND PREVIOUS WORK

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| <p>1. <b>Initiative for Smallholder Finance and RAF Learning Lab.</b> 2016. <i>Inflection Point: Unlocking growth in the era of farmer finance.</i></p> | <p>Provides a sophisticated picture of how the smallholder finance space currently operates by describing the key actors and the nature of their interactions, and conceptualizing these in a new “industry model”.</p> |
| <p>2. <b>RAF Learning Lab: Learning brief:</b> The business case for digitally-enabled smallholder finance</p>  | <p>The Learning Lab’s second deep-dive exercise explores the business case for smallholder finance, in particular the role of digital approaches in making it possible to profitably serve this market at scale.</p>    |
| <p>3. <b>IDH:</b> Service delivery models research</p>  | <p>This research brings a quantitative approach to supply chain structures that can facilitate access to finance and other services for smallholder farmers.</p>  |
| <p>4. <b>CGAP:</b> <i>Designing Digital Financial Services for Smallholder Families</i></p>   | <p>This publication builds on past segmentation research to explore design dynamics for smallholder farmer financial services and the importance of user-centred design.</p>  |
| <p>5. <b>IFC.</b> 2014. <i>Access to Finance for Smallholder Farmers. Learning from Experiences of Microfinance Institutions in Latin America.</i></p>  | <p>A study to identify and disseminate the best practices of MFIs that have successfully implemented agricultural lending operations targeting smallholders in Latin America and the Caribbean.</p>                     |
| <p>6. <b>Root Capital.</b> 2017. <i>Towards the Efficient Impact Frontier</i>, by McCreless, M.</p>   | <p>An approach to building a portfolio with the greatest possible impact for the level of expected return.</p>  |
| <p>7. <b>World Bank Group.</b> 2016. Agriculture Finance Support Facility: Lessons Learned</p>  | <p>Lessons learned from AGriFin’s Technical Assistance program.</p>   |

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This paper is part of a set of six that explore the six themes covered in the design workshop “Towards a Global Research and Learning Agenda for Inclusive Agribusiness”. Over two days 40 senior practitioners looked at how to deepen understanding and improve practice through more structured collaboration. While the themes do not cover all that is important in inclusive agribusiness, they are part of the potential for structural and systemic change inherent in many initiatives.

Each paper aims to trigger thinking on what could be done through collective action. It does not provide a complete picture of the theme but indicates the bandwidth of possibilities that could be worked on. We hope it will help you think where working with others can make your work easier, more interesting or more useful. For more information or if you have ideas please get in touch with [joost.guijt@wur.nl](mailto:joost.guijt@wur.nl).

The workshop was a good example of the value of combining skills and resources, and came out of joint thinking, time and funding from Wageningen University & Research, Global Donor Platform for Rural Development, Food & Business Knowledge Platform and BEAM Exchange.

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This paper is part of a series of papers on inclusive agribusiness written for the “Towards a Global Research and Learning Agenda for Inclusive Agribusiness” workshop in March 2017. Read all the papers as well as a series of blogs on ‘What’s new in inclusive agribusiness’ here: <http://www.inclusivebusinesshub.org/inclusive-agribusiness/>