

Good Practices in Agricultural Value Chain Financing

Savings and Credit Forum

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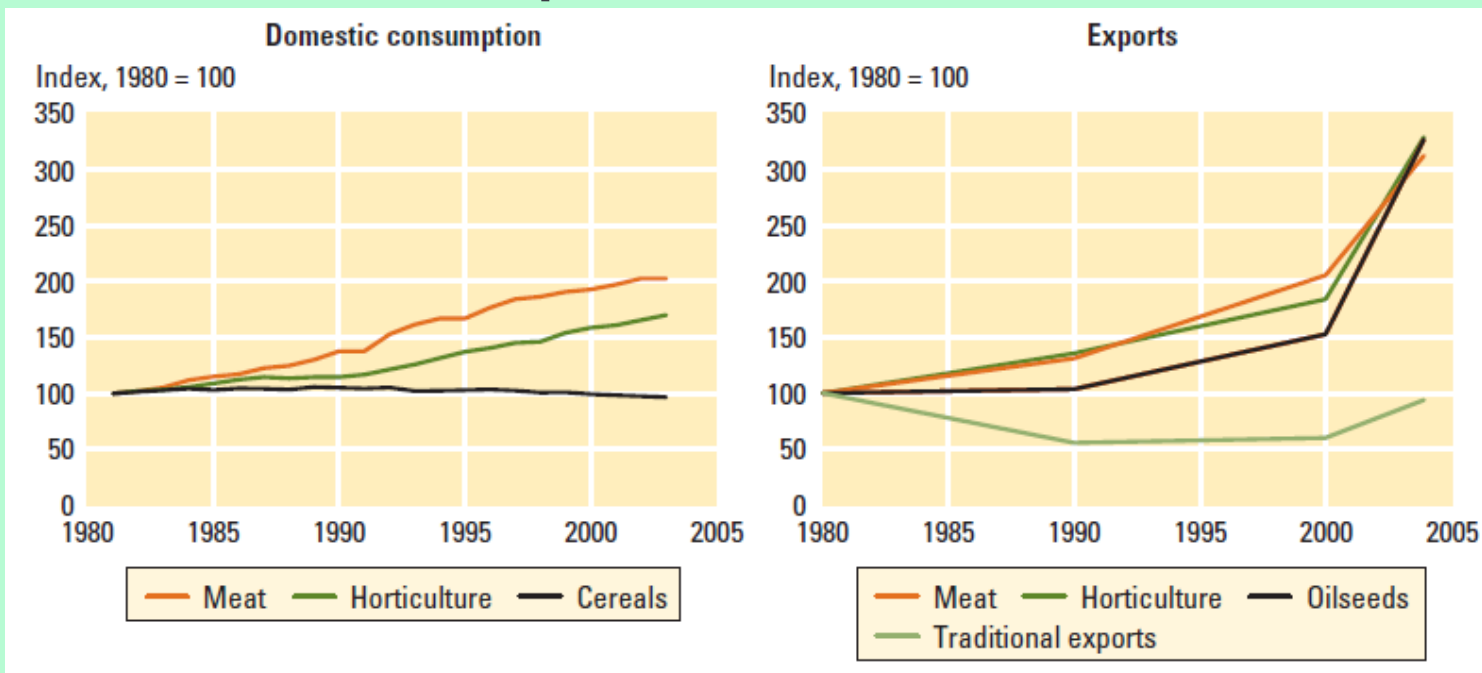


Presentation: Agricultural VCF

1. The changing agricultural scene
2. Using strategic alliances in financing
3. Value chains as a business approach
finance
4. Value chain financing products
5. Lessons and policies



New Opportunities for Agricultural Development



Source: <http://faostat.fao.org> and <http://comtrade.org>

Note: agro-processed goods represent an expanding market in agriculture worldwide

Expanding **high-rent markets** in agriculture represent an enormous opportunity for the sector's growth

An Evolving Agriculture

- Market integration
 - ✓ Tighter supply and value chains
 - ✓ Increased concentration of power of market leaders
- Open trade with intense regional and global competition
- Consumer changes
 - ✓ Segmented demand
 - ✓ Stringent standards, specifications and conditions
- Information and communication technology (ICT)
 - ✓ access to information is easier and more important
 - ✓ back-office technologies are more robust to manage data



The Concept of AVCF

Where do farmers and agro-processors turn when banks or other financial institutions are unable or unwilling to provide them with financial services?



What is a value chain?

Value Chain describes the full range of activities involved in getting a product or service from conception, through the different phases of production, transformation and delivery to the final consumer.



Value chain finance – financial products and services flowing ***to*** and/or ***through*** a VC to address the needs of those involved in that chain, be it a need for finance, a need to secure sales, procure products, reduce risk and/or improve efficiency within the chain.

Objectives:

- Align and structure financial products to fit the chain
- Reduce costs and risks of finance



The use of VCF

- Supply (or Value) Chain Finance is the next wave of cost improvement for organizations. More than two-thirds of companies are investigating or putting in place supply chain finance programs to improve financial metrics and lower end-to-end costs.

The Aberdeen Group

- The worldwide market for receivables finance is US\$1.3 trillion. Payables discounting is US\$100 billion and asset-based lending is US\$340 billion.

- With the financial and economic crisis, value chain finance is more important than ever.

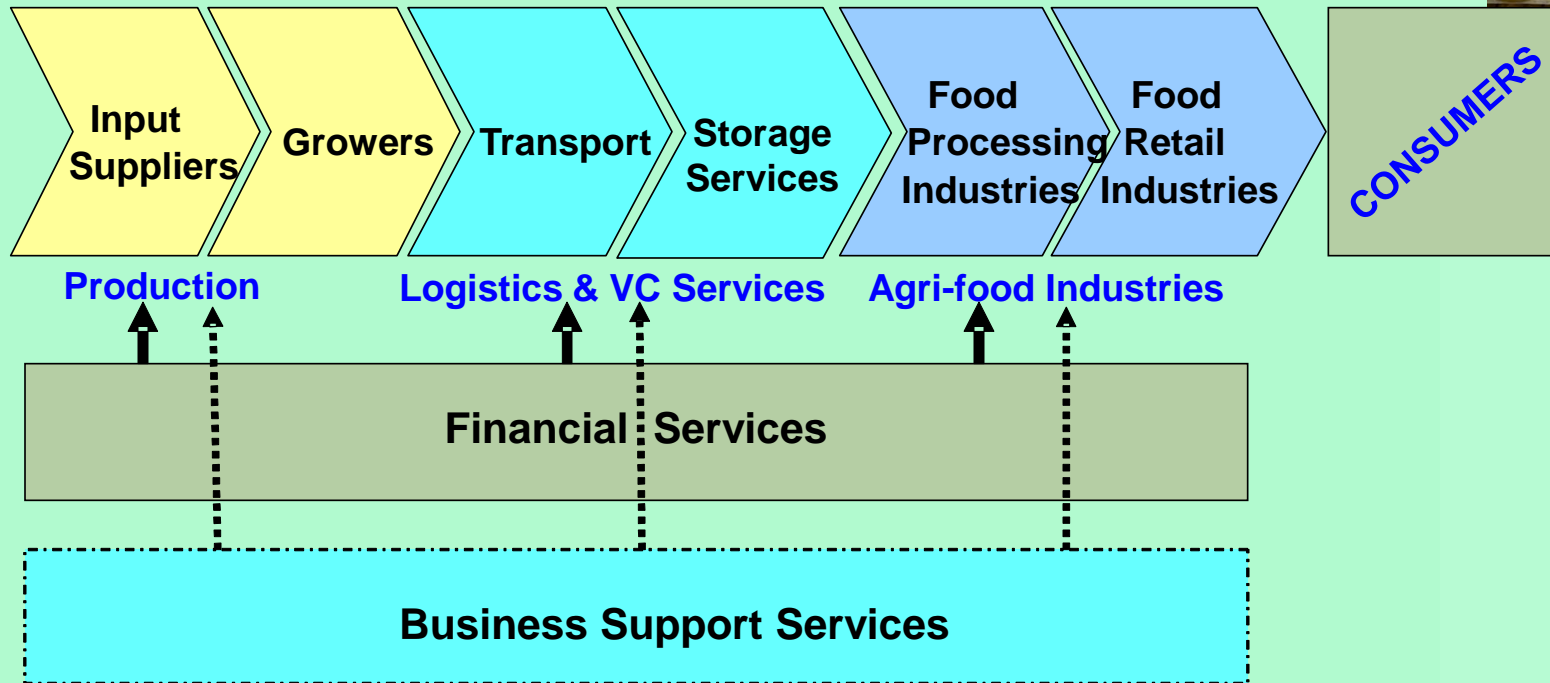
Ken Shwedel, Rabobank Mexico



Stakeholder Roles in Agricultural VCs



Operating Environment



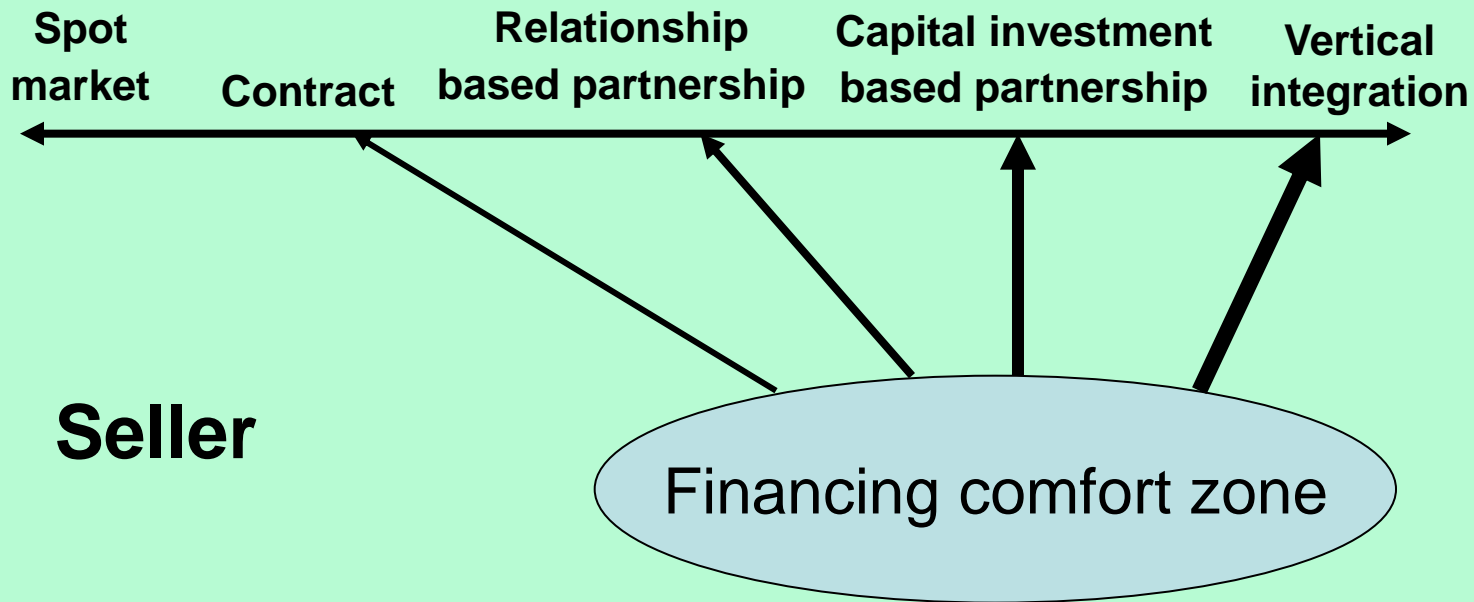
Identification of:

- *Structure* of the value chain: all individuals and firms that conduct business by adding value and helping move the product toward the end markets
- *External* framework, or the broader legal / national context in which the chain operates
- *Dynamics* of the value chain: individual and firm behaviors and how these affect the functioning of the chain
- *Trends* and future *risks* and *opportunities* in the chain and its participants

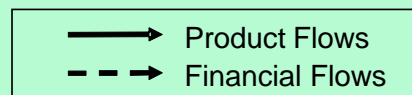
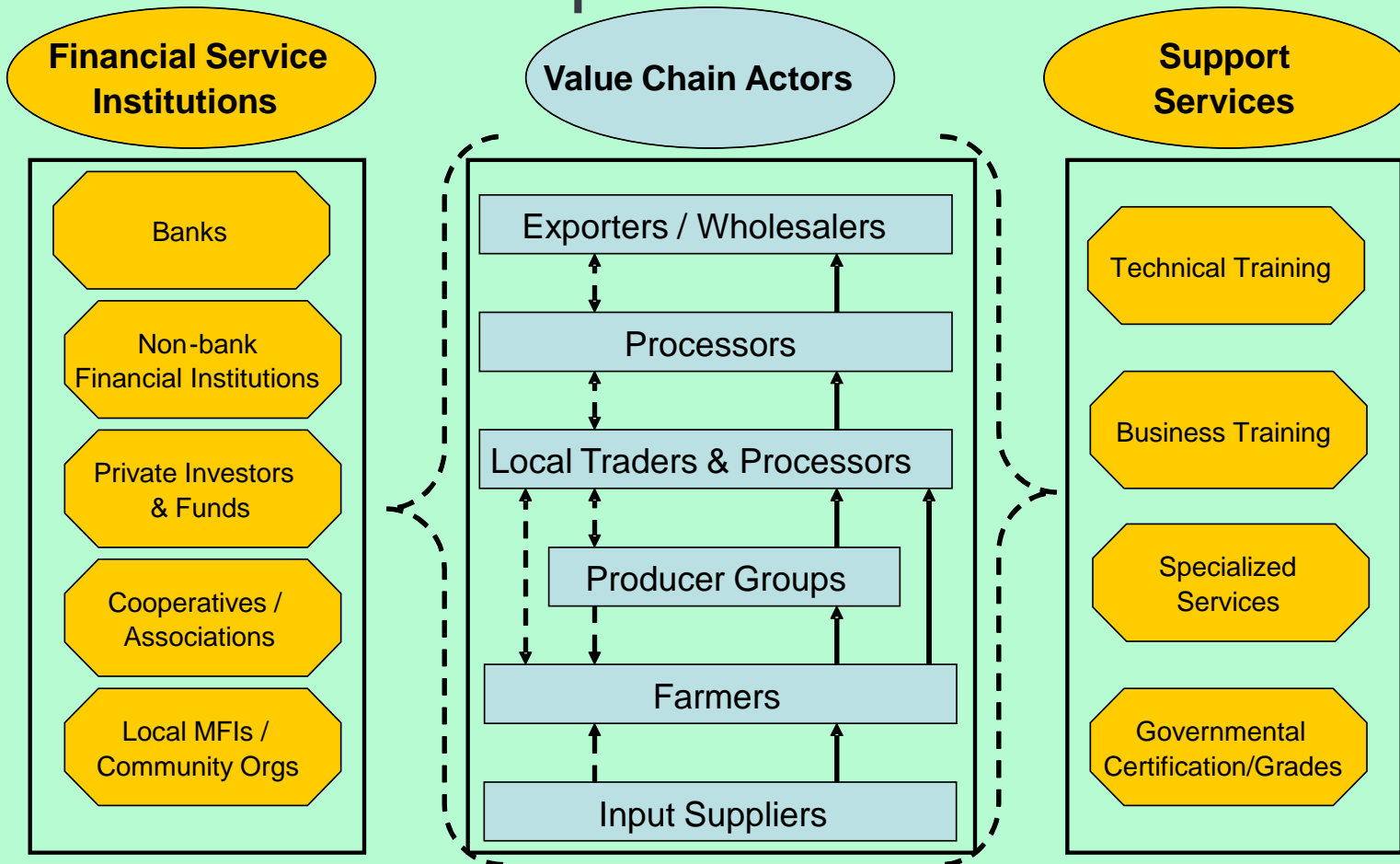


Value Chain Relationship Structures

Buyer



Product and Financial Flows along a VC



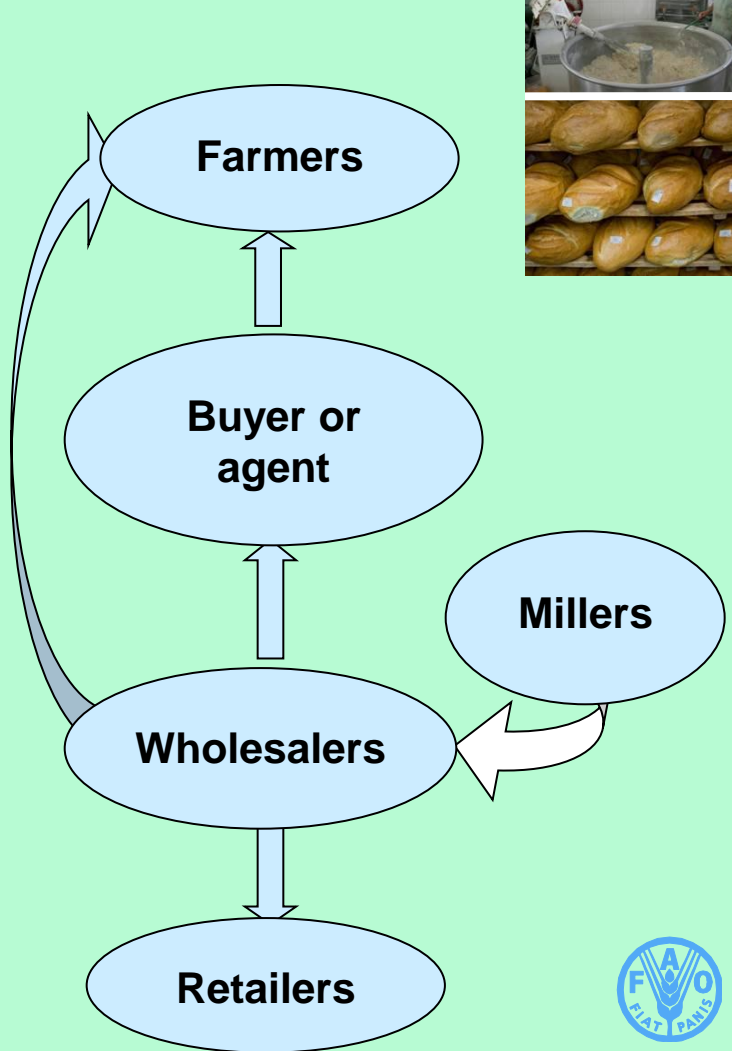
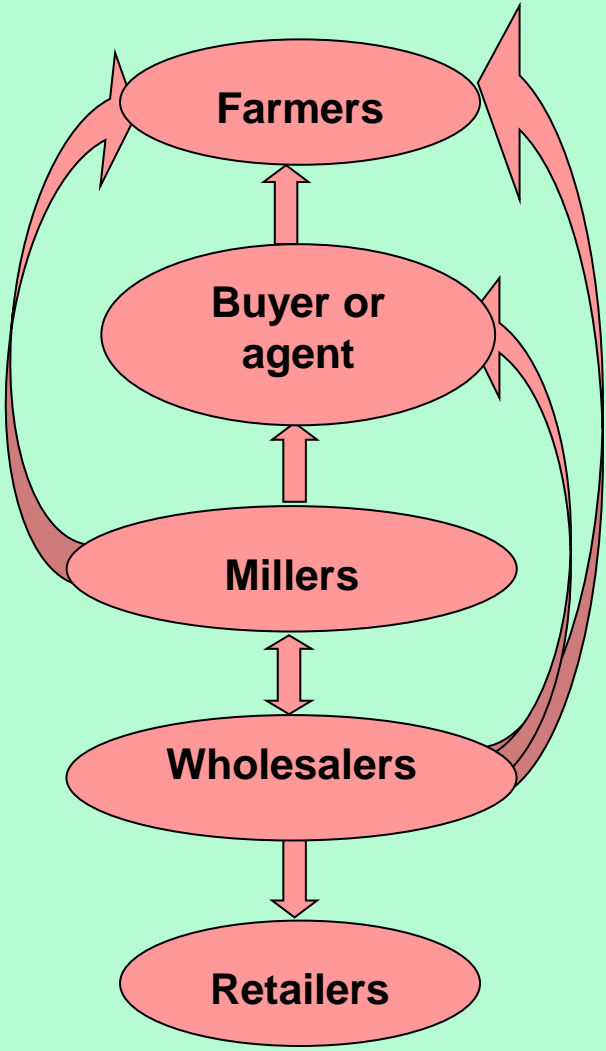
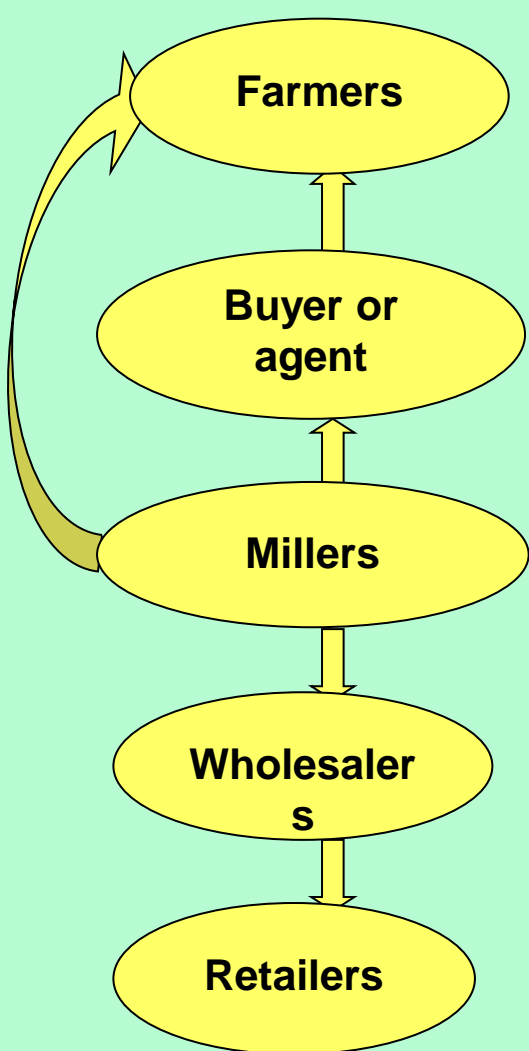
Example: Flow of finance in rice VCs



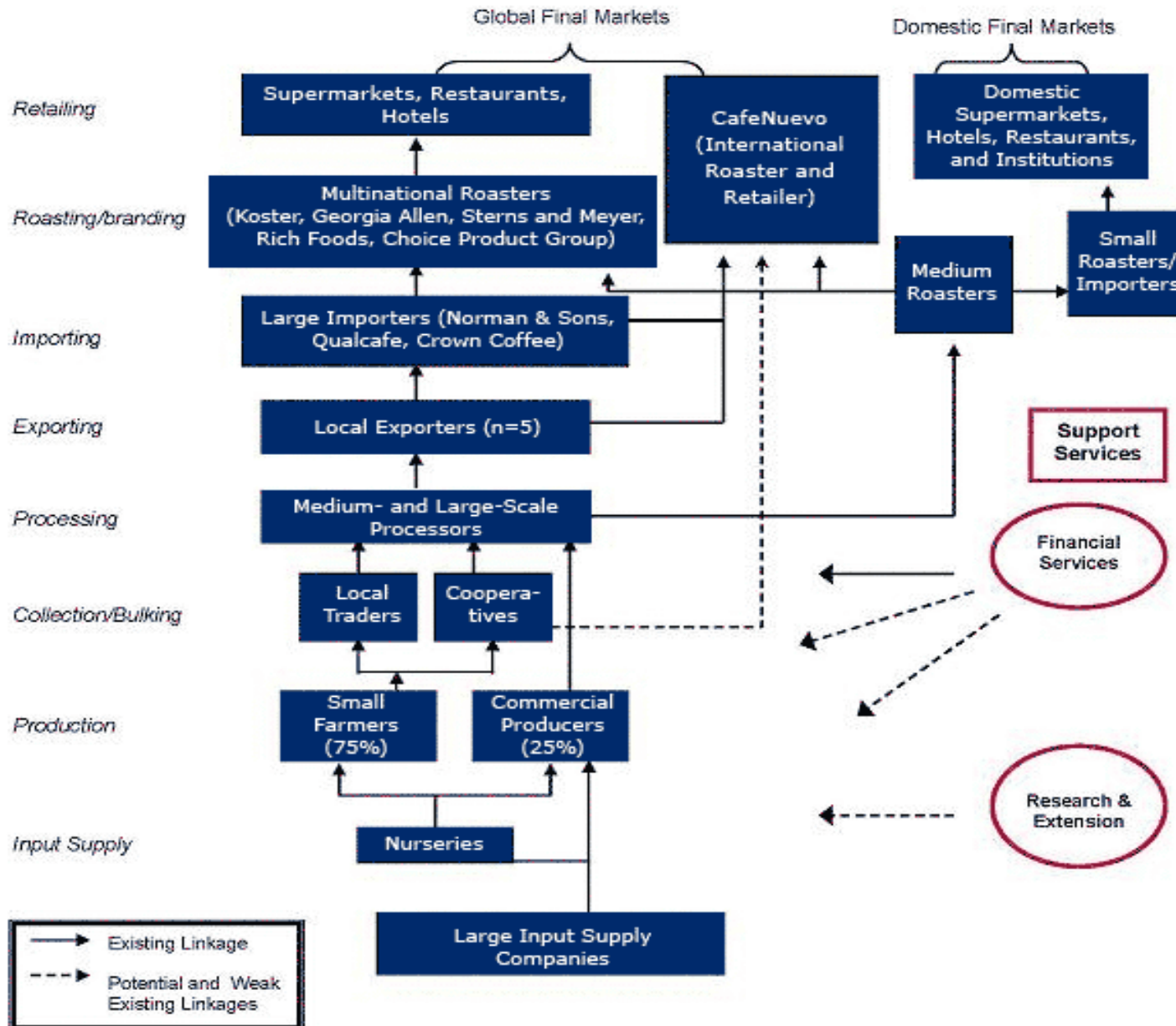
Asia

Latin America

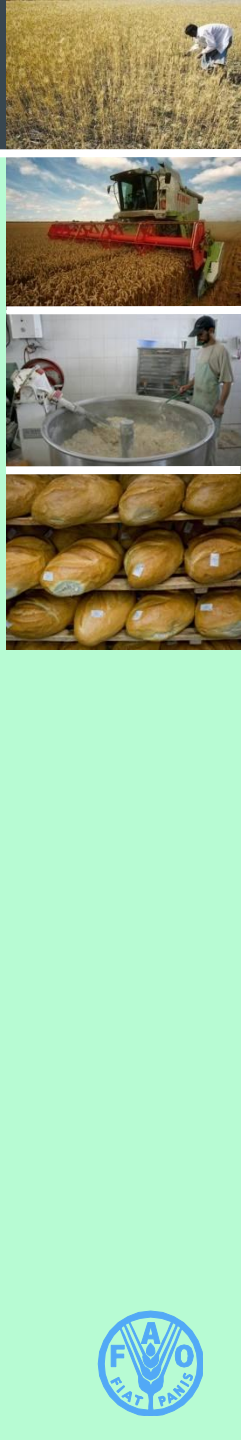
Africa



Example: Knowing the sector and VC



AVCF: Demand side



Demand

Needs of finance

Input suppliers

Seeds, fertilizers, pesticides, livestock feed, medicines, farm equipment

Growers

Farmers, dairy units, fisheries and other livestock growers

Storage & warehousing

Storage facilities for grains, fruits vegetables; cold chains & logistics

Processors

Processing plants, packaging facilities etc.

Retailers & wholesalers

Inventory, trading & marketing

Exporters

Pre & post-shipment commitments

AVCF: Supply side

Financial Intermediaries

1. Commercial banks
2. Credit unions
3. Co-op banks
4. Agriculture & Dev. banks
5. Microfinance institutions
6. Non-bank financial inst.
7. Leasing companies
8. Insurance companies
9. Venture capital investors
10. Private investor funds

Non-financial Intermediaries

1. Input suppliers
2. Equipment suppliers
3. Marketing companies
4. Traders & wholesalers
5. Exporters
6. Lead farms/firms
7. Corporations
8. Farmers' organisations
9. Producers' companies
10. Family & friends

Governmental subsidies on inputs and exports and tax incentives may also contribute as a source of finance



Approach: Why is AVCF Important?

1. It allows sellers of inputs to increase sales
2. It facilitates produce buyers to get what they want when they want it (quantity, quality, timing, & price of goods)
3. Financial institutions can learn from and engage more with value chain actors in order to develop new products and reach new markets
4. The Value Chain approach as a comprehensive approach to lending is useful for improving and expanding financial services, not just for enterprise development

If designed well, value chain finance interventions can increase the competitiveness of small producers, as well as a range of agricultural and agribusiness enterprises.



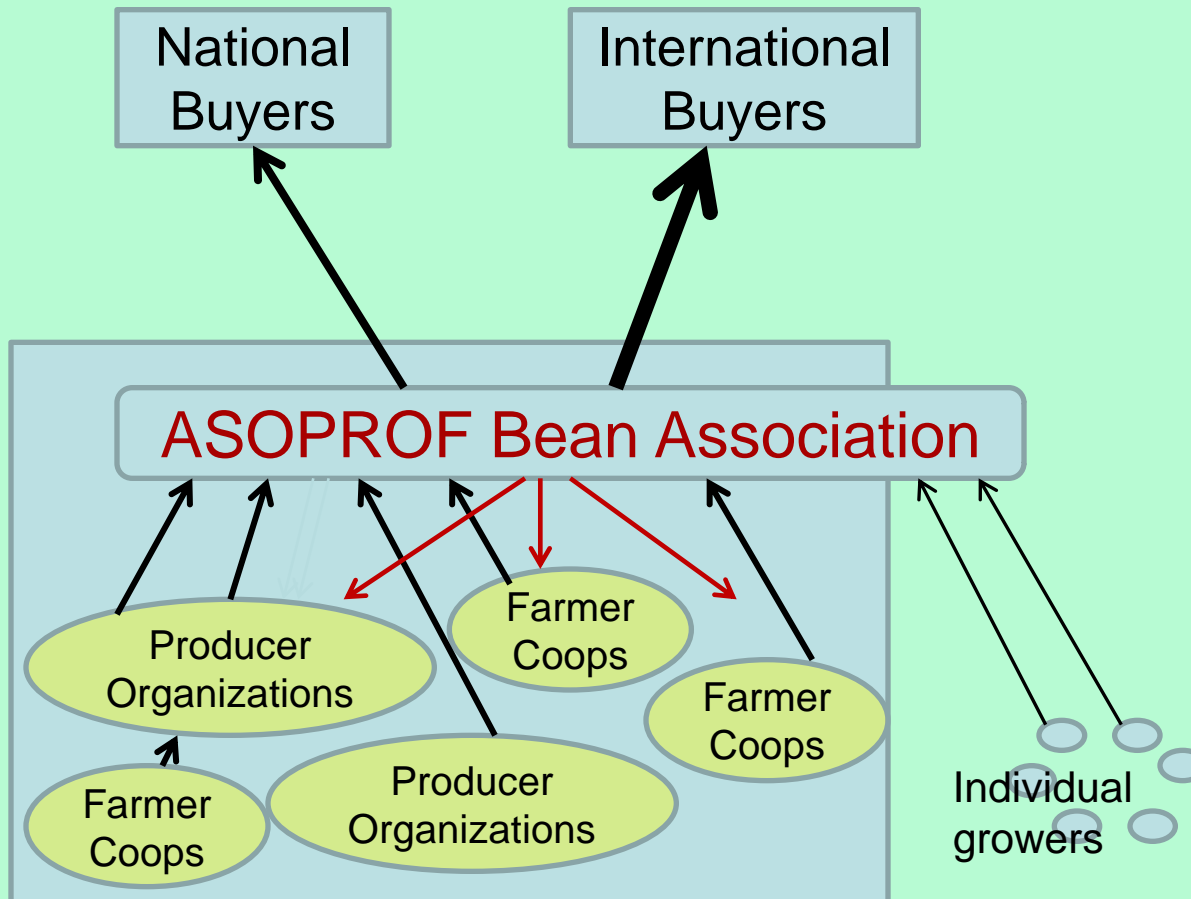


Business models in agriculture value chains in terms of small holders can be divided into four types:

- Producer-driven
- Buyer-driven
- Facilitator-driven
- Integrated

Example: Producer-driven Models

ASOPROF Producer-owned Model



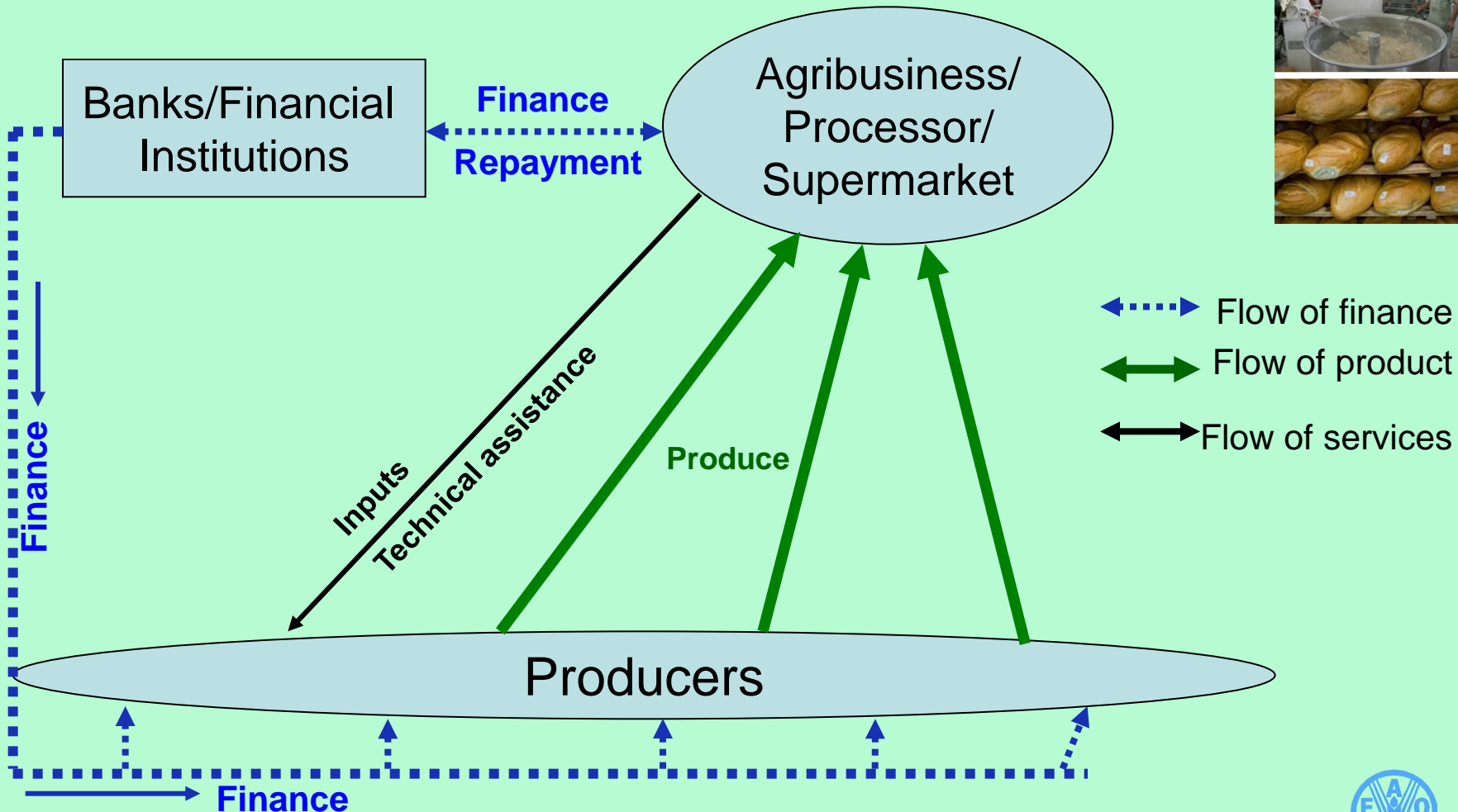
ASOPROF Services:

- Seed production
- Technical assistance
- Processing
- Marketing/export
- Member profit share
- Financing linkages (not direct financing)



Example: Buyer-driven Models

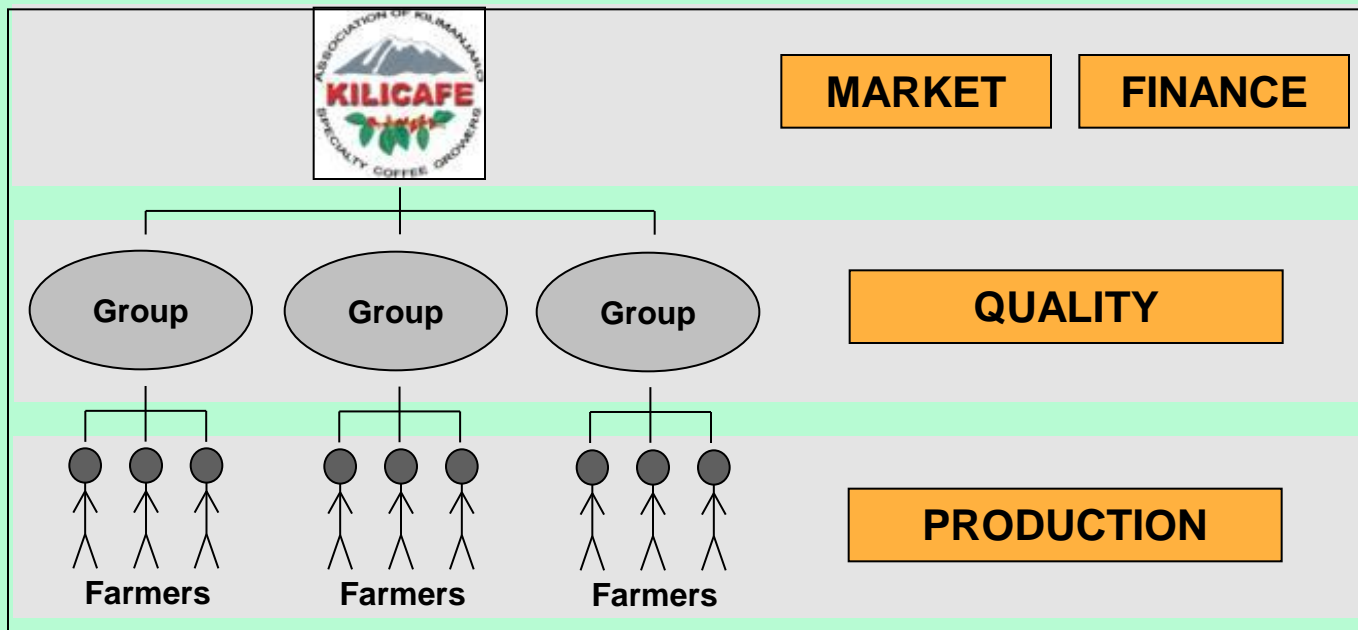
Contract farming with indirect financial flows



Example: Facilitator-driven Business Model

TechnoServe Model

- Supporting a service provider to provide marketing support and financial partnerships with farmer groups
- Identify and organize farmers' groups with the potential to produce quality
- Help groups to improve production quality



Example: LAFISE Integrated AVCF Model



1



Identify organized producers

2



Financing:

- * Asset management
- * Warehouse receipts



Technical Assistance
Quality Certification

3



Productora cosecha



Insurance - transport, life, fire, etc.

4



Consolidation



Processing Added Value



Product in storage

5



Identify markets And buyers



Place Products



Network of offices in 10 countries



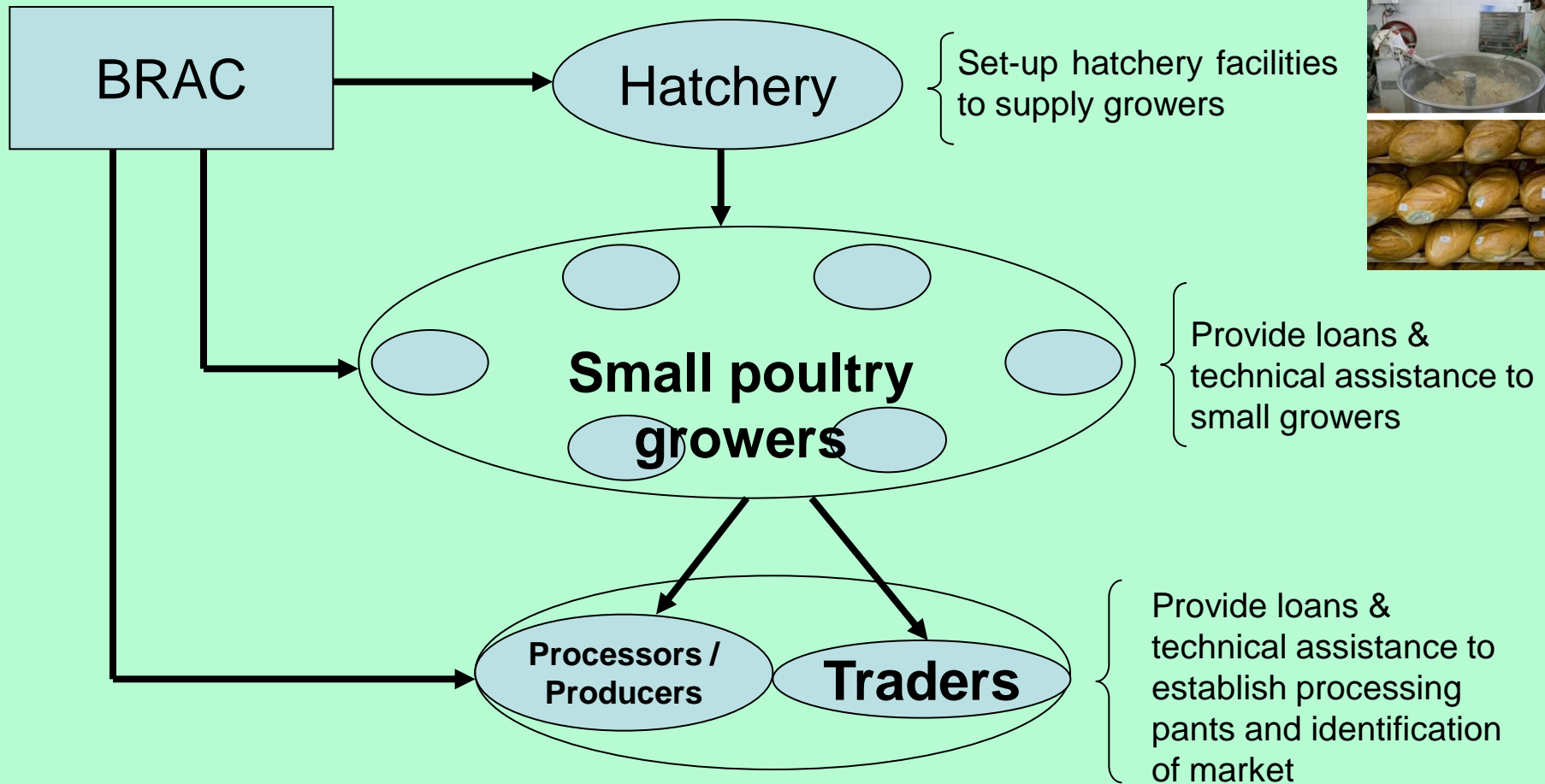
Certification of Deposit and Warrants

Collection and payment to producer

6

Example: Integrated AVCF Business Model

BRAC Integrated Model



AVCF Tools/Instruments

1. Product Financing

2. Receivable Financing

3. Physical Asset Collateralization

4. Risk Mitigation Products

5. Financial Enhancements





1. Product Financing

1.a) Trader Credit

1.b) Input Supplier Credit

1.c) Marketing Company Credit

1.d) Lead Firm Financing



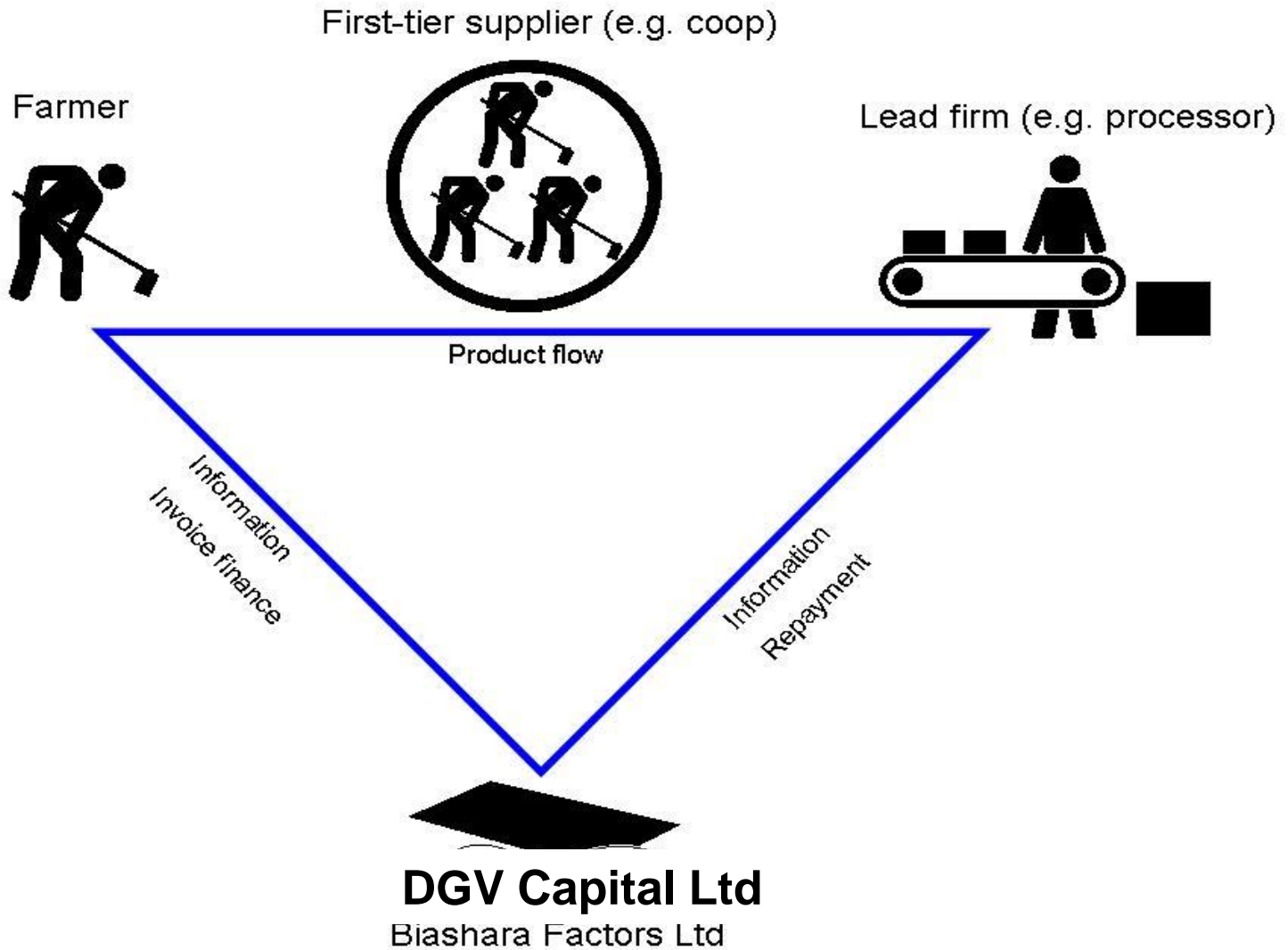
2. Receivable Financing

2.a) Trade Receivable Finance

2.b) Factoring

2.c) Forfaiting

Example: Dederby Green Ventures





3. Physical Assets Collateralization

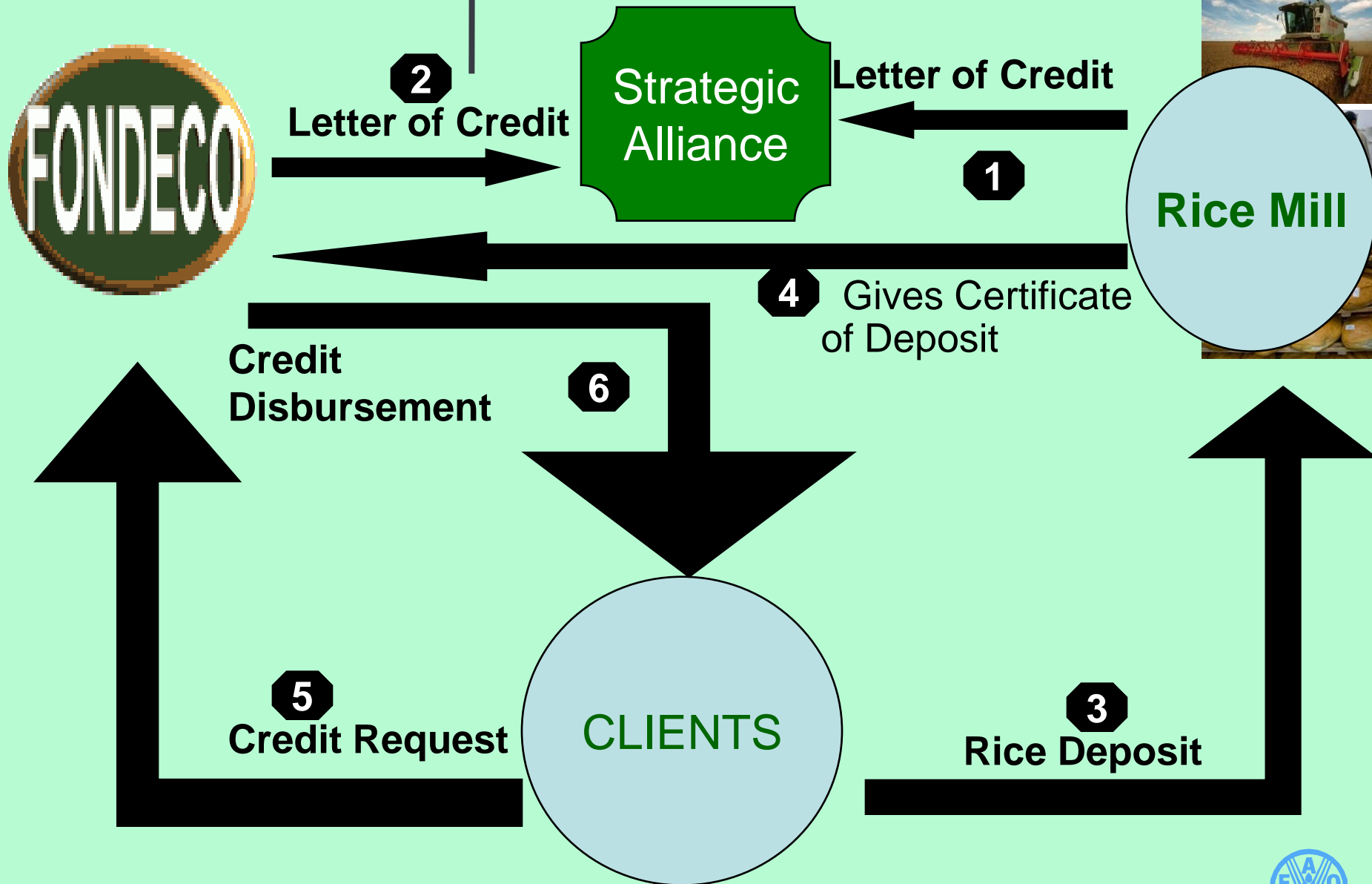
3.a) Warehouse Receipts

3.b) Financial Lease (Lease-purchase)

3.c) Repurchase Agreement (Repos)



Example: Warehouse Receipts



4. Risk Mitigation Products

4.a) Insurance

4.b) Forward contracts

4.c) Futures



Tools to Mitigate Market Risks

- Use of futures and options
- Warehouse receipt finance
- Market information services
- Contract farming
- Insurance
- Access to technical assistance

Some risk management tools are more practical for agro-industries and wholesalers, but can stabilize prices and reduce risks for all producers and bankers.





5. Financial Enhancements

5.a) Securitization Instruments

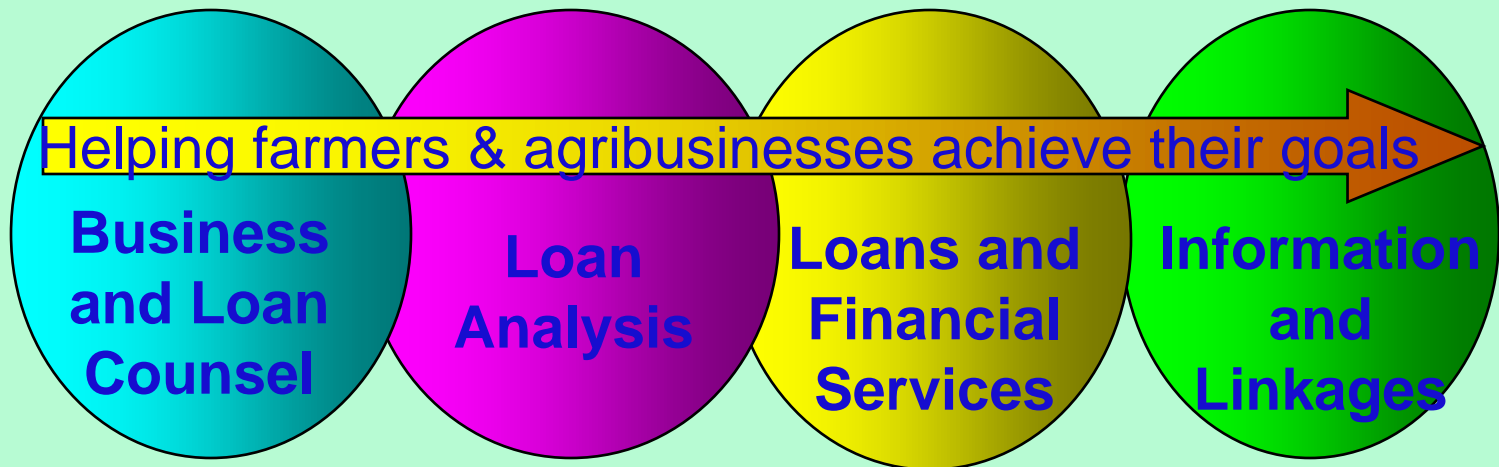
5.b) Loan Guarantees

5.c) Joint Venture Finance

NACF, Korea

Banks are not technical advisors but should invest money & knowledge in the value chains they finance:

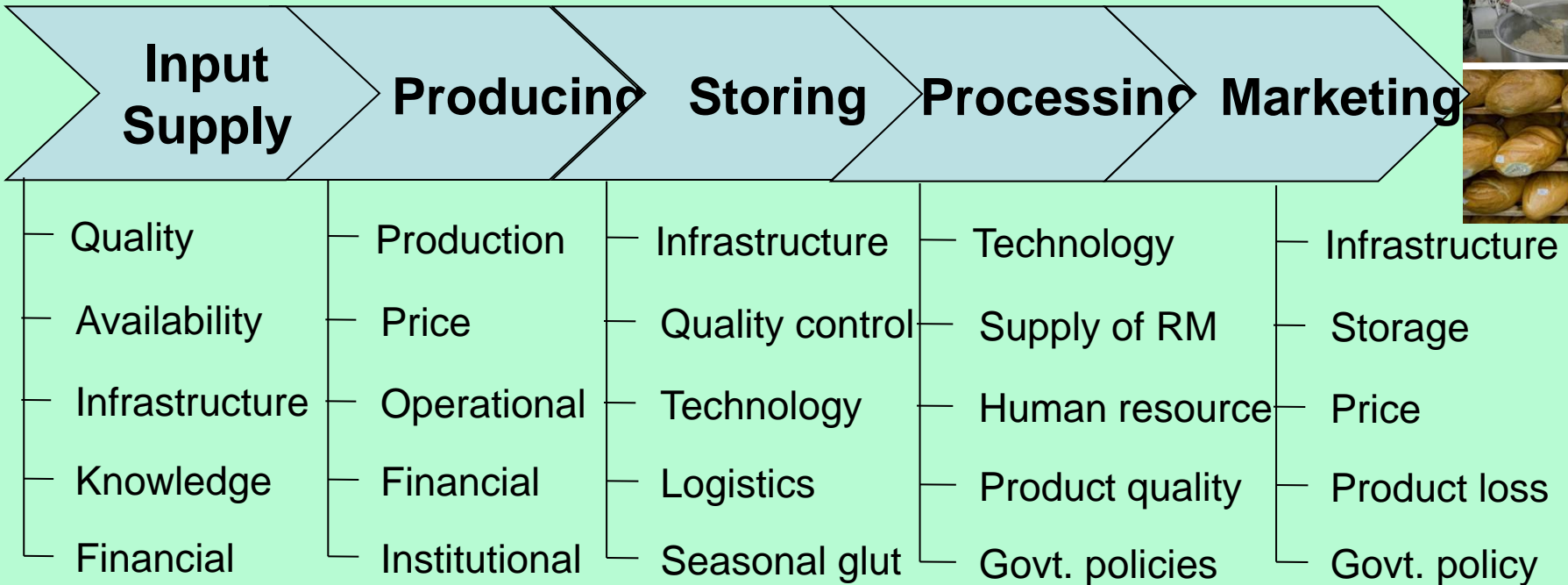
- market trend knowledge
- understanding of key risks
- alliance and linkage opportunities



Addressing Risks along the VC



Knowledge risk is one major risk that can be readily addressed through VCF



*From supply-driven “how we lend”
to client driven “how can we structure
finance to address client needs and risks”*

Summary: Key Factors for Consideration

- Understanding 
 - market and industry
 - client and strategic partners
- Administration 
 - fund the chain at most strategic points
 - ensure effective and transparent partnerships
- Risk 
 - innovate with new technologies and products
 - take advantage of the value chain
 - analyze and structure loans properly
- Service 
 - offer timely, multiple and flexible financial services
 - focus on client and business



13 Lessons to consider for AVCF

1. Use a comprehensive assessment approach
2. Make use of insider knowledge
3. Beware of the weakest link
4. Be forward focused on market and future
5. Use but re-focus 5 C's credit assessment
6. Embed finance for access and efficiency
7. Reduce financial risk reduction by financing through the strongest chain actors



13 Lessons to consider for AVCF

8. Apply innovation; it's needed for competitiveness
9. Chain diversification is important
10. Structure finance to fit the VC, applying models and diverse instruments accordingly
11. Emulates stakeholder participation or mutual interest in banking
12. AVCF is a struggle for policy makers and Central Bankers; development agencies can help
13. AVCF does not replace traditional finance



Government: Policies to Support AVCF

- Business capacity building and market integration
- Contract farming and out-grower schemes
- Technical capacity in market norms and standards
- Commodity exchanges and active futures markets
- Insurance innovation, data collection and initiation
- Market information and access
- Infrastructural investment
- Product and service innovation and diversity
- Technology adaptation and access

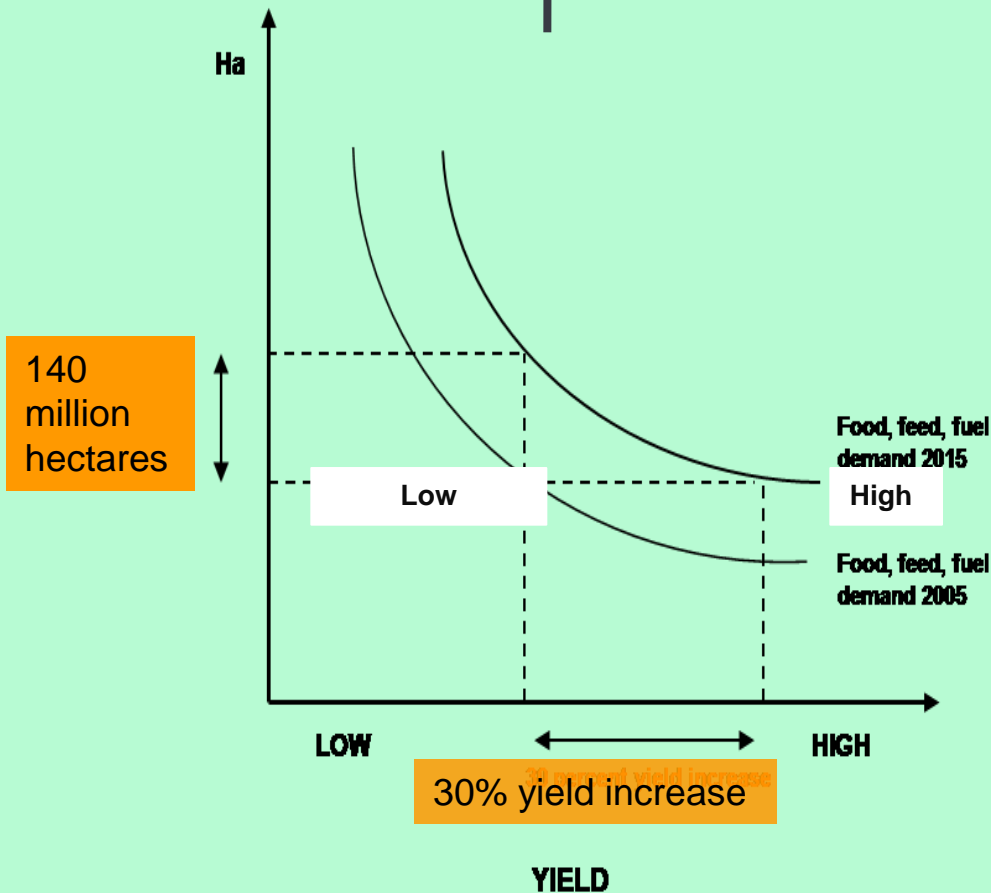


Enabling Environment Requirements

- Agriculture extension services
- Strengthened farmer and producer companies/organisations.
- Contract farming and outgrower schemes to build economies of scale for suppliers and for farmer competitiveness
- Promotion of agribusiness as a sub-sector.
- Import and export competitiveness
- Legal structures which ensure fairness



Need: Food Security Challenge



The economic crisis is ending but the food crisis persists. The organization and financing of the agricultural chains will require 860 million small producers to meet the food requirements for the future. K. Shwedel, Rabobank Mexico



Useful Websites

» **FAO**

www.fao.org/ag/ags



» **Rural Finance Learning Centre**

www.ruralfinance.org



Thank You