

Fair Trade – Investing in Sustainable Agriculture

The case of SOPACDI Congo



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Who we are and how we arrived at financing SOPACDI, Congo

FAIR TRADE

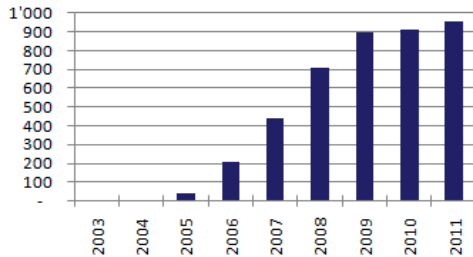
1. Fair Trade: Background & Basics
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INVESTING IN FAIR TRADE

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4. Types of Investments
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Who we are

A world leading social investor



- Founded in 2003
- 1 billion USD AuM
- 8 products investing in microfinance, fair trade and SME financing in developing countries, debt and equity
- 40 Fair Trade clients, 7 different commodities and approx. 50 M USD disbursed 2011 YTD
- 80 people
- 8 offices, in Switzerland, France, Peru, Kenya, India, Hong Kong, Lebanon, Melbourne
- FINMA-regulated asset manager
- Focus on risk management, transparent reporting and corporate governance

rA and FT

The short story

1. Starting point: Agriculture is very important!

- $\frac{3}{4}$ of the world's poor depend on agriculture for their income
- Increasing global demand for food vs. lack of investment holding back food supply

2. The problem: Vulnerability, unfair trading system & lack of credit

- Small farmers face a number of problems, from volatile prices, low incomes to lack of financing

3. One Solution: (Investing in) Fair Trade

- Fair Trade principles and system: better trading conditions
- Investing in Fair Trade: Access to Finance

4. The Outcome

- Fairer prices and income for farmers. More environmental and social protection.
- Fair products for consumer in Switzerland etc.

The case of SOPACDI, Democratic Republic of Congo

The recent history of DRC :

- **Democratic Republic of the Congo remains one of the poorest countries in the world** with a 2010 HDI ranking 134th over 135 (UNDP ranking)
- **Income per Capita among the lowest in Sub-Saharan Africa:** 80% of DRC population lives with less than 2 dollars a day
- 44.4% of the population is under 14 years old
- Two recent conflicts (the First Congo War and Second Congo War, **claimed over five million lives** since 1996)
- The coffee sector in DRC has declined in line with the rest of DRC's agricultural economy for the last 50 years since Independence. With the restoration of security, there is currently a significant opportunity to start to rebuild the coffee sector



The case of SOPACDI, Democratic Republic of Congo

- The main reason for starting the cooperative was to help farmers realize the true benefits of growing coffee through increasing coffee prices
- The cooperative was initially started by 19 members in 2008, but has grown since then and now **includes 3,195 small holder farmers**
- SOPACDI is based in Minova, Northern Kivu and employs 3 full time permanent staff
- In the Kivu region, Arabica coffee is the only major cash crop in the area offering a significant potential of economic development
- Growth of coffee volumes since 2008 multiplied by 10



SOPACDI, Democratic Republic of Congo



Details

- Provide cash to the FT coop to purchase coffee from its 3.195 small holders farmers most of them making less than 2 \$/day
- Located in the Kivu region, battered by several conflicts and volcano eruptions
- Founded in 2008
- More coffee Sopacdi can buy from its farmers, greater will be the social impact

Investment Facts

Type of funding:	Pre-export finance
Investments:	USD 200 K debt
Interests:	10.50%
Duration:	6 Months



A. FAIR TRADE

- 1. Fair Trade: Problem and Solution**
- 2. Fair Trade Value Chain**

A. FAIR TRADE

1. Problem & solution

1. Fair Trade: Problem & solution

Problem



Solution

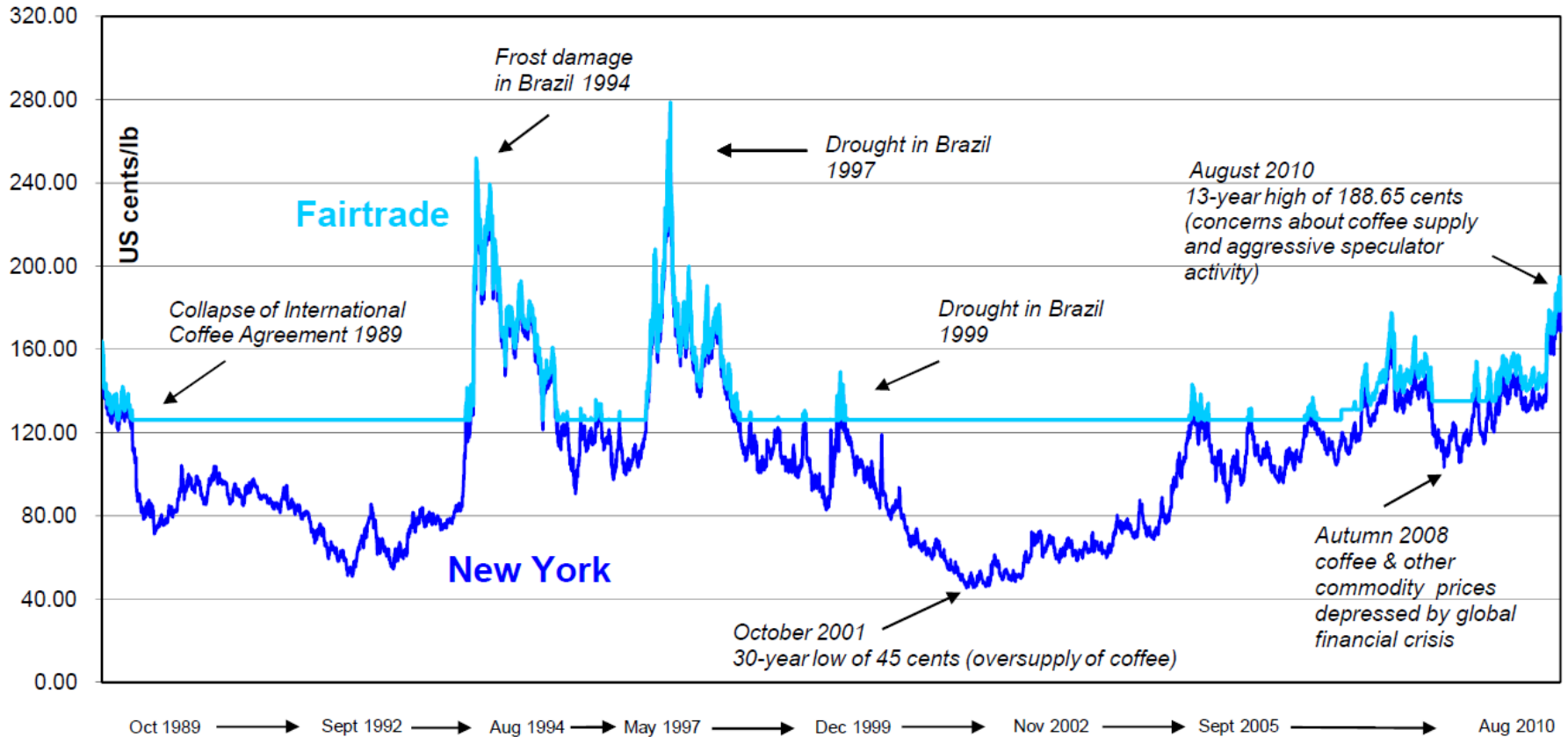
- Most agricultural producers are **small farmers**
- Highly **vulnerable** livelihoods, no possibilities to develop
- They lack **scale, knowhow, skills and assets** to be more productive, avoid exploitation by local traders and deal with major risks:
 - Highly **volatile commodity prices**
 - No bargaining power (→ low prices) and no market access
 - very limited potential for processing, marketing and exporting their products
 - **no access to financing**

Fair Trade

- ... is a **market-based approach** to help producers in developing countries achieve **better trading conditions** and therefore improve their livelihoods.
- ... is a **trading partnership** that seeks greater equity in international trade based on dialogue, transparency and respect between producers and consumers.
- ... sets **standards** guaranteed by **labels** which inform consumers under what conditions a product is being produced and traded.

1. Fair Trade: Background & Basics

The Minimum price

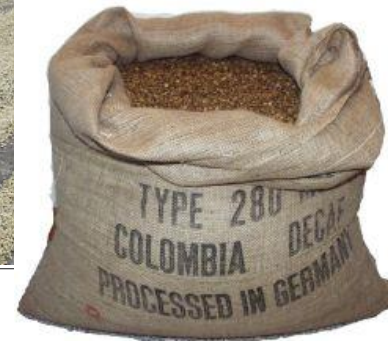


FT price = FT min price* of 125 cents/lb + 10 cents/lb FT premium** When NY price is 125 cents or above, the FT price = NY price + 10 cents

* Min price was increased from 121 cents on 1.6.08; ** Premium was increased from 5 cents on 1.6.07

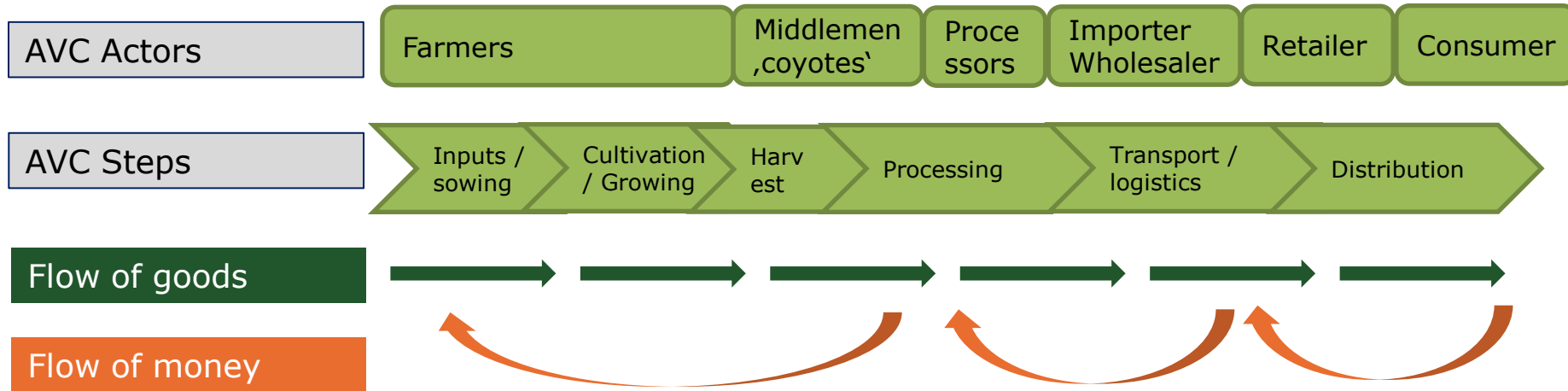
A. FAIR TRADE

2. Fair Trade Value Chain



2. Fair Trade Value Chain

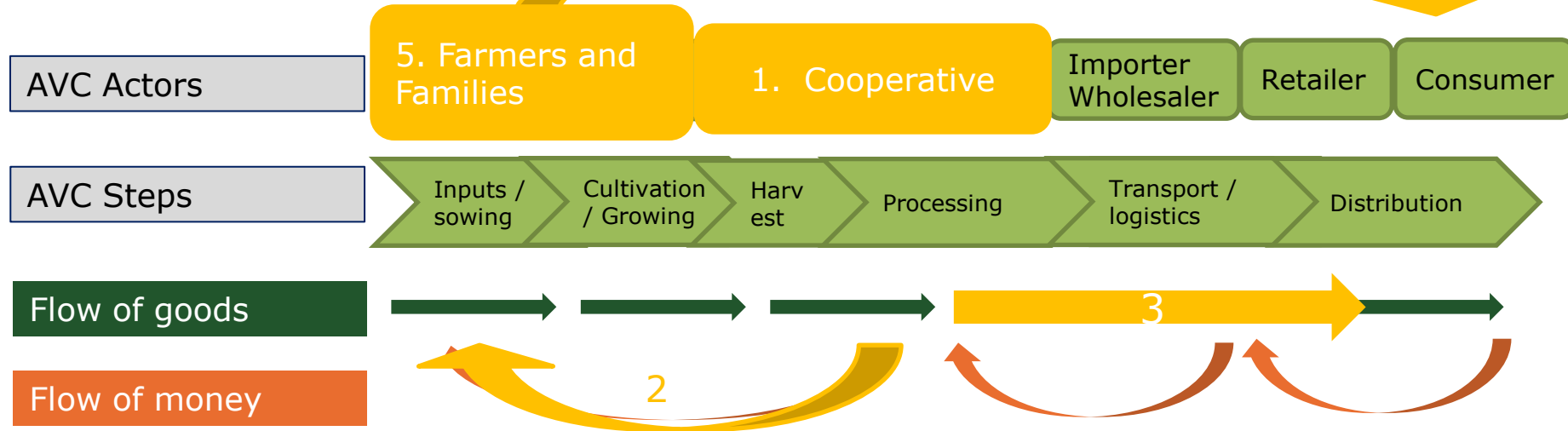
The Agricultural Value Chain (AVC)



- AVC = Chain of actors, goods and processes from the seed and farmer in the south to the end-product and the consumer in the north; and the financial back-flow
- Every step adds value to the final good (like in any value chain)
- In agriculture the value chain works in cycles (= seasons)

2. Fair Trade Value Chain

The FAIR TRADE Agricultural Value Chain (AVC)



1. no middlemen, democratic decision making, more professional, more scale, more value added, market access
2. more stable, higher prices for farmers
3. long-term, stable trading relationships
4. More transparency
5. Farmers and their families have more stable incomes and better working conditions. Their environment is better protected.

B. INVESTING IN FAIR TRADE

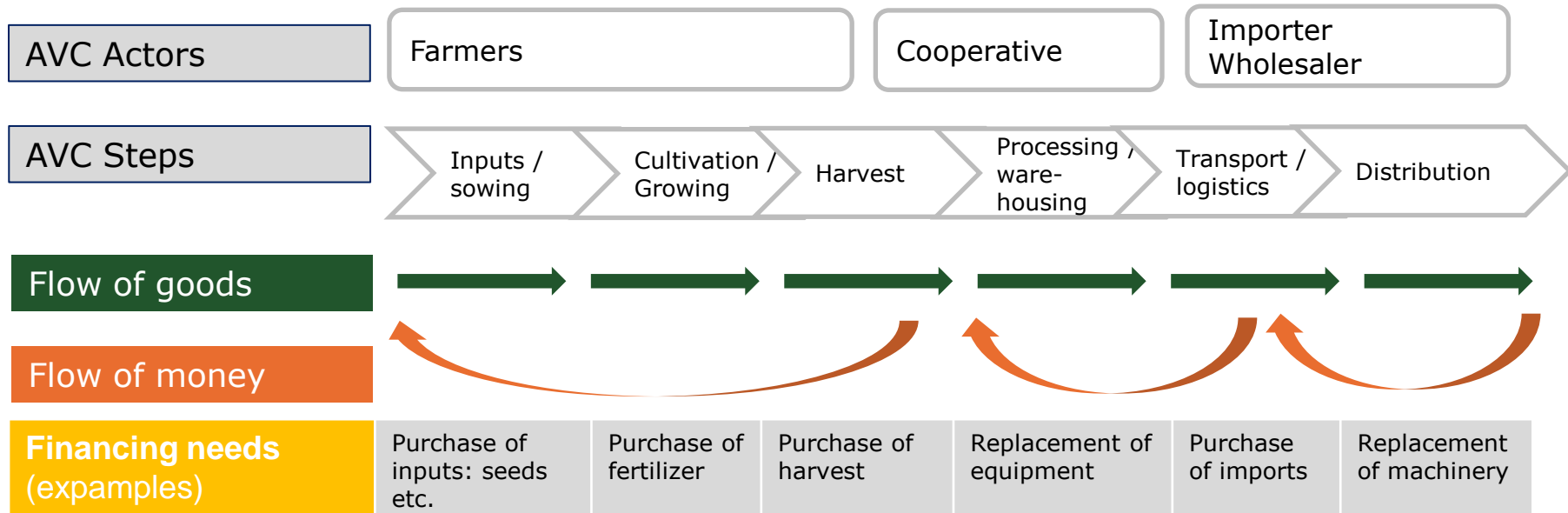
3. Financing Needs and the role of r_A
4. Type of Investments
5. Demand and Supply for Export Finance
6. Risks & Mitigating Factors
7. Hot Topics

B. INVESTING IN FAIR TRADE

3. Financing Needs and the role of r_A

3. Financing Needs and the Role of rA

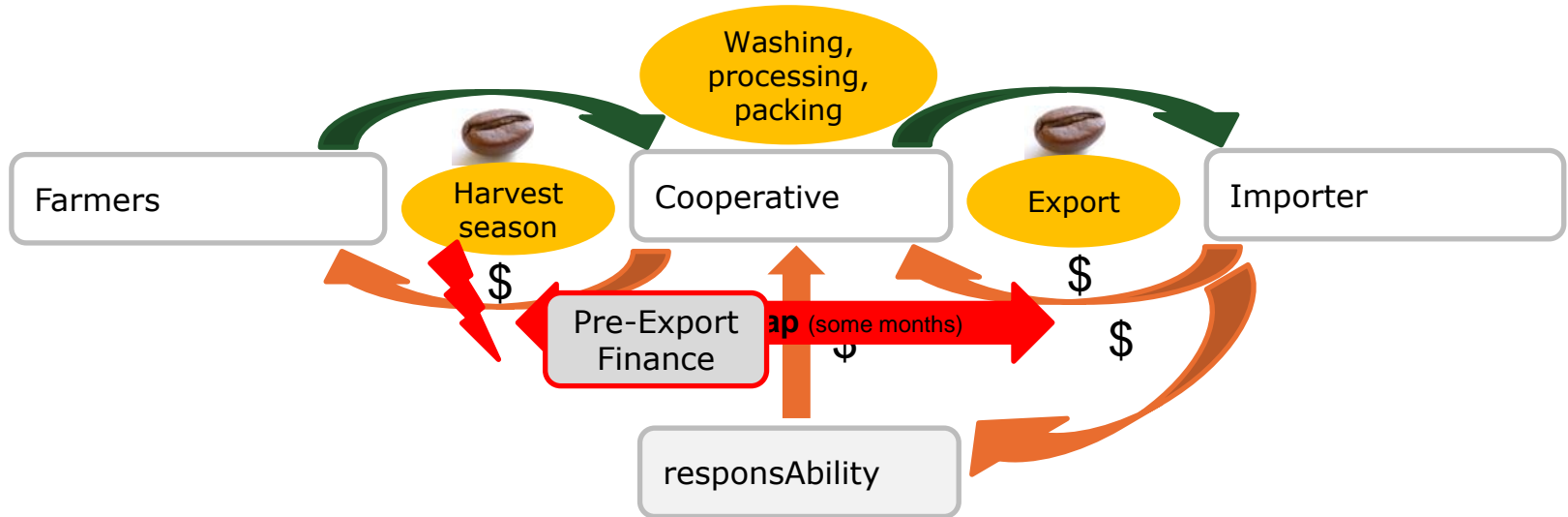
The Agricultural Value Chain and financing needs



- Lack of short term financing for working capital requirements → cooperative cannot buy the crop from the farmers. Farmers sell their production to other (non Fair Trade) intermediaries ('coyotes') which are able to provide up-front cash payment (especially during period of high prices).
- FT trading companies are encouraged to pre-finance up to 60% of the sales contracts. Nevertheless, most of them are not able to meet this requirement, e.g. due to very high commodity prices that would require a great increase of their credit facilities.

3. Financing Needs and the Role of rA

rA Pre-Export Finance



Pre-Export Finance allows cooperatives to pay farmers **up-front**

- ... allows cooperatives to buy, process and sell larger amounts resulting in more scale and better trading conditions
- ... ensures fair prices for farmers since they don't have to sell to the coyotes/middlemen
- ... allows farmers to invest in next crop season

B. INVESTING IN FAIR TRADE

4. Types of Investments

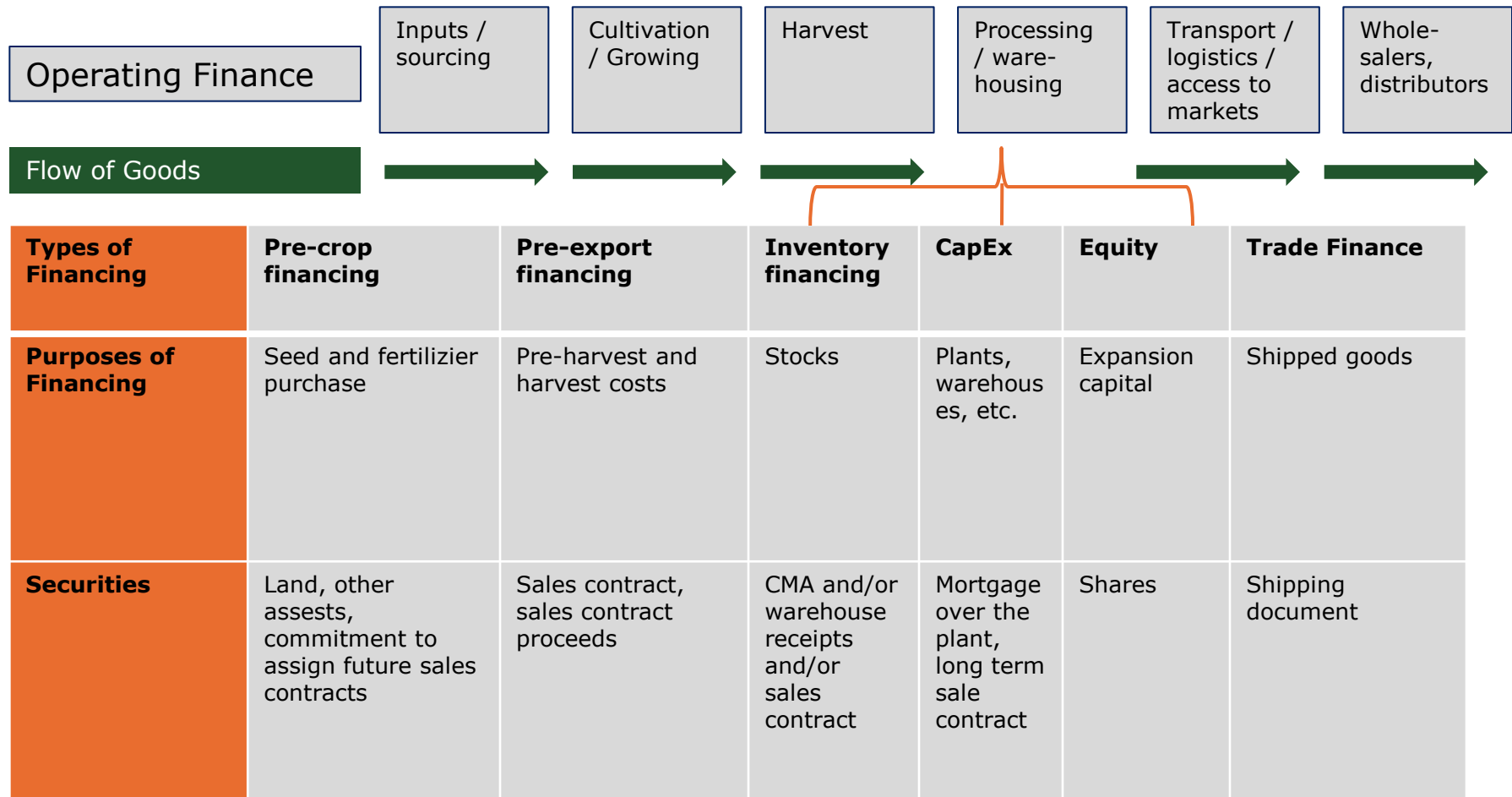
4. Types of Investments

Focus

- **Focus on cash crop commodities** with existing reference market, denominated in hard currency and backed by formalized sales contracts.
- In general, **short term financing** (i.e. working capital, crop finance, trade finance and in some cases inventory finance)
- But also **fixed assets financing** to improve quality, yields and in the end income for small holder farmers
- **Regional/local commodity** flows
- And look at **food security** flows

4. Types of Investments

How to invest into Fair Trade



B. INVESTING IN FAIR TRADE

5. The market for Export Finance: Supply and Demand

5. The Market for Pre-Export Finance

Demand & Potential

- Demand consists primarily of **short-term working capital financing**, i.e. pre-financing of commodity flows at the level of rural producer organizations.
- The majority of the demand is commodity-wise in **coffee** and geographically located in **Central and South America**.
- With more than USD 4 billion sales in 2010, the “Fairtrade” certification is the most widely recognized social and development label in the world.
- Fairtrade: Between USD 200 and 250 million is currently served by social and traditional Lenders, leaving **about 50% of the demand unmet**, i.e. there is a **potential of around USD 500m**.
- Sustainable agriculture (a wider concept than just “Fairtrade” such as Utz): Global demand is estimated at over **USD 800m**.

5. The Market for Pre-Export Finance

Supply of Financing

- **Local banks:** in most cases they are risk adverse to agri-businesses (even greater aversion when the borrower is a cooperative). Interest rates charged to the agri-sector are sometimes extremely high. Moreover, local banks don't really understand the trade finance business.
- **FT trading companies** are encouraged to pre-finance up to 60% of the sales contracts. Nevertheless, most of them are not able to meet this requirement due to very high commodity prices that would require a great increase of their credit facilities, not easily available.
- **International social lenders**, such as Root Capital, Rabo Rural Fund, Alterfin, Triodos, Oikocredit, Shared Interest. They are all rather small. rA with its current FT portfolio already being among the largest.
- For **MFIs** the amounts are too high

5. The Market for Pre-Export Finance

Why are there no other sources of financing?

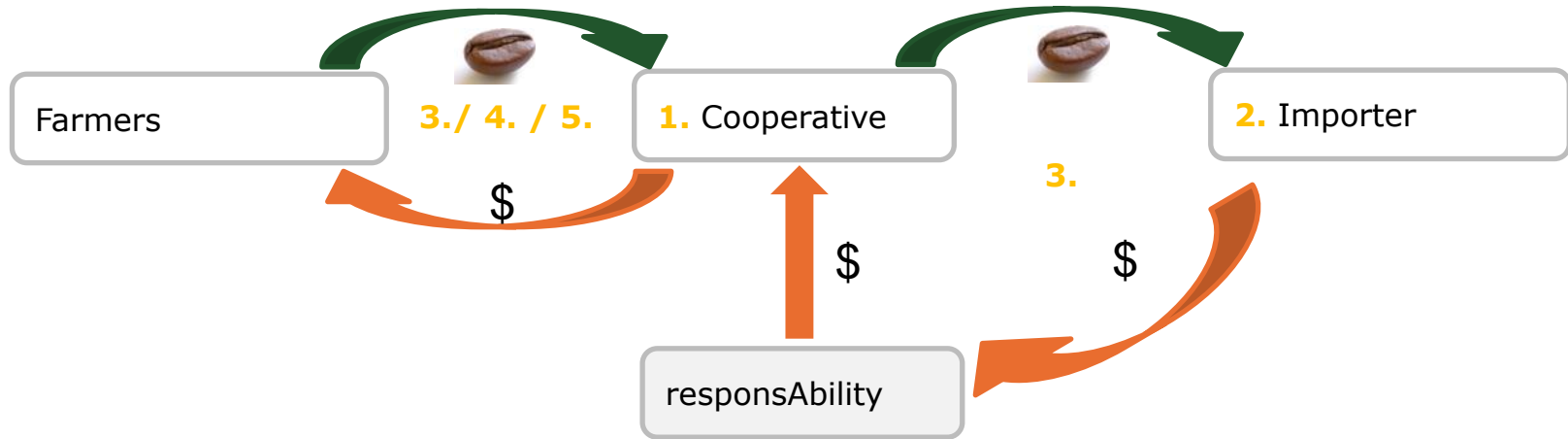
- The problem is that farmers, even when they form associations, are often **too small and risky** to be served by banks. Cooperatives however are too big for MFIs while serving individual farmers is very costly and risky.
- To succeed, they typically need access to loans between \$10,000 and \$1 million. This is a banking no-man's land — often called the “**missing middle**”
- Banks are uncomfortable lending to people who **lack hard collateral**. The rural poor often have no land, buildings or legal titles. And government rural credit schemes have been riddled with corruption and waste.

B. INVESTING IN FAIR TRADE

6. Risks and mitigating factors

6. Risks and Mitigation

Transaction Level



Level	Risk	Mitigation
1. Cooperative	Mismanagement, Unprofessional risk handling (price risk), fraud, insolvency	Comprehensive DD; long-term relationships; contract based lending (80%); repayment from importer (2.)
2. Importer	Counterparty risk	Assessment of importer
3. Commodity Risk	Price volatility (upward and downwards), production risk	Systematic and ongoing commodity risk assessment
4. Market Risk	Price differential, political interfer., environmental & infrastructure risk	Systematic and ongoing market risk assessment
5. Country Risk	Political and economic risk	Country risk assessment

B. INVESTING IN FAIR TRADE

7. Further case studies

Manduvirá Co-operative, Paraguay



Details

- supports its members in marketing their sugar cane and other crops and provide a range of services such as credit and savings facilities, welfare programs, technical support and agricultural training
- 1,450 Members
- Founded in 1975
- Generates approx 150 jobs in the area
- Volume of processed sugar 1,200 - 1,500 tonnes

Investment Facts

Purpose : Financing a sugar plant

Investment: USD 2 m debt

Interest: 9.00%

Duration: 5 years

Coopeterrazú, Costa Rica



Details

- One of the leading coffee cooperatives in Costa Rica
- Cooperation founded in 1960
- 2,600 members
- Social benefit: improvement of sustainable, stable household incomes, better nutrition, health, education

Investment Facts

Purpose:	Pre-export finance
Investment:	USD 2 m debt in 2010, 6 m in 2011
Interest:	8.50% fix
Duration:	8 Months