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Value Chain Finance the Hard Way: Lessons from Zambia

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TOPICS

- 1. The Situation in Zambia**
- 2. USAID/PROFIT's Response**
- 3. Lessons Learned (So Far...)**

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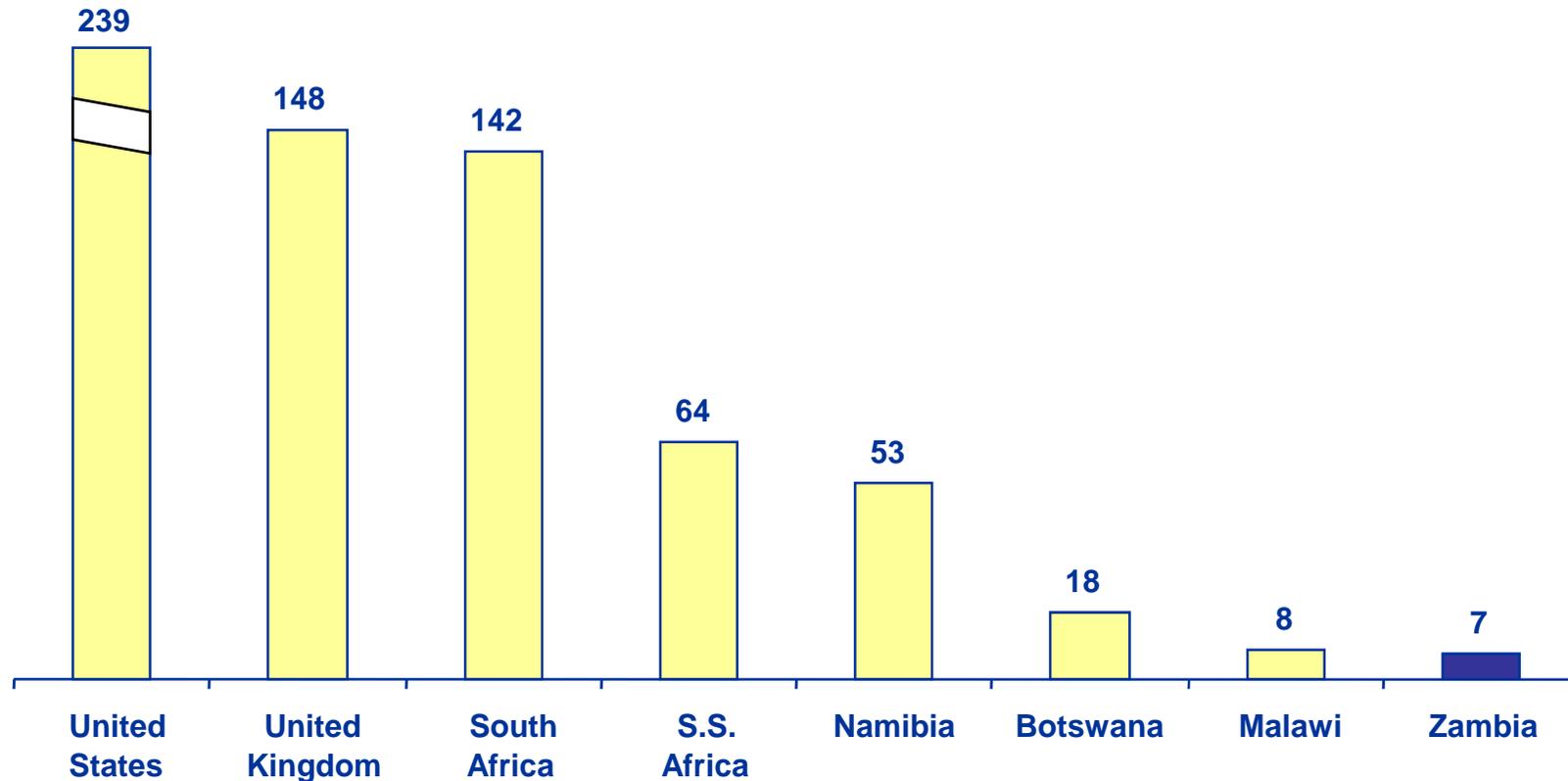
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ZAMBIA AT A GLANCE

- 12 million people, sparsely populated countryside
- Agriculture employs 85% of workforce, but accounts for only 17% of GDP – i.e. very low productivity
- Poverty declining, but 67% still below poverty line
- 3 out of 4 of Collier's 'Bottom Billion' poverty traps
 - Landlocked with bad neighbors
 - Poor governance in a small country
 - Natural resources (copper)
- Growth slowed from 6-7% to 2-3% this year

Zambia's Financial Sector: It's Very Small

Credit to the Private Sector as a Percent of GDP, 2003



Credit rose to nearly 10% of Zambia's GDP in 2008, but is still well below regional benchmarks.

FINSCOPE FINDINGS AND OTHER OBSERVATIONS

- ✓ 78% of population have never had a savings account.
- ✓ Less than 4% have ever had insurance.
- ✓ Less than 2% have ever had a formal loan – around 14% have had an informal loan, mostly for consumption.
- ✓ Medium or small business loans are rare, with collateral requirements upwards of 200% - agric not a priority area.
- ✓ Intra-firm value chain finance is limited and informal.
- ✓ Treasury bill rates fell in 2005/06 from above 30% to below 13%; deposit rates have remained the same.

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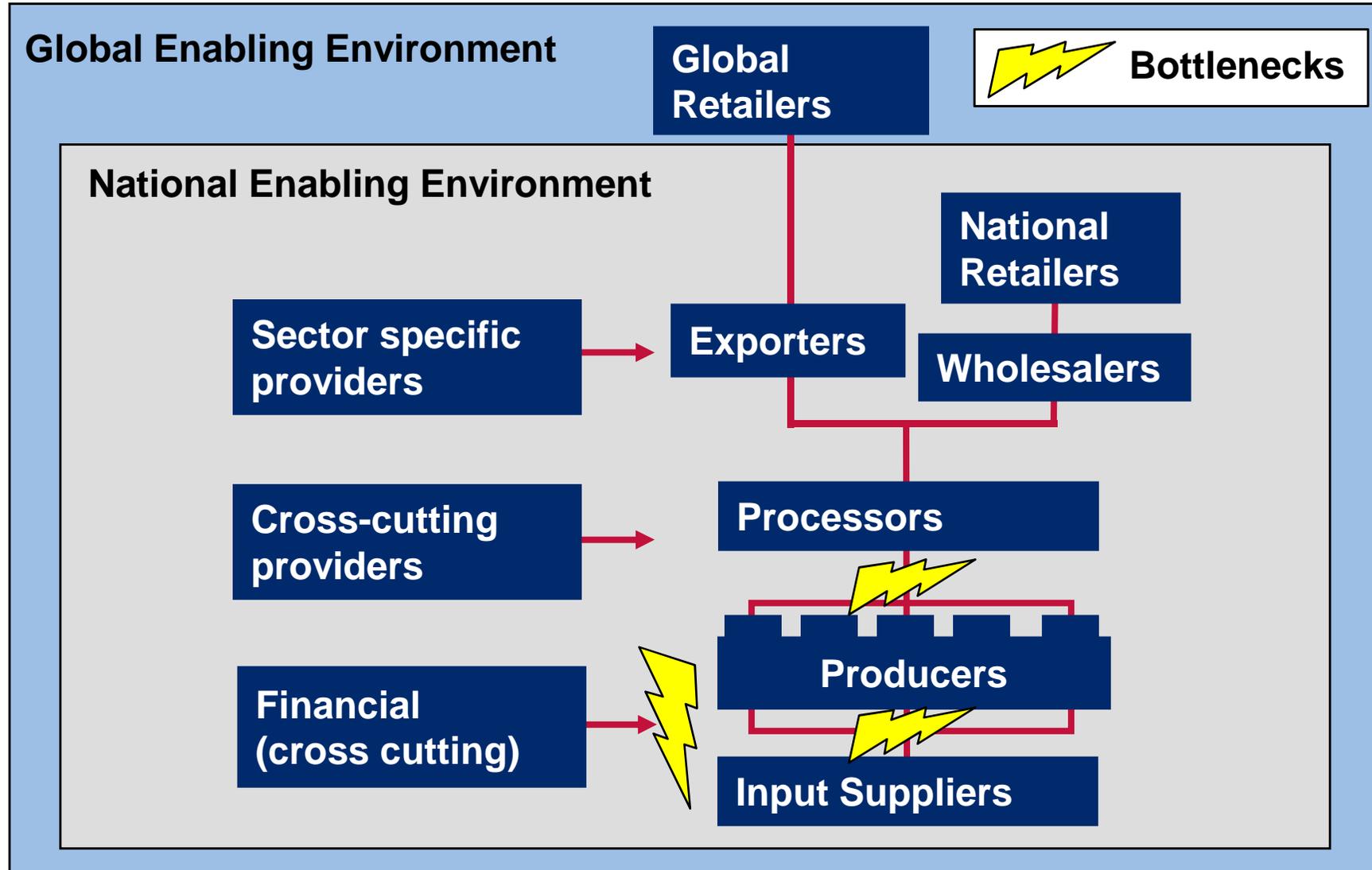
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USAID PROFIT PROJECT

- **PROFIT** = Production, Finance, and Technology
- 5-year, \$17.5 million (\$7 m grants) cooperative agreement implemented by **CLUSA** with assistance from **EMG**
- **Mission:** Improve smallholder and small business productivity (and income) in selected value chains
- **Approach:** Value chain analysis and market facilitation



VALUE CHAIN ASSESSMENT RESULTS



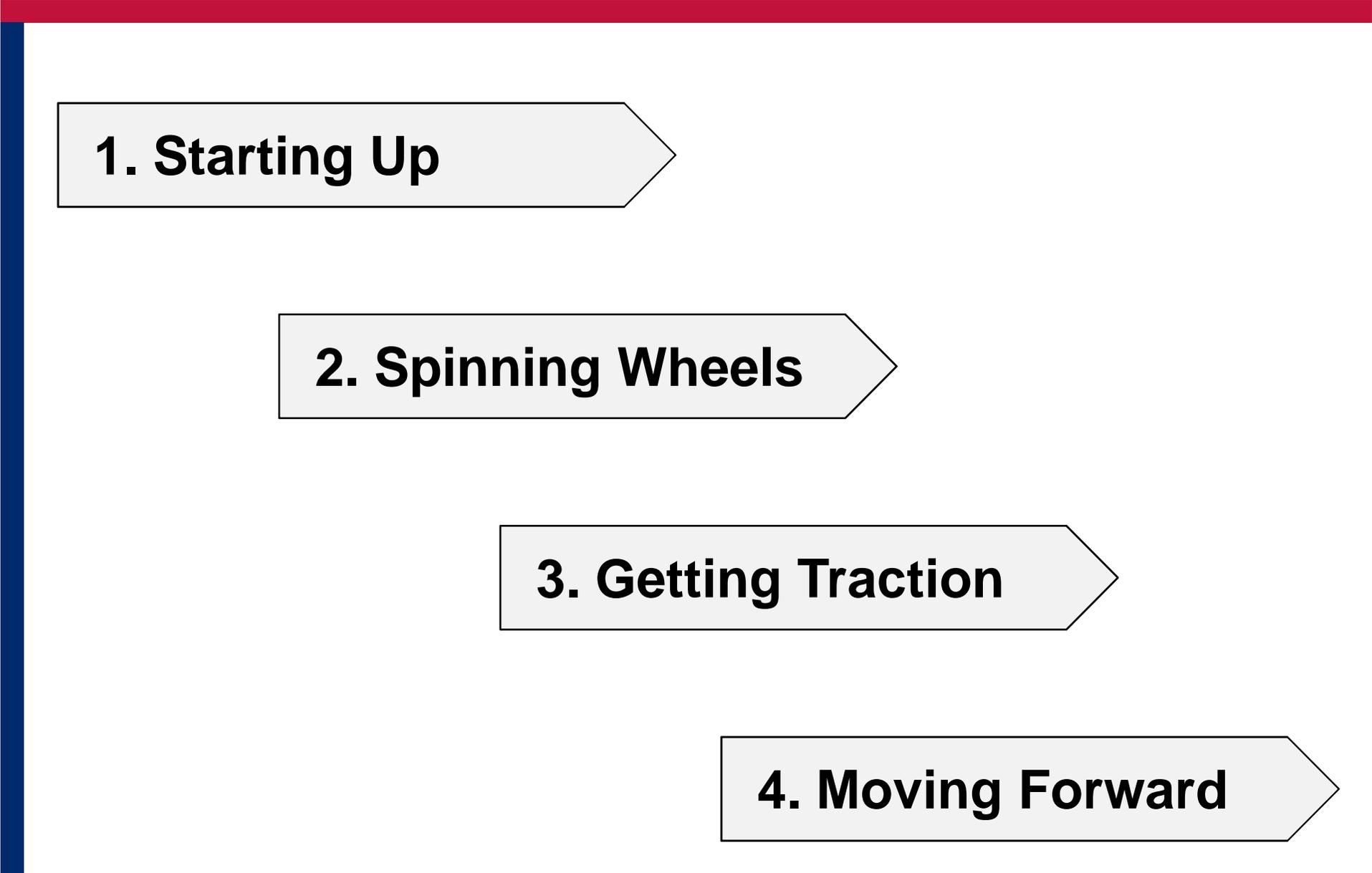
WHAT IS VALUE CHAIN FINANCE ANYWAY?

“Financing provided to or by a value chain actor in order to increase value-chain growth and competitiveness.” (USAID)

Purpose Focus	Value Chain Finance as Analytical Lens	Value Chain Finance as Intervention Approach
‘Direct’ Finance (Along the Chain)	<i>Include in overall approach to value chain assessment</i>	<i>Be very careful about power relationships, capacity, and risk</i>
‘Indirect’ Finance (Into the Chain)	<i>Build on systemic understanding of financial sector</i>	<i>Focus on individual creditworthiness – not chain competitiveness.</i>

**Increased access to finance is usually desirable;
but increased usage of finance is *not* always desirable.**

PROFIT'S APPROACH TO VALUE CHAIN FINANCE



1. Starting Up

2. Spinning Wheels

3. Getting Traction

4. Moving Forward

1. STARTING UP

1. Carried out training needs assessment in banking sector
2. Delivered credit skills training to 50 bankers
 - ‘Senior summit’ on SME and agricultural lending
 - Basic credit analysis and credit administration
 - Agricultural lending techniques and products
 - Workshop on Barriers to Agric Lending
3. Issued RFP for T.A. and grants under ‘Financial Services Development Fund’



2. SPINNING OUR WHEELS

- Offered grants and training to Zambian Institute of Banking and Financial Services to build capacity
- Reviewed Zanaco's agricultural loan portfolio and recommended restructuring approach
- Evaluated First Alliance Bank's credit policy and recommended new text in line with best practices
- Helped Sapitwa Leasing Company find clients for tractor leases, then complete and analyze applications



3. GETTING TRACTION

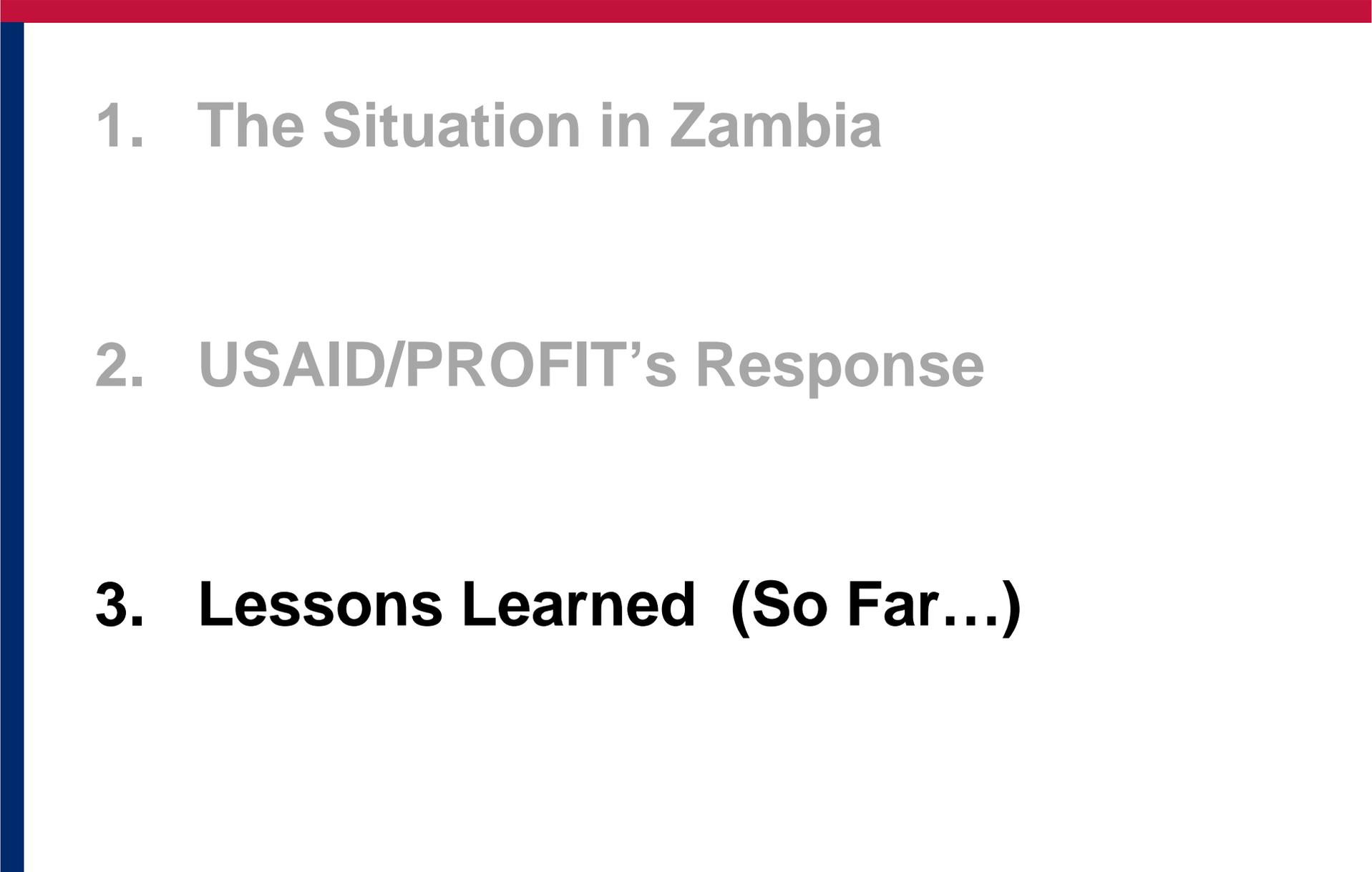
- ✓ Trained Zanaco and ABC Bank on agricultural lending
- ✓ Developed small business borrower training material for African Banking Corporation (ABC Bank) SME Division
- ✓ Assessed legal / regulatory framework for leasing and, recently, drafted new leasing law for central bank
- ✓ Brokered vendor agreements between leading equipment leasing company and agric equipment distributor
- ✓ Facilitated pilot of cell phone-based rural payments system with Zambian IT company and large cotton buyer – now BOZ approved national e-transactions platform

4. MOVING FORWARD

- Continue to support Zanaco and ABC Bank – TBD
- Continue to facilitate leasing vendor agreements
- Consider using DCA to expand equipment leasing
- Leverage development of ZAMACE (agric commodities exchange) to promote warehouse receipt lending
- Work with proactive NBFIs to development alternative mechanisms (corporate bonds, carbon credits, insurance)
- Conduct financial literacy and management training

PROFIT now has as much FS work as it can handle.

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LESSON 1: ADDRESS CAUSES, NOT EFFECTS

- **Ask why five times**: Identify specific constraints to v.c. productivity, then work backwards to the root causes
- **Example**: Tractor leasing
 - Farmers not plowing in time to maximize yields. *Why?*
 - Limited availability of serviceable tractors. *Why?*
 - No financing available to purchase new tractors. *Why?*
 - High transaction costs for leasing companies. *Why?*
 - **AND** unfavorable tax and legal treatment of leases. *Why?*



LESSON 2: USE SYSTEMS THINKING

- **Understand how finance works**: Recognize that increased usage of credit is not an end in itself; and that access depends on many factors outside the value chain.
- **Examples**: Agriflora and the IFC/ZNFU program
 - Banks lent heavily to large horticulture company in 2002/3; it failed spectacularly and agric lending dried up.
 - IFC program works with Farmers' Union to identify mid-sized farmers and help them get loans – can't find enough farmers who qualify *and* who need or want a loan.

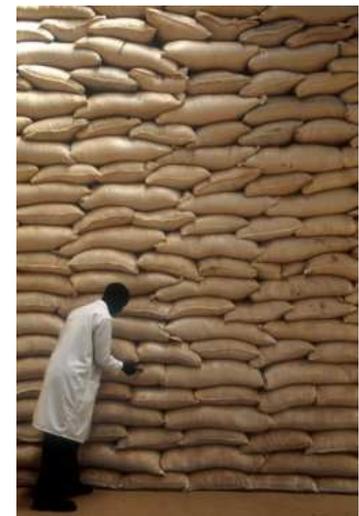
LESSON 3: LET THE MARKET LEAD... REALLY

- **Don't push too hard**: Instead, 'go fishing' and see what bites. Let counterparts lead.... But be patient!
- **Example**: FSDF Request for Proposals
 - Issued 5-page RFP to 40+ banks, leasing companies, MFIs, insurance providers and lead firms in May, 2007
 - Response was less enthusiastic than expected, initially
 - But interest grew as market conditions changed and word spread about PROFIT's work



LESSON 4: ADMIT & EXPLORE 'NON-SUCCESSSES'

- **Know the difference between a miss and a mistake:**
Accept misses as worthwhile efforts, and learn from both.
- **Examples:** First Alliance Bank, Zanaco and Sapitwa
 - First Alliance Bank requested assistance to upgrade credit policy, PROFIT responded, but bank never followed up.
 - Zanaco requested assistance with its agric portfolio – PROFIT STTA delivered report but didn't build rapport. No follow-up.
 - PROFIT compiled lease applications for Sapitwa leasing company, then Sapitwa went bust.



LESSON 5: BUILD COMPETITIVE PRESSURE

- **Capitalize – carefully – on successes**: Find opportunities to expand or replicate successful interventions *in order to build competitive pressure*.
- **Example**: Zanaco v. ABC Bank
 - Zanaco ('leader' in agric lending) requested training.
 - PROFIT told others that competitors were being trained.
 - ABC bank then requested training and assistance.

'Value chain finance' – however it's defined – requires hard work, patience, and an opportunistic approach.



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THANK YOU!

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