# Speaker's Corner Summary Report on Value Chain Finance

*The three-day online discussion forum brought together over 100 participants from nearly 30 countries to discuss their experiences and ideas related to value chain finance, including implementation challenges and innovative applications in the field.*

**Speaker's Corners are online discussions hosted by subject matter experts, designed to help practitioners share and learn from each other. They are hosted on microLINKS (*www.microLINKS.org*) and Poverty Frontiers (*www.povertyfrontiers.org*)**

A Speaker's Corner was held from March 24-26, 2009 entitled, "Increasing Incentives and Reducing Risks: How Value Chain Finance Can Increase Industry Competitiveness." More than 100 practitioners, donors and academics participated in the three-day event punctuated with a lively debate on topics ranging from sustainability to next steps for the field.

This report summarizes key themes and ideas raised over the three days and provides a platform for next steps. The Speaker's Corner was led by ACDI/VOCA with hosts from Crimson Capital, the World Council of Credit Unions (WOCCU) and AZMJ. This Speaker's Corner is part of a series of activities on value chain finance that is being supported through USAID's AMAP BDS[1] Knowledge and Practice II Task Order.

***Welcome message:***

*The next three days of discussion will have the following objectives:*

- *Gain greater consensus on value chain finance's definition, current best practice programs and on-going challenges*
- *Discern a set of recommendations for practical value chain finance tools that can lead to improved best practice implementation*

## Introduction

Value chain finance refers to financial products and services that flow to or through any point in a value chain in order to increase returns on investment and growth and competitiveness of that value chain. Whereas value chain finance transactions are not new (production finance could be considered value chain finance), the emphasis on improving finance at one point in the value chain to increase the competitiveness of the entire value chain is. With value chain finance, the risks and returns of the finance provider are considered along with the risks and returns to value chain actors.

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Access to finance remains one of the critical obstacles to the growth of micro and small enterprises. Understanding and drawing on the lessons from value chain finance is therefore imperative to advancing its use. This Speaker's Corner discussed current understanding of value chain finance, implementation challenges and innovative applications in the field. Two guest facilitators included winners from the recent AMAP-funded contest on "Innovations in Financing Value Chains."

**Day One:** Hosted by Janice K. Stallard, Senior Technical Director at ACDI/VOCA. Ms. Stallard led a discussion among the participants focusing on: (1) the definition and use of value chain finance; (2) the current state of the practice; and (3) field-based challenges to best practice implementation.

**Day Two:** Hosted by guest speakers from the AMAP BDS K&P II "Innovations in Financing Value Chains" competition, Luis Jimenez Galarza and Stephanie Grell Azar (representing WOCCU) and Megan Falvey (representing Crimson Capital). These facilitators discussed their work in Peru and Bolivia, respectively, and solicited suggestions from the audience regarding examples of how their projects have increased incentives and reduced risks for better value chain finance interventions.

**Day Three:** Anita Campion of AZMJ hosted and led a discussion on successful methodologies and possible tools needed to advance value chain finance best practices.

## Defining Value Chain Finance

The morning of the first day was devoted to a discussion of the definition of value chain finance. The briefing paper titled "Finance in the Value Chain Framework,"[2] produced under AMAP, defines value chain finance as the following:

*"Financing provided to or by a value chain actor in order to increase an industry's growth and competitiveness"*

This definition may be too narrow and need to be more inclusive noted **Geoffrey Chalmers**, from USAID/Mexico:

*"We should be looking at ways of improving the lot of the excluded and poor communities as a key part of making value chains more competitive. Broadening the definition to explicitly include the small producer also opens the door for including access to broader range of financial services in rural areas that are not exclusively linked to a specific chain. This cannot be left out of the equation. We need to think about it in a holistic way or else inevitably we get what we've gotten so many times: finance is facilitated for a specific chain, but no strong, long-lasting financial intermediaries are left behind because the focus was so narrow on the competitiveness of that particular chain."*

Many other comments followed that added more depth and texture to the current definition. Participants such as **Calvin Miller** of FAO took the time to provide examples from their project work and recent academic publications:

*"The definition I use in an upcoming book on agricultural value chain finance, based upon the collective input of many persons from around the world is: Finance that takes place within the value chain, such as when an input supplier provides credit to a farmer, or when a lead firm advances funds to a market intermediary and finance that is made possible by value chain relationships and mechanisms, such as when a bank issues a loan to farmers based upon a contract with a trusted buyer or a warehouse receipt from recognized storage facility. While financing is often needed to improve competitiveness and growth, it is not necessarily a direct correlation since there are so many other factors involved."*

**Linda Jones**, who has also been working on the FAO value chain financing book, noted that value chain finance includes financial services provided to chain operators either by their partners in the chain or external actors that contribute to chain competitiveness. In working towards a common definition, we should note that these services should allow chain operators to:

[1] Accelerated Microenterprise Advancement Project, Business Development Services

[2] Available at http://www.microlinks.org/ev_en.php?ID=34299_201&ID2=DO_TOPIC

- assure timely financial and product flows;
- manage risk related to chain activities;
- invest to upgrade capacities; and
- strengthen relationships with others in the chain.

**Nicole Pasricha** of the Mennonite Economic Development Associates noted that value chain finance has other goals besides the growth and competitiveness of the value chain. While the aim is that individual business upgrading leads to value chain upgrading, when the financing arrangements are small in scale, they might not impact the entire value chain. While undertaking a value chain analysis and developing interventions, the focus should be kept on not only developing the value chain as a whole, but making sure that the poor and marginalized are proactively included. Nicole proposed the following definition for value chain finance:

> *"Financing arrangements that involve at least one value chain actor with the objective of increasing growth and/or competitiveness of the value chain or its individual businesses."*

## Designing Sustainable Interventions

The Speaker's Corner spent quite a bit of time on the issue of designing sustainable interventions. That is, interventions that seek to create incentives for the private sector to act in new ways and reach new target groups.

It was noted that there are many sides to the sustainability question with respect to value chain finance. When working with a financial institution, the intervention is fairly clear: help the institution develop a profitable product that meets the needs of the targeted value chain. Sustainability is defined as continuation and/or expansion of the product line.

However, many value chain finance interventions are designed to create incentives or reduce risks for non-traditional financial intermediaries. Some of these interventions are single events and do not need to be 'sustainable' in the traditional sense of the word. In these cases, success can be defined in terms of increased growth and competitiveness of the industry. As donors and practitioners design new interventions, it is important to think through the differences of these approaches and define from the outset what sustainability or success will mean.

**Geoffrey Chalmers** from USAID/Mexico noted that sustainable interventions must be "win-win" activities that demonstrate business sense to private sector actors, showing reasonable risk with the potential for profitable returns. The best way to reduce the risk for financial intermediaries is by improving the flow of *knowledge* and information: helping financial intermediaries and value chain actors gain a new level of understanding regarding how the value chain works and how its actors work together to create a more competitive operating environment. For example, this can be done by facilitating direct relationships with buyers, processors and other value chain actors. But this takes time and patience and only works with those intermediaries with the interest in pursuing these opportunities. In summary, we need to work to address risks and create incentives to effect sustainable solutions.

### ICT-Enabled Due Diligence

Geoffrey Chalmers gave an interesting example from USAID/Mexico of their use of information and communications technology (ICT) in expanding access to knowledge. In this case, USAID has used an ICT platform to put information that buyers have about their suppliers into a format that is useful for a lender. As such, lenders can easily access this information to assure them that a buyer has a "good" history of delivering on time, with the required quality of products, with prompt repayments to buyers. The key has been making more information available to a wider set of people.

**Anita Campion** agreed with Geoffrey's statement that knowledge is a big part of the equation to encourage lending within the value chain. In conducting a training in Mali, she found that providing details on market segmentation, consumer demand for processed artichokes, and ongoing value chain finance interventions to financial institutions made a huge difference in how they viewed the risk profile of potential borrowers. The difficulty is that it is not easy for one producer to demonstrate the potential of a value chain on their own. In the case of artichokes in Peru, financial institutions were willing to lend to producers not just because they had contracts with an artichoke processor, but because they clearly understood the market demand with respect to the variety and quantity of processed artichokes being produced.

ICT can also play a critical role in facilitating the sharing of information in a cost effective and secure manner. Comments were made that more must be done to draw on the opportunities offered through ICT interventions that can lower costs and risks, while increasing incentives (through better and more accurate information) for private-sector participation in a value chain.

**Building Trust**

Participants noted the importance of bringing stakeholders together to come up with solutions that are mutually beneficial. Face-to-face meetings increase the likelihood that financing arrangements will continue. This is particularly important in populations that do not know, trust or understand each other.

Participants also brought up the importance of donors supporting pilot projects as a demonstration effect for the private sector. The private sector must clearly see the profitability of launching a new product and that the market has unmet demand. This is an important role for donors to play to create sustainable interventions, i.e., viable business models.

In summary, participants agreed that when designing interventions, donors should focus on how their support must *facilitate change*—and not become a player in the value chain. This is one of the keys to successful and sustainable interventions.

## Tool Development

The final day focused on a dialogue around tools that are needed to advance value chain finance interventions. An opening set of questions included the following:

- What is the appropriate amount and kind of subsidy to avoid market distortions?
- How can we use the value chain framework to facilitate access to longer-term finance, instead of just short-term working capital?
- What are appropriate government interventions that would actually stimulate value chain finance?
- What are common issues related to value chain finance regardless of the sector, whether agriculture-related or not?

While subsidy is often used to reach poorer beneficiaries, many argued that this was not necessary and more work needs to be done to identify facilitation interventions that lower risk and increase incentives for private-sector participation. Donors must strive to do this with the limited use of subsidies.

Participants acknowledged the difficulties most value chain finance interventions have had in delivering longer-term finance that would allow farmers to purchase fixed assets and make strategic investments in their businesses. It was noted that some commercial banks have piloted these products, but that they are not widely available. Leasing was noted as an interesting example, but one that comes with many complex legal framework issues that must be addressed before leasing programs can be launched.

Regarding government subsidies, none of the participants were able to note positive interventions and many referenced government programming that had a negative impact on intended beneficiaries. These included various government-funded guarantee schemes that have lead to skewed access and created limited incentives for the private sector to play a role in that market.

A list of tools to facilitate value chain finance activities was suggested:

- More detailed documentation on the 'how to' of value chain finance (with tables that walk practitioners through processes, provide sample tools and resources – such as MOUs and warehouse receipts)

- Training modules on the subject of value chain financing

- Standardized approaches to evaluating the finance potential in a value chain (i.e., not all value chains are appropriate for finance, for example, perishables); how to assess that a value chain is dynamic and offers significant growth potential

- Templates for contracts (between value chain actors and financial institutions)
- Methodologies for pricing financial products for different value chains in various country contexts
- Tools for monitoring and assessing impact associated with value chain finance
- Guidelines for when and how to expand the provision of value chain finance from among value chain actors to the formal financial sector
- Guidelines on how to determine the appropriate use of subsidies and the provision of technical assistance that does not distort markets

There is still much to be done to advance practice in value chain finance. USAID has recently supported several initiatives to address identified gaps. USAID expects to publish several new tools on microLINKS in June/July 2009:

- Two value chain finance case studies using value chain methodologies (WOCCU's Value Chain Finance Methodology from Peru and a Purchase Order Finance case study from Crimson Capital and Chemonics in Bolivia).
- A Technical Brief is being prepared by Chemonics under the Financial Sector Share contract (2008-2011) that will summarize much of the value chain finance work to date, discuss how it can be incorporated into program design activities, provide tools for evaluating potential value chain finance interventions (including a diagnostic checklist, value chain analysis tools) and offer several case studies.

*This synthesis report was prepared by Janice K. Stallard, Senior Technical Director at ACDI/VOCA. The original postings from this discussion and other related resources can be accessed at www.microlinks.org/sc/valuechainfinance.*

## Resources

- The USAID Value Chain Development Wiki's section on value chain finance: www.microlinks.org/vcwiki
- The FAO has a Contract Farming Resource Centre website that houses sample farming contracts, briefs on different contract issues and a selection of presentation resources at: www.fao.org/ag/ags/contract-farming
- The Rural Finance and Business Organization Program on Competitiveness and Value Chains in Costa Rica (www.catie.ac.cr/cecoeco) is finalizing a 'guide for facilitating value chain finance' (in Spanish) that will be available on their website as of May 2009
- AN ADB/DFID value chain toolkit is available at: www.valuechains4poor.org
- A Nairobia writeshop summary on value chain financing is available at www.drop.io/chainfinance
- AZMJ is conducting research in Honduras and Nicaragua for the IADB, results will be available by the end of 2009 at: www.azmj.org
- MEDA market research tools on value chain initiatives at www.meda.org
- The SEEP Network currently has a learning topic on "scale and sustainability" regarding value chains; go to www.seepnetwork.org to learn more.