INCREASING INCENTIVES AND REDUCING RISKS: HOW VALUE CHAIN FINANCE CAN INCREASE INDUSTRY COMPETITIVENESS?

AN ONLINE SPEAKER'S CORNER FACILITATED BY JANICE STALLARD AND HOSTED ON WWW.MICROLINKS.ORG.

March 24-26, 2009

This publication was produced for review by the United States Agency for International Development.
It was prepared by The QED Group, LLC and International Resources Group.

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DAY 1: INTRODUCTION

Post by: Janice Stallard

Subject: Welcoming Remarks

Hello to my fellow practitioners! It's great to have the opportunity to get together for three days and talk about value chain financing.

I have been working on a range of value chain activities under AMAP, including a briefing paper, wiki, and a contest to identify best practices from the field. The next three days of discussions will build on all of these activities, with the objective to:

• 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

As your host over the next three days, I will endeavor to facilitate discussion and raise key issues. However, this is an open forum and we encourage you to throw out issues important to your work, to offer advice, or to provide useful examples.

Thank you for your time and participation and I look forward to our discussion.

DEFINING VALUE CHAIN FINANCE

Post by: Janice Stallard

This morning, I would like to get our discussion going with a quick conversation on the definition and use of value chain finance. The AMAP value chain finance briefing paper defines value chain finance as: Financing provided to or by a value chain actor in order to increase an industry's growth and competitiveness

As practitioners, do you feel this is your working definition? Does it fit the real practice in the field?

Post by: Rodolfo Quiros

The definition is useful because it includes both financing within the chain and from outside the chain (see Campion). The end ("to increase and industry's growth and competitiveness"), however, may seem too strong, in the sense that financing by itself cannot do all that, because there are key variables to be considered as for example in-depth information about the chain, risk management systems, minimal transaction costs, effective chain governance, ability to develop partnerships and well designed financial products (Gonzalez-Vega, summarized by Weener).

Post by: Calvin Miller

I want to agree with Rodolfo that value chain finance is both finance within the value chain and that which is in to the chain because of the value chain linkages. For agriculture, 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 a 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.

Post by: Stacey Young

Good point that VC finance is not the only obstacle to increased growth and competitiveness. And, just as competitiveness hinges on more than finance, VC finance interventions sometimes need to address not just availability and access to finance, but also appropriate policy and regulatory frameworks as well. Perhaps the definition could acknowledge these realities if it were revised to say: "Measures to remove key constraints to an industry's growth and competitiveness that relate to financing or to financial policy and regulatory frameworks." Does this clarify, or obfuscate?

Post by: Ms. Anita Campion

I completely agree with Stacey that value chain finance interventions often need to address policy and regulatory issues as well and I agree with Rudolfo that finance alone does not always result in value chain growth and competitiveness. Perhaps a slightly revised definition of "value chain finance" could be "Funds or in-kind resources provided to a value chain actor (from within or outside the value chain) with the objective of facilitating the industry's growth or competitiveness."

Post by: Geoffrey Chalmers

I think we also need to remember the multiple dimensions of what VC finance is all about. Yes, the competitiveness of the VC is both a necessary element (ie there must be potential in the VC to make it worth it to focus on) and a goal of an intervention. But the small producers, the "excluded", are also a necessary element (ie if there are no poor or excluded involved in the chain, it probably won't warrant donor/government intervention) and a goal of any intervention. To me, both are crucial elements and should be included in any definition. Sure, we don't want to lose our focus, but I think there's room in there to remind ourselves that particularly when we discuss access to finance, we should be looking at ways of improving the lot of the excluded and of poor communities, as a key part of making VCs 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: that 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.

Post by: Nicole Pasricha

Dear all:

I am very interested to read the posts so far and looking forward to the discussion topics. Regarding the proposed definition of VCF, I feel that maybe it is a bit too narrow, for two reasons:

1) "Financing": this term might be interpreted as only credit services, while actually VCF incorporates a lot of different financial arrangements and products that facilitate the businesses of the actors in the chain. Maybe we should consider broadening the term to say "Financial relationships", "financial arrangements" or "Financing models and products" or similar to get this point across better.

2) Industry growth and competitiveness: first, should we refer to the growth and competitiveness of the >, not the >? Industry is a big term! value chain is more manageable. Second, perhaps the VCF has other goals besides growth and competitiveness of the VC, potentially of the individual actors as well. So it could be broadened to say: of the value chain and/or value chain businesses. Of course the aim is that individual business upgrading leads to VC upgrading, but if the financing arrangements are small in scale it might not impact the entire VC in the short term.

So, maybe the final definition would be something like:

"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."

I'm very interested to hear others thoughts on these points!

Post by: Narayanan Raghunathan

Dear all,

This is a good starting point for the definition of the Value Chain Financing. As development support group, we work with this focused definition of - "Inclusive Value Chain Financing/ VC Development". The focus is on "developing products, processes, services and interventions in the value chain to improve its growth and competitiveness, while enabling the poor and marginalized communities to be significant contributors and beneficiaries of the Value Chain."

So, while undertaking the VC analysis, developing interventions, the focus is kept clearly on not only developing the VC as a whole, but making sure that the poor and marginalized are proactively included in these. Care is also taken while introducing technology, financial and other products not to exclude the marginalised communities.

Post by: Tracy Gerstle

Hi,

First off, thanks Janice and to Microlinks for hosting a very timely discussion. I appreciate Raghu's and Geoff's point much-to not be too narrow in our definition and to keep the ultimate goal in sight in terms of ensuring the poor can contribute to and benefit from participation in the value chain.

As Geoff notes, financing around specific value chains are critical to the poor's participation, but so of course are their ability to leverage financial services and products to meet other needs that limit their participation, including savings and the ability to accumulate assets, as well as access to health and life insurance. A good analysis of financing within a VC, should be scoped to identify the other root causes that keep people poor and to determine what contributions financing can made to address these causes. It will also help significantly in the uptake of new behaviors and attitudes among the poor, promoting their engagement in higher value, higher risk activities, by providing them with different means of risk management.

Building on Raghu's definition, how about: "developing products, processes, services and interventions in the value chain to improve its growth and competitiveness, while enabling the poor to manage the risks and leverage the opportunities offered by higher value contributions to value chains.

Post by: Linda Jones

Thanks for this discussion of value chain finance. I have been working with Calvin on the VCF book for the FAO so this discussion is very timely. I like the refinement the definition is taking, but I wonder about the implication of intent. Yes, value chain development is an approach, and value chain finance may leverage that approach. But, if a value chain business receives finance that results in the development of the chain, but is not the explicit intent or objective of the lender, does that mean it is not value chain finance? I would change the "in order to increase" in the following to "that increases".

"Financing provided to or by a value chain actor in order to increase an industry's growth and competitiveness." For example, an input supplier may provide finance to a producer in order to increase their sales. If they don't care about the VC as a whole, does that mean it's not VCF.

I would say that it is value chain finance and we can't assess intent.

Post by: Ruth Junkin

Dear all,

My definition would be:

"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. These services allow chain operators to:

- assure timely financial and product flows

- manage risk related to chain activities
- invest to ugrade capacities
- strengthen relationships with others in the chain.

Post by: Calvin Miller

In the discussions of definitions of value chain financing, several persons indicated the need for it to be inclusive and/or to help the poor. While I am very conscious of that, I think we need care to note that value chain finance, like any finance, is in and of itself not necessarily inclusive, not necessarily to reach the poor, etc. Value chains, especially some of the most integrated ones, are often among the rich and well connected. Even so, there is interest on the part of the many of us who work in development to use value chains and value chain financing as an approach to deepen financial services and impact for the poor and it can be effective in promoting this.

Post by: Tony Pryor

As we segue to the next question on reducing risk, let me add just a small point or (4) related to definitions. I understand the tension between defining VC finance too narrowly, or too broadly. But I think some of the discussion is less about the terms used and more about a couple of things which make this subject so tricky:

1. Finance as a necessary but not sufficient condition. To be effective, those interested in the financing element of VCs need to understand the full range of other variables that impinge on/interact with/support the VC, particularly any of those which, while seemingly small are in fact critical to success, or failure. "We got the flowers all the way to the specially-financed cold storage at the airport, but we forgot that British Air just changed its policy on freight..." , "we got the farmers the fertilizer they need, and provided financing for the processors, but no one told us that the Ministry of Agriculture was about to ban the import of the hybrid maize seed from our neighboring country...". The solution is not to expand the definition until the "financing of VCs" covers ALL elements, but rather to realize that one needs to look at the factors systemically, not just identify one and focus on it.

2. Scale matters, good and bad. Sometimes providing financing may lead to the impact one is expecting, but it also could lead to some fundamental alteration of one of the relationships within the VC. "The farmers were indeed able to double their mango production and sales with the extra investment but when the entire valley started to grow mangos the market collapsed".

3. Not always will financing be used for the "rational" purposes you had expected it to go for. A family isn't a "value chain agent", but rather a multi-tasking, risk-spreading entity that will optimize all sorts of things, and sometimes not fully the way we'd calculate - "optimize" learning opportunities, or social standing, or ! quality of children's health, etc.

4. And finally, on a related point, there are few "value chains" that exist, in all their segments, just for the purpose at hand. "I finance the buying of more trucks in Madagascar so produce can get to town more readily, but what this REALLY does it to increase charcoaling in the area, which not only bumps the target crop, but ends up damaging the sustainability of the same rural region I was trying to help...", etc...

Just some thoughts, and now on to risk!

REDUCING RISKS AND CREATING INCENTIVES

Post by: Janice Stallard

Subject: Increasing Incentives and Reducing Risks

Thank you for everyone's excellent discussion on the definition of value chain finance. I would like to move the discussion along and begin a dialogue on how to facilitate interventions that are sustainable. That is, interventions that are seeking ways to create incentives for the private sector to act in new ways to reach new target groups (e.g., rural businesses, farmers). At the same time, we as designers and practitioners need to seek opportunities that can reduce the risk of private sector engagement. Coupling new types of incentives with reduced risks opens the doors for more sustainable programming.

What have you seen that has worked in the field?

Post by: Geoffrey Chalmers

I think this is exactly our principal challenge, especially when we look at the challenge of increasing and improving the provision of financial services by financial intermediaries (as opposed to within-the-chain financing by VC actors). This challenge is, how do we encourage private sector actors to "act in new ways", when we look at a given situation and don't see what we as "development types" would like to see (fin institutions providing a wide array of services that help upgrade producers, contribute to the competitiveness of a chain, etc.)? We can't very well just convince them in their offices that this is a great idea, so what incentives and risk-reduction can we foster so they will WANT to enter into this kind of arrangement?

Clearly, designing situations that are "win-win" and that demonstrate business sense to private sector actors such as financial intermediaries, is a necessary starting point - anything that doesn't recognize private sector actors' need to make money will not be sustainable. But it doesn't seem to be enough, does it? WE look at a given situation and think "hey, we've got a win-win-win here! These producers need credit, they're willing to pay market rates, and there are buyers who are willing to vouch for them (if not actually guarantee them) that they are good credit risks. What's the problem? If the lender lends to them, everyone is happy, including the buyer who no longer has to use his or her scarce capital to finance the production!" But yet somehow the financier doesn't see it that way - they may have other more attractive options, they may be very tied to traditional collateral-based models, or they may just not have the time, interest and/or patience to get to know these clients and chains/sectors to the point where they feel comfortable lending.

But the minute you start to talk about buying down risk through the typical means, especially guarantee funds, you are putting at risk the whole sustainability question. What will happen when the guarantee disappears? Are you building up financial intermediaries to really LEARN how to do VC lending and rural financial service provision, or is the lender simply pumping out credit without a good analysis because little or none of his/her own capital is at risk?

For me, the best way to reduce the risk for financial intermediaries is KNOWLEDGE and information: helping them little by little to understand enough to be comfortable lending: facilitating direct relationships with buyers, processors and other VC actors, for example, so they know that producers have a market. But this takes time and patience and only works with those intermediaries with the interest in pursuing this - a minority, to be sure, but a good start because they can serve as models in the future. In the meantime, a well designed (partial and temporary) guarantee could be helpful in certain countries (not in Mexico where there already exists a glut of government guarantees that are having a negative impact specifically on this point of incentives: lenders' only incentive is to pump out credit with little or no analysis). So policy work is important as well, in parallel: removing incentives that are having a negative effect on sustainable solutions.

Post by: Ms. Anita Campion

I completely agree with Geoff that KNOWLEDGE is a big part of the equation in attracting formal financial institutions to lend to various value chain actors, especially small holders. In conducting a training in Mali, we found that showing representatives of the financial institutions the big picture in what the market potential was for certain value chains (e.g., shallots) made a huge difference in how they viewed the risk profile of the potential borrower. The difficulty is that it is not easy for one producer to demonstrate the potential of a value chain on their own - this is why the linkages and industry advocates are so important. In the case of artichokes in Peru, financial institutions were willing to lend to producers not just because they had contracts with the artichoke processor, but because they understood how solid the market was for processed artichokes. Again, KNOWLEDGE was power here.

Post by: Geoffrey Chalmers

An interesting example we are exploring here in Mexico has to do with the role of info/communications technology (ICT) in achieving this: can we use an ICT platform to put the valuable information that buyers (in this case a mango packhouse) have about their suppliers, in a format that is useful for a lender, so the lender can easily access this information in order to assure them that a buyer has a "good" history (on time delivery, quality, repayment of buyer/supplier credit, etc). But regardless of how you go about it (at first, access to the information itself is the main hurdle, more than the technology per se), the important thing is making more information available to a wider set of people.

Another example is related to Anita's comments about the market potential of a given product. We have found in Mexico that the role of market studies is hugely important for this same reason. But the public sector people who do this (product by product market studies) well here are not always good at dissemination and sharing - they see it as proprietary. So we need to get the quality studies more in the public domain, then help lenders to access and understand these studies. This will be an important first step in getting lenders to be more comfortable lending into a certain VC - a lot more will be needed but at least that foundation will be set.

Post by: Linda Jones

Related to Geoff and Anita's comment on knowledge of the markets, another 'incentive' that we found for bankers/lenders when we were researching the FAO VCF book, is knowledge of a specific buyer rather than market knowledge in general. So, for example, if a banker/lender knows that a farmer is supplying Hortifruti or Starbucks, the farmer may not even need a contract in place to get finance. The knowledge of the buying/selling relationship can be enough.

Related to this, but going beyond knowledge, legal mechanisms / instruments such as purchase contracts and warehouse receipts can also be strong incentives for lenders/bankers to release funds to farmers.

Post by: Drew Tulchin

Good discussion so far, folks. And, many good points. I'll try to avoid re-iterating previous points. My concern is how to avoid positive value chain advancements from being a donor 'flavor of the month' attention so that we get some real progress that is sustainable, leads to market changes, and results in people/businesses improving.

I believe one way to safeguard this is appropriate involvement from subsidies, grants and donor/philanthropic involvement. (and government, too for that matter). I see great value in donors, gov't agencies, and others acting as conveners and enablers in value chain efforts. They can get folks in a room (bankers and SMEs) that typically aren't together. And, it is gov't that has to foster a positive enabling environment through regulations and laws. When those are efficient and effective, the whole 'system' can work better. I get concerned when gov't and donors swing in with lots of! money, statements, and people for a period of time. I don't see such efforts as maintained when the people leave and the money dries up.

Sometimes knowledge (as stated) previously might be something as unsexy as just getting value chain stakeholders to talk to each other directly and get to know one another as people but also to understand one another's needs/problems. Again, really basic and unsexy, but can be the solution to greatness.

Post by: Virginia Sibanda

I find that most interventions from a lender perspective are restricted due to the lack of infrastructure developments around the areas that these interventions are required. Our experience has been that reaching out into the remote areas has serious challenges that have nothing to do with skills, access to finance etc but the mere fact that they are so cut off from the rest of the areas where markets are etc pose the major challenge. I would then suggest that there should be serious considerations in infrastructure enhancement first and foremost as it is lack of good road networks, ICT etc that this hinders any serious engagement and any attempts to bring the poor into the main stream.

Post by: Peter van Dijk

TX Geoffrey, I totally agree that "easy access to information in order to assure them that a buyer has a "good" history (on time delivery, quality, repayment of buyer/supplier credit, etc)" is crucial in the VC. Having a network of data providers on quality, price, quality control, ESH (environment, health, safety), packaging, transport as well as financial data on the specific market player is the basis for VCF to support sustained growth and inclusiveness. Setting up and maintaining such a network requires a wide and committed alliance of all involved and cannot, may not depend on donors as it often means governance issues and risks of discontinuity.

Obviously, government and big local business players have an important role in providing support. They need to take the lead and accept and ensure Transparent Performance Measurement (standardised regular reporting and regular verification and branding, with ensured inputs of small producers and consumer protection representatives) as well as that they need to understand and accept the the positive role for all of fair competition (and fighting mono-/oligopolies).

Financial institutions have a potentially important role in promoting and supporting all of the above as they know a lot on all individuals, companies and authorities. They are decisive in increasing incentives and reducing risks. And ICT are important partners of (M)FI's (as well as of the entrepreneurs and authorities) in making the network happen, communicate in a cost-effective and secure (including managing well confidentiality issues) manner.

Post by: Lloyd Borerwe

I agree with Peter's contribution. Financial institutions have a big role to play and that is providing financial inclusion services. However, services and products must be availed at minimal cost and risk. For instance to successfully finance small scale farmers in the rural community transaction costs are high both to the farmers and financier. To circumvent this problem there is need for Institutional development services and integration of ICT in service and product delivery. Business development services that ensure productivity enhancement, market linkages and insurance will guarantee that credit risk is minimised. It is critical therefore for an integrated approach is requisite in VCF to reduce credit risk.

DAY ONE: VALUE CHAIN FINANCE SUMMARY

Post by: Janice Stallard

There has been a lively discussion on the definition and use of value chain finance today. I want to thank everyone for their time and participation. There will be a summary of the entire three day available next week which will be posted on MicroLINKS.

A quick recap of some of the key issues raised today include:

An important discussion on definitions

Various definitions were offered – most emphasizing the need to be more inclusive. In one of the closing statements a participant noted, "In the discussions of definitions of value chain financing, several persons indicated the need for it to be inclusive and/or to help the poor. While I am very conscious of that, I think we need care to note that value chain finance, like any finance, is in and of itself not necessarily inclusive, not necessarily to reach the poor, etc. Value chains, especially some of the most integrated ones, are often among the rich and well connected. Even so, there is interest on the part of the many of us who work in development to use value chains and value chain financing as an approach to deepen financial services and impact for the poor and it can be effective in promoting this."

Other proposed definitions included: "financing provided to or by a value chain actor in order to increase an industry's growth and competitiveness." And "developing products, processes, services and interventions in the value chain to improve its growth and competitiveness, while enabling the poor to manage the risks and leverage the opportunities offered by higher value contributions to value chains."

One participant summarized the discussion well, noting: "Finance is a necessary but not sufficient condition. To be effective, those interested in the financing element of VCs need to understand the full range of other variables that impinge on/interact with/support the VC, particularly any of those which, while seemingly small are in fact critical to success, or failure. The solution is not to expand the definition until the "financing of VCs" covers ALL elements, but rather to realize that one needs to look at the factors systemically, not just identify one and focus on it. Scale matters, good and bad. Sometimes providing financing may lead to the impact one is expecting, but it also could lead to some fundamental alteration of one of the relationships within the VC. Not always will financing be used for the "rational" purposes you had expected it to go for."

Reducing risk and creating incentives, some of the key points raised included:

The best way to reduce the risk for financial intermediaries is KNOWLEDGE and information: helping them little by little to understand enough to be comfortable lending: facilitating direct relationships with buyers, processors and other VC actors, for example, so they know that producers have a market. But this takes time and patience and only works with those intermediaries with the interest in pursuing this – a minority, to be sure, but a good start because they can serve as models in the future. Knowledge is a big part of the equation in attracting formal financial institutions to lend to various value chain actors, especially small holders knowledge is power.

Another 'incentive' found for bankers/lenders is knowledge of a specific buyer rather than market knowledge in general. So, for example, if a banker/lender knows that a farmer is supplying Hortifruti or Starbucks, the farmer may not even need a contract in place to get finance. The knowledge of the buying/selling relationship can be enough. Related to this, but going beyond knowledge, legal mechanisms / instruments such as purchase contracts and warehouse receipts can also be strong incentives for lenders/bankers to release funds to farmers.

DAY TWO: BEST PRACTICES FOR INCREASING INCENTIVES AND REDUCING RISKS

DAY 2: OPENING REMARKS

Post by: Janice Stallard

GOOD MORNING

Welcome to our second day of exciting discussions on value chain finance. Today, we have Luis Jimenez from WOCCU/Peru and Megan Falvey from Crimson Capital Corporation as representatives of the winning applicants from AMAP's "Innovations in Financing Value Chains" competition in February 2009. Our guest facilitators will discuss their work and solicit suggestions from the audience regarding concrete examples of how their projects have increased incentives and reduced risks for better value chain finance interventions. Mr. Jimenez will lead the discussions in the morning from Peru and Ms. Falvey will have the lead in the afternoon sessions.

Enjoy and looking forward to our second day's dialogue.

WOCCU PERU PROJECT

Post by: Luis Jimenez

Good morning,

Greetings from Peru. I am the WOCCU USAID Peru Project Director. I look forward to facilitating this discussion and share WOCCU experience in financing value chains through credit unions in Perú

Post by: Luis Jimenez

I would like to start speaking about the USAID-WOCCU-FENACREP Project.

In partnership with Peru's National Credit Union Federation (FENACREP) and with funding from the Office of Microenterprise Development at the U.S. Agency for International Development (USAID), WOCCU and six credit unions in Peru are collaborating with local producer groups and other value chain actors to develop a market-driven model for value chain finance.

WOCCU provides technical assistance to the credit unions in Peru, and they assume full risk of the loans they make. They do not receive any grants, external funding, subsidies or guarantees.

While the methodology has been developed and tested in Peruvian credit unions, it is adaptable to other types of financial institutions and may be applied to agricultural and non-agricultural value chains.

WOCCU FINANCE METHODOLOGY

Post by: Luis Jimenez

Snapshot of the WOCCU value chain finance methodology

Reducing risk

The four-phase value chain finance methodology (outlined below) is designed to assess and mitigate the specific risks associated with financing existing rural value chains and to determine at which point in the process—from production to commercialization—financing adds value to the actors. The risk dramatically increases if the credit union skips any of the phases of the value chain assessment process. Loan officers and their managers should be trained to understand the importance of following through with each phase.

Increasing incentives for all actors

A key focus of the methodology is to make the financing arrangements mutually beneficial for all value chain actors in order to increase sustainability and create market-driven financing arrangements. Value chain actors are involved! early on in the process and open conversation about each actor's objectives is encouraged. Together, they identify problems and commit to solving problems that would increase the efficiency and competitiveness of the entire value chain. As actors understand "what's in it for them," they have more incentive to provide resources and follow-through with commitments.

The four phases of the methodology

Most credit unions hire staff with a background in agriculture to manage the process.

Phase I: Identify and evaluate potential value chains
The credit union first ensures that market demand exists for a particular product and that the producers have the ability to meet the demand. Without adequate product demand, both the financial institution and the producers are at risk of significant loss.

Next, the credit union analyzes the strengths, weaknesses, opportunities and threats of each value chain. It then identifies points along the value chain where providing access to finance could bring the greatest value to small producers and would represent a good investment for the institution. At the end of this phase, it uses a scorecard tool to evaluate and rank each value chain and create a map of potential financing options.

Phase II: Facilitate and leverage market linkages
To help eliminate the presence of intermediaries, the credit union brings together all of the value chain actors to review their needs based on the evaluation in phase I. The credit union gathers production and financial data at the meeting to design appropriate loan products, and the actors identify and agree on quality standards, minimum purchase prices for the producers' goods and non-financial activities that would improve the value chain's efficiency. The direct connections provide reliable market information to solidify the small producers' business relationships and secure market access for years to come. The commitment actors make in this phase is an integral part of mitigating the financial risk of lending.

Phase III: Design the products and evaluate capacity to pay
In the third phase, the credit union analyzes potential cash flows based on information gathered during the workshop. It then designs a product that directly reflects the financing needs of the borrowers and the specific characteristics of each commodity and value chain. The credit union bases disbursement and repayment schedules on production cycles and cash flows and sets competitive interest rates to cover costs and provide a profit margin.

The credit union also establishes the processes and policies needed to address the risks associated with value chain loans, especially those made directly to producers. It then determines the best combination of collateral and signed contracts to cover the loan.

This step reduces the financial risk of granting loans with unrealistic terms and/or inadequate amounts. By basing loans on both the actors' real needs and capacity to pay, the credit union's investment is more likely to increase productivity and guarantee repayment.

Phase IV: Grant, monitor and collect loans

Before a loan is granted, all participants sign contracts that include penalties for not fulfilling responsibilities. While this is not a 100% guarantee, it reduces the risk of abuse by any one actor.

The credit union disburses loans in cash or in vouchers that permit the borrowers to obtain discounted inputs such as quality seeds, fertilizers, pesticides, tools, labor and equipment from other value chain actors. Farmer associations and technical assistance providers help monitor production, which reduces the credit unions' operational costs and allows them to reduce interest rates on loans.

Once the buyers receive the products, they channel payments to the producers via the credit union. The credit union deducts the producers' full loan payment of principal plus interest from the sale amount and deposits the remainder into the individuals' or producer associations' savings accounts.

After financing a value chain once, the credit union only needs to apply phases III and IV to grant subsequent loans unless there have been significant changes to the value chain structure. It should, however, reestablish the market argument for each investment.

PROMOTING SUSTAINABILITY

Post by: Luis Jimenez

The topic of sustainability came up in discussion a few times yesterday.

What has been your experience? How can practitioners and donors promote sustainability and increase the likelihood that financial institutions will continue to provide value chain finance after technical support and/or donor support ends?

Post by: Janice Stallard

Hello Everyone

This is a really good question that Luis raises. 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 them 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 also seeking ways to create incentives or reduce risks for nontraditional financial intermediaries. Some of these interventions are time sensitive and perhaps 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 I think it's important to think through the differences of these approaches to define - from the outset - what sustainability or success will mean.

Post by: Calvin Miller

Luis,
Having worked many years in S. America with Credit Unions providing agricultural, SME and microfinance, I know that CUs can be effective in this VCF work. Having stayed in touch with a couple of those CUs for over 25 years, I have continued to watch the progress in this area. We did a lot of VC finance from the beginning even though the VC term was not in our vocabulary but improvements, new technologies and changes in the structure of value chain relations validate the need for the kind of discussion and learning we are having today. You point out the 4 phases used by WOCCU in Peru. They are fine and effective, but a bit rigid. I see the need to understand the chain, evaluate the market, the credit risks, look at how to best structure the financing, and have direct payments from the buyers to the CU, etc., but I am not sure of the need to "eliminate the presence of intermediaries" or the use of the scorecard. If a good CU member is a! maize farmer and maize ranks low relative to green beans with a guaranteed market, does this client not get financing? I think the fundamental success factor in VCF for a financial institution is knowing the market and risks in the chain and the client risks and acting accordingly.

I would like to relate and example of the broom sorghum chain. In a region where about 90% of the broom sorghum was produced, 90% of the brooms were made for the country, and 90% of formal financing came from the local CU, we had the challenge of who to finance -- the producer, the intermediary trader/inventory accumulator, the broommaker, the woodshop handle maker and/or the buyer-exporter from the region. What is efficient, what is fair, what are the risks? All had access to finance. The most important was for the CU to gauge production levels and inventory so as to not over-finance a chain with an somewhat inelastic market, and to monitor the effects of imp! orted plastic brooms. We found that finance could come in at any level in this case (not necessarily for all types of VCs) and that it flowed up and down easily. Financing was structured according to the level in the chain. Also, if clients had less than acceptable credit history, then buyer contracts could be used. Therefore, as you note, knowledge of the chain, structuring and monitoring were success factors.

Post by: Luis Jimenez

Thanks for the responses and getting the conversation going.
I would like to start by giving a bit more background on our experience related to sustainability and then will respond to Calvin's points.

From the perspective of a Financial Institution, the credit products to finance value chains have to be profitable and sustainable. It depends on the real market potential to generate enough volume (in money) of operations under the value chain financial products. So, in the case of Peru, the credit unions have tried to finance most of value chains with real potential and have tried to encourage the weak value chain actors to strength their value chains in order ! to meet the main requirements to receive credit: good level of organization, real market demand, technical assistance and strong relationship among the actors. The credit unions along with WOCCU have worked as facilitators in these processes.

In addition, both credit unions and WOCCU through the methodology encourage every actor takes specific responsibilities, for instance the monitoring and technical assistance job, this causes the operational cost can stay low.

However, we have to recognize the number of value chains in a specific region has a limit, so, in order to maintain the value chain credit officers productivity the credit unions have come up with several solutions, for instance, the credit offi! cers also offer another kind of rural products: rural individual micro credit, agricultural credit targeted to medium and big agricultural producers, and may also have urban micro credit portfolios.

Finally, the credit unions set the interest rate on the value chain credits on an individual basis, trying to cover all the involved cost and get a adequate profitability, trying to maintain the interest rate as low as possible.

Post by: Luis Jimenez

Calvin, thanks a lot for your contribution and your comments about our methodology. Really, you are right. Our methodology tries to evaluate deeply all the value chain structure and relationships, link by link, through the value chain. Phase two in our methodology takes into account all those factors, so the credit unions and all value chain actors can identify and find solutions to several problems in the value chain and identify all specific credit needs in different links along the value chain structure. As you mentioned, we also use a mix of guarantees, i.e. buyers contracts, for actors that don't have a good credit history. Also,

We use a score in order to identify the value chains with more market potential and work with them all the process, so credit unions can choose the value chains with less risk and more potential, and use more productivity their resources. In reference to th! e "good CU member" that is a part of a value chain that won't be financed, he/she may still be eligible for another type of rural loan from the CU.

Sorry for not explaining clearly our statement "eliminate the presence of intermediaries". Really, as you know, in Latin America the intermediaries get most of the money in the commercial process, so credit unions, WOCCU and other actors have worked in building direct relationships among the true actors, in order to share the money equitably.

Post by: Megan Falvey

I think Calvin's comments touch on some of the initial questions we had yesterday and earlier today of how to define VCF and issues of sustainability.

If by definition, you include specific underprivileged groups (poor, rural farmers, etc) in VCF, then it follows that the chosen VCF intervention will be designed to give special "attention" to those groups: in Calvin's hypothetical example, the maize farmer whose crop rates low relative to green beans. This definition tries to take into account issues/questions of "fairness", as raised in the broom example (who to finance?).

However, this definition VCF must generally work harder to address the "sustainability" issue. The more VCF is designed to open finance for actors whom, under other conditions the market wouldn't service, the more care must be taken to think about a donor/project exit strategy.

Post by: Nicole Pasricha

Hi Luis and all:

From the perspective of a practitioner working on VCF from the side of VCD projects or with agricultural / rural development organizations, I see that sustainability is related to capacity building amongst staff and other actors on the basics of rural finance, investment, and value chain financing. Since the people designing the VCD / VCF interventions often aren't finance specialists they don't know how financial institutions evaluate risk, price products, or decide which regions or sectors to focus on. They do have a wealth of information that could be helpful to the institutions (along the lines you and others have outlined above), but haven't learned how to share it, nor build these relationships with the financial sector. Understandably, they are often wary of approaching financial institutions or feel intimidated by the complex requirements / product terms they see on offer, and don't know how to link those services to the activities of their VC producers or businesses.

So, for the sustainability of financing arrangements, there is a need to do capacity building and mentoring of non-financial institution staff about how to interact with the financial sector, basics of VCF product and model/partnership development, and sometimes even to the level of end-client financial education about how VC actors can better evaluate and manage financing for their VC business. These needs apply to VCD organizations, producer organizations, or any other non-financial actor or VC support organization.

BUILDING THE "HUMAN CAPACITY" OF VC FINANCE

Post by: Luis Jimenez

Thanks a lot for your contribution to the first question. Now, I would like to bring up an interesting topic; the human resources.

Just as lending is not a core function of value chain actors (and can be a key constraint in actors providing financing to other actors), agriculture is not a core function of financial institutions, and can potentially be a constraint in evaluating agricultural value chain finance loans. What do financial institutions need to do to build their "human capacity" to have the expertise on staff to provide value chain finance? What types of skills does the loan officer need to have to effectively evaluate and monitor value chain loans?

Post by: Ms. Anita Campion

I think the first issue related to capacity building has to do with convincing the FIs of the value and potential of the value chain to even interest them in considering lending to a value chain actor, especially if it is a small producers. This is the largest hurdle and requires a fair amount of the same information and capacity building that the loan officers will need to have, but first you must convince management of the viability of the model. This is often done in concert with a lead firm (often a wholesaler or processor), who can demonstrate their interest in the product,
ideally through the use of a written contract with clear terms, quantities and prices.

Post by: Luis Jimenez

On the basis our experience in Peru, we believe the building a solid base of human resources is very important in order to assure the FI will continue with the value chain financing model after project job ends.

First, the FI must hire people with deep knowledge about the region and the rural producers, with strong analytical capacity and with a very good basis in agricultural topics. Besides, a potential value chain credit officer must have a real concern in working with rural producers and strong skills in facilitate links among value chain actors.

Sedong, from the donor or project perspective, to build a good human resource basis to allow both transferring the methodology faster and, to "seeding on a good land". Besides, this assures FI can manage the value chain credits (methodology) by themselves in less time. Finally, a good human resource basis allows the FI to hire and train new staff more efficiently.

Post by: Janice Stallard

I agree with what Anita is saying and second the need to address the hurdle of high cost and risk that FIs attribute to many value chain finance activities. In addition to building an understanding we must also have concrete (in-country) examples of others doing this type of lending successfully/profitably. Donor support of pilot projects (such as the WOCCU in Peru and Crimson Capital work in Bolvia) have proven to be extremely valuable - providing a demonstration effect that is needed to encourage broader participation and increasing industry-wide competition.

SUMMARY OF MORNING SESSION

Post by: Stephanie Grell

Thank you for taking the time to share your experiences and insights on value chain finance during the morning session on day 2.

Luis Jimenez, the WOCCU Peru Project Director, moderated the session. The discussion focused on sustainability and capacity building. Here's a quick overview of what was discussed.

SUSTAINABILITY

Participants provided recommendations for donors and practitioners when tackling the question of sustainability.

Clearly define sustainability and success

One participant noted that there are "many sides" to sustainability when it comes to value chain finance and the definition of sustainability should depend on the approach. From the perspective of financial institutions, sustainability can be defined as the "continuation and/or expansion of product line." However, in value chain finance interventions involving nontraditional financial intermediaries, the definition is not as clear cut and needs to be tied to the intended "success." For example, in some cases, financing interventions are designed to increase incentives and reduce risks at a certain time. Success may be based on increased growth and competitiveness rather than "sustainability" as traditionally defined.

Cross-train value chain loan officers in other financial products

Another participant mentioned that there is usually a limited pool of value chains in a particular region, which may impact the sustainability of the value chain finance product line. Therefore, to maintain the productivity of value chain finance loan offers, they should also be trained to offer other types of rural products.

Build the capacity of development organizations and other actors to understand value chain finance

We were also reminded not to forget the importance of building the capacity of other value chain actors and development organizations involved designing value chain interventions. In many cases, they do not have a financial background and don't understand the needs of financial institutions or how to interact with them. The participant recommended capacity building and mentoring related to the basics of value chain finance, interacting with the financial sector and building partnerships with financial institutions. In some cases, financial education may be appropriate to help actors evaluate and manage financing opportunities

Bring value chain actors together

Several participants mentioned the importance of bringing participants together to come up with solutions and arrangements that are mutually beneficial. The face-to-face meetings increase the likelihood that the financing arrangements will continue. This is particularly important when we are talking about "populations that don't know, trust or understand each other."

In addition, the importance of designing interventions that are market-driven and profitable was raised again today. There was also acknowledgement that reaching sustainability is more difficult when we are talking about financing underserved groups that may require more "special attention." Finally, a few components of the WOCCU approach were discussed in more detailed.

CAPACITY BUILDING

The moderator asked the participants to discuss what financial institutions need to do to build their in-house capacity to provide value chain finance. And, what types of skills do the loan officers need to have?

Here are some highlights from the discussion:

- Capacity building is critical to the ability of financial institutions to continue financing value chains after technical assistance and/or donor support ends.

- Capacity building of a financial institution starts with convincing management of the viability of the model. This is the "largest hurdle." Information used during this process is usually the same information needed to train the loan officers.

- Building on the previous point, when trying to convince management, we need to provide them with concrete examples of other institutions that are providing value chain financial in a profitable way.

- Financial institutions should hire staff with a strong understanding of the region, rural producers and agriculture. Value chain loan officers need to have an interest in working with rural producers and the ability to facilitate relationships between different actors.

- Value chain financing usually goes beyond the relationship between the financial institution and the borrower. Often, there is a facilitator involved that is working with the financial institution, borrower and other actors. Capacity building for value chain finance and should be expanded to include these other actors. "It's a huge topic, and one that is often underestimated and underfinanced."

Thanks again for participating. I look forward to applying some of the "lessons" I have learned from your experience.

INTRODUCTION FROM CRIMSON CAPITAL

Post by: Megan Falvey

Thanks very much Luis and WOCU team!

I work for Crimson Capital and have come into this discussion based on Crimson's work on the ARCo project in Bolivia.

I think this morning's discussion has been very interesting in terms of looking at where VCF get the "most bang for the buck" or how to design these programs so that they have sustainable impact. On the most recent discussion of capacity building and human resources, Luis began by asking what skills/capacity do FI staff need to have in order to understand (and to be able to evaluate) agricultural value chains. Anita pointed out that it is not only an issue of loan/credit officers understanding agricultural value chains, but that senior FI staff need to buy into VCF.

Under ARCo in Bolivia, we took the approach that Anita suggests - initial agreement was reach with the senior management of the FI we are working with ("FIE") and then we worked through senior managers to build capacity of loan/credit officers. But we also added something different to the mix, which is Purchase Order Finance (POF) . POF is a transaction-driven, rather than collateral-dependent form of working capital financing. Through POF, the potential borrower submits a purchase order for its products to the financial institution. The purchase order itself acts as collateral and the financial institution provides the borrower with a loan to cover the costs of raw materials and packaging and other costs associated with completing production and making delivery of the specific customer purchase order. Under POF the loan/credit office must absolutely know how to structure the loan and evaluate risks (which are mostly on the side of the buyer), but they do not need to ha! ve an in-depth knowledge of the agricultural value chain and can of course make POF outside of the ag sector all together.

I find the POF approach rather unique in VCF because instead of trying to train FIs to better understand existing potential markets (SMEs, small scale farmers, etc) as is typical with most VCF projects, POF offers FI a new product to fit existing potential markets.

Are there other examples out there of new products?

Post by: Christian Pennotti

Megan,

Thank you for this really interesting example. It gets at something I've been thinking about as I tracked the conversation. I recently visited a project that was trying to facilitate improved access to value chain finance, in this instance, working with FIs as the source of funds. A major challenge was overcoming the amount of information the FIs needed in order to overcome the risks they perceived in lending to MSE farmers and groups. Thanks to a highly engaged local government and some other actors in the value chain, getting that information was not necessarily impossible (the FIs wanted to know the size of the market, who the buyers were, how profitable the crops were in that area of the region, etc). But, getting it did require a lot of farmers, who were not necessarily equipped to pull all of this information together. It was also expensive.

It seems like the POF approach may reduce a number of these costs at the FI and farmer levels by inherently placing them on the buyers.

I'm curious though whether you or others on this forum have found this POF approach to be an easy sell to the various partners, including buyers, as well as what shortcomings this approach may have.

Post by: Megan Falvey

Our experience is that POF works in nearly every environment and across sectors (no reason to limit it to "just" ag); we've successfully launched POF and/or Accounts Receivable Financing (ARF) in Macedonia, Kosovo, Armenia, Bolivia and Moldova and are working to introduce it in Azerbaijan and Peru. It works because it is a profitable activity for the FI and because it provides working capital with reduced collateral requirements to borrowers.

Concerning limitations:
1. POF takes time to introduce and requires carefully planning, negotiation, buy-in from the FI and then TA to implement. From start to finish, it can take more than a year to process the first POF in a new country. There are a variety of ways to introduce it, but all should require significant commitment from the FI. In Bolivia under ARCo we invited interested FIs to "apply" for the program; out of 10 initial expressions of interest, only 1 institution ended up making the cut.

2. POF should be seen as a compliment to other activities to strengthen the value chain. It provides working capital only and therefore will not address all the lending needs of the value chain.

Post by: Geoffrey Chalmers

I think the mechanism Megan describes - as well as similar but less formal arrangements in which no formal document is needed - are a great way of facilitating more external finance into a chain. They effectively buy down risk to lenders by increasing information (esp about market access of the borrower) available to them. If successful, it's likely to be sustainable b/c the lender sees it works and continues on their own and then others copycat it.

As Megan pointed out, these arrangements are mostly for working capital for those who ALREADY have good market links.

So my question is: has anyone seen a mechanism that goes the next step and gets finance to help either a) a small producer invest and upgrade; or b) a producer who is NOT yet in a high value/potential chain get INTO such a chain? (Example: fruit producer with good product is selling locally but wants to move into a more attractive channel)

The 2 are inter-related b/c investment (eg irrigation kit) is often one of the things that allow a producer to move into a new, more attractive market channel (which in itself is another form of upgrading.

Clearly, the financing in such a case is not going to magically allow a producer to upgrade and/or take advantage of a new, more attractive market opportunity.

Just as clearly, I am not suggesting that the more "advanced" case of VCF helping these upgrading cases somehow diminish the importance of examples such as POF - the examples where it helps bring in new working capital are welcome and make sense as the first place to focus, since they are more viable mechanisms, the FIs are more likely to come on board, etc.

But I'd like to think we can keep our eyes on the prize at the same time and ask the question, if and how access to fin services can really make a significant difference for the producers and for the chain as a whole by being one piece of the puzzle of upgrading??

Post by: Ruth Junkin

I have found that the case of FondeAgro in Nicaragua is very interesting for its integrated approach to inserting financial services into a broader value chain development effort. This project is run by the Ministry of Agriculture and funded by the Swedish government. It started by selected sectors (coffee and milk) and specific territories in the country that showed potential.

For the milk sector, value chain development efforts began with technical assistance to farmers to improve production practices. Technical service providers identified issues with market conditions - sales of low quality milk to local buyers for cheese production. Demand was highly variable by season, as were prices. The project identified improved market opportunities with larger-scale industry in the capital, facilitated discussion of these opportunities and requirements that these oppo! rtunities implied with the farmers. These requirements included investments at the farm level, business organization, investments in refrigerated collection centers, among other issues.

Financing was brought through a number of different actors and using different models, depending on the financing needs and lender profiles. For example, microfinance institutions and savings and loan cooperatives provided financing for some farm-level investments (incentives were provided for the first MFIs to establish offices in the territories). A partial guarantee fund was established in a commercial bank, to encourage financing of larger investments in equipment for producer cooperatives. One microfinance organization developed a product to co-finance poorer farmer´s initial investment into newly formed businesses. A commercial bank developed a leasing product to provide refrigerated tanks to newly-formed collection centers.

Producing higher-quality milk allowed ! the producers (through their cooperative) to negotiate better conditio ns with businesses in the capital, providing higher prices and profits overall, as well as increased price stability.

It is clear to me that in this case, the interaction of technical, business and financial services was crucial. The on-the-ground contact through technical and business service providers clearly identified needs and opportunities for the development of new financial services, which were further developed in coordination with the financial service providers.

If anyone would like to see more detail on this effort, I can provide you with the systematization that we worked on. Just contact me directly.

Post by: Linda Jones

Hi Geoff,

You asked about a case where VCF was used to bring smallholders into a chain and enable them to participate.

This was a key objective of a MEDA program that ran from 2004 to 2008 in the horticulture subsector in Tajikistan.

We brought (thanks to CIDA) $1 million loan capital for smallholders to the table, along with the development of extension services, market access facilitation, business development services and both a small loan fund and matching grants for SME processors in the horticulture value chain.

We worked with a local MFI (ABW that evolved to IMON) to develop their Ag portfolio - at that time they were lending mainly to traders. We agreed to a plan that saw over 3000 smallholders receive microfinance loans to upgrade their farms/businesses within the first couple of years. Once the portfolio was established and the MFI was successfully lending to smallholders, and certain criteria were met, we transferred ownership of the loan capital to the MFI.

The fund was very successful, and ED of the MFI (Sanavbar Sharipova) indicated that it was knowledge of the chain that enabled the loan officers to make good decisions about loans. They worked closely with extensionists who had firsthand knowledge of the farmers as well as their specific plans/crops.

We did not use a lead firm model but targeted multiple processors as well as semi-processed markets in the region (Russia and Kazakhstan were big markets). Some farmers continued to sell fresh and home-processed goods at local markets.

Does this fit the type of example you were wondering about?

(PS I will be offline Thursday but will look forward to reading the debate Thursday night or later in the week.)

Post by: Drew Tulchin

Dear Colleagues,

Ah. Sustainability. It can be a valued concept, a catch phrase, or a bogeyman. I don't mean to be cynical, as I believe it to be vital to our development efforts and often projects do not consider it enough. It is frequent that when new initiatives begin, they do not consider what might occur at the end.

I do feel we collectively need to structure interventions and efforts which can lead to behavior and economic change (for the better). A practice in North American philanthropy which I have seen less in international efforts is to step down financing from full or near full subsidy (i.e. paying for everything), to a weaning where market costs are gradually assumed.

In specific terms of financing, sustainability appears most likely if a value chain initiative is filling a real need that extends beyond those involved in the pilot. And, if bankers can make money from it. Also, there is real power and effect in bringing the participants of a value chain together to seek common (and self interested) solutions. This component is really unsexy, but the facilitation – particularly to assist populations that don't know, trust, or understand each other – can generate extensive value. For example, campesinos and bankers can benefit from one another, but do not understand each other and perhaps don't know the right questions to ask each other or to present them in ways that will be more receptive.

I am interested in others' experiences where different players in the value chain are found to speak completely different languages than each other, making it difficult to find common ground and financial engagement.

PROJECT SUSTAINABILITY, SUBSIDIES & PROJECT DESIGN

Post by: Megan Falvey

I'd like to return to some key issues discussed over the past 2 days:

Basically all of our VCF projects offer some form of a subsidy: some projects offer training to FI staff to better understand VCF; some offer training to VCF actors; in Crimson's case in Bolivia we offered both training to FI staff and a small grant to establish FI branch operations in the target areas.

Are there implications for project sustainability in working with and subsidizing particular segments of the equation (FI institution, small scale farmer, farmers cooperative, distributors, etc)?

Post by: Linda Jones

Hi Megan & co

You ask if there are "implications for project sustainability in subsidizing particular segments of the equation."

I am answering based on the assumption that you mean the sustainbility of the value chain itself and therefore the value chain financing, (not the project).

This has received enormous effort in VC circles - and SEEP currently has a learning topic on "Scale and Sustainability" regarding value chains in which Mary McVay and myself have put a lot of time and energy.

In my experience, I would say the answer is "It depends". Subsidies from training to matching grants to subsidized interest etc. need to be assessed in the context of the value chain - what are the opportunities, what is the financial potential to the various individual and aggregated value chain players, where are the bottlenecks, what are the solutions etc.....When we know this (through value chain analysis) then we can design a strategy that puts the 'incentives' in the right place and in a way that builds sustainability rather than dependency.

The latter is key - subsidies, incentives, interventions of any kind need to know from the start what the sustainable outcome will be. Exit strategies have to be designed before the project begins.

In general though - guarantee funds make me very nervous. It encourages risk that may not be warranted, which can lead to bankruptcy on the part of the borrower and no accountability on the part of the lender. I'd love to hear more from someone who has good experience with guarantee funds and what are the factors / limitations that can make them a positive influence on sustainable solutions.

RE: INCREASING INCENTIVES AND REDUCING RISKS

Post by: Mary McVay

Thanks to everyone for an informative dialogue on this critical issue. A few thoughts:

1) I usually think of value chain finance as ...There is a development organization working intensively in a value chain and one thing they need to do is improve availability of finance in that particular system. I can see a situation where several programs are approaching financial institutions with knowledge about a particular value chain, trying to get them engaged. I very much like the concepts of having some kind of "convener" and ITC platform that would promote the "market segment" of value chain financing as a product line, a methodology in general. The convening organization and IT platform can be the interface between the financial institutions and the value chain development programs/leaders that have the industry level knowledge and understand the intricacies of specific markets. I can envision tools for financial institutions helping them understand the concepts, select viable sectors, develop products/methodologies, work with VCD programs etc. And, parallel! tools for VCD practitioners. The point being - it's too difficult to approach this one program or one industry at a time. MFI associations might be a good place to start, understanding that a range of financial institutions need to come into play. Are there other existing platforms that might take on this role of "convener" .. who might own the IT platform?

2) It seems that most value chain finance experience comes from agricultural marketing ... is anyone familiar with urban examples of value chain finance? The Value Initiative will be exploring this learning theme with our 4 pilot program and would be interested in literature, examples and partnerships in this arena.

BUILDING THE HUMAN CAPACITY TO HANDLE VALUE CHAIN FINANCE

Post by: Linda Jones

Often value chain financing is not simply between a FI and a borrower, but involves a facilitator - that is and NGO or other organization that is facilitating the development of the value chain. The facilitator may be developing value chain linkages, including those between value chain businesses (including small producers) and FIs. When we take this broader view of VCF (to be part of VCD) then we see expanded needs for capacity building - not just the FI but the facilitator's staff, the value chain businesses, perhaps enabling environment agencies and other stakeholders.

It's a huge topic, and one that is often underestimated and underfinanced.

DAY 2: CLOSING REMARKS

Post by: Megan Falvey

Hello all and thank you very much for sharing your experiences and comments on VCF today.

I think today's questions and discussion all stem from following dilemma: the more value chain development is designed to support small scale producers and poorest actors (something we all agree is good), the more "subsidy"/donor support is generally required, which can make sustainability and successful donor exit strategy difficult. The further you get away from actors the market is willing to serve, the more effort it will take to extend financing to those actors. Perhaps there are some exceptions to this, but I haven't seen any.

I don't have an answer to this dilemma, so instead I'll close today by summarizing some (yet) unanswered questions raised this afternoon. Perhaps these questions can be used to enlighten tomorrow's session, which will look at methodologies and tools to advance VCF.

1) Linda expressed concern over the use of guarantee funds and asked for practitioners' experience with guarantee funds

2) Geoffrey asked how to open access to finance to help support small scale producers invest and upgrade to get into high potential value chains

3) Mary expressed interest in examples of non-ag sector VCF and how ICT platforms can be used to promote the marketing aspects of VCF

Today's discussion also touched on how to get FIs information they need (in a cost effective way) to get into VCF, especially in the ag sector; on introducing new financial products such as Purchase Order Finance -- what it can be used for and what its limitations are; on capacity building along the VCF; subsidies and sustainability/donor exit strategies.

Thank you to all and enjoy your evening!

DAY THREE: TOOLS TO DELIVER SUCCESSFUL VALUE CHAIN FINANCE PRODUCTS

DAY 3: INTRODUCTION

Post by: Janice Stallard

GOOD MORNING EVERYONE

Welcome to our third and final day of our value chain finance discussion. Thank you for everyone's participation so far. It has been a tremendous debate and sharing of ideas.

Today, our guest facilitator will be Anita Campion who is a leader in the financial services delivery. Ms. Campion will facilitate a discussion to solicit ideas from the audience regarding tools needed to advance value chain finance best practices.

We welcome your participation today and look forward to an active dialogue to help us identify, design, and develop tools that will support our practitioners to implement successful value chain finance programs.

Janice K. Stallard, ACDI/VOCA

TOOLS

Post by: Ms. Anita Campion

Thanks for the introduction Janice and for all the great comments and experiences shared to date. This has been a fruitful discussion, which shows how much we all still have to learn about to maximize our ability to improve value chain actors' access to finance. So, today, I would like us to try to think about what is needed next to continue the learning process. There are an increasing number of documented cases out there, especially related to value chain development, but it seems to me that we don't know all the answers yet, especially related to:

- 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 VCF?
- what are common issues related to VCF regardless of the sector, whether ag-related or not?

In regards to tools, would any of these be helpful to facilitate VCF:

- standardized approach to evaluating finance potential in a value chain (e.g. not all VCs are appropriate for finance - i.e. perishables
- how to assess that a VC is dynamic and offers significant growth potential?
- templates for contracts (between VC actors and with financial institutions)

- methodology for pricing finance associated with a value chain product (i.e. input or supply)
- tools for monitoring and collection associated with value chain finance
- guidelines for when and how to transition finance from within a VC to a financial institution
- how to determine the appropriate use of subsidies and factoring in the costs of technical assistance

I look forward to hearing participants' ideas on what is most needed next and please let us know if there are other tools already out there, so we can build on those and avoid unnecesary replication of efforts.

Post by: Linda Jones

Hi all,

Thanks to everyone for the great discussion so far. I have very much enjoyed the exchange and learning.

I am very excited about Anita's questions re tools - in my experience, good tools targeted at the right level with a suitable complexity work well in supporting capacity building and effective programming.

A quick note on what FAO is doing re VCF resources and what are possible next needs....

As mentioned earlier, Calvin and I have been working on a VCF book coalesces the experiences of a broad range of practitioners / financiers from around the globe. The book shares those experiences and describes the various instruments that are used in VCF from traditional trader credit within the chain through to highly structured financial tools. Innovations, lessons, recommendations and cases are also included.

We hope people will see it as a useful reference, but it is not a detailed 'how-to'. I think such a step by step guide would be a nice addition to the field - with tables that walk practitioners through processes, provide sample official documents such as MOUs and warehouse receipts, etc. etc.

It would be great if such a 'toolkit' were in modular form. In fact, I could see a group of us developing such a toolkit, with a person or few people responsible for each tool. We could do it in wiki style so that others could comment and embellish (with citations). To my mind, this would get the job done fast and benefit from our collective experience and strengths.

I'd love the opportunity to collaborate with you in such a productive effort!

Post by: Ms. Anita Campion

Thanks for sharing that Linda and speaking of Wiki's USAID just announced that it is planning on launching a wiki for value chain development on April 13 from 3-5PM at the AED Conference Center at 1825 Connecticut Ave. NW. I don't know anything about it, other than if you want to attend, you just need to email:
vcwiki@microlinks.org
If someone else knows more, please explain what this wiki will do!

Post by: Ruth Campbell

Yes, there is a very comprehensive value chain development wiki about to be launched. It is still -- on always will be -- under development, but the content to date has been put together by more than 50 contributors from about 20 different organizations. (If you want a sneak peek, it is at www.microlinks.org/vcwiki.) There is a section on value chain finance -- and we would love to hear your comments on it.

For those of you that will be in the Washington D.C. area on April 13, the invitation is posted below. We would love to see you there!

Ruth Campbell, ACDI/VOCA (on behalf of the wiki development team)

Post by: Rashmi Ekka

As we continue this learning process, many more questions arise. Thank you Linda for sharing about the VCF book you're working on.

Drew has also raised an important point of facilitating conversations between different actors within the VCF which will nudge them in the direction of finding joint solutions. However can we realistically expect longer term, larger finance to happen within a VC or is it only going to happen between a Financial Institution and a VC actor? One way this could happen is if some of the bigger multi-national companies such as DelMonte would be interested in expanding value chains and engaging in public private partnerships. I'd be interested to know about other people's experience in doing this.

Post by: Calvin Miller

Anita has asked many questions and I will comment on a few. First, I want to echo the need for a joint effort on training modules on the subject. We in FAO are contemplating doing some work on this but would prefer a collaborative effort, both funding-wise and content input-wise.

Regarding subsidy, I first want to note that we should not assume a need for any subsidy. Most chains have developed that way. We can intervene to help them be more inclusive, to take the rough edges off risk and new types of chains, and to build competitiveness. We can also add a lot of useful donor and governmental support through improving value chain dev. by the policies, the way collateral is treated by Central Bank rules, the way the courts (formal and informal systems) work to ensure compliance, etc. The other major area of support without distorting the system is training and capacity building -- group bus. dev., understanding standards, improved varieties, etc. When these! are not enough, as is the case with many smallholders in value chains such as vegetables for export, then a model such as a facitator model (often as a fee-based service company) or lead company model can be needed, .

On the topic of tools, there are many tools and financial instruments, many of which are new to micro and SME finance but commonplace for large banks such as Rabobank. Understanding and having the capacity to directly use some of them is beyond the realm of many organizations but can often be used higher in the value chain and/or by linking with the institutions that have this capacity. (Sorry there is not space to explain further.) Regarding pricing, monitoring, etc., I have found that plain vanilla cost accounting built in to the business model at all levels is about as good a source of information as well as for building accountability as anything. Finally, Anita notes the need for templates for contracts. In FAO we have a Contract Farming Resource Centre website specifically on contracts, templates, etc., which is: www.fao.org/ag/ags/contract-farming/en/ Thanks again for promoting the dialogue on this topic.

Calvin Miller, FAO Rome

Post by: Ruth Junkin

Regarding tools...

We are currently finishing a guide for facilitating value chain finance that will be available by the end of April. The guide will be in Spanish and is aimed primarily at value chain development facilitators - not financial institutions. It describes a process and has practical tools to help analyze the chain, analyze the interests and capacities of the actors, design a financing strategy and implement and monitor the strategy. The guide is being developed by CATIE and RUTA and will be posted on our site once it is ready. If anyone would like to receive a copy, you can also send me an e-mail and I will send you a copy once it is published.

We are also currently developing a tool box (CATIE, GTZ, RUTA) on value chain development. There will be some tools included related to the issue of value chain finance. This is scheduled to be available to the public mid-year. Again, the tools will be in Spanish.

We are also very interested in continuing this work on tool development, training modules and would also be interested in collaborating on research initiatives.

Post by: Ms. Anita Campion

Thanks for the sneak peak at the Wiki Ruth, It looks fantastic and covers a lot of important ground, while facilitating the reader's ability to focus on whatever they are most interested in! Kudos to all those who worked on developing it. The only suggestion I have is to make sure that in the Value Chain Finance discussion that it is explained that finance within the value chain often comes embedded in the costs of an input, so it doesn't always look like what we think of as finance. In the case of artichokes, for example, the producers received the seedlings from the processor for which they did not have to pay until after harvest (so the finance was essentially a part of the end cost that those producers had to pay back to the processor). Traditional finance types sometimes have a hard time seeing the finance in value chains, as it rarely looks like a traditional loan.

Post by: Linda Jones

Hi Ruth,

I look forward to seeing the toolbox on value chain development, and the VCD wiki.Good news to have more of such resources.

Are you familiar with the MEDA tools: there is one on market research for value chain initiatives, and another on program design for value chain initiatives.

They are both available at
http://www.meda.org/WhatWeDo/ProductionMarketingLinkages/Resources/Publications.html

DFID and ILO have also put out some very good practical materials..

None of these (as far as I know) incorporates tools for value chain finance.

Post by: Harry Clemens

Regarding tools and training

I would like to advise that last February a number of Dutch and international institutions brought together in Nairobi (organised by IIRR, and KIT) practitioners from 13 value chains to document their experience with value chain finance using a 'writeshop' methodology. A writeshop is a methodology to document real-life experience and to learn from them. At this moment draft materials that came out of this learning event can be accessed at http://drop.io/chainfinance but please note these are drafts. Later on it is expected that materials can be transformed into training materials (case studies), but this is still in a planning phase. I think there are different training needs by different target groups. We hope to cover some of them.

The chains range from milk to fish, and from India to Rwanda and Peru.

Unfortunately I have to leave, so I wil not be able to respond to questions in the course of today. I must say this is a very interesting discussion. The questions raised today are very good!

Post by: Ruth Campbell

Thanks, Linda -- these look like great resources. I will check to see if they are already linked into the wiki resources page, and if not, contact MEDA to request permission to link to them.

If anyone else has value chain development resources that they think should be added to the wiki, please let me know. Many thanks!

Post by: Ruth Junkin

I also say thanks - it seems we are two Ruths here! Linda, have these or will these documents be translated into Spanish?

Post by: Linda Jones

Hi Ruth,
They have not yet been translated into Spanish, but MEDA was in dialogue with an organization regard to use and possible translation - I can check into that for you and let you know.

Post by: Ms. Anita Campion

Here are a couple other upcoming resources related to value chain finance:

AZMJ is researching agricultural value chain finance in Honduras and Nicaragua for the Inter-American Development Bank, the results of which will be available in English and Spanish on the website at www.azmj.org by the end of 2009.

ACDI-VOCA is getting ready to launch a new global investment fund (including equity and debt) for Rural and Agricultural Finance, for which approximately 10% will be aimed at direct investments in value chain firms.

Are there any others out there we should know about? What else do you think is needed to answer the remaining unanswered questions we have on value chain financing?

Post by: Linda Jones

Hi Ruth,

MEDA has given permission for them to be linked, uploaded and distributed, so please do go ahead.
If you would like a direct confirmation, please contact Jerry Quigley jquigley@meda.org

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DAY 3: SUMMARY

Post by: Ms. Anita Campion

To summarize, today we talked about tools and resources that are available or needed to facilitate value chain finance and development.

There were some new tools mentioned:

Drafts from a "writeshop" in Africa, which engaged actors from 13 value chains to document their experiences with value chain finance available at: http://drop.io/chainfinance

A Value Chain Wiki to be launched by USAID at AED's Conference Center in D.C. on April 13, 2009 and located at www.microlinks.org/vcwiki

Tools for Value Chain Development on MEDA's website at www.meda.org/WhatWeDo/ProductionMarketingLinkages/Resources/Publications.html

Tools soon to be available:

A Guide for facilitating value chain finance in Spanish, by CATIE and RUTA, by the end of April, 2009. If you would like to receive a copy, contact Ruth Junkin at rjunkin@catie.ac.cr

Linda Jones and Calvin Miller of FAO are working on a VCF book that coalesces experiences of a broad range of practitioners / financiers from around the globe.

AZMJ is researching agricultural value chain finance in Honduras and Nicaragua for the Inter-American Development Bank, the results of which will be available in English and Spanish on the website at www.azmj.org by the end of 2009.

ACDI-VOCA is getting ready to launch a new investment fund for Rural and Agricultural Finance, for which approximately 10% will be aimed at direct investments in value chain firms.

Tools we would like to see developed:

A step by step guide on VCF with tables that walk practitioners through processes, provide sample official documents, such as MOUs and warehouse receipts, templates for contracts (between VC actors and with financial institutions), etc.

Methodology for pricing finance associated with a value chain product (i.e. input or supply)

Tools for monitoring and collection associated with value chain finance

Guidelines for when and how to transition finance from within a VC to a financial institution and/or how to determine the appropriate use of subsidies to stimulate value chain finance.

Experiment and conduct pilot tests to find solutions to tough problems, such as access to longer term finance, possibly engaging the multinational companies in the solutions.

Finally, I thank all of you for contributing to the dialogue today and throughout the event. Clearly, by sharing in these ways we move a little closer to understanding the complexities and the potential for value chain finance.

Post by: Ruth Campbell

Yes, there is a very comprehensive value chain development wiki about to be launched. It is still -- on always will be -- under development, but the content to date has been put together by more than 50 contributors from about 20 different organizations. (If you want a sneak peek, it is at www.microlinks.org/vcwiki) There is a section on value chain finance – and we would love to hear your comments on it.

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Ruth Campbell, ACDI/VOCA (on behalf of the wiki development team)

CLOSING: DAY FOUR

Post by: Janice Stallard

GOOD MORNING EVERYONE. Thank you for a wonderful three days of discussion on value chain finance. I learned a lot from my colleagues and want to thank you all for sharing your on-going challenges and opportunities. Please feel free to continue the discussion today (Friday) with any concluding remarks.

I will be summarizing our three days of dialogue in the near future; this summary document will be posted on MicroLINKS. The AMAP team will continue to work on this important topic and we'll have more to share with you in 2009.

Thanks again to all of you and look forward to our future discussions. Please feel free to contact me directly at jstallard@acdivoca.org

Post by: Anna Van der Heijden

Dear all,

On behalf of the microLINKS team, I'd like to thank Janice Stallard for hosting this forum, and all the excellent facilitators – Luis Jimenez, Stephanie Grell, Megan Falvey, and Anita Campion – for their dedicated support. Of course another big "thank you" goes to all the 108 participants, without whom this dialogue would have never happened. The forum included 75 messages posted in 3 days, with participants coming from 28 different countries.

The messages and related resources shared in the forum will continue to be available at www.microlinks.org/sc/valuechainfinance, and in about 2 weeks we will add to those resources a document that includes all the postings in one easy-to-search document. The summary, prepared by Janice, will also be posted in that resource section.

If you are interested in future activities on microLINKS, USAID value chain research activities, or other information related to microenterprise development , please consider signing up for our monthly electronic newsletter, Connections, at www.microlinks.org/connections

Thanks again to everyone. I hope you enjoyed it and we look forward to seeing you online (or in person) again soon.

Brandon Szabo, Anna van der Heijden

microLINKS team

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