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Finance for Small-Scale Commodity Processing: From Micro to Meso Finance

Summary of presentations and discussions

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1. Workshop scope and objectives

The main focus of the Workshop was on sustainable financial services for the first stages of commodity processing to support small-scale producers to move up the value-added chain and increase their efficiency and earnings in commodity production. In this regard, the Workshop carried out an assessment of investment opportunities and financing needs at the producer level. It further considered whether there is a lack of financial services in the middle-range or meso-credit category around USD 3,000 and above for rural commodity processing.

The Workshop addressed the following topics:

- Micro and meso-credit requirements of commodity producers and processors
- Mechanisms currently employed by financial institutions, non-bank financial institutions, regional agricultural credit associations and donors in micro and meso-credit to the commodity sector and their experience in this area
- Measures and options that would alleviate identified problems
- The role of the Common Fund for Commodities and other financial and development institutions in this sector.

Four organizations were involved in the organization of the Workshop: the Common Fund for Commodities and the Arab Organization for Agricultural Development, the Ministry of Foreign Trade and the Ministry of Agriculture and Forestry of the Republic of Sudan. Their joint objective, and the key challenge of the Workshop, was:

- the promotion of investment and financing opportunities along the commodity chain.

There was agreement among the organizers and participants of the Workshop that commodity production, processing and trade are the backbone of the rural world in developing countries, providing subsistence food, income, employment and opportunities for growth and development. Finance – comprising savings, credit and insurance – was found essential in this commodity-dominated rural world.

There are two sides in the financing of the commodity sector:

(i) the demand side, with strategies for processors, producers and traders; and
(ii) the supply side, with strategies for financial institutions.

There was agreement at the Workshop on two issues which are crucial in combating poverty in a sustainable way: (i) on the demand side, there has to be a shift away from a sole emphasis on commodity production towards value addition through processing and marketing the processed goods; (ii) on the supply side, there has to be a shift away from charity and interest rate subsidies towards dynamically growing financial services at commercial terms.

In this perspective, the challenge is now how to turn effective demand for financial services (ie, not any and all demand) into effective supply of financial services. The two sides have sometimes contradictory, but mostly complementary, though not identical interests. These are not two different worlds, but two sides of the same world: they can only grow together or fall together. Each contributes to the other's growth or failure: viable financial institutions provide financial services to producers, processors and traders , thereby contributing to their viability and growth; viable producers, processors and traders contribute to the viability and growth of financial institutions. **Viability** is crucial.

Short-term benefits of small entrepreneurs – gained, eg, by running away with a loan – are of little benefit to them if this is the last loan they received. Squeezing collateral out of a small entrepreneurs who cannot repay a loan is of little benefit to an MFI as this will be the last loan given to that customer. **Sustainability** is crucial: of producers, processors and traders one the one hand and of MFIs on the other hand.

A few high-quality loans to a few first-rate producers, processors and traders do little good: be it to the commodity sector or to the MF sector. **Outreach** is crucial.

2. Potential and needs for rural agro-processing

Three examples of the potential and needs for rural agro-processing were presented at the Workshop: cassava, leather, and preserved and processed fruits and vegetables.

In Ghana, as in numerous other countries, cassava processing offers highly profitable, diversified investment opportunities. 80% of farmers produce cassava, amounting to 10 million tons, which accounts for 22% of agricultural income and supplies 25% of calories consumed. Access to finance is only one problem. Interest rates used to be as high as 80%; and investors put their money into government papers with a yield of 60%. Interest rates are now down to 20%; but farmers still have a bad name among bankers. The other problem is agriculture itself. In the words of David Pessey: “Everyone in Ghana who can leaves agriculture.” The IITA in Nigeria exhibits 32 cassava products; very few of them are found on local markets, commercialisation being the bottleneck. In this situation, Feed & Flour (Ghana) Ltd. (FFGL) proposes to set up a plant for the processing and marketing of high quality cassava flour, based on a modification of the gari-making process developed by IITA. Facing an estimated annual demand of 144,000 tons, FFGL would either need a grant of USD 110,000 for a quick start; or “go at its own pace”, starting on a smaller scale with existing own resources, which are more in the range of meso-finance. The latter course is the more likely and the less risky one. Participants suggested that, “commercial ideas need to be tested with your own money at your own risk.”

In rural Sudan, more than 75% of the labor force depend on livestock: a cattle population of 132 million, mostly raised under traditional nomadic conditions. Cattle, sheep, goats and camels are kept for meat, as draught animals and as a store of wealth. Livestock yield 35% meat and 65% by-products, among them hides and skins. Traditionally, there is a wide variety of leather products, processed in artisanal tanneries, of which there are more than 290 scattered all over the country, and financed from own local resources. Two national centers have been established: one for the collection and preservation of raw hides and skins, one for research and development. The focus is on small and medium enterprises (SMEs) to increase the efficiency and quality of leather processing. The CFC supports a project to improve the processing of leather after the tannery stage, applicable throughout the COMESA region.[1] One of the findings lies in the importance attributed to quality in the process of adding value. Quality is crucial throughout the commodity chain, starting with the quality of livestock and its veterinary care, which has a bearing on the post-processing of meat and leather. Major needs are training of producers in clean production and processing, quality awareness and quality management, capacity-building, access to finance, accurate information, and essential utilities and services. For a substantial improvement in the processing and marketing of leather, better cooperation between private producers, producer associations, commercial institutions, government agencies and donors is required. Historically, dating back to the 8th century, several Arab countries have excelled in the quality of leather production and in the organization of artisans. This raises the question how the exchange of experience with countries like Morocco where these traditions are as alive as ever can be built into donor and government support of countries where such traditions have declined or are absent.

Depending on seasonal and regional variation, the Sudan is one of many countries which produce an excess of tomatoes, yet import large quantities of tomato concentrate, amounting to 9-10,000 tons annually. Also, there is an abundance of mangoes in Sudan: 200,000 tons in a particular area, 60 % of which are lost through the lack of proper post harvest treatment and/or the absence of processing facilities. The drying and processing of fruits and vegetables offers solutions to these problems, indicatively described here for Sudan.

The preservation and processing of fruits and vegetables adds value, generates employment and improves diet. Key issues are: Is processing worthwhile? And can farmers supply the material on a regular basis? Value addition requires the planning of diversified processing of several fruits and vegetables over the year to maximize plant utilization; intermediate-scale processing through contract farming and the pooling of producers; the use of locally available raw materials and appropriate technologies to minimize capital expenditure and, at the same time, maximize product quality. Success factors are adequate training, the quality of raw material, and market analysis. The history of financing is full of failures, as reported in chapter 1.2. The sector needs experienced micro-entrepreneurs linked to farmers who are willing and able to grow fruits and vegetables, thereby guaranteeing a steady source of supply; appropriate risk management, such as spreading production over several fruits and vegetables; good linkages between producers and processors; and financial engineering comprising savings mobilization as a basis for self-financing, the provision of investment capital, a balancing of individual and group lending technologies, and a legal framework for sanctions against defaulters. Experience in several countries has shown that the informal financial sector is quite able to cater for small-scale financial needs, but not for larger loans; that rapid access to finance is more important to borrowers than cost; and that agricultural banks, as in Thailand and Bangladesh, are able to successfully diversify their portfolio by combining loans to agricultural producers and non-agricultural small enterprises and processors. Last but not least: the FAO has a technical manual for fruit processing on offer.

3. Non-financial services for commodity processing, diversification and trading

[1] See Session 1.2, chapter on *Adding Value to African Leather*.

Business development services (BDS) can be of crucial importance to small and micro enterprises in various sectors of the economy, but have generally been of limited success. Not only have many heavily funded BDS programs broken down; it is being argued that it is the very fact of donor support which has undermined the market for BDS. Just as subsidized interest rates have undermined financial markets, so has donor support undermined the viability of BDS. This, however, can be turned around, as the experience with CEFE shows, a medium, small and micro enterprise development training concept. CEFE, an acronym for *Competency-based Economies through Formation of Enterprise*, has been developed since 1979 by GTZ, the German Technical Cooperation Agency supported by the German Ministry of Economic Cooperation and Development. It is an action-oriented adult training tool, applied in numerous countries around the world, which helps micro, small and medium entrepreneurs developing a realistic business plan, which they then put into practice at their own risk . To break the vicious circle between donor dependency and lack of viability, the proponents of CEFE have proposed a new paradigm: BDS is a private good! therefore the delivery of BDS should be done by the private sector and governments should only facilitate the market development of BDS. Accordingly, the delivery of CEFE has now been made a private business in various countries, including Sri Lanka. In Sri Lanka, 18 organizations are making use of CEFE as a fee-based BDS in different contexts and environments, 10 of them in the private sector. To a good number of them, BDS is a major source of income. These organizations use CEFE for three major components of their portfolio: training & capacity development of BDS organizations; brand image development; and product packaging & marketing. Market orientation, marketing and diversification for agricultural producers, processors and traders is one of several products, with two major parts: market orientation and business planning .The benefits include: sustainable increase in income, better ability to analyze production and marketing patterns, and the identification and use of opportunities for improved marketing. The CEFE team in Sri Lanka has also analyzed most of major microcredit schemes, which were all donor-driven, and found that most of them were not successful. They have already tested and introduced a new approach to link commercial BDS and commercial micro finance schemes operated by micro finance institutions and banks. The approach includes direct linking of CEFE training and micro credit and opening of CEFE training for micro credit customers on a commercial basis.

A different experience is reported from India, where Nabard, the National Bank for Agriculture and Rural Development, has promoted the establishment of about 800,000 self-help groups (SHGs) of the rural poor and their linkages with some 20,000 bank branches. The approach, referred to as SHG Banking, is applied all over India: in marginal as well as high-potential areas. Numerous NGOs and government organizations are involved in social mobilization and non-financial services. An example is the BAIF Development Research Foundation, an NGO which has helped some 13,000 tribal families, who are among the disadvantaged in India, to cross the poverty line: (i) through sustainable agri-horti-silvicultural production on 12,000 acres of rehabilitated lands and (ii) through commodity processing. Against a historical background of the direct sale of raw materials, six vertically integrated layers of production, processing and marketing were established in remote forest areas: (i) individual farm households for basic production on wastelands, (ii) small farmer groups for procurement and grading, (iii) community organizations (*Gram Vikas Mandals*) for the establishment of community processing facilities, (iv) village planning committees for the organization and coordination of activities, (v) regional cooperatives for finishing and packaging; and (vi) an apex organization for federated marketing. BAIF acted as a resource and technology sourcing agency, introduced streamlined systems, provided managerial backup services, and facilitated credit and market linkages. The two major products where producers took control of the full commodity chain were mangoes and cashews. In the case of mangoes, procurement and grading alone added 20% value. In a second step, the raw mangoes are cut into pieces and semi-pickled at village level, which are then brought to the final pickling stage by cooperatives, where they packaged and forwarded to a Producer Company for federated marketing. Value addition through processing contributed substantially to a sustainable increase in employment and income.

In a multi-country evaluation of NGO programmes with financial and non-financial services in francophone West Africa, it was found that great care has to be taken on how financial and non-financial services are linked. Among the non-financial services were literacy training, group formation, organizational assistance, empowerment assistance, information dissemination, and skill training. Some NGOs had carried out both types of services themselves, some had created external MFIs, some had transferred the execution of financial services to existing MFIs. However, some similar weaknesses were found in most of the models:Social and business orientations were rarely separated, and/or the transformation from a socially oriented to a business-oriented design of the financial programmes proved to be very difficult and lengthy. MFI membership and credit approval was at least partially directed towards (former) beneficiaries of NGO programmes. Credit from donor resources, with strings attached, was frequently used to push technologies selected by the donor, which turned out to be inappropriate and restrictive of innovative indigenous entrepreneurship. All this led to inefficiencies, misallocations of funds, inappropriate groups (eg, entrepreneurship organized around literacy or health training, groups not based on solidarity ties) and an overall lack of sustainability. Credit offered on soft terms was found to undermine the sustainability of MFIs. Many NGOs were found that depended on continual donor funding; typically, they were neither self-managed nor member-controlled. On the other hand, it appeared that many MFIs newly created with the help of NGOs were inclined to be ruled by a minority of better-off members which sought to get large amounts of credit at the detriment of weaker members. Among the conclusions drawn and lessons learned were: Non-financial services and commercial financial services must be institutionally separated; autonomy of MFIs in credit decisions are crucial; MFIs must diversify their portfolio in terms of clients, crops and sectors – including producers, processors and traders among their customers and not just one of these; service providers must take great care in assuring good practices; MFIs should be very careful in financing agricultural innovations pushed by well-meaning NGOs or other donors; new member-based MFIs need guidance for *good practice* and effective supervision ; and, last but not least, institutional development takes a long time.

4. Constraints and challenges of physical commodity infrastructure

The physical commodity infrastructure, or the lack thereof, presents constraints and challenges not only to the commodity sector, but equally to the financial sector, on two accounts: as a prerequisite to commodity production, processing and trade; and as a field of financing. Three examples are given, to which this applies: warehousing and storage, transportation, and packaging.

Security is a key issue in the context of warehousing. Security can be described in two different ways – (i) security against loss or damage of goods and; (ii) security for banks making loans. Warehouses have a key role to play in both contexts. In the case of (i) above, warehouses protect against natural risks such as adverse weather, theft and fraud. In the context of financing structures - (ii) above - warehouses play a key role in ascertaining who has title to the goods and who can take possession of them. In commodity trade finance transactions, the “taking of security” is a key element of financing the transaction and this is where the goods held in a warehouse are pledged to a lender. However, for the bank to be comfortable with making a loan, it has to ensure the warehouse is reliable. This means the warehouse operator must have a good reputation and be reliable. He must be solvent and have adequate working capital to support the operations and services being provided. There is a role for micro-finance institutions to ensure that the warehouses used for transactions are dependable. In some instances they could even regulate warehouses so that farmers or farmers’ groups could deliver stocks and have warehouse receipts issued against those stocks that could then be financed. The fact is that lenders may have concerns as to whether commodities they lend against are actually held in the warehouse. Therefore, the scrutiny of warehouse operators and assessment of storage conditions and suitability is an invaluable development in the creation of micro and meso finance structures.

Participants pointed out that warehouse receipts are a mechanism of creating bankable collateral and play a lending risk mitigation role. Through deferred sales, it is also a mechanism of value addition. Underdeveloped and underrated almost everywhere in Africa and the Near East, it has been of great importance to the development of agriculture in some countries, most notably among them the United States. Warehousing is as much a storage facility for commodities as a financial institution, supervised in some countries (eg, in Latin America) by the bank superintendency. Its focus is on risk management, which benefits both those who put commodities into consignment and the financial institution accepting these commodities as collateral. Security is a key issue that must be adequately resolved. An unresolved issue in developing countries is who should organize the due diligence examinations, work out prudential regulation, supervise warehouses, and rigidly enforce the regulation. This is a great challenge CFC is confronting in several eastern and southern African countries through its support for a project. The question was raised whether in any of these countries micro and meso finance institutions have the competence and clout to carry out, or initiate, such a task. Commercial banks, the central bank and perhaps associations in the commodity sector may be more appropriate agencies, but would require massive capacity building first. Participants suggested to examine the feasibility of cooperative ownership.

Cost and availability of transportation are key determinants of the effectiveness and competitiveness of the commodity sector. Sudan is one of many developing countries with serious transportation problems. Processed and unprocessed goods both compete for the service, in a vast country with a widely dispersed population. This raises issues of the economics of plant location, a nonexisting discipline in Sudan. River freight would be the cheapest, but stopped in 1983 with the onset of the civil war. Rail is the next-cheapest, at 45% of road transport, but is down to 20% of capacity utilization and has deteriorated to the limits of being of any practical use. Air freight is practically almost nonexistent: there is no internal freight services; international flights are irregular; there is no cooling storage facility at the airport; and the loss ratio is high. Remains road transport, segmented into transportation by small, medium and large trucks. Of these, only small trucks are of any significance; and there is considerable competition in that sector. Lowering the cost of transportation from farm gate to market is a major policy objective. Incentives for investments in road transportation by trucks include the elimination of road taxes, a reduction in import taxes, and an income tax reduction. A contrasting case is India, also a vast country. Taking one single commodity as an example: 100 million tons of sugar cane are crushed annually in India. Of these, 70 million tons are transported by the farmers, either individually or through cooperatives:, constituting a major portion of value added.

Packaging of agricultural products is a major value-adding process if rigorously submitted to standards and quality assurance. As a *silent salesman*, packaging constitutes a key link between producers and markets and comprises a coordinated system for production, distribution, marketing and consumer satisfaction. It provides three *P* functions to any product: preservation, protection and presentation. Adherence to international standards under ISO 9000, comprising a quality spectrum of 20 aspects, have greatly contributed to acceptance by customers and and to exportation in India. Under pressure from major importing countries, India is a country where the introduction, propagation and supervision of standards is professionally handled: much to the advantage of the commodity sector as well as the consumers. Here standardization and quality assurance at satisfactory levels at reasonable costs (and not at optimal level at exorbitant costs) have led to higher sales and more profit to the producer; they have eased trade and have provided better value to the consumer. Major product groups where packaging is submitted to standards and contributes to value added are cereals (particularly rice, whet and barley), pulses, oil seeds, tea, coffee, spices and some horticultural products such as flowers, fruits and vegetables. Most of them are further converted into processed food items by industries submitted to standards. These include the basic food industry (rice, sugar and pulse mills), the processed food industry and the industry dealing with fresh fruits, vegetables and cut flowers. Key terms in packaging as the material dimension of standards and quality assurance are diversification, quality, standardization and value-addition. Groups, associations, networks and linkages are key concepts in organizing the dissemination of standards.

5. The experience of banks in finance for small and micro enterprises in commodity production, processing and trade

Union Bank of Nigeria is a private national commercial bank with a diversified portfolio. Its agricultural credit department has succeeded in moving from losses to profits in rural and agricultural finance. It found chain financing a key concept in profitable agricultural lending, assuring that there is an uninterrupted link between production, processing, trade and exportation. The Bank finances production technologies and improved varieties developed by research institutions such as the IITA as well as farming implements, pesticides, herbicides and fertilizer. It provides microcredit to microenterprises in the first processing stage and meso-credit ranging from US$3,500 to 35,000 to small- and medium-scale processors. The Bank has gone through a long learning experience. In 1978, it was submitted by the central bank to mandatory lending to agriculture in the framework of a national agricultural credit guarantee scheme, ACGSF. Not surprisingly, under these terms farmers viewed the scheme as distribution of the national cake, with pieces for everyone. Default rates were high, and the commercial banks pulled out of agricultural lending – except Union Bank, which came up with a new scheme. Similar to GTZ's and AFRACA's approach *Linking Banks and Self-Help Groups* promoted in Nigeria by the central bank, farmers were required as of 1988 to organize in groups and save regularly for periods of six to twelve months to become eligible for a loan. Recovery went up to a level where agricultural lending became profitable to the bank. During 2003-04, the Bank expects to disburse N 1.5 billion (US$ 10 million) under this scheme. There is the story of one farmer who borrowed N 10,000 in 1989 and recently received a loan of N 300 million. The Bank is now developing a new market-driven lending strategy, with a focus on processors as a highly profitable market segment. At the same time, the Bank is getting into a new scheme for remote areas, *Global Limit for Farmers (GLF)*: farmers have to come up with a 25% savings up-front as collateral; they continue saving after disbursement; thereby they increase their deposits as well as the size of their next loan. However, coming up with savings does not confer a right to a loan; all applications are duly appraised: a prerequisite to any type of lending.

The Agricultural Bank of Sudan has experienced, time and again, that lending to agriculture only, without adequate portfolio diversification, can be very risky. In 1977, it first responded to the request for seasonal production loans by farmers who had formed two primary credit and marketing cooperatives. The Bank designed a supervised credit program, with credit to cooperatives, partlyas meso-credit to be invested in cooperative enterprises to be retailed by the cooperatives as micro-credit to their members. Between 1977 and 1984, the number of cooperative customers increased to 48; repayment rates where reportedly in the range of 90% to 100%. However, the drought of 1983-84 led to the decline of agriculture and the closure of the program. Nevertheless, the scheme was revived in later years and, with support by the World Bank and IFAD, expanded to eleven branches in Western Sudan. The Bank concludes that group lending can help in overcoming problems of outreach, transaction costs, lack of collateral and deposit mobilization. It is perhaps the most suitable approach to rural finance in Sudan, provided it originates from the farmers felt needs and own initiatives. However, lending decisions must be based on strict feasibility assessments and profitability, not on social considerations. To insure sustainability, credit must be granted on real banking terms without undue subsidization, says the Bank.

Centenary Rural Development Bank is a small commercial bank of national outreach in Uganda, which has turned micro and meso-finance in highly profitable business. Its exclusive approach is individual lending and deposit mobilization; the group approach is practiced by other institutions in Uganda, such as Commercial Microfinance Ltd. (CMF). In rural and peri-urban areas, Centenary RDB provides deposit, credit and money transfer services indiscriminately to men and women of lower income. Since 1998, its branch in Mbale has specialized on agricultural and agro-ecological lending, testing its feasibility before it is now gradually, and carefully, expanded to the other branches. During the experimental phase, arrears in that branch have oscillated from a low of 1.1% in August 2001 to a high of 7.0% in November 2001 and fell to 3.2% in July 2002; only a fraction of that is to be written off as bad debts: certainly an excellent performance. How has the Bank accomplished this? By insisting on loan recovery and cost coverage, it has reached more customers in rural areas than any other institution in Uganda. With minimum deposits of $5 and minimum loans of $58, access barriers are low. 73% of its deposits and 82% of its loans are in rural areas. Established by the Catholic Church of Uganda as a trust fund in 1983, it developed a strength in savings mobilization but performed poorly as a financial intermediary. In 1990, the political will to reform the fund evolved in the board, resulting in the fund's transformation into a commercial bank in 1993. With donor support, the Bank introduced a highly effective individual lending technology based on the analysis of total household activities; an incentives-driven repeat loan system; flexible but comprehensive loan security requirements; and stringent enforcement of timely repayment. This is backed by a system of computerized daily loan tracking, instant recovery action, and staff performance incentives with an emphasis on portfolio quality rather than productivity. This has made the bank the African flagship of rural and agricultural banking,[2] combining sustainability with outreach to the rural poor and demonstrating the feasibility of agricultural lending. By Dec. 2002, total assets amounted to $61.3m, total deposits to $48.7m (316,650 depositors), and loans outstanding to $23.05m (31,500 borrowers). The Bank earned 4% on average assets and 27% on average equity. During 2002, the bank has started to overcome its quality-vs.-productivity dilemma: (i) shifting incentives from repayment towards disbursement; and (ii) adding mesofinance for small and medium entrepreneurs, while microentrepreneurs, without mission drift, continue to constitute 99% of its borrowers. This move has substantially contributed to both, the bank's sustainability and its outreach to the poor.

6. The experience of other financial institutions and of regional agricultural credit associations

In the Gambia, microfinance is still in its infancy. The sector comprises 16 retail MFIs, 7 refinancing agencies, 6 training and promoting agencies and the Gambia Microfinance Network (GAMFINET), which provides capacity building and coordination services. The existing MFIs have been initiated and capitalized by donors. Lacking capital of their own, their overall orientation tends to be social rather than commercial, which has curtailed their growth. The main services of MFIs are credit, which is now being expanded to comprise not only loans income-generating activities but also consumer loans, and savings, comprising compulsory and voluntary savings, group and individual savings. At 90-95%, repayment rates are considered satisfactory. The MFIs reach about 200,000 clients, mainly the rural and urban poor. 70% of them are women, who are traditionally responsible for the processing and preservation of food. Food processing is carried out at the house in a rather rudimentary way and is not part of any of the existing agricultural development projects. MFIs finance equipment for the processing of raw groundnuts into flour, parched groundnuts into butter, cassava, vegetables, meat and fish. Loans in the meso-credit range exist, eg, for rice mills, but are rare. This business has being undermined by government and donor practices to provide such machines to communities on a grant basis. This turned out to be not viable because of a lack of ownership and political interference, which means that benefits ended up in the pockets of a few. Other constraints include a shortage of loanable funds and an overall lack of support to micro and small enterprises. It is suggested to the CFC to support associations of commodity producers, processors and traders and to establish a refinancing facilities for this sector. Participants questioned the need for donor funding, given the excess liquidity in the banking sector. They also pointed out that there is a strong demand for savings deposit facilities, as evidenced by the large number of self-financed informal financial institution all over West Africa, comprising rotating and non-rotating savings and credit associations as well as private deposit collectors. In contrast to such informal institutions, there are credit NGOs which are

[2] Recently published as: Centenary Rural Development Bank, Uganda: A Flagship of Rural Bank Reform in Africa. In: *Small Enterprise Development*, vol. 14 no. 3 (Sept. 2003, pp. 35-46.

doing poorly and being kept alive by donors, while some others are doing reasonably well but still are not put on their own feet by their parent organization.

In Benin, agricultural processing (with the exception of cotton) used to be financed by an agricultural development bank, CNCA, through regional and local cooperatives. In the context of a general banking crisis, 1986-88, the CNCA collapsed. Subsequently, the financial cooperative sector was reorganized, and numerous new MFIs emerged with donor assistance. The sector now comprises a total of 1,192 MFIs with a total of 435,000 members or clients, 89% in the cooperative network FECECAM. Most loans are short-term, up to 12 months, with an emphasis on the financing of working capital, including agricultural processing and trade. There is also some medium-term meso-finance available, albeit on a limited scale. Processing is largely in the hands of women, who may obtain credit either as individuals or through solidarity groups. A new institutional development, since 1998, has been the establishment of 144 equity-driven MFIs at village level, referred to as Financial Service Associations (FSAs; *ASF* in French). Like cooperatives, they are self-financed; unlike cooperatives, which are savings-driven, their sole source of loanable funds are multiple shares and retained earnings. While cooperatives adhere to terms and conditions defined by FECECAM, each FSA, with an average of 350 shareholder-members, is fully autonomous including the determination of interest rates: the source of dynamic growth of funds. The FSAs have been supported in Benin by IFAD through two projects which at the same time promote the establishment of groups of women engaged in agricultural processing, particularly of cassava, palm oil and fruit juice. FSAs provide two types of loans for processing: short-term loans to individual shareholder-members (starting as low as US$18) or to solidarity groups of women too poor to acquire shares at their own; and medium-term loans to groups of women engaged in the establishment of a joint processing facility. Such a medium-term loan product is rare among MFIs and is more the result of simultaneous donor support to FSAs and groups of processors than of the independent decision of each FSA. Beyond the pilot phase, which is under evaluation, it will be up to each FSA to decide whether or not, and under which terms and conditions, to continue with the two loan products. The FSAs are presently in the process of establishing an association, which will also decide how to separate financial and non-financial services.

In Syria, a network of village-based MFI has emerged since 2000, which are self-financed from equity and self-managed. These so-called *sanadiq* (sg.: *sanduq*), based on ancient Arab traditions, are member-owned local financial institutions in a command economy where all banks have been state-owned. With a mixture of member-equity and external equity contributions, the sanadiq have been shaped in their structure and functioning by the local people in Jabal al-Hoss, one of the poorest areas of Syria, through an intense participatory process. Support has come from the Ministry of Agriculture and Agrarian Reform and from UNDP. Through self-help as the basic principle, cost-coverage and profitability have been attained by the sanadiq within their first year of operation. In a national situation of incipient liberalization, self-reliance and local initiative, together with an excellent performance record, have earned the Sanadiq national visibility in government and donor circles. The start-up of a sanduq is self-financed through member share capital, from which small loans are given for up to three months. Whenever initial financial intermediation is satisfactory, UNDP provides an additional capital injection, thereby increasing outreach, loan sizes and loan periods. Between September 2000 and December 2002, 22 sanadiq were established, with close to 5000 members. Loans permit farmers to bypass trader-moneylenders and sell their produce at a higher price; laborers turn into farmers; and microentrepreneurs use quick-turnover repeat loans for new investments and rapid business growth. Special attention is given to women, most of them illiterate. They opted for integrated sanadiq, in which female members participate in management committees. They find access to loans easy, as sanadiq do not require physical collateral. Loans are used by younger and older women to do business of their own, eg, fattening sheep, raising cows, opening small shops and renting land to plant cash crops. They are now learning to focus on high-yielding activities outside traditional agriculture. In 2002 first steps were taken towards the establishment of a network which will provide apex services and initiate the dialog on a legal framework; and of a central fund. There are plans for extending such networks throughout Syria as a strategy for rural development, poverty alleviation and employment generation.

Networks and associations have an important role to play in promoting capacity building among their member institutions, in the dissemination of tested financial strategies and products, and in policy dialogue, particularly concerning the legal framework, prudential regulation, and the direct or delegated supervision of MFIs. Three networks and associations were presented: the African Microfinance Network (AFMIN) In Abidjan, established in 2000, which comprises 17 member networks with 500 MFIs; the Near East-North Africa Regional Agricultural Credit Association (NENARACA) in Amman, an association of 25 member institutions, mostly agricultural banks, from 16 countries; and the African Rural and Agricultural Credit Association (AFRACA), with 61 members, composed of commercial banks, agricultural development banks, co-operative banks and major MFIs. AFMIN emphasized the importance of capacity building of national networks of MFIs. NENARACA stressed the urgent need for reforming agricultural development banks as the main providers of rural financial services throughout the region, which in the future may include wholesale credit to MFIs on an increasing scale. AFRACA presented the major roles of the RACAs, comprising policy development and advocacy, capacity-building of the association and member institutions, dissemination of good practices, innovative product development, and partnerships with other organizations for the promotion of income-generating activities including processing in the commodity sector. FAO, IFAD and GTZ have been the major donors of the RACAs (including APRACA for Asia and the Pacific). There was agreement among the participants that networks and associations can be powerful partners for the CFC in the promotion of investment and financing opportunities along the commodity chain, particularly in the spheres of micro and meso finance.

7. Opportunities, Options and Recommended Course of Action

Financing strategies for processors, producers and traders have been developed in Cameroon over a period of almost 20 years by an institution which has evolved from an unsustainable project, the Gatsby Root Crops Project, 1985-93, to a sustainable financial institution, the Cameroon Gatsby Trust (CGT) as of 1994. During an initial phase, the project focused on the solution of commodity production problems by developing and disseminating improved technologies for cassava, yam and sweet potatoes. During the second phase, the project continued multiplying and disseminating improved varieties of root crops and provided at the same time microcredit to the producers. This led to the establishment of a financial institution, the CGT, and a third phase characterized by the switch from individual to group lending, comprising microcredit through solidarity groups and mesocredit to associations of small groups (at a satisfactory repayment rate of 96.5%). This also marked the cultivation of a most remarkable approach: building on pre-existing indigenous self-help groups including rotating and non-rotating savings and credit associations, which are ubiquitous in Cameroon and neighboring countries. A fourth phase started in 2003 by adding a range of nonfinancial services, comprising skill training in such fields as soap-making and tie-dye making, food conservation and tuber multiplication; group and association management training; financial management; and facilitation of local and regional trade fair participation. The trade mark of CGT is now the combination of financial services with business development services, for three major market segments in the commodity sector: producers, comprising yam, coco yam, sweet potatoe, plantain, corn and cassava farmers as well as livestock farmers; processors, particularly cassava processing and textile processing; and traders in food, handicrafts, textiles and livestock. The CGT approach constitutes an option in which, in the framework of an integrated approach of financial and non-financial services, special emphasis is placed on (i) group and association formation on the basis of pre-existing indigenous group structures, (ii) internal financial intermediation based on savings, (iii) their upgrading to sustainable formal organizations, (iv) access to refinancing by CGT, (v) networking among associations, and (vi) linkages of associations with other institutions.

Strategies for financial institutions and their products must focus on sustainable financial institutions with sustainable financial services, combining credit with savings as a service to customers and as a source of loanable funds, thus moving away from *credit-only* provided through projects and programs. Workshop participants from such sustainable institutions have stressed that any MFI, bank or microbank striving for sustainability must do the following:

(1) mobilize their own resources,
(2) apply appropriate lending technologies,
(3) provide attractive loan products
(4) with appropriate interest rates,
(5) have their loans repaid,
(6) manage their risks,
(7) make a profit,
(8) finance the growth of outreach from the growth of savings and profits,
(9) operate in a conducive policy and legal environment.

The most important conclusion of this Workshop is that, evidence to contrary in the old world of development finance notwithstanding, sustainable MFIs, microbanks and AgDBs in the new world of development finance, with appropriate risk management technologies, are able to lend to the agricultural sector including producers, processors and traders at low default rates and high profits. The number of such institutions has substantially increased in recent years: in all ownership categories, including government-owned banks, private and community-based rural banks, and various types of MFIs. Networks and associations of MFIs and banks – like AFMIN, AFRACA, APRACA and NENARACA – have a crucial role to play in disseminating the positive experience and developing support strategies in cooperation with government and donor agencies such as the CFC.

Many donors pursue objectives of poverty alleviation, the improvement of income and income-generating activities in rural and urban areas, and the promotion of financial services to the poor. Among these, the Capital Development Fund of UNDP (UNCDF), through its Special Unit for Microfinance (SUM), is mandated to contribute to the reduction of poverty alleviation and the achievement of the Millennium Development Goals in 2015 by ensuring permanent access to sustainable financial services for a majority of poor and low-income households. Initially, UNCDF supported selected MFIs financially through equity grants and soft loans and technically through capacity building and policy advice, using MicroStart as its signature product. It now follows a new dual strategy: supporting the development of self-sustaining microfinance sectors including policy and legal frameworks; and strengthening the capacity of the UNDP system to apply sound microfinance principles in its programming. It is guided by three operating principles: developing the microfinance industry as part of the formal financial sector to achieve a lasting impact on poverty reduction; the translation of a shared vision among all stakeholders into national policies and collaborative strategies; and an emphasis on product designs and delivery systems that support expanded and permanent access to financial services by women. UNCDF propagates three guiding principles of microfinance sector development, which are, or should be, shared by donors: (i) focusing on coordination and the promotion of the microfinance sector as a whole rather than individual donor projects; (ii) influencing the policy environment through concerted donor/government action instead of seeing it as an external risk; (iii) promoting policy change to increase the speed of development of the sector. Sharpening the focus of such operating and guiding principles on the commodity sector may be a task for the Common Fund for Commodities.