RETHINKING TECHNICAL ASSISTANCE TO UNLOCK SMALLHOLDER FINANCING

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The gap between demand for and supply of financing for smallholder farmers in the developing world is estimated at over $400 billion. Agricultural technical assistance, when provided effectively, can address many of the constraints to the expansion of smallholder financing.

Financial services and advisory support programs can help banks and financial institutions (on the supply side) overcome constraints of product design and distribution for smallholder farmers. Technical assistance can prepare farmers (on the demand side) for financing through value chain development programs or government extension programs. Public sector institutional strengthening programs can address constraints in the enabling environment by increasing effectiveness of government institutions or supporting credit bureaus or land title reform.

Combined with financial tools from donors—such as credit guarantees, insurance, or concessionary lending to local credit providers—agricultural technical assistance plays an important role in mitigating risk and boosting confidence for financial institutions involved in smallholder financing. However, 97% of technical assistance funding currently goes to programs that address demand side constraints, while relatively little funding supports financial institutions to develop and deploy viable products that will increase the overall supply of smallholder financing.

To expand financing for smallholder farmers, we believe three key activities need to happen in the agricultural technical assistance market:

i) Donors should direct more funding to supply side technical assistance that supports financial institutions to develop and deploy viable products for smallholders.

ii) Financial institutions and providers of financial advisory technical assistance should establish consortiums (possibly supported by donors) that share evidence and lessons learned across institutional boundaries to learn approaches and establish best practices for smallholder financing.

iii) Technical assistance providers and donors should coordinate across the supply side and demand side to share perspectives and deploy financial tools and technical assistance that simultaneously addresses multiple constraints across specific crop and country markets, including enabling environment constraints. They should also coordinate these approaches with downstream value chain buyers and agro-businesses.

ABOUT THIS BRIEFING

This Initiative for Smallholder Finance briefing is the eighth in a series about catalyzing smallholder finance. It discusses agricultural technical assistance in the developing world and its linkages to financing constraints for smallholder farmers.

This briefing builds on information presented in a previous briefing titled, Technical Assistance for Smallholder Farmers: An Anatomy of the Market.
Agricultural technical assistance, when provided appropriately, can address many of the constraints to the expansion of smallholder financing.

The total amount of debt financing that local banks supply to smallholder farmers in the developing world meets less than 3% of total demand. As discussed in a previous briefing note on local bank financing for smallholder farmers, a series of constraints hinder the expansion of access to finance for smallholder farmers. Although they vary by market, common constraints include:

- **Supply side constraints (for financial institutions).** Creating a smallholder financing program requires large upfront investments in staff skills, technology, and back-office processes. Banks need specific agricultural expertise to assess smallholder loans and design appropriate products.

- **Demand side constraints (for smallholder farmers).** Low margins, variable cash flow, and limited collateral make it difficult for smallholders to service typical bank loans. Furthermore, limited penetration of producer organizations or integration into structured value chains makes it difficult for financial institutions to reach farmers through standard bank distribution channels. Finally, it is challenging for banks to assess smallholder farmers’ creditworthiness due to low financial literacy and financial management skills among farmers.

- **Enabling environment constraints.** Land titles are often not available for collateralization and a lack of credit bureaus makes it difficult for banks to assess smallholder farmers’ creditworthiness.

Technical assistance can resolve a range of these constraints to smallholder financing on both the supply and demand sides, as well as those created by the regulatory environment. In our previous briefing note, we introduced a range of different types of technical assistance programs in the market. Each of these programs maps to a different set of constraints (see Figure 1). For example, supply side constraints in designing and
rolling out products that financiers provide to farmers can be addressed through financial services advisory and support programs. Demand side constraints can be tackled through government extension programs, as well as a variety of forms of corporate-sponsored or non-governmental technical assistance that support smallholders. Public sector institutional strengthening programs can address constraints in the enabling environment by increasing effectiveness of government institutions or supporting credit bureaus or land title reform.

A comparison of technical assistance funding deployed towards addressing supply side constraints versus demand side constraints reveals a strong skew towards the demand side. The Initiative for Smallholder Finance’s analysis of the agricultural technical assistance market identified a handful of supply side technical assistance providers and a market for services worth an estimated $25-35 million. This figure is only 3% of the $1.1 billion in donor funded agricultural technical assistance that primarily goes to demand side support (see Figure 2), not to mention the $5 to $9 billion from government extension programs.

To be clear, both agronomic farming skills and financial/business management skills fall under demand side support. Still, $25 to $30 million in supply side technical assistance is a small amount to be spread across the 290 banks globally that currently offer products for smallholder farmers and barely scratch the surface of the global demand for financing.

To put this supply side figure in perspective, consider that a commercial bank may spend tens of millions of dollars setting up and furnishing a single retail branch. The cost of one retail branch is nearly equivalent to the total funding for supply side agricultural technical assistance in all developing countries. This disparity suggests a severe underinvestment in the allocation of donor funding to supply side support for smallholder financing.

Furthermore, the level of competition among supply side technical assistance providers is low; only about 20 providers offer supply side support, compared with hundreds of providers that offer demand side support. These supply side providers include 8 to 10 specialized providers (e.g., Horus Development Finance, Grameen Credit Agricole, ShoreBank International, or Making Cents) typically contracted directly by financial institutions or by donor-funded agricultural development programs that have smallholder financing components. An additional 4 to 5 generalist providers (e.g., TechnoServe, ACDI/VOCA, or Fintrac) incorporate financial service advisory into larger value chain development programs they deliver for donors. Finally, 4

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**Figure 2: Technical assistance funding that addresses supply side constraints versus demand side constraints**

<table>
<thead>
<tr>
<th>State of smallholder financing</th>
<th>Agricultural technical assistance funding in relation to resolving smallholder financing constraints</th>
</tr>
</thead>
<tbody>
<tr>
<td>Supply from banks</td>
<td>Addressing supply side constraints for financial institutions</td>
</tr>
<tr>
<td>Gap</td>
<td>$25-35 million</td>
</tr>
<tr>
<td>Demand from smallholders</td>
<td>Addressing demand constraints for smallholders</td>
</tr>
<tr>
<td>$10-20 billion</td>
<td>$1 billion</td>
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**Despite the extreme lack of smallholder financing supply, the vast majority of technical assistance goes toward addressing the quality of demand**

Note: The chart compares funding addressing supply and demand, and does not include the funding for institutional programs that address the enabling environment; It also excludes government extension

to 5 corporate finance consulting firms (e.g., Deloitte, Pricewaterhouse Coopers, and Ernst & Young) offer services to commercial banks looking to move down-market.

As a result of difficult market entry and scarcity of funding on the supply side, often it is a push from donor advocacy organizations or governments, rather than a request from financial institutions, that gets many providers involved. External experts with both agriculture and banking expertise are hard to find and typically expensive; even practitioners at leading banks with smallholder financing programs are still figuring out how to do smallholder financing well. Until there is a clearer path for financial institutions to get involved in smallholder financing, donors will need to fund technical assistance providers. Supply side technical assistance providers and financial institutions can expedite the expansion of best practices in smallholder financing, however, by improving their coordination and by sharing lessons with each other more frequently (see Box 1).

An optimal approach to unlocking smallholder financing will combine financial tools—such as credit guarantees, insurance and concessory lending to local credit suppliers—with technical assistance that simultaneously addresses constraints on the demand side and the supply side in a given market (see case studies). Preparing smallholders for funding is useless if no financial institutions offer appropriate lending products. Similarly, there is no use in pouring time and resources into product design when farmers do not have adequate financial management skills or viable access points to financial institutions. On the financial institution side, guarantees, insurance, or concessional lending alone will not address the limited agricultural knowledge of bankers; nor will an agriculture lending mandate from the local government. In fact, providing an incentive for a financial institution to increase exposure to smallholder farmers without helping the institution design appropriate agricultural products and credit assessment mechanisms can encourage irresponsible lending in the agricultural sector and may ultimately lead to overextended farmers and higher default rates.

Approaches to smallholder financing will be even more effective if downstream buyers and agro-businesses participate. Incorporating a full value chain perspective and working with downstream actors has several benefits: i) it provides clarity on volumes and pricing at the end market smallholders are selling into, ii) financial

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**BOX 1: AGRIFIN – AGRICULTURAL FINANCE SUPPORT FACILITY**

AgriFin is an initiative that aims to strengthen the ability of financial institutions to deliver agricultural finance for farmers and agro-enterprises in developing countries. The Bill and Melinda Gates Foundation supports AgriFin, while the World Bank manages it. The initiative is facilitating knowledge sharing and networking among practitioners by organizing a range of events for peer-to-peer learning, facilitating production and dissemination of knowledge products and tools, and creating a global web-based platform to connect agricultural finance practitioners. To date, over 500 institutions primarily in developing countries have exchanged experiences on agricultural financing through the AgriFin network.

*Source: AgriFin*

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**CASE STUDY: EQUITY BANK IN KENYA**

Equity Bank in Kenya provides loans to farmers with little or no collateral through the “Kilimo Biashra” program, which aims to serve 2.5 million farmers. To reduce risk, the Alliance for a Green Revolution in Africa (AGRA) and the International Fund for Agricultural Development (IFAD) provided an incentive in the form of a 10% first loss guarantee to Equity Bank. Meanwhile, the government extension program provides financial literacy and farm management training to farmers. The integration of farmers into supply chains, including via an agreement with the World Food Program, also helps reduce risk.

*Source: IFC, “Innovative Agricultural SME Finance Models,” 2012*

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**CASE STUDY: ZANACO BANK IN ZAMBIA**

Zanaco, one of the leading banks in Zambia, launched a program in 2009 to provide financing and technical assistance to emergent farm businesses. IFC and Rabo Development funded the supply side technical assistance to Zanaco, including agricultural credit skills and farm performance monitoring training for bank staff. External specialists support individual farmers with loan applications and business plans. Agricultural input suppliers and end-buyers are also involved, including the Omnia fertilizer company, Parmalat, Afgri, and Zamace (the local commodity exchange). The commercially driven nature of the partnership facilitates involvement and coordination among all actors.

*Source: IFC, “Innovative Agricultural SME Finance Models,” 2012*
institutions can use buyer relationships and value chain transparency to better assess and manage risk, and iii) in some cases, downstream actors may be willing to offer, support, or even subsidize technical assistance for farmers as a strategic action to strengthen sourcing relationships.

To improve the efficacy of technical assistance that promotes smallholder financing, we believe that three key activities need to happen in the agricultural technical assistance market:

i) Donors should direct more funding to supply side technical assistance that supports financial institutions to develop and deploy viable products for smallholders.

ii) Financial institutions and providers of financial advisory technical assistance should establish consortia (possibly supported by donors) that share evidence and knowledge across institutional boundaries to learn approaches and establish best practices for smallholder financing.

iii) Technical assistance providers and donors should coordinate across the supply side and demand side to share perspectives and deploy financial tools and technical assistance that simultaneously addresses multiple constraints across specific crop and country markets, including enabling environment constraints. They should also coordinate these approaches with downstream value chain buyers and agro-businesses.

Technical assistance, deployed effectively in coordination with other financial tools, plays an important and complementary role in unlocking financing for smallholder farmers.

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**NOTES**


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**SCOPE AND METHODOLOGY OF THIS STUDY**

The findings in this briefing note form part of a broader effort by the Initiative for Smallholder Finance and Dalberg to understand the agricultural technical assistance landscape and its impact on smallholder financing. First, this research placed technical assistance in the agricultural development landscape by determining how much is spent on technical assistance programming within the context of overall agricultural development spending and how funding of technical assistance is evolving. The team did so through a predominantly top-down analysis of spending trends with some literature and portfolio analysis including: i) a literature review of past research on technical assistance, ii) review of previous studies and World Bank global data on government agricultural and technical assistance spend, iii) analysis of bilateral and multilateral spending based on program data in creditor reporting system databases, iv) a portfolio review of the Bill and Melinda Gates Foundation’s agricultural portfolio, and v) interviews with four donors and other industry experts to identify funding trends.

Second, this research effort sought to understand how agricultural technical assistance is designed and delivered across the world, including how providers differentiate themselves and how technical assistance programs are funded. To do so, the team used a predominantly bottom-up review of programs and providers with some top-down sizing and country context analysis that included i) development of a database of key funders, providers, and other relevant organizations, ii) detailed organizational profiling of over 50 providers and funders, iii) desk review of about 50 technical assistance programs across program types, iv) interviews with 21 providers and other experts, and v) desk research into country contexts and country case studies.

Finally, this research sought to identify how technical assistance can better enable smallholder financing. The team conducted a narrow, deep-dive review of provider approaches and perceptions to do this, including i) analysis of technical assistance links to drivers of smallholder financing, ii) desk review of 6-7 provider programs and M&E systems and measurement tools, and iii) targeted interviews with five providers to explore approaches to efficacy.

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**RESEARCH BY**

Dalberg Global Development Advisors is a strategy and policy advisory firm dedicated to global development. Dalberg’s mission is to mobilize effective responses to the world’s most pressing issues. Dalberg works with corporations, foundations, NGOs, and governments to design policies, programs, and partnerships to serve needs and capture opportunities in frontier and emerging markets.
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ABOUT THE INITIATIVE FOR SMALLHOLDER FINANCE

The Initiative for Smallholder Finance is a multi-donor initiative hosted by the Global Development Incubator to build research and development infrastructure in the smallholder finance industry and make progress toward filling the gap in financing through targeted product development, piloting, and partnerships.

For the original report that led to the creation of the Initiative for Smallholder Finance, see “Catalyzing Smallholder Agricultural Finance” (2012).

AUTHORS:

This study was authored by Dan Zook from the Global Development Incubator, with input and support from Angela Hansen, Matt Shakhovskoy, Rezvan Ma’ani, and Rasesh Mohan from Dalberg Global Development Advisors. Sara Wallace provided editorial and design support.

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