



Change with Innovations

Rural Finance Knowledge Management Partnership (KMP)

Experiences from East and Southern Africa- ESA



Value chain design for food security

The value chain approach and value chain financing are new in the eastern and southern Africa region. Value chains impact food security through improving farming and post-harvest practices, and by strengthening farmers' diversification strategies through on- and off-farm income-generating activities for improved household income.

Introduction

Many value chain interventions focus on supplying national and international markets. This often concerns commodity products, in many cases cash crops or products that do not meet local food needs. Smallholders, especially those operating at subsistence level, can have widely different priorities; their main concern is ensuring food security of their household. They seek continuous physical and economic access to sufficient food to meet their dietary needs; not just on the short run, or incidentally, but sustained for the future. Farmers do so through a range of on- and off-farm income diversification strategies,¹ which means that improved food security can be achieved either when farmers increase the quantity (and variety) of food they produce and consume themselves or increase the income they earn from selling products or services.

Value Chain Finance and Food Security

In value chain finance, financial service providers link with the chain by offering financial services that build on existing relationships in the chain. Banking on these business relations provides service providers with additional security that they will get a return on their investment. Thus, lowering risks makes financial service provision a more attractive business proposition and can lead to lower prices. For value chain interventions to improve local food security, two issues need to be tackled:

First, to distinguish themselves from regular microfinance schemes, which are often unavailable, unaffordable or unattractive to subsistence farmers, interventions need to overcome the lack of continuous buyer-seller relations in subsistence food production. Although farmers occasionally sell surpluses on local markets or buy production inputs, there are often no formal business relations to lower risks of financial service delivery.

Second, interventions need to strengthen diverse income-generating strategies of households, especially in terms of the diversity of crops they grow or livestock they keep, instead of overexposing subsistence farmers to additional risks of specific (commodity) markets (see Box 1).

Box 1: Barriers to smallholder participation in markets

- No capacity to achieve significant volumes.
- Lack of economies of scale reduces bargaining power of rural producers on the marketplace.
- African farmers are poorly linked with consumers, especially those in regional urban centres.
- Volatile food markets in Africa with strongly changing market conditions create wide price fluctuations.
- Inconsistent supply to markets.
- Lack of cost-effective logistics due to fragmented production by scattered farmer groups.

Smallholder Commercialization and Market Access Financing (MAC FIN) by Mr. Stanley Mwangi, Farm Concern International. KMP Workshop 2010, Lusaka, Zambia.²

A value chain approach to food security differentiates itself from microfinance approaches to food security by identifying causes of food insecurity. Such understanding allows designing sustainable solutions by using market forces. Moreover, a value chain approach facilitates market actors instead of providing services directly to beneficiaries. Value chain interventions can impact food security by 1) improving farming and post-harvest practices, and 2) by strengthening diversification strategies.³

First, value chain interventions can enhance food security by reducing (post-) harvest losses or increasing yields. Improvements in quality and quantity can be accomplished through training (e.g. improving techniques for sorting, grading or drying), often carried out by development actors directly, but preferably through local service providers. Other interventions include setting up local seed banks to provide improved seed, facilitating the provision of better fertilizer or pesticides, leasing oxen with modified ploughs that can be maintained locally. Furthermore, the introduction of drought-resistant crops can improve farmers' yields, especially if they implement improved water control systems that use the landscape's existing hydrology, such as training to plough along elevation lines.

KMP workshops have shown several examples of how such improvements can be achieved through sustainable and market-based approaches. First, taking a value chain approach enables practitioners to identify incentives and disincentives for sustainable behaviour from all players involved in the chain. In this way, they can ensure that opportunities and risks for all actors in the value chain are made transparent and can be managed. Second, practitioners can set up tripartite partnerships among financial service providers, farmers (organizations) and input and training suppliers, or establish community-based financial organizations to invest in improved farming practices.

Improving storage and post-harvest processing facilities can have significant impact on food security by reducing losses or making produce less perishable (Box 2). Such investments are often beyond the financial capacities of farmer organizations or community-based financial organizations. Joint ventures between

farmer organizations and private companies, and investments by microfinance institutions (MFIs), banks or private investors could prove a solution. However, a value chain approach to food security would need to have clear business proposition for these investors to step in.⁵ For example, rural finance practitioners can assist farmer organizations to develop business cases that are 'bankable' to financial service providers. Another option is to establish joint ventures with commercial enterprises to invest in improved post-harvest facilities.

Box 2: Adding value for local and national markets—processed fruits and vegetables

Syngenta Foundation finances value interventions in the fruits and vegetables sector in different African countries. These countries produce surplus fruits and vegetables, yet import large quantities of processed products outside of the harvest season as they lack adequate processing facilities. Processing produce adds value to products, reduces losses, generates employment and improves the diet of subsistence farmers.

Syngenta identified the following requirements to make interventions successful in improving food security:

- Successful local processing requires maximum utilization of equipment to achieve sufficient returns on investment. Ensuring that crops with different harvest times are produced throughout the year means a stable, local surplus of raw materials for processing.
- Demand needs for processed fruits and vegetables have to be analysed up front.
- A multi-stakeholder set up is necessary in order to ensure trust and commitment between chain actors and financial providers.
- The use of appropriate processing technologies to minimize capital expenditure and allow for maintenance locally, while complying with target market requirements.
- Structures that give farmers access to credit to buy better seed varieties and training on their proper use (improved quality / quantity) to achieve a sufficient scale of production.
- Risk sharing is needed: farmers need to be able and willing to take risks, financial service providers need to be confident of returns on investment, and processors need to be sure they invest in a profitable business.

As presented during the KMP Workshop Conference Paper in 2010⁴

A value chain approach to food security aims for a market-based approach that strengthens and diversifies the production of subsistence farmers. Crop diversification, in contrast to single crop production systems, is important to make farmers less vulnerable to market and weather-related shocks. Also, non-farm activities, such as food processing or trade, are important for local economies. In many cases, farmers view credit for off-farm activities as a priority compared with investing in their farms. Rural finance can provide credit for these activities as a strategy to mitigate risks for actions taken in the intervention which expose farmers to additional risks.⁶

Strengths and Weaknesses of VC interventions for Food Security

Strengths

Value chain interventions for food security can:

- **Identify incentives** for desired behaviour for producers and the private sector,⁷ such as incentives for the production and sale of nutritious food vis-a-vis less nutritious options, including consumer demand and production costs.
- **Identify disincentives** for sustainable behaviour, such as:
 - disincentives for private sector investments in food production and processing, for example, price controls that lower potential returns.
 - disincentives for producers to increase productivity and switch to more lucrative crops, such as inadequate market infrastructure or inappropriate subsidies.^{9,10}
- **Work towards sustainable solutions.** Value chain interventions identify underlying constraints and address these through sustainable local solutions by leveraging market forces to achieve long-term change.
- **Link farmers' households with growing local food markets,** ensuring additional income to secure their livelihood. Linking with local food markets can reduce the risks of relying solely on own production and can diversify diets.

Weaknesses

Value chain interventions tend to **focus on one or only a few crops.** Interventions focused on growing one specific crop run the risk of subsistence farmers not meeting their food needs when yields are too low or when market prices are under pressure. Value chain interventions should therefore aim to address the need to diversify crops, but also to develop off-farm activities that generate income.¹¹

Critical Success Factors

Improving food security not only means investing in on- and off-farm value chain improvements. Complementary interventions are often needed to make interventions successful.¹² KMP conferences provided many cases and lessons learned, and called for the following success factors to be taken into account:

- **Entrepreneurship** is crucial for any value chain intervention. Rural finance practitioners need to be aware that subsistence farmers are not a uniform group. These farmers show large variations in entrepreneurial skills and commercial orientation, and as such in their ability and willingness to take on risks. These differences include:
 - a reluctance by farmers to venture into unknown activities
 - low-income perspectives, leading to limited aspiration to develop new business
 - a cultural bias towards a limited variety of activities.

As such one-size-fits-all approaches are not possible. Each intervention needs to cater to a specific context.¹³

- Successful value chain interventions for smallholders are characterized by a **sequencing of interventions** that upgrades are perceived as small and 'risk-able' steps, leading to sustained changes in entrepreneurial behaviour to take on the next step.¹⁴
- **Strengthening horizontal linkages** enables farmers to increase their bargaining power in smallholder groups.¹⁵ Common goals can be accomplished through cooperative arrangements involving interdependence, trust and resource pooling to:
 - reduce input, transaction and financial services costs
 - contribute to increased efficiency and competitiveness
 - enhance product quality through common production standards and collective learning
 - increase the potential for upgrading and innovation.

Critical Failure Factors

The KMP workshop 2010 in Lusaka also identified several critical failure factors.¹⁶

Project management risks are among the main risks of any intervention. Value chain interventions are often multi-stakeholder projects, where each stakeholder works through different processes to achieve different returns, requiring clear expectation management and a long-term commitment among programme partners.¹⁷

Depending on the breadth of the intervention, **project costs** of food security interventions can be high. In contrast, in many cases there are only limited opportunities to sustain projects by service charges on business within the chain.¹⁸

Government and donor interventions have in some cases **crowded out private-sector investment** in the input supply sector, as well as in post-harvest handling and processing. This has led to a lack in development, or even deterioration, of the local agricultural input and services industry, endangering the sustainability of value chain interventions after projects are finalized. As such, interventions should be focused on strengthening the local agro-service sector through capacity building and education by local service providers.¹⁹

It is also important to keep in mind that **external interventions** in value chains are not always needed and might be counterproductive by creating dependencies and distortions.²⁰

Conclusion

To enhance food security through effective value chain interventions, it is necessary to include various financial and non-financial institutions in the intervention that suit the different needs in the chain: banks for larger investments and as providers of funding to local financial institutions, MFIs, and community-based finance organizations to work together in partnership(s) with farmers, farmer organizations, and input and training suppliers. Food security also relies on improved social service provision, including health, entrepreneurial capacities and infrastructure. Solving these issues requires the involvement of additional stakeholders—local and national governments, multilateral donors, social service NGOs, and education and training providers.

More Information

For more information, please refer to KMPs website at <http://www.ruralfinancenetwork.org/>, or contact KMP staff at info@ruralfinancenetwork.org.

Disclaimer

Although the content of this market profile has been compiled with the greatest care, we cannot guarantee that the information provided is fully accurate and/or exhaustive. Therefore, KMP cannot be held liable for claims pertaining to the use of this information.

Endnotes

- 1 KMP Conference paper. 2010. Exploring best practices in rural finance along value chains, Lusaka, Zambia.
- 2 KMP. 2011. Exploring rural finance best practices along value chains: Cases from East and Southern Africa Joint Regional Thematic Workshop on Rural Finance for Eastern and Southern Africa, 22–24 November 2010, Lusaka, Zambia.
- 3 KMP Conference paper. 2010. Exploring best practices in rural finance along value chains, Lusaka, Zambia
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- 9 Jayne et al, Patterns and Trends in Food Staples Markets in Eastern and Southern Africa: Toward the Identification of Priority Investments and Strategies for Developing Markets and Promoting Smallholder Productivity Growth, 2010.
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- 11 KMP Conference paper. 2010. Exploring best practices in rural finance along value chains, Lusaka, Zambia
- 12 Davis R. 2003. The rural non-farm economy, livelihoods and their diversification: Issues and options. Rural Non-Farm Economy. NRI Report No. 2753
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- 16 Burns J, Bogale S, Bekele G. 2010. Longitudinal impact study of the PSNP plus program—baseline assessment in Doba Woreda.
- 17 KMP. 2011. Exploring rural finance best practices along value chains: Cases from East and Southern Africa. Joint Regional Thematic Workshop on Rural Finance for Eastern and Southern Africa, 22–24 November 2010, Lusaka, Zambia.
- 18 KMP Conference paper. 2010. Exploring best practices in rural finance along value chains, Lusaka, Zambia
- 19 KMP. 2011. Exploring rural finance best practices along value chains: Cases from East and Southern Africa Joint Regional Thematic Workshop on Rural Finance for Eastern and Southern Africa, 22–24 November 2010, Lusaka, Zambia.
- 20 KMP Conference paper. 2010. Exploring best practices in rural finance along value chains, Lusaka, Zambia.

About The Rural Finance Knowledge Management Partnership (KMP)

The Rural Finance Knowledge Management Partnership (KMP), now in its third phase, is an initiative of the International Fund for Agricultural Development (IFAD). The partners are the Alliance for a Green Revolution in Africa (AGRA), the Regional Universities Forum for Capacity Building in Agriculture (RUFORUM) and the African Rural and Agricultural Credit Association (AFRACA).

KMP aims to strengthen rural finance delivery in Eastern and Southern Africa- ESA through knowledge management and experience sharing, capacity building and providing technical and implementation support. It does this by developing new, innovative ways to provide financial services to the rural poor. An important focus of KMP is to share and disseminate best practices. The KMP experiences are intended to do just that, by bringing together all information collected by KMP and its partners on specific rural finance subjects, most notably during its Rural Finance Thematic Workshops.

This guide highlights experiences in Value chain financing to improve local food security, combining the results of Rural Finance Thematic Workshops which were held in Kigali- Rwanda, Lusaka- Zambia and Maputo- Mozambique, with other KMP activities and recent information on this topic.

After detailing the benefits and difficulties of improving food security through value chain financing. The experiences provide a comprehensive analysis of strengths and weaknesses, and offer practitioners critical success and failure factors they need to consider in their value chain financing interventions.

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