Food and Agriculture Organization of the United Nations

INCLUSIVE FINANCE FOR RURAL DEVELOPMENT

OVERALL GOAL

To scale-up innovative approaches to improve access to rural agricultural finance for smallholder farmers and small and medium agro-enterprises (SMAEs) in developing countries.

About the priority area

Agriculture and rural off-farm activities have enormous potential to foster inclusive economic growth. Cross-country evidence shows that growth of agricultural production is 2.8 times more effective in reducing poverty than growth in industrial and services sectors. Yet, investments in agriculture lag that in other sectors. Between 2000 and 2011, worldwide, agricultural investments only grew 0.6 percent in real terms. In the developing world, over 60 percent of these investments were made by private domestic agribusinesses, including smallholder farmers. Lack of access to credits of smallholders and SMAEs is one important reason of sluggish investment in agriculture and rural development. Improving access to agricultural and rural finance will help unleash agricultural and agribusiness development and contribute to poverty reduction in rural areas.

MAKING A DIFFERENCE

Increasing access to agricultural finance for unbanked smallholder farmers, women and youth and the SMAEs they participate in, requires addressing both supply and demand-side constraints.

Addressing supply-side constraints

Specialized financial institutions face challenges in extending credits to producers in the agricultural sector as they see high transaction costs and risks. Detailed information is needed about the peculiarities of the biological processes and often volatile climatic conditions associated with agricultural production. The associated risks are shared by all actors along agricultural value chains.

Moreover, agriculture has bulky, seasonal, and long-term financing requirements that financial institutions find hard to satisfy. In addition, property rights on land and water may be poorly defined providing a weak basis for collateral, and policy incentives are often unfavourable to private (including smallholder) investments. Moreover, population density in rural areas tends to be low and, if compounded by poor communication infrastructure, this makes financial service delivery the more costly.

To address some of the challenges, FAO collates and facilitates exchanges of knowledge about the financial needs of agricultural finance clients, the dynamics of their diverse household income-generating strategies and the production constraints they face. The knowledge sharing also involves innovative mechanisms to overcome hurdles to agricultural and rural finance as piloted elsewhere. FAO is a leading agency of the CABFIN partnership, which also includes IFAD, GIZ, UNCDF, and the World Bank. Over the past ten years, CABFIN has documented experiences of innovative forms of financing agricultural value chains and has supported the scaling up of those experiences at national or regional levels through technical guidance on how to adapt and promote innovative financial and risk management tools and approaches.

Addressing demand-side constraints

Because agricultural value chain actors are strongly interdependent, analyses by financial intermediaries must go beyond assessing risks of individual clients and assess them in the context of the value chain at large. Supporting actors, including producer organizations, to develop effective risk management strategies is one aspect of addressing the constraints on the demand side. Even when risks are properly identified, required interventions often lie outside the capacity and mandate of financial institutions, such as developing financial literacy and record-keeping skills of women, youth and producer organizations; changing government policies and regulatory frameworks to support the financial instruments, and improving coordination among actors in agricultural value chains. These are serious barriers for the inclusion of the 'missing middle' and vulnerable rural groups. The few financial intermediaries that are engaging significantly in the sector have been able to establish cooperation with private and public actors that help them reduce these constraints through FAO support. FAO is also facilitating the promotion of producer organization or community-based savings and loan groups , which may serve as stepping stones to foster financial literacy, better risk management, and access to finance from the formal banking sector.

FAO's COMPARATIVE ADVANTAGE

Working with its partner organizations, FAO facilitates exchange of experiences among countries and addresses non-financial constraints that limit the development of agricultural finance markets. This is enabled by the diverse technical expertise of FAO staff that facilitates identification of innovations and adaptation of products and services to local circumstances and through extensive country presence. Furthermore, FAO works closely with the four regional Rural and Agricultural Credit Associations (RACA) networks it created in Africa, Asia, Latin America and North Africa and the Near East in the late 1970s.

IN PRACTICE

FAO is currently supporting field projects, inter alia, in the following practice areas:

Adapting warehouse receipt systems to smallholder clients in Tanzania, Ethiopia, and Niger. In each country, FAO partners with local actors specialized in local agricultural and financial systems to tailor financial services to meet the needs of the diversified income-generating activities of smallholder families.

Adapting the village savings and loan association (VSLA) methodology to serve agriculture in South Sudan. FAO has been working closely with the local CARE office in South Sudan to adapt the VSLA method to fit agricultural production activities led by women through the combination of local extension services and the use of matching grants for small agricultural enterprises.

Mainstreaming agricultural value chain finance approach in lending processes in Thailand and Pakistan. FAO has provided technical assistance to the Agriculture and Cooperative Bank of Thailand (BAAC) to mainstream agricultural value chain finance analysis into its lending process. Similarly, in Pakistan and through funding by the State Bank, FAO provides guidance and training for all commercial banks and micro-finance institutions providing finance to the agricultural sector, with an emphasis to expand outreach to the unbanked smallholder family farmers.

Enhancing the cost-effectiveness of the national agricultural insurance programme in Mexico. At the request of the government of Mexico, FAO has provided technical assistance to identify the potential for efficiency gains in the implementation of the CADENA programme, which provides weather-index insurance against catastrophic risks affecting the agricultural sector. As a result organizational processes are improved to improve reach out to smallholders.

Using non-bank providers for financing in Somalia. In Somaliland and Puntland where formal banks are lacking, FAO works with financial intermediaries specialized in transferring worker remittances and local micro-finance institutions to adapt tools and build capacity to use mobile technologies in providing financial services to agricultural and agribusiness organizations such as livestock associations and warehouse managers of sesame.

SCOPE FOR DOING MORE AND BETTER

FAO is:

- Expanding its work with local financial institutions to adapt or design new agricultural finance products for smallholders, women and youth and SMAEs
- Testing and scaling up agricultural finance products and inclusive agribusiness models developed by financial institutions and value chains actors
- Testing and scaling up use of mobile banking and ICT to leverage finance for all actors along agricultural value chains
- Facilitating public-private platforms to promote policies conducive of better access to finance for smallholder farmers and SMAEs
- Developing the capacity of financial institutions and producer organizations to apply agricultural risk management models and promote financial literacy among members of producer organizations, associations of women and youth
- Providing support to improve coordination among public and private stakeholders in the implementation of common agribusiness investment promotion strategies at national and regional levels
- Supporting countries in enhancing synergies between financial risk management instruments and social protection for farm and non farm rural populations.

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MORE INFORMATION

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