Value chain Financing

Introduction
Samriddha Pahad UK (formerly known as The Blueberry Hill Charitable Trust) is a UK-based organization registered as an international non-government organization in Nepal since 2011. Samriddha Pahad UK (SP) carries out interventions aimed at improving the living standards of hill and mountain communities through sustainable access to finance linked with appropriate livelihood opportunities and local institution strengthening. SP is currently implementing Samriddha Pahad Project (through core funding) in Taplejung and Terahthum districts. SP in January 2016 completed SAFAL (Sustainable Access to Finance and Livelihoods) a USD 1,460,000 project funded by UKaid through DFID. This project was rated as A+ program by the DFID team and was implemented in Ilam, Panchthar, Taplejung, Doti, Dadeldhura, Achham and Bajura districts of Nepal.

One of the main components of SP on access to finance is Value Chain Financing for various subsectors. Our role as a facilitator is to create an enabling environment for financial intermediaries and government extension agents to create vertical linkages. SP promotes external financing through financial intermediaries to agriculture and multipurpose cooperatives and ultimately to producers. We believe external financing improves the likelihood of establishing a viable and long term commercial relationship between the chain actors and capacity to scale up their services bringing a systemic change in rural financing market.

In Nepal, banks and financial institutions still see rural areas especially hills and mountains as not profitable zones due to high client origination, operation, high perceived risks and monitoring costs. Due to this conventional thinking and lack of access to finance rural smallholder producers cannot be an active member of a commodity chain forcing them to continue as subsistence farmers. SP’s goal is to make the small holder producers and
cooperatives inclusive in the value chain by building their capacity for value added production and support them to compete in the market. The benefit of these capacity building initiative are improved skills of producers and cooperatives which will help them to attract financial institutions for lending.

**Samriddha Pahad’s Approach: Innovative Value Chain Financing**

SP has been practicing various innovative value chain financing while implementing its access to finance projects:

**Agriculture value chain financing**

SP supports the cooperatives to build their capacity to fulfill the requirement of BFIs for wholesale loan. One of the key constraints for cooperatives is lack of fund for lending to its members for use in productive sectors. SP has been facilitating financial linkages between banks and financial institutions and agriculture cooperatives. One of the most successful cases in Ilam district is the linkages between milk cooperatives, Dairy Development Corporation (DDC) and NMB Bank. SP facilitated linkages between DDC, NMB Bank and 12 dairy cooperatives; where NMB provided loan of more than NPR 3 crore to these cooperatives which was loaned to 432 members. Cooperative acts as a collection centre of milk and sells it directly to DDC on behalf of the farmers. Monthly instalment is paid to NMB by DDC and the remaining earning is transferred to farmers through the concerned cooperatives. This link between the producers, buyer and financial intermediaries has greatly reduced financial risk to banks and contributed to institutionalize the market system.

Similarly, SP facilitated loan linkages of NPR 2,240,000 between the Dorumba Agriculture cooperative in Panchthar, RMDC and RSRF. The loan was utilised by farmers to buy inputs for tomato farming and the cooperative now acts as a collection centre for the tomatoes which are sold in Birtamod market fetching a higher price. Besides creating and facilitating linkages SP also plays a crucial role in developing the capacity of the producers and cooperatives to help them be a part of formal value chain.

Furthermore, the Kanyam Tea Producer Cooperative in Ilam acquired NPR 2,000,000 loan from the National Cooperative Bank to upgrade its factory. The cooperative is registered in VAT and have started exporting tea collected from the cooperative members to India where they fetch higher price compared to selling in the local/national market. The cooperative members participated in a tea pruning and enterprise development training which has helped them to produce quality value added product.

While linking agriculture cooperative to financial intermediaries most of the loans are used for gaining inputs, land leasing or technical capacity building of the cooperatives such as purchasing of equipment for processing or investment in transportation facilities to fetch better price of the produce.

**Cattle Insurance**

Insurance is another instrument SP is using for value chain financing. SP has facilitated a tripartite agreement between dairy cooperatives, NMB Bank and NLG insurance where access to finance is
coupled with cattle insurance. It is compulsory for milk producers to insure their cattle after purchasing using loan from NMB Bank. Insurance is a means of protecting low income households in remote hill and mountain regions against specific risks in exchange for a regular payment of premiums. Over the past 2 years, NLG Insurance Company has insured over 200 cows for a total value of more than NPR 1 crore. Cattle insurance has gained considerable popularity as farmers understand associated risks.

**Reaching to rural areas where financial intermediaries hesitate to reach out**

In rural and remote areas, it is difficult for bank and financial institutions and cooperatives to establish its presence. The existence of cooperative is still at an infant stage. As financial intermediaries do not have enough incentives to extend its services in rural areas SP through a subsidy model supported 4 Micro Finance Institutions (MFIs) to open and operate 17 MFI branches in some of the most remote areas. These MFI branches have reached more than 5,655 loan clients with loan outstanding of Rs. 26 crore. SP also provides technical capacity building training in enterprise and livelihood to clients of MFIs.

**Risk sharing between SP UK and Banks and Financial Institutions (BFIs)**

SP has realized cooperatives operating in the remote areas are deprived from basic services and are institutionally weak compared to cooperatives operating in comparatively accessible areas limiting weak cooperatives from accessing financial services from BFIs. To overcome this constraint, SP works with these cooperatives to build their institutional capacity and helps them to qualify for the services available from BFIs. SP has piloted loan guarantee scheme with BFIs where SP shares local market information along with certain percentage of investment risk (repayment guarantee) and post investment monitoring. SP’s role has helped BFIs increase their investment in remote areas with confidence to increase their coverage.

**Value Addition by SP UK in VCF**

SP UK provides various value added services to strengthen the value chain at institutional and producer level:

**Institutional level**

1. **Market Information**

   In value chain financing the financial intermediaries lack sufficient market information on rural areas due to which they foresee greater risk. SP bridges the gap between financial intermediaries and value chain actors, especially those on the production side (producers and cooperatives, sometimes also a collector) by providing market information. To date, SP has partnered with 15 BFIs, facilitated NPR 450 million loans to 9,000 rural clients through 85 cooperatives.

2. **Loan Documentation**

   The cooperatives operating in rural areas lack basic capacity to fulfil the extensive loan documentation process due to which they often hesitate to approach banks. SP supports these cooperatives by rigorously building their capacity for actual loan documentation and application process for availing loan with financial intermediaries.

3. **Technical capacity building of cooperatives**

   A key step is to focus on building the technical capacity of the cooperatives which enables them to operate as a truly private entity. Since many agriculture cooperatives are part of the value chain as collectors, it is important that their institution capacity is built especially in governance and accounting.
Producer level

1. Financial Literacy Training (FLT)
   The other value addition SP offers is Financial Literacy Training for small producers or clients of MFIs and cooperative on Financial Planning, Cash flow and Budgeting, Savings, Debt, Insurance, Investment and Remittance. FLT helps to build the capacity of small holder producers for better utilisation of loans acquired from MFIs/cooperatives. To date SP has provided FLT to 15,498 clients of MFIs/cooperatives.

2. Technical Capacity building of Producers
   Another value addition that SP has been providing is technical capacity building of producers on different agriculture subsectors such as vegetables, dairy, goat farming, mushroom farming, bee keeping, and enterprise development training among many. These specific targeted training support producers to produce better quality product and also to produce value added product. SP has provided livelihood training to 14,000 community members. The capacity development training to cooperatives and its members will result in business growth which will enable the members to make informed decision improving their financial management and income.