DESPITE IMPRESSIVE STRIDES MADE IN RECENT DECADES, THE FINANCIAL INCLUSION MOVEMENT (LED BY COMMERCIAL, MICRO, COOPERATIVE, REGIONAL AND GLOBAL FINANCIAL INSTITUTIONS) HAS YET TO CLOSE THE GAP IN FINANCING TO SMALLHOLDER FARMERS, WHICH HAS BEEN ESTIMATED TO BE AS HIGH AS $270 BILLION GLOBALLY.

RURAL FINANCE TRENDS

This briefing paper presents the main messages discussed in the "Rural Finance Trends" at the Social Finance Vibe 2021: Pandemic Reboot conference in September 2021. Speakers Mark de Sousa Shields (IFAD), Lea Soroka (IFC) and Perlat Sulaj (FED Invest, Albania) talked innovative approaches and the future of financing rural businesses. Watch the session recording: https://www.youtube.com/watch?v=fp495ssT5Vk

This funding gap is being driven by a number of factors, not least of which are levels of perceived risk, lack of market scale, high transaction costs and a want of ag knowledge on the part of lenders (mirroring a lack of financial knowledge on the part of smallholders).

There is however, cause for optimism in light of a number of recent advances in recent years, including in climate risk management, agricultural loan product innovation and reductions in the cost of digital lending. Alongside this, we see increased interest in agricultural lending from impact investors of all types as well as from public sector and international financial institutions—particularly in terms of innovation and scale.

RISK AND DATA: THE IFC VIEW

The gap being perceived and actual risk in lending to small farmers is to a large extent the result of a lack of agricultural understanding and experience on the part of lenders. The business risks faced by smallholder farmers are different to those faced by the typical small enterprise; while they may be unique they are not insurmountable. In fact, the longevity of the lending relationship between a lender and a farmer can greatly exceed that of a typical microenterprise, where business failure is a far more likely outcome. Agriculture can be unpredictable within any given year, but more predictable over the long term, inasmuch as farmers expand and diversify production over successive business cycles and pass on the business to future generations upon retirement. It's not uncommon for a farmer–lender relationship to last 40 years or more. This difference between perceived and actual risk was particularly on display when the COVID-19 pandemic lockdown shuttered many micro and small businesses—even as farms continued to operate and feed their communities.

While better knowledge about ag businesses can help lenders mitigate portfolio risk, so too can better data. The challenge here is that financial institutions have strict data requirements for reporting and security that can present a challenge to farmers in terms of the informality of their businesses. Here we see emerging opportunities when it comes to using big data and artificial intelligence to automate decision-making and lower transaction costs. In today's market, even off-the-shelf management information systems (MIS) can be affordable and beneficial in terms of raising a lender's operational efficiency. Technology can also help social finance institutions better assess a farm's capital needs and asset holdings using GPS surveys and commodity price indexes—as well as to keep track of a farm's movable assets (including livestock, vehicles and machinery).

In a similar vein, technology can help good farmers become better farmers. For instance, external RFID tags or ingestible microchips allow farmers to digitally track their herds and protect against theft. The latter can also trigger automatic alarms when an animal's health is under stress or at a certain point in the breeding cycle. Tech innovations continue to emerge, including a new bovine facial recognition application to track livestock movements.

SMALL AND BOUNTIFUL: THE IFAD VIEW

Smallholder farms account for the majority of the world's food supply—in some places (such as Africa) up to 70 per cent of the national food supply comes from farms under two hectares. While digital solutions are useful for farmers and lenders alike, there are limits to what it can achieve in a landscape where feature phones, rather than smartphones, are the norm—and where uptake of digital lending solutions among banks is limited. Thus reason, it's important to understand the diverse needs of a small farm, which may go beyond simply needing credit products.

In the first instance, smallholders are increasingly developing value-added activities in special market niches, including territorial origin, natural and organic products. These are fast-growing markets, and we need to support smallholders to take advantage of these opportunities as they arise. At the same time, lenders need new types of risk measurement and management to help farmers weather climate and socio-economic emergencies.

It's also important to consider the economy of the household rather than of the farmer themselves, because most smallholder families develop and nurture a diverse economic basket wherein each income stream has its own seasonality, risk and reward. These can include (but are not limited to) remittances and agritourism. The challenge here is for lenders to have robust market intelligence to enable them to serve the needs of smallholder families with a range of products at different stages of the business cycle (including credit, insurance and savings products) and to do so at scale.

GROWING A NETWORK: THE FED INVEST VIEW

FED Invest is the largest cooperative institution finance institution in Albania, with more than 75,000 members and 60 branches throughout the country. FED Invest has served rural micro entrepreneurs and small farmers for more than 30 years, and recently launched a new initiative called the ABA Center. This agribusiness support mechanism has both a physical and an online presence, and aims to be a "one-stop shop" of financial and non-financial services for all parts of the agribusiness value chain, including (and especially) farmers.

Users can visit the ABA Center via a website or a smartphone app (iOS and Android) to access daily market prices for key agriculture products, seasonal and monthly farm calendars, agricultural export standard information, details of government subsidy and incentive schemes, and contact/service details of companies across the agricultural value chain, including farmers, agricultural input providers, livestock veterinary services, equipment manufacturers, processors, exporters and more.

The ABA Centre also hosts a virtual marketplace where registered users can promote their own products or buy from others; it also features a forum where users can propose topics for discussion, crowdsource answers to their problems or share their expertise. Finally, it includes a "hotline" that allows users to get expert advice within 24 hours online. The ABA Center is the result of FED Invests' strategic partnership with JICA, Rabobank and EFSE—and it welcomed 7,000 users within 12 months of launch. It will continue to evolve based on user feedback in future.

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