



Savings and Credit Forum: Refinancing of Rural and Agricultural Financial Institutions and Agricultural Production Co-operatives 15 May 2009

The first Savings and Credit Forum of 2009 was opened by Peter Tschumi, head of SDC's Employment and Income Focal Point, who welcomed the participants and presented the program of the day.

The first presentation by Florian Gross, regional manager of Oikocredit in Central and Eastern Europe (CEE), provided the participants with **key challenges and good practices in refinancing rural/agricultural financial institutions and agricultural production cooperatives**. Florian Grohs recalled the main difficulties in providing financial services in rural areas: high transaction costs, seasonality of income, high risks and weak institutional capacity. In the CEE countries the low population density in rural areas and the reduced size of the MFIs lead to high transaction costs compared to countries in Asia where the population density is high and institutions are very large. As a consequence in rural areas of the CEE countries most financial service providers are saving and credit village cooperatives.

Regarding the lending to agricultural production cooperatives, Mr. Grohs related to the experience from Bulgaria and Romania which shows that critical success factors are to finance the complete amount and not only part of a project, to match the repayment plans of the loans to the farming cycle, to ensure that farms are stable and have not debts, to make conservative projections and take good securities. Moreover, the provision of both advice on how to manage the loan and technical assistance on the financed project are key success factors for the timely repayment by the cooperatives. Currency risks affect agricultural production cooperatives in many countries. Oikocredit thus lends money in local currency and hedges its risk with a high interest rate¹. Transparency and good governance of the agricultural cooperatives are key success factors, reasons why Oikocredit works only with cooperatives which are well established, of a certain size, have a long track record with exporting to the international market and are well integrated into the value chain (e.g. milk processing in Kenya, sugar and banana in Philippines, coffee in Costa Rica). Moreover, Oikocredit maintains offices in 35 countries with 2 to 5 local staff each who maintain a close relationship with partner cooperatives.

Fair Trade is a very positive innovation for producers in the South and East, because it allows involved families to improve their living conditions (building of schools and roads), increase and stabilize their income and create sustainable business relations. Nevertheless, Fair Trade also has some negative sides - which have to be taken into consideration when financing value chains - namely that Fair Trade is unattractive when prices on the international market are high.

The second presentation of Florian Grohs dealt with the **impact of the food and financial crisis on the refinancing of rural/agricultural financial institutions and agricultural production cooperatives**. Mr. Grohs reminded the participants that the increase in world food commodity prices was due to a combination of poor harvests in many countries, increased demand for basic goods (meat and dairy) from China, increased production of bio fuels, and accordingly more speculation on the World market. Poor urban people and rural non food producers were the most badly affected by the crisis. Small scale farmers have first benefited from the increase in food prices, but this has then been compensated through the increase in the prices of inputs (seeds, fertilizer). Large farming units

¹ Oikocredit manages its own currency risk fund.

and cooperatives have most benefited from the crises because they could quickly respond to the increasing demand from supermarkets, especially in the CEE and Latin America.

The financial crisis strongly hit the retail financial institutions, both on the side of clients (reduced demand, increased portfolio at risk due to the economic slowdown) and on the side of the funders and investors (less money available for refinancing, increase in interest rate). In this difficult situation Oikocredit continues supporting its partner institutions by increasing their equity and providing technical assistance. At the same time, Oikocredit aims at increasing its loans to agricultural production cooperatives because the demand for food commodities will steadily grow in the coming years and cooperatives will play a more and more important role in the production of food commodities. Finally, Florian Grohs made a call to the donor community to support the development of rural financial services (loans, savings, and remittances) and technical assistance services and the promotion of sound regulatory framework condition.

Mr. Grohs' presentations were followed by three illustrative case studies of rural/agricultural financial institutions in Nicaragua, Bulgaria and Togo. The case of the FDL (Fondo de Desarrollo Local) in Nicaragua was presented by Isabelle Dauner from Intercooperation. The **FDL**, a leading rural lending institution in Nicaragua, was hit by both the food and financial crisis. The food crisis affected mostly clients from urban centers who were net consumers of food products and suffered from the increase in food prices. Agricultural producers first benefited from the increase in food prices, but benefits were quickly absorbed by the increase in input prices. The financial crisis, which resulted in a serious economic slowdown in Nicaragua, affected the overall performance of the FDL, since many clients could not pay back their loans on time. At the same time, the cost of funds to finance FDL's portfolio increased and was not passed on to the customer, which reduced the financial margin. FDL's coping strategy in that situation, was to become more selective on the lending side, to slow down portfolio growth, concentrate on the agricultural sector, and remain flexible on lending principles (reschedule loans for farmers who cannot pay back on time).

The second case study was presented by Nikolay Draganov from Oikocredit. In **Bulgaria**, Oikocredit has supported 12 savings and credit cooperatives from different networks since the year 2000. Until end of 2008, these cooperatives have passed from 14'000 to 19'000 members, increased their total assets from 13.7 to 43.6 million BGN (22.8 million euro), doubled their portfolio of agricultural loans and decreased the average portfolio at risk (30 days) from 3.4% to 2.3%. The expansion of Oikocredit's portfolio in Bulgaria has been very prudent due first to the absence of a special law and regulations for microcredit activities and the according systematic supervision, and second, to the weak capacities of the cooperatives in establishing internal risk control mechanisms and implementing high management standards. In such a context, Oikocredit, through its country office, has to invest much on selecting the cooperatives², improving management practices together with the board members of the cooperatives, monitoring and capacity building.

The last case study of the day was presented by Thierry Pleines from Brücke-Le Pont. **FECECAV** is a union of 11 savings and credit cooperatives in Togo. While it had a very difficult initial phase from 1996 to 2003, due to lack of professional management, the network is now well performing, thanks to the steady support from the Swiss NGO Brücke Le Pont and its insistence on building up internal capacities and restructuring the network. Since beginning of 2009, FECECAV has a loan from Oikocredit. The presentation on FECECAV showed that important factors for the development and viability of rural savings and credit cooperatives are: a sound legal framework, long term commitment and responsibility from funding partners, partnership with non financial service providers, excellent human resources and the provision of savings services. Remaining challenges for the FECECAV are the development of financing products for the development of sustainable agricultural value chains, diversification of the portfolio, protection against exchange rate risk when borrowing money from international investors.

² Oikocredit has developed a Project Viability Risk (PVR) System in order to assess the portfolio quality, governance and management skills of potential partner institutions.