



Zoom microfinance

Alliances with financial institutions: the best solution for financing needs of farmer organisations and their members?

Summary

The different strategies of farmer organisations (FOs)

The example of FONGS

A "win – win" FO-microfinance institutions (MFIs) strategy in the Office du Niger zone: the KAFO JIGINEW network and the SEXAGON union

An example of a concerted FO-MFI approach within a regional framework

The Latin America Guarantee Fund (FOGAL): a tool for financing producer organisations' economic activities

Conclusion

Farmer organisations and farmers often encounter difficulties accessing finance, both for their own needs and for those of their members. To overcome them, they adopt different strategies, including the creation of alliances with financial institutions. What are the advantages of this approach? What are the risks? While avoiding overwhelming detail, this Zoom Microfinance will attempt to answer these questions using four different cases: two in Senegal, one in Mali and one in Latin America.

The different strategies of farmer organisations (FOs) ⁽¹⁾

Difficulty in accessing finance can be explained by several factors:

- Agricultural finance requires large sums, often much greater than those available to microfinance institutions which are the main financial players in the countryside.
- Family farms need a broad range of loan products (short-term for inputs, storage and consump-

tion, medium and long term for equipment and infrastructure, such as land development), whereas microfinance has developed especially around short-term credit (due to the short-term nature of the resources available to it).

- Financing agriculture is a risky activity, on three levels: the risk of production (climate and health); market risk (price fluctuations of agricultural products); individual risk (disease, death).
- Participants are unfamiliar with and mistrustful of one another: it was moreover, as a reaction to this reality that in January 2003 in Ouagadougou⁽²⁾ (Burkina Faso), SOS Faim, Inter-Réseaux and SIDI brought together a set of representatives of FOs, MFIs

1) The description of different FOs strategies is a summary taken from « organisations paysannes et institutions financières rurales: construire une nouvelle alliance au service de l'agriculture familiale. Un guide opérationnel » CERISE/IRC-Montpellier SUPAGRO by B. Wampfler, F. Doligez, C. Lapenu and JP Vandenbrouck, 2008.

2) Workshop: dialogue à deux voix pour un financement de l'exploitation familiale rurale; Ouagadougou, January 2003.

and agricultural banks of four Saharan countries to engage in dialogue about the financing needs of family farms.

Faced with these difficulties, from a strategic point of view, farmer organisation responses can be classed into three categories. FOs that:

- set up a financial department for members;
- set up their own financial institution to serve members;
- seek alliances and synergies with existing financial institutions (MFIs, banks) out of shared interest and for mutual benefit.

The first strategy certainly offers some advantages (a financial department is generally inexpensive as it may be subsidised by external funds or the FO's own capital, it may strengthen the credibility of the FO amongst its members, and can better adapted the product offering where the FO has a guaranteed market), however, more importantly, there are a whole range of disadvantages: legal (grey area of the law), technical (unprofessional management), financial (lack of sustainability) and governance (use of credit by FO officials, muddled objectives). Even if this approach is sometimes applied by FOs for whom this is the only possible solution in remote rural areas, the difficulties encountered make it less and less frequent.

The second strategy is to create a subsidiary financial institution. Most often this is the second step in an FO's evolution, after a phase of internal credit management and the compliance problems that result. Here, the MFI put in place is therefore destined to become the financial arm of the FO. These often mutual or cooperative approaches, have led to the creation of a number of isolated credit institutions or enduring autonomous networks built

over a relatively long period. Their concentration on the financing of agriculture (which increases their risk) or their evolution, sometimes in accordance with their own financial principals, which gradually turns them away from the financing of agriculture and can lead to a sense of disengagement, are some of the pitfalls to avoid.

This publication will present a number of examples illustrating the third strategy: when FOs develop alliances with financial institutions (FIs), whether MFIs or banks.

This path is certainly not the easiest because it requires the parties to come to terms with, get to know and to trust, as well as negotiate with each other. But in terms of the chances of success, it probably offers the best means of responding en masse to the financing needs of farmer organisation members with shared benefits for all parties concerned.

In this negotiation, FO mostly starts out with the lesser hand. Indeed, FOs generally are in a financially weaker position than FIs and, ultimately, have very little alternative financing options. So there is an asymmetry that can not be negated at the outset.

One way to circumvent this difficulty, as in the case of FONGS (Federation of NGOs in Senegal), is to participate in the decision-making bodies of the FI in order to influence policy and decisions.

The example of FONGS : a way of combining all three strategies outlined above

FONGS is one of the main components of the peasant movement in Senegal: it is made up of 31 local and regional associations representing 120 000 families. For nearly 20 years, the federation has pursued a three-pronged strategy to facilitate access to financing for rural family farms. One of the pillars of this strategy is precisely having a shareholding in the Caisse Nationale de Crédit Agricole of Senegal (CNCAS).

In light of the state's disengagement from agriculture during the 1980s, FONGS adopted a strategy of raising funds to invest in ownership of CNCAS, both to preserve the existence of this instrument, but also to influence policy through participation in meetings of the bank's Board of Directors.

In doing so, FONGS was rewarded by CNCAS extending its rural network (12 new branches located in rural areas) and gradually reducing interest rates for rural credit (18 % to 7,5 % per year). In recent years, this financing has fluctuated between 8 and 12 billion CFA francs (between € 12,3 million and € 18,4 million).

If this kind of result seems both interesting and promising, FONGS believes that it can succeed only if its members continue to set up initiatives of their own (mutual savings and credit institutions), with a view to bringing them all together (and why not?), and seeking real future linkages between the members' decentralised financial systems and CNCAS (strategy number 2).

This is the second pillar of the FONGS's strategy: currently, 50 mutual savings

and credit institutions (MECs – Mutuelles d'Épargne et de Crédit) exist and represent more than 30 000 members. More than 800 million CFA francs (roughly € 1,22 million) have been collected in savings. The MECs were created by FO for various reasons:

- no other savings and credit network nearby;
- services offered were judged unsuitable (demands for guarantees, excessive entry fees or interest rates, loan products too short-term,...);
- pressure to become more professional often from external partners, after a phase of credit granted directly to the FO.

Specifically, FONGS supports the training of elected MEC officials and leaders and facilitates licensing procedures for the institutions as well as incorporating them into the network. Incorporating them into the network and provides significant advantages in terms of cash management, economies of scale (oversight, IT,...) and exchanges of best practices. These benefits seem largely to offset the risks of a sense of dispossession that is inherent in larger structures.

In addition to the credits granted by MECs (often short-term), since 2006 FONGS has developed a pilot project (strategy number 1) to fund the investment needs of its member associations, called FAIR (Funds to Support Rural Initiatives). 30 investments have been financed to date.

Finally, the strategic plan is supplemented by active participation in the formulation and implementation of the regulatory framework:

FONGS has argued from the outset that the PARMEC law takes into account the concerns and realities of rural life. During the consolidation phase of decen-

tralised financial systems (DFSs), the Federation also actively participated in the creation of a technical assistance team for credit unions and savings credit (AT/CPEC) charged with supervising the sector in Senegal. Finally, the national policy paper setting out DFS guidelines for the “FONGS network”, drafted in 2003, largely inspired the sector policy paper finalized in 2005 by the Senegalese State.

It should be noted here that an approach like the one undertaken by FONGS over a period of nearly 20 years is much more likely to succeed when adopted by the widest possible membership base rather than being the work of a few executives (elected or appointed).

Even if the relationship initially is often skewed against the FO, the latter nevertheless has certain bargaining chips, its members may become new customers of the financial institution and, on the other hand, the FO can also play an important role in ensuring the quality of the loans that are granted.

The FO may indeed contribute to both an analysis of the region concerned (which enables the FI to react in a timely manner to crisis situations, if any) and of its members (which allows selection of only the most reliable borrowers). The following example in Mali illustrates this.

A “win – win” FO-MFI strategy in the Office du Niger zone: the KAFO JIGINEW network and the SEXAGON union :

a nascent but promising initiative

In Mali, KAFO JIGINEW is the largest MEC network with over 240 000 members. It was created in 1987 and has built its success mainly in the Southern region

of Mali, where cotton production is the country’s main foreign exchange earner.

The uncertain evolution of the cotton sector led KAFO JIGINEW to diversify its business, especially through urban settlement in Bamako, the capital of Mali.

But the deep rural roots of KAFO JIGINEW have also driven the institution to look at sectors other than cotton.

The Union of Farmers of the Office du Niger (SEXAGON) is the main rice farmers’ union in this irrigated region. It has about 12 000 members. The rice farmers face a number of constraints in terms of organisation, access to inputs, marketing of production, but also access to finance.

Prompted by a common partner (SOS Faim), the two structures entered into a relationship in order to develop a new strategy in the Office du Niger zone to actively address their respective concerns regarding the set up of financial services for small farmers.

For KAFO JIGINEW, entering a new geographic area, organized around an important sector (rice), represents strategic growth with diversification of the risks involved. In addition, rice production is tremendously important in Mali in terms of both national food security and the household incomes of those involved in its production.

SEXAGON meanwhile, is making a variety of appropriate financial services available to its members: savings and short, medium and long term loans. These services are designed for service cooperatives and for their members; SEXAGON actively encourages the creation of these cooperatives.

At the moment, the two partners are working on the following products:



- short-term credit for inputs (implications for yields) and for the payment of ‘water fees’, via a system of warrant discounting (implications for securing access to land);
- medium-term credit for equipment (implications for yields);
- long-term credit for the development of additional areas for rice production (implications for food security).

Another comparative advantage of FO is the important role they can play in monitoring local borrowers, as is the case of groups promoting women’s interests in the Fatick region of Senegal.

An example of a concerted FO-MFI approach within a regional framework

Since 2001, GERAD and SOS Faim have initiated an integrated development programme in the Fatick region of Senegal (PDIF). It is designed to create links between parties in the same area, through various lines of work:

- capacity building amongst the partners;
- support for promising sectors such as salt, cashew nuts and small-scale breeding;
- support for the economic activities of members of groups promoting women’s interests (GPWI⁽³⁾).

Support for GPWI was built from a regional base and emerged following the establishment of a solidarity fund.

The fund is financed by a portion of the interest generated by the micro-credits granted to members of the GPWI, in partnership with various MECs in the region. These micro-credits are for women to develop income-generating activities (small-scale breeding, rural crafts, retailing). Seed capital has come from international aid agencies (10 mil-

lion CFA francs or € 15 267 per solidarity fund). The MECs are important in order to bring a professional approach to microcredit but GPWI play a fundamental role in identifying beneficiaries and in monitoring and collecting funds.

Last of all, the decentralised state entities (Centres to Support Local Development – CADL) complete the picture by being involved in the process of awareness raising, training and monitoring of the parties.

In practice, interest generated through granting micro-credits (20% per annum in total) is shared three ways:

- GPWI unions for monitoring loans: 12 % of the interest revenue;
- MEC for financial intermediation services: 18 % of the interest revenue;
- Solidarity fund: 70 % of the interest revenue.

Since the introduction of the scheme, several indirect effects have been observed:

- GPWI women members have been responsible for a substantial increase in savings;
- MECs are becoming more professional and governance has improved;
- the region’s MECs are entering into a greater number of positive collaborations with each other.

The solidarity fund has two main aims:

- to serve as leverage in refinancing negotiations for players in the region;
- to enable local participation in social infrastructure projects in the Fatick region.

Beyond improving financial services, this experience shows how microfinance can play a role in structuring the local economy of a region. It can catalyse different

³⁾The GPWI work with women who work for themselves at the village level.



energies, actors and resources of a region to go beyond existing divisions.

Finally, FOs can also provide guarantees, either using its own funds (capital, real estate), or by obtaining them from outside. This approach helps in a number of situations to start up a relationship with a financial institution.

The Latin America Guarantee Fund (FOGAL):

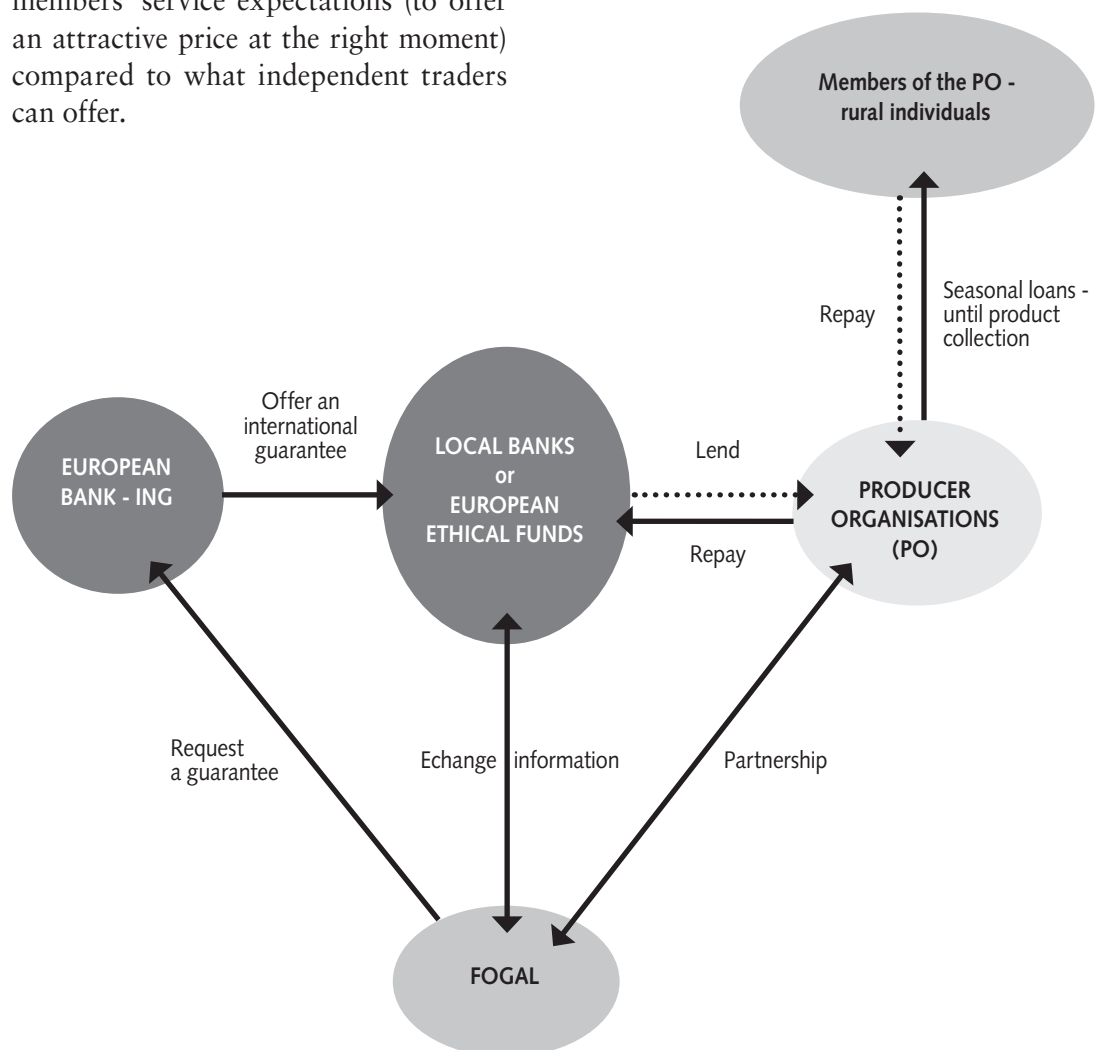
a tool for financing producer organisations' economic activities.

Many producer organisations face difficulties financing the collecting and marketing of their members' products. Indeed, the required capital is often lacking and it is therefore difficult to meet members' service expectations (to offer an attractive price at the right moment) compared to what independent traders can offer.

As a result, SOS Faim has promoted the creation of the Latin America Guarantee Fund (FOGAL), specially designed to deal with this problem.

The fund was created in 1991 and given a legal basis in 2004 as a non-profit association under Peruvian law with South American members.

It thus meets the needs of coffee, cocoa, quinoa, banana and other producer associations by giving them access to financing from both local banks and socially responsible developed world financial entities to market members' products on good terms, as illustrated in the diagram below.



In December 2007, FOGAL had a portfolio of guarantees worth US\$ 2 235 000 (roughly € 1 435 000), with a leverage ratio of 2 to 1 (i.e. the amount lent was twice the amount under guarantee). About 60 % of this volume is lent to farmer organisations in the Andean countries.

The existence of these international guarantees (the facility is paid for by a 2,5 % annual commission on the guarantee amount) enables partners to access additional funds but more importantly, to:

- create relationships with financial entities over the long term;
- improve their ability to negotiate, including over loan interest rates;
- put together a package along with other types of guarantee (mortgages, export contracts...), which enable access to significant lines of credit from local banks.

For example, two coffee and cocoa producer cooperatives (La Florida and Naranjillo) in central Peru have been able, in a matter of a few short years, to establish lasting commercial relationships with several Peruvian private sector banks that currently provide them with credit lines in excess of a million dollars at competitive interest rates (7 % to 8 % per annum), thanks to an initial guarantee of no more than US\$ 50 000 (€ 32 100).

Conclusion

For an FO to address the issue of its funding and that of its members is often both a delicate and a crucial matter. It determines whether a lasting sense of satisfaction and fidelity is established between members and their organisation.

Often, FOs are initially inclined to provide the financial services themselves. This solution seems the easiest, although upon reflection and with experience especially, the pitfalls discovered are numerous, and, lead to a process of outsourcing: the services are “removed” from the FO, to a subsidiary financial institution.

The success of these financial institutions created by FOs, however, does involve a risk of a shift in focus: the institutions open their doors to customers other than the FO’s members, engendering a sense of disengagement from the FO’s and members’ activities.

The third way, which is to seek alliances and synergies with existing financial institutions, may therefore be seen as potentially the most promising in the medium and long term. For FOs, it has various advantages such as, in principle, more appropriate size of financing, clear definition of roles for the different parties, and a greater sustainability. For the financial institutions, this strategy brings in new customers and diversifies its risks.

But the different experiences presented above also show how the reality of alliances and synergies can be complex, and complicated. One of the key challenges for FOs is certainly the issue of strengthening their ability to negotiate agreements that have technical, financial and legal aspects to them.

And finally, rather than present the three strategies available to FOs as following on one from another, why not widen the response, as we encourage FONGS to do, so that FOs adopt the three strategies concurrently in line with their members’ needs? ■

This issue of Zoom Microfinance was written by Marc Mees, Coordinator of SOS Faim's Partner Support Service. June 2008.

SOS Faim and microfinance

For several years, SOS Faim supports different microfinance institutions in Africa and Latin America. As with all development tools, we have to analyse the aims, models and implementation conditions of supports to farmers' organisations. With this frame of mind, SOS Faim edits "Zoom microfinance". You can find this publication and download it in French, English and Spanish on the website of SOS Faim: www.sosfaim.org.

The last issues of "Zoom microfinance" have dealt with the following topics:

- Popular investment associations in Ecuador: A case of "solidarity-based micro-investment" (#24)
- Equipment loans provided by Kafo Jiginew (Mali): investing in family farms (# 23)
- Moving towards a structured microfinance sector in Senegal - Development of a network: the experience of FONGS (# 22)
- Buusaa Gonofa in Ethiopia: marketing vision and fighting against poverty (# 21)
- Innovative credit and savings institution: RENACA in Benin (# 20)
- The link between a micro finance institution and the modern banking sector: the cases of MC2, the NGO ADAF and Afriland First Bank in Cameroon (# 19)
- Microfinance and rural financing (# 18)
- The savings-credit cooperatives in Peru and Ecuador and the development of rural financial services (# 17)

Apart from "Zoom microfinance", SOS Faim publishes another newsletter, "Farming Dynamics", which deals with the challenges faced by agricultural producers' and farmers' organisations in their development. You can also find this publication and download it in French, English and Spanish on the website of SOS Faim: www.sosfaim.org.

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