

Executive Summary

For many microfinance institutions (MFIs), farmers are inconvenient. Their lives and livelihoods do not fit neatly into traditional disbursement and repayment regimes that have proved successful for urban clients. Their cash flows are lumpy, unreliable, and can change with the direction of the wind.

One Acre Fund has created a loan product that fits the needs of these farmers. We provide tangible goods to our clients, rather than cash. The key features of our asset-finance model are:

- The procurement of high-quality farm inputs, including improved seed and fertilizer.
- The on-time distribution of those inputs to a location within walking distance of farmers' homes.
- Training on how to use the farm inputs correctly to maximize return on investment.

The combination of these factors produces greater productivity, increasing income per acre by 50 percent and generating a dollar impact of roughly \$135 USD per farmer.

Asset finance provides farmers with access to consistently high-quality inputs and other products that might not otherwise be available. It also ensures that the full loan amount is invested in productive assets and not diverted to pay for other household needs, increasing impact for the farmer and hedging risk for the lender.

MFIs introducing asset-finance should develop simple products that offer a high return to the farmer without unnecessarily increasing operational complexity, and should build their organizational capacity to match forecasted demand.

Why Money Isn't Enough

Farmers have unpredictable lives with a very limited ability to make significant investments. Their participation in farming and markets is a function of their opportunities and capabilities (Dunn, 2014). In order to achieve a profitable harvest from their land, farmers need access to high-quality seed and fertilizer, financing, information on planting and fertilizer application techniques, and markets. The majority of farmers lack access to at least one, if not more, of the above value chain components.

As a result, the rural finance sector has historically comprised farmers with low income, a low investment rate and then, inevitably, low productivity (Pearce et al, 2004). If a farmer has access to a cash loan, but can't find a place to buy quality seed and fertilizer, that cash will likely be used for other household needs, not to improve agriculture productivity. As shown in Figure 1, basic consumption or emergency healthcare may take priority over spending on the farm.

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Figure 1: demands on smallholder household income. Photo by Hailey Tucker/One Acre Fund.

Because the household needs of smallholder farmers are complex, and because many rural communities lack access to quality seed and fertilizer, it is difficult to ensure that a cash loan will be used as an investment in agriculture activities. To overcome both of these challenges, One Acre Fund developed an asset-finance product that addresses the single most significant investment a farmer will make in any given year. We believe asset financing is the most powerful and scalable means of improving farmers' livelihoods, but it should be considered within the broader context of farmers' financial needs, as shown in Figure 1.

Asset Financing at One Acre Fund

Asset financing can mean many things (USAID, 2010). At One Acre Fund, asset finance includes the direct procurement and delivery of farm inputs on credit. Farmers can access loans for staple crops and some vegetables, with additional crop and non-crop products under development.

The key features of our asset-finance model are:

- **The procurement of high-quality farm inputs, including improved seed and fertilizer.** In 2014, we worked directly with local seed companies and global fertilizer companies to procure inputs for over 200,000 clients in Kenya, Rwanda, Burundi, and Tanzania. After purchase, we are responsible for transporting inputs to our warehouses for storage.
- **The on-time distribution of those inputs to a location within walking distance.** We deliver inputs to farmers at the village level a few weeks before the agriculture season begins. In most places, a “drop distribution” method is used, in which a truck delivers inputs to the village level, on a specific date and time that is communicated to farmers in advance by a One Acre Fund staffer.
- **Training on how to use the farm inputs correctly to maximize return on investment (ROI).** One Acre Fund staffers deliver extensive trainings on proven agriculture techniques. Farmers learn

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how to use their seed and fertilizer, thus increasing their farm productivity and ultimately maximizing their ROI.

This asset-finance model helps the lender meet the needs of farmers in many ways that standard loan products cannot. These are the primary benefits for farmers:

- **Consistently high-quality inputs.** If seed and fertilizer is available locally, the quality is often questionable. Farmers know that One Acre Fund provides high-quality seed and fertilizer, which improves the likelihood of higher yields, quality of harvest product, and return on investment.
- **Inputs are price-competitive.** By leveraging economies of scale and buying in bulk, One Acre Fund is able to provide higher quality inputs at a similar price to inputs already on the market.
- **Timeliness when timing is everything.** Standard cash lending does not always account for crucial seasonal deadlines, such as the narrow window of time in which the rains are suitable for planting. By focusing on the provision of inputs in stages, delivered throughout the season, One Acre Fund ensures farmers have what they need at the right time.
- **Fully investing credit in the farm.** Providing inputs instead of cash means the whole loan goes into productive assets and is not diverted for other uses. This increases the return on investment for the farmer.
- **Tailored and uniform training.** Limited “loan uses” allows uniformity in training that is quickly and easily scaled. This drives greater efficiency and ensures farmers get the most from their inputs.

However, this asset-finance model has required One Acre Fund to develop its operations to include capabilities that many MFIs do not have. These are the major operational implications of direct provision of assets:

- **Expertise in logistics.** One Acre Fund imports more than 15,000 tons of fertilizer into East Africa each year, and has developed a logistics team to manage every aspect of the process, from landing the inputs at port to storing them in our network of warehouses.
- **Finance team has to manage lumpy cash flow.** Because we are making large seed and fertilizer purchases at specific times of the year, the finance team needs to carefully manage liquidity over seasonal cycles, unlike the more predictable churn found in traditional MFIs.
- **Distribution capability.** We use “drop distribution,” in which farmer groups meet at nearby locations such as schoolyards to receive their inputs. Fleets of trucks run between our warehouses and drop points (often on poor roads), and the logistics team deploys carefully planned processes to ensure all farmers receive the correct inputs.
- **Staff capacity to deliver agriculture training.** Our loan officers are trained to deliver high-quality agriculture trainings to clients. Our monitoring and evaluation (M&E) team measures compliance with trained techniques, as well as the yields of more than 1,000 farmers every year. This allows us to assess how well we’re doing, and where we can improve.

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Next Steps

When making the shift to delivering asset financing, organizations must consider two areas: product development and organizational capacity.

Product Development:

- **Deliver a high return on investment (ROI) for the farmer.** Asset financing means the lender knows where the loan is being invested and has the opportunity to help the farmer increase ROI. By helping farmers increase their incomes, the lender significantly reduces the risk of default. At One Acre Fund, we always ask ourselves: “Is this going to make farmers better off?”
- **Create simple products.** We focus on financing assets that are easy for farmers to adopt, and easy to scale. More complicated assets that promise high returns are not always the most successful. Impact should be balanced against simplicity.
- **Minimize operational complexity.** Although providing assets may seem more complex than cash, the uniform nature of the demand means products need not increase operational complexity. It is helpful to develop products in a modular way, so that they can be easily delivered by staff through existing channels and quickly scaled to reach new clients.

Organizational Capacity:

- **Build IT, procurement, and logistics capacity.** Dealing in goods rather than cash requires an organization to be able to manage the purchase, storage, and movement of those goods. Management Information Systems (MIS) need to accommodate new products, software installed to manage stock control, warehouses rented, and drivers hired. However, much of this can be achieved using fairly simple processes, particularly for MFIs that have a large network of branches to leverage.
- **Understand farming as much as finance.** Developing simple products that offer a high ROI means organizations must understand farming processes as much as financial processes. Hiring agriculture experts to develop products and training tailored to staff and clients is essential. Unless the lender is able to pass on this knowledge to clients, they cannot maximize the potential income from their assets.
- **Monitor, evaluate, innovate.** Asset financing makes understanding outcomes more important than ever. An ill-invested cash loan will be redirected at the earliest opportunity by the borrower. A limited menu of asset-finance products reduces this flexibility. It is crucial that the lender monitors client compliance with trained techniques, evaluates the impact on yield, and develops improvements where possible. This continues to stimulate demand and hedges credit risk by reducing the incidence of unproductive loans.

Key Conclusions

- ▶ Asset financing ensures farmers invest their full loan in high-quality, productive assets. This is more difficult to ensure with cash loans.
- ▶ The combination of procurement and delivery of high-quality farm inputs, accompanied by trainings on how to use those inputs, results in greater productivity for smallholder farmers.
- ▶ In order to successfully deploy an asset-finance model, MFIs must prioritize developing the products and organizational capacity needed to serve rural smallholder farmers. This includes acquiring agricultural expertise, developing rigorous M&E processes, and keeping operational complexity minimal.

Appendix

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