Sector Project Agriculture | Policy Brief 10

Agricultural Development Banks and Finance Facilities

Backgrounds, Lessons, Trends and Case Studies from Seven Countries in Sub-Saharan Africa

Implemented by

Deutsche Gesellschaft
für Internationale
Zusammenarbeit (GIZ) GmbH

Published by:
Deutsche Gesellschaft für
Internationale Zusammenarbeit (GIZ) GmbH

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Projects Involved:
Sector Project Agriculture, Competence Centre Financial System Development and Insurance

This policy brief is based on the study "Agricultural Development Banks and Finance Facilities (AgFiFs) – Background, Lessons and Trends and a closer look at seven Sub-Saharan Countries", which was prepared in 2020 by Martina Wiedmeier-Pfister, Claudia Huber and Bastian Domke on behalf of the Sector Project "Agricultural Trade, Agribusiness, Agricultural Finance".

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On behalf of the Federal Ministry for Economic Cooperation and Development (BMZ), Division 123

GIZ is responsible for the content of this publication.

Dezember 2021

BACKGROUND

Farmers in partner countries of German development cooperation often cite the lack of access to financing as the greatest obstacle to development. While access to credit, savings services, payment systems, and insurance has improved in many countries, the situation in rural areas and especially for agriculture is critical almost everywhere. In Sub-Saharan Africa alone, the annual capital required to modernise agriculture is estimated at over 200 billion euros with a particular need for small-scale farmers.

German development cooperation (DC) is working to close this funding gap, using a variety of instruments ranging from advisory services to improve framework conditions, training for financial institutions, agri-businesses and farmers, to the provision of credit lines and equity investments for banks and microfinance institutions.

One possible instrument is to promote(semi)-**governmental agricultural development banks and finance facilities** (AgFiFs).

Since the 1970s, developing, emerging, and industrialised countries have been using AgFiFs as an important rural development tool. AgFiFs were largely state-owned and financed by governments and international donor organisations. AgFiFs were not only politically instrumentalised (corruption, nepotism), but were also exposed to considerable **problems** such as a lack of distribution networks and the granting of loans without simultaneously offering savings opportunities for the borrower. For the most part, they were therefore institutionally unable to achieve the expected effects and their original purpose. Many AgFiFs were subsequently phased out and closed, and since the 1980s German DC **largely discontinued cooperation**.

In recent years there have been renewed efforts to establish AgFiFs in many partner countries – especially in Sub-Saharan Africa (SSA). German DC has often been invited by partners to support such projects. In response to these requests in 2020/21, the GIZ-Sector Project was commissioned by BMZ to conduct a study on the potential of promoting AgFiFs entitled “Agricultural Development Banks and Finance Facilities (AgFiFs) – Background, Lessons and Trends and a closer look at seven Sub-Saharan Countries”. The main findings of this study are presented in this policy brief.

FINDINGS OF THE STUDY

- Since AgFiFs are found in many of the BMZ's partner countries in SAA, the question arose as to the fundamental **evaluation of these institutions**. Together with the KfW, the study analysed AgFiFs in seven SSA countries (Benin, Togo, Mali, Burkina Faso, Nigeria, Cameroon, Malawi) and found the following results:
  - The role and potential of development banks to act as a catalyst for structural change are widely accepted. This is achieved through refinancing of financial institutions or direct lending through commercial or development banks, loan guarantee mechanisms, or hybrid forms such as the *"Mécanisme Incitatif de Financement Agricole"* (MIFA) (Togo) and *"Nigeria Incentive-Based Risk Sharing System for Agricultural Lending"* (NIRSAL) (Nigeria).
  - They make an important contribution to achieving socio-economic goals by serving the market areas that commercial banks do not consider marketable.
  - Government financing mechanisms offer potential for major international agendas such as the financing of climate projects (adaptation and mitigation) and the associated transformation of the agri-food sector. However, this requires medium to long-term efforts in the building, governance, and implementation capacity of institutions. It is beneficial to include representatives of the (micro-)finance sector as well as the private sector in supervisory bodies and when taking preparatory steps for reforming or founding new AgFiFs. An (overly) influential role of individual large agricultural corporations must be prevented.
- Agricultural development banks and finance facilities (wholly or partially state-owned) are **a finance sector instrument for financing** agriculture which is now being used again by many governments and some donors. Cooperation with AgFiFs can be a **promising funding approach** for rural development.
- Although data and qualitative assessments of these institutions are incomplete, AgFiFs have experienced a certain **renaissance in SSA** since 2008.[1] This is also reflected in the fact that governments and some donors (e.g. IFAD; AfDB) have increasingly used public banks for agricultural financing and have also founded some of them. Since 2000, **20 new AgFiFs were founded** world-wide, also in Sub-Saharan Africa, e.g. Banque Agricole Du Faso (BADF) in Burkina Faso.
- An attempt was made to adapt the intervention mechanisms and the attention to due diligence in **governance structures** within the institutions to experiences gained in SSA. Good practices from Asian regions (regarding governance structures, the central role of regulatory frameworks and integration into overarching agricultural development strategies) were also taken into account.
- In countries across Africa, some of the institutions follow a **sustainable approach** with sound governance structures and comprehensive transparency to provide development-oriented financial services as a market-oriented commercial bank (*Banque Nationale de Développement Agricole* – BNDA in Mali) or as a development bank (Development Bank of Nigeria – DBN in Nigeria, founded in 2015 with the support of KfW, among others).[2]

[1] See Eurodad, Public development banks: towards a better model, 2017
[2] KfW as a model: Nigeria establishes development bank – Link

- Some AgFiF institutions (e.g. in Cameroon or Anchor Borrower Programmes in Nigeria) have proven to be problematic due to misaligned incentives and non-transparent distribution mechanisms.

In 2021 after the completion of the study, **GIZ and KfW prepared a short practice-oriented manual[3] on how to work with AgFiFs**. It has already been tested in Togo and Malawi for potential practical applications. This ensures that the promotion of AgFiFs by KfW and GIZ can take place on the same conceptual foundation and be designed in a complementary manner. Possible support interventions must be prepared jointly by GIZ and KfW right from the beginning. Both Implementation organisations can contribute with their specific instruments. It is essential that these are coordinated and that the German DC speaks with one voice.

NEED FOR ACTION WITHIN THE FRAMEWORK OF THE BMZ CORE AREA STRATEGY "SUSTAINABLE AGRI-FOOD SYSTEMS"

- According to the **BMZ core area strategy**, "access to finance is a prerequisite for small farmers and small enterprises to invest in their farms and, in addition to securing their basic needs and self-sufficiency, to be able to produce for the market and thereby increase their income and leeway in decision-making when it comes to their own economic activities and life in general." One possible instrument for achieving this goal is the promotion of AgFiFs.
- Within the framework of the BMZ **Special Initiative (SI) "Transformation of Agricultural and Food Systems" (AGER)**, the BMZ's agricultural financing portfolio in SSA has considerably expanded, including the GIZ Global Project (GP) Agricultural Finance and various KfW Projects among many others.[4] Access to finance continues to be considered as a fundamental key to rural development and it remains important to continue to promote these issues in countries related to the SI AGER (and potentially also promote trainings and sustainable growth for good jobs). AgFiFs are one approach of support that is requested by partners.
- However, this requires careful **coordination with the donor community and private financial institutions**. Cooperation with other donors such as the World Bank, regional development banks and UN organisations such as FAO and IFAD is central to establishing a consensus on the role and cooperation with AgFiFs. Planning and implementation experiences have proven that GIZ and KfW can complement each other perfectly.
- In this regard, policy dialogue **with partner governments** is of central importance in order to work out the regulatory framework and governance structures for AgFiFs and, if necessary, to support reform steps.

[3] How to Appraise Agricultural Development Banks and Other State-Owned Agricultural Finance Facilities – A Practice Guide for German Development Cooperation – Chhatwal, Domke, Pace, Salzer, 2021
[4] The SI AGER Portfolio in the Agricultural Finance field amounts to a total of € 250 Million

BENIN AS A PRACTICAL EXAMPLE

- These experiences were applied when BMZ, GIZ and KfW reviewed further cooperation with the *Fonds National de Devéloppement Agricole* of Benin (FNDA).
- While the BMZ is working towards improved governance in the policy dialogue, GIZ has already been working with FNDA since 2019 in business and financial capacity development for loan applicants (GP Agricultural Finance, GP Green Innovation Centres) as well as advising financial institutions on needs-based financial services (GP Agricultural Finance).
- In preparation for KfW's commitment to financing the FNDA, all relevant actors were consulted. Specifically, the implementation of the SI AGER accompanying measure, especially the selection of the financial institutions to be supported and the concept for supporting applicants, is to be carried out in close consultation with GIZ.
- KfW and the SI AGER GP Agricultural Finance agreed upon a cooperation model, according to which a concrete plan will be elaborated between the GP Agricultural Finance and KfW with a contracted consultant to support with the implementation.

Other possible cooperations

- A cooperation with MEREF in Mali is currently being reviewed. Partners in Togo and Cameroon have also requested support.
- Possible funding interventions by German DC are always decided jointly with the BMZ regional departments, must fit into the country portfolio and are to be discussed during government negotiations. This would then be reflected in a concerted approach between the two implementing organisations.

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