CAADP

THE COMPREHENSIVE AFRICA AGRICULTURE DEVELOPMENT PROGRAM

PILLAR II

AREA C

Framework for the Improvement of Rural Infrastructure and Trade-Related Capacities for Market Access (FIMA)

STRATEGIC AREA C

Value-Chain Development and Access to Financial Services

The renewed focus on agriculture and agribusiness, as priority sectors for spurring economic growth in Africa, calls for developing value chains that integrate producers and markets to make the agricultural sector more responsive to consumer demand. The value-chain approach builds on conditions in the consumer market and emphasizes the interface, linkages, and segments that connect the final product demanded by consumers all the way to agricultural commodities produced at the farm level. This market-driven approach to formulating investment plans, public policies, and partnerships to integrate smallholder farmers can bring about the significant changes being sought in Africa's agriculture and agribusiness sectors.

The key segments in the value chain are (1) the consumer market, (2) trade logistics, (3) packaging, (4) processing, (5) postharvest risk management, and (6) agricultural production. These segments may be different businesses, or they may be combined through vertical integration. The strategic benefit of the value-chain approach for Pillar II of the Comprehensive Africa Agriculture Development Programs (CAADP) derives from the contribution that public investments in agribusiness and financial services make has to the overall CAADP goal of 6 percent agricultural growth. The Pillar II objectives and activities are summarized in Box 1.

Challenges and Emerging Trends

The most critical challenges and emerging trends with respect to value-chain development and financial services are the following:

- **Fragmentation of the agricultural value chain at the production segment level**. African agriculture is dominated by geographically dispersed smallholder farmers who produce limited surplus quantities. This geographic and quantitative dispersion of farm-level supply has resulted in many barriers to marketing, which in turn result in high product assembly and marketing costs, high cost of access to modern inputs, slow diffusion of technical innovations, relative vulnerability to weather-induced supply fluctuations, and in many cases low level of and returns to productive investments.

- **Limited availability of adapted financial services products**. Banks and nonbank financial institutions often cite the high cost of reaching individual smallholders as a key constraint to serving the vast group of smallholder producers. The Pillar II agenda will need to address the host of disincentives and obstacles linked to the sector policy and regulatory environment in order to accelerate expansion of the finance industry in Africa and promote the introduction of financial services products that are adapted to the needs of smallholders as well as the small and medium-size enterprise operators across the value chain.

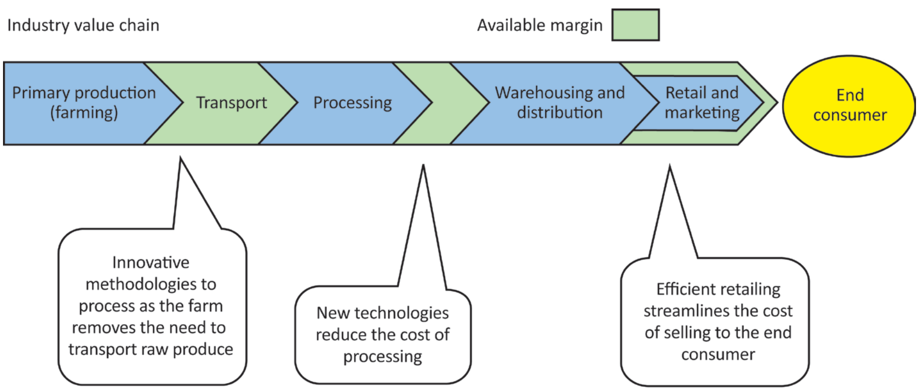
- **High cost of establishing and operating businesses**. Despite improvement in governance effectiveness in a growing number of African countries, it is relatively difficult to establish and operate a business in African countries compared with other major regions. At the country level, the challenge is to reduce obstacles related to laws and regulations affecting business registrations, licensing, worker employment and compensation, property registration, investor protection, taxes, financial sector transactions, and contract enforcement. At the regional level, the challenge is to rapidly advance toward establishing effective economic unions.

Responses and Opportunities for Action

- Promising areas for response and action are discussed here. The core elements of a program to exploit these opportunities are summarized in Box 2.

- **Public-private partnerships (PPPs) and business-to-business (B2B) alliances focusing on strategic commodities and markets**. Exploiting the opportunities created by rising demand and prices will require both private sector and public sector involvement. Such partnerships would target agriculture-friendly infrastructure investments, including transport, information and communication technologies (ICTs), and commercial infrastructure, as well as training, institutional support, quality management, logistics, and market intelligence to reduce cost of doing business along the value chain, as indicated in Figure 1.

Figure 1—Segment-level cost-reduction actions



Source: NEPAD Secretariat (2005).

- **Modernization of agricultural commodity trading systems**. Recently established trade associations in East Africa for dairy, coffee, grains, and textiles highlight the opportunities for organized commodity trade. Trade associations can help establish commodity grades and standards and serve as vehicles for establishing market information networks. Better organization of commodity trade also contributes to strengthening existing commodity exchanges and spurs the development of new exchanges, all of which is necessary to integrate and stabilize local markets and improve conditions for the creation and growth of agribusiness enterprises.
- **Effective communication of investment opportunities and changes in the policy environment in Africa.** The CAADP process is fostering renewed African and international attention to key value chains in agriculture. Converting this attention to Africa's agricultural sector into investments in poverty-reducing economic growth will require advocacy on the continent and beyond to transform international investors' perceptions of risk with respect to investment in Africa. A few African countries have invested in country marketing programs, and stepped-up investment by regional economic communities (RECs) to promote Africa's subregions would complement these national efforts.

Strengths to Build Upon

Future strategies for value-chain development ought to fully exploit the following strengths:

- **Growing awareness of the opportunities and interest in value-chain development**. Urbanization and changing consumer preferences, along with new developments in distribution, processing, and packaging, have led to a rapid expansion of value chains for traditional staples in many parts of Africa. Globalization and advances in communications technologies have also increased the interest of private sector actors in value-addition opportunities in the traditional commodity sectors.
- **Demonstrated capacity by smallholders and commercial farmers to integrate into value chains**. Smallholder farmers have, under the right conditions, participated in fast-growing value chains as individual entrepreneurs, contract farmers, members of out-grower schemes, and participants in other contractual arrangements. Smallholders in most countries have successfully integrated into value chains in horticulture, traditional export

commodities, staple foods, meat, or dairy. Such successes should and can be emulated and scaled up.

- **Introduction of innovative mechanisms to deliver financial services**. Advances in ICTs and the process of administrative decentralization can be used to improve the supply of financial services to smallholder farmers and rural enterprises. Strategies are also needed to build upon the rapidly growing microlending institutions to extend the reach of financial services providers into rural areas.

Levers for Agricultural Enterprise Growth and Value-Chain Development

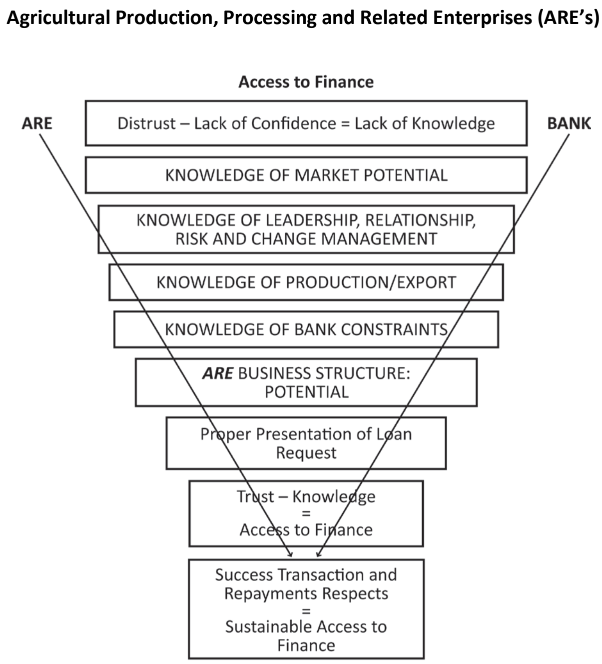
A value chain must be seen and understood in its full context, from the primary producer/farmer through the final consumer. A successful agenda to support value-chain development needs to target (1) the factors that determine the success and failure of agribusiness enterprises and (2) the type of interventions that would raise the value accruing to actors at each level of the chain. The pillar agenda needs to focus on helping African countries and private sector actors, including farmer organizations, stimulate the process of enterprise creation while effectively controlling the factors that lead to business failure.

Three key levers that African countries and private sector operators, including farmer organizations, must concentrate on to stimulate their value chains are (1) unit cost reduction, (2) volume expansion, and (3) product value addition. It will also be important to ensure that as much as possible of the added value is captured within Africa, including by smallholders.

Financial Sector Development for Agricultural Value-Chain Growth

Value-chain development is impossible without adequately functioning financial institutions to provide funding for investment and business operations across the various segments. Specific segments have different needs and capacities to access finance. The pillar agenda can build on the various types of financial institutions, ranging from commercial banks to group-based savings organizations such as rotating savings and credit associations (ROSCAs). Financial institutions in most African countries, in particular commercial banks but also microfinance institutions, in general lack the skills to assess and manage risk related to lending to agricultural production, processing, and related enterprises (AREs). These constraints not only limit absolute access, but also add to the cost of credit. AREs, conversely, lack the knowledge or skills to produce accurate information presented openly and transparently (see Figure 2).

Figure 2—Barriers to adequate access to financial services for agribusiness development



The focus of the Pillar II agenda in this area, as summarized in Figure 3, is to establish (1) partnerships and alliances that can help lead to better knowledge among lending institutions about AREs' financial strengths, requirements, and risks; (2) lending facilities that adequately cover the working capital needs of ARE; and (3) long-term capital funding to support needed investments in plants and equipment.

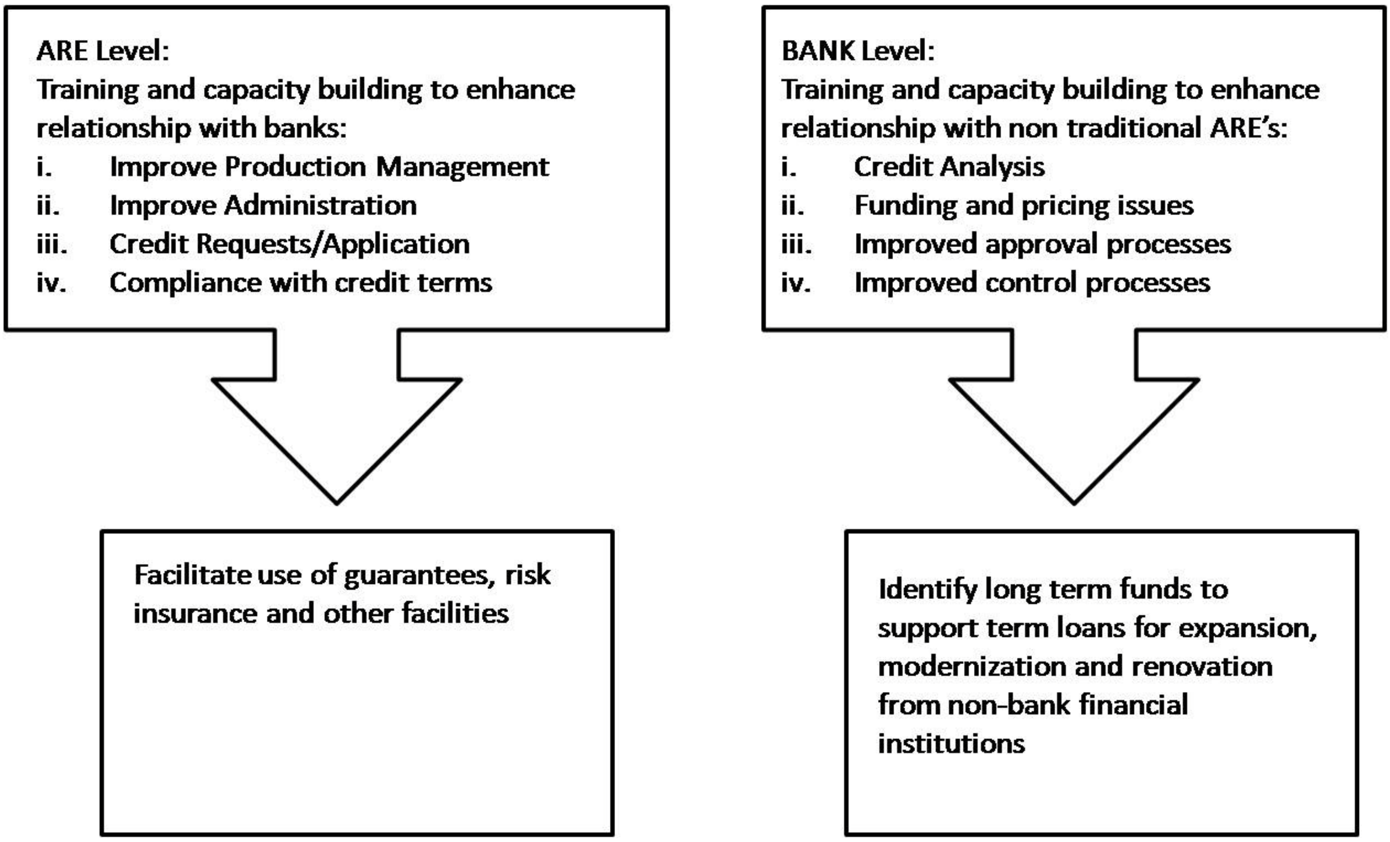
Proposed Early Actions under Pillar II Area C

The proposed early actions under this and other strategic areas serve as entry points to scaling up the Pillar II agenda at the country and regional levels. They target key areas and activities that respond to needs that are broadly shared across countries and regions and that hence require collective action and lend themselves to economies of scale. In several cases, they start with pilot programs that can be scaled up as implementation proceeds.

- **Agricultural investment and enterprise development platforms**. The objective is to promote the adoption of effective and efficient tools for PPPs and B2B alliances to boost agricultural value-chain development. Indicative activities would consist of piloting platforms in 10 countries—5 each in the Common Market for Eastern and Southern Africa (COMESA) and Economic Community of West African States (ECOWAS) regions—to remove the regulatory, technical, and financial obstacles to enterprise creation and growth and to develop the commercial infrastructure and build skills that would facilitate the integration of smallholder farmers into dynamic and higher-value chains.

- **Agribusiness joint venture fairs**. The objective is to expand joint venture opportunities in agribusiness by facilitating contacts between entrepreneurs and investors in the early stages of enterprise creation or product development. The main indicative activities are to (1) design a fair to link investors and entrepreneurs at the business planning stage; (2) develop the capacities of African entrepreneurs to participate in such a fair; (3) ensure the financial sustainability of such an effort; and (4) pilot the organization of such a fair in the COMESA region.
- **Fertilizer and seed systems development**. The objectives is to speed up the emergence of broadly accessible, cost-effective, and competitive seed and fertilizer supply and financing systems and to significantly raise the use of both inputs by smallholder farmers. Main activities include establishing strategic PPPs and B2B alliances between key actors along the seed and fertilizer supply chains to lower transaction costs, facilitate access to finance, and expand distribution networks. Early actions will also build the institutional and commercial capacities of farmer organizations to manage procurement and financing of seed and fertilizer requirements.

Figure 3—Intervention points to raise access to and reduce cost of financial services



BOX 1
Pillar II of the Comprehensive Africa Agriculture Development Program

CAADP Agenda and Objectives
The Comprehensive Africa Agriculture Development Program (CAADP) is at the heart of efforts by African governments under the African Union (AU)/New Partnership for Africa's Development (NEPAD) initiative to accelerate growth and eliminate poverty and hunger among African countries. The main objective of CAADP is to help African countries reach a path of higher economic growth through agriculture-led development, which eliminates hunger, reduces poverty and food insecurity, and enables expansion of exports. As a program of the AU, it emanates from and is fully owned and led by African governments. Although continental in scope, it is an integral part of national efforts to promote agricultural growth and economic development. NEPAD's overall vision for agriculture seeks to maximize the contribution of Africa's largest economic sector to the achievement of self-reliant and productive economies. In essence, NEPAD aims for agriculture to deliver broad-based economic advancement, to which other economic sectors, such as manufacturing, petroleum, minerals, and tourism, may also contribute in significant ways, but not to the same extent as agriculture.

CAADP, as a common framework for agricultural development and growth for African countries, is based on the following key principles and targets:

- the principle of agriculture-led growth as a main strategy to achieve the Millennium Development Goal (MDG) of poverty reduction;
- the pursuit of 6 percent average annual agricultural growth at the national level;
- the allocation of 10 percent of national budgets to the agricultural sector;
- the exploitation of regional complementarities and cooperation to boost growth;
- the principles of policy efficiency, dialogue, review, and accountability;
- the principles of partnerships and alliances to include farmers, agribusiness, and civil society communities; and
- implementation principles that assign roles and responsibilities for program implementation to individual countries, coordination to designated regional economic communities (RECs), and facilitation to the NEPAD Secretariat.

CAADP identifies four major intervention areas, or pillars, to accelerate agricultural growth, reduce poverty, and achieve food and nutrition security:

- Pillar I: extending the area under sustainable land management and reliable water control systems;
- Pillar II: improving rural infrastructure and trade-related capacities for market access;
- Pillar III: increasing food supply, reducing hunger, and improving responses to food emergency crises; and
- Pillar IV: improving agriculture research and technology dissemination and adoption.

Pillar II Agenda and Objectives
The ultimate objective of Pillar II is to accelerate growth in the agricultural sector by raising the capacities of private entrepreneurs, including commercial and smallholder farmers, to meet the increasingly complex quality and logistics requirements of domestic, regional, and international markets, focusing on strategic value chains with the greatest potential to generate broad-based income growth and create wealth in the rural areas and the rest of the economy. The pillar agenda focuses on policy and regulatory actions, infrastructure development, capacity-building efforts, and partnerships and alliances that could facilitate smallholder-friendly development of agricultural value chains to stimulate poverty-reducing growth across African countries.

Key Pillar Strategic Areas
Actual implementation of the agenda under Pillar II is to be carried out through the following main clusters of activities, or strategic areas, guided by the vision described:

- *Area A:* raising competitiveness and seizing opportunities in domestic, regional, and international markets;
- *Area B:* investment in commercial and trade infrastructure to lower the cost of supplying domestic, regional, and international markets;
- *Area C:* value-chain development and access to financial services; and
- *Area D:* strengthening the commercial and technical capacities of farmer organizations and trade associations.

BOX 2

Strategic Area C — Value-chain development and financial services: Core program components

1. **Levers for agricultural enterprise growth and value-chain development**
    a. Targeted actions on country- and sector-specific determinants of agribusiness enterprise growth;
    b. Priority interventions that raise the value accruing to actors at each level of the chain focusing on:
        i. Unit cost reduction;
        ii. Volume expansion; and
        iii. Product value addition.
2. **Financial services sector development for value-chain growth**
    a. Development of adapted credit information systems;
    b. Creation of new and strengthening of existing regulatory mechanisms for collateral enforcement;
    c. Provision of training and other capacity-building mechanisms to improve risk perception and thus reduce the barriers to as well as cost of borrowing;
    d. Mobilization of nonbank financial institutions (insurance, pension funds, microcredit systems) to ease access to long-term investment funds and expand financial services in rural areas;
    e. Enhancement of agribusiness enterprises' capacity to improve business reporting and provide satisfactory documentation in support of loan applications; and
    f. Enhancement of banks' capacity to provide affordable, flexible, and innovative financial products that meet the varied needs of AREs.
3. **Sector policy and governance**
    a. Stable and well-balanced exchange rate, monetary, and fiscal policy regimes; and
    b. Conducive bank regulations, business and trade taxation, regulation of business start-up and closing, legal compliance of business operations, employment laws, and contract enforcement.

Technical Lead Institution CAADP for Pillar II
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PARTNERSHIPS IN SUPPORT OF CAADP

NEPAD
A Programme of The African Union