The state of the agri-SME sector - bridging the finance gap briefing

The workshop, hosted by SAFIN and co-organized by CASA, took place in March 2022. This CASA video digest contains the presentations by Jérôme Van Innis, Senior Manager at ISF Advisors and lead author of the report.

Current state of the sector: a long-term change agenda

Policymakers and capital providers recognize the need for improving agri-SME's access to finance, so that they can scale and support local food value chains.

A significant gap remains between the demand for and supply of finance, exacerbated by; a lack of understanding of risk in financing institutions, low levels of collaboration between lenders and the lack of a pipeline of investment-ready agri-SMEs.

New funding structures and specialized financial intermediaries now complement the local financing landscape of lending programmes, but they don't yet fully deliver the necessary funding to unlock the sector's potential.

Meeting agri-SMEs capital requirements

In sub-Saharan Africa, an estimated 130,000 agri-SMEs are seeking $90bn of finance, whilst in South East Asia (excluding India) there are around 90,000 agri-SMEs seeking $70bn of finance. Collectively $54 funding is supplied, mainly by commercial banks. There is a $106bn gap between the demand and supply of capital for agri-SMEs in these two regions.

Funding requirements for SMEs focus on:

- Sustaining current growth – acquire goods and services, maintain inventory & support the trading cycle
- Accelerating growth to achieve the market potential – expanding assets and/or improving productivity
- Building resilience while innovating to adapt to the changing environment

Demand for capital varies depending on the enterprise's growth potential and ambition, with static enterprises; traditional business that enable markets; and dynamic enterprises that transform markets seeking different kinds and volumes of finance.

Capitalizing on financial service providers and blended finance as a tool to unlock agri-SME finance

Blended finance can help de-risk early-stage venture funds, leverage local and regional funds, provide niche funds.

(e.g. climate adaptation funds) or work through intermediaries to create large pools of capital for multi-faceted agricultural funds.

DFIs operate like private investors, only innovating off -balance sheet. Aid and philanthropic investors provide catalytic capital to mobilize DFIs, or innovative finance structures or products.

A dynamic approach to understanding the agri-SME demand for finance

At the top of the market, innovative agri-tech and high growth agri-SMEs' are funded via private equity, venture capital, non-banking financial institutions, and commercial banks. At the bottom, low-growth agri-SMEs rely on informal finance, as they are often not able to access or service commercial loans. In between, and making up the majority of the market, there is sub-commercial financing where social lenders and impact investors provide lower cost capital through blending finance and other de-risking tools.

Only 5% of climate finance for agri-SMEs comes from private sources, mainly grants or concessional debt.

Of the $20bn global; $5bn gets to agri-SMEs in South East Asia and sub-Saharan Africa. Only $700m gets to value chain actors in these regions.

The report recommends four change priorities:

Change priority 1 *Intentionally growing larger numbers of agri-SMEs into commercially investable prospects to anchor local bank markets for finance:*

- Growing agri-SMEs within specific markets
- Closing the long-term debt and local equity finance gap
- Ensuring government support and consistent agricultural development policy

Change priority 2 *Developing capacity, incentives, and infrastructure for local banks and funds to profitably serve smaller, less commercial agri-SMEs over time:*

- Fostering more local coordination and more effective investment intermediation
- Providing intentional long-term subsidies
- Building on the potential of agriculture technologies

Change priority 3 *Making blended finance more efficient & effective:*

- Developing a more sophisticated view of the market and shared learning agenda
- Catalysing new commitments by leading donors, DFIs/IFIs, and public development banks to promote transparency, collaboration, and commitments to smarter subsidies
- Establishing more consistent taxonomies, data, and reporting requirements

Change priority 4 *Building the infrastructure around climate finance:*

- Developing new models and taxonomies for investment strategies and reporting
- Motivating large donors to create a viable pipeline at scale
- Integrating climate expertise into all channels of agri-SME finance

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