The Agricultural Finance Situation in Uganda – Documents Review Findings

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Objectives

- Documenting experiences of agricultural financing in Uganda
  - Successes
  - Failures
  - Reasons for successes and failures
- Identifying demand-related hindering factors
- Identifying supply-related hindering factors
- Making recommendations on how to improve the agricultural finance situation.
Approach and Methodology

- Extensive review of existing documents on agricultural finance
  - Donor projects’ reports
  - Financial institutions’ reports
  - Workshops’ presentations
  - Other publications
- Contacts for verification, validation and updating of documented information.
- Synthesizing and consolidating the information.
Perspective for functioning finance

Borrowers and Lenders Needs

BORROWERS
- Priorities
- Price
- Capacities
- Timing

LENDERS
- Priorities
- Price
- Capacities
- Timing

APPROPRIATE
LOAN
PRODUCT
Findings – Demand side

- Generally low levels of production – operation scale
  - Constrain market access
  - Constrain realization of strong producer groups that can facilitate effective linkages
- Reasonable flow of finance to non-production value chain actors (though largely considered to be non-agricultural finance)
- Other than high value commodities, access to production finance is highly constrained
  - Fungibility problem
- Qualified demand for many commodity value chains
  - IRR greater than Interest rates
Findings – Demand side Continued

- Agribusinesses are conscious of cost, timing and convenience while accessing finance
- Not only credit but full menu of financial services
- Poor track record of past performance
- Unwanted collateral
- Strong producer groups influence access
- Production and market risks
- There are unexploited linkage opportunities
- No third party risk mitigation for production
  - Producers bear full risk of their operations
Findings – Supply side

- Myriad of financial service providers but fewer engaged in agricultural financing
  - Commercial banks
  - Development banks
  - Finance companies (Tier 2)
  - MDIs
  - MFIs
  - SACCOs
  - Others (mainly self-help groups)
- Financial institutions’ cardinal role
  - Maximize profit
  - Minimize cost
  - Seek to achieve these through the 5Cs
Findings – Supply side Continued

- Agricultural lending risk perception is very high
  - Taking a narrow view (agriculture = production)
- Constrained skills for agricultural lending and limited outreach capacities
- Some FIs not consciously engaging in agricultural lending
- Costs of lending are of crucial concern
  - Need cluster of mass producers/actors
  - Recovery through third parties
- Largely inappropriate financial products for specific value chains (structuring)
Findings – Supply side Continued

- Regulatory requirements impact lending to agriculture
  - Quality of loan assets
- Impact of alternative low risk and low cost opportunities (TBs)
- Limited products diversification for agriculture
  - Warehouse receipt system
  - Invoice factoring
  - Inventory credit
- Relative low competition in the financial market
- Opportunities for alternatives for collateral
  - Guarantee programmes
Findings – Supply side Continued

- Conducive policy environment
  - Addressing demand-side constraints
  - Legal aspects for financial products
  - Incentives for financial institutions
    - GoU Guarantee
    - Agricultural credit fund (UGX 30B)
    - Fiscal incentives
- Constrained access to third party risk mitigation for agricultural lending
  - High risk ranking for agricultural clients
- Fiscal incentives for value chain actors
Fig 6: Share of Borrowers by Economic Activity

- Commerce: 72%
- Crop Production: 9%
- Animal Husbandry: 4%
- Manufacturing: 3%
- Services: 11%
- Agro Processing: 1%
Cases in Agricultural Finance

- Working capital for production
  - Maize production credit (esp. Kapchorwa)
  - Smallholder tea growers in Kayonza
  - Sugar cane outgrowers for Kinyara
  - Generic production credit – Kyamuhunga SACCO, Pearl Microfinance, Centenary Bank

- Finance for Marketing
  - Warehouse receipt system for maize – Stanbic
  - Warehouse receipt system for coffee
  - Crop finance for maize (Masindi area)
  - Many financial institutions are interested
Factors for success

- Proactive lending approach
- Demand-driven lending and good borrower attitude
- Presence of strong and focused producer groups/associations
- Appropriate loan products – developed with TA support
- High intensity of capacity building for both borrowers and lenders
- Effective monitoring of loans
Cases in Agricultural Finance – Cont.

- Factors for successes (Cont.)
  - Critical mass of clients (low cost)
  - Leveraging with borrower equity
  - Timely appraisal and disbursement
  - Focus on commodities with good and stable market
  - Opportunities for structured trade finance products
  - Linkage banking opportunities
Cases in Agricultural Finance – Cont.

- Factors for successes (Cont.)
  - Developing partnerships/collaboration
  - Lack of side-selling opportunities
  - Guarantees
  - Effective finance mediation
Term finance products

- Gaining good ground in the finance market
  - Term loans
    - equipment/asset loans
    - Non-asset term working capital for term value chain activities
  - Asset leasing
    - Production and post production equipment
    - Both micro and big assets
- Mainly by commercial banks (DFCU, Stanbic, EADB, Centenary bank, Equity), but also non-commercial banks (Faulu is very interested)
Issues for term finance

- Access to term liabilities and compliance with regulatory pressures, and limited opportunities to raise term liabilities
- Structuring of term finance products
- Inappropriate categorization of loan products
- Failure to analyze value chins
- Lack of secondary market is limiting leases to finance leases only
- Challenges of skills and assets maintenance
Strategic challenges

- Demand side challenges
  - Increasing productivity
  - Surmounting collateral dilemma
  - Realizing strong producer groups
  - Market linkages and contract production
  - Agribusiness management BDS
  - Finance mediation
  - Smoothening incomes of smallholders

- The focus should be on making the actors bankable
Strategic challenges

- Supply side challenges
  - Product development support
  - Skills enhancement
  - Identifying new opportunities and marketing them to financial institutions; role of financial value chain mapping and analysis
  - Support for replication of successful products
  - Ensuring effective outreach
  - Increasing access to offsetting liabilities
  - Risk mitigation mechanisms development
Value chain approach for market opportunities
Strategic challenges

Policy Challenges
- Reviewing and amending relevant laws
  - Leasing law
  - Warehouse
- Enforcement of contracts to diversify collateral options
Strategic challenges

- Other challenges
  - Fertiliser usage
  - Strategic government interventions to protect value chains
  - Regulatory reviews to increase the flow of finance to agriculture
    - Mobile banking
    - Agencies and satellite branches
    - Other low cost-delivery mechanisms
Strategic challenges

- Technical assistance coordination
- Commitment by financial institutions and government to increase agricultural finance
  - Deliberate efforts to increase portfolio targets
  - Pressure on financial institutions
  - Government commitment to agriculture in the national budget
## Sectoral shares in the national budget

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Conclusions

- Improving the agricultural finance situation in Uganda is highly feasible but will require coordinated efforts of all the interested stakeholders.
- There is no need of placing and shifting blame.
  - Financial institutions are there to make profits and avoid risk.
- Risk mitigation options have proved to be effective and need to be enhanced and diversified.