Financial Inclusion via Agriculture Value Chains

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Australia-Indonesia Partnership for Rural Development

• The Government of Indonesia has partnered with the Government of Australia (AIP-Rural).

• The long-term goal is to improve the income of at least 1m poor men and women smallholder farmers in five provinces in Eastern Indonesia by 2022.

• AIP-Rural is focused on market based development aimed at improving agricultural competitiveness and access to markets, better inputs, know-how and technology.

• Of the projects being implemented under AIP-Rural, PRISMA is the largest, primarily focused on agricultural value chains, targeting 300,000 farmers by the end of 2018.

• The fourth, SAFIRA, focuses on agriculture value chain financing to expand access to finance for 12,000 farmers.
Key Driver: Indonesia Lending to Agriculture is Low as a Proportion of Total Lending

<table>
<thead>
<tr>
<th>Sector</th>
<th>Commercial Banks</th>
<th>Rural Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade</td>
<td>19.46%</td>
<td>12.71%</td>
</tr>
<tr>
<td>Processing...</td>
<td>25.65%</td>
<td>1.27%</td>
</tr>
<tr>
<td>Agricultures</td>
<td>6.06%</td>
<td>6.21%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>4.54%</td>
<td>2.44%</td>
</tr>
<tr>
<td>Construction</td>
<td>4.38%</td>
<td>2.41%</td>
</tr>
<tr>
<td>Transportat...</td>
<td>4.38%</td>
<td>1.89%</td>
</tr>
<tr>
<td>Financial...</td>
<td>4.09%</td>
<td>4.09%</td>
</tr>
<tr>
<td>Other sectors</td>
<td>59.98%</td>
<td>38.71%</td>
</tr>
</tbody>
</table>
AgriFinance as % of Total Lending is Even Lower in Eastern Indonesia
It is Not Due to a Lack of Financial Institutions

<table>
<thead>
<tr>
<th>Type of FIs / Numbers</th>
<th>East Java</th>
<th>NTT</th>
<th>NTB</th>
<th>Papua</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial Banks</td>
<td>85</td>
<td>17</td>
<td>29</td>
<td>19</td>
</tr>
<tr>
<td>Sharia Banks</td>
<td>36</td>
<td>na</td>
<td>8</td>
<td>na</td>
</tr>
<tr>
<td>Rural Banks</td>
<td>325</td>
<td>11</td>
<td>32</td>
<td>6</td>
</tr>
<tr>
<td>Co-operatives (of which, Credit Unions with &gt;1000 members)</td>
<td>27,140</td>
<td>2,818</td>
<td>2,283</td>
<td>1,784</td>
</tr>
</tbody>
</table>
There are Farmer Demand and Supply Side Constraints

*Demand side barriers* include:

- land title;
- a lack of collateral generally;
- poor financial literacy and product knowledge;
- the small loan sizes needed; and
- the prevalence of informal structures.

On the *supply side*, there is:

- a lack of knowledge on the part of the FSPs;
- an undiversified and untailored product range;
- a lack of liquidity;
- high costs;
- inadequate risk management capacity and availability of risk mitigation eg insurance.

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**SAFIRA**

*Strengthening Agricultural Finance in Rural Areas*
The Solution: Use Farmers’ Relationships as Assets
Value Chain Finance (VCF)

• VCF is made possible by value chain relationships and mechanisms.

• It is used primarily to reduce:
  • lending risks by leveraging relationships as assets, and/or
  • transaction costs of lending by using value chain actors as loan assessors, distributors or collectors for financial services.

• The rationale for these types of financing arrangements is that, when properly constructed, they are profitable for and beneficial to:
  • providers of financial services (e.g. banks),
  • their customers (e.g. seed producers, processors, buyers), and
  • farmers.

• VCF is a method that has been used successfully worldwide and there are many examples in Indonesia.
Sample VCF 3, 5 and 6: Maize Farmers in NTB
Sample VCF 4: Sugarcane Farmers in East Java

PTPN X/Sugar Mill
- Provide list of good farmers to the Bank
- Receive harvest from farmer
- Payment to farmer via the farmer’s account at the Bank

Bank
- Loan analysis
- Disburse PKBL loan
- Deduct the harvest payment from the account

Sugarcane Farmers
- Submit necessary loan documentation to bank
- Submit the harvest to Sugar Mill
What SAFIRA offers for VCF

• SAFIRA seeks to introduce more rural banks and financial service providers to the agricultural sector and develop their competencies to take advantage of the opportunities that VCF can provide.

• SAFIRA also assists value chain actors to:
  • interact more effectively with financial institutions,
  • deliver credit to smallholder farmers more efficiently, and
  • facilitate the growth of their businesses through expanded outreach.

• This is done through capacity building and technical support, provided for free by SAFIRA under an MOU with our partners.

• Essentially, SAFIRA aims to replicate and expand the VCF models existing in Indonesia and from overseas.
AIP-Rural Survey on Financial Inclusion and Access

• The key goals of SOFIA are, like a Finscope study, to:
  • Measure and profile levels of access to and use of financial services, and
  • Make this information available for use by key stakeholders such as policy-makers, regulators and financial service providers.

• SOFIA will:
  • Measure the levels of financial inclusion in Eastern Indonesia,
  • Determine the needs for financial products in general, with particular emphasis on the agricultural sector, and
  • Describe the landscape of access, i.e. the type of products and services used by financially included individuals, and the gap with supply.

• AIP-Rural is considering extending the survey to other provinces and deepening the analysis in certain districts.
Thank you

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