

Opportunities, Challenges and Evidence Needs for Investing in Smallholder Farming

CASA Research Brief 01



Executive Summary

Commercial Agriculture for Smallholders and Agribusiness (CASA) is a flagship programme financed by the UK Department for International Development (DFID), which seeks to increase economic opportunities for smallholders to step and trade into growing commercial markets. The programme aims to increase investments in agribusinesses which source from smallholder farmers and to generate new evidence and research that amplifies the case for doing business with smallholders.

During the inception phase, CASA conducted a survey of 25 investors and investing support stakeholders, to determine key constraints, opportunities and evidence needs for unlocking investment opportunities in agribusinesses and smallholder farmers globally, and to identify information needs and seeking behaviours. The three top constraints identified were: limited availability of investable agribusinesses; low productivity of smallholder farmers; and existing gaps in infrastructure and value chains. The main opportunities for increased investment are: investing and improving infrastructure; incubating and supporting early stage businesses with donor funding and technical assistance; and supporting shareholder services like aggregation and mechanisation initiatives. The main evidence gaps identified through the survey are: case studies and examples of profitable and impactful business models; a mapping of actors involved in agricultural finance; and crop and country specific data on productivity and impact.

Despite the widespread agreement on the key issues, the survey also identified divergent opinions: inappropriately applied grants and donor subsidies create uneven competition for commercial investors and can harm value chains, while less commercial investors emphasised the importance of these subsidies for de-risking their investments. There was agreement among investors that technical assistance needs to be used appropriately and not to finance operations, while this observation was not mentioned by investment support stakeholders. Additionally, having a minimum ticket size was mentioned by investors as a critical factor, while this was not such a priority for investment support stakeholders.

One of the main priorities emerged from this survey, and with the aim of achieving additionality of existing investments, would be to produce a map of investors, types of investment and support service in specific countries, as well as a list of investable agribusinesses. This resource could potentially be co-financed and shared by investors targeting smallholder agribusinesses, which would help them reduce the time and cost needed to identify direct and indirect investment opportunities. New partnerships with on-the-ground networks combined with technical assistance, incubators, and grant funding would also help reduce some of the current risks related to investing in smallholder farmers and agribusiness.



Context and Objectives

CASA aims to bridge evidence gaps and to ensure investors and policymakers have access to information and relationships to inform their decisions. CASA's Investor and Investment Support Stakeholder Survey had the following learning objectives:

- Ascertain the main constraints and opportunities for catalysing smallholder investments;
- Determine the key evidence needed to reduce perceived risks for investment; and
- Identify partnerships, key influencers, and preferred communication channels.

Methodology

CASA defines investors as: "individuals or organisations that directly invest their own capital into a person, group, SME or bigger enterprise with the aim of either directly receiving financial returns or having a positive social or environmental impact". This survey sampled investors from four out of the six subcategories of investors developed by the programme:

- Impact investors: mission-driven funds investing in smallholders and agribusinesses;
- Commercial Lenders: financial institutions providing loans to smallholders or cooperatives;
- International Finance Institutions: bilateral development finance institutions government-backed funds which provide early stage seed capital or concessionary loans alongside capacity-building support and do not seek a commercial return; and
- Venture Capital and Private Equity: venture capital and private equity investors investing in agribusinesses and smallholders.

Local institutional investors (pension funds and insurance companies based in the local market, often government-owned) and global institutional investors (pension funds, insurance companies, hedge funds and mutual funds looking for investable opportunities worldwide) were not prioritised for this survey. The Investor selection criteria were the following:

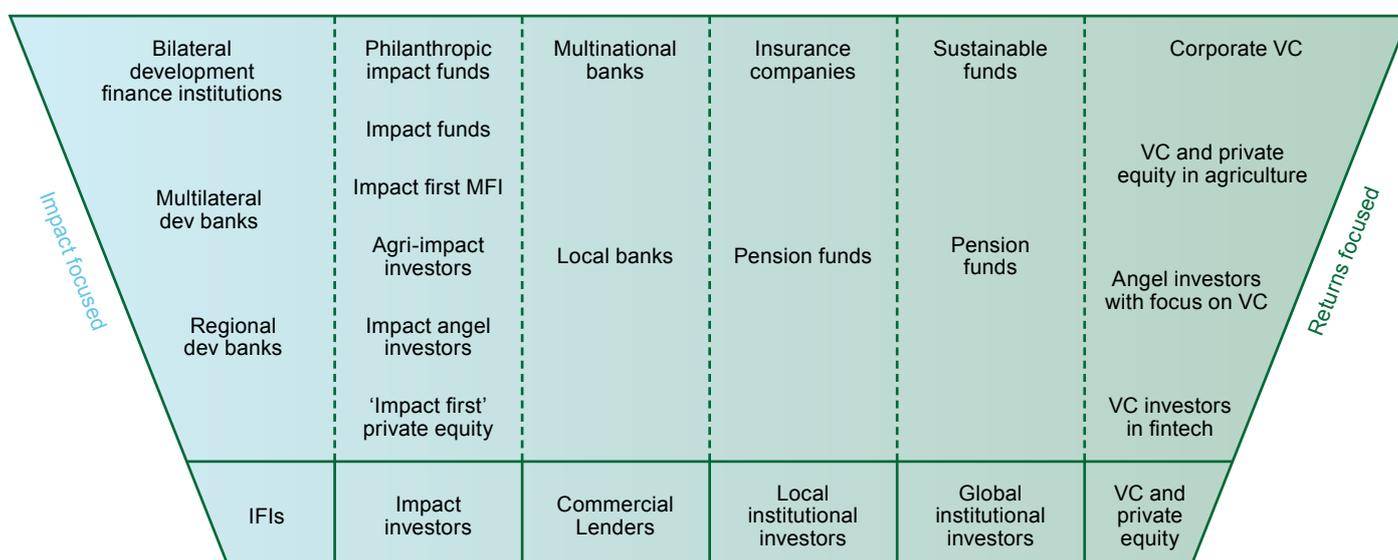
- Focus on Agribusiness and Smallholders: investors selected needed to invest in smallholders either directly (e.g. cooperatives and producer organisations) or indirectly (e.g. through SMEs providing services to smallholders); and
- Geography: investors interviewed included those with global missions as well as those specialised in Africa, Asia, and Latin America.

CASA defines Investment Support Stakeholders as: "individuals or organisation that offer a support function to direct capital investments from investors with the aim of improving efficiencies and overall functioning of industries and sectors". The type of support can range from development and promotion of knowledge, policies and regulations, provision of inputs, producer groups or development of platforms for increased trade and market access.

The Investment Support Stakeholders criteria were:

- Focus on Agribusiness and Smallholders: organisations selected provide support to smallholders in a range of ways (e.g. business incubation or enabling market access);
- Geography: organisations selected have a mixture of global programmes and more geographically-focused activities (e.g. Africa); and
- DFID programmes: those with an agribusiness focus and likely to generate investment insights, particularly those with wider outreach.

Figure 1. Investor Categories



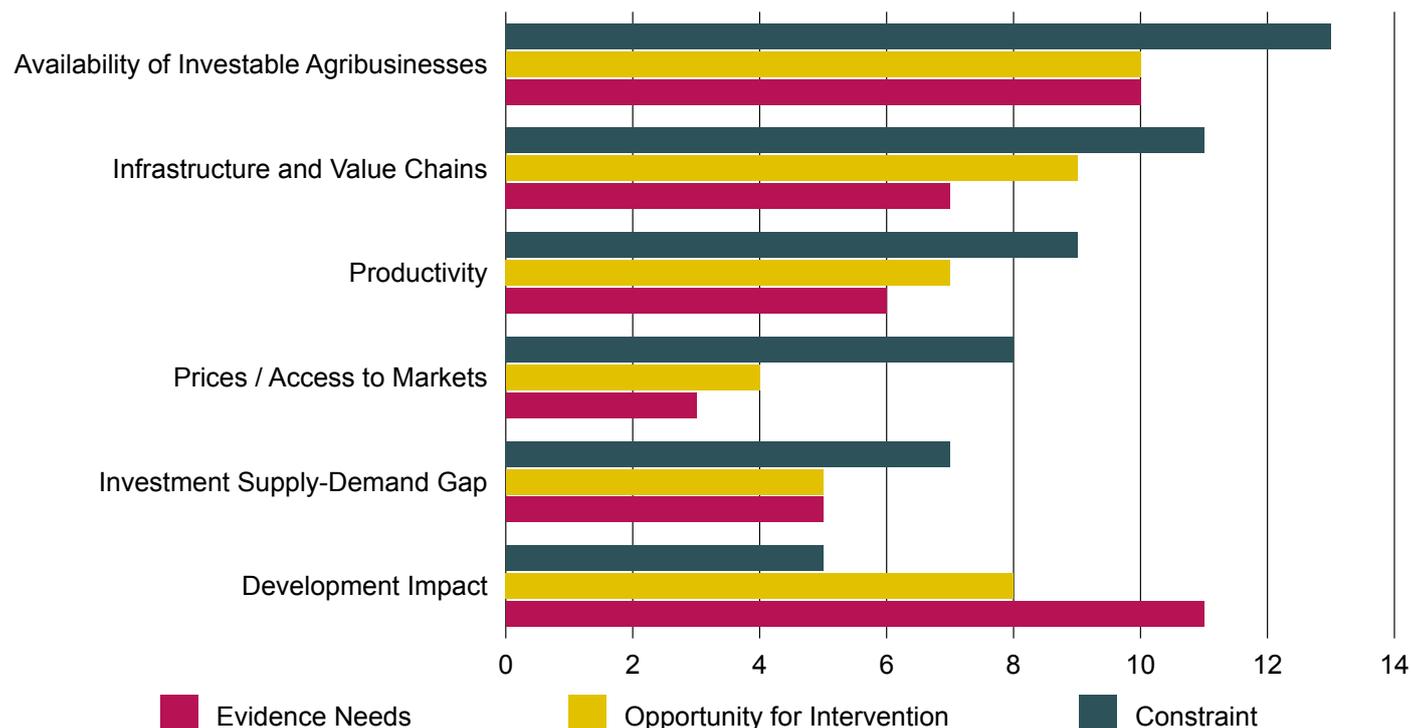
Key Findings from Interviews

Through the course of the interviews several recurring themes appeared, summarised in the following chart. Patterns emerged across these themes, namely focused on aggregation, mechanisation, and smallholder-adjacent activities.

Investors and investment support stakeholders identified similar constraints and opportunities. This is perhaps not surprising, given that the investment support stakeholders were selected largely on the basis of their

close links with investors and their focus on creating an enabling investment environment. The most striking difference between investors and investment support stakeholders was their perspective on competition for deals. While investors highlighted the limited number of deals of sufficient size and investability, investment support stakeholders were making the point that some investors (particularly DFIs) could create a stronger pipeline of investable companies through patient pre-commercial funding.

Figure 2. Key Themes Cited by Investors



Availability of Investable Agribusinesses

Constraints	Opportunity	Evidence Needs
Lack of investable business models	Incubators and technical assistance for business plan development	Database of crops / sub-sectors relevant to smallholders showing the range of returns achieved
Limited management capacity	Ongoing technical assistance for management	Pre-investment technical assistance needs
Small investment size is uneconomic for due diligence and carries greater risks	Aggregation	Case studies of where aggregation has been successful

Constraints: Lack of **investable business models** and **limited management capacity** of agribusinesses, including unsustainable or inadequate business plans limit the amount of deals. **Small ticket sizes** (lower than \$ 500,000) are also a barrier to investment, given that smaller transactions tend to be riskier and to require co-investment. **Forex risk** and lack of **local presence** also pose constraints to investment and achieving higher volumes of deals.

Opportunities: **Incubator programmes, seed capital, and technical assistance** can contribute to increasing the pipeline of investable smallholder agribusinesses.

Improving business literacy and management skills through technical assistance is also critical and it **should be provided by local experts**. Technical solutions enabling efficient **aggregation** would help address the constraint of inadequate scale.

Evidence Needs: There is a limited amount of successful case studies available, since geographical and value-chain differences make overarching models difficult to replicate, **a library of country-specific and crop-specific case studies** (particularly on export-commodities) would bridge existing evidence gaps.

Infrastructure and Value Chains

Constraints	Opportunity	Evidence Needs
Inadequate infrastructure in rural areas	Financing new infrastructure technologies	Measure and communicate the impact of improvements in infrastructure
Lack of industry associations for farmers' agency and cross learning	Learn from the way associations operate in other sectors	Data on the role of associations in other sectors

Constraints: Investment in wider **infrastructure such as energy, transport, and communications in rural areas** is critical to increasing the productivity and viability of smallholder farmer activity, although these kinds of investments are less appealing to impact investors seeking personal stories. **Soft infrastructure support, like industry associations and knowledge sharing networks**, are also important for socio economic empowerment of smallholder farmers.

Opportunities: **New technologies**, such as waste to energy and new communications technologies, and **creating a more engaging narrative around the impact of basic infrastructure**.

Evidence Needs: The evidence needs that were proposed in this area were mainly about the principal infrastructure gaps facing smallholder farmers in particular geographies.

Productivity

Constraints	Opportunity	Evidence Needs
Low productivity limits the capacity of smallholders to achieve adequate incomes	Smallholder support services (e.g. value chain management, aggregation, insurance, & technical assistance)	Data on regional and crop-specific yields
	Agriculture technology and equipment leasing	Indicative baseline and endline yields

Constraints: **Low productivity and the associated low profitability** of smallholder farming makes it difficult for smallholders to achieve adequate incomes and diminishes their bankability. Smallholders' relatively low productivity makes most smallholder crops **uncompetitive in global markets** when compared to corporate conglomerates.

Opportunities: **Smallholder support services** from macro-level value chain management to aggregation enterprises to highly customised technical assistance; **Crops that do not require mechanisation; Accessible**

agriculture technology like mechanisation, climate-optimised inputs; Small **equipment leasing**; Crop and climate **insurance**; and **Fintech**.

Evidence Needs: **Data on regional and crop-specific yields**, including **indicative baseline and end-line yields** for specific financeable interventions would help them determine the feasibility of prospective investments. A **network of on-the-ground consultants** with the knowledge and experience to conduct or assist with thorough due diligence.

Prices and Access to Markets

Constraints	Opportunity	Evidence Needs
Low prices at the farmgate reduce profitability	Aggregation and premiums paid for sustainably sourced foods	Country and crop specific case studies with evidence of positive financial returns
Gaps in the value chains prevent farmers from capitalising on value addition	Financing storage and processing facilities	Quantitative data on how integration into value chains benefits smallholder farmers
Inability to meet standards of formal and regulated markets	Aggregation and macro-level value chain management	

Constraints: Low productivity and **low prices** result in **low profitability** for smallholder farming. **Lack of access to markets** and **gaps in the value chains that prevent smallholders from benefiting from value adding activities** (e.g. storage and processing facilities). **Inability to meet the standards of formal and highly-regulated markets**, including cost-barriers to relevant certifications.

Opportunities: **Aggregation**, also supported by digital solutions and social networks, combined with **consumer's preferences for sustainably-sourced foods** (premium prices) could help counteract artificially low market prices.

Macro-level value chain management and government led market building could increase smallholders' viability on a larger scale.

Evidence Needs: **Quantitative data on how integration benefits smallholder farmers** and a library of country-specific and crop-specific **case studies** of achievable positive financial returns. **Increased availability of climate and market information**, particularly through digital solutions, also presents an opportunity to achieve better market outcomes.

Investment Supply-Demand Gap

Constraints	Opportunity	Evidence Needs
Excess of financing for few investable agribusinesses	Technical assistance & seed funding to increase pipeline of investable agribusinesses	Database of investable businesses done with in-country stakeholders
Market distorted by grants and subsidies	Ensure additionality of donor money	Types of commercially viable activities

Constraints: Excess of financing available to a small number of investable enterprises, particularly in Africa, where less commercial investors (e.g. DFIs) are focused, which creates unsustainable financing models. **Inappropriately applied grants and subsidies distort the markets** and harm value chains (e.g. technical assistance used to finance operations).

Opportunities: Ensuring the **additionality of donor money**, like subsidies or grants, to facilitate higher-level interventions. Need for **patient pre-commercial funding to help to grow the pipeline of investable enterprises**, although more clarity is required on where the private sector can intervene and therefore where public money could potentially crowd it out.

Evidence Needs: A mapping of actors involved in **agricultural finance and adjacent activities** (such as infrastructure), would be needed to demonstrate and avoid overlap, find partnerships for syndications, and help certify investor's own value-added to the market. The **market needs to be more clearly segregated by commerciality** (e.g. enterprises that can be supported with commercial funding, those which require concessional seed funding to become commercially-viable, and those which might never be appropriate for commercial investment). This would reduce market distortion of commercially viable enterprises/business lines and ensure additionality for donor money.

Development Impact

Constraints	Opportunity	Evidence Needs
Difficulty in measurement , determining methodologies, and high associated costs	Social impact is a key motivation for investors to assume the risk of investing in smallholders and agribusiness	Impact measurement data and assistance in collecting inputs and determining reporting methodologies

Constraints: Impact is difficult to measure by impact-seeking investors due to the lack of methodological knowledge and pre-investment costs needed for conducting baselines for impact evaluation.

Opportunities: **Development and social impact are two of the greatest opportunities of smallholder finance** and an essential motivator for anyone active in this segment of the agribusiness sector. Successful investments targeted at smallholders can contribute to decreasing global poverty, addressing food security issues, increasing employment and improving livelihoods, improving the sustainability of consumption, and reducing inequalities.

Evidence Needs: Investors need **impact measurement data and technical assistance**. This evidence would vary between types of investors but could include baseline data across a range of high-level impact metrics (e.g. yields, income and productivity) for each crop and country as well as macro-level data such as export volume. Technical assistance would include the provision of services to impact investors on conducting baselines and evaluating the impact of specific investments.

Cross-theme Patterns and Divergent Opinions

Aggregation is an essential component to increasing smallholder investment. Investors and investment support stakeholders agreed that providing and improving existing shareholder and shareholder adjacent services, since many of these services are already investable, would be critical to improving the outputs and prices received by smallholders.

Commercial investors highlighted that **inappropriately applied grants and donor subsidies create uneven competition for commercial investors and can harm value chains**, while less commercial investors emphasised the importance of these subsidies for de-risking their investments. However, there was agreement among investors that technical assistance needs to be used appropriately and not to finance operations, while this observation was not mentioned by investment support stakeholders. There were also slight **differences of opinions with regards to the investment size**, this being a crucial factor for investors and not so often mentioned by investment support stakeholders.

All investors highlighted the **time and resource consuming nature of identifying investable agribusinesses, potential partnerships and technical assistance providers** to inform their investments and maximise additionality. This activity, which is generally conducted by the investors in isolation, could potentially be coordinated by CASA and co-financed by a number of investors, which would help maximise efficiencies, minimise costs and ensure additionality of investments, while unlocking funds for increasing the pipeline of investable agribusinesses. The end resource would be a **map of investors, types of investment and support service in specific countries, as well as a list of investable agribusinesses.**





DFID's Commercial Agriculture for Smallholders and Agribusiness programme (CASA) makes the commercial and development case for investing in agribusinesses that source produce from smallholders. It does this by bridging evidence gaps and by ensuring investors and policymakers have access to the right information and people to make inclusive agribusiness models succeed.

CASA is a consortium of organisations (CABI, NIRAS, Swiss Contact) working with associate partners (iied, Malabo Montpellier Panel and TechnoServe).

The Investor and Investment Support Stakeholder Survey and Research Brief have been conducted by CABI in collaboration with Innpect and Impact Value.

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