Reflections on the IDH Innovation Forum

Building blocks of successful R&R schemes, key learnings and next steps

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On November 2 and 3, 2015 IDH, the Sustainable Trade Initiative (IDH), together with our knowledge partners Dalberg, IFC, Rabobank and Root Capital organized an Innovation Forum on “Renovation and Rehabilitation” (R&R) of smallholder tree crops. Representatives from the coffee, cocoa, palm oil and tea sectors came together with financial industry and agronomic experts to learn, share and shape approaches to long term investments in R&R projects.

Around 100 participants from 19 different countries contributed to lively discussions on the attributes of success and key building blocks for R&R interventions. While the global need for R&R is vast, the market is in a pioneering phase, therefore the exchange of experience across sectors and geographies was much appreciated.

In this concise report, we would like to share some key emerging insights with you as well as some knowledge questions, which we’ll use to set the knowledge agenda for R&R going forward. Also included are some of the next steps as identified by the representatives of the coffee, cocoa, tea and palm oil sector.

We would like to thank you for your participation in the event and for sharing your experiences. If you are interested in staying engaged on the topic subscribe **here** for our mailing. We look forward to our continued dialogue and partnership in driving the R&R agenda forward and creating real change on the ground to the benefit of smallholder farming communities.

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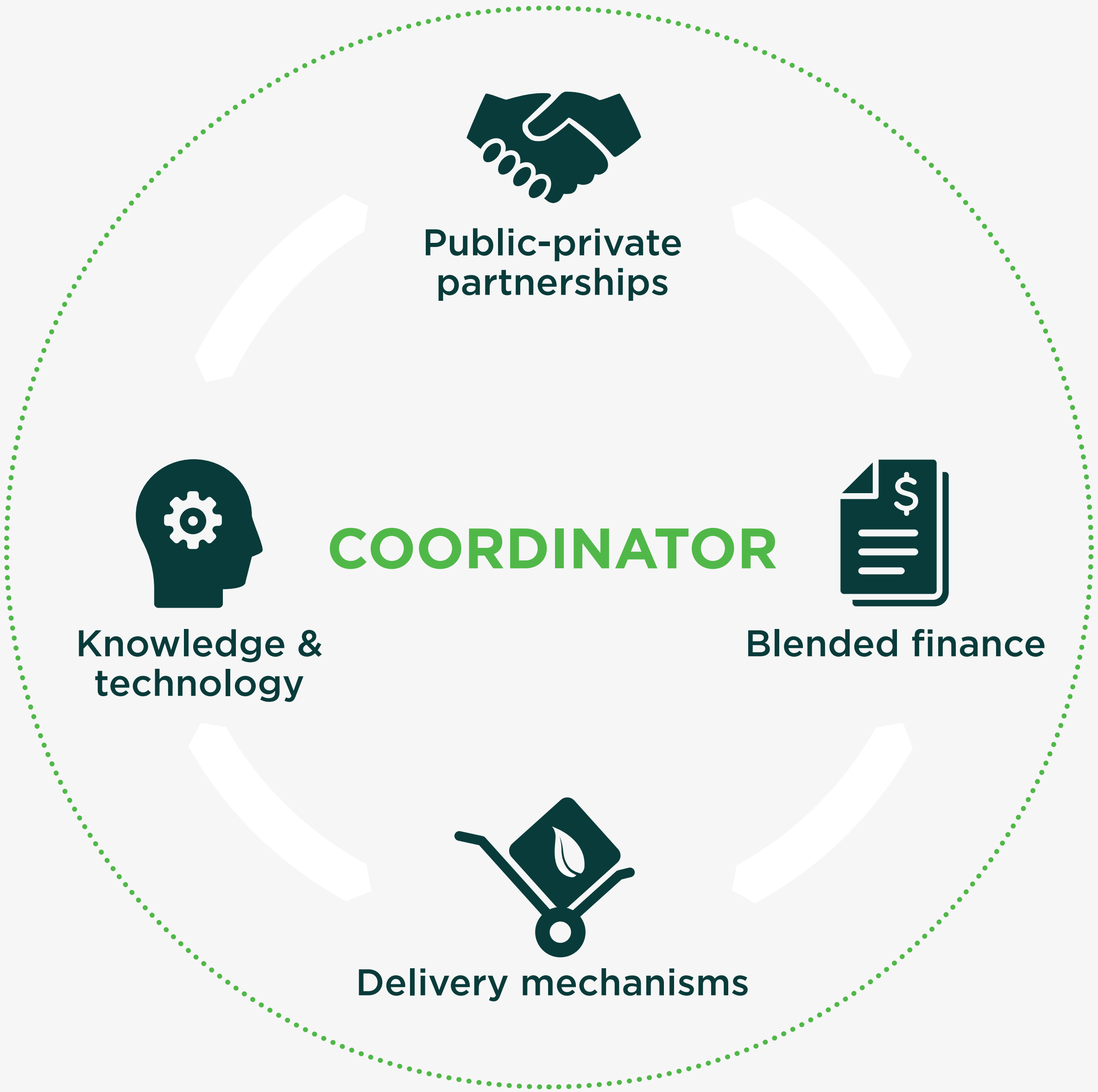
BUILDING BLOCKS OF SUCCESSFUL R&R INTERVENTIONS



BUILDING BLOCK 1:

Public-private partnerships

- Given the risks and uncertainties of R&R, public-private partnerships need to be formed to share knowledge, capacities, costs and risks.
- A strong business case is needed for farmers, industry and government to invest in R&R.
- Farmers need land titles and need to be either self-organized or aggregated to reach scale.
- To incentivize farmers the supply chain industry needs to take leadership and have skin in the game.
- Governments should be able to de-risk investments in R&R through the use of guarantees and subsidies for (local) banks that finance the smallholders.
- Governments are instrumental in creating an enabling environment for sufficient and good quality seed supply and regulation around R&R techniques (like grafting).

Knowledge questions

- How to build a strong business case for investing in R&R for each involved player (farmers, investors, supply chain players, seed suppliers, government etc.)?
- How to create the minimum conditions for R&R investments by farmers (e.g. land tenure)?

Key learnings

- A farmer can best invest in R&R when commodity prices are low since the investments that are needed are lower with low prices and the benfits will come at a period of high prices.
- Governments play a diverse and important role as enabler of successful R&R interventions. They are a player in the provision of extension services, they play a role in the availability and distribution of certified seeds, they create the environment of regulation on R&R techniques and they can support finance mechanisms for R&R. There is a need to better understand how governments can learn of other governments that have set up successful R&R schemes.
- Government subisdies can be a key enabler for smallholder finance for R&R, especially subsidies of interest rates during the non-productive periods (as applied in Colombia and Indonesia).
- You need the public and private sector to reach scale in R&R. Experiences so far show that private extension services and provision of seeds can be effective but have limitations in the total reach of farmers.
- In the examples where R&R interventions were successfully implemented, one organization acted as a “central coordinator”. Such a central coordinator ensures that all the four building blocks are present and act with one common objective. Different types of organizations can play this “coordinator role”; a farmer organization, an NGO, a private sector party, etc.

BUILDING BLOCK 2:
Knowledge & technology

- Before a smallholder decides to invest in R&R, it is crucial that the smallholder applies "Good Agricultural Practices" (GAP) and well maintains his/her plantation. In many cases, technical assistance is needed for farmers to become ready to invest in R&R.
- When a farmer invests in R&R, it is important that the right varieties of good quality planting materials are available and used for the specific soil conditions, and that there is a professional breeding and propagation program in place.
- For all investors, there needs to be data available at farm level (prior to and after the investment in R&R).
- IT systems and mobile technology can play a big role in lowering transaction costs in reaching large numbers of smallholders.

Knowledge questions

- How to best organize farmer data management?
- How to reach/build up capacity to increase the availability of certified seeds and inputs?

Key learnings

- Farmers that do not apply GAP and do not know how to do R&R run a major risk that their investment will not yield as expected and therefore they will not be able to repay their R&R loan.
- A farmer will look at his / her total farming system to decide whether or not to invest in replanting or rehabilitation of their perennial crop. Also non-agricultural opportunities for generating income will be taken into account when taking a R&R investment decision.
- Farmer data management systems are a key condition for successful R&R schemes and a topic where both the private and public sector should cooperate in a pre-competitive way.

BUILDING BLOCK 3:
Blended finance

- Investments in R&R require long term loans including grace periods for the unproductive first period of R&R. These loans are conceived to be risky. Therefore, risk sharing arrangements are crucial to unlock long term finance for R&R.
- Risk sharing arrangements can be set up with support of government, but also with supply chain partners, development finance institutions and donor organizations.
- Risk mitigation measures like phased replanting and guaranteed off-take agreements of buyers play a major role in reducing the high risk finance needed for R&R.
- The transparency of financing schemes is important for both the financer and the smallholder that receives the loan.
- In some cases, corporates are best positioned to support smallholders with R&R services (including finance) since they are closest to the smallholders. In such cases, corporates need to have the capacity to administer the R&R loans.

Knowledge questions

- How to overcome the first years of no / low income for the farmer?
- How to structure risk-sharing partnerships?

Key learnings

- Living costs need to be included in the loan amount to the smallholder. If living costs are not covered, a smallholder cannot invest in replanting since their cash flows will be insufficient to cover their basic needs during the first years of no production.
- There is a need for long term capital for financial institutions which can be used for long term loans that are in line with the period that is needed for smallholders to repay the loan. Besides the duration of the loan, the loan needs to be designed with a grace period for the repayment of the loan during the first years of no production.
- The information gap between supply chain partners and investors needs to be bridged, but investors should also find ways to deal with incomplete data when making investment decisions.
- New risk-sharing partnerships need to formed, in which supply chain partners and donors step in to provide first-loss facilities to de-risk the loans of financial institutions to smallholders..
- There is a need for pipeline developers that create potential deals for the financial institutions. Financial institutions could start at smaller scale with new deals that have the potential to develop into large scale schemes.

BUILDING BLOCK 4:
Delivery mechanisms

- When the infrastructure for developing planting material is present in a country, the logistics to actually distribute the planting material, but also the required extension services and financial services are key. Without these last mile delivery mechanisms, the services do not reach the smallholders.
- Farmer selection and segmentation are key factors for successful R&R interventions. There is a need to understand which farmers are ready for investments in R&R, and how to select them.

Knowledge questions

- How to select smallholders that are ready for R&R investments?
- What distribution mechanisms need to be in place to reach the farmers with extension services, planting material and financial services?

Key learnings

- In the schemes of FNC in Colombia and the scheme of Sinarmas farmer segmentation and farmer selection is being applied. For different types of farmer groups, different service packages are being developed. There is a minimum level of 2 hectares for smallholder palm farmers in Indonesia to be eligible for the R&R support package of Sinarmas.
- Private sector players are testing new ways to get their services to the doorstep of farmers. There is a need to share these experiences in a pre-competitive setting and cooperate with the government for investments in infrastructure.
- It is not feasible to work with all smallholders on R&R since not all of them are technically ready and have sufficient land to make the investments profitable. “Dare to choose” with whom to work was one of the key learnings.

Key highlights from the case presentations

Palm Oil

- Sinarmas has introduced its innovative financing scheme for smallholder palm oil replanting, in which cooperatives play a central role. Local banks are providing funding to cooperatives, which on-lend to the palm oil smallholder. The loans have a five year grace period, cover living costs next to replanting costs, and the **loan interest is subsidized by the government** during the replanting period. The program currently reaches 269 farmers with a total land area of just under 600 hectares.

- SPKS, the Association of Independent Palm Smallholders explained that there is a need for **tailor made support packages** for independent smallholders. Some independent smallholders prefer to replant in a phased approach in stead of one-go.

- In Ghana there was a **subsidy needed of 50% of the costs** in the first year to convince smallholders to replant. After the first year, there were significant profit increases with tripling of productivity.

- The Indonesia Estate Crop Fund described how they are collecting levies on exported palm oil to reinvest in the Indonesian palm oil sector. The Fund can be used for a variety of support measures like subsidizing interest rates for loans to smallholders, **land certification support**, support for seedlings, fertilizer and fire awareness.

- GAPKI, representing 680 members in the palm industry in Indonesia, indicated that independent smallholders are struggling to have **access to good quality seedlings** and lack knowledge about how to develop a good palm oil plantation.

- GPPI, the Planters Association in Indonesia, explained that productivity gaps between smallholders and large-scale plantations are widening. Therefore there is a need for transferring technology to smallholders, for enhancing smallholders to comply with standards and for **capacity building of farmers' organizations**.

- The Advisor of the Governor of South Sumatra made a plea for **"Landscape Management Partnership Models"** in which activities of stakeholders in a landscape are coordinated in order to organize legal issues, access to finance, conflicts in water management systems and fire control.

Tea

The Tea Association of Malawi explained the case for re-investment in the Malawi Tea sector. In order for the tea industry to remain competitive, yields and quality have to improve significantly. **Replanting and infilling** with higher yielding and better quality varieties is one of the key interventions.

The Tea Association of Malawi is one of the 20 organizations that formed a "public-private partnership" under the flag of the "Malawi 2020 Tea Revitalization Program". This partnership contains stakeholders across the tea supply chain. All producers, the main buyers of Malawi tea, certification bodies and civil society are part of the program. The partnership is endorsed by the Malawi government and coordinated by IDH, the Sustainable Trade Initiative as neutral convener.

The Malawi Tea Industry is looking for partners that can support them with blended finance (grants, patient capital and affordable loans) that help them realize the required investments in order to achieve the program's target: to revitalize the industry; ensure employment is secured on tea plantations, a living wage is being paid, and smallholder yield in Malawi is increased. The total investments needed amount to USD 63 million.

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Coffee

- R&R is important for Nestlé's business and the company is providing R&R expertise in origins where local structures do not have sufficient resources and expertise. Nestlé stresses the importance of the availability of improved planting material (quality and variety). **Public funding is needed for breeding** and can also help to develop training curricula and train future experts.

- Ecom has set up a finance program for replanting for coffee farmers in Nicaragua. Ecom provides technical assistance to the farmers and selects the farmers that can apply for direct finance from local banks. Ecom is documenting the loans on behalf of the local banks to lower the transaction costs. Starbucks provided an **off-take agreement to mitigate the risks** for the bank and for Ecom. It took 10 – 15 years to build up the relationships with the farmers.

- In Nicaragua, the farmer organization SOPPEXCCA (with the support of Root Capital) provides **finance for 50% of the costs of replanting** of their members. Their members need the financial support to overcome the first three years of no production. Year 3 – 7 are the peak production years and after 10 – 12 years the new cycle for renovation starts again.

- FNC has **integrated approach** to smallholder R&R, which includes research, extension services and finance. It is one of the largest R&R programs currently being implemented, 3,2 billion coffee trees have been replanted. The FNC approach uses farmer segmentation to effectively target each segment of coffee smallholders. Farmers that struggle financially are able to get government subsidies during the first years of the replanting period.

Cocoa

Barry Callebaut has learned that before replanting at scale it is important to **maximize smallholder farmer's assets** by providing them with knowledge on GAP (particularly pruning) and supporting farmers with access to crop protection products and fertilizers.

Barry Callebaut also underlines the need for investing in R&R, and is taking first steps to support smallholders in this process.

In the "Cocoa Fertilizer Initiative" IDH, the Sustainable Trade Initiative, convenes the major players of the cocoa industry to support smallholders in Cote d'Ivoire with a productivity package to ensure that all necessary services reach the farmers. Besides the "Cocoa Fertilizer Initiative", IDH is exploring opportunities to establish a "Farm Finance Program" with key stakeholders in Cote d'Ivoire. Blended finance will play a key role in this program.

The "Farm Finance Program" plans to improve producer-level access to finance by working with exporters to identify cooperatives and farmers with whom good governance and financial capacity can be developed to the point of bankability; and simultaneously work with local banks to build this capacity, eventually providing the financing necessary for cocoa farmers to invest in their farms.

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Next steps

The Innovation Forum helped to define next steps for the four sectors:

For **palm oil**, the Indonesian delegation committed to continue the discussions on R&R in a working group in Jakarta, in order to develop a pilot for innovative replanting in South Sumatra. Within this initiative, specific attention will be given to the legalization of the land status of smallholder farmers, the organization of independent smallholder farmers, and access to innovative financial structures during the first four years of replanting. The IDH palm oil team will specifically support this initiative on exploring the possibilities of blended finance to get the pilot project started.

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In the **tea** sector, there is a large need for R&R to increase both yields and quality. For example, IDH's partner KTDA has identified a need for R&R for up to 560.000 smallholders in the Kenyan tea sector, estimated total costs are USD 19.2 million. An important next step for the IDH tea program is to further develop the Malawi Tea Revitalization Programme. This will be done by defining the individual business cases per plantation in Malawi, as well as by developing a pitch book that will not only include the commercial business case, but also the wider development goals on employment, worker welfare and smallholder livelihoods.

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For **coffee**, R&R is perceived to be key in mitigating the effects of climate change. The IDH coffee team incorporates R&R in the climate smart agriculture agenda. For the coffee sector, three key aspects have been identified to further R&R practices in the sector: data on the (financial) performance of farmers (for financial institutions to manage investment risks), government involvement in creating sector coalitions and an enabling environment, and economically viable nurseries with good quality planting materials.

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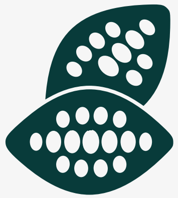

The IDH **cocoa** team underlines the identified building blocks, and more specifically sees a need for the development of farmer selection criteria, for knowledge on adoption rate enablers, for pipeline development to create alignment, and for de-risking measures to enable investments in smallholder R&R. A next step is to further integrate R&R in the Farm Finance Initiative in Côte d'Ivoire, to have a holistic approach to move smallholder farmers from poverty to middle class. The cocoa sector could benefit from learning from the R&R schemes in coffee, such as the one in Colombia, to understand the key attributes that need to be put in place through public-private cooperation.

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R&R INNOVATION FORUM

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