

## ***Creating a buffer fund to help farmers access the hotel trade in St Lucia***

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### **Introduction**

For centuries the name West Indies or Caribbean was synonymous to large-scale horticultural production for export to Europe. Today, the Caribbean is a net importer of agricultural produce especially to support the growing tourism. Tourism is the mainstay of many Caribbean territories' economies. But this reliance on tourism still leaves their economies wide open to external shocks. On average, 75% of the tourism expenditure leaks outside the Caribbean economy - and has hence failed to impact broadly on poverty in the region. Linkages to local production have not developed and there has been a steady decline in agriculture resulting in the loss of livelihoods for many.

In 2003, Oxfam GB launched an initiative in St. Lucia, a small eastern Caribbean island, to increase access to markets in the local tourism sector. The pilot project is aimed at increasing sales of fresh fruits and vegetables to hotels. Pioneered by David Bright from Oxford, the Market Access Initiative (MAI), as it is called, also aims to increase the power of small-scale rural farmers through advocacy and lobbying for the implementation of a positive policy framework which creates an enabling environment. The pilot has also worked to develop a strong enterprise operating in farmers' interests, to enable sustainable trading linkages with the tourism sector.

In summary, the objectives of the MAI are:

1. To increase trade in fresh produce by developing hotel demand and production capacity through strengthening farmers' organisations
2. To foster the development of an efficient St. Lucian enterprise, operating in farmers' interests, to commercially trade in fresh produce initially with the hotel sector
3. To advocate for a supportive national and regional trade policy framework to develop farmer linkages to the tourism sector
4. To create a model for ensuring agro-tourism linkages are developed between the private sector, small-scale farmers and governments in small island states
5. To advocate for and support replication of the model in other Caribbean states

Several interventions were carried out to support the farmers to access the markets, including working with the East Caribbean Agricultural Trading Development Agency to set up the production, distribution, marketing and information systems and with the Windward Islands Farmers Association (WINFA) to provide support in group dynamics, agricultural practices and production planning. The Caribbean Policy Development Centre (CPDC) has led the lobby against unfavourable regional and international trade regulations and urged a local policy to increase hotel engagement with small scale local producers.

To ensure that the trade linkages are sustainable, a group of key private and public sector institutions, who share common interests around the development of farmers' and hotel trade linkages to alleviate poverty, have been partners in the process. The private sector organisations are from the tourism, farming and agro supply sectors, with public organisations including the Government and Non-Governmental organisations. The target beneficiaries have grown from around 400 to 1,000 farmers in the rural districts. Increasing levels of gender sensitive and disaster risk reduction is being integrated into the programme.

The MAI has had some impact on local and Caribbean agro-tourism policy. These can be summarised as follows:

1. St. Lucia tourism and agriculture policy was developed taking into consideration many of the recommendations coming out of discussions facilitated between farmers and officials of the Ministry of Tourism and the Ministry of Agriculture.
2. The St. Lucia Chamber of Agriculture and the St. Lucia Hotel and Tourism Association developed a policy for moving more agro-produce to hotels. This plan involves the establishment of a hub with shareholders from the private and public sector as well as farmers' organisations.
3. The government in 2005 appointed a representative of the farmers from Belle Vue Farmers Cooperative Society Limited to the Board of management of the St. Lucia Marketing Board.
4. Several organisations in St. Lucia (including the credit unions, banks and IICA) have been trying to set up a new scenario for micro financing. This proposed scheme has taken into consideration the need for holistic support for farmers as they produce. It recognises that simply giving loans to farmers is not enough.
5. Caricom has recognised the MAI as a key intervention to address some of the key constraints to agriculture under what it calls the Jagdeo Initiative.
6. Caricom agri-business desk has identified the MAI as a model which the region can learn from in relation to growing sustainable farmer-led agro enterprises.
7. IICA agro-business has utilised the learning to help structure its ten year plan for agro-tourism development in the Caribbean.
8. The World Bank in September 2008 signed a project with Oxfam to use some of the learning in a pilot in Jamaica to link small-scale farmers to the hotel sector.

The aim of this paper is to show how farmer-led enterprises require viable forms of micro financing to increase market access. The paper shows the importance of intermediaries and monitoring mechanisms in the management of micro financing facilities. It discusses how an innovative way of providing financing in St. Lucia is structured and how it has begun to impact on models of financing elsewhere in the English-speaking Caribbean. It is argued here as well that to increase impact, these micro financing initiatives need to be scaled. The paper concludes by advancing options for scaling these mechanisms.

### **Developing the buffer fund**

In designing the MAI, it was learnt that credit, irrigation, inputs, business development services, transportation and market intelligence are some of the key market services required by farmer-owned enterprises in the Eastern Caribbean. While these are available, they are not very affordable. Moreover, to be efficient enterprises need to access these on a timely basis. One of the challenges plaguing farmers who sell produce to the tourism sector is the long delay in receiving payments from hotels. During the initial stakeholder consultations in 2003, Jethro Green, a well-known Caribbean advocate for small farmers, of the East Caribbean Agricultural Trading Development Agency, urged the establishment of a Buffer fund to ease cash flow challenges among the farmer-owned enterprises. But the stakeholders in association with Oxfam insisted on a scientific approach to understanding the nature of the problem for the development of sound solutions. Consequently, research was undertaken in 2006 by Prosperity Concepts Inc (PCI), a wealth enhancement company owned by retired bankers. In their report, PCI found farmer-owned enterprises had to wait on average 70 days for hotels to pay for their purchases. Up until the research was done the farmers had been claiming a delay on average of 90 days. The delay in collecting payments from hotels and the large expenditure on inputs have led to an over reliance on bank overdrafts. The PCI recommended a buffer fund, a fund secured by a deposit or guarantee and a fund

managed by an intermediary. The farmers' leadership were unhappy with having an intermediary; they wanted the fund deposited into their bank account.

Farmers' Assoc/Hotels/Financiers sign a Tripartite Agreement
Farmers buy inputs
Farmers harvest crops
Farmers sell to Farmers' Assoc.
Farmers are paid on 7 <sup>th</sup> day By writing a cheque on NRDF
Farmers' Assoc. sell to Hotels
Hotels confirm purchases in writing
Signed-Off Invoices are presented to NRDF for immediate reimbursement
Hotels reimburse NRDF within 30 days
A Fee of up to 2% is levied

Figure 1: The Microfin Model

Research also found that farmers in several islands where a micro finance facility operated named Microfin, funded by the European Union, was abandoned by farmers because it removed the power and respectability from them through the hotels not paying them but paying Microfin. The farmers in the MAI were adamant this most not happen with the Oxfam intervention and so the Buffer fund was designed with the deliberate protocol that the hotels must pay the farmer enterprise directly, and the enterprise then repays the fund. This model helps to build the financial management capacity of the co-ops. It is also practical because the fund is monitored by a Business Review Committee comprising representatives from the public and private sector. The co-op on a monthly basis have to demonstrate to this committee how business is going as a basis for continued access to the fund. It is this principle of capacity building by providing mentoring and other support why WINFA and the Credit Union League were selected to assist with the fund. WINFA is a farmers' organisation nearly 30 years old. It pioneered FairTrade bananas, with the help of Oxfam, in the Windward Islands and has presence in St. Lucia. In fact, two of the groups in the St. Lucia MAI are WINFA affiliates.

Several local financial institutions and government and non-government agencies were approached on the idea of establishing a Buffer fund. While they all liked the idea, they expressed scepticism with the capacity of farmers' organisation such as co-ops to manage it. In particular, they had no confidence in the two main farmers' groups/co-ops. They were insistent that these groups lacked financial prudence. The analysis by the stakeholders revealed there was cause for concern and to be on the safe side the decision was taken to use an intermediary. Of all those approached, the Credit Union League was most committed on the grounds of supporting the agricultural sector as well as the fact that the co-ops were their members too. With the coalition of the willing, the fund was established with the intention of proving the sceptics wrong and winning them over later. The recent audit of the fund reveals the fund can now be scaled.

### How the fund operates

In 2007, Oxfam made a grant of £10,000 to WINFA, which then placed the equivalent EC\$50,000 with the St Lucia Credit Union League Ltd. This deposit increased the farmers' co-op share in the credit union and an entitlement to a dividend of 4% against this collateral, the credit union set up a facility that enabled Belle Vue Farmers' Cooperatives to borrow 50% of the amount, EC\$25,000, at an 8% pa interest rate. This was later increased to the full EC\$50,000.

The Revolving Loan Account (RLA) must be balanced and brought to a mathematical Zero (on paper), monthly and quarterly.	The Accountants and the Business Review Committee (BRC) must ensure and validate.
Belle Vue cannot use this account to effect any purchase other than items from Farmers' harvests.	The Accountants and the BRC must ensure and validate.
All Capital purchases must be funded from profits or other sources.	The Accountants and the BRC must ensure and validate through review of the RLA.
All Operating expenses must be funded from profits and via the account at Bank of St Lucia.	The Accountants and the BRC must ensure and validate through review of the RLA.
Initially, the Credit Line will be limited to *ECD\$50,000.	As circumstances dictate, and based on the Financial performance or new Business Plans, approved by the BRC, the limit can be increased.
BelleVue will submit to the BRC within 5 Business days of each monthend, a statement of all transactions on the Account, together with a reconciliation statement bringing the account to a Mathematical Zero.	BRC
The BRC will undertake reviews, monthly, quarterly, six-monthly and yearly	BRC. Reviews done at the six-monthly and yearly stages will be strategic in orientation. The monthly and quarterly reviews will be transaction-oriented.
The BRC will formally advise Belle Vue and the League of major concerns or positives. Minor concerns will also be recorded.	BRC
Belle Vue must formally respond within 5 days of receipt, presenting a plan or defence to nullify the concerns of the BRC.	Belle Vue
Accounts Receivables from the Hotels must never exceed 50% of the Limit of the Revolving Loan Account, ie, ECD\$50,000 at this time. The aggregated Accounts Receivable should never exceed ECD\$25,000 at this time. If so, the prior approval of the BRC must be sought and a formal plan to reduce the excesses must accompany the request to exceed.	League/BRC
A Production Forecast must be submitted annually prior to start of the Fiscal Year. The BRC will review Production performance on a monthly basis against the Forecast to ensure progress. Production versus Forecast figures must be submitted within 5 days of each monthend.	Belle Vue WINFA/Oxfam will support with provision of the software "Cropware"  BRC
The BRC has veto power and can instruct the League to cease allowing Vouchers to the Account. During this period only Deposits will allowed against the Account	BRC Veto powers will be informed specifically by abuse of the RLA, untimely presentation of Accounts, but generally by non-adherence to these Rules.
In Year 4 WINFA/Oxfam will review the need for Financial support. Notwithstanding, the Credit, Financial and Management reviews will stay in place.	WINFA will undertake.

By end of Year 3, Belle Vue must be in a position to operate in an independent Commercial manner.	
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Figure 2: Rules of the Buffer Fund

In essence the Buffer Fund is a type of revolving loan facility much like a credit card. The loan funds are used to purchase agricultural produce from members for sale to mainly hotels, restaurants and supermarkets at a mark-up. The mark-up is typically 40% of sales price. This means that if the sale price of fruit and vegetables to the hotel is EC\$1000, the farmer receives EC\$600. The timing of the different transactions is as follows:

1. Farmer provides produce with a market value of EC\$100 to Belle Vue (and other cooperatives)
2. Belle Vue gives farmer a voucher/cheque (post-dated by 8 days) for EC\$60. Farmer cashes this cheque at nearest branch of SL Credit League.
3. Belle Vue delivers produce to the hotel and invoices them for the total market value of the produce.
4. Around 30 to 70 days after the delivery, the hotel pays Belle Vue (EC\$100).
5. Belle Vue, then returns EC\$60, plus interest to the credit union. The mark-up is used to cover interest, operating costs and to build up a collateral fund to replace that provided by OGB.

Vouchers can be cashed at any of the following four credit unions once the payee is also a member of the Belle Vue Farmers Co-operative Society Ltd. as well as a member of the credit union where the voucher is presented.

1. The Laborie Co-operative Credit Union;
2. The Choiseul Co-operative Credit Union;
3. The Saltibus Co-operative Credit Union;
4. The Fond St. Jacques Co-operative Credit Union.

This membership requirement for having vouchers cashed was not in the initial agreement. The membership requirement places a constraint on the ability of Belle Vue to expand the initiative for the benefit of more of its members and other farmers. Some farmers do not live in close proximity to those credit unions and are not interested in joining them so as to benefit from the Buffer Fund initiative. The participating credit unions have agreed in principle to waive the membership requirement for the cashing of vouchers. Once this arrangement is implemented more farmers will be able to benefit from the Buffer Fund.

### **Impact of the fund**

Belle Vue Co-operative currently has about 100 active members and a share capital of EC\$101,496. Belle Vue pays the Credit Union League a 2.5% service charge for the service provided by the fund. In essence this is the Credit Union's management fee.

To date 22 members are benefiting directly from the existence of the buffer fund. All other members who Belle Vue purchases from are paid from outside the fund. The lack of cash flow has resulted in the society's bank account going into overdraft from time to time and attracting the overdraft interest of rate of 13%.

The fund has had the impact of bringing down the annual bank overdraft. The overdraft for 2008, the first full year the fund was in operation, is EC\$61,120. In 2007 the overdraft was EC\$95,053 which was an increase from EC\$79,503 in 2006.

Here is a sample of the overdrafts from the first quarter for 2009:

<u>Overdraft Balance</u>	In EC (£1= EC4)
January 31st, 2009	58,290.60
February 28th, 2009	49,843.78
March 31st, 2009	43,373.40
<u>Overdraft Interest</u>	
January 31st, 2009	364.12
February 28th, 2009	561.52
March 31st, 2009	458.35
Total	1,383.99

For the first quarter of 2009, the Belle Vue Farmers Co-operative incurred overdraft interest of EC\$1,383.99. Overdraft interest is charged on the daily overdraft balance.

The terms and condition of the Buffer fund/loan from the League to Belle Vue Farmers Co-operative Society Limited compares favourably with other types of financing that are available. The loan is at 8% reducing balance with no processing fee. It is secured by a deposit made by WINFA of EC\$50,000 in the name of Belle Vue with funds provided by Oxfam. Financing could have been secured from other sources on terms and conditions that are different from what is available under the Buffer Fund initiative. Here are a comparison between a bank loan and the credit union.

(A) Bank Loan

Interest rate of 10% - 13% per annum.

Processing fee must be paid.

Fixed period loan with monthly repayment.

Security provided by Belle Vue Farmers Co-operative.

Presentation of a comprehensive Business Plan with adequate financial projections prepared by a professional acceptable to the bank at Belle Vue's expense.

(B) Credit Union Loan

Interest rate of 8% per annum.

Fixed period loan with monthly repayment.

Belle Vue must be a member with qualifying share balance and/or deposit as security. The qualifying share balance being 20% of the loan.

Presentation of a comprehensive Business Plan with adequate financial projections prepared by a professional acceptable to the Credit Union at Belle Vue's expense.

An audit of the Voucher Payment System in April 2009, by a well-experienced auditor from the international finance and anti-money laundering sector who has worked with friendly societies and credit unions as well, reported as follows:

1. The voucher payment system is effectively administered with participating members receiving payment vouchers on a timely basis.
2. All vouchers sampled by the auditor were found to have been correctly prepared and signed by the relevant authorizing officers.
3. The duplicate of all vouchers issued to farmers were found filed in numerical order at Belle Vue's office.
4. All vouchers are signed by two authorized signatories. Unused payment vouchers are safely secured and accounted for.

For the period August 2008 to March 2009 monthly voucher payments range from \$5,700 to \$11,500.00

The Buffer Fund was established with a clause providing for a 4% dividend per annum to be paid by the League to Belle Vue. To date, the League has paid no dividend on the fund.

The dividend outstanding for 2007 is EC\$1,260.27. This is calculated thus:  $\$50,000 * 4\% * 230\text{days} / 365\text{days} = \text{EC}\$1,260.27^1$

The dividend outstanding for 2008 is EC\$2,050.41. This is calculated as follows:  $\$50,000 + \$1,260.27 * 4\% = \text{EC}\$2,050.41^2$

Dividend Receivable 2007	1,260.27
Dividend Receivable 2008	2,050.41
Total Dividend receivable from League	3,310.68

The explanation given for the non-payment of dividend is that the League's AGM has not taken. The date of the League's AGM has not been set.

#### Effective Interest Rate

The effective interest rate depends on the way in which the loan is compounded by the League. However, the Buffer fund agreement does not indicate how the League will be compounding the loan. The effective interest rate has been calculated on the Buffer fund loan based on the following compounding factors:

	%
Daily	8.33
Monthly	8.30
Quarterly	8.24
Semi-annually	8.16

Based on the above calculations of the effective interest rate the Buffer Fund arrangement is less expensive for the Belle Vue Farmers Co-operative Society Limited than financing in the form of bank overdraft. Bank overdraft will be charged at an interest rate of 13% calculated on the daily balance. The effective interest rate is influenced mainly by the nominal interest rate of 8% and whether or not the loan is compounded daily, monthly, quarterly or semi-annually. There is no one-time charge such as a processing fee on the facility. When the 4% dividend is received the effective interest rate is likely to be reduced as follows:

	%
Daily	4.88
Monthly	4.07
Quarterly	4.06
Semi-annually	4.04

To date the participating Credit Unions have earned approximately EC\$2,588 in service charge from the cashing of vouchers. Their earnings will increase as the Buffer Fund expands.

<sup>1</sup> 230 days being number of days in 2007 to which the 4% dividend is applicable to, which is from May 16, 2007 to 31 December 2007.

<sup>2</sup> 365 days being number of days in 2007 to which the 4% dividend is applicable.

No monthly management accounts are prepared requesting funds from the Buffer Fund. Belle Vue prepares a monthly Revolving Fund Report which summarizes all activities for the month. This report is done for the monthly Business Review Committee meeting. However, the following shortcomings affect conducting of a proper assessment:

1. Sale of produce purchased from Buffer Fund beneficiaries are reported separately.
2. Belle Vue does not receive a copy of the report submitted to the League by participating Credit Unions for reimbursement.
3. The League does not provide Belle Vue with regular activity reports on the Buffer fund/loan facility; neither does Belle Vue request such reports on a timely basis.
4. The Buffer Fund account is not reconciled on a monthly basis to coincide with the balance reported by the League.

Despite these shortcomings as at March 31, 2009 total Revolving Fund Vouchers used amounted to EC\$103,531. For the period August 2008 to March 2009 vouchers issued as a percentage of sales range from 10% to 23% per month. As at March 31, 2009 the League's records show the Buffer fund/loan balance at EC\$42,992.35, while the monthly Revolving Fund report prepared by Belle Vue show that it has been overdrawn by \$5,988.21, a difference of:  $\$50,000 - \$42,992.35 + \$5,988.21 = \$12,995.86$ .

The recent audit has suggested that the monthly report should be revised to show in more detail the activities of farmers benefiting from the Buffer Fund. To this end, there should be a separate accounting for the reporting of Buffer Fund activities. This process can be carried out manually, using Excel or using a simple and user-friendly accounting package such as Quick Books.

The Buffer Fund account has never been cleared. On April 9, 2008 the balance stood at \$140.78, which was interest outstanding as at that date.

While the fund has increased cash flow, account receivable remains high. Amounts receivable from Hotels for the period January 2009 to March 2009 were as follows:

January	EC\$
February	51,051
March	53,338
	64,920

Over the same period one hotel accounted for following percentage of receivables:

January	%
February	42
March	30
	23

The monthly Hotel receivable balance averages over 50% of monthly sales. As such, the Belle Vue Farmers Cooperative Society Limited has a lot of its financial resources tied up in receivables which are liquidated over 30 to 90 days. The cost to the Society is not limited to cash flow constraints but bank overdraft interest rate of at least 13%.

### **Expansion and enterprise development**

The evidence above shows that the buffer fund has enabled farmers to access the hotel markets in St Lucia and consequently to improved their incomes. However, there is scope to develop the work we were doing further. A 3-year Enterprise Development Project (EDP) is supporting the expansion of the programme and demonstrate the potential of farmer-owned enterprises to make a sustainable contribution to the tourism sector, cutting imports, and hotel costs. A larger buffer fund is needed for Belle Vue to provide a greater volume of credit as their trading activities expand. Hence, the EDP is providing a loan of GBP30,000 to expand the

Buffer fund in mid-2009. The St. Lucia Credit Union League will continue to manage the expanded fund with modified guidelines to increase efficiency. Also, the League is being asked to add some of its own resources to the total deposits in the fund. Now that there is evidence of the good working of the fund, the government of St Lucia and the St. Lucia Chamber of Agriculture will be asked as well to contribute to the fund. A non-negotiable is that hotels must pay farmer-owned enterprise directly and not the intermediary.

The integration between financial services and other business development services are crucial for the success of the enterprise. This means that the expanded Buffer fund will lead to an increased demand on extension and business development services. The good thing is that in St. Lucia there exists an enabling environment such as a policy/regulatory environment that enabled the fund to be successful.

### **Exit mechanism**

It is envisaged that the Credit Union League will eventually acquire the Buffer fund and offer it as one of its services. The inclusion of the government and other agencies are key to the fund achieving sustainability. The fund has to operate in conjunction with ensuring adequate support mechanisms exist and already there is sufficient evidence in St. Lucia that the MAI is no longer simply an Oxfam initiative but a St. Lucian-owned model. It is with the anticipation of Oxfam's exiting that WINFA was included from inception as a major monitoring agency in the Buffer fund and wider programme. All fund in the Buffer Fund made as grants by Oxfam are held in the credit union as WINFA funds. The loans under the EDP will be repaid by Belle Vue.

### **Conclusion**

The Buffer fund model of financing has begun to impact of models of financing elsewhere in the English-speaking Caribbean such as Barbados and Jamaica. Among the agencies canvassed were the Jamaica Agricultural Society (JAS), the Jamaica Social Investment Fund (JSIF) and the Jamaica Co-operative Credit Union League Ltd (JCCUL). These agencies are collecting data from farmers to allow the preparation of a case for a buffer fund/credit line. A new European Union/World Bank funded programme through the Jamaica Social Investment Fund has promised to incorporate the learning from the St. Lucia Buffer model. In Barbados, the Barbados Agriculture Management Company (BADMC) is using the learning on the Buffer fund in its design of the management system of a USD\$0.5 million fund for paying farmers who sell to hotels. Elsewhere, the Caribbean Farmers Network has shared components of the St. Lucia MAI with several farmers' organisations and ministries of agriculture who have begun to adopt different elements and change their policies on financing for small farmers.