

Factoring The Fijian Model

A value-chain and market linkage review

By Robert Horton
Pacific Island Consulting
Pacific Regional Capacity Building Workshop on
Enhancing Success for the Agricultural Sector
20-21 October 2011, Nadi



Agriculture in Fiji

- Fiji is often referred to as the Garden Isles because virtually anything can be grown
- The islands have traditionally been a land of plenty and surplus
 - Fijian farmers successful in grow high value speciality cash-crops
 - Widespread demand for high-value crops
 - Rural and small scale farmers have land for a wide variety of crops



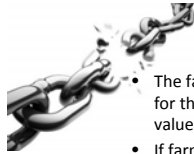
Agriculture in Fiji The value-chain and market linkage

- Fijian farmers enjoy a successful value-chain
- Large scale and commercial agricultural interests complete the value-chain with a market linkage through successful sale of their output and payment received
 - Small scale and rural farmers often fail to successfully complete the linkage between the value-chain and the market or ultimate payment received for their goods



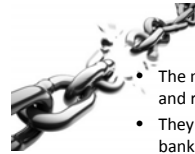
The value-chain and market linkage in Fiji

- Fijian agriculture has been provided many resources by Government and international organizations to build their capacity and empower farmers to grow a wide range of high value specialty crops that contribute to their income and the food security of Fiji
- This then is a successful value-chain as farmers meet every step in the successful cycle
- The difficulty faced by many Fijian famers is in their failure to link their successful value-chain with a market linkage for high value output



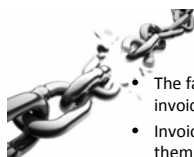
Obstacles to Success for Agriculture in Fiji

- The failure of farmers to sell their high-value output for the expected premium price then puts the whole value chain and market linkage in jeopardy
- If farmers are encouraged to grow speciality crops that they cannot sell, there is little motivation to continue raising them
- Although there are vertically integrated support programmes that provide farmers with guaranteed pricing and sale of their output – particularly for the export market – these programmes are relatively small, only available in certain areas and for specific crops.
- What are these barriers or why is there a failure to complete the value-chain with a market linkage?



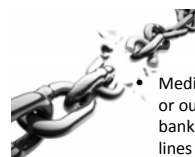
The break in the chain

- The market linkage is a critical step for medium, small and rural farmers
- They often do not have available any financial or banking relationship that helps facilitate their ability to develop their farm and sell their output
- They do not have access to a banking relationships that may include commercial credit, credit lines or bank accounts
- These farmers sell their output and desire cash at the point of sale
- The breakdown occurs when farmers with high-value speciality crops sell to middlemen, supermarkets, wholesalers or hoteliers who desire to pay by invoice with delayed payment



The break in the chain

- The farmers desire cash on delivery - buyers pay by invoice
- Invoices have been abused in Fiji - farmers distrust them
- Invoices and payment not monitored
- Little penalty for failure to pay invoices for buyers
- The buyer has the crop and has most likely sold it leaving the farmer with little recourse towards the buyer for collection of his payment



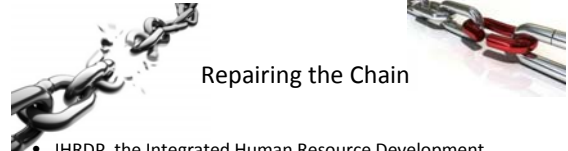
The break in the chain

- Medium, small and rural farmers often sell their crop or output when needing cash. As they do not have a banking relationship with credit and short-term credit lines available to them, they demand immediate payment for their delivery
- Cash on the barrelhead
- As commercial buyers pay by invoice, the farmer then refuses the sale and takes the high value speciality crop and sells it for pennies wherever they can – most often a municipal market
- The value chain and market linkage are then irrevocably broken



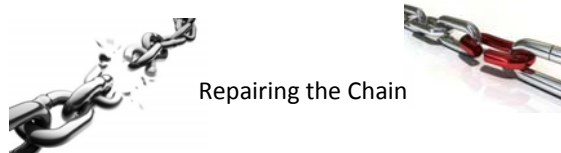
Repairing the Chain

A Fijian Approach for Agricultural Commodity Finance



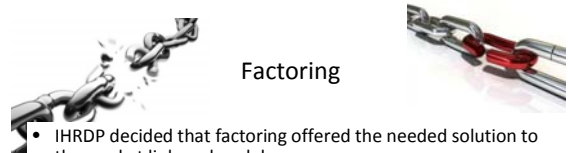
Repairing the Chain

- IHRDP, the Integrated Human Resource Development Programme, a joint Fijian Government and ILO – International Labour Organization - economic development programme identified SMEs' and farmers' inability to complete the value chain with a market linkage as a key obstacle to the success of their efforts
- The successful rural project management provided by IHRDP to support projects requires an end-to-end solution – as such a solution to the market linkage breakage was required



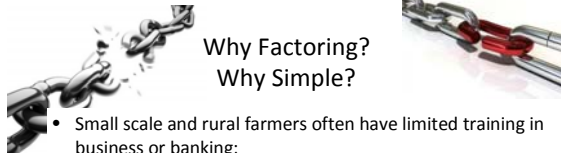
Repairing the Chain

- IHRDP reviewed a number of financial programmes that helped facilitate commodity financing in other areas
- The UNCTAD/ACP programme in the Caribbean was noted as having addressed a similar need
- During the time of evaluation, the *Microfinance in Fiji* study was underway. It was anticipated that the outcome of this survey would be new and innovative programmes to provide commodity financing among other needs
- IHRDP then sought a short-term and very specific programme with limited application but that could be expanded



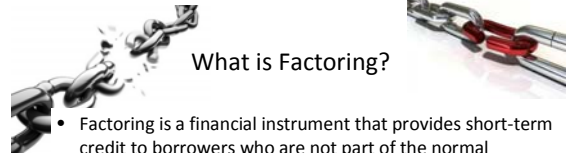
Factoring

- IHRDP decided that factoring offered the needed solution to the market linkage breakdown
- A modified version of the factoring programmes offered in more developed countries was proposed
- As Fijian SMEs and farmers have straight forward and simple requirements, for a relatively small amount of money and a minimal number of sellers and buyers, a simple version of the factoring programmes used in developing countries was proposed
- ANZ Rural and Microfinance is IHRDP's banking partner and were approached to collaborate on this programme



Why Factoring? Why Simple?

- Small scale and rural farmers often have limited training in business or banking;
- Little understanding or use of formal banking resources - knowledge of what services are available for their needs;
- Often have only savings accounts or no bank account;
- They are blocked-out for any financing resources and therefore unable to expand or grow;
- Commercial banking is unsuitable to their needs;
- Normal rural banking is beyond their current understanding or capacity.



What is Factoring?

- Factoring is a financial instrument that provides short-term credit to borrowers who are not part of the normal banking system;
- Factoring and invoice discounting are financing techniques that can be used to help farmers access financing;
- They help to integrate small-scale farmers into the supply chain and complete the market linkage to commercial buyers.

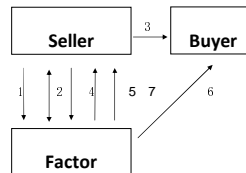


The Fijian Context

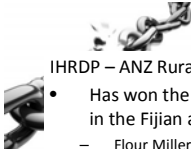
Fundamental points:

- Farmers or SMEs (Sellers) have high-quality speciality output desired by commercial Buyers;
- The Sellers do not have conventional banking relationships or access to short-term credit;
- The Buyers are required to be "trusted" banking clients of ANZ Fiji;
- Finance only post-invoice contractual obligations;
- Factor (ANZ) needs confidence that Buyer accepts goods;
- There needs to be absence of continuing obligations by Seller after delivery of goods.

Domestic Factoring Flowchart



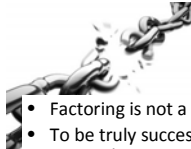
1. Seller submits the request (invoice) to the Factor.
2. Factor considers Buyer's creditworthiness and approves financing limit. Factor and Seller sign factoring agreement.
3. Seller delivers the goods to Buyer and issues the invoices. Buyer stamps and endorses invoice. Buyer must be trusted banking client of ANZ.
4. Seller assigns the invoices to Factor and informs Factor of any special payment arrangements.
5. Factor finances – provides cash – for the value of the invoices at the previously agreed rate.
6. Factor collects receivables at the end of the credit period from the Buyer.
7. Factor remits to Seller the balance in excess of the finance cost.



The Fijian Context Benefits


IHRDP – ANZ Rural and Microfinance Factoring;

- Has won the acceptance and endorsement of key Buyers in the Fijian agricultural market;
 - Flour Millers of Fiji Ltd.
 - Morris Hedstrom Supermarkets
 - Carpenters Wholesale
 - PAFCO
 - Hotels and resorts
- Is easily understood and accepted by rural farmers
- Provides an effective way for any Seller (farmer or SME) to sell their high-quality speciality output and receive immediate cash;
- Is simple, easily understood by Buyers and Sellers and poses little risk of loss for the Factor (ANZ).



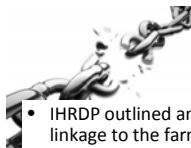
The Nadarivatu Proposal Integrated Approach

- Factoring is not a stand alone solution
- To be truly successful it needs to be integrated as part of a comprehensive solution that meets the many and varying needs of farmers
- The Department of Agriculture engaged the farmers of Nadarivatu to re-introduce large scale potato farming to Fiji
- Commissioner Western engaged IHRDP to ensure the value-chain launched by Agriculture to raise potatoes translated into a successful market-linkage



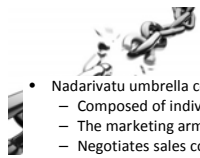
The Nadarivatu Proposal Integrated Approach

- IHRDP – in partnership with ANZ Rural Banking – met with farmers in a village meeting. All potato farmers participated in the meeting.
- It was noted that the farmers had successfully raised and sold crops in the past but had little to show for their efforts:
 - Output sold but nothing retained to enable future planting
 - All money earned spent within 30 days – no savings or financial discipline – noting held back to support replanting
 - Good farmers but unknowledgeable about business or financial management
 - No group support capabilities – farmers raised and sold crops in isolation
- Farmers agreed to terms and conditions of engagement



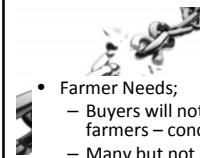
The Nadarivatu Proposal Integrated Approach

- IHRDP outlined and integrated approach for the market-linkage to the farmers;
 - Farmers form agricultural cooperatives - each geographic pocket would form a western style agricultural cooperative.
 - To organize the harvest
 - To monitor quality
 - To organize shipment per buyer criteria or needs
 - To record the total shipment of each member and the quality of that shipment for payment
 - To forward recording keeping to the umbrella central cooperative



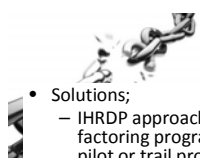
The Nadarivatu Proposal Integrated Approach

- Nadarivatu umbrella central marketing cooperative;
 - Composed of individual local cooperatives
 - The marketing arm for all of the cooperatives
 - Negotiates sales contracts with commercial buyers;
 - FMF for potato chips
 - Carpenters Wholesale for sale to supermarkets, restaurants and hoteliers
 - RFMF – army contract
 - Consolidates shipments from all cooperatives to meet buyer needs. FMF required specific quality control of shipments for size, quality and maturity
 - Prepares invoices to support shipments
 - Ships
 - Receives payment
 - Disperses payment to individual cooperatives
 - Offers support services to member cooperatives – extension, business, banking, etc.




Nadarivatu Factoring

- Farmer Needs;
 - Buyers will not accept multiple shipments from individual farmers – concerned about consistent quality
 - Many but not all farmers had savings accounts
 - Farmers distrust invoices due to previous difficulties – desire immediate cash
 - For potatoes to be a sustainable programme independent of Government support, they need to operate farms as a business




Nadarivatu Factoring

- Solutions;
 - IHRDP approached ANZ Rural Banking with a simplified factoring programme to meet Fijian farmers needs as a pilot or trail programme;
 - ANZ conditions;
 - Seller must be trusted banking partner
 - Non-recourse – if invoice accepted for payment by buyer, they can't charge their minds later
 - 30 day payment period by buyers
 - Cooperatives and farmers required to have or open personal or business bank accounts
 - Agreements put in place by sellers and buyers to support the programme
 - Attractive transaction fee



Nadarivatu Factoring Process

- Farmer's Cooperative
 - Shipment organized for specific buyers and their needs – quality, size, maturity
 - Invoice prepared and included with shipment
 - Buyer receives shipment and inspects samples
 - Buyer stamps and signs provided invoice. Invoice now a negotiable financial instrument – essentially a cheque
 - Farmer's designated representative takes invoice to ANZ Rural for payment



Nadarivatu Factoring Process

- ANZ Factoring;
 - ANZ accepts invoices per in-place agreements from specific agricultural cooperatives and trusted banking clients
 - Payment is distributed to previously agreed upon accounts based on designated payees and ratios
 - 25% of payment retained in cooperative commercial accounts for reserves, replanting expenses, business operations, etc
 - Farmers receive flow through payments from cooperative commercial account to their personal bank account based on the cooperatives provision of specific ratios for payment. If Jone delivered 100kgs of # 1 quality, he is entitled to x% of total net payment



Nadarivatu Support

- To ensure the success of the factoring programme a variety of educational and support programmes were to be provided to the cooperatives for their needs and the farmers for their personal needs.
 - ANZ
 - Personal financial literacy as accounts are opened
 - Business banking management for cooperatives officers
 - Support in determining structure of ratios and payments
 - On-going support as needed, when needed



Nadarivatu Support

- Department of Cooperatives
 - Business management, financial management, on-going support
- IHRDP
 - Project management – as most business are able to launch but 80% of new business fail in their first year, on-going project management support at the moment of crisis and to ensure business and financial management is taking place in a timely manner
- Commissioner Western
 - Monitoring and support by Provincial Officers
- Department of Agriculture
 - Provincial and District Officers to provide extension services to ensure quality, consistency and trouble-shooting

Lessons Learned

The Way Forward

Financing Constraints in the Agricultural Sector

- A coordinated approach for facilitating financial services to agriculture is needed with the active participation of all stakeholders;
 - Central banks
 - Planning Ministeries
 - Agriculture Ministeries
 - Commercial and Development Banks
 - Agricultural cooperatives for and by the farmers themselves
 - Private sector partners
 - Donors for funding and technical assistance to develop appropriate tailor-made financial products to meet the specific needs of agricultural borrowers for each level of development.



The Way Forward Financing Constraints in the Agricultural Sector

- The need is great
- The programmes exist
- The only question is whether the motivation is there to implement these programmes through a coordinated action plan