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Agriculture Value Chain Finance in Myanmar

A Role for UNCDF

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Acronyms

GDP	Gross Domestic Product
MADB	Myanmar Agriculture and Development Bank
MAP	Making Access Possible
MoAI	Ministry of Agriculture and Irrigation
MFI	Microfinance Institution
NGO	Non-Governmental Organization
PARDAP	Poverty Alleviation and Rural Development Action Plan

Summary

Despite the fact that some 58% of its population is involved in rural activities, Myanmar is lagging behind its neighboring countries when it comes to agricultural production. The most powerful explanation of Myanmar's underdeveloped agricultural industry is a lack of sector financing. National and international organisations have not focused extensively on agricultural development, even though such development constitutes a first step in ensuring sustainable economic growth in Myanmar.

The financial products that are currently available on the market are not suitable for farmers and other actors in the agriculture value chain. Neither government actors, such as ministries and national banks, nor microfinance institutions and non-governmental organizations (NGOs) are currently developing financial products that aim to integrate actors in the value chain. This leaves a huge gap in agricultural development.

A well-integrated agriculture value chain, defined as the sequence of value-adding activities from production to consumption, through processing and commercialisation (APO, 2007), would bring economic and social benefits to all stakeholders involved. To effectively integrate the value chain, proper financial products are required. Since most of the financial products required to enable such a value chain to function are not available, the United Nations Capital Development Fund (UNCDF) has the opportunity to play a critical role in facilitating the introduction of such products to the market.

This paper highlights the problems related to agricultural finance in Myanmar and proposes a solution that will benefit everyone in the agriculture value chain, from farmers to regulating institutions, improving their role in the chain.

Context and the Importance of the Problem

Myanmar's economy has always been heavily dependent on agriculture and in 2010, agriculture and agricultural related production accounted for 60% of Gross Domestic Product (GDP). However, agricultural contribution to GDP is decreasing (in line with the traditional growth model

which suggests that agricultural contribution to GDP and employment decreases as GDP increases). Despite this decrease, the proportion of the population involved in agriculture will decline more slowly than the agricultural contribution to GDP. In terms of employment, agriculture will likely maintain its prominent role in Myanmar's economy. The potential for the sector is still substantial given the country's substantial resource endowment and its strategic location (Making Access Possible (MAP), 2015). The modernisation of the sector is a top priority in the economic and social development agenda for Myanmar's government since *increased agricultural production* and *reduced poverty* are noted as priorities in the Poverty Alleviation and Rural Development Action Plan (PARDAP) (USAID, 2015).

Public and private financial investment are have been slow to embrace the great potential of the agricultural sector. The FinScope survey conducted in 2013 showed that 58% of the population is involved in agriculture and particularly in crop production. Due to the nature of this business, farmers need to have financial access in order to cope with seasonal expenses. Although 43% of farmers and 12% of farm workers have access to financial services, only 37% of farmers report to borrow from a regulated institution – of these institutions, the Myanmar Agriculture and Development Bank (MADB) is by far the most dominant. It was also shown that access to finance does not translate into high take-up of other financial services, as only 8% of farmers and 2% of farm workers use more than one regulated financial product. In addition, there is an alarming tendency to resort to informal and unregulated financial services, especially amongst the very poor. Indeed, 16% of farmers and 32% of farm workers rely exclusively on unregulated services, incurring very high rates of interest and suffering from reduced product availability (MAP,2015).

There is a well-recognised gap in the agricultural finance sector which has a significant impact on overall productivity. This is especially problematic because the rural economy suffers from a lack of access to appropriately tailored services that can increase agricultural production. There is no diversification in the industry and the market lacks dynamism: 94% of the people who report to be working in farming are involved in crops, and 73% of those crop farmers are engaged in paddy production. Moreover, 37.8% report to only grow one crop. Greater financial inclusion would allow farmers to be involved in the production of more than one crop, and eventually to take part in the agricultural value chain, defined as the sequence of value-adding activities from production to consumption, through processing and commercialisation (APO, 2007). In addition, farmers are often hit by natural disasters (droughts, floods) and insurance product availability is limited. Indeed, only 8% of farmers have access to regulated or unregulated insurance services, and a wide majority reported to have suffered losses from such disasters (MAP, 2015 and USAID, 2015).

Furthermore, the agricultural sector encounters financial and technical challenges on its development path because modern practices such as value chain finance and digital financial services are not sufficiently advanced. Any financial service, product or support service flowing through the value chain is considered as value chain finance. This can include direct financing from one value chain actor to another, or external financing from financial institutions or investors

(Miller and Jones, 2010). For agriculture to reach its maximum potential, financing is required at each stage.

To create an enabling environment for value chain finance to be effective, multiple levels have to be addressed (Cherogony, 2007):

- Macro Level- this is the policy level that creates an enabling environment
- Meso Level- takes into consideration financial institutions and the private sector
- Micro Level- involves local and grassroots institutions.

At the macro level in Myanmar, regulations need to be changed to facilitate agricultural development. However, for the purposes of this paper, micro and meso levels are addressed in greater detail. A substantial amount of work on financial literacy must be accomplished in order to make people aware of unexploited potential in the agricultural sector. The role of financial institutions must also be redefined.

Agricultural Finance Product Providers

The major financial service provider in the rural area is the Myanmar Agriculture Development Bank (MADB), which accounted for 23% of total bank branches in Myanmar by 2013 (MAP, 2015). MADB has since gone on to reach now 1.85 million households (UNSAID, 2015), though shows some weaknesses - only those relevant to the study are reported here - that prevent it from taking a lead role in agricultural development (LIFT and World Bank, 2014):

- Lack of portfolio diversification (as mentioned earlier, most financial services target paddy, and the MADB is no exception - 88% of MADB portfolio is concentrated in paddy farmers).
- Limited range of financial products to serve the needs of all the participants in the agriculture value chain. MADB does not finance farmers engaged in commercial agriculture, nor agribusiness firms; in addition, it does not provide services to traders, warehouses, transport firms or other firms further along the value chain. Finally, it does not finance vegetable nor fruit production (which have a higher value added).
- Formal credit products offered by MADB are poorly structured and not tailored to match crop cycles. Farmers are under pressure to sell quickly in order to repay their debt, which causes paddy to go market without being adequately dried. This adversely affects quality and the farmers receive far lower prices for their crop.
- Risk management: the MADB rates on deposits and loans are not set by the market, but are instead set by the Ministry of Agriculture and Irrigation (MoAI), without taking into account the borrowers' risk profile. Since the loans are not collateralised, farmers are required to join a group of 5 to 10 farmers to 'guarantee' each other's loans.
- Inadequate financial regulation: since the MADB is not supervised by the Central Bank of Myanmar (CBM), but instead by the MoAI, prudential standards are not applied.

The MADB mission is to "*support the development of agriculture, livestock and rural socioeconomic enterprises in the country by providing banking services*". However, a large portion of potential clients remain unserved. Although there are some MFIs are working in rural areas, the demand for credit and customised products remains overwhelming. The market for innovative products such as supply chain financing, is in its infancy.

MADB offers only two types of product - seasonal crop production loans, and term loans. This offering strictly limits farmers' choices, and larger farmers are completely cut off the market. In addition, although digital financial services are now breaking into the market - the rural population does not yet have capillary access to it and formal branches are still necessary to provide banking services (MADB, 2013). Notwithstanding its limits, MADB has the most extensive branch network in rural Myanmar, and is therefore crucial in serving a part of the population which would remain unserved otherwise.

Smaller farmers are not able to increase or improve production standards due to a lack of financial services. Organised value chains improve access to credit because buyers and sellers can contribute to finance actors in the value chain; and that being part of a value chain also reduces risk, making it easier for chain actors to obtain financing also from external intermediaries such as banks and MFIs (APO, 2007). It has also been shown that agricultural credit becomes more profitable if producers are well integrated into a viable value chain (Shwedel, 2007).

The majority of the microfinance institutions find themselves trapped and limited because legislation prevents them from engaging in a wider range of activities. World Vision, for example, is particularly interested in expanding operations in rural finance but are not allowed to provide insurance services. They are currently developing a special agricultural loan. In the same way, DAWN is only engaging in ordinary seasonal loans and Alliance is studying the market to determine possibilities for expansion in agricultural value chain finance. On the other hand, a big MFI such as BRAC, that has extensive experience in agricultural finance and in international value chain finance specifically, has not started this kind of programme in country, due to market conditions and a poorly-informed public. PACT, which is the biggest microfinance institution in the country, does offer an agriculture loan but has not yet engaged in value chain finance; although it purports that higher actors in the chain are also its clients, there is no strategy to integrate these clients in a value chain[1].

Overall, the increasing need for financial services in the agriculture sector and specifically in value chain finance has been studied by USAID. In their 2015 report, the main challenges impeding development of the sector were identified as:

- Insufficient access and application of inputs: a lack of financing is the main constraint to putting inputs to best use.

[1] All information regarding MFI positions on agricultural financing comes from email exchanges between UNCDF staff and MFI staff, as well as meetings.

- Labor shortages and limited access to equipment: labour shortages are caused by shifts in urbanisation. Impact is felt through the entire agriculture value chain as the cost of labour is driven up. Financing and supporting change towards mechanisation would help farmers in reducing their need for seasonal labour.
- Limited availability of appropriately structured credit insurance and saving products.

Such obstacles limit productivity, since resources are not allocated efficiently. Farmers find themselves trapped in a vicious cycle since, without sufficient financial resources, they face barriers in accessing inputs and equipment. These accessibility restrictions, together with a lack of insurance, cause farmers to take on unsustainable levels of debt from money lenders. This in turn makes farmers them riskier clients for formal financial service providers.

UNCDF role and Recommendations

There is a wide gap in the market that needs to be addressed in the short-term. UNCDF could take a crucial role in facilitating the process - both on the financial literacy side and in value chain product development. As a matter of fact, UNCDF is already engaged in a UNNATI project in Nepal, which aims at strengthening and improving selected value chains, improving rural infrastructure and enhancing the business and policy environment. In particular, the value chain sector is addressed through two sub-components, namely *Access to Finance* and *Commercialization of Value Chains*.

UNCDF has the capacity to conduct an in-depth market research on agricultural value chain finance, with an objective to map the product supply side. Some research has already been conducted. The aquaculture value chain has been studied[2], as well as the value chains for rice, sesame and mung beans[3]. However, an overview of agricultural sector needs is still missing, particularly one that focuses on the needs of actors higher up in the value chain.

The value chain has to be prioritised in Myanmar and a sustainable implementation of programmes similar to those developed in Nepal should be strongly considered. A challenge fund could be foreseen as a possible solution to engage the private sector in agricultural development. UNCDF could play the role of facilitator, engaging in technical assistance, capacity-building and advisory services.

Under the challenge fund the participants would be called to submit innovative proposals to improve agricultural value chain financing and UNCDF would contribute a share of capital (in the form of grants or loans to the selected institutions). Under such terms, the UNCDF SHIFT

[2] The paper is available at: http://fsg.afre.msu.edu/fsp/burma/Myanmar_Aquaculture_Value_Chain_Study_Report_FINAL.pdf

[3] The paper is available at: http://encludesolutions.com/wp-content/uploads/2016/01/Myanmar-DFS-Assessment-Report_Enclude_201512.pdf

programme could eventually open a challenge fund window to pursue agricultural finance in Myanmar.

The results expected from the programme are:

- Achieve a more well-integrated value chain
- Introduce innovative products to the market that would serve irrigation, production and storage.
- Introduce more financial products to satisfy farmers and actors higher up in the value chain (leasing, warehouse receipt, agricultural insurance, savings and credit).
- Take steps to move the industry toward agri-business

UNCDF would have a central role in providing technical support in the product roll out phase. Therefore, this challenge fund would see UNCDF becoming more involved in programme implementation with respect to previous windows, since the aim is to slowly mobilise a sector – which requires a slower and more cautious approach.

Additionally, UNCDF could position itself as a technical assistance provider - especially in terms of capacity building development. UNCDF could, in collaboration with Ministry of Agriculture and Irrigation (MoAI), develop financial literacy modules for farmers. The Nepal team could also support the team in Myanmar since financial literacy modules have already been drafted for the same objectives there. When the modules are developed, UNCDF will the best actor to disseminate, by means of communications to be distributed in rural areas and a workshops to raise regional/international interest on the matter. UNCDF also has the capacity to solicit additional stakeholders engagement and/or investment.

Aside from the necessity of farmer training, it also imperative that a national partner be engaged to ensure the project's success. In this regards, MADB is identified as the most suitable counterpart to add value to the project. Since MADB is currently the most dominant rural finance, providing capacity building modules to its staff, and its involvement would produce a multiplier effect on productivity that could benefit a large portion of the rural population. First, trainings are required to show the importance of having a structured flow of money in any value chain. In this regard, basic trainings on value chain finance need to be organised. Exposure visits should be organised to other countries in which well-functioning value chains are in place that actually produce a beneficial impact for the rural population (and where donors' aid in the sector has proved helpfuL). Examples include Cameroon for banana production and export, West Africa for cotton and rice production, and Ethiopia and Tanzania for coffee (OECD, WTO, 2013).

It is also essential to transition from a completely hand-recorded information management system to a digital one, which would decrease the risk of losing documents and increase productivity. Trainings would address MADB capacity to develop more financial products to satisfy its customers needs, and to encourage value chain integration. Finally, trainings will aim at increasing MADB capacity to risk-assess its clients.

Conclusion

Myanmar' s economy is still heavily reliant on agriculture, since more than half the population lives in rural areas and derives its income from rural activities. The UNCDF mandate is to "*assist LDCs in the development of their economies by supplementing existing sources of capital assistance by means of grants and loans*" (UNCDF, 1973). It seems straightforward, therefore, that the agency should to engage in a programme that aims at increasing the competitiveness of agricultural enterprises, which would result in increased income for farmers and MSMEs and contribute to poverty reduction in Myanmar.

Value chain finance has been identified as a powerful tool to include most actors in sector development. Well-integrated value chains lead to higher income for all actors, and increase productivity for the country on a macro level. UNCDF aims to bring increased investment to the agricultural sector and increase access to finance. To achieve these outcomes, UNCDF needs to focus on increasing the availability and diversity of financial products for farmers, and increase technical capacity for both farmers and financial institutions.