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REACHING RURAL HOUSEHOLDS AND COMMUNITIES BY ADVANCING INCLUSIVE FINANCIAL PRACTICES

A SYNTHESIS OF PILOT PROJECT IMPLEMENTATION PROCESSES IN CHINA, INDONESIA AND PHILIPPINES

Prasun Kumar Das
Michael Hamp

APRACA RuFBeP Publication 2018/1

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Foreword

Promoting pro-poor rural finance system is one of the important ingredients for stimulating local economy under any context, which however is not the only answer to reduce rural poverty, but it is a key part of the response as per the mandates of the Rural Credit Associations like APRACA which aimed to support building capacity of its member institutions towards providing improve services to rural clientele. Encouraging innovative ways to improve the flow of finance to rural areas could support the entrepreneurship in agriculture and other rural industries which are otherwise not receiving much attention and financial opportunities.

APRACA since last 41 year of its existence is in the forefront to lead access to finance in the rural areas working closely with its member institutions spread over 24 countries in the Asia-Pacific region by providing technical assistance in capacity building, research and knowledge management. I believe that the good practices implemented and the process that was undertaken in three countries were based on the commitment to support sustainable rural finance service provision for poor people, recognizing that on-going access to a wide range of financial services is needed in order to impact rural poverty more effectively. I am confident that this document will be extremely useful to the countries in the Asia-Pacific region to draw lessons in evolving suitable strategies for the benefit of their people and will add value to global knowledge resources.

APRACA received generous funding from International Fund for Agricultural Development (IFAD), the global leader in development finance and inclusive financial system development, for implementing the project to 'Document Global Best Practices on Sustainable Models of Pro-Poor Rural Financial Services in Developing Countries (RuFBeP)'. The knowledge gathered will help APRACA and ultimately its member institutions in 24 countries across the region in disseminating the information that promotes innovations, productivity, inclusive growth, self-reliance, and welfare of the rural poor in the region.

It was observed that not many documents are available to support piloting and scaling up process and introduction of good practices in rural finance. I am sure that this synthesis report on the process undertaken to pilot test good practices of rural financial services in the select countries of Asia will fill in the knowledge gap in this particular area. The APRACA member financial institutions can be immensely benefitted from this document. This document also has the potential to serve as the source book for the government line departments and non-government agencies supporting innovative practices of rural finance. The process document may also support the bilateral and multilateral donor agencies implementing new and innovative financial products and services and support the objectives of sustainable development goals.

SHIBA RAJ SHRESTHA

Deputy Governor, Nepal Rastra Bank and Chairman, APRACA

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We also acknowledge the generous co-financing received from the International Fund for Agricultural Development (IFAD) to conduct the study across member countries of Asia-Pacific Rural and Agriculture Credit Association (APRACA) to help explore innovative and effective models and approaches to extend sustainable rural financial services to rural households and communities. This process document constitutes the third and final part of RuFBeP following deep dive country studies and a synthesis report already produced and disseminated between 2016 and 2017.

This synthesis report of pilot project implementation processes in China, Indonesia and the Philippines comprises knowledge products (such as on cash-flow based lending, agricultural value chain finance, Islamic finance system, role of electronic platforms etc.) that are relevant to both the APRACA membership and to IFAD partners and investments.

The work was carried out under the management of China Banking Regulatory commission (CBRC), Bank Indonesia (BI) and Agricultural Credit Policy Council (ACPC), Philippines, who supervised the experts and members of the three country teams from Huainantongshang Rural Commercial Bank (HTRCB) and Nanjing Agricultural University in China, MICRA, Indonesia, Seeds and Fruits Multi-Purpose Cooperative in Benguet and Bukidnon Multipurpose Cooperative Bank in Philippines. We are thankful to the institutions supported this pilot testing process.

The editors would like to put in record special gratitude to those individuals who prepared the report and the colleagues of IFAD from Asia-Pacific Division who provided valuable information and shared their insights and experiences and supplied the requisite and appropriate information and data to synthesize this report on implementation process.

Further, we would like to extend our thanks for the active participation of the members of the Study Country Working Groups, particularly: Dr. Longyao Zhang of Nanjing Agricultural University and Dr. Enjiang Cheng of Ford Foundation, China; Ms. Yunita Resmi Sari of Bank Indonesia, Mr. M. Alfi Syahrin of MICRA-Indonesia and Mr. Joel Q. Matira and Ms. Cristina G. Lopez of Agricultural Credit Promotion Council, Philippines. Their feedback provided from the conceptualization to the completion of the final draft of this publication has been very useful to the study team. We are also thankful to Ms. Angela Orlando for helping us to edit the synthesis report.

Last but not least, this regional project has helped strengthening APRACA as knowledge hub, building on the three phases of RuFBeP, and will continue beyond its completion.

Prasun Kumar Das
Asia-Pacific Rural and Agricultural Credit Association (APRACA)

Michael Hamp
International Fund for Agricultural Development (IFAD)

Abbreviations

ACPC	Agricultural Credit Policy Council
ACPC–ICB	ACPC–Institutional Capacity Building group
AGFP	Agricultural Guarantee Fund Pool
AgVCF	Agricultural Value Chain Finance
APRACA	Asia-Pacific Rural and Agricultural Credit Association
ASHTI	Asian Hybrid Seeds Technologies, Inc.
AVC	Agricultural Value Chain
BCB	Bukidnon Cooperative Bank
BMT	Baitul Maalwat Tamwil (Islamic Cooperative)
CBRC	China Banking Regulatory Commission
CFPA Microfinance	China Foundation for Poverty Alleviation Microfinance
CWG	Country Working Group
HTRCB	Huainantongshang Rural Commercial Bank
IDR	Indonesian Rupiah (Indonesian Currency)
IFAD	International Fund for Agricultural Development
KSP	Koperasi Simpan Pinjam (Saving and Lending Cooperative)
KSU	Koperasi Serba Usaha (Multipurpose Cooperative)
KUD	Koperasi Unit Desa (Village Cooperative)
LKMA	Lembaga Keuangan Mikro Agribisnis (Microfinance Institutions for Agribusiness)
M&E	Monitoring and Evaluation
MBO	Microbanking Office
MFI	Microfinance Institution
MICRA	Microfinance Innovation Center for Resources and Alternatives
MSEs	Micro and Small Enterprises
NLDC	National Livelihood Development Corporation
NGO	Non-governmental organization
NPL	Non-performing loans
OBO	Other Banking Office
PCIC	Philippine Crop Insurance Corporation
PHP	Philippine Peso (Philippines Currency)
RCB	Rural Commercial Bank
RCCF	Rural Credit Cooperative Federation
RFI	Rural Financial Institution
RMB	Renminbi Yuan (Chinese currency)
RuFBeP	Rural Finance Best Practices
SFMPC	Seeds and Fruits Multi-Purpose Cooperative
UGT	Usaha Gabungan Terpadu (Integrated Joint Business)
USP	Usaha Simpan Pinjam (Savings and Loan Unit)
VCF	Value Chain Finance

Conversions:

- Currencies: *US$1= 6.28 RMB (Yuan); 51.25 PHP (Peso) and 13,390 IDR (Rupiah)* (As on 31 January 2018)
- Land Area: *1 Hectare = 15 Mu of Land in China; For Philippines and Indonesia they use the international measurement systems in Acre and Hectare.*

Executive Summary

Improved access of rural households and communities to financial services continues to be crucial for agricultural development and poverty reduction in Asia. Despite numerous barriers that still exist, innovative ideas and good practices in rural finance are constantly being developed and tested that, nonetheless, have achieved success in many countries of the Asia-Pacific region.

Against this backdrop, the International Fund for Agricultural Development (IFAD) has partnered with the Asia-Pacific Rural and Agricultural Credit Association (APRACA) on a project to identify opportunities available for expanding access to rural financial services for the poor in the region and to document global best practices on sustainable models of pro-poor rural financial services. (RuFBeP project). The project is being carried out in four phases.

This document is the synthesis of the processes adopted during Phase II of the project: the adaptation and piloting of selected innovative good practices within specific country contexts. This report describes the process of implementation of pilot projects in the People's Republic of China, the Republic of Indonesia and the Republic of the Philippines. This document captures the experiences of the three country project teams and is meant to share findings, lessons and recommendations regarding their suitability for scaling up at the larger context.

COUNTRY SPECIFIC FINDINGS

China

- Three best practices of China's rural finance sector were selected for detailed study during Phase I of the RuFBeP project: (i) mobile banking for the poor by Chongqing Rural Commercial Bank, (ii) microfinance programme for the rural poor by China Foundation for Poverty Alleviation Microfinance and (iii) microfinance downscaling by city and rural commercial banks in China. After close consultation with the China Banking Regulatory Commission (CBRC), the country working group decided that the second phase of the pilot should concentrate on microfinance downscaling with loan products aimed at strengthening the actors within the agricultural value chain (AVC). AVC finance is rapidly developing in China in response to the process of urbanization and farm consolidation. While many rural financial institutions in China have been interested in AVC finance, few have experience with these schemes or knowledge about best practices. The urbanization and farm consolidation has also increased the capital requirements of small and medium rural enterprises. The smaller loan sizes offered by MFIs mean they are less able to meet these new financial demands. This has created opportunity for formal rural financial institutions to fill the gap in microfinance lending and to simultaneously strengthen the value chain. The China pilot was conducted in Huainan province and led by the Huainantongshang Rural Commercial Bank (HTRCB). A central component of the project was the building of the bank staff's knowledge of and capacity to apply the model of microfinance downscaling and to shift from more traditional lending methods to agricultural value chain lending. Major clients of the downscaling were AVC actors: individual farmers, agricultural cooperatives, traders and agro-processors. Four new products were designed by HTRCB to target these clients: cash-flow-based lending, a group guarantee loan, an insurance combined loan and a mixed guarantee loan.

- External challenges identified in China were credit risks as a result of rising debt and an expected rise in unemployment as a consequence of government adjustments in certain industries. Project-related challenges included establishing buy-in and commitment to the pilot from the bank partners, devising strategies to include small operators in value chain finance and sustainability beyond project.

- Overall, the experience in China demonstrated that it was possible for the bank to adapt their loan products and grow in their capacity to reach more small and medium enterprise clients as well strengthen the agricultural value chain in Huainan province. The success there depended on a number of factors, for instance the large farm sizes, a well-developed infrastructure and good communications systems. These factors should be carefully considered before replicating the project in less developed regions of China. The project recommended extending the pilot to other branches of the bank before replicating it by additional rural financial institutions in other areas.

Indonesia

- The Indonesian country working team selected innovative products and lending schemes from the case studies of cooperative financial institutions that were documented in Phase I of the project. The Microfinance Innovation Center for Resources and Alternatives (MICRA), an Indonesian foundation focused on development of the microfinance sector, was the lead coordinating institution for the pilot project. MICRA worked with existing microfinance institutions (MFIs) in the target areas to deliver the financial products developed for the pilot. KSP Sekartani Mandiri, a savings and loan cooperative, implemented the pilot in Sausu Gandasari, Central Celebes. KSU Bina Laut, a multi-purpose cooperative, implemented in Sekotong, West Nusa.

- The project adapted two innovative financing schemes for two pilot locations: collateral-free loans and group lending products. MICRA's project model included targeted interventions for both the borrowers and the local microfinance institutions. Four strategic interventions were designed to achieve project outcomes: Group strengthening of smallholder groups, improved smallholder productivity, broadened market access and improved financial access. MICRA also provided support to the community-based MFIs to enable them to carry out the pilot and continue offering the pilot products even after the project ended. Support to MFIs included training and workshops on financing models and schemes, linking them with micro-insurance providers and connecting them to investor organizations. A key aspect of MICRA's model was devising a loan guarantee scheme to reduce the financial risks to MFIs that delivered the pilot loan products.

- Anticipated challenges centered on the capacity of MFIs to implement new lending products, farmers' capacity to modify farming techniques in order to increase production, farmers' gaps in financial literacy and adjusting to unpredictable market fluctuations. Project implementation revealed additional challenges including limited capital of MFIs resulting in an inability to expand outreach to other beneficiaries, restrictions of a cooperative's activities based on its legal entity status and some operational challenges related to outdated administrative procedures used by the MFIs.

- The Indonesia pilot has increased the number of people who: (i) access formal financial institutions, (ii) are aware of financial products available to them, and (iii) take advantage of financial products that are suitable for them. Both productivity and incomes of fishers and farmers have increased as a result of the project.

- At the end of the project, the county working group discussed how to strengthen the piloted schemes and reach more people. They recommended the adoption of a business-to-business model whereby MFIs would operate at the centre of the initiative and would strengthen, maintain and cultivate partnerships with a broad range of stakeholders to deliver services, broker market linkages and extend financing to more rural clients.

Philippines

- Several successful practices were considered for piloting in the Philippines. Among them were examples from *microbanking* offices that successfully expanded outreach in hard-to-reach areas, the utilization by GM bank of the government's loan guarantee scheme to lower the bank's cost in providing services to high-risk borrowers and a value chain financing scheme that secured contracts between an onion farmers' cooperative and a multinational chain of fast food restaurants. The Philippines chose to pilot agricultural value chain financing modelled after onion farmers' experience. The scheme was piloted in two provinces with local MFI implementing partners: the Bukidnon Cooperative Bank, in Sumilao, Bukidnon and the Seeds and Fruits Multi-Purpose Cooperative in Buguias, Benguet. The project was structured around four main components: capacity building for small farmers, financing, crop insurance and credit guarantee schemes and market linkage.

- The Philippines foresaw difficulties in moving farmers from a traditional to a more entrepreneurial and business-minded way of farming, the potential for fund diversion, potential for calamities resulting in crop failure and non-payment of loans and possible low harvest. Key challenges that arose during implementation included the need to strengthen the business, management and accounting systems of the MFI partners, need for additional capital to extend loan terms, sustainability and expansion of piloted practices beyond the project and poor road conditions making transport of good difficult.

- Important results of the pilot in Benguet include increased membership in the cooperative, 100 percent loan collection, expansion of cooperative activities into livestock production and a dramatic increase in supply contracts with institutional buyers.

- The Bukidnon pilot successfully established a tripartite agreement between corn farmers, the Bukidnon Cooperative Bank and Asian Hybrid Seeds Technologies, Inc. (ASHTI), a hybrid seed corporation. This agreement guaranteed a market for the farmers' produce and gave them a better price and ensured ease in loan repayment.

- The experience with agricultural value chain financing in the Philippines led to some key recommendations for increasing the viability of AVC financing schemes. In sum, strong AVC financing will build the capacity of small farmers to participate in the value chain, base interventions on a solid understanding of smallholders' needs, familiarize all stakeholders with the structure and dynamics of the value chain, identify an effective lead partner in the AVC scheme, provide both financial and non-financial services and work with policy makers to ensure adequate infrastructure in rural areas.

PROJECT MONITORING AND EVALUATION

All project teams engaged in on-going monitoring of activities and measured progress towards outcomes during implementation. Each pilot also carried out an end-of-project impact evaluation. Teams developed indicators in alignment with their project frameworks and carried out baseline studies. Subsequent measurements were compared against the baseline. In addition to assessing the degree to which projects achieved the intended outcomes and impact that the pilots aimed for, key lessons were derived from monitoring and evaluation exercises.

KEY LESSONS FROM PROCESS OF IMPLEMENTATION

There was considerable variation regarding the financial practices that were piloted in the three countries, the characteristics of the pilot locations and beneficiaries and the types of institutions involved in project implementation, nevertheless, some common lessons have emerged. These can be summarized as follows:

- It is imperative to invest proper time and resources in project design when introducing new and complex innovations or schemes.
- Targeted capacity development at all levels of the project is fundamental to success.
- A strong enabling environment is vital for successful implementation and future sustainability.
- Loan products must be adapted to fit borrowers' needs.
- Adaptation of loan products helps financial institutions mitigate risk.
- Institutions should improve communication with clients about loan product details and other services.

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SECTION 1
Introduction

1.1 PROJECT BACKGROUND

The rural economy of Asia is huge and heterogeneous. On the one hand, Asia is home to some of the most dynamic and successful agribusinesses setups in the world that satisfy domestic food demands and also penetrate competitive foreign markets. On the other hand, it is home to millions of poor people who are only slightly better off than their ancestors and further progressing on the path of development. Prior to the financial and economic crisis that began in 1997, the region had some of the fastest-growing economies in the world alongside some with poor economic performance. While the rural financial markets in a few countries are served by strong financial institutions that provide sophisticated services on market terms, others are still dominated by weak and subsidized institutions and non-governmental organizations (NGOs) that are dependent on donors and whose sole function is to dispense credit.

Improved access of rural households and communities to financial services continues to be crucial for agricultural development and poverty reduction. Despite numerous barriers that still exist, innovative ideas and good practices in rural finance are constantly being developed and tested that, nonetheless, have achieved success in many countries of the Asia-Pacific region.

It was observed that many of the institutions across the globe introduced pro-poor, innovative best practices in rural financial services most of which are regional and targeted for certain communities and eventually emerged to be scalable. However, the process of designing, and implementation process for practical use by the interested institutions are almost absent. In one of the study made by World Bank (1997) documented the issues related to design and best practices of rural financial services across the globe. This report is an effort to enrich the body of knowledge in this sector and support financial institutions in expanding access to rural financial services for the poor. IFAD has partnered with The Asia-Pacific Rural and Agricultural Credit Association (APRACA) to carry out the project "Documenting Global Best Practices on Sustainable Models of Pro-Poor Rural Financial Services in Developing Countries" (RuFBeP).

The overall goal of the RuFBeP project is to sustainably reduce rural poverty and improve food security for rural communities in the Asia-Pacific region. It seeks to assist rural finance providers and governments in extending financial services on a sustainable basis through the application of best practices suitable to their unique operating environments.

The project in being carried out in five countries[1] in the Asian subcontinent and implementation is spread over four phases (*Box 1*).

Box 1: Four phases of the RuFBeP project

Phase I: mapping and surveying select global best practices in identified themes and rating their appropriateness for the Asia-Pacific region

Phase II: adapting and piloting selected best practices to test their effectiveness

Phase III: promoting best practices through awareness raising, advocating their implementation, and hosting policy dialogues

Phase IV: sharing best practices through workshops, conferences and the establishment of a knowledge hub

[1] The five project countries are China, India, Indonesia, the Philippines and Thailand.

1.2 BEST PRACTICES IN RURAL FINANCING

The aim of Phase II of the RuFBeP project was to test the effectiveness of a selection of high-impact best practices and to determine their suitability for scaling-up in projects sponsored by financial institutions, governments, the International Fund for Agriculture Development and/or other funders. Insights from the case studies documented in Phase I shaped the recommendations for pilot testing of the good practices in three countries: China, Indonesia and the Philippines.

1.2.1 China

The Chinese Government is committed to the elimination of rural absolute poverty by 2020. China's efforts in poverty reduction have been characterized by development-oriented poverty reduction primarily through agricultural development and job creation in rural areas. Agricultural finance is an integrated part of the rural poverty reduction strategy in China. The first phase of the RuFBeP project in China identified three best practices by rural commercial banks and microfinance institutions:

1. mobile banking for the poor by Chongqing Rural Commercial Bank;
2. microfinance programme for the rural poor by the China Foundation for Poverty Alleviation Microfinance (CFPA Microfinance); and
3. microfinance downscaling by city and rural commercial banks in China, in which a bank or other formal financial institution expands its services to work with clients traditionally served by microfinance institutions.

In addition to these practices, strong recommendations to invest in efforts to promote agricultural value chain (AVC) finance also emerged from the Phase I case studies.

The second phase of the RuFBeP project was conducted in China at a time of accelerated agricultural transformation. As more and more labourers moved out of agriculture, many small farmers rented out their land and the average farm size in Anhui province, where the project was piloted, and neighbouring provinces jumped from less than a hectare to ten hectares or more. As a consequence, farm production became more specialized. The agricultural transformation in China has important implications for rural financial services and products. First, the market for traditional rural microfinance loans [in the range RMB 3 000 to 5 000 (USD 500 to 800)] for mixed income generation activities has shrunk. Second, the markets for larger agricultural loans and loans for off-farm employment in rural townships and small cities have been on the rise. These new financial circumstances created an opportunity for formal rural financial institutions to fill the microfinance gap. A third result of the process of urbanization and farm consolidation in China is the rapid development of AVC finance. Although many rural financial institutions in China are interested in AVC finance, they have limited prior knowledge of these types of schemes and lack training in good practices.

Given the presence of all of these factors, the China Banking Regulatory Commission (CBRC) and the project team decided to concentrate the second phase of the pilot on the Phase I best practice of microfinance downscaling with loan products targeted toward AVC actors. Originally based on a model introduced by IPC, microfinance downscaling by rural commercial banks increases access of micro and small enterprises to formal credit based on cash flow analysis. This process evaluates the capacity and willingness of clients to repay loans based on field visits by a credit officer who aims to understand the client's production, marketing, fund flows, purpose of the loan, assets and liabilities, income, profit and loss, credit history and reputation. Soft data is translated into financial statements upon which the bank can determine loan viability.

Capacity development in both microfinance downscaling and in AVC constituted an essential component of the project framework.

1.2.2 Indonesia

Globally ranked, Indonesia is the fourth most populated country in the world with an extensive coastline and great agricultural potential. As of 2014, 27.7 million people in Indonesia are living below the poverty line with the majority of them being scattered in rural areas. Therefore, poverty alleviation programmes are considered critical in these rural areas. Agriculture is the main source of livelihoods in Indonesia. An estimated 38.97 million people (34 percent) work in the agricultural sector[2]. Additionally, in 2012, around 6.4 million people were engaged in inland and marine fishing and fish farming. However, low credit disbursement in this sector is one of the indicators of the lack of financial access in rural areas. Therefore, improving access to the financial services for the agricultural and coastal communities in Indonesia is one of the key factors to support national growth.

The first phase of RuFBeP in Indonesia successfully documented three case studies of membership-based cooperative financial institutions that promote inclusive rural financial services.

The Phase I study looked at key features of each of the financial institutions themselves as well as the innovative services and products they offer. One innovative product from each institution was chosen for pilot testing as outlined below:

1. **LKMA Pincuran Bonjo** is a community-initiated rural financial service scheme operating in West Sumatra province. Pincuran Bonjo uses an integrated rural financial framework by providing financial and non-financial services to the clients and the community. Their innovative collateral-free loan was selected for pilot testing in both of the pilot locations.
2. **USP Grameen Pesisir** is a business unit of the KUD Mina Samudera cooperative. Its products include loans and savings. The Phase I study documented their group lending approach. The loan target is poor families, especially women who have a potential business or will develop a business or need additional money to support their husband in running household business activities. There is no physical collateral but each loan is a joint liability of the group members. If the members show good performance in repayment and obey the rules, they can apply for a second loan and the value can be doubled. For the Phase II pilot, a group lending scheme was developed for members of fishers' cooperatives based on the Grameen Pesisir model.
3. **BMT UGT Sidogiri** is an Islamic financial services cooperative based on the Islamic/sharia system. As a general principle in Islamic finance, interest is prohibited. Therefore, BMT UGT Sidogiri uses an *aqad,* or contract, called sharia contract/agreement. Based on the *aqad*/sharia contract agreement, the returns can be in the form of trading margin, profit sharing, rental fee, guarantee fee and others. The pilot project replicated financing for unbanked micro and small enterprises based on best practices of BMT UGT Sidogiri.

An important consideration in the selection of best practices and development of products for the Indonesian pilot projects was the country's geographic and regional diversity with its unique cultural, social and economic values. Replication or scaling up of rural finance best practices was carefully adjusted and adapted to the local political, economic, social and environmental circumstances of the pilot areas. This is described in more detail in Section 4.1.2.

1.2.3 Philippines

The Phase I case studies of best practices for the Philippines were chosen based on three criteria: accessibility for the poor, technical and financial feasibility and cost effectiveness and profitability.

The first case looked at the way in which the establishment of microbanking offices (MBOs) and other banking offices (OBOs) has enabled CARD Bank to significantly expand its outreach even in hard-to-

[2] Statistical Yearbook of Indonesia 2014; BPS-Statistics Indonesia, August 2014 (https://www.bps.go.id/publication/2014/05/05/8d2c08d9d41aa8c02fad22e7/statistik-indonesia-2014.html)

Table 1: Best practices piloted in Phase II

Pilot Product/Services	Brief Description of Product	Pilot Location	Implementing Partner	Implementing Agency
Indonesia				
1. Non-collateral lending for micro loans *2. Sharia-based financing loan scheme with profit sharing feature*	Collateral-free lending system for small farmers based on the Phase I case study of LKMA Pincuran Bonjo. Non-interest bearing loans based on a profit-sharing agreement. Loans were targeted at non-banked small and medium enterprises based on the model from the Phase I case study of BMT UGT Sidogiri.	Village: Setkong Barat District: Setkong Province: West Lombok	*KSU Bina Laut*, and MFI based in Lombok Island	MICRA Indonesia under the supervision of Bank Indonesia
1. Non-collateral lending for micro loans *2. Group lending*	Collateral-free lending system for small holders based on the Phase I case study of LKMA Pincuran Banjo. Group lending to members of fishers' cooperatives based on the Phase I case study of USP Grameen Pesisir.	Village: Sausu Gandasari District: Piragu Moutong Province: Central Celebes	*KSP Sekartani Mandiri*, an MFI based in Central Celebes province	
Philippines				
Value chain finance	Financing the value chain of highland vegetables	Benguet; La Trinidad; Baguio City	*Fruit & Seeds MPC* in Benguet province	Agricultural Credit Promotion Council, Philippines
		Malaybalay Municipality, Bukidnon province	Bukidnon Cooperative Bank	
China				
Microfinance lending downscaling	The adoption by a rural commercial bank of advanced lending technology to downscale microfinance to lower-end clients on cash flow basis in order to expand outreach. Building capacity of bank staff to adopt this technology and to shift from traditional lending to value chain lending was a central part of the project framework.	Huainan Prefecture, Anhui province	Huainantongshang Rural Commercial Bank	Huainantongshang RCB under the supervision of the China Banking Regulatory Commission

reach areas. The second case documented how GM Bank, a rural bank, has utilized the government's loan guarantee scheme to lend to small farmers who cannot provide collateral. The guarantee scheme lowers the bank's risk and cost allowing GM Bank to successfully expand its financial services lending to small farmers who are perceived as high-risk borrowers. The third case described a value chain financing project in which the Kalasag Farmers' Cooperative, a cooperative of onion farmers in Nueva Ecija, organized and successfully linked with Jollibee Foods Corporation, a Filipino multinational chain of fast food restaurants. The fourth case documented the growth and development of microfinance under a conducive policy and regulatory environment created by the government with donor assistance. Originally, three best practices were considered for pilot testing. However, due to budget and time constraints the country working group decided to focus on agricultural value chain finance patterned from the Kalasag Cooperative experience for pilot testing in two provinces.

A summary of the best practices chosen in each pilot project, the pilot locations and implementing partners is presented in Table 1 below.

1.3 PURPOSE OF THIS DOCUMENT

This document aims to improve inclusive rural financial services in Asian countries by documenting the experiences and lessons from the process undertaken in piloting rural finance best practices for example downscaling of rural finance products in China, Innovative lending products in Indonesia and agricultural value chain finance in Philippines. It is a synthesis of all the processes involved in the selection, design and implementation of the best practices that were pilot tested in each country. The documentation of these experiences is intended to support the development of rural finance framework and to serve as guide for the implementation of financing schemes that will help achieve a sustainable market for and stabilized pricing of farmers' agricultural products. The information shared in this report can also serve as a reference for mainstreaming these projects should the pilot testing be a success. This document is written for commercial and policy banks in agricultural and rural development, relevant government agencies, academics and rural finance practitioners.

The report is divided over eight sections. The next section presents the three distinct project frameworks followed by Section 3 illustrating each project's theory of change. Section 4 describes the implementation processes followed in each country providing contextualised details for each pilot. Section 5 summarizes the key lessons learned during implementation while Sections 6 and 7 present in detail the project challenges and the monitoring and evaluation plans for the three countries respectively. Finally, Section 8 concludes the report with a summary, conclusion and main recommendations emerging from the country experiences.

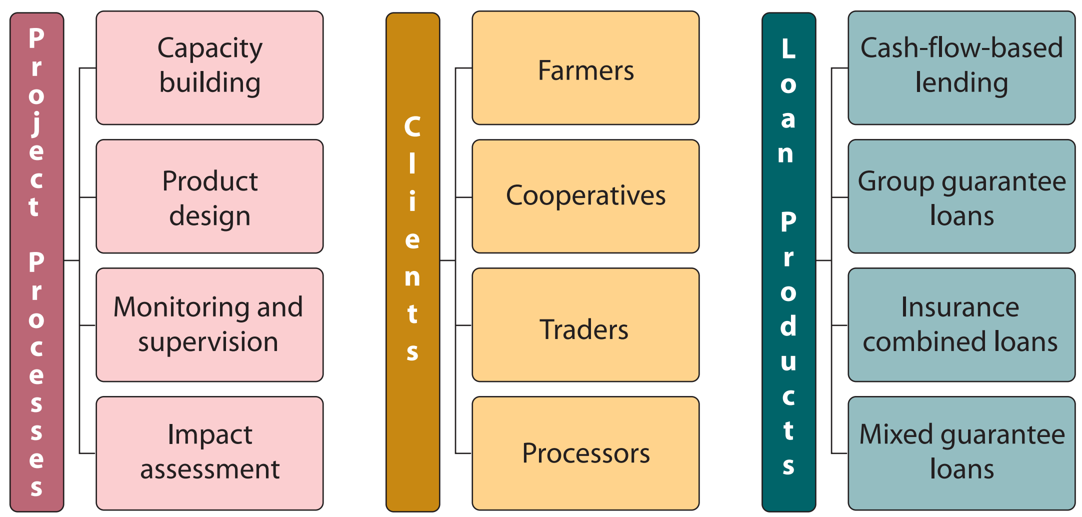
SECTION 2
Project Framework

The project frameworks here present a concise summary of main interventions in each type of rural finance products and in each country, however with some variation. For example in case of China, the framework provides a short description of the major components of each project, targeted beneficiaries and loan products. The other two project teams in Indonesia and Philippines also identified the main activities and intended outcomes for each component in formats similar to a results chain.

2.1 CHINA

Huainantongshang Rural Commercial Bank (HTRCB), the main project implementation partner, and associated consultants formulated a project framework for the microfinance downscaling at the project inception in mid-2016. The framework consisted of the following three major components: project processes, project clients or beneficiaries and the lending products designed and to be tested on the ground. The project framework for the HTRCB pilot is displayed in *Figure 1*.

Figure 1: Project framework of HTRCB pilot



Source: Country Process Document, 2017

Four key project processes supported the piloting of the AVC scheme.

1. **Capacity building** was considered essential for project success and was delivered in two major areas: microfinance downscaling lending and AVC finance. Because the lending products were targeted to AVC actors it was critical for the bank officers to understand not only how to adopt the downscaling but also to learn more about value chains and value chain financing. A study tour and in-house training were two key elements of the capacity building component.
2. **Loan product design** was conducted by staff from HTRCB, based on the training and the results of the local economic potential and demand studies.
3. **Monitoring and supervision** concentrated on specific credit risks related to AVC financing. Important information was fed back to management for product redesign.

4. **Impact assessment** was conducted at the two levels: product impacts on the borrowers and the impact on all the other players in the value chain.

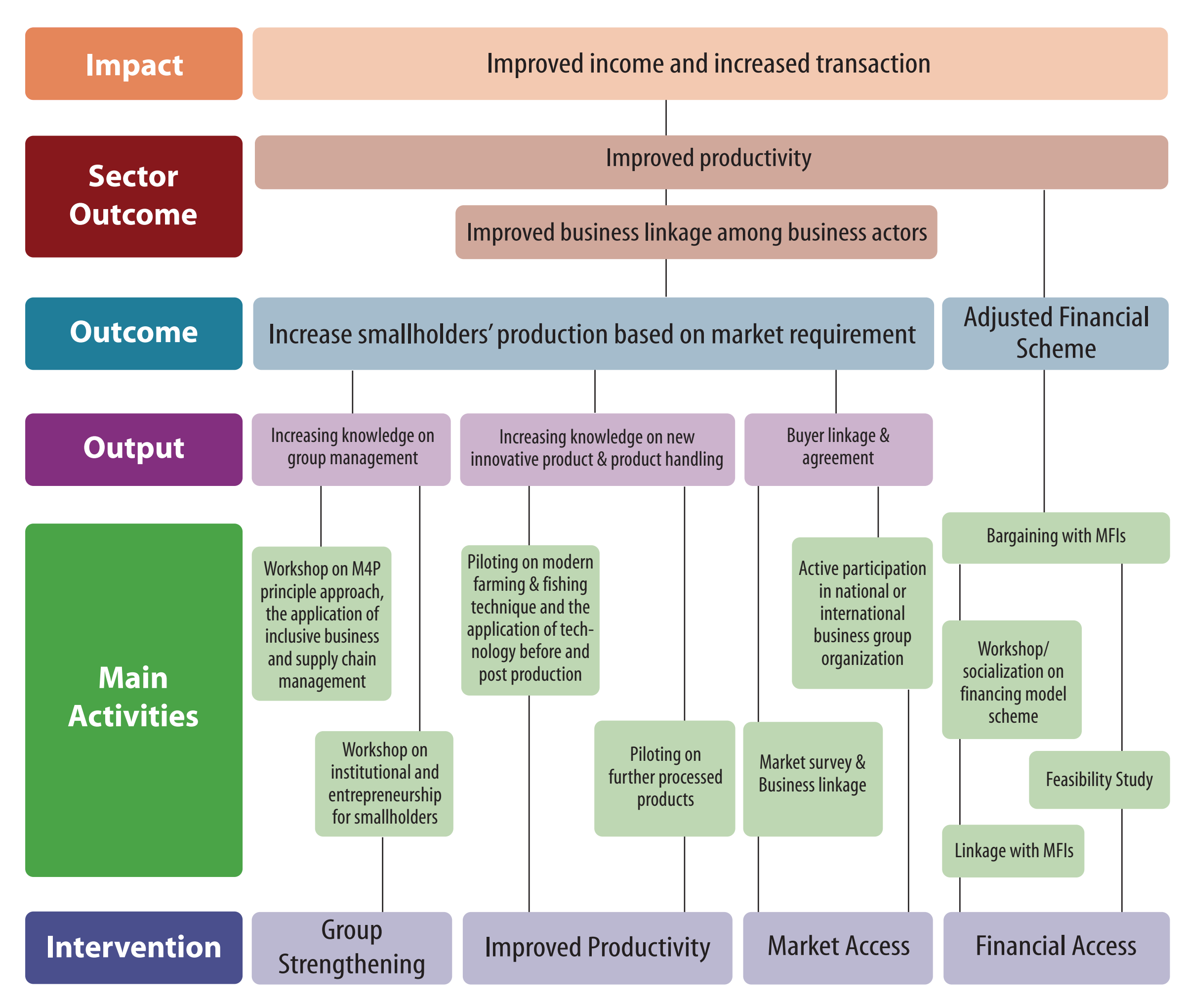
Major clients of the AVC scheme were identified as individual farmers, agricultural cooperatives, traders and agro-processors. Four new products were designed by HTRCB to target these clients (see *Figure 1*). Efforts were made to provide loans to those AVC clients who had sales contracts. The bank also considered providing loans and other forms of financial products based on receivables and future warehouse receipts, following AVC development in the region.

2.2 INDONESIA

The Microfinance Innovation Center for Resources and Alternatives (MICRA), an Indonesian foundation focused on the development of the microfinance sector, was the lead coordinating institution for the pilot project. MICRA disbursed funds to existing MFIs in the target areas who delivered the financial products developed for the pilot.

The project provided three innovative financing schemes in two pilot locations: collateral-free loans, group lending products and Sharia-based financing. The project framework, summarized in *Figure 2* below, included benefits for both the local microfinance institutions and smallholders. Support for MFIs was intended to ensure the continuation of best practices after the completion of the project.

Figure 2: Project framework of MICRA



Source: Country Process Document, 2017a

Four strategic interventions were designed to achieve project impacts:

1. **Group strengthening** of smallholder community groups encouraged the formation of strong internal foundations to keep up their businesses and allow them to explore and develop their business potential. Workshops on entrepreneurship and programme management knowledge were offered to business groups as part of this component.

2. **Improved productivity** to meet the demand for increased quantity and higher quality standards was of critical importance. The project provided expert assistance in farming and fishing production processes to increase smallholders' knowledge about innovative products. It was also projected that improved quality would broaden opportunities for market access.

3. **Broadening market access** involved brokering long-term buying contracts for smallholders. Smallholders with buying contracts tend to increase their revenue and improve their production systems and financial management. In addition, buying contracts prevent farmers and fishers from selling their products early for lower prices. The project carried out a market survey and encouraged active participation in national and international business group organizations.

4. **Improving financial access** for smallholders was seen as central to their ability to obtain the additional capital required to increase volume and product quality. The project planned a feasibility study to identify proper financial services available to smallholders that could accommodate the demands of increased production. It was projected that once communities increased their production, other related stakeholders and microbusinesses would also be impacted including distribution carriers, warehouses, packaging services, processed product businesses, etc.

   MICRA recognized that MFIs would need additional support and training to improve financial access for smallholders. To address this, the project planned to link MFIs with other related organizations and provide workshops on financing models and schemes. The aim was to increase the likelihood that the piloted financial services and products would be continued after the project ended. Main activities of the financial access component included:

   1. Introducing micro-insurance products and connecting MFIs with insurance providers to help the MFIs mitigate risks and provide convenience for their clients,
   2. Connecting MFIs with available capacity building programmes to improve their knowledge and support the advancement of the best practices,
   3. Connecting MFIs to investor organizations to ensure the pilot's sustainability, and
   4. Broadening market access by increasing the involvement of related stakeholders such as buyers, government and local NGOs.

2.3 PHILIPPINES

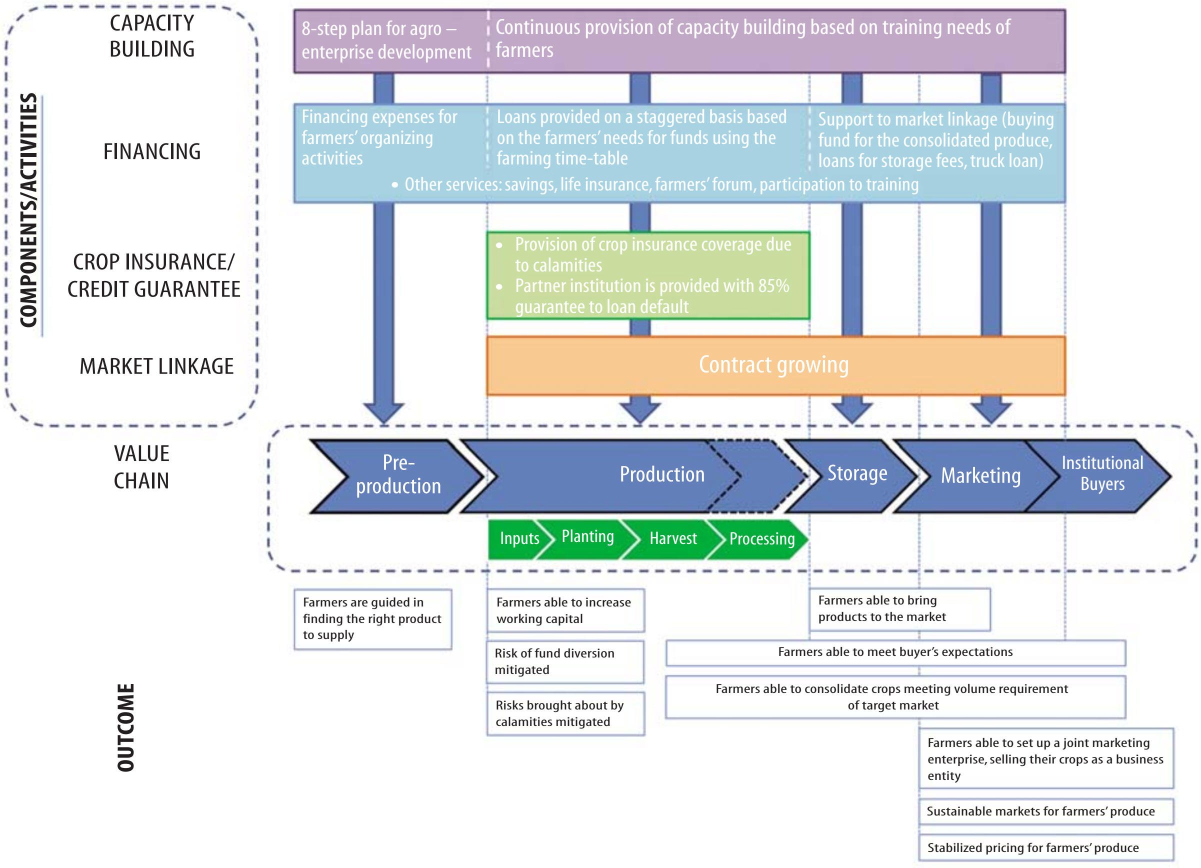
The Philippines pilot project framework was based on the design of the Kalasag Cooperative's agricultural value chain with the important addition of crop insurance and credit guarantee. The four pilot project components included:

1. **Capacity building**, which involved organizing small farmers into small agro-enterprise clusters and providing on-going capacity building activities based on the needs of the individual farmers and their organizations.
2. **Financing**, which was made available throughout all phases of the value chain; from pre-production to production to marketing.

3. **Crop insurance and credit guarantee**, which was incorporated based on another of the Phase I best practices, to help mitigate the inherent risks in financing agriculture.
4. **Market linkage**, whereby the project assisted farmers in finding institutional buyers and establishing contracts and agreements between the farmers' organizations and the buyers.

The flowchart of the agricultural value chain finance pilot testing is presented in *Figure 3*.

Figure 3: AVC pilot project flowchart, Philippines



Source: Country Process Document, 2017b

SECTION 3
Theory of Change

The theory of change for the pilot projects articulates the thinking behind the interventions describing why and how they will lead to a project's intended changes or outcomes. The theory of change provides details that link the project's activities and the achievement of the project's long-term expected goal. Pilot project teams developed their theories to change to inform the development of their project framework, results chain and project monitoring and evaluation plans.

3.1 CHINA

The pilot project by HTRCB expected to initiate the downscaling model with HTRCB in Huainan and then extend it to other financial institutions in Huainan, Anhui and other parts of China. Given limited project implementation time (about 12 months), it was reasonable to anticipate that HTRCB would continue and expand its AVC finance programmes beyond the project, to move beyond the four existing loan products to loans based on receivables and warehouse receipts, and other financial products based on AVC, such as financial leasing. Other financial institutions in China, such as other rural commercial banks (RCBs), urban commercial banks and MFIs, even the state owned commercial banks were expected to follow suit. The project team anticipated that the introduction and replication of microfinance downscaling with associated AVC financing would greatly improve access to affordable financial services for smallholders and traders and possibly agricultural cooperatives, through collateral and guarantees linked to AVCs.

The following four new loan products were designed by HTRCB for the pilot in Huainan Prefecture in Anhui province of China:

1. Cash-flow-based lending guaranteed by a third party up to 24 months (<=RMB 500 000)
2. Family union guarantee loans up to 36 months (<=RMB 1 000 000)
3. Mixed guarantee loans (collaterals plus guarantee) up to 60 months (<=RMB 1 000 000)
4. Insurance policy loans up to 36 months (<=RMB 1 000 000)

HTRCB introduced cash-flow-based loans targetting micro and small enterprises in the non agricultural sectors before the project implementation. The introduction of cash-flow-based lending system into agricultural production and marketing meant that the bank's loan officials had to learn techniques for the assessment of net assets and cash flows for their clients in commodity value chains. The group guarantee loans under the project targeted agricultural-related businesses while the traditional group guarantee loans in China targeted small rural households with a loan size.

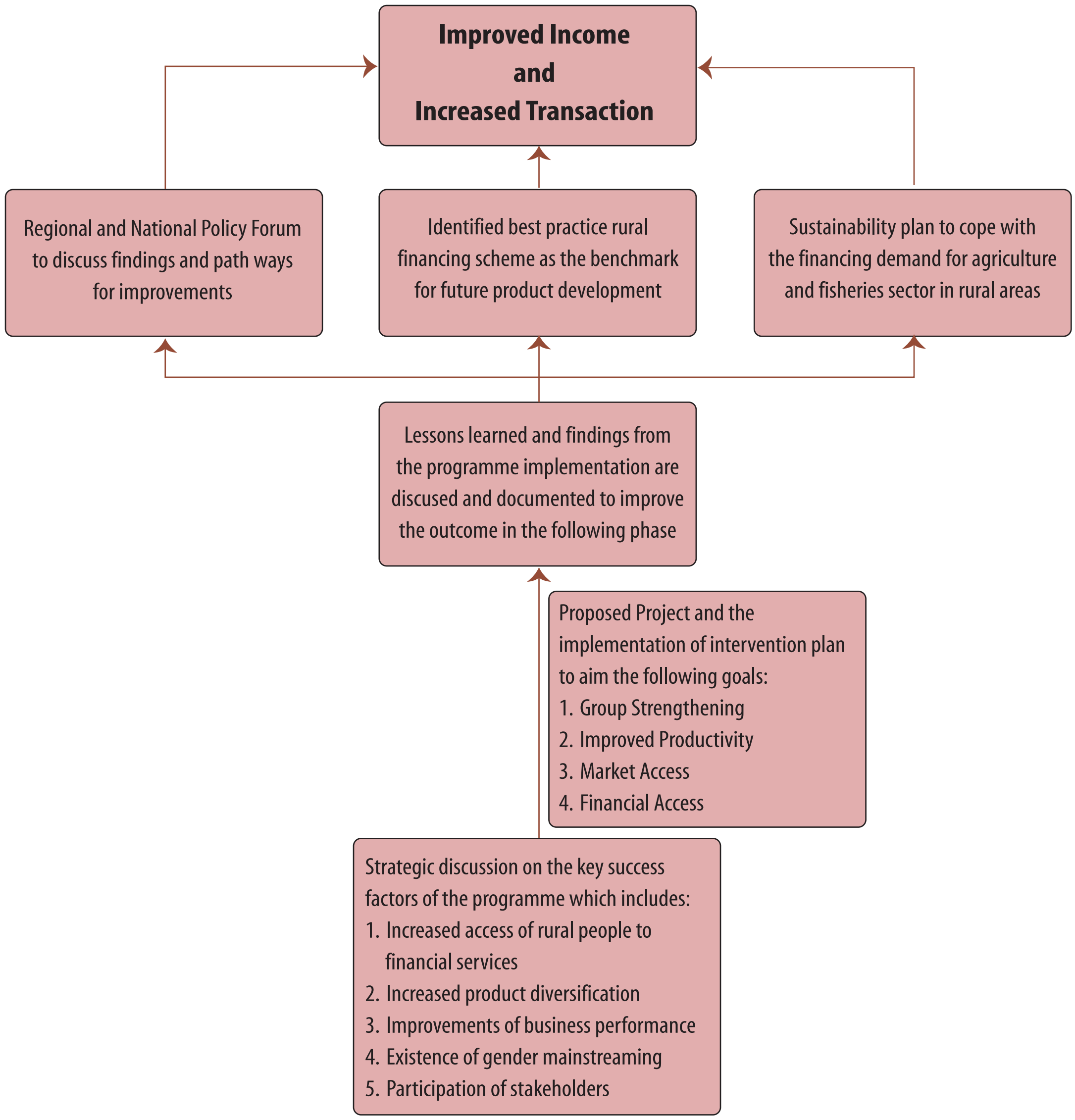
The key to the success of collaterised loans was expected to depend on the varieties of collateral used to access loans. In China, farmland and farmhouses are not eligible as collaterals for loans. However, the government has recently encouraged the use of land operations rights as loan collateral. This new policy approach was tested under the pilot project. The insurance policy loan was a new loan product jointly developed with a large agricultural insurance company in China, loan repayment was insured by the insurance company.

Taken together, the increase in the loans disbursed for agricultural trade processing and the supply of farm input is expected to greatly enhance the development of agricultural value chains in the project area and address the growing financial needs created by rapid urbanization and farm consolidation.

3.2 INDONESIA

As stated in the framework, the project was expected to improve smallholders' income and business transactions. To support this goal, the project started off with a strategic discussion with stakeholders to enhance cooperation and determine the project's key success factors. MICRA then took these ideas forward and proposed to implement the pilot with the selected MFIs. The lessons learned and other findings derived from the on-going project implementation were projected to result in better performance in the subsequent phases of the RuFBeP project. It was expected that the lessons on the results of the rural financing pilot would serve as a benchmark for future development on which to build a comprehensive sustainability plan to cope with the financing demand for the designated sectors. Considerations for scaling up the idea would be further discussed with a larger audience at a regional or national policy forum. Eventually, the schemes piloted this project are expected to responsibly and sustainably improve the business of smallholder farmers and coastal communities. The ideas visualized for the theory of change are presented in *Figure 4*.

Figure 4: Theory of change, Indonesia



Source: Country Process Document, 2017a

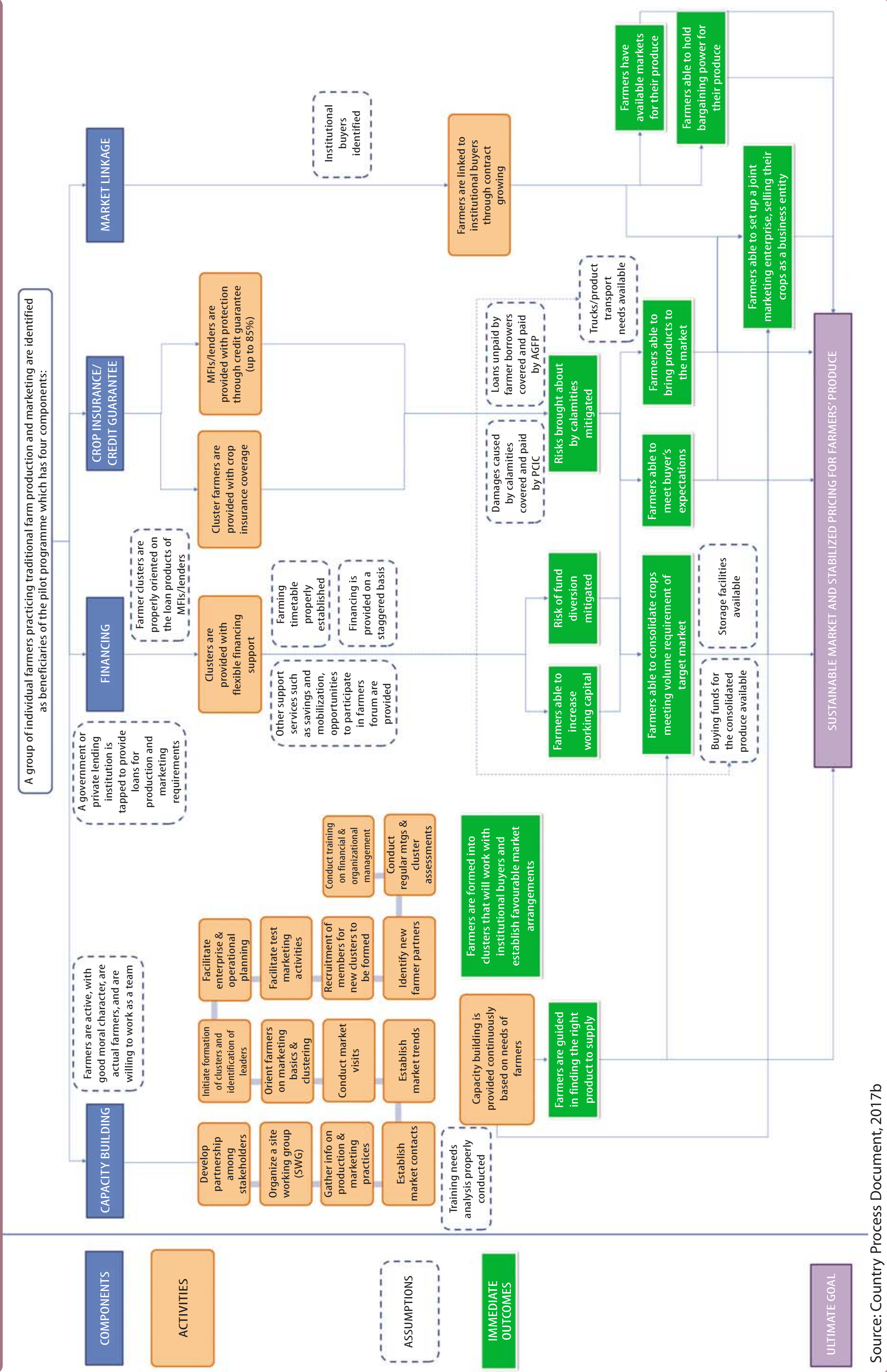
3.3 PHILIPPINES

The project's theory of change (*Figure 5)* suggested that its ultimate goal of a sustainable market and stabilized pricing for farmers' produce would be attained when the following outcomes were achieved: (i) farmers were formed into clusters that worked with institutional buyers and established favourable market arrangements, (ii) farmers were guided in finding the right product to supply, (iii) farmers were able to increase working capital, (iv) financing risks were lessened, (v) risks brought about by calamities were mitigated, (vi) farmers had available markets for their produce, (vii) farmers held bargaining power for their produce, (viii) farmers consolidated crops and met the volume requirements of the target market, (ix) farmers met buyers' expectations, (x) farmers were able to bring their products to the market and (xi) farmers set up a joint marketing enterprise, selling their crops as a business entity.

These outcomes were predicted to be achieved through the various activities under the four components of the project: capacity building, financing, crop insurance and credit guarantee and marketing. To support these changes, the following were the key assumptions:

1) For capacity building activities to work: That the farmers were active with good moral character, were actual farmers, were willing to work as a team and that training needs of individuals and organizations were properly identified.
2) For financing to serve its purpose: (i) that a government or private lending institution was tapped to provide loans for production and marketing requirements, (ii) farmer clusters were properly oriented to the loan products offered by the MFIs/lenders, (iii) an accurate farming timetable was established, (iv) financing was provided on a staggered basis, (v) that other support services such as savings and mobilization, opportunities to participate in farmers' forums were provided.
3) For crop insurance and credit guarantee to protect individual borrowers and financing institutions: (i) that damages caused by calamities were covered and paid for by the Philippine Crop Insurance Corporation (PCIC) and (ii) loans unpaid by farmer borrowers were covered and paid for by the Agricultural Guarantee Fund Pool (AGFP).
4) For market linkage to be sustainable: That institutional borrowers were properly identified, that buying funds for consolidated produce was available and that storage facilities were available.

Figure 5: Theory of change, Philippines



Source: Country Process Document, 2017b

SECTION 4
Process of Pilot Testing

A number of coordinating mechanisms, processes, frameworks and plans were designed and followed by all three of the pilot projects. Each of the project implementation teams:

1. Collaborated with a country working group made up of key stakeholders;
2. Selected the best practices, pilot locations and implementing partners based on the specific country/local context and needs of targeted beneficiaries;
3. Developed a theory of change;
4. Designed a project framework;
5. Developed mechanisms and strategies to create a supporting environment;
6. Carried out a baseline survey;
7. Created a plan for project monitoring and evaluation;
8. Identified expected challenges and plans to address them;
9. Devised frameworks and action plans for project implementation;
10. Carried out the implementation;
11. Established a strategy for capturing lessons learned and documented them; and
12. Reported on project progress.

Although all of the above processes were part of each pilot, there were differences and variations in how they were designed, carried out, tracked, etc. Where possible, relevant considerations that were taken into account in each specific project environment and decisions that were made as a result are explained. For example, in China, the pilot introduced a new financing approach of which few rural banks had prior knowledge or experience. China's project framework included considerable capacity development in order to make the pilot viable. Indonesia's cultural, economic and environmental diversity had a strong influence on which best practices were selected and how they were adapted in each pilot location.

The project frameworks and theory of change were already presented in Sections 2 and 3 respectively. Some of the other implementation processes are also described in separate sections of this report: lessons learned (Section 5), expected challenges (Section 6) and project monitoring and evaluation (Section 7). The remaining processes, and how each country pilot undertook them, are described in detail below.

4.1 SELECTION OF BEST PRACTICES, PROJECT SITES AND PARTNER ORGANIZATIONS

In each of the three country pilots, best practices and pilot locations were selected by the country working groups (CWGs) in close consultation with key project partners.

4.1.1 China

China's country working group and the China Banking Regulatory Commission (CBRC) decided that the Phase II pilot should concentrate on microfinance downscaling with loans targeted to agricultural value chain (AVC) actors in order to respond to the changing needs of China's agricultural sector.

Huainan Prefecture, in Central China's Anhui province was selected as the pilot area. Huainan has a population of 3.8 million, of which 2.06 million live in rural areas and the area has been under the process of accelerated agricultural transformation for some time. There are five districts and two counties in the prefectures. Pilot programme implementation was planned in at least one county and/or one district in the prefecture. A number of townships in the project areas were also selected for piloting. In the head office of the bank, a group was created to oversee the progress of the pilot. A number of bank branches in the pilot county/district were selected to participate in the pilot. The pilot is expected to positively impact AVC players as well as smallholders in the region.

After discussions with CBRC in Beijing and Anhui and with relevant banks and the consultants, Huainantongshang Rural Commercial Bank (HTRCB) was selected as the implementing partner of the pilot. HTRCB is a leading rural financial institution in Huainan Prefecture of Anhui province with its operation covering all four districts and one county in the prefecture. HTRCB is also the largest shareholder of another smaller rural commercial bank in the prefecture.

4.1.2 Indonesia

Two villages in Eastern Indonesia were recommended as pilot project locations based on strategic discussions with the Indonesia country working group. The first village is a farming community in Sausu Gandasari, Central Celebes Province. Smallholders in this region rely on cocoa and copra as the major income-generating commodities. The second village is West Sekotong, West Nusa Tenggara province, where fishing and tourism are the principle economic activities. MICRA identified potential implementing partners from existing microfinance institutions in each project location. To inform the selection, MICRA conducted a simplified social assessment of the potential MFI partners to analyse their institutional and operational capacity to serve the designated communities and assess their potential for social impact and their level of social responsibility. Based on the results, MICRA proposed the following organizations as implementing partners:

1. KSP Sekartani Mandiri in Sausu Gandasari, Central Celebes. KSP Sekartani was initially a farmers' social group named "Sekarsari Farmers Group". KSP Sekartani was officially incorporated in 2009 as a savings and loan cooperative (a Koperasi Simpan Pinjam, or KSP). To date, the institution has grown to include three branches and one headquarters office with 370 active clients.
2. KSU Bina Laut in Sekotong, West Nusa. Since its establishment ten years ago, KSU Bina Laut has been serving the agriculture sector. It was originally a collection of four joint business groups with 40 initial members, all of whom were fishers. In 2005, this cooperative obtained legal status as a multipurpose cooperative (a Koperasi Serha Usaha or KSU).

The Indonesian best practices that were documented in Phase I of the project appeared to have no weaknesses. However, it was not clear to what extent these practices could be adapted to different socioeconomic environments. Indonesia's geographic and regional diversity with its unique social, cultural and economic differences poses a unique challenge for replication and scaling-up of rural financial practices. To address this, MICRA carried out local economic potential analyses and baseline surveys in the target communities. This information, coupled with the analysis of MFI capacity, informed the selection of best practices in each of the pilot areas.

In Sausu Gandasari, KSP Sekartani piloted a non-collateral taking loan as the financial product innovation. Informal leaders, whose influence is still important in the mostly Hindu communities, would serve as the guarantee of the members' loan. Many of the smallholder farmers in this area are aware of the importance of savings and already set aside some of their income from the current harvest for future crop cycle needs. Therefore, it was also planned that the loan product would be embedded with saving accounts enabling members to save their money for future needs. KSP Sekartani also provided additional services by visiting their clients' businesses to take loan repayments. KSP Sekartani Mandiri's board members were highly familiar with the agrobusiness model in Sausu Gandasari. Their thorough understanding of agro-input availability, production process, postharvest flow and the market schemes was seen as providing significant value added for their members.

In Sekotong Village, KSU Bina Laut piloted a group lending programme to members of fishers' cooperatives. This loan product was recommended because the local culture revolves heavily around social gatherings that form strong bonds between the community members. It was foreseen that these relationships would work as a social guarantee when the loan product was disbursed in a group. Loan products were also embedded with saving accounts so that members were able to save money for future needs including planned saving for education. Finally, KSU Bina Laut had some experience providing a Sharia financing product that has performed well. Since the majority of the communities in this village are Muslim, the available Sharia financial products were integrated into the group lending scheme to adapt them to clients' cultural requirements.

4.1.3 Philippines

In the Philippines, a series of consultative meetings among the members of the country working group (CWG) was conducted to decide on the selected best practices to be pilot tested, to identify target areas and to identify potential partner organizations for the implementation of the pilot project. The CWG was composed of the Agricultural Credit Policy Council (ACPC), which oversaw the pilot project, along with the following government institutions: National Livelihood Development Corporation (NLDC), Philippine Crop Insurance Corporation (PCIC) and the Agricultural Guarantee Fund Pool (AGFP).

Similarly to Indonesia, the Philippines pilot was coordinated by a lead institution with MFI partners at the community level who implemented the pilot schemes and provided credit and guidance to the farmers. The country working group decided to focus on agricultural value chain finance patterned from the Kalasag Cooperative experience for pilot testing in two provinces: Bukidnon and Benguet. The implementing institutions were the Bukidnon Cooperative Bank (BCB) and the Seeds and Fruits Multi-Purpose Cooperative (SFMPC) in Benguet.

Bukidnon Cooperative Bank (BCB)

The Bukidnon Cooperative Bank (BCB) has the goal to provide more accessible and affordable financing to small farmers in the community and help them obtain better prices for their produce. BCB's role in the pilot was to provide direct financing to individual corn farmer-producers of Sumilao, Bukidnon who were clustered into groups and later linked to institutional buyers of corn. BCB also provided counterpart funds to be loaned to any players identified in the value chain. For the pilot, the bank agreed to provide its own fund to finance the working capital of the institutional buyer of the corn produced by the farmer-borrowers.

Seeds and Fruits Multi-Purpose Cooperative

The Seeds and Fruits Multi-Purpose Cooperative (SFMPC) has a defined membership (closed cooperative) whereby only those who belong to their clan (Kankana-ey and Kalanguya Tribes in Buguias, Benguet) can join. Members include vegetable farmers, small entrepreneurs and employees of the local government unit. The cooperative provides a variety of services such as financing, marketing and vegetable production training to members as well as to non-members who are willing to engage in vegetable production. The cooperative also provides hauling/transportation of vegetables and farm inputs. For the pilot, the role of the Seeds and Fruits Multi-Purpose Cooperative (SFMPC) was to provide loans to farmers for farm production and link farmers directly with institutional buyers/users who could guarantee them better prices for their harvested crops.

4.2 CREATING A SUPPORTING ENVIRONMENT

The creation of a supporting environment for the pilot by Huainantongshang Rural Commercial Bank (HTRCB) in China was a complex process. First of all, rural commercial banks (RCB) in China are supervised by multiple agencies. In theory, rural credit cooperatives (including RCBs) in China should be controlled by their shareholders and supervised by the China Banking Regulatory Commission (CBRC) and the People's Bank of China. In practice, RCBs in many parts of China have been controlled to a large extent by the Provincial Rural Credit Cooperative Federation (RCCF). The CBRC, Anhui Bureau, together with the People's Bank's Anhui branch, is the financial supervisor of HTRCB. During the pilot, the provincial CBRC remained responsible for monitoring and supervising the operation of HTRCB. After being nominated by the CBRC in Beijing to carry out the pilot, HTRCB gained some support from CBRC, PBC and RCCF in Anhui province. HTRCB invited the officials from the Anhui CBRC and RCCF to join the project launching ceremony in Huainan and reported all the project progress to CBRC and RCCF in the province. The support from local government agencies, especially the Bureau of Agriculture and the Bureau of Commerce were important for the pilot programme. HTRCB engaged relevant government departments, traders and suppliers of agricultural input and other stakeholders in the pilot programme through workshops and discussions. Particular attention was given to the agricultural cooperatives which are capable of organizing smallholders in farm production and marketing. HTRCB worked together with CBRC and other parties to address barriers to lending to cooperatives in China.

In Indonesia, MICRA looked for an implementing partner in each pilot location. The implementing partners were chosen based on a social-financial assessment of existing MFIs in the pilot areas. In addition to the MFIs, MICRA also established collaborations with other related organizations to support the programme deliverables and increase project impact. This was mainly achieved through a policy forum during which all the related parties were able to meet and discuss the development of the programme (described in the following Section, 4.2.1).

The Philippines project put several mechanisms in place to create an enabling environment for the project. The lead agency, the Agricultural Credit Policy Council (ACPC), mobilized support from the members of the country working group to establish the following commitments:

- ACPC, being the lead institution, oversaw the progress of the pilot project implementation. In addition, the ACPC's existing institutional capacity building programme was tapped in support of the capability building component of the project.
- The National Livelihood Development Corporation (NLDC) was to act as the lead government agency in charge of the piloting the agricultural value chain finance scheme.
- Philippine Crop Insurance Corporation (PCIC) provided crop insurance coverage to the farmer-borrowers to reduce the production and weather-related risks faced by farmers.
- The Agricultural Guarantee Fund Pool (AGFP) guaranteed coverage of up to 85 percent of unsecured loans extended by financial institutions and other eligible lenders to small farmer borrowers engaged in rice and/or other food production activities.

The Philippines project also conducted a policy forum for both external interested parties and pilot project stakeholders. The goal was to extend the project's impact by sharing information, examples and promoting discussion on some of the additional best practices identified during Phase I of the RuFBeP project that were not piloted, but that have the potential for replication in other regions in the country. This is described in more detail in the Section 4.2.1.

Finally, a project management team was created to jointly oversee the pilot project. The team was composed of the head of the MFI or its representative and a local government unit representative. Through this team, ACPC was able to identify project problems and sustainable solutions, while the required technical, financial, and institutional support was called in through the horizontal and vertical networks of support agencies, as coordinated through the country working group.

4.2.1 Stakeholder consultation

Both Indonesia and the Philippines conducted policy forums to encourage discussion between and among project implementation partners and other interested parties not directly involved in the project, such as rural/cooperative banks, NGOs, government agencies and smallholder groups.

In the Philippines, ACPC conducted one policy forum to present and discuss some of the best practices that emerged in the Phase I study but were not piloted in Phase II of the RuFBeP project. The focus was on the experiences of microbanking offices (MBOs) in providing credit and other financial services to the rural poor and the development of appropriate micro-insurance practices.

Session one of forum highlighted the success of CARD Bank and a microfinance cooperative rural bank in increasing outreach and serving the rural poor in hard-to-reach areas through MBOs. The regulatory framework, policies and guidelines in establishing MBOs was presented by the Bangko Sentral ng Pilipinas while the Land Bank of the Philippines shared its views on MBOs and presented its experiences in lending to the rural poor, especially small farmers and fishers through their network of offices and conduits.

Session two focused on micro-insurance practices with the National Credit Council of the Department of Finance presenting the government's national strategy on micro-insurance while the Philippine Crop Insurance Corporation presented its agricultural insurance programmes and products. The RIMANSI Mi-MBA Association of the Philippines, Inc. and one of its members (i.e., CARD MBA) shared its initiatives and experience of the private sector in providing micro-insurance services for the rural poor. GM Bank, a private microfinance rural bank also shared its experiences in relation to micro-insurance. Congressman Agapito Guanlao from the House of Representatives took part in the discussion and presented his proposed bill, which aims to strengthen agricultural insurance.

The policy forum was attended by 107 participants representing rural/cooperative banks, Department of Agriculture Regional Field Units, attached agencies, bureaus, non-governmental organizations, people's organizations, farmers' organizations, APRACA representatives, ACPC officers and technical staff, other government institutions and agencies and members of the media.

The main goal of the Indonesian policy forums was to get third party perspectives from related stakeholders about the project's framework that could support the activities of the pilot and provide input to the develop a comprehensive implementation plan. A policy forum in each pilot located was held before the disbursement of funds to the MFIs. In each case, they brought together a broad variety of stakeholders including technical ministries, NGOs, insurance companies, banks, local buyers, microfinance institutions, famer and fisher groups, etc. The policy forum in West Nusa was attended by 23 people and in Central Celebes by 22 people.

4.3 BASELINE SURVEY

Each project carried out a baseline survey in order to determine the initial conditions prior to the project intervention and establish a starting point against which the projects' progress and effectiveness would be monitored and evaluated.

4.3.1 China

The baseline survey for the agricultural value chain finance pilot in Huainan Prefecture of China was undertaken by HTRCB in December 2016. Forty farmers were sampled in the survey. The sample selected was somewhat biased towards large family operators because this was the population for which the agricultural value chain finance products were being developed. The results from the baseline survey indicated that about half of the operators sampled had access to formal loans, which was low considering many of them were large farm operators. Farmers in the sample reported having difficulty accessing loans from formal sources because they lacked the physical collateral needed to obtain them. Traditionally, RFIs in China have accepted mainly real estate assets as collateral for loans. From the survey, it appeared that only around 10 to 20 percent of the family operators in our sample had the physical assets required as collateral by formal financial institutions. This clearly indicated an opportunity for the development of loan products based on alternative forms of collateral.

In addition to the baseline study, China also conducted an economic potential analysis to better understand financing opportunities for the project and to inform the design of the loan products. The results of the local economic potential analysis helped the project determine what other forms of collateral might be introduced through the financing scheme. Accounts receivable was identified as one form of collateral for loan access as over 30 percent of the operators sampled had accounts receivable. Most of those with accounts receivable were suppliers of farm inputs. In addition, some mobile assets, such as inventory and farm machines were also to be used by HTRCB as loan collateral. Additionally, the bank agreed to use contractual relationships between the buyers and sellers of farm goods in designing loan products for agricultural value chain actors with the large operators providing a guarantee for small operators in the upstream or downstream of the value chain.

4.3.2 Indonesia

Indonesia's baseline survey and report were submitted to MICRA in November 2015. Baseline surveys were conducted in the two locations selected for pilot implementation. The local economic potential analysis and baseline survey was the first field-based analysis activity prior to the pilot launch. The research activities aimed to map the local economic potential by identifying the current level of business management and financial schemes available to smallholder farmers and coastal communities in the targeted areas. In addition to that, the study also measured the baseline points of the programme to portray the current condition of the targeted population before programme implementation. These same baseline points were measured at the end of the project to assess the impact of the pilot. Both primary data, gathered from questionnaires and in-depth-interviews conducted with the targeted population, and secondary data, from Statistics Indonesia and related agencies, were used. The following indicators comprised the baseline points:

- **Economic potential:** identified the smallholder farmers' and coastal community's financial competence level, financial services access, and business-management capability.
- **Financial access:** portrayed the available common mechanism of working-capital funding existing in the target areas and its performance quality.
- **Financial product availability:** identified the financial products available to smallholder farmers and coastal communities, the financial institutions' plan for and capacity in providing the products and the clients' expectations of the financial products.
- **Gender mainstreaming:** depicted the role of the minority gender (in this case, women) in the business chains and how they managed their household's finances and the available opportunities to increase support for women in business.
- **Stakeholder participation:** identified the current role of the formal or informal leaders and the related government agencies that support the development of agriculture and fisheries business sector. This indicator also depicted the role of local facilitators and applied policies for the business sectors.

4.3.3 Philippines

The Philippines carried out a baseline survey in the identified project sites during the early stages of project implementation. Prior to pilot testing, it was critical to determine what information was already available regarding farmers' profile, their on-farm and off-farm activities, assets, household income and expenses, sources of financing, volume of production, marketing of produce, average farm size and loan usage, among others. The baseline questionnaire was approved by the APRACA RuFBeP project manager before the start of the survey.

4.4 PROJECT IMPLEMENTATION

This section provides a narrative of the overall implementation followed in each pilot project and includes detailed descriptions of the loan products, roles of project partners and action plans that were developed by each project. The CWG of Indonesia and Philippines organized to implement the pilot testing of identified good practices during September a and October 2015 respectively, while China initiated the piloting during March 2016.

4.4.1 China

After the inception of the project in September 2016, HTRCB organized a study tour to Wuwei Village Bank in Anhui province to look at the bank's agricultural lending programmes. This study tour was requested HTRCB prior to the project implementation in order to increase their knowledge of AVC-based lending.

The implementation of the pilot programme in China was delayed considerably, mainly because of institutional and personnel changes with CBRC, but got underway in November 2016 with an in-house intensive training programme in AVC finance. The project engaged two international experts on AVC finance to provide three-day capacity building programme on AVC finance in Huainan Prefecture. The training covered the concept of value chains, AgVCF approaches, business models, financial tools that may be used in AgVCF, and lessons using case studies from numerous countries as well as China. The participants included the managers at the financial institutions (mainly HTRCB), lecturers and postgraduate students from Nanjing Agricultural University, rural finance specialists in China and practitioners of rural finance in China. Loan officers at HTRCB were also trained in cash-flow-based lending as part of microfinance downscaling. The training was focussed on building a basic foundation for understanding the approach, the key principles, business models and selected financing instruments used in downscaling.

HTRCB designed four loan products to target the AVC players in the pilot area based on learning from the intensive training programme and results of the baseline survey. Loans were designed for farmers, farmers' groups and micro and small enterprises (MSEs) operated by farmers and migrant workers. Lending priority was given to those enterprises that have an important role in the processing, storage, branding and trading of agricultural products produced in the local areas so as to promote the development of agricultural value chains. The bank planned to apply innovative loan collateral alternatives, for example mobile assets, land use rights, warehouse receipts and accounts receivable, to offset the risks associated with the non-traditional loan products.

Valuable lessons and innovations from the three Phase I case studies were integrated into the development of loan products through pilot programme. The products included:

- **Cash-flow-based loans:** cash-flow-based loans were targeted to farmers, farmers' groups and micro and small enterprises operated by farmers and migrant workers. These AVC players did not have physical collateral for bank loans and did not comply with the current bank rules on collateral and guarantees. Cash-flow-based loans allowed the bank to assess the creditworthiness of a loan applicant based on the cash flows of the applicant and by crosschecking with other information obtained from peers and third parties. Priority was given to those enterprises that have an important role in the processing, storage, branding and trading of agricultural products produced in the local areas so as to promote the development of agricultural value chains.

- **Group guarantee loans:** this loan product targeted those AVC players who had no physical collateral for bank loans under the current bank rules on collateral and guarantees. Applicants provided two guarantors who were linked to the applicant through AVC, serving as the upstream and/or downstream players. In other words, three value chain players who were connected through the same AVC could provide group guarantees for each other. This was an innovation on group guarantee for microloan programmes in China. The loan applicants for this product included individual households, family farms, agricultural cooperatives and agrotraders and processors.
- **Credit linked with insurance:** this product was designed and launched with Guoquan Insurance Co. Ltd., a small insurance provider in the region. The borrowers were required to buy insurance to cover the loan repayment in case the loans become non-performing.
- **Mixed guarantee loans:** these loan products targeted agro-enterprises and cooperatives. The loans could be guaranteed by a mixture of mobile and immobile assets and third party guarantees. The loans could be used for farm production, trade, input supply and agroprocessing.

Thirty borrowers took loans under the pilot project. The average loan size was RMB 481 000 (with minimum and maximum ceilings of RMB 30 000 and RMB 1 000 000, respectively). Loan terms were between 6 and 36 months, rates of interest were between 5.255 percent and 10.2 percent (and 12 to 18 percent for loans for non-farm activities). Eighteen loans (60%) were group guarantee loans while 12 (40%) were cash-flow-based loans.

Three departments of the bank were involved with the project implementation: the agricultural loans department, the credit department and the marketing department. Beginning in January 2017, the agricultural loan department became principally responsible for the pilot testing. Initially, the new products were introduced to 2 of the 14 branches and later to the remaining 12 branches of the bank. By May 2017, it was found about 70 percent of the loans disbursed under the pilot project were group guarantee loans.

The action plan for the implementation of the selected interventions in China is summed up in *Table 2*.

Table 2: Action plan for implementation, China

Name of deliverables/milestones	Type of deliverable	Estimated submission date
1. **Inception report**	Report	15 September 2016
2. **Develop questionnaire for the baseline survey**	Document	November 2016
3. **Report on the baseline survey**	Report	31 December 2016
4. **Process document**	Document	25 September 2017
5. **Final report on pilot testing**	Report	30 November 2017

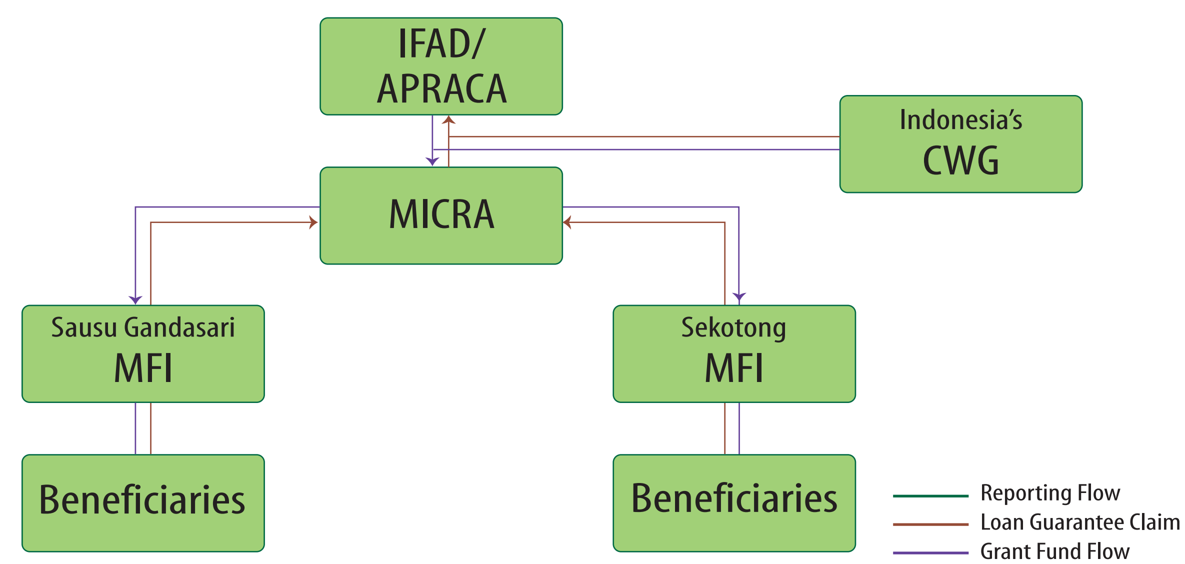
Source: Process Document, 2017

4.4.2 Indonesia

In the Indonesia, MICRA partnered with local MFIs who delivered the financial products to AVC clients. MICRA received USD 15 000 of seed capital from IFAD/APRACA then disbursed those funds to the selected MFI implementing partners under the guidance of the country working group.

Thus, MICRA acted as the grant manager, while MFIs were responsible for disbursing loan products to selected clients or members. The fund disbursement was done once, in advance of the programme. Each MFI received USD 7 500 deposited in their account as a loan guarantee in order to support the implementation of pilot programme. The disbursement process is presented in *Figure 6* above.

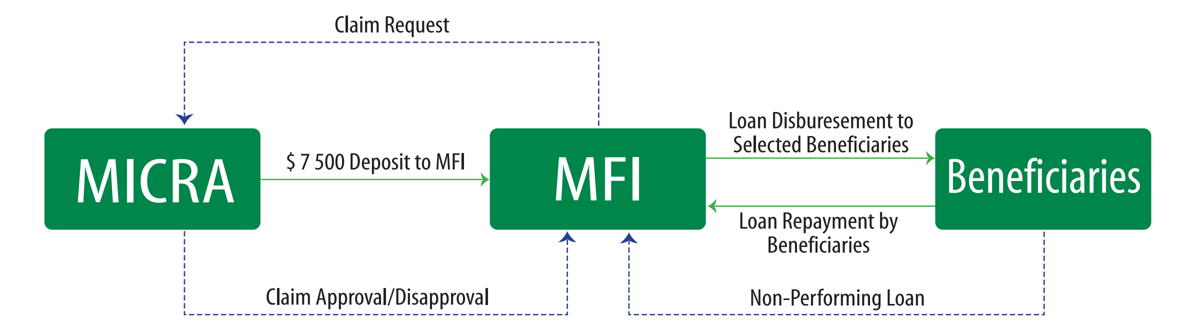
Figure 6: Fund disbursement followed in Indonesia



Source: Country Process Document, 2017a

The loan guarantee scheme ensured that each loan disbursed would be guaranteed by the deposited fund should the clients fail to fulfil their responsibility. The fund could then be used to cover the bad debt expense to the institution. In order to claim against the deposited fund, the MFI had to request the claim approval from MICRA. This request was evaluated based on the agreed upon terms and conditions. If the request was eligible for claim, MICRA issued the approval letter to transfer the deposited fund. The loan guarantee scheme is pictured in *Figure 7* below. This method allowed the MFIs to disburse loans to beneficiaries without requiring any collateral.

Figure 7: MICRA's loan guarantee scheme



Source: Country Process Document, 2017a

KSP Sekartani Mandiri piloted non-collateral taking loans to smallholder farmers. The loan term was approximately six months with 1 percent monthly interest and loan ceiling of IDR 4 000 000. The farmers were incorporated into farmers' groups and needed references from their group's leader to apply for a loan. The leader did not provide a guarantee for the member's loan, but gave references about the farmer's character and business performance upon which the MFI based its decision on whether or not to grant the loan. Upon approval, farmers could visit input shops to purchase what they needed for the new crop cycle. The farmer submited receipts, or the input shops (that were partnering with the MFI) reported the farmer's purchases to the MFI. MFIs paid input providers directly and the farmer-borrower paid back their loan to the MFI.

KSU Bina Laut piloted a Sharia-based financing scheme in the form of non-collateral taking loans within a group lending model. Loans had a 12-month term, and maximum ceiling of IDR 4 000 000 with profit sharing of 80:20 based on the negotiation (80% for MFIs and 20% for beneficiaries). Social guarantee was used to ensure that the loan was repaid, meaning that if one borrower from the group did not repay his/her loan, other members were liable and that member was suspended for the next loan cycle. In this village each fisher was usually a member of one group consisting of up to ten fishers. Fisher groups had internal discussions about how to invest or spend working capital to best accommodate the group's needs. The group leader would then bring a proposal to the MFI. If the loan was accepted, the group leader then met with the lending institution to do the *akad* (Sharia financing agreement). The financing went individually to group members and loan ceilings varied depending on each member's capability to repay the loan.

Both MFIs also offered voluntary savings bundled with insurance as part of the loan products. This was made possible through a cooperative agreement, brokered by MICRA, between the Social Trust Fund, the initiator of the savings and insurance product, and the MFIs. The Social Trust Fund managed the insurance fund and advised the MFIs on the savings product. MFIs managed the relationship with their clients, the savings fund and deposited the insurance premium to the Social Trust Fund.

MFIs periodically reported the progress of the loan portfolio and programme implementation to MICRA. It was planned that MFIs would submit fund usage reports to MICRA on a monthly basis. MICRA would then report the summarized fund usage activity to the country working group and APRACA. By the end of the programme, it was hoped that MFIs would be able to achieve financial and social goals in alignment with agreed upon evaluation criteria such as clients' general profile, loan size per clients, non-performing loan rate, etc. In the final evaluation, MFIs that were able to meet 80 percent of the criteria were awarded the fund to support the sustainability of the piloted best practice.

The action plan proposed for implementation of interventions in Indonesia is described in detail in *Table 3*.

Table 3: Action plan for implementation, Indonesia

Date	**16**	**23**	**30**	**22**	**17**	**5**	**31**	
Month	**May**	**May**	**May**	**Aug**	**Oct**	**Dec**	**Jan**	**Notes**
Rural Financial Best Practice Project – Phase II								
Policy Forum 1	■	■						This policy forum was dedicated to bridge a discussion between implementing MFI with related stakeholders including local cooperative agency, smallholder groups, insurance company, NGOs etc. to compose a comprehensive strategy to deliver the project.
Fund Disbursement		■	■					MICRA disbursed the seed capital (amounting USD 7 500 for each MFI) to support the implementation of the programme.
Progress Report/ M&E Activities				■				Monitoring and Evaluation summarized the MFIs experiences in delivering the programme during the given period. The lessons learned were drafted in the form of progress report which was used to consider a follow up strategy.
Impact Assessment					■			The impact assessment measured the level of accomplishment towards key success factors defined in the baseline survey.
Policy Forum 2						■		This policy forum was dedicated to host a discussion between the implementing MFIs and related stakeholders that have been actively involved in the programme including CWG members, related private companies, NGOs, academia, etc.
Final Reporting							■	The final report documented all the activities done, lesson learned and recommendation for future projects.

Source: Country Process Document, 2017a

4.4.3 Philippines

The Philippines pilot project implementation took off in the third quarter of 2015, with a series of consultative meetings with the members of the country working group to determine the best practices to pilot, identify pilot locations and implementing partners and to mobilize support from participating government institutions. The country working group was composed of the Agricultural Credit Policy Council (ACPC), as the lead institution overseeing pilot project, with the following government institutions as members: National Livelihood Development Corporation (NLDC), Philippine Crop Insurance Corporation (PCIC) and the Agricultural Guarantee Fund Pool (AGFP).

These consultation meetings resulted in an agreement on the responsibilities that each institution would assume for the facilitation of each of the four project components: capacity building, financing, crop insurance and credit guarantee and marketing. The commitment of each government institution is described in Section 4.2 and in *Table 4* below.

Table 4: Philippine project sites, target number beneficiaries, crops and lead institutions

Lead Institution	Province	Municipality	No. of farmers	Crop
Fruits & Seeds MPC	Benguet	Buguias	100	Vegetables
Bukidnon Cooperative Bank	Bukidnon	Malaybalay	100	Corn

Source: Process Document, 2016b

Originally, the National Livelihood Development Corporation was the lead government agency in charge of the implementation of the Value Chain Finance for Agriculture pilot project. Once pilot sites were selected, MFIs in those areas that were accredited by NLDC were chosen as implementation partners. NLDC was also tapped as the main provider of capacity building interventions for the project.

However, on 9 September 2015, Memorandum Order No. 85 was issued which effectively dissolved the NLDC. This prompted the working group to convene and discuss NLDC's circumstances and the implications for its role in the project. As a result of the consultation, the ACPC agreed to take the initiative to lead the implementation of the value chain finance pilot testing as well as the capacity development component.

The pilot sites and MFI partners, which NLDC had initially identified, were also changed. *Table 4* shows the final project sites, including the target number of farmer beneficiaries, corresponding crops and lead financial institutions.

The project developed an 18-month timeline to complete activities. The implementation of the project is described below and summarized in *Table 5*.

The capacity building component was delivered by the ACPC–Institutional Capacity Building (ACPC–ICB) group. The ACPC–ICB group adopted the 8-Step Clustering Approach to Agro-enterprise Development[3] which was modified accordingly to fit the needs of the project's lead institutions. The highlight of this approach was the organization of small farmers into agro-enterprise clusters that function as microfinance centres for pooling logistic requirements, consolidating product supply, linking to formal business entities and managing their own agro-enterprise. This clustering was expected to link farmers with institutional markets and other buyers establish sustained demand for products and favourable market arrangements such as better prices for farmers' products.

[3] The 8-step clustering approach was developed by CRS-Philippines. Steps include site selection, product selection, supply assessment, market chain study, cluster formation, cluster plan formulation, test marketing and cluster strengthening.

Table 5: Implementation process followed in the Philippines

COMPONENT	RESPONSIBLE INSTITUTION	INNOVATION	SCHEME	OUTCOME
Capacity building	ACPC	Clustering Approach	• 8-step-Plan for Agro-enterprise Development • Forming farmers into small clusters of 10-15 farmers	• Farmers are guided in finding the right product to supply, how to bring the products to the market, and how to meet buyers' expectations • Farmers able to set up a joint marketing enterprise, selling their crops as a business entity • Farmers can consolidate crops meeting volume requirement of target market
Financing	ACPC, MFI	Provision of flexible financing support based on requirement of farmers	• Production loan made on a staggered basis based on the farmers' needs for funds using the farming timetable	• Farmers are able to increase working capital • Risk of fund diversion mitigated
			• Support to market linkage (buying fund for the consolidated produce, loans for storage fees, truck loan)	
			• Other services: savings, life insurance, farmers' forum, participation to training	
Crop Insurance and Credit Guarantee	PCIC, AGFP	Provision of Crop Insurance to farmers and Credit Guarantee to MFI/lender	• Crop insurance coverage due to calamities • Up to 85% guarantee to loan default	Risks brought about by calamities mitigated
Marketing	Institutional Buyers	Linkage to institutional buyers	• Contract growing • Capacity building	• Sustainable markets for farmers produce • Stabilized pricing for farmers produce

Source: Country Process Document, 2017b

The provision of financing support was facilitated by ACPC and participating MFIs. Loans were extended to farmers based on the requirement of each farmer to be involved in the pilot testing. Loans were also provided on a staggered basis to match the farmers' needs for a specific purpose in the chain which could include production loans and loans to support market linkage (e.g. buying fund for the consolidated produce, loans for storage fees, truck loan). Moreover, other services were provided such as savings mobilization, life insurance, farmers' forum and participation in training, among others.

The Philippine Crop Insurance Corporation (PCIC) and the Agricultural Guarantee Fund Pool (AGFP) led the third component providing farmers with crop insurance and credit guarantee to mitigate risks brought about by natural calamities.

Lastly, farmers were linked to institutional buyers through the practice of contract growing and continuous capacity building. This component was carried out by institutional buyer partners.

Box 2: Philippine crop insurance and credit guarantee schemes

Crop insurance coverage was offered to the farmer-borrowers to reduce the production and weather-related risks resulting from natural calamities such as typhoons, floods, droughts, earthquakes, volcanic eruptions, plant pests and diseases and other perils.

Credit guarantee protected financial institutions by covering loan defaults owing to weather, pests and diseases and other unpredictable events. It did not cover those arising from wilful default and/or fraud. In case of default or non-repayment of the guaranteed loan by the farmer-borrower for any of the said valid reasons, AGFP paid the lending institution the guaranteed portion or 85 percent of the unpaid loan.

Two policy forums on the two other best practices documented in the Phase I study were also planned.

The Philippines' action plan for implementation of the project interventions is presented in *Table 6*.

Table 6: Action plan for implementation, Philippines

ACTIVITY	OUTPUT	TIMELINE								RESPONSIBLE INSTITUTION
		2015			2016				’17	
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	
Conduct of the 8-step clustering approach to agro-enterprise development	Farmers are clustered and trained									NLDC/ACPC
Evaluation and processing of loan application	Loans granted to farmers									ACPC
Evaluation and processing of PCIC crop insurance and AGFP guarantee	Loans secured with crop insurance and guarantee cover									PCIC/AGFP
Facilitation of marketing agreement	Farmers are linked to institutional buyers									MFI
Conduct of policy forum	Policy forum on MBO-OBO									Consultant/ ACPC/CWG
	Policy forum on micro-insurance									
Conduct of periodic monitoring activities	Progress monitoring report submitted									ACPC
Conduct of project evaluation	Report on evaluation of the pilot project									Consultant/ ACPC

Source: Country Process Document, 2017b

4.5 FINAL REPORTING

The pilot projects’ final reports were intended to concisely summarize the outcomes of the project and serve as the final documents of the RuFBeP Project Phase II. The report format included documentation of project performance, project successes and lessons learned in order to signal improvements for potential replication in the future. The RuFBeP Project Phase II final report also required the inclusion of formal and informal feedback collected from project stakeholders and participants throughout the pilot testing. Some projects planned follow up activities to explore in more depth the experiences of the project participants. The information collected would then be aligned with the details included in the final report.

SECTION 5
Lessons Learned

Pilot projects developed strategies to capture the procedures and practices used to plan, manage and execute their pilot projects. Overall, lessons learned during implementation were gleaned from: the experiences of the implementing partners, events that significantly affected the project, changes resulting from the project, strategies that helped in achieving project goals, as well as challenges and reflections on how to best address them. There was considerable variation regarding the financial practices that were piloted, the characteristics of the pilot locations and beneficiaries and the types of institutions involved in project implementation, nevertheless, some common lessons have emerged. Where possible, these have been clustered into categories.

Additional lessons culled from the overall project experiences were produced from the tangible results of project evaluations and communicated as actionable conclusions. Some of these broad conclusions have been translated into overall recommendations that can found in the last section of this report.

1. It is imperative to invest proper time and resources in project design

A well-designed project is crucial for effective implementation. It requires the investment and earmarking of adequate resources. Both the Indonesia and the Philippines project teams would have benefited from more time and resources during the design phase of the project. In Indonesia, the project invested a significant amount of time to prepare MFI partners to replicate the best practices of rural financial products. This required working with the MFIs to adjust loan features, loan ceilings, the calculation of interest rates and one of the most important factors, identifying the existing clients' business needs. This left considerably less time to disperse the loans. As a result, the project was only able to cover half to one cycle of the loan product (more or less six months) before the date for impact assessment. Thus, some indicators were not extensively explored during the assessment.

Similarly, in the Philippines, it was necessary for project preparatory teams to clearly identify all the key building blocks in the targeted agricultural value chain (i.e. inputs, production, packaging, distribution), in order to put financing arrangements in place for the implementation of each of the components in tandem. Without the time to invest in this, it would be difficult to ensure the achievement of the overall objectives of the value chain financing scheme. Both governments and donor partners should be called upon to show more commitment to the project preparation phase.

A related lesson, specific to the design of an AVC financing scheme, is the importance of conducting a thorough value chain analysis so that the ensuing implementation is more precise and the chain processes more sustainable. The Philippines project experienced a major delay when the local government unit was unable to identify farmers in Sumilao, Bukidnon. This postponed the clustering of farmers which was one of the key initial steps for project implementation. The project learned that the strength of a value chain depends on the ability of all chain actors to perform well. Failure brought about by any chain actor can adversely affect the success of the value chain.

Also under the rubric of project design is this lesson from the Philippines that the development of a business plan is crucial for any substantial implementation and impact on the ground. A business plan is essential for clarifying targets and therefore for providing a way to monitor results. Importantly, without a business plan, there is no basis for estimating the adequacy of the resources provided to the MFI.

2. Targeted capacity development at all levels of the project is fundamental to success

All three projects incorporated different forms of capacity development in their projects and the benefits were undisputed. As emerging financial instruments in China, it was essential for the project to conduct training programmes for the implementing partner on both microfinance downscaling and agricultural value chain financing prior to project design and implementation. In the Philippines, the continuous provision of capacity building support to both the lead institutions and farmers was important for project success. Farmers, for example, who had been using traditional farming practices, needed training to help shift toward a more entrepreneurial mind set. Many believed that partnering with big corporate partners was nearly impossible, especially for farmers who didn't even issue receipts for their sales. This led the project to focus their capacity building on equipping farmers to be able to meet the requirements of their respective institutional clients.

Related to capacity development is the specific skills mix that the project team needed in order to successfully implement the pilot. The Philippines experience showed that the implementation of AVC financing projects required additional skills outside agriculture. Agricultural projects with large infrastructural components cannot be successfully implemented without engineering and microfinance support. In the Philippines pilot, the inclusion of a microfinance expert in the project, for example (ACPC, BCB) would have greatly enhanced the project implementation, procurement processing and increased the level of success and sustainability of the project.

In Indonesia, capacity building for clients' business improvement, which included financial literacy, entrepreneurship and skills training, was observed as the key factor to empower the borrower-community to strengthen its businesses, improve skills and potentially contribute to job creation to bolster the local economy. Financial cooperatives also needed to expand their capacity and readiness to handle more clients and reach more rural areas.

3. A supporting environment is vital for both the implementation and sustainability of the project

The success of any rural finance programme depends on the extent to which supportive policies are in place and on the development perspective of the regulatory authorities. The project team in China noted the importance of collaborating with relevant government agencies and credit guarantee agencies in order to share the risks and improve the policy and market conditions for the financing schemes that were piloted. In both the Philippines and Indonesia, building and maintaining a reassuring environment for the project was a key factor that contributed to the success of pilots. The Philippines project relied on the collaborative effort of various national government agencies, local government units and dedicated members of the lead institutions. For Indonesia, good coordination at the local level between cooperatives, government agencies and other related stakeholders also contributed to the success of the project. The project solicited stakeholder inputs by engaging them a discussion of the baseline survey results as well as in a local policy forum. Even though some of the inputs were not incorporated because of the limited duration the project, the suggestions are important contributions to making future improvements in the project. It was also noted that the Indonesia project became a stimulus to engage more parties to be involved in strengthening the upstream support of the sector.

Taking this further, the Philippines pilot noted that public-private partnerships would greatly enhance project sustainability. Governments can be used to create an enabling environment and foster the establishment of any public good for the benefit of the project and the beneficiaries. For example, the government can provide loan funds to sustain the financial needs of the farmers for production. Where effective public-private partnerships are not established, the risk of failure is high because the government agencies would be both the facilitators and the implementers but would lack the crucial link of private enterprises. The project learned that a private enterprise approach has the greatest chance to ensure project sustainability. Where this is lacking, project continuity is threatened when the development partner's support ends.

4. Loan products must be adapted to fit borrowers' needs

The ability of the partner institutions to provide flexible sources of financing that were adapted to the borrowers' needs was important in all three pilots. In China, the financial products used by RFIs were successfully adjusted and incorporated into the new products designed for AVC finance scheme. Examples include the application of cash-flow-based lending and group guarantee by HTRCB. In addition, the project believes outreach would be further improved if RFIs expanded the acceptable forms of collateral to include real estate, forestry rights, farm land operations rights, warehouse receipts, and agricultural insurance.

In Indonesia, two factors were identified as underlying the success of the products offered: simple qualification requirements and the social approach used by the cooperative account officers. The non-collateral-taking policy for microloan applications was a huge innovation. Many, if not most, of the rural people targeted in the pilot own nothing but their business as a guarantee for accessing loan from financial institutions. For these clients, the breakthrough of accessing a loan that did not require collateral was one of the most respected features of the project.

The social approach adopted by the Indonesian MFI cooperatives in marketing the loan product and maintaining communication with beneficiaries led to an emotional closeness and increased trust between the clients and financial institution. This improved clients' sense of responsibility for loan repayment and their willingness to save in the cooperative. The business assistance services provided by the MFI's also contributed to the improvement of beneficiaries' business quality. Loan officers visited the beneficiaries not only to collect repayment but also to discuss the borrowers' business progress.

Related lessons from the Indonesia experience on understanding borrowers' needs and fitting products to them are described in Box 3 below.

5. Adaptation of the loan products helps financial institutions mitigate risk

In China, HTRCB learned that increasing the opportunities for the bank to use account receivables and warehouse receipts as collateral helped to manage risks in the AVC loan products. In addition, establishing lending procedures and developing a rating and scoring system for farmers can further mitigate lending risk. Likewise, in Indonesia, the adjusted adoption of financial product features identified in the best practice case studies, helped the cooperative partners to prepare for challenges and reduce risks during implementation of the programme.

Box 3: Additional lessons from the Indonesia pilot

1. Financial institutions need to understand their clients' need

MFIs in Indonesia learned that it can be both feasible and affordable to provide product innovations and non-financial services that improve their clients' business growth. However, in order to design the appropriate innovations, they needed to understand their clients' profiles and conduct research before marketing a financial product.

2. Maintaining client profiles can help financial institutions map the fit between potential clients' and future products.

The prudent banking principles held by one of the Indonesia pilot's MFIs led to a less optimized disbursement of the seed capital. Because it was their first experience in offering a product with no collateral, they were quite careful in selecting the beneficiaries. Having existing client profiles would have helped to more quickly identify potential clients for that loan product.

3. Clients need to understand the products offered by the financial institutions.

Clients need a clear understanding not only of the loan, (including the loan ceiling, interest rate, minimum savings requirement, why they should save money, the banks procedures, how much should they repay, etc.). but also of the cooperative itself (what the cooperative does, their role in the cooperative, what business opportunities membership can provide, etc.).

SECTION 6
Project Challenges

Each of the three pilot project teams identified expected challenges and some mitigating strategies to address them before the projects were launched. As would be expected, projects also encountered and documented some of the unexpected challenges they faced during implementation.

6.1 CHINA

Sustainability beyond the project was expected to present a great challenge to Huainantongshang Rural Commercial Bank. The project was launched later than planned so the bank had less time to undertake the pilot. However, HTRCB crafted three strategies to mitigate possible negative effects. First, the bank carefully monitored the loans disbursed and revised the product based on the feedback from the monitoring process. The project planned to continue this even after the project officially ended in 2017. Second, the bank planned to replicate the new financial products to more branches in Huainan once they were successfully tested in the pilot branches. Finally, the bank planned to produce and share the project report with the China Banking Regulatory Commission in Anhui province and beyond for possible replication in other regions of China.

Other expected challenges depended, in part, on a number of factors that were outside the control of the project. For example, the project relied greatly on the willingness and commitment of the bank management to conduct the pilot study. This was an important consideration when the project team constructed the project framework and its supporting environment. Another factor that was seen as potentially impacting the project was the lack of income generation opportunities in the pilot areas. The Chinese economy faced a number of challenges in 2016 and 2017 as the government adjusted the economic structure by cutting down excessive capacity industries, mainly in the area of steel and iron, ferrous metals, coal, cement and plate glass. It was predicted that unemployment would increase in certain areas and economic adjustment was expected to impact jobs and income generation opportunities in the pilot counties/district. Credit risks in the pilot sites were a third area of concern. With rising local government debt and enterprise debt, credit risk was also on the rise in some regions of China. As a result, the pilot programme targeted rural areas and agro industries with less exposure to credit risks.

Shortly after the pilot began, HTRCB faced some major setbacks in terms of change in the leadership of the bank and the in-charge of project implementation. These changes were expected to have a negative impact on pilot project implementation. A second challenge was devising strategies to include small operators in value chain finance and the third was motivating the bank branches and staff to provide loans to non-farm enterprises and projects that had higher expected risk adjusted returns.

6.2 INDONESIA

While implementing the programme in Indonesia, MICRA anticipated challenges from two sides: the MFI as the financial services provider and the supply chain system. *Table 7* lists the expected challenges along with corresponding mitigation strategies.

MFIs also experienced some other challenges while carrying out the pilot. One of them was their reduced ability to broaden outreach to other beneficiaries because of limited capital availability. Lower interest rates of the piloted loan products made it especially difficult for the MFIs to cover the operational expenses of the loans. This meant they were constrained to using only the seed capital

Table 7: Expected implementation challenges and mitigating strategies, Indonesia pilot

Challenges	Mitigating Strategy
Effort is required to adapt the new microfinancing scheme, which has more product features, to the MFIs' current capacity for implementation. Therefore, the MFIs' commitment to provide the financial product based on the agreed programme procedures is expected to ensure better programme execution.	Responsive communication flow is important to monitor the MFIs' activities and track any variances. We require MFIs to report on their experiences with the programme periodically to capture any success stories or failures that would improve the programme in the future.
MFIs have limited knowledge and field experiences with insurance product. This product enables them to provide a more secure assurance for their clients' activities.	MICRA plans to introduce the MFIs to a micro-insurance scheme and assist them in choosing the most suitable providers for their clients. Insurance is one of the solutions to mitigate the risks inherent in the business they run.
MFIs' common strategy to mitigate lending risks is oftentimes limited to clients' repayment capability. Meanwhile, if the MFI puts the same amount of focus on supporting, managing and creating clients' business market competitiveness, it will increase clients' production numbers and sales volume.	MFIs' involvement in supporting smallholders' supply chain is vital and will effectively scale up their business volume. There are a number of possibilities to create an inclusive scheme in which MFIs are able to provide not only financial support but also business model development for their clients. MICRA will assist the MFIs in developing the business model and link them with the related stakeholders.
Farmers' limited knowledge of traditional farming techniques or their lag in catching up with modern technologies oftentimes become the driver of lower product quality and harvest volume.	Strategic collaboration with local government bodies, NGOs, other related stakeholders to provide the smallholder communities with technical assistance in farming and/or fishing techniques. These collaborations are expected to increase smallholders' capability to effectively and efficiently produce their products.
Pest problems and the less active market fluctuation are some of the factors that affect smallholders' production and income.	
Clients' limited capability to manage their household finances might also be consuming their business capital. Gaps in financial literacy is one among many factors that prevents the smallholder communities from expanding their business.	MFIs will deliver financial literacy training to the clients as part of the project.

Source: Country Process Document, 2017a

allowance from the project. One procedural difficulty worth mentioning is that KSU Bina Laut was using manual record keeping and this affected the information flow.

Another complication related to one of the cooperative partners' legal entity status as a KSP. A KSP (Koperasi Simpan Pinjam), or saving and lending cooperative, is prohibited by law to run other business units besides savings and loans. This restricted KSP Sekartani Mandiri's ability to adopt some of the selected best practices.

Market price uncertainty, especially for agriculture products, was one of the obstacles to achieving the project's intended impact. Even though farmers' production did increase, the market price was lower than in previous cycles, which made farmers' revenue stagnant.

6.3 PHILIPPINES

The Philippines pilot mapped their expected challenges to each of the project components and came up with contingency activities to counter them. These are explained in *Table 8* below.

As was the case in Indonesia, the MFIs in the Philippines also encountered some procedural/operational challenges during implementation. For example, the Seeds and Fruits Multi-Purpose Cooperative needed capacity development specifically to strengthen its marketing/trading capabilities, accounting and

Table 8: Implementation challenges and contingencies, Philippines

COMPONENT	CHALLENGES	CONTINGENCIES
Capacity building	Changing the mind set of individuals who are accustomed to traditional individual farm production and marketing of produce	Organizing farmers into an efficient, business-minded cooperative
	How to instil in farmers the discipline to maintain high quality produce	
Financing	Fund diversion	Financing shall be provided on a staggered basis based on the farming timetable
Crop insurance and guarantee	Onset of calamities which results in crop failure and non-payment of loans	Facilitate application and payment of claims through crop insurance and credit guarantee
Marketing	Low harvest owing to unforeseen events	Provision of technical assistance in meeting the market requirements for volume and market quality

Source: Process Document, 2016b

recording system and business management, among others. There was also a long waiting time (45 to 60 days) for clients/institutional buyers to repay the cooperative, which constrained the cooperatives from expanding business activities. The cooperative also needed additional loan funds with longer terms to be able to serve more farmers. External factors posed additional challenges. Poor road conditions from farm to market increased the cost of transporting goods (harvests and farm inputs) and it was costly to hire additional farm labourers because few were available in the community.

Furthermore, it was difficult to foster improvements in some of the farming techniques. For instance, postharvest handling was purely manual resulting in a reduction in the value of harvested crops. Also, despite provision of training on good agricultural practices and values formation among the farmers in the community, uptake was slow.

In Bukidnon, most of the challenges related to the sustainability and potential extension of the pilot. Farmers expressed concern that the project was only short term. They wanted it to continue and if possible, to be expanded to be able to help more small farmers in the province. Farmers also suggested that a similar scheme be applied to other crops and that the Agricultural Credit Policy Council and the Department of Agriculture facilitate or link them directly to institutional buyers. Since plans and programmes of the newly elected officials in the local government unit had not yet been set, farmers suggested that ACPC spearhead the process of organizing their group and to providing assistance in capacity building activities in their community.

SECTION 7
Project Monitoring and Evaluation

Constant monitoring of project activities and measuring progress towards outcomes as well as an end-of-project impact evaluation were essential elements of each project framework. Monitoring generally involved the routine tracking and reporting of priority information during implementation. The main purpose of the impact evaluation was to assess the degree to which projects achieved the intended outcomes and impact that the pilots aimed for.

Some project teams also used the evaluation to identify the factors of success or failure, to assess the sustainability of the benefits generated and to draw conclusions to inform future programming, policy making and overall organizational learning. Project monitoring and evaluation (M&E) plans and specific indicators are described below.

7.1 CHINA

HTRCB created a number of indicators to monitor the progress of its loan programme, in addition to the normal monitoring processes of the bank which apply to all the bank's loans and other financial products. The monitoring indicators are shown in *Table 9*.

Table 9: Monitoring indicators for China pilot

Lending Indicators	Other Indicators
Loan Size	Scope of Operation
Loan product	Upstream link
Disbursement date	Downstream link
Interest rate p.a.	
Guarantee	
Repayment Methods	
Loan terms	

Source: Process Document, 2017

Other indicators, or non-lending indicators listed in the table, were designed to track the value chain links that were related to group guarantee for loans to value chain players. Additional monitoring indicators for pilot project loans included loan uses, loan arrears and productivity of loans as compared with the bank's other lending programmes.

The project evaluation in China aimed to assess the project impacts from a number of perspectives. The following indicators were developed to assess the impacts on clients who have borrowed from the bank under the pilot project:

- Changes in credit access following the project implementation
- Changes in farm productivity and incomes following the project implementation
- Any improvement in capacities and value chain links following the project implementation.

Secondly, it was important to measure the impact on those bank employees who participated in capacity building and in project implementation. Their understanding of the downscaling project procedures, techniques in AVC finance and management capacities following the project implementation were analysed. Finally, the impact on managers of the bank, including the branch managers, the bank chairman and chief executive officers was also measured.

7.2 INDONESIA

MICRA worked closely with a local consultant and MFI partners in both pilot areas to design the monitoring and evaluation plan. Monitoring activities included:

- Quarterly onsite monitoring activities to gather direct information about the programme implementation, the response of targeted beneficiaries to the financial services schemes and to identify and address any challenges.
- Quarterly reports of the activities submitted on the 15th of each quarter.
- Monthly check-in call from the implementing partners and local coordinator. The purpose of this activity was to identify any challenges or any improvements that were needed and allowed the project to draft any necessary interventions as quickly as possible.

The monitoring and evaluation framework for the programme in Indonesia was done using both quantitative and qualitative approaches to track progress made towards each indicator and compared against baseline data. The project team devised a framework based on the model in *Table 10.*

Table 10: Approaches to track progress in Indonesia

Indicator	Definition	Unit of Measure	Baseline Result	Data Source	Frequency	Responsible Party
Based on baseline indicator	Definition of indicator	%, No. of people etc.	The result taken from baseline study	Key person, interview, secondary data	How often measurement is taken	Who will carry this out

Source: Country Process Document, 2017a

The monitoring and evaluation activities were also designed to capture the current condition or level of progress made by the project towards desired impacts.

The research indicators and framework used in analysing the impact were derived from the indicators used in the baseline survey (see Section 4.3.2). Key areas for measurement included: economic potential, financial access, financial product availability, gender mainstreaming and stakeholder participation. The specific variables and their method of measurement are available in the annex.

Overall, the Indonesia pilot made a positive contribution to the achievement of the key success indicators. As of December 2016, the cooperative partners disbursed 95 percent of the seed capital to 52 beneficiaries with a rate of non-performing loans at 0 percent throughout the project. The project was able to foster financial product innovation by enabling MFIs to integrate new features into their loan products, such as bundled savings plans and micro-insurance. The following points describe the project's impact on the key success indicators:

- **Increased access to financial services by rural people:** The number of the beneficiaries who accessed microfinance institutions has increased. At the time of the impact survey, all beneficiaries (100 percent) indicated that they used the cooperatives on a regular basis (deposits and savings). This is an increase from the amount prior to the start of the project which showed less than 50 percent of the community as having savings and loans. As more people accessed loans from microfinance institutions, the number of people accessing financing from non-formal institutions, especially moneylenders, has decreased. The Indonesia pilot has increased the number of people who: (i) access formal financial institutions, (ii) are aware of financial products available to them and (iii) take advantage of financial products that are suitable for them.

- **Increased function/diversification of rural financial services:** the partnering cooperatives provided capital assistance to the beneficiaries and were expected to provide support for business development as well. At the writing of this report, activity groups for agriculture and fisheries were being initiated but did not yet conduct any marketing activities of their products. Generally, they already have regular customers or they sell to middlemen. In addition, both KSP Sekartani and KSU Bina Laut provided payment point services for electricity and telephone utilities. However, most of the beneficiaries showed more interest in making payments at the counter or post office because of proximity to their homes.
- **Improvement of business performance of the target groups:** The productivity level of the farmers and fishers increased due to the improvement of production processes that were supported by the additional capital of the cooperative. Fishers' and farmers' incomes also increased. Some indicators for this were the ability of beneficiaries to save and the use of additional revenue to improve the means of production, to invest in education for children and to renovate housing.
- **The existence of gender mainstreaming:** The participation of rural women in making business decisions primarily related to capital increased for those performing both programme and non-program activities. Both of the MFIs also disbursed loans to women beneficiaries who participated in their family business (both farming and fishing).
- **Stakeholder participation:** The evidence showed that most beneficiaries received general assistance from the government. Stakeholder participation was relatively high in the project.
- **Efficiency:** The performance of project was efficient, which was indicated by the increase in production and income of the beneficiaries because of venture capital stimulus loaned by the partner MFIs.

7.3 PHILIPPINES

Indicators were developed in key areas for measurement based on the project's goals and objectives:

- the extent to which borrowers were empowered and strengthened through the provision of capacity building activities,
- whether financing was sufficiently provided,
- whether risks were lessened through the provision of crop insurance to farmer borrowers and credit guarantee to MFIs, and
- the extent to which small farmers were enabled to hold the bargaining power in market or price negotiations.

The Philippines project planned to conduct the final project evaluation in the 13th month of the pilot testing, shortly before the end of the project. The aim was to determine the extent to which planned and unplanned objectives and outcomes were achieved, to identify the factors of success or failure, to assess the sustainability of the benefits generated, and to draw conclusions that may inform future programming, policy making, and overall organizational learning. The evaluation also looked at the effectiveness of the scheme which the project hoped to share in the form of recommendations to policy makers and stakeholders to encourage wider adoption/replication of the pilot model. Data was gathered through secondary sources, a survey with the farmer beneficiaries and key informant interviews with partner organizations and institutional buyers.

Finally, the information gathered was compared with the results of the initial baseline survey conducted during the early implementation of the pilot testing. The logical framework along with specific indicators that were measured are presented in *Table 11* below.

Table 11: Monitoring and evaluation framework, Philippines pilot

Narrative Summary	Objectively Verifiable Indicators & Targets	Means of Verification	Frequency	Responsible Institution
GOAL				
Small farmers are able to hold the bargaining power in market or price negotiation	• Farmers able to meet required volume of produce of institutional buyers • Required volume of produce • Volume of production per cycle • Prevailing wholesale price • Actual selling price of produce	• Survey & KII • Monitoring report Secondary data	End of project	Consultant/ ACPC
OUTPUTS				
Farmers are clustered through the 8-step clustering approach to agro-enterprise development	• No. of trainings conducted • No. of farmers trained • No. of farmer clusters organized	Monitoring report	Quarterly	NLDC
Farmers are provided with flexible financing support based on requirement of farmers	• No. of loan applications processed • Amount of loans approved • Type of activity/commodity financed • No. of farmer borrowers • Amount of loans matured/ collected/past due	• Evaluation report • Monitoring report • Loan disbursement report • Loan collection report	Quarterly	NLDC ACPC MFI
Loans to farmers are secured with PCIC and MFIs are covered with AGFP	• Amount of loans covered • Amount of insurance claims paid • Amount of loans guaranteed • Amount of guarantee claims paid	• Evaluation report • Monitoring report • PCIC/AGFP coverage report	Quarterly	PCIC AGFP

Source: Process Document, 2016b

The following results were gathered during the implementation of the agricultural value chain financing for the two project sites.

1. Seeds and Fruits Multi-Purpose Cooperative (SFMPC)

Among the significant improvements noted as a result of the pilot project to SFMPC are as follows:

- **Membership:** Prior to the project implementation, the SFMPC had a defined membership (closed cooperative) whereby only those who belonged to their clan (Kankana-ey and Kalanguya Tribes in Buguias, Benguet) could join. By January 2016, the cooperative expanded its membership to 69 farmer members. With the inclusion of more vegetable producers/ growers to the project, the cooperative was able to sustain the volume of produce required by its five institutional buyers.
- **Fund utilization:** The loan fund made available to the cooperative by ACPC was mainly utilized to cover members' costs related to vegetable production and trading activities of the cooperative, including packaging of produce, transportation, salaries and wages, etc. Also, the cooperative was able to buy a truck (chiller/cold van) for transporting vegetable products.

- **Market linkage:** Prior to the start of the project, the cooperative had a contract with one institutional buyer. They now have supply contracts with five institutional buyers namely, Miascor Catering Services, Shangri-La Restaurants Philippines, Boracay Resorts and Restaurants, Foresca Food Service and Tiger Resort, Leisure and Restaurant, Inc. (Okada Hotel Manila).

- **Financing support to farmers:** By December 2016, the cooperative provided a total of PHP 4 000 000 in credit funds to 34 farmers charging them low rate of interest (1 percent per month) with no collateral required. Loan processing took a maximum of only two days. Loan collection was 100 percent except when farms were ravaged by heavy rains. In such case, the cooperative refinanced the loans of the farmer-borrowers.

  The cooperative is currently expanding its business activities by engaging in livestock production (swine and cattle). They currently have 20 sows and two dairy cows (imported from New Zealand). Litters or offspring of the pigs are distributed to the farmer-members for fattening. To date, they distributed 40 piglets to four farmer-members (minimum of ten heads per recipient).

- **Crop insurance:** As part of the innovations integrated to the AVC model, vegetable production financed under the project had to be insured with the Philippine Crop Insurance Corporation (PCIC) to be able to help the farmers mitigate risk brought about by natural calamities. However, very few (4 out of the 30 farmers interviewed) enrolled in the crop insurance programme. Those who did have their crops insured did not utilize the insurance when they were hit by a typhoon in June 2016 because they did not know how to file their claims for the damages.

- **Loan guarantee:** Another innovation of the model was the inclusion of the credit guarantee for partner organizations to provide protection against loan defaults of borrowers. However, the cooperative has yet to apply for accreditation from the Agricultural Guarantee Fund Pool to have their loan portfolio guaranteed.

2. Bukidnon Cooperative Bank (BCB)

With the implementation of the AVC financing scheme in the area, farmers experienced growth in farming business opportunities. The following are the results of the implementation of the AVC financing model in Bukidnon province:

- **Loans disbursed to farmers:** By December 2016, BCB disbursed a total of PHP 20.07 million (USD 416 666) in loans to 146 farmer-borrowers. These loans were extended to corn farmers who had a marketing agreement with the Asian Hybrid Seeds Technologies, Inc. (ASHTI), a hybrid seed corporation that purchases corn seeds from its accredited corn growers/farmers. The company is a client of BCB under the project to whom the bank provided a working capital loan fund in the amount of PHP 5 000 000. The release of loans to the farmer-borrowers was staggered based on the farm plan and budget as endorsed by ASHTI to BCB. Upon harvest, ASHTI procured the corn produce from the farmer-borrowers and remitted the corresponding sales proceeds directly to the farmers' savings account with BCB. BCB then deducted the amount equivalent to the farmers' loan obligation from the farmer-borrowers' savings account. The amount of loans to farmers ranged from PHP 90 000 to PHP 350 000 (USD 1 875 to 7 292) with total finance charge pegged at 15 percent per annum. The scheme is covered with a tripartite agreement among the farmer, BCB and ASHTI.

- **Fund utilization:** The loan fund was fully utilized for the intended purpose.

- **Market linkage:** Farmers in Sumilao, Bukidnon agreed to cluster and enter into a tripartite agreement with BCB and ASHTI. Previously, farmers sold their produce to traders from whom they also borrowed money for farm and household needs. Interest rates charged by money lenders ranged from 3 percent to 5 percent per month. With the AVC scheme, farmers were linked and entered into a marketing agreement with ASHTI. Aside from accessing credit from BCB, they also obtained a more favourable price for their corn produce.

- **Crop insurance:** All loans under the project were automatically enrolled in the crop insurance programme.
- **Loan guarantee:** BCB's loan portfolio under this project was guaranteed under the Agricultural Guarantee Fund Pool.

SECTION 8

Summary, Conclusions & Recommendations

It is widely recognized that the lack of access to a range of financial services is a major hindrance to lifting the typical rural smallholder out of poverty. Without access to financial capital, poor farmers and small entrepreneurs are unable to buy the inputs necessary to augment production and increase income. Furthermore, the limited availability of credit in general has held back the rural and agricultural sectors of many countries within the Asia-Pacific region, which has negatively affected the overall development of national economies. Yet, the ability of many governments and rural finance service institutions to effectively facilitate/provide such services on a sustainable basis has proved elusive.

8.1 RISKS ASSOCIATED WITH RURAL FINANCE

The reasons for the lack of success in delivering rural financial services and the perceived risks associated with this are well researched and documented. Among others, high transaction costs to cater to the large rural population and the problems of providing collateral by the rural clientele are seen as the major barriers to improving the impact of the pro-poor rural finance programme in the Asia-Pacific region. The risks associated with smallholder agricultural production include natural disasters, unforeseen declines in prices, low yields because of several factors,[4] etc. More recently, adverse impacts emanating from climate change have also been seen as a constraint. All of these factors can result in low revenue, which in turn may lead to high default rates on loans and a limited use of other services, such as savings and insurance, thus aggravating the situation. Hence, many financial institutions[5] are often reluctant to extend credit services to smallholder farmers and other rural entrepreneurs.

8.2 BASIS FOR PILOT IMPLEMENTATION

This second phase of the RuFBeP project, provided the opportunity and appropriate resources to field test a selection of new and innovative approaches to rural finance in the Asia-Pacific region that effectively address these barriers and risks and show promise for replication and scaling-up in underserved rural areas. The first phase documented the best practices in select countries for scaling up were the base for undertaking the pilot testing of some pro-poor rural finance and designed to fit to the context in the geographical area where the piloting/scaling up was planned and implemented.

8.3 PRODUCT DESIGN FOR PILOT

All of the projects designed loan products with credit enhancements such as loan guarantees and risk protection schemes using, for example, micro-insurance, crop insurance or credit linked with insurance, which play a critical role in overcoming perceived risks in smallholder lending. Most of the piloted products also addressed the critical gap among rural borrowers in providing traditional collateral by introducing loans with a variety of collateral alternatives. Collateral innovations included mobile assets, land use rights, warehouse receipts, accounts receivable, group guarantees, cash-flow-based lending as well as the introduction of non-collateral taking loans.

[4] They are poor rainfall, lack of access to markets, or crop loss owing to numerous other agronomic factors.

[5] This includes those that are specifically created to cater to rural clients, such as state-owned development banks, rural cooperatives/commercial banks, etc.

8.4 RESULTS OF PILOT

Overall, the pilot results have been encouraging. In Indonesia, the project significantly increased the numbers of rural borrowers who access formal financial institutions. In one of the pilot locations there were no non-performing loans. There were also increases in farmer/fisher productivity. In one of the Philippines pilot locations the number of corporate market linkages that provided a secure market for farmers' produce was dramatically increased. Membership in one of the cooperatives was also boosted and loan collection was 100 percent. There were mixed results with the crop insurance and loan guarantee scheme in one of the locations mainly due to poor communication about benefits and procedures.

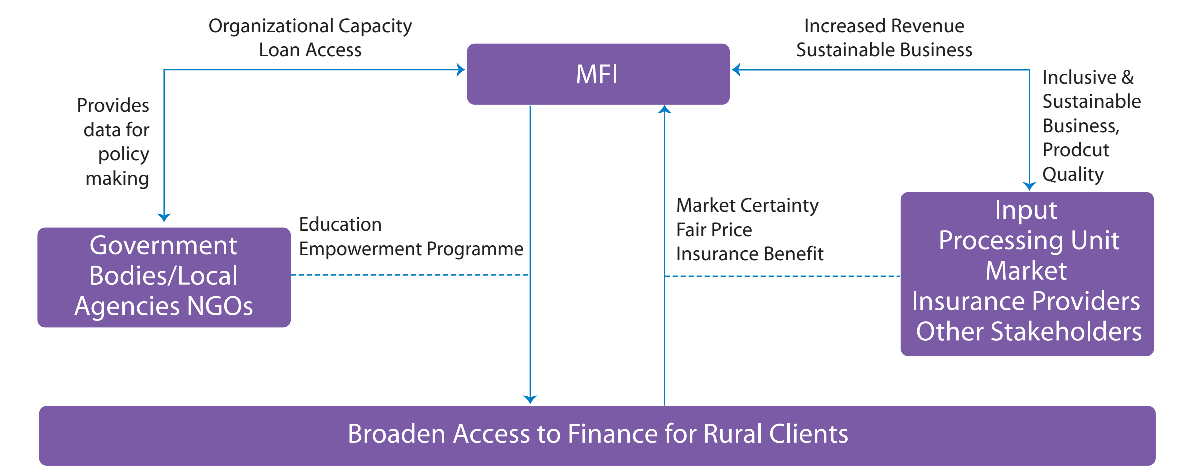
8.5 CONCLUSIONS AND POTENTIAL FOR SCALING UP

The conclusions and recommendations for potential scaling up as they relate to each project experience are described below.

8.5.1 China: In China, the implementation of the pilot project in Huainan has a number of policy implications for agricultural and economic development at the prefecture/county levels. First of all, following the rapid process of urbanization and land consolidation, a large amount of funds are required for agricultural development in the project areas. Second, an increase in the loans disbursed for agricultural trade processing and the supply of farm input is expected to contribute to the development of AVC in the project area. Finally, after testing the new lending technologies, HTRCB has concluded that the financial products tested in the pilot should first be replicated by other branches of the bank before being replicated by other RFIs in the province. Replication in other regions of China may be challenging. For example, replicating the pilot in less developed western regions of China, with small farm sizes and less developed infrastructure and communication systems would be difficult. It would also be problematic to identify leading players of AVC in those regions.

8.5.2 Indonesia: Towards the end of the Indonesian project, the country working group met and discussed how to continue the piloted financial schemes in order to impact more rural people. Their recommendations focused on creating a model for the business sustainability of the pilot. From the discussion, it was agreed that a business-to-business approach would be more sustainable for all parties: MFIs, clients and other the related stakeholders. The recommended model places the cooperatives or MFIs at the centre of the initiative with their main goal to broaden financing access for clients who live in rural areas. To accomplish this, MFIs must be able to strengthen and maintain connections with current stakeholders and develop new partnerships (*Figure 8*).

Figure 8: Recommended business-to-business model, Indonesia pilot



Source: Process Document 2016a

The left side of the diagram illustrates the need for MFIs to build strong relationships and communication systems with government bodies or local agencies, NGOs and other related organizations who could assist the MFIs in improving their organizational capacity through trainings, certifications, etc. MFIs should also be able to access loans from government or non-governmental programmes should they need to increase their capital. Some organizations also regularly offer programmes to empower borrower-communities through training to improve skills such as financial literacy, craftsmanship, entrepreneurship, etc. Such programmes could be delivered effectively and efficiently by partnering with MFIs to reach their clients that are classified as marginalised or rural communities. This partnership model could increase the clients' capability in improving their business management skills. It would also affect the clients' repayment capacity to the MFIs. In addition, MFIs could monitor their clients' progress and improvement, for example by documenting alternative sources of income yielded by innovation, value added to the end products, current economic behaviour, etc. and use what is learned to develop additional financial products or make policy recommendations to the government. The right side of the diagram suggests that MFIs need to form and maintain robust partnerships with stakeholders who are able to support the clients' business. These partnerships would provide clients with access to a business value chain that will help ensure sustainability, for example, by linking clients' businesses with the availability of access to input, processing unit/house and markets. The form of partnership would vary based on the MFIs' legal entity status and its limitations. The provision of insurance would complete the benefits for clients and protect them from unexpected loss. By partnering with these stakeholders, MFIs can offer input and market certainty, price transparency and insurance benefits for their clients as additional advantages, which enable them to obtain fair prices. In exchange, these stakeholders are part of an inclusive business as a sustainable value chain scheme, enjoy higher product quality and gain trusted partners.

8.5.3 Philippines: The experiences of Seeds and Fruits Multi-Purpose Cooperative and Bukidnon Cooperative Bank in the Philippines have demonstrated that agricultural value chain financing can be viable provided that the market for agricultural produce is assured. This involves linking small producers to lead actors in the value chain to enable them to secure technical, financial and marketing assistance. This assurance is a risk-mitigation measure that counters voluminous risks, specifically those brought about by natural disasters and infestations. Financing structures still need to be aligned with the specific requirements of the small farmers at precise times in their farming cycle and thus, are best delivered through a value chain financing approach. It is important to note that corporate markets are accessible to smallholders if the farmers know how to be competitive in terms of prices and are consistent in delivering quality and quantity of produce. In this project, linking the farmers to large markets has improved the farmers' income in a more sustainable manner. Overall recommendations for improving the quality and efficiency of AVC finance are to:

a) identify the financing needs of different actors in the chain, especially smallholders;
b) tailor financial products to fit the needs of the actors in the chain;
c) reduce financial transaction costs through direct discount repayments and delivery of financial services; and
d) use value chain linkages and knowledge of the chain to mitigate risks within the chain.

Box 4: Linking farmers to markets in the Philippines

- The finance provider must have a goal of social responsibility in conjunction with business interest to make the project more sustainable.
- Successfully linking farmers to the market requires quality and consistency of supply.
- It takes time for the farmers' groups to be in the forefront of market negotiations, therefore the finance provider could assume this role in the initial stages while the farmers' groups observe and learn the process.
- Public-private sector collaboration is crucial for assisting farmers in getting involved in a complex mechanism such as value chain financing.

8.6 CONCLUSION AND WAY FORWARD

Servicing rural financial markets is important because of the combined (1) high incidence of poverty in rural areas and growing income inequality between urban and rural markets and (2) concerns for food security and population vulnerability in rural communities. The question is not whether to address these issues, but how. This IFAD funded project being implemented by APRACA intended to document some best practices which have the potential to resolve the issues related to rural financial market.

Pilot testing and scaling up process continued for 24 months and almost for 3 cycles of loans were disbursed by each of the financial institutions involved in the process. This extended time period for piloting provided enough opportunities for the lead institutions and the CWGs in all the three countries to consult with the stakeholders and take the remedial measures if any to adjust the pilot testing process. It was envisaged that the piloting of rural financial services will capture the lessons and best practices – both the successes and failures in agricultural finance, financial liberalization, risk management and microfinance – to pave the way forward for smart, sustainable financial market services programme tailored for the specific challenges of rural economies in Asia-Pacific region.

While a number of the specific interventions discussed in this document have been implemented as elements in this project, one of the key points raised by many at the dissemination forums held in Manila, Philippines and Lombok, Indonesia is the need to utilize effective programming approaches, whether proven or innovative, with the conscious objective of promoting rural financial markets as part of broader financial sector strengthening. Unlike earlier generations of rural finance programming, the approaches here are direct where the implementing institutions are directly providing financial services. It is expected that the result should be a stable yet dynamic financial sector, capable of operating without subsidy, and freed of the sustainability limitations that plagued earlier rural finance efforts.

The products and services piloted in this project are organized into for strategic areas that address the issues related to (a) non availability of collaterals and cash flow method of financial requirement were tried out, (b) building capacity of financial institutions to improve the delivery of rural financial services, (c) enhancing the outreach of financial services through new and innovative rural finance products and (d) financing agricultural value chains to improve efficiency in rural entrepreneurship. It is firmly believed that alleviating these constraints could reshape the rural economy, opening the way for vibrant rural financial markets poised to service agricultural enterprises and rural households.

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ANNEX 1. Gender Mainstreaming in Rural Finance (Indonesian Case)

Regarding gender mainstreaming, it is recommended that projects encourage the participation of women in local social committees at the village level where they can voice their needs. This will encourage more equitable participation of women in planning and decision making. Cooperatives could also develop a financial product for women with adjusted terms to help them in establishing small businesses that would contribute to their families' finances. To support the recommended plan, the following interventions are suggested:

1. **Technical assistance for MFIs:** To maintain the continuity of the project and broaden their geographical reach and number of beneficiaries, MFI cooperatives need to strengthen both their financial and organizational management capacities. Indonesia's Ministry of Cooperatives and SMEs offers regular training programmes that could upgrade the cooperatives' capacity in running their activities. MFIs also need additional sources of capital to finance clients' business and to cover the operational costs of the loan products. The cooperatives should be very thoughtful and strategic about accessing funds that support their ability to sell the products with reasonable interest rates. One opportunity for sustainable alternative for funding in Indonesia is provided by the Ministry of Cooperatives and SMEs which has been managing an organization that offers a revolving fund for the cooperatives at a very competitive rate to escalate the improvement of SMEs.

2. **Continuous financial literacy training for clients:** One key lesson learned during the pilot implementation is that most project beneficiaries did not properly manage their family finances. Financial literacy training should be offered that helps people understand that managing family finances is not complicated but requires intention. Clients should be helped to identify their own spending priorities and future goals then create a simple budget to guide them in spending money. Simple financial records will also help them track their income and spending patterns.

3. **Entrepreneurship training and business improvement for clients:** In order to improve and succeed, a strong willingness to learn and lead one's business is required, regardless of the size of the business. MFI cooperatives can assist clients in understanding their business potential and how to take advantage of opportunities at the next level. Entrepreneurship training will allow them to be keener to add value to their products and create innovation. In the long run, this capability could also empower the people around them through job creation. In relation to the inclusive business, both cooperatives and local government agencies should provide training to farmers' and fishers' groups to improve their production skills and also update the market information. Another recommendation is to promote the development of processing and packaging services as an alternative business unit.

ANNEX 2. Approaches to Agricultural Value Chain Finance in Philippines

The agricultural value chain is a comprehensive and holistic approach that covers a whole range of value-adding activities. AVC finance can improve access of smallholders to agricultural loans and also offers an opportunity to expand the financing for agriculture, improve efficiency and repayments and strengthen linkages among participants in the chain.

The following recommendations provide general guidance on increasing the viability of agricultural value chain financing schemes:

1. **Build capacity of small farmer-producers to participate in the value chain.** This involves increasing their understanding and capacity to participate. In the evolution of a value chain involving small farmers, two important steps can be distinguished: first, the effective linkage of farmers to more attractive markets which requires their ability to produce to exact product specifications required; second, is the transition towards sustainable local finance delivery.

2. **Base interventions on a solid assessment of actual smallholders' needs.** For each of the financing opportunities in a value chain, corresponding capacity building needs should be identified. While financial service providers will not take prime responsibility for these interventions, their involvement is crucial to arrive at a joint strategy. Moreover, MFIs also need to build up their own capacity to deal with these issues, to develop appropriate products and to appraise clients from a value chain finance point of view.

3. **Familiarize small farmers and other stakeholders with the structure and the dynamics of the value chain.** This will involve, among other things, an analysis of the value added potential in the chain. This will reveal whether benefits can accrue to primary producers by organizing the chain more efficiently and whether the cost of chain organization and financial services can be covered from product margins.

4. **Consider enhancing financial interventions with non-financial services** such as: (i) ensuring contact with financial institutions; (ii) bringing stakeholders together in workshops to see whether solutions can be found within ordinary business relationships; (iii) providing technical assistance to producer organizations or lead actors in the chain to increase their ability to meet the requirements of chain operations; (iv) facilitating linkages offering finance providers the comfort of well-established market outlets and providing sufficient value added potential at the local level.

5. **Identify an effective lead partner in the AVC scheme.** An active player in the chain, like a farmers' marketing organization or a processing company, can take the lead in streamlining the value chain, thus providing a degree of "chain governance". Such a party can also play a role by providing embedded finance to suppliers and/or to establish a working relationship with a finance provider for financing to producers and input suppliers.

   Weakness at any link in the chain can increase financing risk at all levels. Value chain finance decisions are derived from the health of the chain or sector, including its cash and commodity flows, rather than on traditional collateral of an individual business or actor. The viability of value chain finance also depends on harnessing 'insider knowledge' of the industry.

   The drivers of a value chain, which are often the businesses involved in the processing and marketing of agricultural outputs, know the business and the other actors in the chain in a way that financial institutions by themselves do not.

6. **Provide the necessary infrastructure in rural areas.** Infrastructure is a critical requirement for area development. Serious gaps in basic infrastructure such as inadequate electricity for operating machinery and processing equipment, lack of storage facilities to ensure product quality, absence of developed road systems to promote fast delivery and reduced spoilage and insufficient water and technologies for irrigation and other farm activities constrain growth of outputs and productivity. Policy makers must make agriculture a priority to overcome these obstacles.

ANNEX 3: M&E Indicators for Indonesia Pilot

No.	Factors	Variables	Target population	Data Source	Indicators
1	Increased access to financial services by rural people	% increase in the number of customers/debtors	Farmers/fishers	Secondary data as reported by MFIs and structured interviews of target group	MFIs' clients who work as a farmer or fisher
					Distance to financial institutions
					Number of savings or loan accounts owned by the villagers
2		% of funds disbursed	Farmers/fishers	Structured interviews and secondary data as reported by MFIs	Funds disbursed to farmer/ fisher clients
					Funds requested by farmer/ fisher potential clients
					The average of loan ceiling disbursed to clients
3		% performance	MFIs	Secondary data as reported by MFIs	Number of non-performing loans to agriproducts
4		% the variety of products that are used	MFIs	Secondary data as reported by MFIs	Available products offered to clients
					The process of disbursing the products to end-clients
5		% adoption of new products (such as insurance bundling, pregnancy or wedding savings, celebration day savings, etc.)	Farmers/fishers	Structured interviews of MFIs	MFIs' innovation for product features
					Additional benefits offered to clients
					Additional social benefit offered to clients
					Saving plans feature to increase people's awareness of prepare the future or unexpected events.
6		% of villagers who take loan from non-formal institutions	Farmers/fishers	Structured interviews of farmers/fishers	Sources of non-formal loan provider institutions/ individuals
					Number of people who take loan from the non-formal institutions/ individuals
					Number of people who take loan from middle-man
7	Increased function/ diversification of rural financial services	business development services (marketing of products)	Farmers/fishers	Structured interviews of MFIs and farmers/fishers	Agriproducts markets
					Agriproducts marketing areas supported by MFIs
					Agriproducts marketing channel
8		Payment services (payment of electricity/water/ telephone bills)	Farmers/fishers	Structured interviews of MFIs	Additional features of utilities payment point incl. electricity and land line payment (one-stop financial payment services concept)
9		Financial innovation products	MFIs/farmers/ fishers	Structured interviews of MFIs and farmers/fishers	Clients who are joining group lending with joint liability feature.

No.	Factors	Variables	Target population	Data Source	Indicators
					Clients using informal leader or particular person as the collateral guarantor.
					The reliance of using sharia financing products for agriculture and/or fisheries business sectors.
					The mixture of both best practices or new financial product innovations that have proven their success.
10	Improvement of business performance of the target groups (groups of farmers or coastal communities)	% increase in production	Farmers/fishers	Structured interviews of farmers/fishers	Farmers' or fisher's productivity
					The period of each cycle production
11		% increase in revenues	Farmers/fishers	Structured interviews of farmers/fishers	Farmer/fisher income
					Other income generated
					Working capital needed to start a cycle
12		business expansion	Farmers/fishers	Structured interviews of farmers/fishers	Agricultural supply chain development
					Agribusiness expansion plan
					Technology involvement in the production process
13		Competitiveness	Farmers/fishers	Structured interviews of farmers/fishers	Product's competitiveness point in the marketing areas
					Standardized products (export quality)
14	The existence of gender mainstreaming	% target group women	Farmers/fishers	Structured interviews of farmers/fishers	Women who manage the financial aspect of farmer or fisher households
					Women in the farmer/fisher families reached by the MFIs services.
15		% of women in the farming or fishing activities	MFIs/farmers/ fishers	Structured interviews of MFIs and farmers/fishers	Women who are directly involved in the farming/ fishing activities
					Women who are empowered by the farming/fishing activities
16	The participation of stakeholders (local government/ relevant agencies)	The involvement of related stakeholders in the farming or fishing sectors.	Government	Structured interviews of stakeholders	The local government level of support in the farming and fishing sectors.
					The existence of policies that will be supporting the farming and fishing activities
17		The increased role of farming and fishing facilitators in the production activities	Farming/fishing facilitators	Structured interviews of stakeholders	The role of local facilitators role in supporting the development of farming or fishing activities

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