Upscaling collaborations among Public Development Banks and private financiers for food security and food systems

Report of ECDPM-IFAD-CDP event, 19 December 2022

Introduction

The Finance in Common Summit (FICS) of 2021 recognized the critical role of Public Development Banks (PDBs) in financing and supporting investments that contribute to the realization of Sustainable Development Goal 2 (Zero Hunger) and launched the Agricultural PDBs Platform for Green and Inclusive Food Systems (coordinated by IFAD).

During the 2022 edition of the FICS, the ECDPM, IFAD, and CDP organised an informal meeting on 19 October, with the objective of discussing the status of the work of the Agricultural PDBs Platform as well as exchanging best practices and blended finance pipelines for upscaling investment in sustainable food systems.[1]

ECDPM, IFAD and CDP, in consultation with FAO, then organised a second hybrid meeting, virtually and in Rome on 19 December, based on the results and open questions from the first event. Around 30 participants, including members of the PDB Platform, private banks, investment networks and food value chain actors, animated a lively debate focused on two main questions: (1) what is a bankable project for sustainable food systems (SFS) and (2) how can blended finance best support SFS? The main points from those discussions are summarised below.

What is a bankable project for Sustainable Food Systems?

In the first session, participants provided diverse perspectives on ways to **assess the Risk, Return and Impact** (RRI) of an investment opportunity and to ensure financial flows reach smallholder farmers and small and medium enterprises (SMEs).

An SME from Kenya kicked off by describing their profitable business model and sustainable impact, as well as outlining the challenges they currently face in accessing finance from commercial banks due to a lack of collateral and high perceived risks. As such, **the question arose whether and how the conventional way banks assess food systems actors' creditworthiness (currently focused exclusively on financial risk and returns) needs to change and take into account their impact(s) on sustainable development goals**, alongside the financial profile of a company.

This would require integrating financial and non-financial criteria into an assessment model to support bankers' decision-making and rebalance the RRI profile of investments in food systems. Better criteria and information systems, in turn, would also help provide higher accountability and allow PDBs to better assess financial partners when putting in place blended finance instruments. Additional non-financial criteria would need to carefully consider the need for higher sustainability impacts while also ensuring farmers and other vulnerable actors are not excluded as a result, but rather supported in a transition to more sustainable practices. Private investors' initiatives such as the Good Food Finance Network (GFFN) are currently working on such a data integration model[2] in the context of the Co-Investment Platform for Financing Food Systems Transformation.

Some banks have made more progress than others in reaching smallholder farmers and SMEs, and participants shared ample experiences and approaches in this regard. Some common elements emerged, providing pointers towards more inclusive finance for food system actors:

- **The need to take a value chain approach** to finance, through e.g. smallholder aggregation schemes, tailored support to farmers to expand their access to profitable markets, and support linkages between the various segments of the value chains, as well as with the ecosystem;

[1] The report of the October side event is available here.
[2] The discussion draft of a *Blueprint for good food finance data systems integration* is available here.

- **The need for effective targeting** through the development of specific financial products and credit lines tailored to different value chains and value chain segments. This requires financial institutions to develop sectoral expertise and understand the differentiated challenges farmers and other stakeholders face;
- The need for those banks that provide direct services to farmers to empower their clients with **financial literacy and business plan development skills**;
- **The need to create a supportive finance ecosystem** whereby PDBs can support commercial banks (who generally have better networks and access to retail customers) with technical assistance, guarantees to derisk investments and concessional finance for on-lending, that can be earmarked to reach specific sectors or target groups (in line with national or international priorities); as well as the need to adopt practical and tailored approaches to sustainability and climate taxonomy, adapted to local context and simple enough to be effectively implemented.

How can blended finance best support SFS?

Blended finance (BF) has the potential to increase sustainable investment and financing for agri-food systems. Yet, BF instruments often take too long to be deployed and procedures are often perceived as very complex, in particular for private sector actors.[3] Moreover, too large ticket sizes and repayment schemes that do not match the farming seasons often lead to excluding certain actors. Thus, in the second part of the meeting, participants focused on identifying opportunities for improvement, both on the supply and demand side of BF.

An impact investment fund from Kenya kicked off the discussion by sharing its experience in financing farmers and SMEs: they have adopted a first deployment approach that allows their clients to access the technical assistance part of the credit facility already in a pre-investment phase while accessing later the rest of the capital for the actual investments and post-investment capacity development. Thanks to this phased approach, they are also able to reduce the interest rates over time, as the risk factor decreases when loans are repaid. The fund also highlighted the importance of informing clients about the exact timeframes of the due diligence process and the finance deployment, as well as ensuring a good understanding of the value chain system.

Participants then highlighted that **despite the wealth of experiences in blended finance, particularly at the EU level, BF instruments have not yet delivered on the high expectations**. Blended finance in the agri-food sector remains marginal compared to other sectors and is too often deployed on a project-by-project basis, with insufficient aggregation. PDBs often tend to adhere to performance indicators similar to those of the traditional banking sector, with a limited risk appetite. Changing this requires focusing on value chains, sectors and countries with a high potential for change, as well as promoting a more conducive public policy environment, both in the EU (where some European DFIs have regulatory limitations to their capital requirement bank exposure similar to commercial banks, institutionally limiting their risk appetite) and in partner countries, aimed at enhancing access to finance for agri-food actors, including through a stronger role of national PDBs.

Another issue participants raised is the perceived limited **availability of profitable investment opportunities** in the agri-food sector. While some highlighted how the investable projects' space is relatively small (not only from a high-risk point of view but also due to a low return on investment), others suggested that there are plenty of bankable opportunities, pointing out instead an information gap problem and the inability of many financial intermediaries to identify investable projects (particularly in Africa).

Next steps

The rich discussion concluded with several remarks on the need for:

[3] A discussion on the barriers to blended finance is available in the report of the October side event.

- **Stronger coordination between different financial institutions and instruments**, including through the fostering of a platform approach to provide finance at scale to agri-food system actors.
- **Deeper and more regular multi-actor policy dialogues at the country level**, including SMEs and farmers organisations since without changing current incentives (e.g. by repurposing subsidies), it will be difficult for investors to leave currently attractive and low-risk sectors (e.g. real estate, government bonds) in favour of the sustainable food economy.

These two needs are **interrelated**: very few countries and investors have yet implemented comprehensive actions across the food system, from land use to food waste reduction to new financial regulations (for investors to be able to take more risk and co-invest with others in food value chains), after their rather general commitments under the UN Food Systems Summit (UNFSS) or the Paris Agreement. But to achieve that, governments and investors need to have confidence that new regulations and shifting to a coordinated approach will increase sustainable financing and investment in food systems, over and above what is currently available for food value chains in their countries.

Following these two identified needs, interested participants could support, as next step, a convergence of actors at a country and value chain level, by **identifying a number of interested PDBs and commercial banks working in a favourable governance environment and collaborating to fill the knowledge gap and match investment opportunities with national level policy plans**. This could take the form of **'joint investment plans' in specific countries and value chains**, characterised by:

- incentives for all players to collaborate on a few pragmatic objectives, e.g. donors matching one-to-one the level of finance by the national government, who in turn would implement the policy reforms needed to make investments in a specific value chain or territory attractive to private financiers;
- the coordination of different financial instruments serving different types of investors and different risk profiles of investees, but also aggregating them (hence the investment projects) around clusters of investment opportunities at country and value chain level, in line with the UNFSS National Pathways;
- strong targeting of (high-risk) value chain players and segments usually marginalised by current investment models, to rebalance the RRI assessment of investment opportunities and ensure financial flows reach smallholder farmers and SMEs.

A number of **existing initiatives in this direction** were mentioned by participants:

- the Co-investment platform for food systems transformation being established by the GFFN with other partners as a concerted effort to bring fundamental change to the global landscape of food finance (across multilateral, public, and private finance, and philanthropic support), including through an Innovative Collaborative Funding Model that establishes an ecosystem aligning the interests of stakeholders to support healthier and more sustainable food systems;
- the design of Pillar 3 of the Food and Agriculture Resilience Mission led by IFAD and AFD, with resources, coordination and commitments dedicated to strengthening, and making resilient, local food production;
- a number of Team Europe initiatives to pilot the upscaling of blended finance for food security and SFS;
- using existing Trust Funds and Facilities for specific sectors and value chain players, such as the Facility for Agricultural Finance in Africa led by AfDB, could also help in selecting grantees.

The organisers of this event will continue facilitating collaborations among participants, drawing on and establishing synergies with such initiatives and the work of the Agricultural PDBs Platform. **The next dialogue will focus on the opportunity of piloting such 'joint investment plan' in Kenya**, given the interest expressed by a number of PDBs, private financiers and other participants to cooperate there around possible investment vehicles and pipelines, and given the maturity in Kenya of both national policy plans as well as blended finance schemes and other financial instruments.