



Reducing Borrower and Lender Risk through Context-Sensitive Product and Portfolio Design: The Case of Complementing Agricultural Development with Microfinance in Tajikistan

Submitted by

Author: Linda Jones, Ph.D., Technical Director, International Operations, MEDA

Co-Author: Nicole Pasricha, Consultant / Project Lead, Microfinance, MEDA

Contact: ljones@meda.org, 1 519 725 1853 ext. 20

This paper is a case study that illustrates MEDA's organizational approach to the development of sustainable financial services for rural households as exemplified by our experience in Tajikistan. Since 2004, MEDA has been implementing a four-year \$4.5 million CIDA-funded agricultural development program that focuses on the horticulture subsector. A key component of the project is to partner with and develop the capacity of a local MFI (microfinance institution) to expand their loan portfolio from mainly urban clients to include smallholder farmers. A \$1 million agricultural loan fund has been made available for this purpose, along with technical assistance and temporary operational support. The primary technical challenges have been to accurately assess the local context, and based on the findings, assist the MFI to design appropriate products and develop a balanced portfolio to meet the needs of the borrower and lender, reducing the risk to both. Special attention has been paid to borrowers' sources of income and agricultural cycles. The disbursement and repayment of the (CDN) \$1m loan portfolio has been so successful that the MFI was able to cover operating costs of the portfolio from interest earned within 18 months and reported almost no default. Farmers continue to take loans, raise their incomes, and seek out additional loan products. The context-sensitive design of products and the portfolio has enabled the MFI to successfully expand into rural lending. Building on this success, the MFI now manages microfinance funds of over \$7 million and has become the leader in rural finance in Tajikistan over the past three years.

Introduction

This paper is a case study that illustrates MEDA's organizational approach to the development of sustainable financial services for rural households as exemplified by our experience in Tajikistan. In 2004, we launched a four-year \$4.5 million CIDA-funded agricultural development program in the northern oblast of Sogd that focuses on the horticulture subsector. During the first three years, the program has achieved significant results, and contributed to industry learning in subsector development and

rural finance. A key objective of the project has been to partner with and develop the capacity of a local MFI (microfinance institution), enabling them to expand their loan portfolio from mainly urban clients, particularly traders, to rural clients with a strong focus on smallholder farmers. A (CDN) \$1 million agricultural loan fund has been made available for this purpose, along with technical assistance and start-up operational support.

The primary technical challenges have been to assess the local context, and based on the findings, work with the MFI to design appropri-

ate products and a healthy portfolio that meets the needs of the borrower and lender. As with all agricultural loan portfolios, it is critical to reduce the risk to both the client and MFI. Special effort has been applied to understanding the income sources for smallholder households, considering agricultural risks and cycles, and creating a balanced portfolio with appropriate loan products.

The disbursement and repayment of the \$1m loan portfolio has been so successful that the MFI was able to cover operating costs of the portfolio from interest earned within 18 months and reported almost no default. Farmers continue to take loans, raise their incomes, and seek out additional loan products. The context-sensitive design of products and the portfolio enabled the MFI to successfully expand into rural lending. Building on this success, the MFI has gone from managing loan funds of \$2 million to \$7.7 million with increased agricultural lending to become the leader in rural finance in Tajikistan over the past three years.

The information provided here is based on MEDA's experiences in program implementation, collection and analysis of baseline and monthly data, and qualitative interviews with staff and clients.

The following sections of this paper provide: MEDA's organizational approach to rural and agricultural finance; details of the case study's country and program contexts; identification and description of the specific knowledge requirements and challenges; discussion of the chosen interventions; and specific results and general learnings.

Organizational Approach to Rural and Agricultural Finance

MEDA's approach to development including rural and agricultural finance has differed from many other organizations in the mainstream. The following description is meant to provide the programming background and context, enabling a better understanding of our methodology and our measurements of success.

Throughout its fifty-year history, MEDA has been committed to finding viable solutions to economic development problems. From our first investment in a locally-owned dairy in Paraguay in 1953, we strive to apply sustainable business principles at every step of programming (Fehr 2004). The selection of partners, design of interventions, program implementation methodologies and exit strategies focus on the building of local capacity for sustainable independent management and ownership. In this process, we have made mistakes and had successes; we have analyzed and shared our experience with the development community; and we continue to refine our practices (see for example, McVay and Ranneklev 2004).

Fundamental to MEDA's approach for achieving sustainable and dynamic local institutions is our identification of suitable local partners – community groups, businesses and institutions – that can be strengthened to continue independently when the project comes to an end. This focus on the strengthening of our partners is reflected in program design and implementation activities that have a critical focus on capacity building through training, technical assistance, mentoring, and results-based management. We avoid the creation of country office structures and ownership models that require us to remain in developing countries over the long term (Fehr 2004), consuming sorely needed local resources for MEDA management and operations.

With specific reference to rural and agricultural finance, MEDA's approach has not been limited to the provision of financial services. Our models of financial intervention in rural areas have changed over the years, beginning with the provision of seed capital for the development of a dairy, to the building of community banks in rural areas, the support of agriculture activities within broader general microcredit portfolios, and the combining of finance with value chain approaches. MEDA's various types of interventions can be summarized into three main approaches: 1) targeted financial services,

2) agricultural market development programs, and 3) complementary programming, which blends the first approaches, often with direct financial investment at the outset (Fehr 2004). Utilizing these strategies, MEDA implements programs and delivers expert consulting world-wide: from our first steps in Paraguay to today's challenging environments such as Afghanistan, Haiti, China and Angola.

In the area of rural development, MEDA increasingly implements or advises on programs that integrate microfinance into market development activities, such as the development of agricultural value chains. In this approach, MEDA incorporates value chain principles and best practices with skills and expertise in rural and agricultural finance. This model is proving to have benefit both as a risk management reduction strategy and a means to identify potential linkages between producers, markets and financial institutions that promote sustainable and holistic growth (Andrews 2006).

Country and Program Contexts

MEDA's overall program goal in Tajikistan is to alleviate poverty of farm families in the northern oblast of Sogd through the development of the fruit and vegetable subsector. Northern Tajikistan has been known historically for the magnificent fruits and vegetables of the Ferghana Valley, and as such provides a rich opportunity for effective agricultural programming.

Tajikistan is a small, landlocked, mountainous country in Central Asia bordering China, Afghanistan, Kyrgyzstan and Uzbekistan. Already the poorest of the republics when part of the Soviet Union, civil war and economic collapse reduced 84% of the population (6.4 million total) to poverty since independence in 1991, with a GDP per capita of just US\$161 in 2001.¹ This number has risen steadily since

then, and climbed over \$1000 in 2005.² More than 70% of the population lives in rural areas that have been further devastated by floods, landslides and a major drought in 2000-2001. Prior to the launch of MEDA's program in 2004, international development interventions had largely focused on relief efforts, but Tajikistan was ready for innovative strategies for private sector development. MEDA realized that the agricultural sector would be critical in the building of sustainable livelihoods and wealth creation, and so focused resources in this area. Specific details of the context and overall program design follow in the next paragraphs.

Program Context: Fruits and vegetables are generally grown by smallholder farmers. Some of these farmers are also microprocessors who prepare their horticultural outputs for local markets according to traditional means (e.g., pitting, cutting and shaping are accomplished with labour-intensive hand tools). Prior to the start of the MEDA program, farmers did not have access to credit to purchase inputs (e.g., fertilizer), improve stock or upgrade irrigation. The limited microcredit available in the region was available mainly to traders, and mechanisms did not exist to deliver appropriate rural credit products. Producers often had only limited access to markets and processors, selling their goods at local markets or to traders. As a result, waste was high, with quoted figures ranging from 25% to 50% spoilage in 2001.³ Producers generally own or lease small plots of land (although some are co-owners of collective farms) with the benefit that that these land

¹ Tajikistan Country Brief, The World Bank Group (2002). www.worldbank.org

² Human Development Report 2006. UNDP (2006). http://hdr.undp.org/hdr2006/statistics/countries/country_fact_sheets/cty_fs_TJK.html

³ Toshali Mukimov, The Chief of the Department of Fruits and Vegetables, Department of Agriculture, Dushanbe, Tajikistan. We were shown figures that indicate that 300,000 tonnes of fruit were sold per year during the Soviet era. Last year, only 147,000 tonnes of fruit were sold. 50,000 tonnes were known to be spoiled, and the remaining 100,000 have not been accounted for (reduced production, spoilage, informal economy).

holdings can be easily upgraded for quick return on investment. This means that farmers were, and continue to be, eager to borrow money to improve their land (e.g., purchase inputs, install small scale irrigation, reclaim hill-sides) and are not dependent on donor infrastructure projects. There was little or no formal organizing of smallholder horticulturalists in Sogd, although there was interest in cooperation. For example, farmers were collaborating in digging community wells or repairing irrigation channels, and were interested in enhanced opportunities to work together for mutual benefit.

Further along the value chain for processed fruits and vegetables, there were microprocessors and large processors, but there was a lack of processors at the SME (small to medium) level. The microprocessors work by hand and in primitive conditions, producing outputs of a quality that are only suitable for household consumption, or local and some regional markets. Although microprocessors are unlikely to produce for international markets, better tools and packaging are available, and microprocessors expressed an eagerness to acquire loans to streamline their work and improve quality. For example, a small hand-turned device available from Iran would minimize the tedium of cracking pistachio shells, a job that is currently done by hand with a hammer. At the other end of the spectrum, huge factories that processed fruit and vegetables for local and national consumption (for example, Siberia was a significant market for Tajik processed foods) during the Soviet era are still functioning at a reduced level. We visited three such factories in Sogd and we noted an interest on the part of management to get up to former capacity and export. We did not endorse this as a realistic goal, however, since the large ex-Soviet facilities and equipment were not only in an extreme state of disrepair but they would also be inefficient in a market economy. Finally, there was no industry-level association or cooperation amongst proc-

essors which had caused the industry to remain static in the face of increasing global competition.

There was evidence of some activity at the intermediary levels of the value chain – that is, wholesalers who purchase produce and resell to traders, exporters or processors, and processors who collect produce from many farmers. However, there was also significant room for development at this level, especially in the areas of business training and market development. For example, one informal group that collected grapes from farmers for drying, packaging and reselling expressed interest in growing their business through a loan, but they had no knowledge of basic business planning such as cash-flow and profit projections. It became clear that the program strategy would need to combine not only financing but also business training.

Program Design: At a primary level of intervention, MEDA designed and launched a program that would assist underserved smallholder farmers in their adaptation to and growth in a globalizing market economy. The program was designed to benefit thousands of rural families, by: 1) providing access to traditional and new production knowledge; 2) supporting the adoption of up-to-date technologies, improved inputs and better services; 3) strengthening farmers' ability to work co-operatively and take collective action; and, perhaps most importantly, 4) establishing a viable rural credit program that would continue to meet the needs of farmers after donors and international NGOs exit from the region.

At a secondary level of intervention, MEDA is advancing the creation and growth of small and medium enterprises (SMEs) that process and market the agricultural output of Sogd's rural population, filling a current gap in the value chain. Main activities at this level include: business development (including market access and linkages), technical assistance and technology transfer, association formation, and SME

finance including both a loan fund and a matching grant mechanism.

Knowledge and Challenges – Rural Finance

When MEDA began exploration for and design of its agricultural development program in Tajikistan, we identified both the knowledge requirements and the challenges that would face us in developing sustainable finance for smallholder farmers. While it is not possible to discuss all the factors and interesting challenges confronting MEDA in Tajikistan, I have classified them into three broad categories:

1. Local Partner – the identification of a strong local partner that would ideally have:

- a. a developed organizational infrastructure
- b. proven experience in or capacity to expand into agricultural finance
- c. a willingness to adapt operations and products to meet the unique requirements of agricultural clients
- d. familiarity with the programming regions / districts
- e. a solid reputation amongst communities and potential clients
- f. technical agricultural knowledge such as seasonal cycles and risks

2. Clients and Context – evaluations of general client capacity and context regarding

- a. attitudes towards credit in the predominantly Muslim communities
- b. population density and potential to physically access financial services
- c. literacy and financial literacy
- d. commitment or ability to repay loans in a timely manner
- e. risks to and risk mitigation strategies for agricultural households

3. Complementing Agricultural Value Chain Programming with Microfinance – intervention design decisions pertaining to the integration of finance with value chain programming for smallholder farmers:

- a. an understanding of how the programs value chain activities – horticulture production (from input supplies and irrigation to crop selection and handling) and market development – could positively impact the viability of farmers and therefore their ability to repay loans, and how the program should deal with the feedback loop between the two
- b. the connection (if any) between specific agricultural extension / market development and financial services clients
- c. the connection (if any) between program extensionists / market development staff and loan officers

Findings and Challenges regarding Local Partner:

MEDA conducted research and carried out an exploratory mission to Tajikistan in the spring of 2003. Through secondary sources, we had identified microfinance institutions (MFIs) that were operating in northern Tajikistan both in the agricultural and non-agricultural sectors. We communicated with the MFIs concerning potential partnership opportunities prior to our mission, and narrowed down the number of institutions with which we would meet. One institution stood out amongst the others – the National Association of Business Women of Tajikistan (ABW) – for its operational success, professionalism and responsiveness. As a result, during our mission, much of our time was focused on meeting ABW's management, staff and clients, reviewing their operational capacity, and discussing their interest in future portfolio and product development. ABW also had wide experience in Sogd oblast, with specific districts of concentration that encompassed areas with strong horticulture production.

ABW demonstrated a strong willingness to expand into rural and agricultural finance and committed management time above and beyond program funding. However, the greatest challenge in partnering with ABW would be their lack of experience in agricultural lending, and the general deficit of knowledge regarding

agricultural issues. This constraint would direct MEDA's intervention design, with a focus on the development of suitable products and a balanced portfolio.

Partner Overview – ABW / IMON

ABW strives to combat poverty in Tajikistan by implementing microenterprise development programs that provide access to economic resources, enable clients to become mobilized, and stimulate new income sources for households. ABW has invested extensively in the development of a vibrant microfinance institution as well as the broader industry in Tajikistan.

In 1999, ABW began the implementation of a microcredit program in close partnership with Mercy Corps (MC). This program was significantly expanded by working with MEDA and diversifying into agricultural lending starting in 2004. Later the same year, with the aim of separating the microfinance activities from the rest of the NGO, MC and ABW began the work to create a microfinance foundation, IMON. MEDA sits on the board of IMON, and is transferring the agricultural loan fund to local ownership. IMON now manages microfinance funds of over \$7 million with loans from EBRD among others.

Currently IMON is going through a transformation process and is planning to become a deposit-taking organization by the end of 2007.

As ABW was not a newly established microfinance institution, it had all the necessary MIS, accounting systems, management systems, hiring processes and training programs in place. This has allowed the MEDA TA team and the ABW / IMON management team to focus on researching and delivering appropriate products and services aimed at the farming and processing markets. (Andrews 2006).

Findings and Challenges regarding Clients and Context: Although Tajikistan is a predominantly Muslim country, we learned that

fair lending practices are accepted and established. Further, despite the fact that literacy rates have dropped in rural areas following the end of the Soviet era, for the most part, small-holder farmers are both literate and financially literate. The population is dispersed, but tends to center around and have moderately good access to smaller cities and towns (where the proposed partner was already operating with urban clients). Tajiks have not been inundated by giveaways nor entrenched in a donor economy – this, combined with their cultural norms, has resulted in a strong commitment to repay loans. Added to this fact, extended families live together and when one member of the household takes a loan, the entire family supports the process from borrowing to repayment. Finally, on the plus side, income diversification is well developed. We met people with an amazing entrepreneurial spirit: for example, a teacher who instructs for a pittance in a local school, makes rope at home in the evenings, and sells clothes imported from China on her day off in the local bazaar; and a doctor who works the early shift at a clinic (for less than \$10 a month), drives a minibus in the afternoons, tends grapes in the kitchen garden, and fattens goats and cattle to augment household income.

Identified challenges and risks with regard to clients would be the suitability of loans for horticulture production, with affordable terms and repayment rates. With typical existing loan product being offered for thirty days, and at 4% interest for that month, the risk was too high for agricultural production.

Findings and Challenges regarding Complementing an Agricultural Development Program with Microfinance:

The integration of value chain and financial services interventions on such a large scale was uncharted territory for MEDA. Based on our past experience in economic programming and the vision we had for sustainable development in Tajikistan, we decided upfront that we would not want to restrict the two separate program components – value chain development and financial ser-

vices – to a single group of clients. We would operate in the same districts, we would make cross-referrals of clients, but each program service would have autonomy in how it was structured and who it served. For donor purposes, the numbers of target clients were enumerated separately as well, with different target numbers. For practical purposes, however, agricultural extensionists and loan officers would be housed in the same office in each district. We believed this would contribute to sharing of information without jeopardizing program goals.

The key program challenge would be to coordinate and share information between the two 'pillars' – particularly at the program level – so that effort would not become scattered and end in reduced impact. With particular reference to the rural finance component, value chain information had the potential to assist in decisions about suitable terms for loans and portfolio diversification.

Design and Implementation

The program operates on multiple levels dealing with a range of implementation issues. This discussion of interventions focuses on the key challenges for the agricultural finance component outlined in the previous section, with special reference to product and portfolio design.

Supporting the Local Partner: As noted above, although the selected MFI partner, ABW, had strong organizational capacity and was established in the selected districts, they had very limited experience in agriculture lending and not much relevant knowledge of agriculture in general. MEDA planned a program intervention to concentrate technical assistance to ABW on the design of the loan portfolio and the specific agricultural loan products. Together, MEDA and ABW prepared a business plan (MEDA 2004) for the loan fund that detailed loan products, repayment terms, interest rates, loan sizes, and group versus loan methodology. It was important for ABW to contribute its expertise concerning the local MF con-

text in Tajikistan, and for MEDA to share its technical knowledge around industry best practices. Where the latter were not available – particularly with regard to the contingencies of agricultural lending – MEDA and ABW worked together to design interventions that could be piloted and then adjusted according to the results and findings along the way.

First, it was important to understand and be faithful to the long-term objectives of ABW's existing microfinance program which were to develop and support existing micro and small enterprises in increasing their profit, creating more jobs, and transforming from the informal to the formal sector of the economy. ABW was interested in having the informal sector (non-registered enterprises) become fully licensed taxpayers of society, and at the same time giving them a chance to conduct their business on a more stable basis. The components of the microfinance program were structured upon the following basic principles of the MFI:

- Utilization of group and individual lending methodologies to meet the needs of informal enterprises (without available physical collateral) and formal enterprises (with registered businesses and available physical assets);
- Setting interest rates at market rates to reach businesses that do not have access to the formal banking sector, while ensuring future institutional sustainability;
- Use of non-traditional forms of collateral, including group guarantees, to offset the lack of physical assets common to micro businesses;
- Simple application procedures and fast turn-around time for loan disbursements;
- Assistance with documentation for clients with little or no education;
- Short loan terms and frequent small repayments to ensure on-time and full loan repayments;
- Training component to further build borrower's competence in developing financial statements and business plans.

Building on these parameters, MEDA and ABW designed the specific agricultural loan products described in the following sections.

In the original business plan for the loan fund, the general categories of economic activities to be financed by the program included but were not limited to (MEDA 2004):

1. Agriculture activities (e.g. fruit and vegetable crops, inputs, fertilizers etc.)
2. Farm-based processing (e.g., drying, pitting, compote production)
3. Agri-business (trading related to agricultural activities – buying/selling fruits and vegetables and animals)
4. Services associated with rural based activities and enterprises (e.g., input supplies, storage facilities, and transportation)
5. Animal husbandry (e.g. fattening of food animals, raising of poultry, small animals etc.)
6. Other related activities.

The agricultural loan fund is one component of a rural development program that centres around the building of the horticulture sub-sector, and program activities also encompass agricultural extension and SME development. Therefore, despite the wide range of activities in the region, it was decided that at least 80% of the loans would be for clients' undertakings in fruit and vegetable cultivation and post-harvest handling. Lending in other areas would be pursued to diversify the portfolio for the reduction of overall risk without much dilution of the original intent. Further, the loans provided for the various economic activities would be designated mainly for working capital inputs and small fixed assets for existing businesses and activities.

Lastly, because the loan fund was to remain the property of the donor until satisfactory performance allowed for transfer of the loan fund to the partner (ABW), MEDA took steps to mitigate the possible exchange rate risk to the partner (in the unlikely event the transfer was not approved and the loan fund had to be

returned). These steps included: paced disbursement of the loan fund by tranche according to disbursements to clients, close monitoring of the projects' agricultural loan portfolio performance, and conversion of the funds into Tajik currency before transfer to ABW, effectively denominating the funds owed to the donor in local currency.

Mitigating Client Risk: The greatest challenge and risks with regard to clients would be the viability of loans designed specifically for horticulture crops.

In October 2004, prior to the start of project implementation, MEDA and ABW together conducted a baseline survey (sampling the target client group), in order to define the main social, economic, and ecological indicators which would serve as a basis for the development and implementation of project activities. The survey collected information on household income and expenses, agricultural activities, markets, and also on credit. The results showed that one-third of interviewees had some experience with credit, but mostly from informal sources without interest or a real repayment schedule. Eighty percent of respondents were interested in taking a loan. About half were interested in a short-term loan, for between \$300-\$1,500, for agricultural inputs or equipment rental. The other half were interested in longer term loans for larger amounts (above \$1,500) for investment in irrigation systems or equipment purchase. Survey participants understood interest rate concepts and had ideas of how much they would be willing to pay: for short-term credit, between 2-4% monthly, and for long-term, between 1-3% monthly. Building on the survey results, some limited experience ABW had had with agricultural loans prior to the project, and our experience in rural credit in other countries, MEDA worked closely with ABW staff – including consultations with loan officers and credit managers – to design appropriate, flexible agricultural loan products that would mitigate against the

inherent risks in borrowing for agriculture (see table below, excerpted from the original business plan for the agricultural loan fund (MEDA 2004). It was expected that after the first four to six months of operations the product parameters, loan processes and approval systems would be reviewed and modified as required.

	General WC	Ag Loan	Leasing – Fixed Assets	Specialty products
Use	Working capital loan or small fixed assets – traders, processors	Production inputs, fertiliser, etc.	All types of fixed assets	For example: Irrigation
Amount (min - max)	0 – 1300 c\$	150 – 1650 c\$	650 – 5000 c\$	Max. 5000
Term (min - max)	3 – 6 months	6 – 9 months	6 – 18 months	To be decided
Payment frequency	2 weeks or monthly	Interest monthly principal in 2 – 4 payments at end	Monthly	Monthly
Grace period	None	3 – 6 months	0 - 2 months	To be decided
Interest range*	3 - 3.5%	3 – 3.5%	2.5 – 3%	To be decided
Fees	1 – 4%	2-3%	2-3%	To be decided
Penalty	1%	1%	1%	To be decided
Collateral	None required but is accepted	Contribute 30% of need	Org. own item until paid for.	To be decided

Other general decisions about the loan products and lending procedures that were taken to protect ABW and its clients included the following:

- The loans are offered for three to twelve month terms, depending upon the type of agri-business activity undertaken (e.g., cultivation vs. processing, etc.) as well as the economic capacity of the group or individual. Larger fixed asset loans or special loans (irrigation) can have longer repayment periods.
- Clients with good repayment histories and / or business cycle that would best be served by a monthly repayment schedule might be given this option while others would start with biweekly repayments. .
- As can be seen in the table there is more than one repayment option. The new agriculture loan has a longer, more flexible grace period (decreasing risk to the client), while still requiring monthly interest payments (decreasing risk to the lender). The final repayments of principal are made over a few weeks or months to allow the client

more flexibility in selling in order to capture better product prices.

- Interest is calculated using the declining balance method.
- A comprehensive loan application process has been implemented, and in the case of group loans, involves extensive participation of the entire group.
 - Borrowers receive training on loans including the management of repayment.
 - Individual loans are only be granted to a few outstanding performers, after they have proven themselves as part of a group.
 - Credit committees initially reviewed all loan applications and the input of loan officers was sought on each application.

In summary, the project aimed to provide flexible products that would meet clients' various needs, mitigate risks for both the lending institution and the borrowers, and contribute to the development of sustainable rural and agricultural finance in Tajikistan.

Sharing Information for Complementary Programming:

We recognized from the outset that a challenge for such a large integrated agriculture program would be the coordination and sharing of information between the two 'pillars' – value chain development and rural financial services – so that effort would not become scattered and result in reduced impact. With particular reference to the rural finance component, value chain information would assist in decisions about suitable terms for loans and portfolio diversification.

We knew that information on the agricultural cycles and risks would assist in designing products, growing a balanced the portfolio, assessing loan applications and making other decisions about the rural finance component. The program is organized so that advisors to field staff from headquarters report to the overall headquarter program manager. This

group meets for annual planning and shares quarterly reports, ensuring coordination at the program level. At the country level, managers for the main components report to the field manager and come together for weekly coordination meetings. Field program issues are raised and dealt with at these meetings. In the field offices in the districts, loan officers and extensionists share offices, and they are able to exchange more detailed information with regard to clients and loan applications. Finally, there is an annual steering committee meeting that brings together the headquarters manager, program field manager, ABW senior management, the donor and a government advisor where successes and challenges can be reviewed across the program.

Despite the best intentions of organizing and information flow, issues arise that must be dealt with above and beyond the regular coordination meetings. For example, given the high demand for credit, the extensionists initially began to spend a lot of time referring clients to the loan officers and reviewing loan applications. However, it was not positive for the extension program as agriculture staff were spending less time setting up their own training and technical assistance programs than desirable. Overall, it was viewed as positive for project start-up but then extensionists were encouraged to focus more on agricultural training and technical assistance, and in some cases moved to separate offices

Results and Learnings

As of October 2006, there had been 3557 loans disbursed totaling US\$1,414,734. The rural finance portfolio is solid (details below) and ABW has joined with Mercy Corps to create a micro-finance foundation, IMON, that now has over US\$7 million in loan funds. Both group and individual loans have been successful and repayment is almost 100%. Loans are mainly for working capital, such as production inputs, however, in the off season, lending for live-stock, produce storage, and winter crops keeps

the portfolio active. Agro-leasing, however, has not been developed as planned due to the absence of local suppliers. The use of extensionists to train and advise loan officers has been so successful for the loan portfolio that IMON has replicated this model in its Central and Kurgantuve branches (Sharipova 2007).

The following tables provide an overview of the portfolio indicators, operational efficiency and portfolio quality. The agricultural loan fund portfolio has excellent performance with a strong return and low default.

Portfolio Indicator	MEDA Agricultural Loan Fund Portfolio	IMON (ABW) Total Portfolio
Gross Loan Portfolio	US\$ 824,988	US\$ 7,519,722
No. Loans Disbursed, 2006	3,621	29,897
No. Loans Outstanding, Dec. 2006	1,924	14,305
No. of clients	1,924	14,182
No. of women clients	525	7,340

Operating Efficiency and Portfolio Quality	MEDA Agricultural Loan Fund Portfolio	IMON (ABW) Total Portfolio
Portfolio at risk (PAR) (>1 day)	0.10%	0.65%
Operating Expense Ratio	15.23%	21.61%
Avg. Outstanding Loan Size	\$1,055	\$1,733
Return on Assets	31.5%	10.4%
Return on Equity	n/a	24.4%

Having a strong local partner with existing structures, systems and staff was critical in the rapid success of the rural program. However, MEDA is beginning to see similar successes working with inexperienced partners to develop their institutions and support rural lending (e.g., Nicaragua, Afghanistan). Although progress has been slower in such cases, the same learnings apply:

1) Capacity of MFI – Whether working with an experienced or fledgling microfinance institution, the overall capacity of the organization has to be sufficient to handle a rural lending portfolio. In particular, the institution needs to have good record keeping and the ability to

constantly monitor the health of its portfolio and the suitability of its products to meet the needs of clients. When expanding into agricultural finance, the portfolio must be balanced to reduce risk – balanced in terms of activity, group and individual lending, and size of loan. In Tajikistan, MEDA learned that an extensionist who could not only advise on general agricultural issues, but also knew specific clients and situations, greatly reduced the risk to the portfolio.

2) Capacity of Clients – In agricultural lending, the diversification of household income is crucial to limiting household risk and enabling prompt repayment of loans. ABW / IMON only lends to one member of a household, with the result that the entire family supports the financial risk through their various income generating activities. With the extended family system in Tajikistan, and a significant amount of remittance revenues, the potential for repayment was further enhanced. Recognizing a community's culture of repayment – such as the strong desire to repay in Tajikistan regardless of the outcome – can also help in designing delivery mechanisms and terms that encourage clients to meet loan schedules. Finally, individual product design needs to take into account information about agriculture practices and cycles to ensure that terms are not unreasonable and doomed to failure.

3) Complementing Agricultural Development Programs with Microfinance – If an agricultural lending program is taking place within a broader subsector or value chain project, a good flow of information between pillars can assist with general and specific decisions. Understanding the overall agricultural context contributes to loan product and portfolio design, while details on specific clients can inform the review of client loan applications. As noted above, this has been extremely positive for the loan portfolio in Tajikistan, it has at times drained resources of the extension component of the combined program. However, now that this dynamic is understood, the program can

mitigate for this with positive impact for both the lending and extension pillars. On the other hand, agriculture extension clients are able to more rapidly apply improved techniques and adopt new technologies when they have access to a loan fund.

4) General Learnings – MEDA has also drawn some more general learnings from the Tajikistan experience that support our findings in rural and agricultural finance elsewhere (Fehr 2004):

- No matter how small-scale an intervention, a program must plan up front for investment in institutional strengthening and staff capacity building, with special attention to the necessary adaptations for rural lending.
- Although it is not imperative to implement programs that combine agricultural development with microfinance – it is optimal in many cases to find linkages to other local services (financial institutions, input suppliers, wholesalers, technology providers) and thus enable clients to participate in growing subsectors.
- Rapid growth in a rural setting is almost always too difficult to manage. We believe the fast growth and achievement of sustainability in Tajikistan is rare, and organizations should plan to grow slowly.
- For agricultural portfolios, diversification of production reduces risk. Since one institution will generally support a narrow range of subsectors, it is wise to balance them, monitoring for markets, crops, prices, opportunities, trends etc.
- If lending to farmers involved in commodity markets, rural MFIs should play a proactive role in keeping abreast of changes in these markets, limiting the amount of financing they put into products with poor or highly volatile futures. At the same time, an informed MFI can help finance successful agricultural practices that improve yields, improve quality, and mitigate risks.

- A complementary program also has the potential to examine how agricultural production loan portfolio can be supported by financing other activities in the supply and value chains, including input suppliers, equipment providers, marketing agents and other support services.

Conclusion

MEDA is continuing to develop, implement, and provide expert advice to rural development programs around the world; programs that either fully integrate or support linkages to microfinance services. Although agricultural finance is viewed by many as an overwhelming challenge, we have found that combining our expertise with the experience and wisdom of our local partners is leading to positive results and models for replication and scale-up.

REFERENCES CITED

Andrews, M. (2006) *Microcredit and Agriculture: How to make it work*. Global Microcredit Summit, Halifax.

Fehr, P. (2004) *MEDA's Approach to Rural Finance: Flexible, Market-led Design*. Small Enterprise Education and Promotion Network, Annual General Meeting, DC.

McVay, M. and Ranneklied, S. (2004) *Towards a Strategy for Business Development Services*. Mennonite Economic Development Associates, Waterloo.

MEDA (2004) *Business Plan for Rural Credit Program for the Association of Business Women of Tajikistan*. Mennonite Economic Development Associates, Waterloo.

Sharipova, S. (2007) Personal Communication from founder of ABW and IMON – email January 2007.

