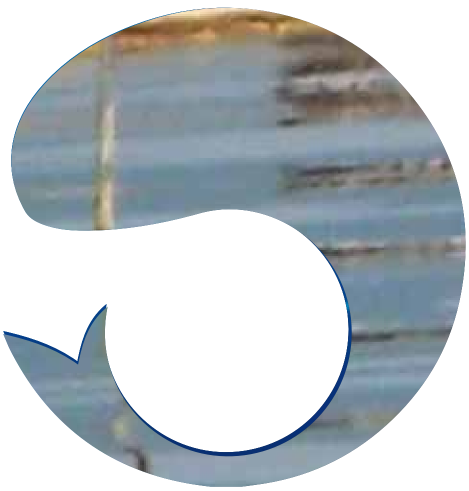
The Pan-African Fisheries and Aquaculture Policy Framework and Reform Strategy: Private Sector Investments and Financing Mechanisms for Fisheries and Aquaculturein Africa

Catalysing Growth in Investments for Small and Medium Enterprises



NEPAD
TRANSFORMING AFRICA

AFRICAN UNION
INTERAFRICAN BUREAU FOR ANIMAL RESOURCES

Executive Summary

Africa accommodates 14% of the world's population, yet it only produces 5% of total and 2% of farmed fish.

The continent imports three million tonnes of fish annually worth USD 3 billion as it does not produce enough to satisfy its own internal markets. However, the continent could produce significantly more if existing resources were effectively harvested.

The underlying barriers to financing Small and Medium-Sized Enterprises (SMEs) in Africa can be classified into five types related to (i) risks involved; (ii) institutional development; (iii) policy and regulatory frameworks; (iv) technical skills; and (v) management capacity.

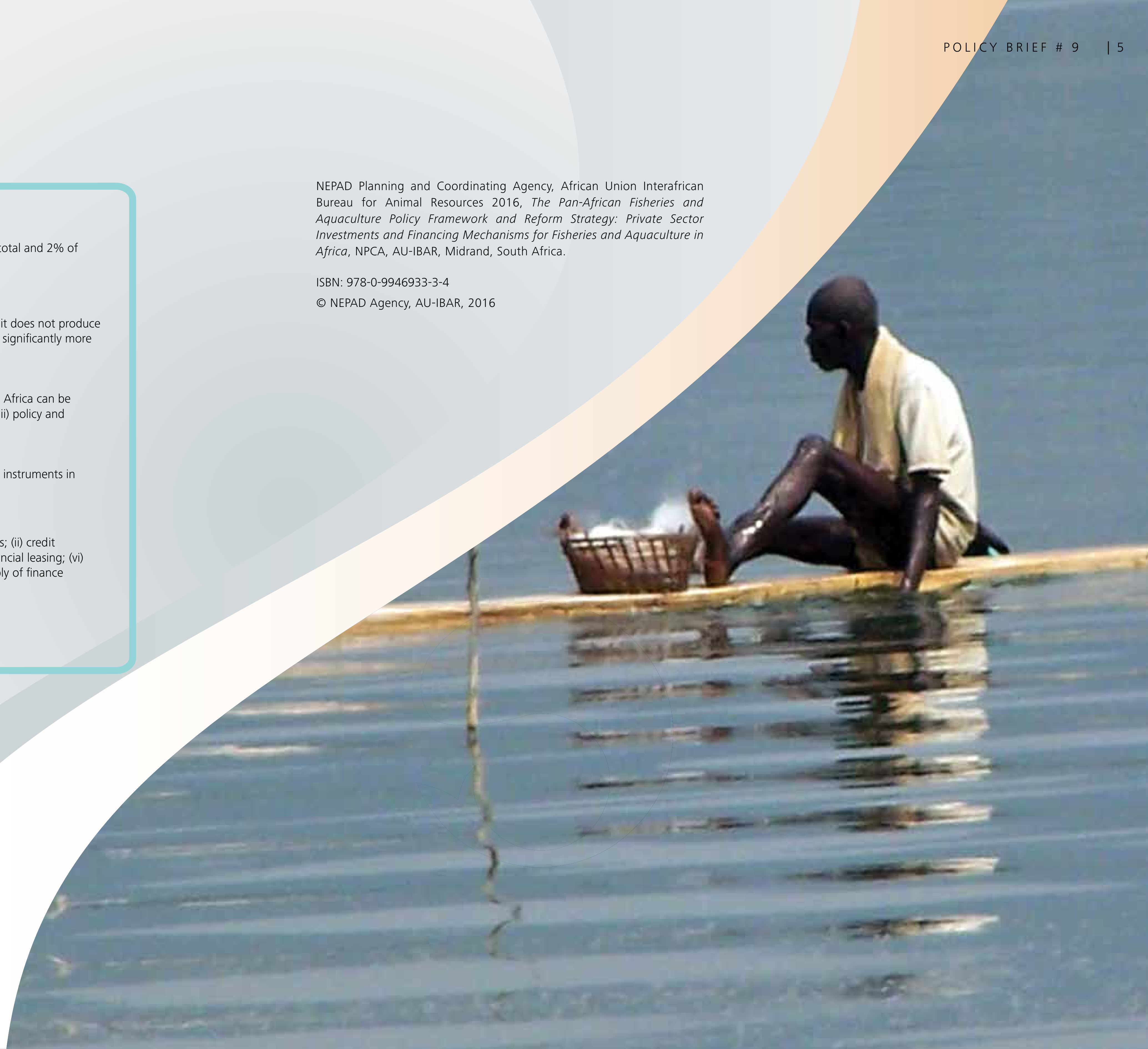
Apart from the need to boost SME capacities, there is a need to promote financial instruments in order to help reduce risks stemming from lack of transparency from some SMEs.

A number of financial instruments are recommended, including (i) guarantee funds; (ii) credit associations; (iii) micro-credit institutions; (iv) warehouse-receipt financing; (iv) financial leasing; (vi) institutional funding; (vii) second-tier intermediation; and (viii) expanding the supply of finance through the non-financial private sector.

NEPAD Planning and Coordinating Agency, African Union Interafrican Bureau for Animal Resources 2016, *The Pan-African Fisheries and Aquaculture Policy Framework and Reform Strategy: Private Sector Investments and Financing Mechanisms for Fisheries and Aquaculture in Africa*, NPCA, AU-IBAR, Midrand, South Africa.

ISBN: 978-0-9946933-3-4

© NEPAD Agency, AU-IBAR, 2016



Introduction & Background

The world's population surpassed seven billion and may grow to 10 billion by the end of the century, hence, the demand for fish will reach an annual level of 200 million tonnes. This is a 33% increase on the current production valued at USD 260 billion.

Africa accommodates 14% of the world's population, yet it only produces 5% of total fish and 2% of farmed fish. In contrast Asia, as the most populous continent with 60% of the global population, produces68% of total fish and 85% of farmed fish. The continent imports three million tonnes of fish annually worth USD 3 billion as it does not produce enough to satisfy its own internal markets. However, the continent could produce significantly more if existing resources were effectively harvested.

- *The conclusion is that if Africa produced more, it could consume more.*

  Fish has the potential to be a lucrative export earner for Africa as the continent exports 1.8 million tonnes of fish at an average price of USD 2,600 per tonne – 22% of what it produces, compared with a global figure of 28%.

- There is no doubt that there is an opportunity for Africa to export more than it does and, thus, add value to what it already produces.

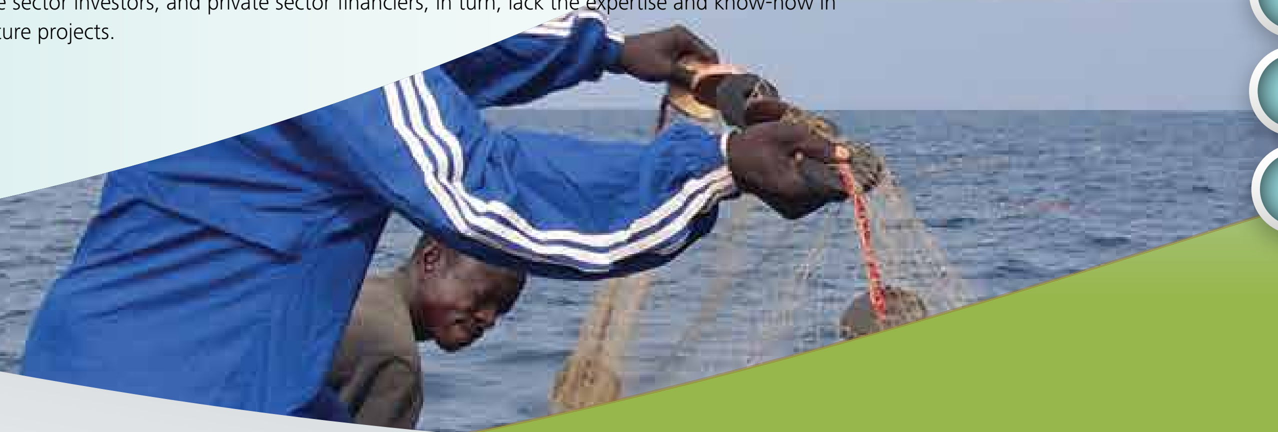
  People have been harvesting and trading in fish since time immemorial. It is based on tried and tested technology using proven business models. Experience in both Africa and elsewhere has shown that this is a profitable and sustainable business.

- *With the right approach and the right support, the SME sector will deliver profits and growth, today and tomorrow.*

The issues of food security, employment, secure and sustainable livelihoods; are embodied in the Millennium Development Goals (MDGs). A vibrant fisheries and aquaculture sector is linked to these issues. Firstly, because fish is a valuable source of essential foods. And secondly, because it creates wealth and employment, not only at point of production but throughout the entire value chain;.

The role of the Small and Medium Enterprises in Fisheries and Aquaculture

There is no doubt that the private sector can play a key role by tapping into the vast opportunities presented by the fisheries and aquaculture sector in Africa. The story is even more compelling when focusing on SMEs in Africa as these are currently under-funded due to an information asymmetry. SME entrants and potential entrants lack the business acumen to fully articulate their projects to private sector investors, and private sector financiers, in turn, lack the expertise and know-how in appraising fisheries and aquaculture projects.



The underlying barriers to financing SMEs in Africa can be classified into five types related to:

i - Risks involved;

ii - Institutional development;

iii - Policy and regulatory frameworks;

iv - Technical skills; and

v - Management capacity.

A quick elaboration on the five factors above reveals the following:

1. Bureaucracy, actual or perceived, and a lack of awareness about SMEs have been identified as serious barriers to the successful development and sustainability of SMEs.
2. Existing relations are crucial to the lending relationship between SMEs and local financial intermediaries, especially when new products are introduced or for speedy approvals.
3. Appropriate monitoring and performance measurement metrics, which are important in a social business model such as a Fund for SMEs in the fisheries sector are lacking. Country-specific legal regulations are cumbersome for some financing instruments such as private equity and venture funds.
4. Business development support from a group of talented management professionals with knowledge of financial accountability, operations, and international/national markets in the fisheries sector – in order to serve as advisors and talent-enablers to SMEs is crucial.
5. Technical skills are necessary but not sufficient, management capability is critical, as is the enabling environment .

This policy brief seeks to identify possible financing instruments and strategies that can be considered in forging a greater and more visible role of large private sector investors/funders in supporting SME development in the fisheries and aquaculture sector in Africa.

Problem Statement

Despite ample evidence of the developmental impact of SMEs, the private sector – particularly banks and financial institutions - still lacks an understanding for the special needs of fisheries and aquaculture SMEs. They prefer to finance large enterprises where they feel more comfortable assessing the risk and return combinations. And even then, when they are prepared to lend, they will often only do so if their exposure is covered by collateral or third party guarantees, neither of which are easily available to the proprietors of small and medium-sized actual and potential businesses.

Start-up ventures and expanding enterprises in Africa, as elsewhere in the world, are frequently hampered by a lack of "own funds" or equity capital. Long-term borrowing is fully justified to the extent that any such loan capital significantly leverages shareholders' investments and provides higher returns on equity. But strict conditions apply: (a) borrowers' realistic cash flow projections must amply demonstrate repayment capacity; and (b) the ratio of equity to borrowings must adequately cover lenders' perceived risks (political, sector, commercial, etc.).

It is immediately apparent that under such conditions, recourse to longer-term borrowing may prove limited or even impossible without the presence and support of dedicated investment and loan institutions or guarantee funds. Short-term credit facilities from banks are necessary to finance working capital needs that are not met by suppliers' credit or shareholder advances.

Therefore, the question that begs an answer is, what can be done to encourage private sector appetite for SMEs in the fisheries and aquaculture sector in Africa?

Approaches and results

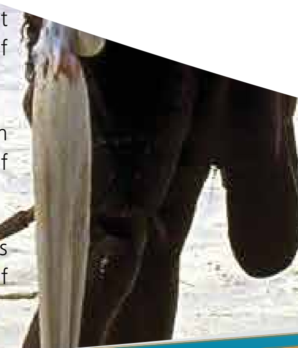
The use of SME facilities and equity funds that enable non-specialist SME financiers to partake in SME financing through intermediaries is a key mechanism for getting long-term development finance into SME/private sector development. The strength of any SME funding facility/model is reflected in its success in attracting local banks and leading international development financiers, and its ability to minimize risk and cost.

Apart from the need to boost SME capacities, some financial instruments can help provide missing information or reduce the risk stemming from some SMEs' lack of transparency. These are:

- **Guarantee funds** to ensure repayment in case of default. In several countries, especially in Central Africa, this has not worked since provision of a guarantee has meant less rigorous choice of investment projects and a lower rate of debt recovery. In successful instances, borrowers and financial institutions have worked together to maintain a good rate of recovery and to reduce interest rates.

- **Credit associations** that reduce risk by sharing it are more common. They help financial institutions choose to whom to lend, by guaranteeing the technical viability of projects, and sometimes providing guarantees. Admittedly, growth of these bodies is limited by the lack of organisation among SMEs in Africa.

- **Micro-credit institutions** could be put on a firmer financial footing by developing and adapting long-term savings products that exist elsewhere, such as life insurance and home-saving plans, and encouraging the setting up of specialized refinance banks.



- **Warehouse-receipt financing** that may be suitable for the fish processing part of the value chain is a form of inventory financing in which loans are made to manufacturers and processors on the basis of goods or commodities held in trust as collateral for the loans. The goods may be held in public warehouses approved by the lender, or may be held in field warehouses located in the borrower's facilities but controlled by an independent third party.

- **Financial Leasing** can reduce risk effectively for credit institutions but are still little used in Africa. Financial lease is a medium-term financial instrument based on a contract between the owner of an asset called the lesser and another party called the lessee who is given the right to use the asset for a specified period in return for specified payments and ownership of the asset is transferred to the lessee by the end of the lease term.

- **Institutional Funding** is also an untapped option for SMEs in general, where we need to encourage local banks to issue local bonds to increase market liquidity, and promote growth and intermediation of local insurance and pension funds

- **Second-tier intermediation** through granting loans to intermediaries (NGOs and federations of SMEs) with the job of allotting funds to members can also help cut administration costs. Solidarity between banks, especially setting up inter-bank financing to pool money to be invested in SMEs, reduces the extra risk of lending to SMEs, as well. Working with banks boosts the financial viability of micro-credit institutions and can also help informal financial bodies to move towards the formal sector.

- **Expanding the supply of finance through the non-financial private sector** is also an option for fisheries and aquaculture SMEs. Apart from remittances by nationals working abroad, which are a key boost to private-sector growth, the interdependence between SMEs, large firms and sectoral "clusters" is a major potential source of finance, as shown in Asia and Latin America. Big firms can do a lot to help SMEs get finance more easily by transferring resources (money and factors of production) and guaranteeing SME solvency with financial institutions.

Links with major companies can also help SMEs get export credits, which are especially important in countries with weak institutions, since commercial partners are better informed than other creditors (especially financial institutions) about the ability of their customers to repay debts. Clusters of SMEs, which are very active in Asia, enable member firms to seek finance together, provide collective guarantees or even set up their own financial body. The threat of expulsion from the cluster ensures that promises are kept, which allows the network to overcome shortcomings in the legal system.

Removing the obstacles to access for SMEs to finance requires that commercial banks, micro-credit institutions, community groups and Business Development Services (BDS) work closely together. Pushing for agreements between financial bodies and BDS suppliers will help make up for lack of capacity and reduce costs by more efficient division of labour. The BDS supplier makes the initial choice of projects on a purely technical basis and the credit institution looks at financial viability.

Policy Recommendations

The policy recommendations address actions that can be taken at political level to facilitate SME access to a wider range of financial instruments as detailed in the previous section.

1. It is recommended that strategies be developed to improve the financial services that are offered to SMEs in the fisheries and aquaculture value chains. These strategies should be developed at national and regional level in partnership with the private sector and the financial services sector.

2. In developing these strategies, it is recommended that similar operations from other value chains and other systems be critically reviewed.

3. It is recommended that as a result of the above, specific actions, aimed at improving the enabling environment for

financial services be included in the Comprehensive Africa Agriculture Development Programme (CAADP) Country Compact Investment Plans.

4. Quantify the benefit of the fisheries and aquaculture sectors in Africa.

Conclusions and Implications

Creating a more effective financial services sector, servicing the fisheries and aquaculture value chains, will make this value chain more efficient and deliver greater benefit to those involved. This is demonstrated by experiences in other sectors such as agriculture. The introduction of commodity exchanges, for example, has delivered considerable value to both producers and consumers.

With regard to quantifying this benefit, the fisheries and aquaculture sectors in Africa currently produce approximately ten million tons with a value of four billion USD per year.

An improved financial services sector, operating in an optimal enabling environment will impact on:

- Efficiency, by empowering private sector players in the value chain to work more efficiently;
- Value, by enabling investment in technology that will give access to high value markets
- Growth, by enabling investment in productive capacity; and
- Profitability, through a combination of the above.

Given the base case of ten million tons at four thousand USD per ton, a 10% increase in production and efficiency will generate an incremental four billion USD of product, contributing 400 million USD in surplus income.

In this context it is noted that the CAADP target is 6% growth per annum – 33% over a five year period.

While growth is possible in the absence of effective financial services, it is probable in an environment where they are provided.

Edited by: Dr Hamady Diop, Dr Sloans Chimatiro, Dr Simplice Nouala, Dr Mohamed Seisay, Abiola Shomang

Compiled by: Amadou Tall (PAF Trade Working Group)

Assisted by: Martin Purves (Marine Stewardship Council), Helga Josupeit (FAO), Yvette Diei-Ouadi (FAO) and Jogeir Toppe (FAO)

2016, Policy Brief #9

ISBN: 978-0-9946933-3-4

Policy Brief 9: NEPAD Planning and Coordinating Agency, African Union Interafrican Bureau for Animal Resources 2016, *The Pan-African Fisheries and Aquaculture Policy Framework and Reform Strategy: Private Sector Investments and Financing Mechanisms for Fisheries and Aquaculture in Africa*, NPCA, AU-IBAR, Midrand, South Africa.

NEPAD Agency: 230 15th Road, Randjespark, Midrand, South Africa

www.nepad.org. Twitter: @NEPAD_Agency Facebook: www.facebook.com/nepad.page

This policy brief was supported through funding from the Swedish International Development Cooperation Agency (SIDA) through the NEPAD FAO Fisheries Programme (NFFP) and European Union through the Fishery Governance Project (FishGov).

NEPAD
TRANSFORMING AFRICA

AFRICAN UNION
INTERAFRICAN BUREAU
FOR ANIMAL RESOURCES