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Balancing risk and striving for impact – Providing finance to SMEs in developing countries

The CFC's mission is to develop commodity value chains and contribute to broader development objectives. The Fund has proven throughout its existence to be a leader in its market driven approach.

The demand for financial support for Small and Medium Enterprises (SMEs) in the commodity sector seen by the CFC in its Open Call for proposals is overwhelming. To maximize the effective use of its resources, from 2013 the CFC has begun expanding the proportion of loan financing in its portfolio of projects and is facing new challenges and opportunities. Balancing different types of risks to ensure CFC's impact, sustainability and relevance is part and parcel of the new operating modalities of the Fund. This article discusses how different types of risk may affect projects implemented by SMEs in the commodity sector.

The private sector is widely recognised as an important partner in development efforts. In particular, studies emphasise the importance of small and medium enterprises (SMEs) as key drivers of economic growth, diversification and employment creation[1,2]. SMEs play an important role in the formalizing of an economy through value chain development, often transacting with large corporations as well as linking with micro-entrepreneurs and small-scale producers. SMEs are active at various points in the value chain as producers, suppliers, distributors, retailers, and service providers[3].

In high-income countries' economies SMEs typically account for over half of all income and added value, yet in developing countries their capacity to spur growth and foster job creation

[1] World Bank (2013). Evaluation of the World Bank Group's Targeted Support for Small and Medium Enterprises. Available from http://ieg.worldbank.org/Data/reports/ap_evaluationof_smes.pdf
[2] IFC. (2013). Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises. World Bank Group.
[3] IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

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is constrained by their ability to access finance[4,5]. Overcoming obstacles to increase the economic role of SMEs in developing countries is regarded as an essential instrument of economic development. This acknowledgement has elevated SME finance to one of the key issues on the global development agenda[6]. SMEs in the commodity sector are well positioned to drive Africa's expected return to pre-crisis growth rates of around 5% by 2016, with agriculture cited as one of the driving factors[7].

SMEs are vital to the agricultural commodity sector as it is a major feature of developing country economies and central to food security. For the 70 percent of the world's poor who live in rural areas, agriculture is the main source of income and employment[8]. The two biggest challenges relating to SMEs in the agricultural commodity sector are commodity price volatility and climate change[9]. Climate factors (such as crop failure due to irregular and erratic weather conditions or pest and disease outbreaks) are believed to have a larger effect on economic capital than commodity price volatility[10].

Developing country governments around the world now recognize the importance of the SME sector for long-term growth and have worked to improve their investment climate and conditions for undertaking business by addressing legal and regulatory barriers and building credit infrastructure[11]. It may be noted that, compared with grants, loan based financing instruments directly targeting SMEs greatly reduce the scope for rent-seeking and other market distortions.

The development of new financing instruments suited to the needs of SMEs go hand in hand with a new dimension of risks which development financiers face. The balance of impact and financial sustainability of projects is closely linked to the financial parameters of returnable forms of financing such as loans.

The 'missing middle' and the importance of finance for SMEs

SME finance is referred to as the 'missing middle', as SME financial requirements are too large for most microfinance institutions, yet are viewed as too small, risky, or costly by traditional commercial banks[15,16]. SMEs seek loans or equity investments of considerable size – perhaps from $100,000 to $1,500,000[17] – at competitive commercial rates. These 'missing middle' SMEs are not sufficiently served by existing financing institutions, yet they are a key driver of development.

Maximizing impact of CFC's resources through financing for SMEs

The Fund's emphasis on loans is consistent with a more general trend towards greater development collaboration with the private sector. In recent years, an increasing proportion of official development assistance (ODA) has been given in the form of loans rather than grants[12]. The OECD notes that while most ODA continues to be provided as grants, loans and blended finance will play a key role in mobilising resources in support of the post-2015 Sustainable Development Goals (SDGs)[13].

The Fund concentrates its resources on SMEs so that they can realize the potential of commodity production, processing, manufacturing, and trade to make ensure that commodity markets can generate economic growth in developing countries for the benefit of the poor[14]. CFC has expanded its capacity to finance loans for a period of five to seven years, giving SMEs sufficient time to grow and repay the loan. The Fund's interest rates typically range between 5 to 10 percent depending on its risk assessment, which is extremely competitive compared with commercial banks.

4 IFC. (2013). Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises. World Bank Group.

5 Kushnir, M. et al. (2010). *Micro, Small, and Medium Enterprises Around the World: How Many Are There, and What Affects the Count?* IFC/World Bank.

6 For example, At their September 2009 meeting in Pittsburgh, the G-20 Leaders announced the creation of the Financial Inclusion Experts Group (FIEG), tasked with: (i) supporting innovative modes of financial service delivery capable of reaching the poor; and (ii) scaling up models of small and medium enterprise (SME) financing. In the constituent meeting of the SME Finance Sub-Group on December 3rd 2009, the G-20 FIEG members agreed to follow a development agenda on SME Finance, focusing on providing SME Finance solutions for developing countries in particular. See IFC. (2010). Scaling-Up SME Access to Financial Services in the Developing World

7 African Economic Outlook. (2015). African Economic Outlook 2015, Regional Development and Spatial Inclusion. Available at http://www.africaneconomicoutlook.org/fileadmin/uploads/aeo/2015/PDF_Chapters/Overview_AEO2015_EN-web.pdf

8 World Bank. (n.d.) *Agriculture & Rural Development, World Development Indicators.* Available at http://data.worldbank.org/topic/agriculture-and-rural-development

9 For shorter loans one can add the challenges of seasonality with long gestation periods. The result is that cash flows are highly seasonal and sometimes irregular, with earnings concentrated in certain times of the year. As such, there is a slow rotation of the invested capital as investments are spread over longer time horizons than for non-seasonal businesses. See IFC and GPFI. (2012) *Innovative Agricultural SME Finance Models.*

10 Castro, C., Garcia, K. (2014). *Default Risk in Agricultural Lending The Effects of Commodity Price Volatility and Climate.* Inter-American Development Bank (IDB), Discussion Paper No. IDB-DP-362

11 IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

12 ODA loans have risen faster than grants and now account for over a quarter of total ODA disbursements to developing countries. Gross ODA lending from DAC donors increased by 73%, whereas ODA grants from DAC donors (excluding debt relief) grew at a much slower pace, rising by just 25%. See Tew, R. (2015). ODA loans: tracking a growing source of development financing. Available from http://devinit.org/wp-content/uploads/2015/06/ODA-loans-tracking-a-growing-source-of-development-financing.pdf

13 OECD. (2014) Modernising Official Development Assistance (ODA). Concessional loans before and after the HLM . Available at http://www.oecd.org/dac/stats/documentupload/ODA%20Before%20and%20After.pdf

14 See http://common-fund.org/about-us/organisation-and-profile/

15 World Bank. (2006). *Making Finance work for Africa.* World Bank, Washington

16 IFC. (2009). The SME Banking Knowledge Guide. World Bank Group.

17 SMEs are defined in different ways by different actors. In this paper we use World Bank definitions (see table 1). For other definitions see Dalberg Global Development Advisors. (2011). *Report on Support to SMEs in Developing Countries Through Financial Intermediaries.* Geneva.

Table 1: World Bank definitions of MSMEs
(enterprise must meet at least 2 of 3 characteristics)

Firm size	Employees	Assets	Annual sales
Micro	< 10	< $ 100,000	< $ 100,000
Small	< 50	< $ 3 million	< $ 3 million
Medium	< 300	< $ 15 million	< $ 15 million
Firm size	**Loan size proxies**		
Micro	< $ 10,000		
Small	< $ 100,000		
Medium	< $ 1 million (< $ 2 million for some advanced countries)		

Source: IFC. (2009). The SME Banking Knowledge Guide

Finance is the biggest constraint to SME growth

Finance is often cited as the primary obstacle constraining SME growth and operations in developing counties, and has real consequences[18,19,20]. SME owners struggle to make the investments they need to increase productivity and the competitiveness of their business, develop new markets, and hire more people. Therefore, a lack of SME finance acts as a constraint on the economies of developing countries.

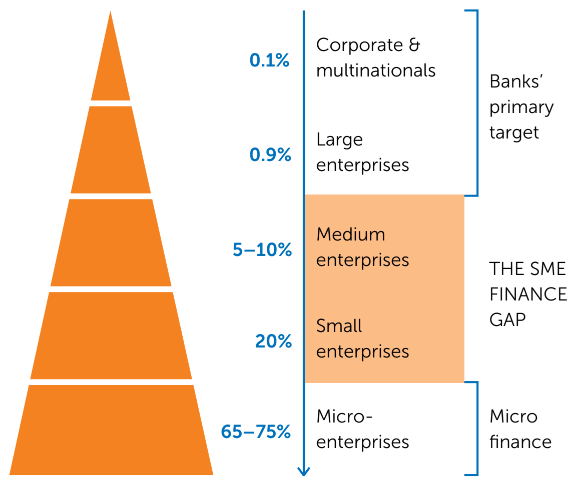
Identifying risks – Why SMEs lack access to finance

The enabling environment and weak financial infrastructure

The most important issue constraining bank lending to SMEs results from deficiencies in the enabling environment for financial services[21]. Developing countries tend to have comparatively weak financial infrastructure (accounting and auditing standards, credit reporting systems, and collateral and insolvency regimes), and weak legal and regulatory frameworks. Studies have shown that loan defaults are a major factor inhibiting bank lending to SMEs when the quality of regulation is poor[22].

In Africa, for example, credit registries are either completely absent or are in their infancy, so screening loan applicants is extremely challenging for commercial banks. The absence of systematic credit history records implies that default does not have any serious impact on credit ratings. Combined with weak contract enforcement, the cost of default to borrowers is relatively low, creating a 'moral hazard' problem in the form of strategic loan defaults[23]. This is an example of how 'information asymmetries' create risks - business owners have privileged information about the enterprise and it is difficult and expensive for financial institutions to access in order to gauge the creditworthiness of SMEs[24]. Another issue related to information asymmetries is that financial institutions find it difficult to differentiate between risky and non-risky projects. This creates an 'adverse selection' problem leading banks to make excessively conservative risk estimates and apply high interest rates to SMEs across the board.

Figure 1: Typical business landscape in emerging economies (percentages represent the number of companies)



Source: IFC. (2009). The SME Banking Knowledge Guide

[18] Unfortunately, the problem of credit is not the only challenge. There are significant nonfinancial barriers that also constrain SME growth: infrastructure-related (for example, lack of electricity), regulatory, tax-structure-related, and corruption-related. See: Stein, P. (2010). *Two trillion and counting - Assessing the credit gap for micro, small, and medium-size enterprises in the developing world.* IFC. In Africa, other factors cited include small local markets, undeveloped regional integration and very difficult business conditions, (including cumbersome official procedures), poor infrastructure, dubious legal systems, inadequate financial systems and unattractive tax regimes. See: Andrianova, S., et al. (2011). *Why Do African Banks Lend so Little?* University of Leicester, Department of Economics

[19] Meghana, A., et al. (2011). *Small vs. Young Firms Across the World: Contribution to Employment, Job Creation, and Growth.* Policy Research Working Paper 5631. World Bank, Washington, DC.

[20] In global surveys, including the World Bank's Enterprise Surveys and Investment Climate Assessments, SMEs report that the cost of finance is their greatest obstacle to growth and rank access to finance as another key obstacle, and this is most acute in developing countries. IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

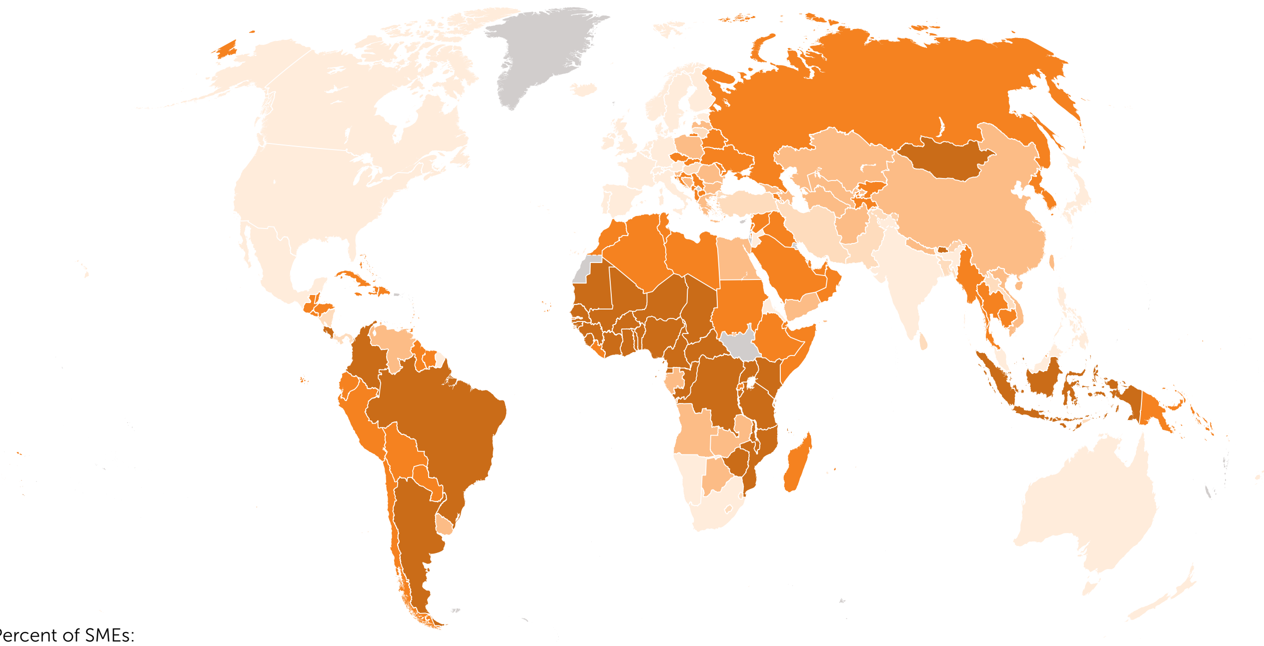
[21] IFC. (2010). Scaling-Up SME Access to Financial Services in the Developing World

[22] However, once a threshold level of regulatory quality (guaranteeing contract enforcement) has been reached, improvements in the default rate or regulatory quality do not matter. See: Andrianova, S., et al. (2011).*Why Do African Banks Lend so Little?* University of Leicester, Department of Economics.

[23] Andrianova, S., et al. (2011).*Why Do African Banks Lend so Little?* University of Leicester, Department of Economics

[24] In Kenya, Tanzania, Uganda and Zambia, a large majority of banks (88 percent) consider the lack of adequate information the most important deterrent to their involvement with the SME segment. See: Calice et al. (2012). *Bank Financing to Small and Medium Enterprises in East Africa: Findings of a Survey in Kenya, Tanzania, Uganda and Zambia.* African Development Bank Group

Figure 2: Credit gap in the SME sector: Unserved and underserved (percent)



Source: IFC. (2013). Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises

Bank capacity for due diligence, monitoring and management

SMEs are heterogeneous and tend to have complex needs. They also operate in different ways than large enterprises and may be less sophisticated financially, lacking in business planning and cash flow management expertise[25]. This means that financial institutions need to have the resources and capacity to carry out sufficient due diligence as well as ongoing monitoring and management of their SME portfolio. This may not be optimal from a cost perspective, especially when compared with large corporations which have established credit histories and require relatively less effort[26,27].

Response to risk by financial institutions

Banks typically offset the risks of lending to SMEs in two ways: by insisting on and applying greater collateral requirements and demanding and charging higher interest rates. Unfortunately, stringent collateral requirements are a primary barrier to SMEs ability to access finance[28]. This is particularly an issue for SMEs in Africa where the type of collateral required by many banks is land title. This can be an issue in African countries where there are lower rates of property ownership and lack of appropriate titling[29].

SMEs also take issue with high interest rates asked by banks. Interest rates on SME clients in Africa are 5-6 percentage points higher than elsewhere in the developing world. Banks in Africa charge on average close to 15.6% for loans to their best small firm borrowers, compared with 11% in other developing countries[30]. Whilst there is an argument that banks may overestimate the riskiness of the SME market, in many cases the pricing of loans by banks appears rational given expected inflation and high historical default rates[31].

[25] IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

[26] IFC. (2013). *Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises.* World Bank Group.

[27] Hansen et al. (2012). *Assessing Credit Guarantee Schemes for SME Finance in Africa Evidence from Ghana, Kenya, South Africa and Tanzania.* Agence Française de Développement Working paper

[28] While some banks offer unsecured loans to SMEs, based on cash flow rather than collateral, these loans often come with shorter maturities; in general, collateral requirements have been the norm. IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

[29] One study by Hansen et al (2012) of SME borrowing in Ghana, Kenya, Tanzania and South Africa found that average collateral levels ranged from 106%-120% for small firms, and 101%-130% for medium-sized firms. However, note that collateral requirements in Germany are 124% for small firms and 130% for medium sized firms, yet access to finance is not considered a major barrier to SMEs there. The authors suggest that it is not the level of collateral required that appears to be the problem for the African countries, but the inflexibility of capital requirements and difficulty in obtaining collateral that particularly affect SMEs. See: Hansen et al. (2012). Assessing Credit Guarantee Schemes for SME Finance in Africa Evidence from Ghana, Kenya, South Africa and Tanzania. Agence Française de Développement Working paper

[30] Peria, M. (2009). *Bank financing to SMEs: what are Africa's specificities?* Private Sector & Development, Proparco's Magazine, Issue 1, SME Financing in Sub-Saharan Africa

[31] Hansen et al. (2012). *Assessing Credit Guarantee Schemes for SME Finance in Africa Evidence from Ghana, Kenya, South Africa and Tanzania.* Agence Française de Développement Working paper

SME banking in developing countries is changing

Nevertheless, SME banking is an industry in transition and the missing middle is slowly shrinking. SME banking appears to be growing the fastest in emerging markets where more banks are creating SME units and developing tailored approaches to come to terms with the particular needs and preferences of SMEs and the historical challenges of high credit risk and cost to serve[32]. Banks consider that the SME lending market is large, not saturated and with a positive outlook[33].

However, it is important to note that banks favour some forms of financing to SMEs over others. Banks may provide overdraft facilities or short-term working capital but hesitate to offer loans with longer maturities that SMEs need for infrastructure investments and growth[34].

In the medium to long term, the recipe to close the SME credit gap is for governments in developing countries to enact further regulatory reform to support the enabling environment and strengthen financial infrastructure[35]. Key elements include securing creditors' rights by allowing out-of-court enforcement of security rights and protecting secured creditors during insolvency processes. The annual Doing Business reports published by the World Bank Group[36] highlight elements of a legal and regulatory framework that encourages lending by financial institutions to the private sector.

Default rates among SMEs in developing countries

Reliable data on rates of default (i.e. non-performing loans) among SMEs in developing countries are also difficult to come by in the literature[37]. One large study from 2007-08 with 91 banks in 45 countries found the average share of non-performing loans to total loans for SMEs to be 6.5 percent in developing countries compared with 4.1% for large firm loans[38]. However, averages conceal the reality across regions. The share of non-performing loans among SMEs in Africa was found to average 14.5%, compared with 5.5% among developing countries outside of Africa[39]. Another study by IFC puts the share of non-performing loans in Sub-Saharan Africa at 11% for small enterprises and 9% for medium enterprises[40].

Gluing veneer sheets at a mill in Cianjur, Java

Photo: Roger Bymolt

[32] IFC. (2009). *The SME Banking Knowledge Guide.* World Bank Group.

[33] Calice et al. (2012) *Bank Financing to Small and Medium Enterprises in East Africa: Findings of a Survey in Kenya, Tanzania, Uganda and Zambia.* African Development Bank Group

[34] Hansen et al. (2012). *Assessing Credit Guarantee Schemes for SME Finance in Africa Evidence from Ghana, Kenya, South Africa and Tanzania.* Agence Française de Développement Working paper

[35] IFC. (2013). *Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises.* World Bank Group.

[36] World Bank. (2015). *Doing Business 2015, Going Beyond Efficiency.* Available at http://www.doingbusiness.org/reports/global-reports/doing-business-2015

[37] Definitions of what constitutes a non-performing loan can also differ between banks, although most banks classify this as missed loan repayment 90 days after the due date.

[38] Among banks operating in developed countries, the average share of non-performing loans is 6.93% for SME loans and 2.54% for large firm loans. See: Beck et al. (2008). *Banking SMEs around the world: Lending practices, business models, drivers and obstacles.* World Bank.

[39] Peria, M. (2009). *Bank financing to SMEs: what are Africa's specificities?* Private Sector & Development, Proparco's Magazine, Issue 1, SME Financing in Sub-Saharan Africa

[40] IFC. (2013). *Financing to Micro, Small, and Medium Enterprises in Sub-Saharan Africa.*

Unfortunately for development financiers, there is a dearth of available data specifically on default rates for *long-term loans to SMEs in the agricultural commodity sector in developing countries.* Given the additional risks and challenges of commodity price volatility and climate factors, it is probably safe to assume that average default rates associated with this profile of SME are higher still.

What the CFC can do

The CFC is an innovator. While there are some positive trends in terms of SME finance in developing countries generally, there are two specific areas of SME financing where others fear to tread: longer term loan provision and the agricultural commodity sector. This is precisely where CFC demonstrates its added value.

CFC deals with longer-term loans as they are vital for core infrastructural and other growth investments. However, they have a longer repayment horizon than commercial banks are willing to consider and thus carry an extended period of risk.

The literature on risk management specifically for long-term lending to SMEs in the agricultural commodity sector lending is scarce. However, as the IFC notes, the challenges of lending to SMEs in agriculture are not insurmountable for institutions that rely on innovative and targeted approaches[41]. This is what CFC does best. The Fund seeks to understand the challenges and implements strategies which mitigate the risks while achieving impact in agricultural commodity chains and help drive socio-economic development.

The Fund particularly targets those SMEs working in production and quality improvements, processing and value addition, technology transfer, product differentiation, and marketing. The Fund looks favourably on those SMEs which are able to take prudent measures to minimise risk whilst striving for growth in a difficult sector. The main criterion for selection of SMEs for support are quality, potential impact, beneficiary focus, replicability, sustainability, cost effectiveness, manageability and dissemination[42].

Devising a risk management strategy

A model risk-management strategy needs to cover four main components: due diligence, credit management, collateral management and portfolio diversification. The underlying premise is that the financier can continuously adapt its mitigation strategy based on insights it gains from practice. It is well understood that the scope of innovative and development impact oriented financing for SMEs in the commodity sector is far from that of commercial banks and mainstream funds who can apply proven predictive models to their lending with a good degree of confidence. The commodities sector is more heterogeneous, fluid and less predictable. This necessitates adaptive learning alongside the use of formal risk modelling approaches.

Due diligence

Due diligence involves a thorough analysis of the risks relating to a proposed loan agreement and is carried out on all of its potential investments. Many financial institutes, both local, national and even international, suffer from a lack of technical knowledge and experience in the agricultural sector in emerging economies. Any institution implementing a risk management strategy in this sector needs to possess or have access to knowledge on all aspects of production and trade of agricultural commodities. The critical issues one needs to look at during the due diligence process includes the company's financial position and reporting, its management and ownership structures, its profitability, issues related to processing (such as technology, volume and electricity supply), legal and compliance issues related to the company's operation, and its collateral arrangements and value (Table 2).

[41] IFC and GPFI. (2012) *Innovative Agricultural SME Finance Models*
[42] See http://common-fund.org/about-us/organisation-and-profile/

Table 2: Summary of due diligence issues

Critical issues	Description
Finance	• Financial position (solvency, liquidity and profitability and off-balance liabilities) • Financial Reporting (debt service capacity, later stage investment and finance, solvency position and the underlying commercial assumptions)
Management, governance and ownership	• Managing director (entrepreneurial / managerial skills and reputation, financial engagement) • Management team, the board, ownership
Profitability	• Sales side • Supply side (small-holder and plantation set-up)
Processing	• Technology • Volume • Power supply
Legal issues and compliance	• Registration and compliance with laws and regulations • Reputation of managing director and beneficial owners • Loan and security arrangements
Assessment of collateral	• Existing collateral arrangements and collateral value

CFC in agricultural value chains

The CFC has more than 25 years of experience in commodity sector development. CFC is also supported by a technical advisory committee, consisting of renowned independent commodity experts with long experience in developing countries who understand the local context of any relevant SME. The committee reviews project proposals on both financial and technical aspects.

Credit risk management

Credit risk management is a particular challenge for a commodity-based development fund dealing with SMEs operating in volatile markets. Proper identification of credit risk is mainly done through the due diligence process (described above). However, quantifying risk is often hampered by a lack of reliable and up-to-date data. Considerable effort is required to collect information from public and proprietary databases and from partners and clients, in order to make decisions based on the best data available, however imperfect.

Credit risk management requires the financier to link its tolerance of defaults with the average rate of return and the availability of collateral. There is a fine line to tread when a development financier considers the interest rate to charge to an SME: if interest rates are too high then the SME would not be able take the loan, and may look for other stop-gap financing solutions elsewhere. This is a lose-lose situation because the SME will likely struggle to find better long term financing elsewhere and the development financier would miss an opportunity to contribute to its mission of achieving development impact.

Collateral management

Collateral management is preferred over charging higher interest rates because it does not risk undermining the project's financial viability and development impact. However, an SME may lack the level of collateral desired by the financier to secure the loan, particularly in the case of a start-up enterprise. When collateral is secured, it is strongly preferred not to have to execute this option in the case of a non-performing loan, but rather to explore all other solutions of restructuring or recuperation of funds, albeit from a strong negotiation position. The reasons are clear – there are costs involved in such execution and legal procedures can become complicated and drawn out. Moreover, seizing assets of an SME would likely threaten the ongoing operations of the company as well as threaten the upstream stakeholders in the value chain.

Collateral also plays a more subtle role in the relationship between the financier and an SME. It confirms a commitment from the borrower, requiring them to 'put some skin in the game' and provides a way to exert pressure if need be, although the latter should be taken with a great degree of responsibility so as not to undermine the development goals of the project.

Table 3 is illustrative of what constitutes an acceptable default rate, based on the collateral ratio versus the portfolio margin. For example, the table shows that if the collateral ratio of the portfolio is 50% and the portfolio margin is 6%, then the financier could tolerate a default rate up to 12% across its portfolio. The development financier's main concern is to cover risks, rather than to profit from returns on investment.

Table 3 Default rate tolerance (%) based on collateral ratio and portfolio margins

	Collateral ratio						
Portfolio margin	25%	35%	50%	55%	60%	65%	70%
5%	7%	8%	10%	11%	13%	14%	17%
6%	8%	9%	12%	13%	15%	17%	20%
7%	9%	11%	14%	16%	18%	20%	23%
7.5%	10%	12%	15%	17%	19%	21%	25%
8%	11%	12%	16%	18%	20%	23%	27%
9%	12%	14%	18%	20%	23%	26%	30%
10%	13%	15%	20%	22%	25%	29%	33%

Portfolio management

A portfolio management strategy should, in principle, aim to achieve a well-balanced, diversified loan portfolio while minimizing risk. This implies soft limits on loans to specific SME profiles in each sub-sector, and a spread across the countries and regions included in the portfolio. This reduces overall risk to the financier in the case of a price crash in a given commodity or an economic crisis in a country.

Staying true to the aim of development impact

A development financier is required to take a prudent position on risk. It can, however, take a degree of risk in the expectation of development impact, whilst avoiding taking an overly risk adverse position at the expense of achieving its core vision. A development financier failing to see risks as opportunities for development innovation would find itself in territory already occupied by conventional lenders, leaving the 'missing middle' of high potential SMEs under-served in the commodity sector. Agricultural commodity value chains offer great opportunities for such risk taking in the interest of development, although careful assessment of risks in this sector still requires much work on the details within the general principles identified above.

It is essential that SMEs gain access to longer-term loans, but the implementation of workable modalities to provide such support for SMEs entails new challenges. As this paper clearly illustrates, there is a degree of uncertainty that one must manage to achieve sufficient returns to compensate for inevitable defaults. Rather than take an 'ostrich policy', a constructive and practical approach should be based on the principles of transparency about risk so that the entire sector may benefit from adaptive learning and experiences in the years ahead.

With proactive management and a strong learning philosophy, financial innovation in agricultural value chains can be a winning strategy, benefiting development financiers, SMEs and commodity dependent developing countries.

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Farming red tilapia on the Mekong Delta, Vietnam

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