AGRA Sustainably Growing Africa's Food Systems

Financing African seed companies

What we are learning?

In this paper, AGRA shows that for seed companies to access finance, support needs to be based on performance and stage of development, be market oriented and blended in nature.

These 3 elements ensure sustainable growth of the African seed sector contributing to a food systems transformation that can feed the continent's growing population.

THREE INSIGHTS:

***Performance based, market oriented** and **blended support** give the best results.*

AGRA has invested USD 26.8 million in financial and technical support to 147 African seed companies since its establishment in 2006. These and other seed companies operating on the continent, are responsible to provide African farmers with climate resilient seed of nutrition dense crops in a competitive manner so that Africa becomes food and nutrition secure, and the SDG 2 ('Zero Hunger') becomes a reality. The goal is to build a commercially viable market for seeds in Africa through the creation of African seed companies to:

- Increase the uptake of improved seed by farmers which currently stands at 40%
- Reduce the seed supply and demand gap left by the public seed companies
- Diversify the availability of certified seed of improved varieties
- Give farmers access to more options of appropriate varieties
- Reduce the price of certified seeds compared to multinational brands

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This paper compiles the lessons learned and provides recommendations on how seed companies can be best supported to enhance their access to finance. Seed companies are important change agents for AGRA because seeds are the main trigger point in a food system based agricultural transformation. Significant crop yields are possible, thanks to improved genetics in planting materials, combined with plant nutrients (from healthy soils) and good agronomic practices adopted by farmers.

AGRA's 15+ years of support to seed companies through technical and financial assistance programs yielded three main insights as follows.

INSIGHT 1:

Seed company support should be based on performance[1] and evolve accordingly.

There are roughly 3 different types of African seed companies with different business models:

- Seed companies that exclusively produce certified seed of public varieties
- Seed companies that have grown to between 1,000-5,000MT of seed per year, have their own maintenance programs and exclusively proprietary public varieties.
- Regional and Multinational companies with own breeding programs.

AGRA's support focused mostly on the first category of companies given that these had limitations to do their own research and development, lacked personnel and experience in seed business. They therefore required a lot of handholding in terms of technical assistance to perfect the art in areas of production, quality assurance, processing, and marketing.

Public research institutions had many varieties of various crops (cereals, legumes, and vegetatively propagated crops) on the shelves and at the same time AGRA was investing in breeding. It was therefore necessary to have these varieties multiplied and made available to farmers. The various evaluations conducted on AGRA's seed company support program[2] concluded that:

AGRA helped African SME seed companies professionalize and expand operations, thus increasing the supply of (certified) improved seed in focus countries. However, providing the requisite technical assistance to mentor and wean SME seed companies out of grant funding, through concessional investment and ultimately into commercial funding has been challenging for all interested parties.

All evaluators found it difficult to assess the financial viability of seed companies because data was lacking on financial performance, sales data, cost data, which are needed to support any loan request. The implicit recommendations were for AGRA to start measuring performance of seed companies also from a financial viability perspective because business management and governance was found to be the weakest link in the performance of most seed companies.

Nurturing SMEs to adopt a culture to work towards a financially sustainable business model and thus the ability to achieve impact at scale requires AGRA to have in place a strong segmentation and selection process at the outset while monitoring performance and progress of seed companies during project implementation.

[1] Performance metrics should be gradually developed over time, taking into account the sector and organizational maturity.
[2] PASS-SEPA (2007-2018), SSTP (2013-2018), FAPA (2015-2017), PIATA (2017-2021) are among the most important programs.

The recommendations to make the Business Development Support more effective were, for AGRA to:

1. **Adopt a standardized assessment tool (a slightly adapted version of SEI or SCOPEinsight[3] tool)** to facilitate the measurement of seed company performance and improvement thereof. The assessment would also be a check to establish whether seed companies are willing to disclose financials and become formalized.
2. **Prioritize strengthening the governance and business management practices** of seed companies, as this has been identified as a critical factor in their long-term success. This includes providing technical assistance and training in areas such as financial management, strategic planning, and governance structures, to ensure that seed companies have the necessary skills and systems in place to operate sustainably beyond grant funding and to be better equipped to attract investment and expand their operations across value chains and geographically.
3. **Encourage seed companies to adopt best practices in transparency and accountability,** including regular reporting on financial performance and adherence to environmental and social standards.

AGRA's Centre of Excellence for Seed Systems in Africa (**CESSA**) will support the Africa wide adoption of such assessment tools and BDS approaches to make sure grant funding for capacity building helps seed companies to become more bankable and investable.

INSIGHT 2:

Markets for seed mostly depend on farmers' access to end markets for their produce

The most viable business case for seed companies is to produce and sell hybrid maize seed which is generally good because Africa has a high per capita consumption of maize, markets are relatively well developed, and hybrid seeds need to be bought every season since recycling will lead to inferior performance.

The business case for *(less productive and less input demanding)* Open Pollinated Varieties (OPV) is less obvious because the seeds can be recycled and only need replacement every 3 to 4 seasons due to reduced yield potential, disease resistance and quality loss.

Demand for seeds such as rice, sorghum, legumes, potatoes, and cassava mainly depends on the existence and requirements of the end market. Farmers need access to better paying and reliable end markets that can justify their investment in improved seeds and planting material. Presently, only a small percentage of African farmers (<20%) buys seeds, due to a lack of access to attractive markets.

Seed companies need to know what the demand from end markets is to plan their production. In many countries, the seed markets are unpredictable and dominated by Governments *(through input subsidy programs)* and NGO's *(through social safety nets and relief programs)* as opposed to market actors like agrodealers and food processing companies. Establishing links between off takers, agrodealers, farmers and seed companies are essential to improve the planning capacity, including working capital requirements for seed companies.

CESSA will support the creation of data driven National Seed Planning and Coordination Committees (SPCC) in each focus country. This will help seed companies to better plan their production cycles and deployment of working capital.

[3] www.scopeinsight.com

INSIGHT 3:

Seed companies have specific risks which justify blended finance instruments.

Seed companies face challenges that are specific to them, and which make financing of their businesses more difficult and less commercially feasible than financing of other agricultural companies like input dealers and processors. These issues include but are not limited to:

Long working capital cycles (from purchase of early generation seed to being paid by a client of certified seeds can easily take 2 years)

Lack of business case for production of seeds obtained through open pollination ("low profitability crops").

These seeds can easily be recycled without losing yields for a couple of seasons.

Lack of ownership of varieties. A seed company that owns a variety can invest in demand creation and know that it will make money from enhanced demand.

Most African seed companies rely on publicly owned varieties where competitors can produce the same variety. Investments in marketing and branding are then unprofitable.

Lack of long-term affordable capital for seed business investments like irrigation, seed processing (grading, sorting, dressing) equipment and storage facilities.

Market related issues as described under Insight#2 (unpredictable and unreliable markets)

These challenges justify the deployment of blended finance instruments which reduce the cost and risk of seed company financing.

From AGRA's investments in two dedicated blended equity funds and one challenge fund, we learned that the financial returns for the funds were negative, but the concessional investments were catalytic and helped seed companies to access other, more commercial debt funding.

Opportunities for blended finance are:

1. Lack of quality of company management and governance issues to execute (sometimes poorly developed, overambitious) business plans.
2. External challenges, such as delayed payments by Government and currency depreciation.
3. Overcapitalization, while the seed sector grows gradually requiring small incremental funding.
4. High risks of scaling up new product lines, like hybrid rice seed and banana plantlets.

SOLUTIONS:

To address these issues, CESSA recommends that funding instruments for seed companies include:

A Conducting performance assessments that inform the stage of development, bankability, debt servicing and management capacity of the seed companies.

B De-risking for currency risks (local currency hedging) and Government default (invoice discounting for public sector bills)

C Supporting business development services based on gaps identified in the assessments including deployment of automated financial management tools and marketing strategies to diversify and develop complementary business lines.

D Leveraging of existing schemes and matching grant facilities for CAPEX financing. For example, asset backed loans or export guarantee schemes from countries of origin of the capital goods.

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