CASE STUDY 2 | Coffee Farmer Resilience Initiative in Latin America

Long-term loans for renovation are provided by a blended finance facility to farmer organizations in Latin America

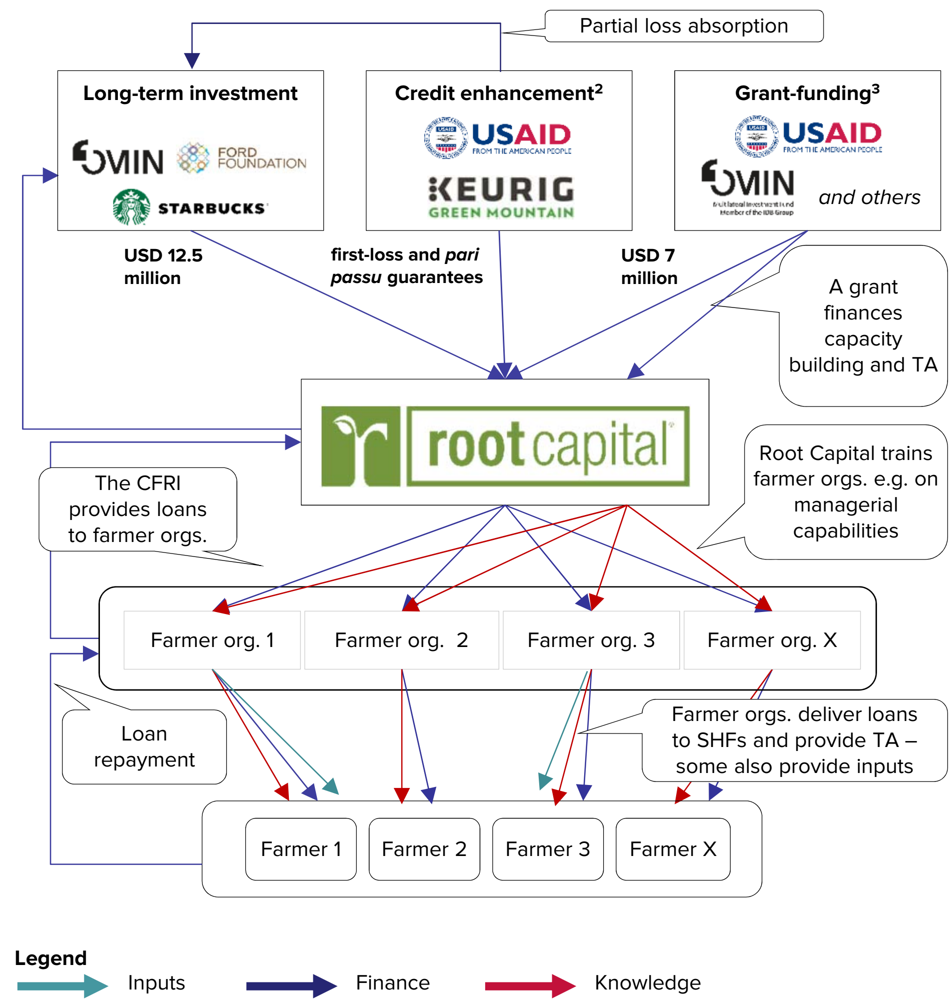
Coffee Farmer Resilience Initiative – *Root Capital*

R&R type	Loan-based renovation
Countries	Honduras, Nicaragua, Peru
Cost	USD 7.7 million in loans approved
Dates	2014 - 2016
Project context	• In 2011/12, *La Roya* affected almost 50% of the total coffee growing areas in Latin America, significantly reducing the SHF production. • *La Roya* outbreak revealed decades of underinvestment in the coffee sector. Over 60% of trees in the region had passed the productivity peak and were more exposed to the disease.
Objectives, activities, and results	• Root Capital provided loans to SHF orgs who then distribute to SHFs to support the upfront cost of R&R. Root Capital also provided technical assistance (free to SHF orgs.) and challenge grants (with cost-share from orgs) to build org. capacity to implement R&R programs. • USD 7.7M in loans were approved to 8 orgs. in Honduras, Nicaragua, and Peru.[1] • Value creation: increased yields and strengthened SHF capacity • Value capture: farmer groups selling higher volumes of coffee

Loan details

Borrowers	Farmer aggregations (e.g. coops)
Currency	USD
Tenor	3-7 years
Grace period	1-3 years
Interest rate	7-10.5 APR

Figure 1: Financial structure of the project and finance delivery to SHFs



Notes: (1) TA and challenge grants were extended to an additional 25+ orgs in El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Peru. (2) Keurig Green Mountain provided a first-loss guarantee of USD 400,000 (~3% of target credit disbursements). USAID provided a 50% *pari passu* guarantee of up to USD 15 million (i.e., USAID absorbs USD 0.50 of the loss for every dollar not repaid by eligible borrowers after the USD 400,000 in first-loss coverage has been used). (3) Specialty coffee roasters Cooperative Coffees, Equal Exchange, and Keurig Green Mountain channelled funding for technical assistance. Other donors (incl. the DOEN Foundation Open Road Alliance, the Multilateral Investment Fund of the IDB Group (FOMIN), the Skoll Foundation, and the Swedish Postcode Foundation, and USAID) provided grant funding to cover cost associated with program design, technical assistance, etc. Source: Root Capital, *Learning Report: The Coffee Farmer Resilience Initiative,* 2016.

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SUSTAINABLE COFFEE CHALLENGE · USAID FROM THE AMERICAN PEOPLE

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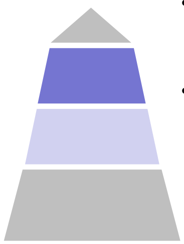
Project context

Coffee viability

- **Relevance**: SHFs in Latin America have potential for yield uplift by applying GAP and R&R (e.g. potential of 31% net income increase from yield improvements in Honduras, 64% in Nicaragua, and possible double of yields in Peru[1]).
- **Willingness:** Farmer public sector (or other farmer organizations) have an intimate understanding of the needs and production capacity of their members and can evaluate their willingness and credit worthiness.

Farmer segmentation



- **Country situation:** In the three countries, coffee producers are SHFs. Their degree of integration within value chains vary by country.
- **Program segmentation:** The program targets SHFs in tight value chains, mostly members of farmer orgs. such as coops or private coffee mills. Some farmers in loose value chains were also targeted via through savings and loan cooperatives where the coops were less strong.

R&R need

- **Country need:** Almost 900,000 ha would benefit from R&R in Nicaragua, Peru, Mexico and Honduras.
- **Program objectives:** Building the capacity of SHF orgs. and farmers to recover from the La Roya outbreak and build resilience for the future through R&R

Management of the three R&R components

Inputs

- **Providers:** Third parties
- **Challenges faced:** SHFs must have access to upfront and ongoing inputs. SHF orgs. must have the capacity to source and deliver appropriate inputs.
- **Solution:** Root Capital only selects SHF orgs. that are able to manage selection and application of adequate farm input. A Root Capital approved agronomist assists SHF orgs. with preparing their input delivery plan for SHFs.

Finance

- **Providers:** Various (cf. previous slide)
- **Challenges faced:** Understanding risk and bringing together funders with aligned risk appetites; protecting investors
- **Solution:**
  - Root Capital conducted intensive due diligence. Selected SHF orgs. must have adequate sources of internal financing to cover at least 20% of the R&R investment. Root Capital also assessed credit risk using in-house tools developed over 15+ years[2].
  - Using a blended finance structure to partially de-risk the investment[3].

Knowledge

- **Providers:** Root Capital
- **Challenges faced:** Most of the farmer groups lack the ability to manage R&R loans for SHFs.
- **Solution**: 35 trainers delivered financial advisory services to managers and accounting staff of Root Capital's potential or existing clients. Training focuses on managerial, organizational, technical capacities, with a focus on orgs' internal credit and technical assistance services

Lessons learned

- **Leveraging blended finance structures enables lenders to partially de-risk R&R investments:** Root Capital used a blended finance structure to align the incentives and risk appetites of the different funders. Mechanisms of partial loan guarantees, risk-sharing, reserves for first-loss capital, and technical assistance funds helped to mitigate risks. These types of blended finance structures should be reproduced to scale R&R financing.
- **Invest in capacity building for aggregation points:** Root Capital relies on farmer organizations to deliver and manage loans to SHFs. Many SHF orgs., however, currently lack the capacity to manage large R&R interventions. Strengthening SHF orgs. or other farmer aggregation points, like local microfinance institutions, is needed to scale R&R.

For more information, please contact: Elizabeth Teague (Root Capital), *eteague@rootcapital.org*

Notes: (1) Source: GCP and Technoserve, *Economic Viability of Coffee Farming,* 2017. (2) Root Capital assesses the credit risk of borrowers using an internal rating system that weighs various risk categories, including scale and buyer diversification, enterprise strength and growth potential, financial flexibility, and financial strategy. This data is combined with the experience and judgment of loan officers to inform a full assessment of credit risk. (3) The funding comes from public and private financers with different return expectations. Credit enhancements reduce the investment risk, and grant funding dedicated to capacity building reduces the client risk, ultimately reducing the investment risk. Source: Root Capital, *Learning Report: The Coffee Farmer Resilience Initiative,* 2016; Dalberg interviews