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For: approval

Evaluation of five BIO Investments in agriculture: Management response to the evaluation's conclusions and recommendations

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Our management contract with the Belgian State foresees that every year BIO commissions external case study evaluations of at least five of its investments. For the 2016 evaluation, it was decided to focus the evaluation on investments in agriculture in Africa (2 direct investments and 3 funds). The evaluation assessed both the financial and development performance of these investments, especially how the different investments have contributed to enhancing food security and rural development.

The following investments were evaluated:

	Country	Investee name	Sub-sector	Start date	End date	Contract amount	Direct/ Indirect	Type	BIO TA
1	Ghana	Niche	Cacao	2011/ 2015	Ongoing	4.3 M€	Company	Loan	Yes
2	Benin	CDPA	Eggs	2013	Ongoing	3.0 M€	Company	Loan	Yes
3	Tunisia & Morocco	Magreb Private Equity Fund III - Vitalait (Tunisia) - Cotugrain (Tunisia) - Sicopa (Morocco)	Dairy, Seed & vegetables (processing)	2011/ 2014	Ongoing (Vitalait exited)	8.0 M€	Fund	Equity	No
4	Madagas-car	Adenia Capital III - Socolait	Dairy	2012	Ongoing	5.0M€	Fund	Equity	Yes
5	Ghana	Rural Impulse Fund II - Sinapi	MFI	2010	2013	5.0 M€	Fund	Debt	No

Main findings

The primary objective of the study was to assess the contribution of BIO's investments to the optimisation of investing in agricultural activities.
The evaluators were requested to investigate and address:
(i) to what extent are the BIO investments directly or indirectly contributing to the optimisation of agricultural sector and
(ii) to what extent are the investments supporting improved food security and rural development.
A secondary objective was to assess the additionality of BIO financing, both financially as non-financially.

As the five case-studies cover different types of investment (direct/indirect, debt/equity) at different points in the agriculture value chain, no aggregated data could be provided. Rather, the evaluators of Enclude have tracked selected key performance indicators per investment and investee.
Overall, 'the evaluation of the five cases has demonstrated important development effects in the agriculture sectors' and the evaluators 'believe that in all cases the investments created critical factors leading to the observed changes'.

Following the DAC evaluation criteria[1], the evaluators conclude that;

- The five investments – which cover seven investees – were all considered as highly relevant with the intended effect following BIO's development goals in 'Food Security and Rural Development', 'Local Economic Growth' and 'Private Sector Innovation'.
- The investments were found efficient in time regarding approval, disbursement and implementation. The delays that were found related to changes in staff and due to lack of local presence of BIO.
- Effectiveness and sustainability were considered positive for all five investments. One investee of a Fund was considered not to have effectively achieved the development targets. This related to unfavourable market dynamics and poor management at the level of the investee. For another investee sustainability – in the sense of commercial viability – was not convincing as a close conjunction with a large donor programme was necessary to be able to serve its rural clients in the agriculture sector.

Regarding the evaluated 'additionality', i.e. the degree to which BIO's financing complements – or is "additional" to – commercially available financing, the evaluation concludes that all five cases were assessed to be additional or highly additional. Specifically;

- Financial additionality scores high for both direct and indirect investments. For two of the three indirect investments (Funds), BIO's additionality was considered lower assuming that other investors for the Funds might have been found however, the Funds themselves were all considered highly financially additional to its investees. In all indirect investments, BIO's value added to the fund was clearly the provision of long-term, mid-sized financing ultimately earmarked for SME's.
- Also non-financial additionality scores positive for both direct and indirect investments. This refers to enhancing business practices to increase sustainability or development effects through advisory services or Technical Assistance (TA). BIO's non-financial additionality for two indirect investments was considered lower, however again, the funds themselves were all considered highly additional.

The learning questions following the evaluation are case specific and have been organized under three themes; (i) impact potential; (ii) performance factors and; (iii) process optimization.

I. Impact potential;
   a. Assessment and due diligence processes: Unexpected events (Arab Spring and political crises). Even though the overall the acquisition process has been experienced in a positive manner, investment funds should ensure to hedge their exposures to reduce risks.
   b. Indirect investments through funds: For none of the cases, an in-depth assessment of the development potential at farmer level has been performed or a baseline established. A clear idea of the development potential can be helpful in decision making, setting targets and assist the move towards a more detailed screening of the potential development impact.

II. Performance factors
   a. Matching TA with investments: The content and relevance of the TA should suit the agriculture impact pathway of BIO. BIO's strategic goals on agriculture development should not only be integrated in the financial instruments (loans & equity) and their targets, but also in the TA grants, in order to optimize the investments' impact on the preferred development goals.

[1] The DAC Criteria for Evaluating Development Assistance are: Relevance, Effectiveness, Efficiency, Impact and Sustainability.

b. Think global, act local? The absence of local presence limits the spectrum of local SME's suitable for direct investments. It seems that one of the prevailing factor in deciding to invest in a local SME without local presence indeed is the track record of the management team – although of course in combination with many other factors.

III. Process optimization.

a. Early stage involvement:

i. Regarding direct investments: The absence of a structured acquisition approach as well as clear goal setting diffuses the value add for BIO: it could be useful to create a strong image which includes clear goal setting on the preferred type of SMEs and impact pathway in attracting an identifying suitable direct investment cases.

ii. Regarding indirect investments: The agricultural impact pathway has to be clear to BIO itself in order for them to be able to inherently integrate this in their investment decisions in investment in a certain type of fund with a related impact strategy on its own. If this is done properly, BIO's indirect investments –although still not selected by BIO itself- can be more spot-on as investees are selected by a fund-manager with matching investment goals to BIO's.

b. Communication and feedback: lack of systemized communication with the clients on development performance.

c. Measuring development impact: Following the five case studies, BIO has achieved important results that are currently not being celebrated and communicated, and also do not serve as learning case to improve future investments. This is due to the absence of clear BIO monitoring and reporting requirements for development results (in the period under evaluation for the five cases).

Evaluation conclusions & recommendations, and management responses

- ***Doubts about the sustainability of the investment in Sinapi Aba***

  The evaluators doubt the sustainability of the investment, by the RIF II fund, in Sinapi, because they consider that Sinapi's offering in the agricultural sector is currently not commercially viable, because its collaboration with its clients is in close conjunction with donor programs providing grants or free loans.
  In response, we signal that BIO's intervention in RIF II was through a loan, and that BIO hence was not provided with a role in the governance of the fund as it is the case when we invest in equity. RIF II's investment in Sinapi itself was also a loan and not equity, giving RIF II a more limited direct influence on Sinapi's evolution. Moreover the loan was awarded in 2009 and fully repaid in 2014, and was then also granted at market as opposed to concessional conditions, in other words Sinapi's situation early 2017 when the evaluators visited the company may be substantially different than it was at the time of the investment. We assume that when RIF II decided to invest, Sinapi had a perspective of economic viability. Assuming the evaluators' assessment is correct that Sinapi currently is not economically viable, internal or external negative developments since 2009 must – regretfully have led to a lack of longer-term sustainability of the company.

- *When considering the investments in the evaluated projects,* ***in none of the cases an in-depth assessment of the development potential at farmer level has been performed****.*

  When assessing a possible investment, of course its effects on farmers, their families and their communities are always part of the investment analysis. This is usually based on information from the investment applicant, country and market intelligence, input from the local Belgian embassy and from other relevant local institutions, and in case the project leads to on-site due diligence, visits to a number of farmers and, if existing, farmer organizations, as well as, regularly, an analysis

of the Environmental, Social and Governance aspects of a project by an external expert. It goes without saying that significant and sustainable impact at farmer level is a pre-requisite to any direct investment in agriculture. Regarding agriculture investment through general funds, this is not always systematically the case, whereas in funds focusing on agriculture this is certainly part of the investment assessments.
But it is true that BIO does not systematically take a farmer perspective in analyzing an investment opportunity, nor in monitoring an investment's impact, also because of lack of resources and internal expertise to do so. We agree that such a perspective enriches the analysis and could help in shaping the investment conditions to achieving optimal farmer benefits. In essence, it would entail on-site investigation to map farmers' situation in terms of assets, social environment, market perspectives as well as their own ambitions and objectives, to ensure that in the end an investment takes these into account as much as possible.
Therefore, we will consider a pilot, with particular focus on keeping the cost and workload as low as possible, so as not to further burden our investment assessment and monitoring processes much, as these already are very heavy both for BIO staff and the potential investees.

- *In 2 out of 3 cases,* ***serious concerns about the content and relevance of BIO's Technical Assistance funding****. The evaluators state that "it should be ensured when devising TA, BIO incorporates the ambitions and desires of the investees". They also recommend for "BIO to explore the possibility to provide conditional financial support upon development performance of the investee."*

  In the case of Niche, the evaluators state that "the focus on the training of organic farmers was not in line with market demand", and report that "the MD of Niche stressed that the focus on this type of development impact was not desired by the firm". In the case of CDPA, "the evaluator could not identify the added value of the ISO certification that was obtained with the TA funds".

  This recommendation is somewhat contradictory to the previous one, which called for more BIO influence on the investee.
  In the case of Niche, it was indeed BIO who at the time of investment asked Niche to adopt with a sustainability certification system. But Niche did not object to this, and when BIO put them in touch with a program to organize cocoa farmers and support them in producing organically, Niche liked this because of the added market value the organic certification would yield, and because the fact that the program had a warehouse in the harbor and Ghana's only export license for organic cocoa created significant synergy. It may, however, well be that prices for organic cocoa have not evolved as foreseen and that the farmers' production of organic cocoa has been insufficient to merit its separate processing and handling by Niche.
  In the case of CDPA, it was the investee itself who asked for support to obtain ISO certification. While it may not have immediate market value, the adoption of a quality management system generally is an important milestone in the strengthening a company and making it fit for further development and expansion. Moreover, it can have a lighthouse function for other companies, and indirectly contribute to a broader improvement of governance and management of the entrepreneurial sector. In fact, both are the case in Benin, where CDPA's CEO has also become the president of the national poultry companies association and of the National Chamber of Commerce.
  More in general: through its investing, BIO does indeed seek to achieve significant improvements in its investees' environmental, social, governance and development-effects performance. When investees agree but do not have sufficient means to achieve these, a TA subsidy can be crucial. Ideally, even if the area of TA was not an investee priority, the results of the TA convince the investee of the measure's adequacy and importance. The challenge is to balance our objectives and requirements with the investee focus and priorities in such a way that ultimately, the investment is successful on all fronts.

Regarding the evaluators' recommendation to consider conditioning financial support to an investee's development performance, we are skeptical. Subsidizing technical assistance shouldn't be a reward for good behavior, but a necessity and make business sense.

- ***BIO should define its exact added value in investing in agriculture, and seek to optimize this added value by selecting the 'right' investments that suit both BIO's goals and that match the instruments it has for agri-investments.***

  In fact the evaluators recommend that BIO goes beyond its general development objective of enhancing rural development and food security to determine more concretely what, on the basis of its available investment and TA instruments, it can achieve in agriculture, and what it cannot. These concrete results sought should then be linked to the specific instruments: direct/indirect, equity/loans, funds/financial institutions etc.. In this respect the evaluators speak of "impact pathways". Once this exercise has been done it should guide the sourcing of new agriculture investments, the evaluators recommend.

  In response, BIO Management stresses that the company's Investment Strategy includes a clear strategy regarding agriculture and agribusiness projects, that focuses on working with players that can play a leading role in their agri-sector whether they are producers, transformers or distributors, and whose development can benefit the full value chain. All due diligence of projects now include discussions with promoter and management of the business model and development effects expected to be achieved.
  Indirectly, BIO does a stringent due diligence on fund managers that are expected to carry out the role of business development, improvement of quality standards and governance and ultimately achieve development goals. Creating a layer of "compulsory" goals to achieve for BIO would be counterproductive as it would prevent the fund to do investments that are still very interesting from a development point of view, and therefore could deter fund managers or co-investors to work with BIO, and end up limiting our agri-investments to direct projects and hence reduce our outreach.

  That said, the evaluators' recommendation can also be interpreted as a call a more in-depth analysis of the needs of agricultural producers and processors, and of opportunities to respond to these. This was in fact the main reason for launching BIO's internal Agri Task Force late last year: not because we felt we are doing a bad job regarding agriculture, but rather to explore how to enhance our relevance and development effects in agriculture, agro-industry and agro-forestry. The preliminary conclusion of this exploration is that although our current instruments could be used in more targeted ways, to really respond to the needs of especially the SMEs and small-scale producers, additional instruments are needed, in particular with concessional components.

- ***BIO lacks clear monitoring and reporting requirements for development results*** *(in the period under evaluation for the five cases)****.***

  The monitoring of investments covers two activities:

  (i) The portfolio monitoring of the investments in view of preserving the asset value of BIO. On that side, all of our investments are closely monitored with regular on-site visits, reception and analysis of the financial reporting, annual review of credit risk rating, treatment of waivers, covenant checks and presentation once a year of a portfolio review report to BIO's governance bodies. The output coming from the portfolio monitoring department is considered as efficient (our auditors – Deloitte – are satisfied with the quality of the reporting produced by the portfolio monitoring department and informed us about the sharp quality improvement since last year).

  (ii) Since the introduction of the development assessment tool in 2015, the team has been also responsible for the collection of the new type of reporting linked to development, and transmission to BIO's development unit for analysis. The new tool requires annual reporting

from BIO's clients. The five cases that were evaluated were investments contracted before the introduction of this new tool, and their contracts indeed do not include the annual development reporting obligation. We are currently investigating how we can introduce such reporting as well for investments contracted before 2015.

- ***BIO has achieved important results that are currently not being celebrated and communicated,*** *because BIO lack of clear monitoring and reporting requirements has not made important development effects visible.*

  It is true that in the past BIO did a thorough ex ante assessment of possible investments, but then didn't systematically monitor development outcomes. It undoubtedly meant losing out on learning opportunities, as well as on successes to communicate and celebrate.
  Early 2015 we introduced a new development effects methodology that enables us to focus our desired development impact, a systematic monitoring of progress achieved as well as better information for communication. This year, we intend to use the different 'modules' of this methodology (*ex ante*, monitoring, *ex post* etc.) to create a 'dashboard' of key development effects performance indicators, that should enable a high-level insight.
  But the biggest challenge right now is to apply the development methodology to our investments in MFIs, banks and other financial institutions. These provide financing to thousands of SMEs, credit groups and other clients, with tenors ranging from a few months to half a dozen years. We – and other investors – still need to find a feasible and affordable way to gain insight into the jobs they create, the economic growth they generate, the taxes they pay, the greenhouse gas emissions they avoid, etc.. Gaining this insight is urgent because with over half of BIO's investments going to financial institutions, our methodology currently misses out on probably even more than half of the total development effects we generate or contribute to – as especially on a micro- and small-level, indirect investments are generally much more effective in terms of development impact than direct ones.

- *Where does BIO want to be in the spectrum going from [maximum] financial return to [maximum] social and/or environmental impact?"* ***BIO and the Belgian government have to agree on the 'risk appetite' that is desirable or acceptable for the BIO investments.***

  With their "spectrum", the evaluators assume that there is a trade-off between financial return and social and environmental impact. This may sometimes be the case, but we strongly doubt the general validity of this assumption. We have made numerous investments with good results on both impact and return. Our mission is to generate optimal impact with a decent financial return, we are generally succeeding in doing so and see no reason to question this ambition.
  Currently BIO and its public shareholder agree on the company's risk appetite. At the same time, the government and BIO are investigating how BIO can increase its risk appetite when it could lead to significantly more development impact, in particular for SMEs and in agriculture/agro-industry/agroforestry. Yet so as to comply with our legal obligation of the perspective of a decent financial return on every investment, concessional means will need to be found to de-risk or provide project risk guarantees.

- *Even though the evaluators consider the Development Assessment Tool that BIO has been using since 2015 as an important step, they recommend "to BIO to have* ***a goal setting that is even clearer, and to define a shorter set of meaningful SMART performance indicators for outcome and impact****". Furthermore, the evaluators state that "The* ***definition of a unified impact pathway for all direct and indirect investments*** *with an accompanying set of indicators will allow BIO to better track its performance by adding up and comparing cases".*

  Besides recommending a more "SMART" formulation of our concrete investment impact objectives, the evaluators insist on the consistent use of the development methodology irrespective of whether an agriculture investment is direct or indirect: "A good system needs to

work towards one impact goal, however defined, that is the “common currency” towards which all reporting structures are working”.

By introducing a new development methodology, BIO reduced its number of development indicators from over 150 to a few dozen, only a selection which is applied to a specific project. Most of these indicators are quantitative and SMART. However, the evaluators believe they are too much focused on output (such as “the number of financial loan products developed” or “agri-portfolio hired”) and not sufficiently on outcome (such as “number of loans to smallholders”).

Regarding direct agriculture investments, BIO management does think that since the new methodology was introduced early 2015 development effects goal setting is clear and the accompanying indicators sufficiently concrete. The methodology gives room to follow up on selected standardized agricultural key indicators as well as customized indicators.
Regarding indirect agriculture investments through funds, MFIs, banks and other development institutions, we indeed do not have a specific development effects methodology regarding agriculture investments. For agnostic funds and financial institutions that can have hundreds or even thousands of clients for (very) small loans, it is not our priority to implement such a methodology in view of its (very) high relative costs. Rather, a first step regarding indirect investments could be to seek to implement such a methodology for fund specifically focusing on agriculture, such as AgRIF or AgriVie. Because these funds have their own development effects methodology and investors other than BIO in these funds may as well, the challenge will be to gather all investors and the fund manager round the table to seek a common methodology that responds to the needs of all involved and yet is feasible and cost-effective.

- *The Evaluators recommend that “BIO could consider a portfolio analysis or* ***impact assessment on regular basis (5/10 years****), both from an accountability perspective (what has been achieved?), a learning perspective (what is more effective and relevant and what is no longer?) and a strategy evolution and development perspective..*

  We think that this recommendation is valuable and could be especially worthwhile – and more affordable – when done per sector. In fact, our current reflection on enhancing our performance in agriculture, agro-industry and agroforestry could be seen as such an assessment: taking stock of our activities, an external evaluation of its impact, and liaising with others in the sector to devise new/improved ways of working.

Follow-up

The evaluation contains many insights, conclusions and recommendations that BIO can use to improve its investment and assistance activities in agriculture, agro-industry and agro-forestry, to enhance its performance in terms of more work, income and secure access to food for people in developing countries, in particular in the rural areas. In the fall of 2016 BIO set up a Task Force for this, which submitted its recommendation to BIO’s Board of Directors early May.

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