FEED THE FUTURE
The U.S. Government's Global Hunger & Food Security Initiative

FEED THE FUTURE UGANDA INCLUSIVE AGRICULTURAL MARKETS ACTIVITY

THE PROMISE OF VALUE FOR SMALL AND MEDIUM AGRIBUSINESSES ENGAGING BUSINESS ADVISORY SERVICES; BID CAPITAL PARTNERS CASE STUDY

BACKGROUND

In Uganda, micro, small, and medium enterprises constitute about 90% of private sector production and play a crucial role in income generation, especially for the poor.[1] However, lack of finance continues to constrain their growth, especially for agricultural small and medium enterprises (agri-SMEs). A growing local industry of Business Advisory Service (BAS) providers in Uganda work to prepare, link, and support businesses to raise the capital needed for their business growth. The BAS market in Uganda is thin and few service providers target agri-SMEs as clients due to lack of understanding of, and networks in, the agricultural sector, limited willingness, or ability of agri-SMEs to pay for support services, and the cost of hiring and retaining skilled advisors who understand investor needs and finance. On the other hand, agri-SMEs lack awareness, appreciation, and willingness to pay for BAS given the lack of appreciation of the benefits relative to the cost and due to the lack of service packages designed to fit their needs.

The USAID-funded Feed the Future Uganda Inclusive Agricultural Markets (FtF IAM) Activity currently works with service providers to demonstrate the value of BAS to 48 inclusive agri-SMEs.[2] The service providers aim to improve the agri-SMEs' business management practices and raise at least USD 10 million in capital for 30 agri-SMEs. In turn, this will grow the

About FTF IAM

The Feed the Future Uganda Inclusive Agricultural Markets Activity (FtF IAM or the "Activity") is a five-year market systems development activity (2019-2024) funded by the United States Agency for International Development (USAID) and implemented by DAI Global, LLC in partnership with TechnoServe Inc. (TNS) and MarketShare Associates (MSA). The purpose of the Activity is to increase incomes and improve the livelihoods of households through agricultural-led inclusive economic growth, targeting 38 FtF districts in Northern, Western, and Eastern Uganda. The Activity contributes to the Global Food Security Strategy (GFSS) Uganda Country plan goal of reducing hunger, malnutrition and poverty and the USAID/Uganda Country Development Cooperation Strategy (CDCS 2016-2021) goal of strengthening Uganda's systems to accelerate inclusive education, health, and economic outcomes.

FtF IAM works through market actors to build capacity and enable them to respond to opportunities in the agricultural sector. The approach empowers local actors, especially the private sector, government, and producer groups, building their capacity and de-risking the use of new business models and technologies. FtF IAM places women, youth, and other marginalized groups at the core of its strategies and focuses on creating efficiencies in market functions that have sustainable impact on the agricultural sector and the country.

[1] Lakuma et al. Journal of Innovation and Entrepreneurship (2019) 8:15

[2] SMEs in the agricultural sector with models that engage women, youth, and marginalized groups as employees/ suppliers/ consumers of productive goods.

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pipeline of agri-SME clients, strengthen the ability of BAS providers to design and offer services that fit this market segment, and incrementally reduce reliance on donor funds as cost reduce and SME contribute more.

In September 2020, FtF IAM contracted BiD Capital Partners (BCP), an international impact investment advisory and asset management firm, to offer BAS to 24 agri-SMEs, targeting 12 for in-depth coaching and transaction advisory support. As this was in the middle of the COVID 19 pandemic, FtF IAM decided to cover the cost of the services, with the exception of a 3% success fee charged by BCP to the agribusiness client upon closing a deal. As of January 2023, BCP has worked with 24 agri-SMEs and six (6) have accessed USD 4.25 million in investment funding. This brief highlights learnings from the investment readiness and capital raising journey of six agri-SMEs and provides insights on the benefits of the advisory services, success factors to raising capital, lessons on targeting, and roles played by agri-SMEs in the investment fundraising process.

SUMMARY FINDINGS

BCP's experience in sourcing and initiating service provision to the agri-SMEs confirmed the assumption that BAS was largely unknown to the agri-SMEs in Uganda. The Activity and its partner, BCP were able to demonstrate the importance of BAS to agri-SMEs, due to BCP's expertise in providing tailored services, mentoring the agri-SMEs, and its knowledge of investor requirements. Agri-SMEs' role in the successful delivery of BAS, however, was as important as BCP's role, with varying commitment and capacity by agri-SMEs. This includes the investment readiness of the agri-SMEs and their willingness and ability to provide requisite information, invest in complementary processes and services (shareholder registration, external audits, market, or product assessments), and modify governance structures to professionalize the business.



Mission Director, Richard Nelson, visiting Masha Quality Coffee, which has investing in a new traceability system with support from BCP.

Only 8 of the 21 targeted agri-SMEs were willing to share all the information needed by BCP.

BCP had to demonstrate its authenticity and build trust before agri-SMEs would share sensitive information required by investors. This process took three to six months and caused unexpected delays. Of the 21 agri-SMEs engaged at the time of this assessment, only 20% had prior engagements with similar firms, which did not deliver on expectations, and two agri-SMEs had lost money to 'fake' investors. Only eight (8) of the 21 targeted agri-SMEs were willing to share all the information needed by BCP to provide business analysis and modeling, investor pitch decks, and networking services.

BCP provided more customized and in-depth services to the agri-SMEs than anticipated. Services had to be defined by the nature of the business. Family-owned businesses or sole proprietors needed to strengthen and formalize their governance, professionalize operations, and register the businesses and its shareholding. The negative effects of COVID-19 on the economy also increased the level of effort required for investment readiness, as many agri-SMEs experienced a reduction in production volumes and revenues. BCP carried out or recommended the agri-SMEs to hire firms to carry out market and product assessments to determine the actual performance of the business and products and identify new market opportunities in the changing business environment. In addition, BCP supported businesses to measure social impact, which was of major interest to investors.



A machine operator at Newman Foods Limited, a snack food processor, that supported to raise capital to expand its facility in Kampala Uganda.

While agri-SMEs realized initial benefits within two to three months of receiving BAS support, it took 12 to 18 months to raise capital and secure investment. One foreign-owned agribusiness appreciated the services that BCP provided to understand the Ugandan context, recruit local and competent staff, and establish local networks. Another Ugandan agribusiness decided to downsize its product offerings and focus on those with higher margins through the product analysis done by BCP. Financial modeling helped one agribusiness to monitor its financial standing in real-time, which improved its operational efficiency and profitability. Despite appreciating these early benefits, agri-SMEs indicated that they are still more likely to pay for such services when payment is tied to raising financing, a success fee.

Overall, the demonstration of BAS has changed agri-SMEs' attitude towards BCP and BAS. All the businesses in the advanced stages of investor negotiations stated that they are willing to pay for BCP's services when raising additional investment in the future. Agri-SMEs appreciated the quick turnaround time by BCP in providing investment readiness support and getting them to meet with investors and understood that BCP's reputation and relationship with investors was a catalyst in the fundraising process.

LEARNINGS

- **SMEs do not currently collect sufficient business data and information that enables firms like BCP to help them to raise financing**. Businesses that were responsive to the needs of BCP and shared prerequisite information quickly advanced to investor negotiation and deal-making stages. These businesses had governance

structures and systems to collect business and social impact data. For example, one of the agribusinesses that raised capital had a system that demonstrated how its product supply chain and market channels engage and increase incomes for the bottom of the pyramid (BoP), including how the firm sourced from smallholder farmers through aggregators and how they used street vendors as one of the channels to sell their products. BAS firms may consider improving the selection criteria used for sourcing and selecting agri-SMEs for their pipeline or building in time and resources for such upgrades to improve the success rate and turnover of the pipeline.

- **Investor matching is a major incentive for agribusinesses to make the necessary upgrades towards investment readiness.** BCP's speed in matching SMEs to a pool of investors and facilitating early introductions, discussions, and even physical site visits for investors increased SMEs' commitment to the investment readiness processes and fulfilling recommendations made by BCP and potential investors. These upgrades significantly reduced the period of investment readiness support and increased the agri-SME's potential to raise capital. BAS firms need to continuously widen their network of investors, bring investors in early and understand investor needs to demonstrate a value proposition to agri-SMEs early.



Employees processing sausages at Sausage King, the first agri-SME that closed a deal with BCP support; additional funding will support them to increase meat purchases from producers and expand its micro-franchise street vendor sales model.
Credit: Sausage King: https://skuganda.biz/production-process

- **BAS is critical to early growth agri-SMEs but realizing service commercialization will take time and may always require some donor funding for the smallest, lowest capacity SMEs.** The high cost of support is driven by the duration of support that is required and the high upfront capacity building often needed in the agri-SME sector. Success fees alone- especially for small deals (ex. Under $1,000) will not cover the cost to the BAS firm. The length of time taken from deal origination to deal closure is on average a year because:
    - Building the trust of agri-SMEs to share private and sensitive information takes time and frequent early engagement.
    - Many agri-SMEs are sole proprietors, family businesses or cooperatives and are less attractive, especially to equity investors; agri-SMEs may agree to re-structure and strengthen governance, but this delays a capital raising process.
    - Businesses need more investment readiness support due to negative effects of COVID-19 and the economic impacts of the war in Ukraine on cost of supplies, outstanding debts and depleted working capital. Investors are also more risk-averse and have expanded due diligence to mitigate perceived risks.

The lengthy process contributes to increasing the cost of BAS, which may continue to be unaffordable, especially for firms raising funds for the first time. The earlier assumption of developing a standard service package for

the agri-SMEs to reduce costs may not be possible as the required support for investment readiness is bespoke due to the different levels of investment readiness of agri-SMEs. Those firms with the highest upfront needs are also likely to have smaller ticket sizes, resulting in lower success fees, which are a percentage of the deal. Of the six deals closed by BCP, three (3) were under $50,000 and the rest were $750-$2million. The missing middle – higher than small impact investors are willing to risk – and lower than the smallest private equity funds are willing to consider, remains a challenge. These firms have limited collateral that they can leverage for commercial loans, and often commercial interest rates are cost prohibitive.

Currently, BCP is targeting agri-SMEs with larger investment requirements to recover the upfront costs for investment readiness through the success fees or commission generated from capital raised. But without support for young and emergent agri-SMEs for smaller early deals, the next generation pipeline of larger deals will remain limited. The three smaller deals closed may be eligible for a next round of funding and are in a much better position to know what the investors are looking for and prepare. Therefore, donor funds have an immediate impact by supporting small investments, and reducing reliance on grant funds, but may have unrecorded secondary impacts for future rounds of investment.

CONCLUSION AND LOOKING FORWARD

The collaboration between FtF IAM and BCP to demonstrate the value and increase awareness of BAS delivered the desired investment results for six companies and offered additional benefits to all other firms in its pipeline (24) and the agricultural sector beyond these deals. All the agribusinesses that BCP supported on investor matching, deal negotiation and closing appreciated the services and were willing to pay for the services for future fundraising, with a focus on a success-fee model.

Drawing from the results and learnings above, BCP's 20% success rate for raising capital for supported agribusinesses could be increased with better targeting and a stronger economic outlook, combined with a minimum financial contribution to the upfront technical assistance, co-funded by a donor, rather than fully financed. BAS can be commercialized for larger agri-businesses as they are more investment ready, have bigger investment needs with a likely higher success rate, and a sizable commission that can cover most of the BAS fees.

There is still a need for market facilitators to increase understanding of BAS among agribusinesses, and the agribusinesses' own role in the process. FtF IAM will continue to increase visibility through business-to-business events and stakeholder engagement meetings to share the interim benefits of BAS among agribusinesses. Additionally, FtF IAM will work with BAS partners to develop commercial packages that are attractive and affordable to agri-SMEs. The Activity will also focus on building demand for services and incrementally asking SMEs to co-fund these services through case studies and presentations at B2B events and other forums.

To target and support agri-SMEs with smaller ticket sizes, especially those impacted negatively by COVID-19, FtF IAM has adapted its approach and is providing small risk capital awards alongside advisory services with three BAS firms, including BCP, to buy down the risk and costs of bridge financing for smaller, higher-risk deals. The BAS firms are targeting inclusive agri-SMEs that have high potential but are not able to raise capital due to the impact of COVID-19 and the risk assessed by the investors. This applies to deals that were close to being signed but the bank or investor assessed the risk as too high. FtF IAM funds will be used to buy down the cost and/or risk of the deal, in an addition to advisory support.

Implementers with similar objectives to FtF IAM, may want to consider tiered approaches, with longer timeframes, that allow BAS providers to move forward with some deals that are closer to investment, while building in time and resources for capacity building for a slightly larger pool of companies that are not yet investment ready and need more support.

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