FPOs as harbingers of agricultural transformation - The significance of credit

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Small Farm Incomes

IRMA

Foreword

Farmer Producer Organisations (FPOs) have become a buzzword in the last few years. The Government of India sees this institution often as a panacea for all problems with Indian agriculture and as *the* vehicle for transforming farming from subsistence to an enterprise. Academic debates compare these nascent institutions with older generation cooperatives and wonder why their scale is low and sustainability suspect. Landscape and state of sector reports have thrown interesting insights on the FPO ecosystem but there is often little clarity on the details of how FPOs are navigating complex relations with markets and financial institutions.

Despite the overall impressive growth in number of farmer producer companies, in excess of 10-12,000 in the last decade and spectacular rise in the last five years, there is little discussion on the credit requirements of these nascent institutions. One of the earliest commentators on FPO finance, Emmanuel Murray's first study in 2008, then for the Reserve Bank of India, was titled "Producer Company Model-Current Status and Future Outlook: Opportunities for Bank Finance". Murray with his background in rural management and over three decades of work in agriculture and rural credit is a rare combination of a professional who not only has a keen feel, or to use Sumantra Ghoshal, the "smell of the organisation" and writes and reflects on his observations. His articles on various platforms have evoked interesting discussions and one felt that if these were put together as a compendium, many young researchers who are trying to understand the FPO space could have interesting ideas and research questions that may not emerge from dry systematic literature reviews.

Murray readily agreed to have his articles put together in the form of a compendium. The selection of twenty articles in this compendium cover his writings from March 2018 to August 2021. They cover a wide range of subjects that seek to inform readers about the general FPOs, their spread or the state of the ecosystem, to a deep dive into the much-neglected understanding of the state of finance or lending for FPOs. This compendium goes beyond mere reflections and speaks directly to professionals engaged in development finance as well as promoters of FPOs. The articles provide useful heuristics and guiding principles for the professionals navigating the terrain. Murray also takes us into the mind of a financier, who evaluates not only the present status of an organization, but its future potential as well. The articles help in understanding both the process of determining the creditworthiness of an organization, and the social and ethical considerations involved in the profession of accounting in the context of the ownership of farmers in financial and operational decision making of the FPOs.

Murray warns us, in an ever so gentle fashion, the need to remain empathetic to the cause and needs of the farmers despite the structural deficiencies and ecosystem failures. While using finance as a lens, these articles provide tremendous insights on capacity building, governance and management and market linkages across the value chain. On the centenary year of Dr. Verghese Kurien it is our pleasure to bring this volume, while insightful in itself would also encourage development practitioners to share and reflect on their insights and work more closely with academics to co-create new knowledge on producer collectives in India. I am sure that Arnab Chakraborty, Abhishek Saxena and Pallavi enjoyed the writings even as they helped put them together and I thank them for their efforts.

Shambu Prasad, C. IRMA November 2021

If only, 'my earnest prayer for Farmer Producer Organisations'

"We are parasites living off FPOs. Therefore, it is in our best interest to see that the FPOs prosper." A senior consultant to many FPOs, at a recent FPO Consultation Workshop

Over the last few months, I've attended several Seminars, Workshops, Conferences and Trainings on FPOs. During the same time, I have turned down an equal number of such events, due to my inability to accommodate them in my calendar.

Today, there are a large number of CAs. CSs, and self-proclaimed experts & FPO consultants (me included) who claim to be working for the benefit of FPOs.

Added to this tribe are the microfinance experts of yore who have migrated & found their new calling in supporting/promoting FPO through what is euphemistically called Capacity Building.

Let me share some interesting innovations that have come to my attention in the FPO space in recent times:

1. CEO Sharing FPOs - One person being the CEO of multiple FPOs – An interesting way to rationalise the cost of hiring a professional.

2. Single-man FPOs – A proprietary concern masquerading as an FPO

3. Non-member FPOs – Practically all the business done is with non-members.

4. FPOs as Financial Intermediary – This is something I have just discovered. Lending to an FPO, not for the FPOs business, nor to supply inputs to members, but plain & simple on-lending to members.

As I attend more of the Workshops, Seminars, Consultations or events by any other name called, I keep questioning myself, am I also becoming a parasite on the FPO bandwagon?

And then, so many *'If only'* questions come to my mind:

· If only we can hold this in a modest place instead of a 5 Star hotel

· If only we can talk less & do more for the FPOs

· If only the institutions who claim to be working for the welfare of farmers collaborate?

· If only the FPO promoting institutions can communicate and freely share experience and expertise with each other instead of working in silos?

· If only ………………………., and the list goes on.

Am I the only cynic having these doubts about intent and actions, or are there others who share the same concerns?

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Contents

Part I: FPOs as instititional innovation

1. The Covid 19 Lockdown and the Coming of Age of Farmer Producer Organisations 5

2. Who conceived and first articulated the idea of Producer Companies in India? 8

3. Policy for FPOs – walking on three legs 9

4. What do local market players think of the new kid on the block - the FPO?....................... 11

5. **The significance of Social Capital in Farmers' Institutions** 11

Part II: FPO Financing: Understanding multiple realities

6. Trends in Lending to Farmer Producer Organisations... 13

7. **Self-Help Groups (SHGs) as lenders to farmer members of Farmer Producer Organisations (FPOs)?** 15

8. Lending to Farmer Producer Organisations (FPOs) in FY 2019-20 17

9. Why Farmer Producer Organisations (FPOs) have challenges in accessing debt, or rather, what challenges lenders face in extending debt to FPOs 19

10. Is FPO lending amenable to productization? 20

11. Financing nascent Farmer Producer Organisations (FPOs).. 22

12. Why lending by banks to Farmer Producer Organisations is a challenge that's not going to go away so easily 24

13. **Enhancing Credit Flow to Farmer Producer Organisations** 26

14. Continuing the discussion on Farmer Producer Companies 29

15. FPO Ecosystem and Credit Absorption Potential of FPOs.. 31

Part III: Building ecosystem support for FPOs

16. Building an Enabling Ecosystem for Farmers Producer Organisations........................... 31

17. Continuing the FPO Saga - Is the David and Goliath story possible with FPOs? 36

18. How procurement methods of FPOs help farmers (and how they are different from conventional trade) 38

19. Strengthening Farmer Producer Organisations 40

20. Farmer Producer Companies as vehicles for Farmer Emancipation................................ 42

Epilogue 44

1.The Covid 19 Lockdown and the Coming of Age of Farmer Producer Organisations

There is a tide in the affairs of men (and of organisations). Which taken at the flood, leads on to fortune.

Julius Caesar Act 4 Scene 3

Every calamity brings out the best & the worst in people. It unfolds their real self, beyond their usual public image. Covid 19 and its global fallout is more than a calamity. Even calling it a catastrophe would be an understatement. And we are still in the midst of it, to conclusively know what impact it would have on the economy and society.

While the Governments of the day moved from denial of the pandemic to the other extreme of panic, it has seen the emergence of new leaders, people and organisations that rose above the call of duty, recognised the need for action and got going!

In India, the nationwide lockdown imposed at 4-hour notice immobilized all activities, bringing everything to a grinding halt. People had little if any time to stock up on essentials, particularly food items. And then how many would have money for the shopping in the last week of the month? Even the bureaucracy was caught off-guard, as the Police took over the streets, and ensured that not a crow moved without a reason and without permission.

The shutting down of the agri markets (mandis) due to both a combination of factors like scare of not maintaining social distance, truckers not ready to move, drop in offtake, and the confusion about what services were exempted led to breaks in the supply chain and traders not operating. Consumers on the other end were locked at home, wondering how they would get their essential supply of groceries and vegetables.

It took a while for people in the agri space to knock doors, push papers and get permissions to move agricultural produce, particularly perishables. Having got that, the search for transporters began, and by about end of day 3 of the lockdown, agri commodities began to slowly move, and continue to move since then. But there continues to be constraints on inter-state movement, and a slump in demand.

For farmers growing fresh vegetables and fruits, the immediate aftermath was a shock, though inability to sell all that they produce is no new phenomenon. Pictures in the early days of the lockdown showed a farmer in Karnataka flattening a ready to harvest cabbage crop into the ground, while another in Maharashtra fed strawberry to his cow.

It is here that the fledgling farmer groups & Farmer Producer Organisations (FPOs) saw the opportunity to bring farmers together, aggregate and take the produce to market. They saw it not just as a business opportunity, but as a humanitarian mission as well. Mention must be made here of the several Agri start-ups that also got into the act, as did local community organisations and NGOs.

These are some interesting documentations of these processes:

Farmer Producer Company Bridges Consumers and Farmers During Lockdown

Social Capital Enables Tomato Farmers to Sell Produce during Lockdown

For the farmers involved in organising supplies during this time, it transcended being a business, into a mission of ensuring essential supplies to those in need. The excitement and the satisfaction of doing something for greater common good made them to sell in many cases, at prices way below market prices, freshly packed and home delivered. And to the poor and needy who could not pay, they even gave free.

In the course of this foray into the consumer market, farmers demolished two bastions, and busted two myths; first that small farmers do not have the physical capability in terms of quantum of material, logistics or patronage to deal with the market. Second, they overcame the mental block small farmers were made to believe, that they do not know how to negotiate the market.

The winner sets the rules

Having overcome the physical and psychological barriers, like in any victory, it is now for the victor to consolidate his position and operate from a position of dominance. It would be disappointing if the Farmers organisations retreat from these commanding heights they gained in the market, as the situation returns to normal.

An opportunity that may never come again

What the Farmers Organisations have won is just the battle. The war is far from over. Here are a few thoughts from my side on what FPOs & farmer collectives should do next to consolidate their presence in the direct to consumer market:

First, recognize the power of numbers. The power of coming together.

Second, recognize that your markets are not just cities. Small towns offer equally good market opportunities.

Third, recognize that you can't just dump everything you grow on the market. Start building a culture of quality at the production stage itself. Sort, grade at point of origin and send only what is marketable to the market. Remember, transport costs can be a heavy burden if you carry trash.

Fourth, recognize that prices can be determined by you. There are buyers for onion at Rs. 20 a Kilo, and there are also those willing to pay Rs 30 for premium quality. You decide where you want to be and what price you want to charge.

Fifth, physical infrastructure is not the key to market access, if you can organise the supply chain at source.

Sixth, 30% spoilage in fresh vegetables is a bogey. If you coordinate well and can cut that down, every reduction in material losses boosts profit.

Seventh, fulfill the basket of requirements of the consumer. Get all that is needed organised (if necessary by procuring), so he/she is need not have to shop at multiple stores. Convenience has a big premium.

Eighth, make use of simple technology; smartphone, WhatsApp, or even the basic mobile for a start to get going.

Ninth, the invincibility of the trader is a myth.

Tenth and most important, be principled. Don’t let greed overtake you, always maintain quality, maintain discipline, adhere to committed schedules. Build an entrepreneurial spirit. You are the transformation.

If you’ve done it in the hard times, it will be a lot easier in the good times.

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2. Who conceived and first articulated the idea of Producer Companies in India?

Cooperative Companies are not a new phenomenon globally. In several countries where the co-operative ethos is strong, such companies exist. They are companies by charter, but cooperatives in character.

The Cooperative movement in India that is over a hundred years old, is a colonial legacy, established in its' time, to address the problem of farmers' distress, something that hasn't changed much after Independence.

The idea that farmers are intelligent enough to be able to manage their own affairs & have the ability to employ & pay for top notch professionals, on-par or better than the private sector was clearly demonstrated by institutions like Amul. However, that farmers need state patronage and be steered by the bureaucracy is a notion that persists even today, compounded by the fact of elite capture of co-operative institutions and their rampant politicisation.

This overbearing attitude of the bureaucracy came to a head in the late 1980's, when the Chairman of the Gujarat Co-operative Milk Marketing Federation (GCMMF), a Federation of the co-operative milk unions of Gujarat that handled marketing and owned the 'Amul' brand was unceremoniously dislodged by the Registrar of Cooperative Societies (RCS) of Gujarat. While the decision of the RCS was overturned by judicial pronouncement, the clarion call for unshackling cooperatives, especially those that do not depended on patronage and doles of the Government from the stranglehold of the RCS took root from there, and grew in intensity and spread far and wide.

To complete the narrative (and give a perspective), the RCS who did this was an Indian Police Service Officer by name Jaspal Singh, who not long thereafter quit the central service to join active politics.

This 'uprising', if we can call it that, was the catalyst for two major reforms in co-operative landscape of India, one, the Producer Companies enactment, and the other the Mutually Aided Cooperative Societies Act.

Although the credit for the Producer Company enactment is attributed to others who appeared on the scene much later, the foundation for the Producer Company model was laid by Dr V Kurien & Chaudhary Brahm Prakash (the Wikipedia page of Mr Brahm Prakash makes a brief reference to this fact). Having been in National Dairy Development Board (NDDB) at that time, some of us were in some ways, part of the launch of this revolutionary movement.

Sharing these notes for those who may not be aware of the background, as it has not been adequately documented and is largely consigned to footnotes.

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3. Policy for FPOs – walking on three legs

"All you are offering is anecdotal evidence. Policy making requires empirical data."

- Dr Bimal Jalan Ex-Governor RBI

In the year 2000, I had the opportunity to be present at a meeting with the then Governor of the Reserve Bank of India (RBI), Dr Bimal Jalan at Lucknow. A presentation was being made on the Microfinance Scenario in India, and the plea for RBI to play a more direct role in Regulation.

Very early into the presentation, Dr Jalan interrupted the presenter, commenting that what was being presented was anecdotal information. Prematurely calling the presentation to a close, he noted that policy making cannot be done on the basis of anecdotal information, it needed deeper analysis based on hard data.

That was an **Aha Moment** for me, and opened my eyes to the fact that one should not get swayed by a few anecdotes on the sector picked up from here & there, good or bad, but rather to look for macro data and patterns for meaningful analysis and arriving at conclusions, and making sure recommendations flow from the analysis.

FPOs policy making is at the same crossroads today that MFIs were back then.

Let us put forward a few questions here on the Status of FPOs in India for consideration.

Do we know:

1, **How many FPOs are actually out there as on date?**

A recent painstaking study by Professors Annapurna and Richa at Azim Premji University arrived at the number of FPCs (Companies) at 7374 as on 31 March 2019. (Govil, Richa, Annapurna Neti and Madhushree R. Rao. 2020. Farmer Producer Companies: Past, Present and Future. Azim Premji University, Bangalore.) What about FPOs in other legal forms? NABARD lists existence of atleast four other forms; Societies, Trusts, Non-Profits & Section 8 Companies. This broader definition of FPOs will encompass all commodity cooperatives, so technically should include for example milk coops & weavers societies.

2. **What is the membership of farmers in these FPOs?**

Again, we have no official data and have to rely on academics, researchers & others to make an assessment. Annapurna & Richa estimate this at 4.3 million, which in my view is an overestimate.

3. **What is the aggregate turnover of FPOs?**

This continues to be another question that begs for an answer. One idea suggested was to download the financial reports of each FPC from the MCA site for a fee and aggregate. This may give the info for FPCs, but what of the others?

4. **How many FPOs are in profit?**

Again, there is total data darkness here. I do realise that FPOs are pitted against traders & it is a contest between unequals. Also an FPO could retain profits and display robust health. But this could be at the cost of not passing-on to the producers the gains from collectivization and disintermediation.

5. **How many FPOs have been able to get Credit Facility?**

Here again, we have a smattering of data from here and there and some informed guesstimates, but precise data is elusive, nay unavailable.

If we go one step up and ask a higher-level question

How much incremental income have FPOs been able to put into the hands of farmers,

The situation becomes even more fuzzy here.

Why you may ask, are these questions important?

Simply because, a significant amount of Public Money (estimated at Rs 2000 to 2500 Crore) has gone into promoting and sustaining FPOs. Hence, it is pertinent to ask - Have the objectives of the program been met?

More important than that, it is now proposed to form a further 10,000 FPOs with public funding of over Rs 6000 Crore. When the achievements of Phase I are still unknown, launching a Phase II programme is akin to changing the packing on a product that didn't work earlier, and hoping that it will work this time around!

Farmers have been at the receiving end of poor policy & planning for years. Inspite of noble intent, not much has worked. Unless we get the design right, things will not work this time as well, and we may end up having created another set of institutions without achieving much.

FPOs have to be a part of the overall programme for transformation of India Agriculture. In my view, the FPO program cannot be the centrepiece of that transformation. It's good to be modest & realistic about what FPOs can contribute in the quest of doubling farmers' income

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4. What do local market players think of the new kid on the block - the FPO?

I've spent over 30 years working in the Agri and Rural space. One of the earliest experiences was trying to form Tilhan Sanghs (oilseeds coops of soya farmers) in Ujjain, MP, without great success. One of the experiences documented as a Case with the Title 'Organising a OGCS (Oilseeds Growers Cooperative Society) in Bhasoda' I understand continues to be used in IRMA, my Alma Mater.

The reaction of local market players can be described in four phases:

Phase 1 - Amusement. Initially they feel it is just another sarkari-wala programme with these shehar se aaye chokre log trying to do something. They've seen it before. Once the program funding stops, 'tambu utar ke chal padenge' (roll up their tent and vanish). Most of the time when we interact with them, especially to do a business potential survey, they are cordial. We invite them to the inaugural function of the Society and they invariably show up and occupy the first row.

Phase 2 - Curiosity. If the Society starts doing well and generates lot of interest among the farmers, the trader gets alert and tries to get more information about 'kya chal raha hai?' What's happening? In a village it is not difficult to keep a tab. The trader also drops by now and then to exchange pleasantries and check things out for himself.

Phase 3 - Turning on the heat. This is where things get more exciting. If the trader sees some who used to regularly transact with him shifting loyalties, he gets jittery and annoyed. Reactions could include offering better prices than what the coop offers to kill the coop, to telling farmers that he will not extend small loans when needed, to refusing to transact at all with the farmers who may have sold part of their produce through the coop. Worst forms could include sabotage and arson. This is where many coops fail. They would be unable to match the financial muscle of the trader.

Phase 4: Adaptation. In case the coop manages to weather the storm and survive or better still prospers, the trader adapts the better business practices brought in by the coop such as quality based pricing, reducing arbitrary deductions and timely payment.

In my experience if a coop has the capacity to garner a 15% market share in the commodity, even if it does not actually deal to that extent, it begins to set the rules and be a market leader in setting price signals and defining the rules of business.

A trader like a cheetah cannot erase his stripes, and keeps trying ingenious ways to maintain his margin, and if the situation gets too tough, moves into other commodities or other locations. After all, he is a 'margin player' and what commodity he deals in really does not matter to him. Quick to learn and adapt, versatile and well networked. the trader in the rural market is not going to go anywhere, however successful an FPO may be.

Published on November 30, 2020

5. The significance of Social Capital in Farmers' Institutions

Some years ago, I joined a colleague in Caspian on a due-diligence visit to a Farmer Producer Company in Bihar that was into maize marketing. It had done impressive business in the earlier year, and the financial statements looked attractive enough for a banker to consider financing them.

Being supported by a reputed promoting institution and under the State Government's umbrella programme, it almost looked a copybook case. Unfortunately, we came back sad. The farmers were really nice, and maize was available in plenty, but things didn't add up. The picture was not as pleasant as the Financial Statements! As lenders, it is our job to ask tough questions. The time we spend on a visit is too short and precious, so we focus on getting a sense of things through interaction, leaving the documents and papers to be read at leisure, more to reinforce and validate the feeling we get of the institution during interaction. Instinct and intuition matter, as the legendary management guru late Sumantra Ghoshal coined the term, 'the smell of the organisation'.

How the chairman of the FPO is treated by the CEO & staff of the FPO and by the promoting institution and vice versa, who responds to questions that we ask, how much do the Board Members know about what's happening in FPO, the coordination between the CEO and the representative of the promoting institutions are all give-aways about how the FPO is doing. Among other things, in the present instance, the FPO was unable to produce a certified stock statement corresponding to the stock as reported in the audited financials (reminding me of an earlier time in my previous job, where the management of Masuta FPC one fine morning informed that the stock of silkworm cocoons as reported in the financial statements didn't exist and were a fictitious asset, leading to a loan of INR 10 million evaporating into thin air), and when some basic questions were asked on the financials, instead of answering them, we were provided the telephone number of the CA to speak to.

Overall, building a robust and sustainable FPO is not a mechanical process, but is 'Social Engineering'. If our aim is to build an organisation **'of'** the farmers, then it is they who need to be at the center. If on the other hand it is '**for**' the farmers, then you might as well run it with managers who understand business, and it can still do good for the farmers by giving them good returns. It's more a matter of clarity about what you want to do, and where you want the institution to be.

It is in this context that I recall what Dr Kurien told us when he commissioned us a Rural Managers. He said, remember, the Farmers you serve are your masters, you are their managers. Let that sink in.

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6. Trends in Lending to Farmer Producer Organisations

Through a recent on-going (and in progress) study commissioned by Bharat Inclusion Initiative of CIIE CO, whose team has painstakingly compiled data on borrowings by FPCs from the Ministry of Corporate Affairs (MCA) database, of the 9521 Farmer Producer Companies in India, 510 (5%) had accessed debt. The interesting fact is that 79 different institutions have lent to FPCs, not just the two-three familiar names, which to me was an eye opener. And with a paid-up capital of Rs 736 Crore, the borrowing potential of FPCs is Rs 3000 Crore considering a leverage of four times. I am eagerly waiting for the study report to be released, to get access to more granular data and insights.

In the meantime, sharing some other insights gleaned from recent interactions with players in the sector:

Good FPOs are seeing interest from multiple lenders: As I had foretold, better performing FPOs will break away from the pack and attain a higher growth trajectory, and will start attracting loans from multiple lenders. For example, an FPO in Vishakapatnam with a turnover of Rs. 10 million has a loan facility from both NABKISAN and Samunnati. This is a killer combination. While NABKISAN will provide a working capital term loan with fixed installments and lower interest rate, the one from Samunnati will be more expensive but flexible, to be drawn and used as per the commodity supply chain cycle. I wonder if the two lending institutions are coordinating while taking credit decisions, but this will be the future way forward. Relying on just one lender is always risky. You can never be sure, when they will pull the rug from under your feet. While the number of such attractive to lenders FPOs will increase, they will still be a small fraction of the total FPOs in the market for credit.

FPOs as on-lenders to farmer-members: This is one thing that FPOs need to be wary of. Both conventional lenders and new-age lenders seem to be in a hurry to leverage FPO networks to on-lend to farmers; both under-served and un-served. The idea being to off-load the credit risk and collection responsibility on the FPO. This in my view is fraught with serious risks for a thinly capitalized institutions and is best avoided.

Challenges in product design: There were some interesting examples that came to light on loan structuring.

In one case, the largest private bank provided loans to member farmers of the FPO with facilitation by the FPO. The only twist was that the loan was given for sugarcane (which the bank knew about), while in the banks' books it was indicated as paddy. The bank now, 5 months down is asking for repayment of the 'paddy loan', when the sugarcane is not ready for harvest! All that would have been okay if it was a matter to be worked-out between the bank and the farmer, except that the FPO has stood guarantee for the loan!

In another case, the lender to the FPO, an NBFC insisted that the FPO close the loan on due-date, even as the FPO had adequate finished goods stocks (as it is into retail sales) to cover the loan outstanding. The FPO was left with no other option than to resort to distress sale and incur loss, to close the loan. What good it did to the lender or to the FPO, I am left wondering?

Both these examples show how loan products are not designed to match the needs on the ground. The lender decides based on what is convenient to him.

In closing, let me say that the biggest problem with Agricultural and Rural Credit in India is not inadequate or improper policy, neither is it loan products, nor is it place (accessibility). The problem is people. Rural banking is largely manned by people unsuitable for the job. Most loan officers are 'lone' officers, with majority of the branch staff kept busy with transaction banking or managing the liability side of business. Hardly 10% of the officer cadre have the competency or capability to manage credit, and most of them are not into rural banking. That calls for a separate and detailed piece, sometime later.

Published on May 4, 2021

7. Self-Help Groups (SHGs) as lenders to farmer members of Farmer Producer Organisations (FPOs)?

At a recent workshop on the theme ‘Enhancing the credit flow to FPOs’, an idea was thrown up for discussion; SHGs becoming lenders to farmer members of FPO. And mind you, this was not a creative idea generated by a researcher, but something they had seen at work on the ground in one of the hill states during the course of their research work, and thought was worth replicating. My initial reaction, (as with anyone with years of work in this space, and having an arrogant sense of being an expert on the subject) was dismissive of the idea, but on second thoughts, felt; let’s examine the suggestion and give a fair chance for consideration and evaluation.

The idea both amazed and amused me!

First let me explain my amazement: Having worked in NABARD and involved in some ways in setting-up the SHG infrastructure in India foundation up, our hypothesis even while conceiving the program was that the poor, irrespective of their income levels had the propensity to save (knowing that they would have emergencies and aware that they are not credit worthy) and save they do, in different ways, in non-financial forms like gold, livestock etc. and were waiting for the right financial savings vehicle. SHGs have been able to be make that happen.

The long-held notion that the poor are “born in debt, live in debt and die in debt” has been proving wrong, as SHGs are turning net financial surplus entities. This is both a cause to celebrate as a matter of concern. The concern is whether the entrepreneurial spirit or the opportunities are inadequate, or the environment unfavourable for the poor to have bigger dreams and plans for deploying financial resources?

Coming to amusement, SHG being an informal, unregistered entity, it becoming a lender to a company is unbelievable. Putting it in a little exaggerated way, it is like a landlord taking a loan from his servant. But it has already happened, is happening.

As long as the money being lent is from the savings of the members of the SHG, I see no issue in on-lending, if it is done after meeting in full the credit needs of the group members, and with the informed consensus of all the members. It is money that belongs to the poor, and this lending is exposing money to high risk.

However, in case the SHG is receiving concessional funding with any form of support from the government in the nature of subvention, it is intended for the exclusive use of the SHG and its members, and on-lending is prohibited. If such a fact comes to light, it will bar them from such benefits in future.

The real reason for a point like this coming up in the first place is the failure of the institutional credit delivery system. It is like saying since the bank pays 3 to 5% per annum interest on my deposits with them, and on-lends my money to my friend or neighbour at 15% per annum, why can’t we just transact directly and let the earnings stay with us?

India has followed the multi-agency approach to lending, and if all the agencies put together are unable to extend credit for genuine needs for agricultural operations of farmers, it presents

a sad commentary. SHGs financing farmer members of FPOs is one of those 'jugad' solutions that is going to take us nowhere.

For more on this subject with thoughts from practitioners, experts and thinkers, please look-up my LinkedIn post on the subject.

Published on April 26, 2021

8. Lending to Farmer Producer Organisations (FPOs) in FY 2019-20

A few days ago, I had the opportunity to interact with representatives of major institutions in the FPO lending space. Over conversations with them, I tried to get a sense of where lending to FPOs is going.

The sense I got is that the enthusiasm and optimism evident a year ago, is dwindling. In overall terms, the disbursements to FPOs in 2019-20 is at a level of @ Rs 180 to 200 Crore from NBFCs and Banking system put together (I must put a caveat here, that this excludes loans to the large FPOs like the FMOs loan obtained by Sahyadri, and the credit facilities to larger Dairy FPOs, whose data I have no access to, as they are not clients of NBFCs).

Let me try and explain some of the reasons that the Lending to FPOs has been flat, or shown a downward trend during this Financial Year:

Drop in Renewals: The CEO of one NBFC commented that when FPOs that have a good record of borrowing & repayment with them do not come back asking for the next loan, it raises a red flag. Did they get better terms from other lenders (which is good) or have they fallen back on business?

Enquiries revealed a different story. Most FPOs that didn't come back for a repeat loan have been incubated & nurtured by PO promoting institutions (POPI) with support from SFAC/NABARD. As the funding support of SFAC & NABARD to POPIs tapered-off, the staff engaged by them for this activity have either been retrenched or redeployed on other activities. This has resulted in FPOs not being able to prepare business plans, and in other cases unable to negotiate the market without hand holding support of the POPI.

Add to this the lenders hesitation to lend to an FPO without a comfort letter from the POPI (to help in loan monitoring and recovery), as they no longer play an active role in FPO nurturing & support.

Overdues: Simultaneously, there have been challenges of collections with some FPOs in some regions. While everyone is dodgy with sharing details, which is understandable, this seems to have happened among some FPOs in North and Central India. If the amounts getting stuck are large, lenders shy away from the region, and FPOs are in for trouble.

Third, the on-lending to farmer-members through FPO model tried by some lenders has met with limited success due to the risky nature of the business. FPOs being poorly capitalised, cannot absorb losses, and these get quickly transmitted upward. This in my view is positive. This portfolio which was there in FY 2018-19 has now shrunk.

Also, FPOs have realised that structures such as a Term Loan with EMIs don't work for their type of business; seasonal trading operations. One FPC in Rajasthan with a turnover of Rs 3 Crore last year reached-out to Caspian, to explore whether we could offer a credit line (analogous to a bank CC limit) in place of a term loan that they had from another NBFC. While the rates at which we offer credit did not enthuse them, it was evidence that FPCs are maturing,

becoming smarter and understanding what to ask of a lender, and ready to shop around for the best deal.

Finally, is the fact that doing small loans to FPOs that are geographically dispersed is unviable in terms of costs and returns. If lending to FPOs is really in national interest, someone needs to come forward to cover the deficit in operational cost.

Have lenders to FPOs learnt lessons and changed their Strategies?

-Well yes.

First – Lenders to FPOs have realised that they need to be closer to the ground. They have recruited field officers or set up offices closer to clients, while also stopping scattered lending.

Second – There seems to be a perceptible shift from financing the FPO to Value Chain Finance – The head of FPO finance in one NBFC put it this way "We are now lending to buyers from FPOs rather than the FPOs themselves."

Third – There seems to be a realisation by the FPOs that they may after all not need all that big money to do business. The head of one large FPO promoting institution said that if a T+7-day payment cycle can be negotiated with buyers, credit will no longer be critical to growth in business of FPOs.

All these trends need greater study and understanding by policy makers & apex FPO promoting institutions, particularly considering the excitement around promoting 10,000 new FPOs. The lessons from how the business of the existing 10.000 FPOs is doing may offer valuable inputs for planning for the next 10,000.

I am of the firm belief that if an FPO does not attain a turnover of at least Rs 1 Crore within three years of commencement of business, it would be better off not promoting it, considering that the promotion cost each FPO is of the order of Rs. 20-25 lakhs.

Published on March 26, 2020

9. Why Farmer Producer Organisations (FPOs) have challenges in accessing debt, or rather, what challenges lenders face in extending debt to FPOs

Over the last few months, a Team of us at Caspian were trying to understand the FPOs Debt Market a little better, and to do that, we interacted with actors across the chain; apex promoting organisations, FPO promoting institutions, some FPOs, service providers to FPOs like warehousing & commodity managers and buyers including corporates.

Almost everyone we spoke to agrees that FPOs is a good idea for aggregation of input demand and output supply for farmers. They also agree that given a choice, they would prefer dealing with farmer collectives because it adds a Social Impact dimension to the work they do.

As of now, there are four major lenders to the FPOs, all NBFCs, and then there are others like us who also have a small FPO portfolio. While the performance of the FPO portfolio of NBFCs has been fairly good in terms of collections, and portfolio quality, growth has been slow in terms of both number of FPOs that were funded and the quantum of credit flow to the FPOs. I would not like to go into the numbers here, but make some general observations on why lending to FPOs has been challenging. The points I make are neither unique nor comprehensive, but as someone who has spent long years in rural credit can say, are clear impediments:

- First, the credit requirements are too small to be meaningful for a lender remotely located to look at.
- Second, the margins in some of the businesses done by FPOs are too small (4-5%) to be funded through credit.
- Third, the duration for which the credit is required is too small, to even cover the fixed costs that will be incurred in processing the loan.
- Fourth, the poor equity base limits the capacity of the FPO to leverage debt.
- Fifth, most FPOs transact business without coverage of insurance while handling the physical produce, a standard requirement of lenders
- Sixth, some lenders do not continue their credit relation with an FPO after a year or two without explaining why. This makes other lenders wary.
- Finally (Final only for this narration, and by no means exhaustive), FPOs trying their hand at on-lending to farmers is scary. FPOs neither have the wherewithal nor the capital to manage on-lending, even as some lenders are eager to offload their credit risk on FPOs.

Anybody with a good understanding of the Rural Credit market will recognize that it is banks with a local physical presence, the experience in handling small ticket loans, and having the ability to offer revolving credit (CC limit) who are best suited to finance FPOs. It requires them either to have the intent, or to be given a push. Both are wanting at present.

Published on February 29, 2020

10. Is FPO lending amenable to productization?

One of the key reasons for the fast pace of scaling-up of Microfinance in India was the standardisation of the loan product. This solved a large number of operational challenges such as:

i) Limiting the decision points for the loan officer to handle, thus being able to employ Xth or XII pass persons and bring down cost significantly

ii) A single product is easier for the clients to handle rather than having to evaluate options and pick from a range of products

iii) The back-end computerisation & MIS is a lot easier and less complicated when there is one product

Can a similar easily doable product be developed for Farmer Producer Organisations?

This question bears consideration because, several banks are looking at FPOs as a new business opportunity. Since this is a new space for banks and other lenders, the field staff would be looking up for guidelines on how to go about it. Also, for institutions like a bank, lending of customised small loans designed for each client on a case-by-case basis does not make sense from a business perspective, unless there is scope to go to scale.

In this context, it is good to share the experience of lenders who are already in this space. Have they been able to standardise the product?

Basically, the things to consider are:

What business does the FPO do?

Does it have some standard pattern?

Is that amenable to productization?

Do the other FPOs in the area also have a similar commodity basket and business activity cycle?

One line of business that FPOs are doing is Input demand aggregation, pooled purchase and sale or stock & sale. This is a fairly simple model. In case of a pooled order & sale model, there may be a part advance collected from the farmer, with the rest collected on delivery or at harvest or deducted from the amount payable for the commodity sold by the farmer through the FPO. There have been instances of challenges being faced by FPOs of farmers not off taking the seed or fertilizer that they indicated they would purchase due to change of choice and/or delay in supply. Either case, the FPOs have faced issues in disposal of such unsold stock and had to liquidate them at a reduced price.

On the other hand, a stock and sale model so far to my knowledge has been minimally adopted. Till such time an FPO becomes robust, trusted by members and capable, funding a stock and sale of input model will be limited.

On the marketing of agricultural produce side, tie-ups with buyers are critical to business. If there is a purchase agreement in place, funding can facilitate transactions, and provide scope for ramping-up business volumes, in case payments to farmers can be faster than other channels. In this, a lender needs to see how the downside risk is covered, particularly price risk. A fall in prices has the potential to wipe out the profit margin that the FPO has, and if it is holding on to stocks, may result in wiping out the networth of an FPO in one season.

Overall, as things stand today, it is too early for productization of FPO lending. As more lending to FPOs happen, and a credit history for the Segment is built, clear patterns may emerge, from which principles can be formulated and norms evolved. One of the prerequisites for this is the sharing of experience and more importantly, data by the major lenders to the segment (NABKISAN, Samunnati, Annanya, Banks). I do hope there would be willingness among the lenders to sharing, considering that it is not just a matter of lending, but of building a network of robust institutions that work for the well being of farmers. Until that happens, lending to FPOs will continue to be a case-by-case lending process, with gut-based decisions playing a key role.

Would be keen to know the thoughts of other working in this space, particularly if you have a contrasting opinion.

Published on March 7, 2019

11. Financing nascent Farmer Producer Organisations (FPOs)*

The process of FPO formation has now gathered steam, with reportedly over 7000 FPOs being there in the country today, thanks to the support from NABARD, Small Farmer Agribusiness Consortium (SFAC) and the Central and State Governments. Formation is the easy part. The tough job comes thereafter. How to make FPOs successful business enterprises?

It is in this growth phase that credit is a critical factor. So the next question then is; How do you make your FPO attractive for a lender? This will be my talk for today.

A lender exists to lend: For a lender, idle money in the bank is a cost. Lending it out is what makes it the money. So, what does a lender look for while lending?

Three metrics: Basically, three things; return, risk and operating cost. The returns need to be more than the cost of funds, the risks need to be at an acceptable level or covered in some form, and the cost of managing the loan needs to be recovered.

From an FPOs as the borrower perspective, the lender will want to know whether the business of the FPO is bankable. What does being bankable mean?

It is the ability to access debt, use it and then make a margin adequate to service the debt and pay back the loan when it falls due. For an on-going FPO, there may be a credit history to establish that it is bankable. But for a nascent FPO, how do we test this?

There are a few generally accepted principles of good conduct of a business enterprise that a FPC also needs to check the boxes.

- A reasonable period of existence with some business traction
- A governance structure and a system of oversight
- A business plan detailing what the enterprise wants to do
- Compliance to the regulations & laws of the land
- Transacting on the books, preferably through a bank account

Banks are the best but: Although banks are best suited to finance FPOs, due to reach (branch that is within a few kilometres of an FPO), lower cost of funds and experience with small ticket lending, their ability to understand FPOs, barring a few exceptions is limited. The institutions that are active in FPO lending are mainly three; NABKISAN, Annanya and Samunnati. Since Samunnati is represented here, you already have their perspective.

Some basic requirements for an FPO: -

- A member base with participating members
- Equity Capital
- A demonstration of the ability to do business
- An understanding of the commodity & the market
- Market linkages to buyers
- Presence & support of a promoting institution helps and adds to the comfort

- Any guarantee or mechanism in case of loss/inability of FPO to repay the loan when it falls due

Coming back to the three points raised earlier:

Loan Pricing – One of the reasons FPOs back-out from taking a loan is pricing. We charge at least 15%, and it could go to 18% per annum. The interest rate should not be seen in isolation. If the FPO can deploy the money to earn margins that are more than 15%, it makes sense to borrow. Not borrowing is a zero-sum game. You need to compare two possibilities (loan from NBFC v/s loan from a bank), instead of a possibility with an illusion (loan from NBFC at 15% v/s a loan from a bank at 10-12% that is never likely to happen).

The other point is turnover. How much business can be done with a loan of say Rs. 10 lakhs? Adding the equity to the loan if it 12 lakhs, and with a margin of 20% turnover could be 15 lakhs? No, the ability of the FPO to rotate the funds is the key. Howsoever many times it rotates, the more profit it can generate.

Market linkages: It is another key factor. If there are market linkages in place, that could be with buyers having a track record, it reduces risk and gives comfort to the lender. Holding of stocks by an FPO expecting an upside is a serious uncovered risk and could permanently finish an FPO.

Covering operating costs: Finally, if a lender has to do small loans, sending an officer for due diligence and loan monitoring, managing the account from origination to closure costs money. A Rs. 10 lakh or 20 lakh loan for an NBFC will never work. It would require an aggregate of at least Rs 1 Crore in a geography to be viable. Therefore, clusters of FPOs being lent is a way out, else a FPO promoting institution performing a BC (Business Correspondent) function and taking responsibility, including a part of the credit risk for a fee is a second option.

We must always remember that credit is not the appropriate tool for experimentation.

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*Based on the talk on 17th January 2019, at the Seminar on Agricultural Finance, as a part of Krushi Odisha 2019 organised by the Government of Odisha and Confederation of Indian Industry. Published on January 19, 2019

12. Why lending by banks to Farmer Producer Organisations is a challenge that's not going to go away so easily

The theme for this year on NABARD Foundation Day (12 July 2018) was FPOs, and one of the panel discussions was on Financing FPOs.

Dr Sudhir Goel, chairing the session raised the pertinent point of why banks were shying away from financing FPOs. There were a few thoughts shared by the panellists there, but let me try and take a shot at it from my experience & understanding.

First let me articulate why banks are the best vehicles for funding FPOs, in quick bullet points:

- Banks have access to low cost funds, and will be the cheapest as compared to any other channel like an NBFC
- It is agreed by all, that lending to FPOs is risky. However, on a large balance sheet of a bank, FPO loans will be small, and therefore a small risk.
- Banks with their network of branches in rural areas are close to the ground and this would help in interaction, understanding the business better and in monitoring the portfolio
- Agricultural business is seasonal and the farmer has a choice of when to bring in his commodity to transact. In such a setting, the best credit product for an FPO is a Cash Credit (CC) Limit that can be drawn-out for the amount and time that is necessary. This can only be done by a bank and no other financial institution.
- Cashing-out by farmers is easy, if it is connected to a local bank branch

Now let me come to the point of why bank lending to FPOs is not going to be easy:

- Like it or not, agree or not, rural banking is constrained by the absence of a specialized and trained cadre of personnel. One of the big blunders in Public Sector banking was dismantling the cadre of Agricultural & Rural Development Officers. The second of course is the way the Regional Rural Bank model was discarded so quickly. Rural branches are largely manned by promotee officers completing their statutory rural posting, aged 40 plus, living alone in most cases & commuting to work from the nearby town or city. Expecting anything much from such a workforce is futile.
- Second & more important is the potential scale that FPO lending offers to banks. It is at present too small, even in aggregate terms, and that too seasonal, to make business sense.
- Third, almost all rural branches are under-staffed and over-worked, dumped with too many programmes already, to be burdened with one more. Trying to get them to understand the creature called FPO will be formidable, and by the time the person starts to get an understanding, it would be time for him to move-on.
- Also, the training being imparted to FPOs are mis-targeted. Usually a person from the bank Head office or Regional Office is sent for training, when the work actually needs to be done by an officer at the branch. Training by NABARD is not valued, as bankers

perceive them to be ‘talking shops’ with limited practical knowledge, and most banks still not having FPO funding built into their own training curriculum.

- Further, the FPOs would not have a business plan ready for evaluation and taking a decision, The bank officer would need to help in the preparation & origination as well
- The multiplicity of agricultural commodities, the seasonal and regional variations make it impossible for productization of an FPO loan, where most variables can be made parametric, and a few inputs like crop and quantum can generate a ready to use output, simplifying the job of the loan officer.
- Finally, FPO loans require customisation, after careful study & understanding of operations in each and every case, which is expecting too much from a general cadre bank officer, from his knowledge and time perspective. Else, the risks of a loan, however small, going bad is high.

In spite of all that I have said to be the challenges, my firm belief is that Banks are, and will be the best suited institutions to fund FPOs.

Published on July 14, 2018

13. Enhancing Credit Flow to Farmer Producer Organisations

"Unless the FPOs are supported with credit, they will wither away"

-A senior banker

Small farmers in India, have inherent challenges. First, they need inputs in smaller quantum, hence miss out on the advantages of economies of scale. Then, when they are ready to sell their produce, their marketable surplus is too small to negotiate a fair deal from the market. The structure of the Indian Economy being what it is, Small Farmer will continue to be around for time to come, for reasons of lack of mobility and alternate livelihood opportunities, and the emotional attachment that people have toward their land.

The key to agricultural transformation therefore rests on the ability to capitalise on the strengths of the small farmer, rather than trying to work on his deficiencies.

On the other side, both corporates in agriculture & newly emerging new-generation players in the Agri space are keen to deal with farmers outside of the conventional channels. They however realise that dealing direct with individual farmers is impractical, and need collective structures. Farmers Producer Organisations (FPOs) are being seen as the 'missing link' to make this happen.

After a fairly slow and long start, the idea of FPOs has gained traction, and today there are over 4000 FPOs across India (NABARD data). The institutions are there now. How do we make the connections?

Capital Requirement

To operate, FPOs need capital, which the member farmers may not have in adequate measure. The options of raising funds from external investors is low due to the laws & regulations governing FPOs. SFAC has a scheme to provide equity support to FPOs subject to certain conditions. However, the conditions for equity support may not be met by all FPCs, and the amount is also limited. The next option is to borrow, but borrowing is a multiple of own funds.

Seasonal nature of fund requirement

The business of FPOs is largely seasonal, hence borrowing for the season works best. In the best of circumstances, the cost of credit may be in the range of 12%, and in agri commodities except F&V, the spreads available may not be large enough to cover these costs. While the prospects of hold & sell look good, the downside price risk is very high.

Credit Flow so far

In spite of several initiatives to promote Credit Flow to FPOs, the progress so far has been limited. The initiatives include a INR 100 Crore Loan Guarantee Fund at the Small Farmer Agribusiness Consortium to partially guarantee loans from banks to FPCs. As per information, only 36 applications have been made for availing this facility so far, and the fund has largely remained idle.

As per market information, NABKISAN, NABARD's NBFC subsidiary doing agri-finance has extended credit to @ 300 FPOs, 150 directly and the rest via on-lending through Annanya & other institutions. A reasonable guess, is that banks & all other institutions put together may have funded another 50 FPOs. All told, an optimistic estimate of Credit Flow to FPOs would be around INR 100 Crore, after adjusting for double counting.

Why has credit flow to FPOs been low, & what can be done to enhance flow to the FPOs?

Let us try to answer this question here:

1. Low Equity base – Credit linkage is a function of own funds. It can be a multiple of 4 to 6. Unless the equity base is good, the eligible loan amount will be small.

2. No market linkage – All producer members of FPOs are linked to some or other market channels. A farmer joins an FPO to explore the option of getting better prices. Unless the FPO can offer a better deal, even if small, there will be no incentive for a farmer to transact through an FPO

3. Lack of credit history

4. The credit requirements are too small to be viable for a lender

5. Weak internal processes and systems

6. Poor governance

7. Limited support of sponsor institution

While absence of collaterals to offer may be also termed a reason, most often it more a fact than a constraint.

Encouraging Credit Flow

The responsibility for being credit worthy first & foremost rests with the FPO. There is no deep science involved here. It's about doing things right, right from the start.

Here is a check-list (not complete) of what FPOs can pro-actively do to make themselves worthy suitors for lenders:

- Borrow, even if it is a small amount, even when you are small, to build your credit history to show to get larger loans when needed

- Route all business transactions through a bank account, That's one of the first rules of transparency
- Ask a lender about the criteria they use for credit assessment & do a self-test and rate yourself – not for the banker, but for yourself
- Keep your books of accounts up-to-date and publish your Annual Financial Statements in time
- Have robust Internal Control Systems in place & a functional Governance structure – simple things like dual signatories for bank accounts, monthly reconciliation of balances with the bank, regular reporting system, periodic meetings of the Board and maintenance of minutes
- Benchmark yourself against the best in class institution in the industry and emulate them
- Build partnership with a Commodity Management Company, to leverage their expertise in storage & marketing of agricultural produce. Generate synergies, and as far as possible, do not keep the commodity risk open for the FPO.
- Ensure the promoting Institution provides reasonable oversight, without baby-sitting them

Some of the things that NABARD can do are:

- Share the database of FPOs rated A & B by NABARD, with information on turnover, nature of business & banking relations so interested banks can reach-out to such FPOs.
- Prepare an Annual "State of the Sector Report on FPOs".

Suggestions for Banks:

While direct lending from your bank to an FPOs is the ideal model, in case you feel FPOs cannot be handled by your branch credit team, use a Business Correspondent (BC) model for origination & management of the portfolio, partnering with players who have an understanding of this business.

Since FPO portfolio counts as Priority Sector Lending (PSL) for banks, and NABKISAN & other NBFCs do not have a PSL target to fulfil, explore portfolio purchase as an option.

For financing of Capital Assets to FPOs, there is need to get a Term-lending institution like NCDC into the picture.

Overall, financing FPOs will continue to be challenging, because of diversity in activities, geographic dispersion, generally small ticket sizes, and likely governance and management issues. In spite of these challenges, a conducive environment needs to be created to enable well-functioning FPOs to access credit.

Published on March 20, 2018

14. Continuing the discussion on Farmer Producer Companies

"When I enter the precincts of Krishi Bhavan (The Government of India's Agriculture Ministry), I walk with my head held high. I am the Chairman of a co-operative representing a million farmers of Amul. The bureaucrats sitting there don't appreciate that. They expect farmers representatives to approach them with folded hands and heads bowed."

- Dr. Kurien, Chairman, NDDB & AMUL speaking at a Conference in 1982

I'm no expert on Farmer Producer Companies, but thanks to several institutions in the sector that I closely work with, and the FPCs and farmers I spend time with, I have a fair sense of what's happening & what's working. This is therefore a continuum on my previous piece, making a few recommendations on what needs doing. So here I go.

The recent Union Budget announcement on FPCs (Tax break, FPCs to be treated on par with co-ops for permissions & licences) have suddenly made them attractive structures, and may result in a large number of new FPCs being spawned to take advantage of the opportunity.

The challenge, therefore, will be to keep the entry barriers high enough to ensure that there is no deluge of traditional co-ops breaking the fence and rushing to migrate and become FPCs, bringing along with them all their infirmities, nor allow business interests to set-up FPCs to appropriate the benefits and incentives that come along with it.

Seriously looking at FPCs for debt funding, we realized that there are very few lendable entities; not because their turnover was low, but rather due to other shortcomings like – weak internal systems and processes, poor governance, low business-orientation and poor farmers connect of the institution. Even in cases were lending was done, there were challenges of delayed reporting, poor quality of reporting & delays in preparation financial statements, and multiple revisions of financial reports.

Institutions working towards supporting the healthy development of the Agricultural Sector through promoting FPCs for the betterment of farmers' lives need to:

1. Study successful FPCs, and de-construct the success and see what worked

2. Study the stunted and the failed FPOs, and understand the causes therefor

3. Put a hold on the 'Big Bang' plans of spawning FPCs, or slow it down significantly

4. Work on the costs and the incentives in incubating FPCs and see who can pitch-in to help cover those costs

5. Invest in building a cadre of professionals for FPOs, with adequate freedom for both FPOs & the professional on their mobility

6. Strengthen the network across institutions having shared mandate for success – NIRD, MANAGE, so that there is effective expertise built-up in each institution on one or more aspect, without duplication of efforts, and bring about strong collaboration

7. De-glamorize FPCs and let the work happen without excessive anxiety for visibility

8. Strengthen collaborations with Academics & Researchers, so they work on topics of relevance, that help feed into policy and operations and support further development of FPCs (since there are a lot of academics working in this space, sadly, mostly working on topics that are of limited relevance or utility)

9. Co-opt corporates to support the development of FPCs through CSR funding as well as in building stronger business relations.

In this way, it will be possible to build sustainable institutions that can make a lasting impact on the lives of farmers.

We should always plan for Farmers Institutions to be the best in terms of Governance, Transparency, Systems & Processes, Management Compliance to the Laws & Regulations as also have the best infrastructure & the best facilities. Indian Farmers deserve that & that is exactly what Dr Kurien desired.

Published on March 8, 2018

15. FPO Ecosystem and Credit Absorption Potential of FPOs*

Thank you Ms Sussela Chintala, CEO NABKISAN for inviting me to the Business Development Meet, and giving me the opportunity to speak on a subject that all of you at NABKISAN do on a daily basis, and of which I am more a student and observer. As someone who interacts with stakeholders across institutions and agencies, I get a panoramic 360-degree view of happenings in FPOs.

Let's start with a quick snapshot of the macro picture of the FPO landscape in the country. As of end-March 2019, there were 7374 FPCs in the country, of which 6926 were active & 448 inactive (MCA data). As on date, this number is more than 9000, and will be in excess of 10,000, if FPOs under cooperative and other legal forms are counted.

When we look at the state-wise distribution of FPCs, Maharashtra leads with 1940 FPCs followed by UP and Tamil Nadu, though MP was the pioneer in FPOs. The paid-up capital of 85% of the FPCs is less than Rs. 10 lakh.

As per data collated from the MCA database, only 5% i.e. 510 FPCs have been extended credit. Nabkisan is by far the largest lender to FPOs, followed by Samunnati. Cumulatively, 79 Banks/NBFCs/FIs provided finance to FPOs.

The credit absorption potential of FPOs is estimated at around Rs. 600 Crore. This estimate is of two years back. With Government's push to promote 10,000 new FPOs by 2024, the total credit market for FPOs will see a big jump.

The products that have been successful in FPO lending are:

- Working Capital Term Loans
- Value Chain Finance (chain may be buyer or producer or FPO)
- Term Loan for Infrastructure & Assets building
- Warehouse Receipt Financing & Pledge Loan

The loan structures that have 'not' performed satisfactorily under FPO financing include:

- FPO as an on-lending institution to farmer members
- Hold & sell with open position (FPOs with low equity capital find it hard to absorb the down side price risk).

Some broad parameters for assessing the capacity of the FPO to do business are:

- Governance & Management (Non-negotiable parameter)
- Business Orientation – Market Linkages (here, partnering with Agri- startups can be a good possibility)
- Risk Management
    - Operational Risk (tightly regulated processes are missing in the FPO ecosystem)
    - Price Risk (loan is often more than their own equity, so downside risk of stock and sell will hit the lender)

- Management Risk
- Other risks

There is a lot of opacity in the FPO lending space due to non-sharing of data by lenders. The first lender tends to treat the FPO as their 'Jagir' and wants to keep it to themselves, even if their product and pricing may not be the best for the FPO.

The following are some tips for sourcing leads:

- Know all the FPOs in your territory, even if they are not credit worthy – as they are future potential customers.
- Engage with the FPOs even if they are not looking for credit.
- Evaluation of loan should not be based on oral conversation.
- Do not rely on the desk assessment – There is no substitute for field assessment.
- Do not give advice / suggestion during the due diligence process.
- Instead, listen attentively & observe keenly.
- Share feedback with the FPOs after you are done with the due-diligence (the Interaction should be development-focused not loan-focused).

Let me illustrate the challenges FPOs face in borrowing:

1. A NBFC funded an FPC, where the loan was not structured factoring in the seasonality in agricultural operations and cash flow, resulting in the FPC having to liquidate stocks at a loss, to repay the loan on the due-date and not default.
2. A Pvt Sector commercial bank continues to lend the same Rs. 15 lakhs to an FPC after 5 years, when the FPCs turnover has grown manifold, while and at the same time showcasing it as a model FPO.
3. An agrifinance NBFC developed a loan product in consultation with stakeholders, to suit early stage, small but well performing FPOs, for Value-Chain Finance. Value Chain finance is a term that is much discussed, but hardly available to FPOs.

One of the simple ways to categorize FPOs is applying the Quality-Capability matrix.

Table: FPO Quality-Capability Matrix

Capacity of FPO to do business	**Quality of the FPO**	
	Good	**Not Good**
Capable	Ready for Lending (20% fall here)	Risky
Not capable	Need Capacity Building (40% are here)	Avoid

In my own assessment, only 20% of the FPOs have the capacity to be provided debt right away, while 40% can be extended debt if bundled with capacity building. Capacity building of FPOs need to be done on a continuous basis.
In conclusion, the following are some tips for lending to FPOs:

- While FPO is advantageous compared to conventional channels in terms of better pricing and market linkage to farmers and assured quality and quantity to the buyers, the quality/capability mix of FPOs has to be carefully evaluated while financing FPOs.
- There is generally no production risk in lending to FPOs, as financing is mostly post-production.

- There is need for positive intent and the fire-in-the-belly to achieve, in spite of underlying challenges and risks involved.
- Credit manager should be easily accessible and respond within a reasonable response time.
- In FPO financing, float is dangerous. Allowing FPOs to sit on idle cash is fraught with risk of misutilization, and unutilized cash does not generate income to service interest.
- Collateralized lending may not work in FPO ecosystem, since FPOs lack assets to offer as collateral, and deficiencies in Governance and Management can never be made-up by taking collateral to secure the loan.

Finally, I would conclude that FPOs lending should be looked at as a **"Mission Beyond Lending".** I wish you all Godspeed in this mission of building a better India. As a Director of NABKISAN, I am an equal partner with all of you on this journey.

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* Transcript of talk delivered on 05 August 2021 to the Business Team of NABKISAN Finance Ltd at the Business Development Meet at NABARD Staff College,

16. Building an Enabling Ecosystem for Farmers Producer Organisations

On the 30th of August 2019, I had the privilege of attending The Partnership Exchange organised jointly by Rabobank, ThinkAg and Access Development Services.

I also was invited to be on a Panel Session that deliberated on the current FPO landscape, the challenges that may impede their future growth and sustainability and the ecosystem building efforts needed to build the FPO model.

Being the last speaker of the last session, on a programme running overtime was a challenge, considering that a large number who spoke during the course of the day were experts, and people from the ground having rich practical experience & insights. Therefore, I made a few quick points, which I am sharing here with a little more detail, so that it reaches a wider audience.

As per the study of FPOs that we at Caspian are in the midst of, over 90% of the FPOs operate in the sub-INR 10 lakh turnover level. Almost universally, the entry-point activity of FPOs is input supply to members. There is no argument that this is a good starting point. But, input business will not enable growth of the FPO’s business, as there are slender margins. Neither does it help strengthen the Balance Sheet of the FPO. We believe, and there is enough empirical evidence to back this up, that Agricultural Produce Marketing will be the growth engine for an FPO.

However, since most FPOs have not been established de-novo, but emerged out of other development programmes of the promoting institutions, whose strength is in community organisation and social mobilisation, they lack business acumen.

This is where emerges the need and the opportunity for Agtech Startups to play a role, in bridging the gap between the producers and the consumers. We already see many such partnerships emerging, but there is need for many more players.

Corporates, for all their public pronouncements of readiness to directly deal with FPOs, have three concerns:

a. Quantity – The requirements of corporates is large, and FPOs can at best supply a miniscule quantity of what they require.

b. Timeliness – Since the produce is held by the farmer member of the FPO, and the decision on when to sell is with the farmer, the ability of an FPO to mobilise adequate quantities in time, is a challenge. Equally, FPOs have a challenge to procure from non-members or the trade to fulfil an order in time, unlike a trader.

c. Quality – Since the produce available to an FPO is from a limited catchment - the pool of stock of their members, there may be challenges in getting produce of the desired quality.

The real concern of corporates is that, if the arrangement with an FPO sours, for whatsoever reason, the reputation risk that the Corporate may be confronted with, and any likely public backlash (like the potato seed controversy a corporate went through recently) far outweighs the goodwill that they may gain from partnering directly with FPOs. We need to appreciate these genuine concerns of Corporates, and solve this challenge through the intermediation of Agtech Startups like Arya Collateral, who have the ability to deal seamlessly with both the expectations of the FPOs, and the needs of the Agri Corporates.

Finally, institutions like us, Caspian, understand that growth in the FPO business need not always be linear & incremental. The business can grow from INR 10 lakhs to INR 100 lakhs in a matter of a year, if the right enablers are in place like market linkage. Most conventional lenders especially banks do not understand, nor have the ability to deal with such a situation, but we do. Institutions with a clear FPO mandate like NABKISAN and Samunnati can meet such credit gaps, and take the FPOs into a higher growth trajectory.

We've already done that with one FPO, where an initial loan of Re 1 Crore could generate a turnover of Rs. 3 Crore, and with a step-up to a loan of Rs. 5 Crore, and another NBFC pitching-in with Rs. 5 Crore, the Farmer Producer Company could grow turnover to Rs, 25 Crore in just two years, and would have touched Rs. 40 Crore, but for some adverse external market conditions.

Such a collaborative and co-ordinated effort could easily see the emergence of over a 100 FPOs with over a hundred crore turnover in the next three years.

Published on September 2, 2019

17. Continuing the FPO Saga - Is the David and Goliath story possible with FPOs?

In the annals of history, a young shepherd boy by the name of David took on the mighty Philistine, Goliath and killed him with a slingshot.

Can the Davids of Agriculture, the FPOs take on the might of the deeply entrenched traders, the Goliaths? I give this analogy not to draw comparison, but to draw attention.

First there is really no one Goliath to fight with, like lucky David of yore, and the plan is not to finish-off the Goliaths, but identify how the upstarts in Agriculture can compete and find their turf.

Let me illustrate with one example. The total Organic Cotton sold in India exceeds the India's Organic Cotton production by a fair margin. How, you may ask can that be? Simple. Non-Organic Cotton passed-off by traders as Organic.

The end users of Organic Cotton of Indian Origin in Europe, the US and Japan among other countries are seriously concerned. For them, protecting their brand reputation is paramount. How can it be addressed?

Well, here's the story. Produce that is sourced from an FPO like Chetna Organic Agricultural Producer Company can be traced back to the Farmer. The cultural practices of the farmer can not only be ascertained, but a Farm Diary maintained by each farmer provides systematic recording of all the farm activities from land preparation to harvest. Therefore, International Fabric Brands flock to Chetna to source Organic Cotton, willing to pay a price premium. This is one space where an FPO has outsmarted the trade.

This model can be replicated in other commodities as well, and set FPOs be one-up on traders. Let's take the case of Turmeric. The additives used to make turmeric look attractive to consumers, I am told are carcinogenic textile dyes. Sourcing from FPOs can help eliminate such deadly practices. The source traceability will create trust.

I asked a senior executive of one of the largest food products companies in India, who incidentally is my classmate (no prize for guessing), why they do not translate their farmer first public talk into action, and procure the agricultural raw material they need from Farmers' Organisations.

His explanation was revealing. He said they are more than willing to procure from farmers' organisations, but their experience compels them to keep this as an 'also' source rather than the 'only' source.

One, farmers organisations are unable to fulfil the required quantities of the commodities.

Two, they do not, many times, adhere to the timelines.

Three and most importantly, they seek concessions and premiums on the grounds of being an FPO.

Let me state this clearly; for too long, the relationship of a benefactor & beneficiary has been assumed for anything to do with farmers. It is time we throw this mindset out of the window. An FPO should deal with a company, however big, as a business relation, not as charity, one of equality than of seeking favor. Only then will an FPO command the respect it deserves in the market.

Slowly but steadily, such institutions are emerging in the FPO landscape, and I am glad they are. The problem is, that the challenges in Indian Agriculture are so immense, and the need to address them so Urgent, that Rural India cannot afford to wait.

The solutions are there. Who's going to drive the Revolution is the question that begs an answer. Are you ready be that one?

Published on March 14, 2019

18. How procurement methods of FPOs help farmers (and how they are different from conventional trade)

The typical sight of a farmer anxiously waiting in the market yard with his pile of produce and bags waiting for his turn for the traders to come & bid for his produce moves many of us. Over time, a lot of improvements have occurred in the Agri Market yards trading methods, but still, farmer is at the mercy of the traders to determine quality & price.

Cut to the FPO model. What I narrate here are live, first-hand experiences from FPOs I personally work with, who trade in Red Gram, Soybean and Maize.

First, the farmer need not go to the Mandi. He can sell his produce at the FPOs collection Centre. This may be in his village, or close to it. As long as the FPO has a trade licence from the local mandi to deal in the commodity & deposits the market cess (usually 1%) for the quantum they procure, the physical transaction can happen outside the market yard. This relieves the farmer of the hassles of transport, queuing, fear of not selling and having to transport back or do distress sale etc.

The flip side in this option is that the village collection is scheduled by the FPO on pre-agreed dates, so if farmer wishes to sell to the FPO, he needs to sell on one of those dates. If the farmer anticipates price to go up and wants to sell later, the choice may not be there.

The Procurement Pricing by the FPOs is usually market linked (with the previous day closing prices as reference) with a discount to cover costs incurred by FPO & a margin. In case they are procuring for FCI/NAFED, then it would be at MSP.

No rush & anxiety: Unlike in the market yard, the farmer need not rush and have anxiety when dealing with the FPO.

Sampling & Testing: Testing is done by the use of a moisture meter and physical testing, by hand picking a random sample and segregating the good seed, brokens, shrivelled, discoloured, infected seed and foreign body, mud, dust etc. After testing a sample of the produce, it is weighed & re-bagged and taken by FPO.

If the commodity quality is not within acceptable range (humidity high, more than acceptable level of brokens, discoloured, foreign bodies etc.,), the farmer is given a choice of moving his produce to the drying area and sun-dry to bring down the moisture level. Provision of a sieving machine is also available to sieve the produce again, for bringing down the level of items that cause quality downgrades and price reduction.

Reduced loss in weighment & bagging: One of the advantages to farmers by selling through the FPO is that the spillage while being procured is reduced. This is because in the market yards, the market convention is that the Hammali (manual labour) get to keep the produce that spills on the ground. Due to this, often the labour deliberately increase handling losses.

Faster payment, mostly on-line: Just like others, FPOs have largely moved to electronic payments to farmers. However, there are serious issues of bank branches ability to cash-out the payments. They usually delay or limit the daily cash withdrawal from an account. During the Demon crisis, the FPOs paid in cash to farmers which was a great relief.

Premium / Price Differential/ Patronage Bonus: Unlike sale in the market, the transactional relationship is not completed on physical handing over of the produce and the farmer receiving the payment. The produce is loaded in the truck in identifiable lots indicating the source of origin. If weight at reception dock of the buyer/ processor is more than the weight recorded at the PCs procurement centre, the benefit is passed on to the farmer. If on the other hand there is a shortage, which also sometimes could happen, it is absorbed by the PC.

Overall, working closely with farmer-centric FPOs over seasons, I have seen that apart from fairness, transparency and being treated better, weighment & payment practices of FPOs have ensured a 5 – 9% better realization over conventional channels.

Published on April 9, 2019

19. Strengthening Farmer Producer Organisations*

The process of formation and nurturing of FPOs broadly happens in three stages viz., Incubation, Emergence & Growth, and Maturity.

In the Incubation stage, the activities of the FPO revolves around mobilizing farmers, registration, operations and management, training, exposure visits, etc. Accordingly, the agencies engaged in promotion of FPOs require grant support to set up FPOs, take them through the various systems and processes, including governance and self-management. Post incubation, the business potential of the commodities being produced by the FPO's members needs to be assessed. The requirements of the FPOs beyond Incubation stage include, among others, equity, credit and market linkages.

Market Linkage

The various channels through which FPOs can be market linked are; direct to consumers, direct to corporates and reaching market through intermediaries.

While direct marketing is difficult, due to issues such as low volumes, lack of brand image and brand connect with customers, reaching market through corporates has another set of problems, such as maintenance of quality, quantity and adhering to delivery timelines on a regular basis, which could be tricky for new FPOs. Therefore, the FPO may have no choice but to go through intermediaries in the trade, by moving up the chain, by passing some layers, and dealing with the larger aggregator.

The other risks associated with the FPO model of aggregating produce from its members and holding for direct sale in the open market / to intermediaries are; price risk (especially when there is a bumper crop and glut in the market) as well as, risks related to theft/ pilferage during storage.

Addressing basic post-harvest interventions can add value to a smallholders producer, whose value erosion is estimated at anywhere between 25-40% at present.

For long-term sustainability of FPOs, they need to be seen as viable business enterprises and agri-business start-ups. Corporates need to look at FPOs as business opportunities rather than as CSR projects, and step-in with processing, warehousing and logistics infrastructure in the commodity value chain.

Convergence with big retailers, processing units, agri corporates, agro processing units, e-market platforms, etc. will facilitate seamless market access and better price realization. A few models of FPO market tie-ups such as by Arya Collateral, Safe Harvest, Chetna Organic and Bangalore Greenkraft, among others were presented.

Credit Linkage

As the FPOs begin business activities such as bulk purchase of inputs,working capital is required. Though the FPOs, at this stage, are expected to have garner a reasonable level of own funds, it takes anywhere between 3 to 4 years for an FPO to stabilise, and be able to raise funds.

Most FPOs in this stage of their lifecycle struggle to get credit, and without access to credit, the FPOs cannot realize their full business potential. As the FPOs scale up their operations, they need finance for setting up the value chain of the produce. Term loans are required to build infrastructure like processing unit, processing/ grading/ sorting yard, storage godowns, cold storage, transport facilities, etc.

While financing FPOs, lenders look for accurate, timely and transparent financial statements, strength of Balance Sheet (Equity/ Net Worth), capacity to do business, governance, management, member participation, credit history and reputation. It is important that the FPO being considered for lending has sufficient credit absorption capacity while giving loan, otherwise the loan will be a bane rather than boon for the FPOs.

The major FPO lending models in the country are direct by banks (very few), banks with SFAC/ Rabo Guarantee and lending by NBFCs (both direct and indirect). The major institutions engaged in FPO financing today are, NABKISAN, followed by Annanya Finance, Samunnati, NABFINS, and a few banks and NBFCs. Based on informed guesstimates, during FY 2017-18, 320 FPOs have been financed in the country, with a total disbursement estimated at ₹160 crores. Some of the major issues faced in lending to FPOs is inexperience of FPOs in managing funds, non-fulfilment of covenants, repayment delays, ability to monitor small loans that are widely dispersed, and language concerns.

Capacity Building

Capacity building in FPOs should not only be focused on CEO/ Board Members of FPO only, but should also educate Members on rights and duties and commodity specific interventions. Alternate methods to impart such inputs should be tried, in place of lectures, such as short videos, field demonstrations, and visits, to better capture the imagination of the target audience to the possibilities of the FPO structure.

The institutions engaged in capacity building of various aspects of FPOs include, National Skills Foundation of India, NIRD, APMAS, MANAGE, NAARM, BIRD, Vrutti, IRMA, Arya Collateral, DHAN Foundation, MYRADA, ASA, etc.

FPO Lineage

FPOs in their lineage could be bucketed into three types, viz. family-based, institution-based and member-driven. FPOs most likely to succeed in the long run would invariably be member-driven.

It is quite evident that one model will not be suitable for all commodities and regions. Also, a federated FPO structure may become burdensome and bureaucratic and add to costs, without adding much value. With a view to ensure profitability and long term sustenance of FPOs, various models need to be explored and customised based on adaptability to local conditions, with market linkage and credit linkage forming two cornerstones of the entities.

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* Highlights of a talk on ‘Strengthening Farmer Producer Organizations (FPOs) in Andhra Pradesh’, delivered on 22 June 2018 to the District Development Managers and officers of Andhra Pradesh Regional Office of NABARD at Hyderabad.

Published on June 29, 2018

20. Farmer Producer Companies as vehicles for Farmer Emancipation

The idea of a Farmer Producer Company has been around for over three decades now. In fact, for those of us who worked closely with Dr Verghese Kurien in NDDB, he spoke about the idea of Cooperative Companies as early as the early 1980's. From an initial hesitant start, the momentum has picked up, and the FPC movement seems to be on the verge of overshadowing the SHG movement in the development sector. The number of FPCs across the country, as per information gleaned by me from various sources has crossed 4000, but more than the numbers, the attention that FPCs as an idea is getting, is disproportionate as compared to possibility.

I would like to mellow down the new-found excitement about FPCs by asking, are we betting on the wrong horse? Are we expecting too much from FPCs?

I speak not as a distant observer of FPCs, but someone who has been associated with FPC from the time when there were so few that they could be counted on one's fingers, and when most current evangelists of FPCs may not have heard of FPC.

Let me briefly list some of the continuing challenges that FPCs face:

To the Registrar of Companies, the FPC is just another form of a company. Therefore, the cost and burden or reporting is disproportionately huge, as the rules are the same as what would apply to a MNC. The Institutions that championed the cause of FPCs have been crying hoarse about the need for a lighter regulatory & reporting regime for FPCs. Thus far, this issue has not received attention. Unless that is done, the risks that farmer directors face are serious. Any reporting shortfalls or violations attract huge fines.

Promoting a PC is the easiest part. But the question is, what promises are you making to the farmers when you make them members? Assuring that a PC will offer a better than market price is difficult to fulfil, and equally so any commitment to accept all that a farmer member produces.

Lack of capital to scale-up business is a serious challenge. The regulations do not allow non-participants in the business to be shareholders, and the participating farmers do not have the kind of capital to capitalise a company.

The FPC has to conduct 100% clean and transparent operations, compared to a trader who operates in an opaque manner. Hidden costs in dealing with a trader include, the need for a farmer to go to him, provide the bags free, weighment discrepancies, payment delays, spillage losses, and arbitrary quality deductions.

Trading in agricultural commodities even with forward purchase contracts are fraught with uncovered business risks, as we have seen with large turnover FPCs this year.

With all kinds of effort, it may be possible to increase realisation to farmer of 2.5 to 5% over current market prices & they can be bettered in future.

Overall, in my opinion, FPCs can be one among the several pieces in the puzzle that need to fall in place, to transform Indian Agriculture and improve the lot of the Indian Farmer. Trying to hype FPC as a potential transformational tool is premature, and needs to be taken with a lump of salt.

Published on March 1, 2018

Epilogue

My entry into the FPO space was accidental, inspired by my boss, Shri HR Khan, the then Principal, Reserve Bank of India's College of Agricultural Banking, Pune, where I served as a Faculty Member, who encouraged me to delve deeper into this interesting area in the year 2006, which culminated in my writing an article, **Producer Company Model – Current Status and Future Outlook – Opportunities for Bank Finance,** published in 2008**,** which still remains a seminal work on the subject, having over 50 citations.

Either it was I who fell in love with FPOs, or the FPOs with me, or it was mutual, but my fascination for the subject grew with time, and I stayed connected with FPOs long after my official posting took me to other spaces. I kept getting invitations to speak/do advisory/consulting work in the subject, which I tried making space for, in my work routines. I was so passionate about the subject, being one of the few who had a panoramic view of the sector, and each opportunity to study/speak added to my pool of knowledge on the subject, and gain new insights.

It's has been a journey of continuous learning, and I would burn with guilt if I just kept these insights to myself. Writing articles on LinkedIn turned-out to be the perfect forum to present my thoughts. The writings attracted the right audience, and I would encourage readers to look for the articles on LinkedIn, because the comments and discussions that followed some of the articles I wrote are much richer and insightful than my own writing. People such as the ex-MD SFAC, and Ex-DMD NABARD who played critical role in building the FPO programme, but have not written on their experiences commented, which gives unique insights not available anywhere else.

I have not just written about FPOs, but funded them, such as Masuta, Bangalore Greenkraft, and Chetna Organic while as head of Operations at Maanaveeya . At Caspian , our portfolio includes Chetna Organic and Jharkhand Women's Poultry Cooperative Federation. I am also on the Advisory Board of DevBhumi FPC in Uttrakhand. At the request of GIZ, we at Caspian put together a **Guidebook on Lending to FPOs**.

Possibly because of my interest in this space, Chairman NABARD invited me to join the Board of their subsidiary, NABKISAN as an Independent Director, which I am, effective August 2021, adding to my engagement with the sector.

I would continue to be a student and practitioner in this space, but my intent of writing has always been to attract more researchers to this space, and inspire practitioners to document and share their experiences. If I can achieve that in even in a small measure, I will be happy that all my effort has borne fruit. This has been my humble contribution to building the Sector. I remain always available to do more.

Finally, I am grateful to IRMA, my Alma Mater and Professor Shambu Prasad, for offering to compile my writings on FPOs and publish them as a compendium during the Centenary Celebrations of Dr Kurien. I hope this will help reach my writings to a much wider audience. My epilogue will be incomplete without expressing my immense gratitude to RBI, NABARD and Caspian who generously extended to me the time, space, resources and support in generous measure.

Emmanuel Murray
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