THE NIGERIAN INCENTIVE-BASED RISK SHARING SYSTEM FOR AGRICULTURAL LENDING (NIRSAL)

1. INTRODUCTION

The agricultural sector is central to Nigeria's economy, accounting for 40 percent of the Gross Domestic Product (GDP) and providing over 60 percent of employment. However, the sector represents only 1 percent of exports. Over the last decade, agricultural growth has slowed down and today it is under-performing despite enormous potentials. To reverse the trend, there will be need to tackle some of its major challenges such as low productivity, poor technology and cultural practices, low research and development, and under-financing of the agricultural value chain.

In particular, funding level in the agricultural sector stands at about 2 percent of the total lending of banks as against 6 percent in a country like Kenya. Some of the reasons for the low funding include lack of understanding of the agricultural sector, perceived high risks, complex credit assessment processes/procedure and high transaction costs. Addressing these issues require an innovative approach, hence the introduction of the Nigeria Incentive-Based Risk Management System for Agricultural Lending (NIRSAL).

2. THE NIRSAL CONCEPT

NIRSAL is a dynamic, holistic approach that tackles both the agricultural value chain and the agricultural financing value chain. **NIRSAL does two things at once; fixes the agricultural value chain**, so that banks can lend with confidence to the sector and, **encourages banks to lend to the agricultural value chain** by offering them strong incentives and technical assistance. NIRSAL, unlike previous schemes which encouraged banks to lend without clear strategy to the entire spectrum of the agricultural value chain, emphasises lending to the **value chain and to all sizes of producers**.

There are five pillars to be addressed by an estimated USD 500 million of CBN money that will be invested as follows:

- **Risk-sharing Facility (USD 300 million**). This component would address banks' perception of high-risks in the sector by sharing losses on agricultural loans.
- **Insurance Facility (USD 30 million).** The facility's primary goal is to expand insurance products for agricultural lending from the current coverage to new products, such as weather index insurance, new variants of pest and disease insurance etc.
- **Technical Assistance Facility (USD 60 million).** This would equip banks to lend sustainably to agriculture, producers to borrow and use loans more effectively and increase output of better quality agricultural products.

- **Holistic Bank Rating Mechanism (USD 10 million).** This mechanism rates banks based on two factors, the effectiveness of their agricultural lending and the social impact and makes them available for the public.
- **Bank Incentives Mechanism (USD 100 million**). This mechanism offers winning banks in Pillar four, additional incentives to build their long-term capabilities to lend to agriculture. It will be in terms of cash awards.

3. CROP VALUE CHAINS AS PILOTS

In the first instance, six pilot crop value chains have been identified based on existing crop production levels and potentials in six high-potential breadbasket areas. The crops are:

■ **Tomatoes**	■ **Soya beans**
■ **Cotton**	■ **Rice**
■ **Maize**	■ **Cassava**

4. NIRSAL TARGETS:

- Generate an additional USD 3 billion of bank lending within 10 years to increase agricultural lending from the current 1.4 to 7 percent of total bank lending.
- Increase lending to the "pooled" small farmer segment to 50 percent of the total (typically, banks do not reach these producers individually but through "pools", i.e., aggregating mediators, such as MFIs and cooperatives).
- Reach 3.8 million agricultural producers by 2020 through pooling mechanisms such as value chains, MFIs, and cooperatives.
- Reduce banks' break-even interest rate to borrowers from 14 to 7.5-10.5 percent.

5. IMPLEMENTATION

NIRSAL and its five pillars will be administered by a Non-Banking Financial Institution (NBFI.) At the national level, the NBFI will administer the five NIRSAL pillars. It will report to a Board of Directors chaired by the CBN and memberships from AGRA, the Ministries of Agriculture, Finance, and Commerce and Industry. The Board will have ultimate decision-making and strategy-setting responsibility for the Fund. The CEO of the NBFI will be responsible for NIRSAL's overall implementation and for maintaining relationships with key stakeholders. At the regional levels, Regional Transformation Engines will administer NIRSAL, through Portfolio Investment Managers and a Technical Assistance Representatives.

6. CRITICAL SUCCESS FACTORS

- Financial support from the Ministry of Finance, state governments and donors to fund the insurance and technical assistance facilities.

- Policy reforms such as:

- Deregulation of the agricultural insurance industry to open access to private insurance companies and pave the way for innovation.
- Shift the fertiliser subsidy from a focus on consumption subsidies to production subsidies and private sector-led fertiliser import system.
- Increased liberalization and competition in foundation seed production and marketing.
- Establishment of staple crop-processing zones to drive import substitution, buoyed by tax breaks stoppage of imposition of import tariffs for agricultural equipment.

- Functional, effective and efficient implementation arrangements and institutions.
- Comprehensive stakeholder buy–in and support.

7. BENEFITS OF THE NIRSAL INITIATIVE

- **Central Bank of Nigeria:** Increased lending to agriculture from 1.4 to 7 percent of total bank lending within 10 years, increased income, GDP, foreign exchange earnings and the implication on the Bank's ability to manage the value of local currency, lower food inflation and maintain monetary robust external reserves as well as monetary stability. In addition the project will absolve the Bank of the need for endless and voluminous subsidies to the agricultural sector.
- **Banks:** Opportunity for capturing latent profits in agricultural lending, maintain long term human, institutional and cultural capacity for value chain financing capacity and enjoy lower loan origination and distribution costs.
- **Agricultural producers**: Increased access to credit, enhanced adoption of better cultural and agronomic practices, use of improved inputs like seeds and fertilizers, increased productivity and profit, income, standards of living, job creation and poverty reduction.
- **Ministry of Agriculture:** A stronger agricultural sector with six showcase value chains, enhanced food security, fewer imports, and higher productivity.
- **Ministry of Finance:** A stronger economy with additional agricultural GDP growth, higher employment, reduced expenditure on food imports, higher tax revenue from the agricultural sector, competitive exports and a more diversified economy.
- **State governments:** An improved agricultural economy at state level creating more employment, less poverty, enhanced food security and higher tax revenue from a better-performing, well-financed sector.