



A Take on Marine Outgrower Schemes in the Pacific

IQ
Q4 2019

IKIGAI QUARTERLY

In this issue we analyse the possibilities and pitfalls of marine outgrower schemes to create sustainable income for coastal communities in the Pacific.

We hope this report shares a perspective on innovative business models and financing mechanisms for coastal communities and smallholders in general, such that it can be applicable to your work in the Pacific or elsewhere.

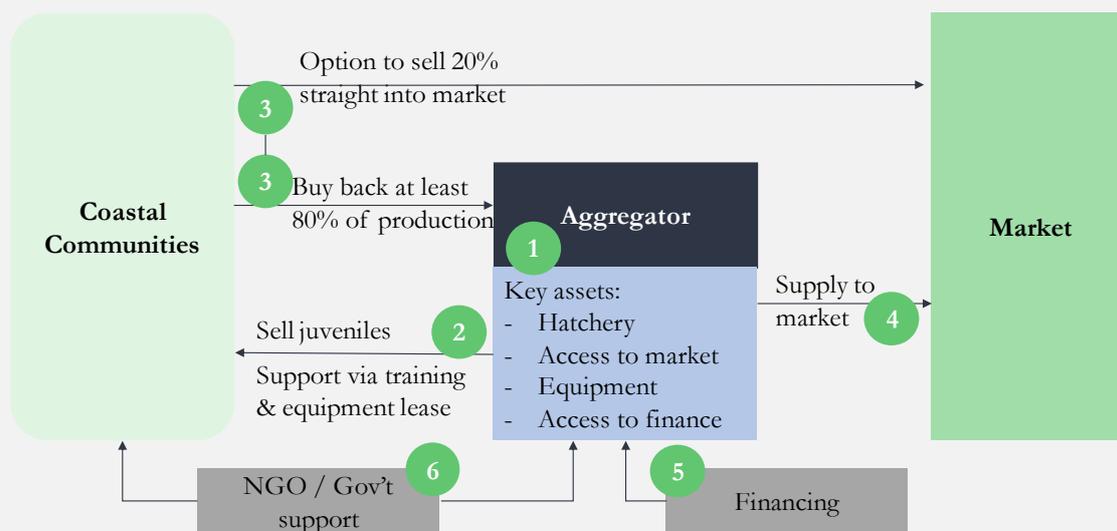
Background

- ❖ Small-scale fisheries contribute about half of global fish catches.
- ❖ Global wild catch production has levelled off since end of the 1980's, while growth in production has been driven by aquaculture.
- ❖ In the Pacific coastal fisheries are negatively affected by habitat degradation, which occurs from destructive fishing practices, pollution, siltation from mining/logging, urbanisation etc.
- ❖ Sustainable small-scale and community driven aquaculture appears to be one of the ways to address the growing pressure on reef ecosystems and secure sustainable livelihoods.
- ❖ Co-operatives and outgrower schemes are a traditional way of addressing some of the challenges smallholder farmers and fishermen, such as access to market, finance and technical capacity.
- ❖ This document summarizes some of the economic and financial opportunities and challenges for marine outgrower schemes in the Pacific, leaving the analysis of their ecological and social sustainability to the respective specialists.

**“In the
beginner’s mind
there are many
possibilities,
in the expert’s
mind there
are few”**

**– Shunryu
Suzuki**

Conceptual Summary



1. The value add of an Aggregator is mostly in concentrating technical and financial capabilities, which might have been too difficult to distribute into communities. Especially for high value-added products (pearls, edible oysters, bêche-de-mer, giant clams etc.) very specific and often proprietary knowledge is required within the hatchery to keep mortality rates low.
2. Providing juveniles to communities to outgrow can be paired with according training and lease of any necessary equipment. Selling rather than giving away the juveniles for free to the community ensures communities' vested interest in the scheme. Communities inability to purchase the juvenile can be overcome by a mixture of small give-aways and phasing-in volumes over time.
3. When ready-to-market production is bought back from communities it is possible to leave a certain percentage (e.g. 20%) for free market sale, providing the communities upside from direct market sales, while ensuring the secure offtake for most of their production.
4. Aggregating from multiple communities enables the steady supply to market, as well as accessing larger off-takers and export markets. Cutting out middlemen is to support margins for communities and the Aggregator.
5. Financing any necessary equipment and working capital appears more efficient on an Aggregator level rather than individual community level. Better financial management capabilities, and higher lending volumes (which decrease relative transaction costs) are some of the key drivers for lower cost of capital. Financing a larger single entity also opens possibilities for financial structuring, e.g. blended finance.
6. NGOs and government are traditionally supporting communities in managing their marine resources and creating alternative livelihoods. With the presence of a technically advanced player as the Aggregator their role is likely to shift to creating appropriate safeguards and potentially providing appropriate incentives to the Aggregator and third-party stakeholders affecting the communities (e.g. polluters).

Potential risks and mitigation strategies:

- ❖ **Negotiation power of Aggregator over communities:** probably the highest socioeconomic risk to the outgrower scheme is the Aggregator's negotiation power over communities, enabling them to potentially squeeze communities' margins. Price regulation is one way of dealing with the matter, however, there are numerous examples of circumvention of regulation (e.g. deep discounts for any product below prime quality). We believe the ownership and governance of the Aggregator are a more effective tool to create safeguards around the Aggregator's dealings. For example, partial ownership by an NGO or an impact investor can influence the Aggregators' articles of association and business conduct.
- ❖ **Quality and quantity of production:** Ensuring a steady quantity and quality of production is key to accessing markets. Diversification between communities largely de-risks variations in quality, however, introduces the complexity of quality control. Achieving consistent quality may be partially created through price incentives for high quality products, however, will largely depend on technical support and training provided to the communities.
- ❖ **Weather risk (especially hurricane risk):** extreme weather conditions have destroyed entire harvests in the past. Transferring crop insurance to marine production or creating a simpler parametric insurance product may be able to largely address such risk. Like attracting financing, insuring on an Aggregator level will decrease transaction costs. The insurance premium will need to be built-in into the pricing mechanism between communities and the Aggregator.

Recommendations for implementation:

- ❖ Numerous livelihoods projects have failed because they have mostly focussed on the production side. In our view finding the right market opportunity (i.e. "product-market-fit") should be primary area of focus.
- ❖ "Middlemen" have been providing access to communities, while possibly leveraging market inefficiencies to their benefit. Studying their role might enrich the understanding of existing supply chains and open possibilities for their inclusion in a more equitable supply chain.
- ❖ Basic blended finance is likely to go a long way. Public and philanthropic funds can be used (as they have been) to build communities' capacity in the context of the outgrower scheme. Concessionary capital could not only improve profitability to the Aggregator and communities, but also "buy" good governance
- ❖ More specific blending strategies could be applied to take out certain low-cost-high-impact risks – weather insurance, commodity price hedging, FX hedging (if applicable).
- ❖ The value of the hatchery and associated know-how increases disproportionately with the value of the end-product – unique hatchery skills can be the differentiator of the entire business model.
- ❖ The ownership and decision making of the Aggregator is likely to be a key driver for the outgrower scheme's social and environmental sustainability. Increasing community involvement and ownership in the Aggregator over time (in line with their improving capacity) provides incentives for communities and exit options for investors with fixed investment horizons.

Reach out and share your thoughts

- Was this document thought provoking?
- Do you have questions or comments?
- Is this concept applicable to your work?

Drop us an [e-mail](#) and let us discuss!

