

Norfund

DEVELOPMENT IMPACT
CASE STUDY



MARGINPAR GROWING PEOPLE GROWING FLOWERS

ABOUT NORFUND

Norfund is Norway's Development Finance Institution. Our vision is to create jobs and to improve lives by investing in businesses that drive sustainable development. We invest in business areas and countries in which we can have the greatest impact, where support from the private sector is weak, and where access to capital is scarce. Norfund therefore prioritises the following business areas: Clean Energy, Financial Institutions, Green Infrastructure, and Scalable Enterprises in Agribusiness and Manufacturing.

SCALABLE ENTERPRISES

AGRIBUSINESS & MANUFACTURING



DEVELOPMENT RATIONALE

Larger companies are engines for growth and job creation because they are more productive, recruit more staff, and pay higher wages than smaller companies.* Investing in scalable, sustainable businesses and helping them to grow can create jobs, generate government revenues, and provide needed goods and services. These investments are central to achieving the Sustainable Development Goals.

Few countries have developed their economies without developing a strong manufacturing base. In Africa, one-third of food, beverages, and similar processed goods are imported, but a large share of these products could be manufactured locally. Manufacturing in Africa therefore has tremendous potential as an enabler of economic growth and transformation.

The agribusiness sector is especially vital for economic growth and job creation in Africa, because it is labour intensive, and demand from local suppliers and local smallholder farmers is high.



INVESTMENT NEED

Investments are needed throughout the value chain. However, agribusinesses and manufacturing companies in Africa often find it difficult to attract investors and access credit. Development Finance Institutions that are willing to take risks are strongly needed in this sector.



NORFUND'S STRATEGY

Norfund invests directly in scalable enterprises within agribusiness and manufacturing, and through funds.

Our direct investments are focused on opportunities in the Sub-Saharan Africa region, and through partnerships with strong industrial or financial partners.

Norfund's investments are also made through private equity and venture funds that invest in scalable enterprises in our strategy countries.

* McKinsey, 2016; AfDB, 2019

CASE STUDY

MARGINPAR

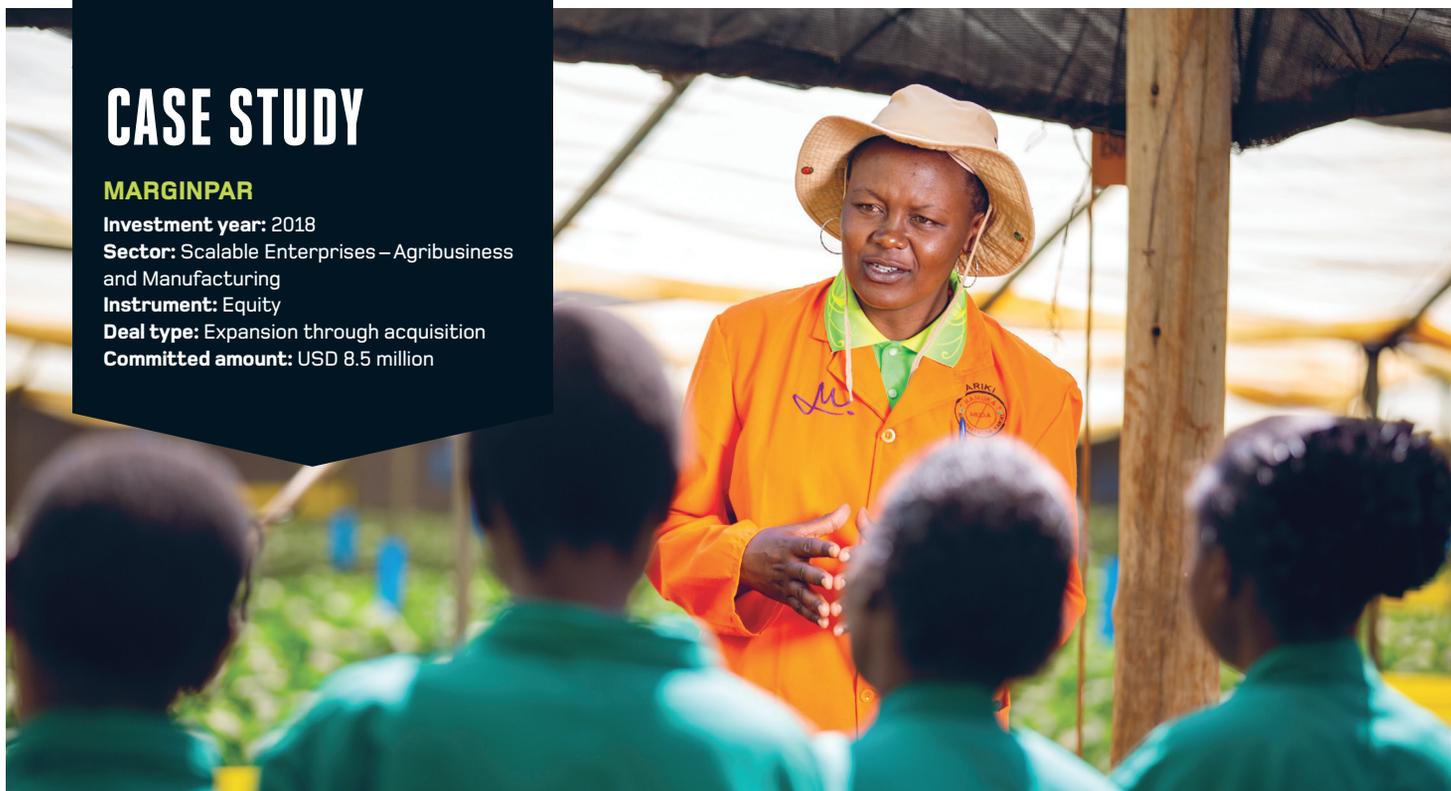
Investment year: 2018

Sector: Scalable Enterprises – Agribusiness and Manufacturing

Instrument: Equity

Deal type: Expansion through acquisition

Committed amount: USD 8.5 million



Teresa Karemi started her career working in the flower fields with harvesting. She is now an Assistant Production Manager. Photo: Sala Lewis

GROWING PEOPLE, GROWING FLOWERS

The climate in East Africa is well-suited to flower production, and the potential for growth in the sector is high. Norfund's investment in Marginpar enabled the acquisition and development of several underperforming farms in Kenya and Ethiopia which have secured decent jobs.

Kenya is a lower middle-income country (LMIC), as defined by the OECD. Despite the country's impressive economic growth, forty per cent of Kenya's population lives in extreme poverty, and those in the poorest 10 per cent of the population earn less than 2 per cent of the national income.¹

INVESTMENT CONTEXT

Kenya's population is expanding by one million people each year, and the country's median age is now 18. This substantial youth population will be important for sustainable development strategies that are aligned to SDG 8 – Decent Work and Economic Growth.²

Each year, one million people join the workforce in Kenya. However, only one in five people are likely to find formal employ-

ment. Most will either be unemployed or engaged in non-wage-earning occupations. Generating jobs for the rapidly-expanding youth population is therefore essential.³

Creating jobs in the private sector

Creating jobs through private enterprises, especially in manufacturing and agribusiness, is a central focus of the Kenyan government's Big Four Transformative agenda.⁴ Private sector development is one of five key priority areas in Norwegian development policy.⁵ Norfund invests in Scalable Enterprises and supports the growth of the private sector by developing strong, sustainable private enterprises.

MARGINPAR

The Marginpar Group is a vertically integrated flower producer which has farms in Kenya and Ethiopia, and a sales and distri-

bution company based in Holland. The company was formed through the acquisition by the Kenyan flower producer Kariki, of the flower producers Carzan Flowers in Kenya, Marginpar Ethiopia, and of Marginpar BV in Holland. The acquisition was facilitated by risk capital provided by Norfund and the Agri-Vie Fund II (an agri-business fund in Sub-Saharan Africa).

Initial screening

Norfund's initial screening of Marginpar revealed a close alignment with our strategy, and with our sectoral and geographic priorities. Floriculture is a major employer in East Africa, and the growth of floriculture in this region help create more jobs. Marginpar is an agribusiness which covers the value chain from breeding to distribution of flowers. The success of the Kariki business model also fitted well with our Scalable En-



Norfund's investment in Marginpar is mainly directed to operations in Kenya, but a small part of the investment has been allocated to the farm in Ethiopia. The map illustrates which flower producers owned the farms before the acquisition. All the farms are now part of Marginpar.

terprises strategy because of its potential to be applied at Marginpar's other farms.

Additionality is a central part of Norfund's mandate. Norfund is financially additional when investing in an entity which cannot obtain finance from the private capital market with similar terms or quantities due to high risk. It also applies if the investment supports capital-constrained markets and if it mobilises capital from the private sector that would not otherwise have invested. Norfund is value additional when offering non-financial value to companies. We do this, for example, by providing or catalysing knowledge and expertise, help to promote social or environmental standards, and foster good corporate governance.

Norfund's approach to additionality was refined in 2018 to ensure alignment with the OECD definition of additionality.⁶ Norfund's ambition on additionality is fulfilled through this investment which met seven out of ten additionality criteria.

Investing in these geographies and this sector poses financial risks and challenges. Marginpar found it difficult to attract aligned investors to finance the acquisition of the distressed farms. Companies operating in the flower sector are faced with a range of commercial and operational risks, such as high price fluctuations, environmental risks and social risks, the latter due to the labour intensive nature of the operations. In addition, climate change presents new high-risk exposures

AMBITION		
Financial	Investing in poorest countries	
	Investing in capital constrained markets	✓
	Investing in risky markets	✓
	Investing in difficult business environments	
	Providing scarce capital	✓
	Contributing to starting new business activity	
	Mobile private investors	✓
Value	Taking an active role in investments	✓
	Promoting social and environmental standards	✓
	Supporting enterprise improvements	✓

and unpredictable weather, which can result in production losses.

Due diligence

Norfund, in collaboration with Agri-Vie, conducted a due diligence of Marginpar. This included visits to the company and its farms, documentation reviews, and discussions with the management of Marginpar and Agri-Vie. Consultations also took place with key stakeholders, such as employees, management, people in the communities surrounding the farms, and experts in the flower sector.

The commercial due diligence process was conducted using an external consultant who had experience in floriculture value chains. The legal due diligence was conducted by a Kenyan law firm, and confirmed that the company had the required operational permits and licenses, and that the ownership and shareholding information supplied by Marginpar was correct. Norfund and Agri-Vie conducted a management, corporate governance and financial due diligence. Due diligence process on environmental, social and governance issues were done in accordance with the International Finance Corporation's (IFC) Performance standards – an international benchmark for identifying and managing environmental and social risk.⁷

The findings from the due diligence convinced the team in Norfund to proceed with the investment to Norfund's Investment Committee, even though the process revealed considerable commercial and financial risks.

NORFUND'S ROLE IN MARGINPAR

In 2018, Norfund allocated USD 8.5 million in equity to enable this acquisition, which resulted in the creation of the Marginpar Group. The merged company needed strong institutional owners and patient capital to ensure long-term growth.

Before the acquisition, the long-term financial sustainability of Carzan Flowers in Kenya, and the Holeta farm in Ethiopia was uncertain. In contrast, the Kariki farms in Kenya were highly productive, using a business model that relied on strong management and traceable yields and results. The Kariki company saw an opportunity to acquire the farms and to make a turnaround by introducing their own successful business model, including the implementation of the Kaizen model.

The results of the acquisition are best seen at the Rongai farm, which was the first farm to implement the Kariki model. Farm managers from the Kariki farms were employed at Rongai to secure good implementation of their business model and the Kaizen model. Although the turnaround has taken longer than expected, partly due to external factors, such as a hailstorm and diseases that required replanting of flower crops, the investment is starting to show positive results. Productivity and yields at the farm are improving, and financial returns have turned positive.

Implementing the Kaizen model in Ethiopia

Norfund offers grant funding to portfolio companies through its Business Support Facility. This is an important tool for practicing active ownership and further enhancing the development effects of our investments. Norfund and Marginpar recently entered into a contract in which Norfund is responsible for co-funding the implementation of the Kaizen model on the Holeta farm, with 680 employees, in Ethiopia.

Strengthening corporate governance

Together with Agri-Vie, Norfund is focusing on Marginpar's development, implementation and monitoring of corporate governance. Norfund is represented on the company board enabling us to influence on developing Marginpar's group strategy and corporate governance. Norfund is also contributing to improvements in the company's reporting, the tracking of its KPIs, and the



KAIZEN – CONTINUOUS IMPROVEMENT

Kaizen is a Japanese method of working to create a culture of continuous improvement in order to increase productivity. The method emphasises active engagement of all workers, called value-adders in Marginpar. In the Kaizen method, employees are trusted, valued, and empowered.

Kariki was the only flower producer that practised the Kaizen method before the acquisition. After the acquisition, Marginpar has implemented Kariki's Kaizen model at other farms. This involves tracking productivity and sharing information with employees through visualising progress. This is expected to provide the same level of operational excellence as already experienced in Kariki, and give an increase in productivity and worker satisfaction.

Many workers at Marginpar began their careers as non-skilled workers and have since become managers. Priscillah Muhonja, for example, started as a value-adder. She progressed from working as a harvester, to being a post-harvest manager at the pack house at the Nanyuki farm. She explains that the communication between value-adders and managers has improved significantly because of the implementation of the Kaizen system. Value-adders are encouraged to present ideas on how to improve production. They work together in small teams to improve and sustain operations.

"When there is a problem in the production, we do not ask 'who', we focus on the process and look for the root cause", says Muhonja.

employment of key personnel, such as Environmental, Social and Governance managers on the farms.

Enhancing environmental and social performance

Ensuring that companies adhere to the IFC's performance standards on environmental and social sustainability is an integral part of Norfund's work. Prior to Norfund's investment, all the flower farms acquired by Marginpar already operated within the national laws of Ethiopia and Kenya, and had all the necessary environmental and social permits. In addition, the farms were compliant with other standards like Kenya Flower Council and GLOBAL GAP, which include management programmes on environment, water, health and safety, agriculture, land acquisition, labour and worker conditions.

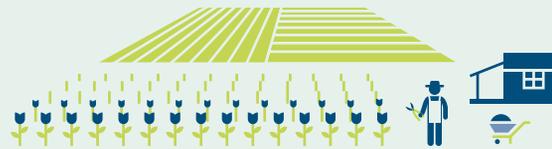
BREEDING

- Cultivate “refined” plants from plants with desired properties
- Collect feedback from other market players
- Multiply the selected cultivars



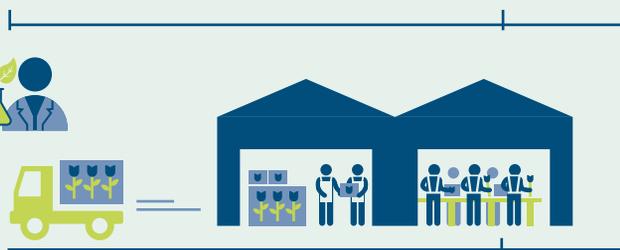
TRANSPORT

- Pack flowers in boxes
- Transport to the airport
- Load on aircraft pallets for transport to the Netherlands



CULTIVATION & HARVEST

- Plant selected cultivars in soil
- Grow in suitable temperature and light
- Employees, referred to as “value adders”, harvest flowers multiple times a day



POST-HARVEST

- Sort and bunch flowers
- Carefully check quality requirements
- Treat and place flowers in the cold store to prevent ripening



DISTRIBUTION

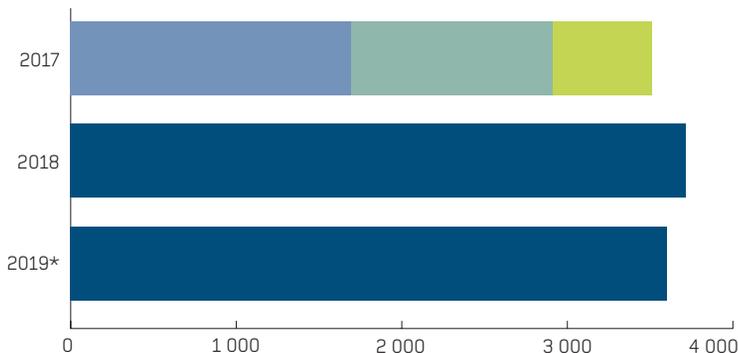
- Arrival at Aalsmeer
- Made ready for sale
- Flowers sold through the Dutch Auctions and directly to main customers who deliver to florists

THE VALUE CHAIN: FROM BREEDING TO DISTRIBUTION

Underdeveloped value chains can often be challenging for farmers and companies. The acquisition included a marketing and distribution agent in Holland. This helped the company to gain better control over the value chain and provided better access to the European market. It is important for Marginpar to cooperate across the different stages of the value chain to reduce waste and improve profitability.

MARGINPAR EMPLOYEES (end of year, *estimated)

■ Kariki ■ Carzan Flowers ■ Marginpar Ethiopia ■ Marginpar



The production of cut flowers relies on relatively high amounts of energy and water, and Marginpar has developed plans to implement cost-effective measures to improve the effective utilisation of these resources. Marginpar has formalised its relationship with the communities that live near the farms, by implementing a formal Stakeholder Engagement Plan, and appointing Community Liaison Officers at the farms. The human resource policies at Marginpar’s farms are guided by national laws, and are aligned with the International Labor Organization’s (ILO) standards, and the IFC’s Performance Standard 2. There was room for improvement in setting up a grievance mechanism and ensuring the emergency preparedness responses procedure also included the local community.

DEVELOPMENT EFFECTS

The formation of the Marginpar Group has contributed to securing decent jobs, increased productivity and job satisfaction through the implementation of the Kaizen model, raising of foreign exchange earnings,

sustainable profits and positive effects for the communities surrounding the farms.

Securing decent jobs in Kenya and Ethiopia

More than 50% of the jobs at the Marginpar Group's farms are undertaken by women, and there is a strong presence of youth employment. The farms were operationally and financially underperforming when they were acquired, and the capital provided has helped to improve performance and secure jobs. The level of production and the number of new jobs is expected to increase at Marginpar's farms. Indirect jobs throughout the value chain are also expected to increase.

The graph shows both permanent and seasonal workers. Seasonal workers account for approximately 20% of Marginpar's workforce at the end of the year. Seasonal workers from the surrounding community are usually employed at the farms during the peak flower production season, between October and March. The legal agreement between Marginpar and Norfund commits Marginpar to complying with specified environmental and social standards, and Marginpar is required to report regularly on its environmental and social management performance.

Increasing productivity and employee satisfaction

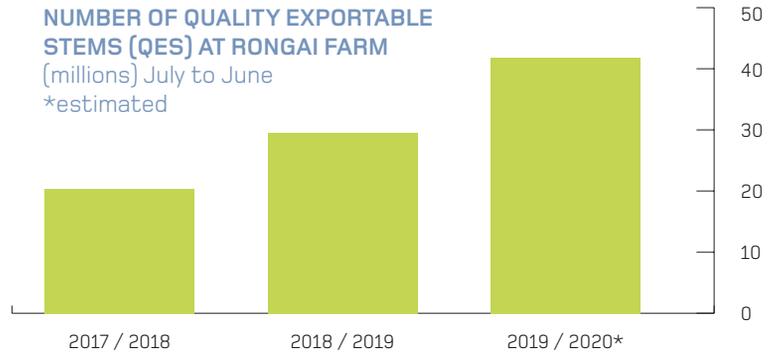
The Kaizen model emphasises the importance of involving employees and give more responsibility in different parts of the farm operations. Employees work together to improve and sustain productivity, and they look for root-causes of problems in operations. The workers are rewarded based on number of Quality Exportable Stems (QES) produced, which means flowers of a certain quality. In this way, productivity and the workers' motivation are aligned. Improvements in productivity have already been seen at the Rongai farm since the Kaizen model was introduced, and the number of QES produced at the Rongai farm has been more than doubled. Similar improvements at the other farms are expected soon.

Raising of foreign exchange earnings

The formation of the Marginpar Group has contributed to better productivity, increases in sales, and better access to European markets. This increase in foreign exchange earnings is important to the Kenyan and Ethiopian economy.

NUMBER OF QUALITY EXPORTABLE STEMS (QES) AT RONGAI FARM

(millions) July to June
*estimated



Positive effects for the surrounding communities

Through Norfund's investment, the farms can further strengthen their relationship with the surrounding community, from which they source most of their employees. The Manager at the Nanyuki farm, Peterson Thuita, emphasises that good relationships with the farms' neighbours are important. Marginpar's social investments at the Nanyuki farm include maintaining the public road that leads to the farm and building a classroom for children in town.



Eunice Mbugua, the Group HR Manager, says that she can clearly see the difference in well-being of the employees and productivity since the implementation of Kaizen: "The employees are happier, have more responsibility, and are also more productive. Productivity and continuous improvement are important for us to survive as a flower company. When we are more productive, the jobs are more sustainable."

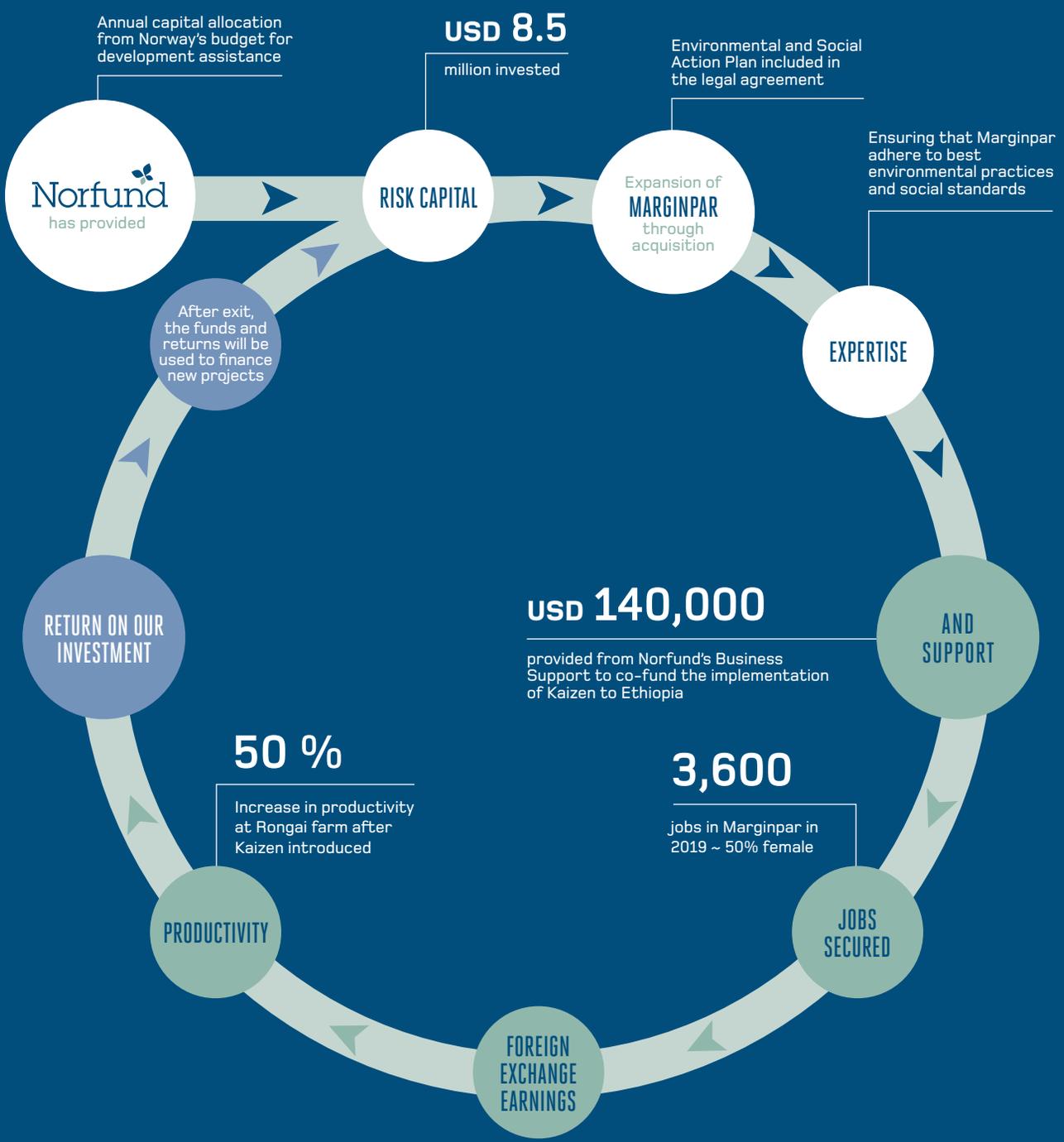
WAY FORWARD FOR MARGINPAR

Marginpar aims to expand its production, develop new markets, and explore new acquisition opportunities. Norfund's key focus areas will be to strengthen environmental and social performance, and maintain Marginpar's robust corporate governance. Mobilising private capital is a central objective for Norfund. Our long-term goal is to attract the interest of financial and industrial investors so that our own capital can be replaced. This allows our funds from the exit to be reinvested in new projects. The improvements following the implementation of the Kaizen model make it likely that Marginpar's operations will be attractive to new private capital. ■

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NORFUND'S INVESTMENT IN MARGINPAR



**NORFUND
CASE STUDY
MARGINPAR IN
EASTERN AFRICA**

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