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The Role of Microfinance in Rural Microenterprise Development

syngenta foundation
for sustainable
agriculture

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Agriculture is an important engine for economic growth in developing countries.

Rural micro-enterprise is critical to that growth.

So what role for microfinance?

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1. Introduction

In October 2006, the Syngenta Foundation held a seminar focusing on Capital for Development. The Foundation had just completed the review of its five years in operations and concluded it needed to focus more on the drivers of rural economic growth – both on-farm and off-farm-if it wanted to achieve significant impact in reducing rural poverty. Business constitutes the major engine for rural economic growth and for efficiently matching urban demand-pull with rural supply. At the lower end, the micro-enterprise sector (small farmers, small-scale traders, artisan producers) needs access to financial services – including credit and saving products, which have been provided through the dynamic and increasingly professional micro-finance sector. Above, the Small and Medium Enterprise (SME) sector is essential in both connecting urban and rural economies and small and large scale industries. It needs a very specific blend of financial instruments and business support.

This paper focuses on the microfinance industry and its role in servicing the rural micro-enterprise sector. It builds on the outcomes from a web-based discussion prompted by an advertisement the Foundation ran in "The Economist's" special issue on microfinance, which Professor Hans Dieter Seibel analysed.

Professor Hans Dieter Seibel is Head of the Development Research Centre, University of Cologne and is a specialist in rural microfinance. He was also Technical Adviser Rural Finance at the International Fund for Agricultural Development (IFAD) and has carried out numerous consultancies for multilateral development finance institutions, bilateral agencies and NGOs. His recent research has examined linkages between banks and microfinance institutions and on reforming agricultural development banks.

2. Changing Issues in Agriculture, Rural Development and Rural Finance

During the 1960s and 1970s the key issue in agriculture and rural development was agricultural production. Agricultural credit was but an input, next to improved seeds and seedlings, fertiliser, pesticides, tools and machines. The target group were farmers. The issue was how to disburse agricultural credit to farmers. The funds were provided by governments and donors. Disbursement mattered, not repayment. The main disbursement channels were agricultural development banks and projects. Agricultural credit was a service, not a business. The strategy had much to show: the green revolution, driven by technology, financed on credit, with subsidised interest rates. The produce was purchased by government at guaranteed prices. So impressive was the business of the green revolution that the business of the financial service was ignored. But when farmers didn't repay their loans, the banks didn't cover their costs and the governments ran out of money to finance the subsidies, the banking business finally failed, and so did the service.

Meanwhile, populations continued growing, increasing numbers of rural people could not live on agriculture alone. To survive they had to engage in numerous activities: on-farm, off-farm and non-farm. Rural households and rural economies got increasingly diversified. Access to finance was the limiting factor. Agricultural credit had been exclusive. It excluded all those who didn't own and till the land: labourers, micro-entrepreneurs, traders, women and large numbers of smallholders too poor to pay the bribes and too uneducated to do the paperwork. The unsatisfied demand prepared the ground for a revolution on the supply side: microfinance. Perhaps this should be called the blue revolution, blue being the bankers' colour. The new emerging issue was now how to link microfinance to rural entrepreneurs: through inclusive financial systems development.

Due to the overall failure of capital transfer and government-directed credit during the 1960s and 1970s, the emphasis in development policy shifted:

- From targeting bigger farmers and SMEs to inclusive finance, including micro-entrepreneurs, women and the poorer segments of the population
- From development banks and, subsequently, credit Non-Governmental Organisations (NGOs) to (rural) financial system development with a conducive policy framework and the building of self-reliant, sustainable institutions
- In rural areas from agricultural credit to rural financial services for a diversified economy
- From development banking to microfinance

Defining microfinance (MF)

So, what is microfinance? The Syngenta Foundation Discussion (SFD) indicates that concepts of microfinance vary widely, with significant implications on development strategies. Many reduce microfinance to microcredit or microfinancing, associating the recent microfinance movement with the so-called microcredit revolution spearheaded by credit NGOs during the 1970s. Given the recent popularity of the concept of microfinance, many players have redefined the concept for their own purposes, bringing it close to the point of meaninglessness. Some have reduced its meaning to such concepts as microcredit, credit NGOs, group finance or Grameen banking. A bias to credit for the poor or very poor is widespread. Statistics on microfinance institutions (MFIs) frequently continue to reflect the old bias to credit NGOs. The fact is widely ignored that in many countries agricultural development banks (AgDBs), various types of rural banks and savings and credit cooperatives continue to be the largest providers of microfinance services in rural areas.

However, the term microfinance was first introduced in 1990 with the specific connotation of encompassing microcredit and microsavings as well as other financial services, in response to Robert Vogel's claim that savings were the

forgotten half of rural finance. While the term is new, the concept is old if not ancient, with institutional origins for instance in European countries in the 18th and 19th century, Nigeria in the 16th century and India around 1000 BC.

This has resulted in a more general concept brought forward in the SFD: Microfinance is that part of the financial sector which comprises formal and informal financial institutions, small and large, that provide small-size financial services in theory to all segments of the rural and urban population, in practice however mostly to the lower segments of the population. This bias is partly due to self-selection of clients and partly to the mandate of institutions according to the will of their owners or donors. Worldwide formal and semiformal Rural Microfinancing Institutions (RMFIs) are in the hundreds of thousands; informal institutions are in the tens of millions. Sustainability is nothing new; without it the large numbers of informal MFIs could not have survived.

Size of financial services is relative and varies widely by the economic development of a country; rigid definitions of size can lead to exclusion and unintended consequences. Microfinance covers a wide array of microfinance institutions (MFIs), ranging from indigenous rotating savings and credit associations (RoSCAs) and self-help groups to financial cooperatives, rural banks and community banks as well as non-bank financial institutions (NBFIs) including credit NGOs, all the way up to development banks and commercial banks. They may also comprise moneylenders and private deposit collectors. In contrast to microcredit, microfinance proper refers to a system of financial intermediation between microsavers and microborrowers; it may further include microinsurance and other financial services such as money transfer.

Implications for development strategies

The two concepts have widely different implications for development strategies and have practically divided the microfinance community, particularly the practitioners, into two camps:

- Advocates of microcredit for the poor, with an emphasis on donor funding and capital transfer from developed countries with little concern for legal status, prudential regulation and supervision – quite pronounced during the 2005 Microcredit Year of the UN and in the Millennium Development Goals agenda

- Advocates of financial systems development and sustainable microfinance institution building, who argue that only healthy and self-reliant institutions will be able to provide sustainable financial services to the vast numbers of the rural and urban poor, but to attain that objective may have to serve a differentiated market of poor and non-poor and will require legal status, appropriate regulation and effective supervision

Three worlds of finance

The concept of microfinance is thus not tied to size nor type of institutions; least of all can it be reduced to credit NGOs or Grameen banking. There are three worlds of finance, each with a great potential to increase outreach to the micro-economy, in which players such as the Syngenta Foundation may intervene in different ways:

- The old world of donor-driven development finance comprising development banks, state cooperatives and credit NGOs which all need to be transformed into sustainable institutions

- A new world of microfinance, comprising viable formal and semiformal institutions with a commercial orientation, which do not, or not fully, rely on donor support for survival and expansion

- An ancient or indigenous world of informal finance including recent innovations, based on principles of self-reliance and viability, with a potential for innovation, upgrading and main-streaming

There are numerous developments in RMF. This had led Malcolm Harper to make the statement that “rural microfinance is pretty well established, and growing fast, and sustainably.” This leaves just two questions which he considers subsidiary to the more general SFD: (1) How (if at all) can (or should) MFIs extend their products so that they can provide larger loans to mainly male-owned and employment generating business enterprises, so that rural people can break out of poverty and rural MF can go beyond the much needed sticking plaster survival enhancement role it is playing right now? (2) Related to the above, how can MF satisfy the needs of on-farm investment, short and long term that it presently fails to do?

In the majority of countries, there are still major shortcomings that call for country-driven, coordinated interventions. E.g. Quiñones lists the following major factors which constrain the access of microenteprises to financial institutions:
(i) limited track record – most micro-enterprises do not have either a deposit account or a loan account with any financial institution
(ii) lack of acceptable collateral – banks require real estate or tangible assets as collateral. Assets in the possession of rural entrepreneurs such as work animals, shareholding contracts with the landowner or a thatched-roof house are not acceptable as security for the loan.
(iii) inadequate financial records and reports– rural entrepreneurs do not keep or maintain financial records of their transactions. They have no financial statements and, in many cases, no declaration of income tax returns either.
(iv) absence of business plans - rural entrepreneurs are not in the habit of preparing a written business plan, as is often required by formal lenders.

Donors with their projects are found in both the old and the new world; but there is an overall move from the old world of supply-driven development finance to the new world of demand-driven commercial finance. The ancient or indigenous world of informal finance has been largely ignored.

Tenets of sustainable microfinance

History has shown according to the SFD that, regardless of ownership, type of institution, and rural or urban sphere of operation, to be sustainable MFIs ultimately have to:

- Mobilise their own resources through savings and equity, augmented by other domestic resources

- Recover their loans

- Cover their costs from their operational income

- Finance their expansion from their profits

- Acquire an appropriate legal status

- Submit to appropriate regulation and supervision

There is no place for charity in microfinance. As one contributor to the SFD put it, “in a situation where there is no strict supervision and monitoring…, working without any hard budget constraints and mixing microfinance business with charity, (will lead to) crowding out the operations of more sustainable rural financial intermediaries.”

Linking microfinance to rural micro-entrepreneurs

From the Philippines Quiñones describes a strategy involving the People's Credit and Finance Corporation (PCFC), an apex organisation wholesaling funds to microfinance-oriented rural banks specifically for the purpose of retailing loans to rural entrepreneurs. The PCFC wholesale funds have enabled rural banks to create a clientele base and establish an operational institutional delivery mechanism ahead of local resources mobilisation. When the number of the rural bank clientele reached a critical mass (1,000 clients in the case of the Producers Rural Banking Corporation in Central Luzon), deposit mobilisation rose in importance as a source of loanable funds and eventually made the microfinance operations sustainable. A relevant lesson from the financial linkages strategy is that microfinance institutions (MFIs) need start up funds to penetrate areas/sectors not served by traditional banks but such funds should be prioritised for use by MFIs with savings mobilisation capabilities inasmuch as they are in a better position to make their operations among the poor/rural entrepreneurs sustainable. One of the crucial factors of success of the Philippine financial linkages is the adoption of microfinance performance standards. Performance criteria include portfolio quality, cost effectiveness, financial self-sufficiency, and outreach which significantly affect the sustainability of MFIs. The setting up of standards leveled off the microfinance playing field for all types of financial institutions. Given the microfinance standards, it no longer matters whether one is a traditional bank or an NGO to be able to provide microfinance services to the poor. The most important thing is that the MFI passes the standards, and when it does, it enjoys the privilege of accessing wholesale funds from PCFC.

3. Who are the Rural Entrepreneurs, and What is Their Demand for Financial Services?

Who are rural entrepreneurs, asks one of the contributors to the SFD, family producers who don't pay for wages and use mostly their own work force? Medium and large producers with lot a workers? Much depends on the local development situation. According to the contributors to the SFD, there are at least three different subsegments of the market where private and governmental agencies may intervene in various ways:

(i) the rural poor, particularly in disadvantaged countries or marginal areas;
(ii) all segments of the rural population in more open economies, particularly non-agricultural entrepreneurs in a situation of increasing diversification; and
(iii) commodity producers, processors and traders, with a tremendous growth potential if the potential for value-added is fully mobilised.

Rural entrepreneurs in stagnating countries

From the perspective of poor countries like Ethiopia, rural entrepreneurs are the rural poor. The communication system, particularly the road network, makes access to financial services difficult. Where access is available, as in the case of the Amhara Credit & Savings Institution (ACSI), one of several large MFIs, clients' low skills and business abilities reportedly weaken their absorptive capacity. Many are found risk averse, or for cultural reasons don't like to venture into non-traditional activities, while others have a low income perspective and simply don't have the demand for income-improving services. Such problems reportedly manifest themselves more profoundly in women, whose access is further limited because of problems emanating from a male-dominated social order; yet the situation of women in microfinance is more differentiated, as will be shown below.

Rural entrepreneurs in more progressive countries

A different part of the rural enterprise spectrum is covered by contributors from countries with a more open rural economy. Here it is argued that microfinance is important to rural entrepreneurs for agriculture, but under conditions of increasing diversification even more so for non-agricultural enterprises. Microfinance thus comprises all segments of the rural population. In fact non-agricultural activities often complement agricultural income and labour flows and hence help build livelihood stability and growth. It is further argued that rural financial services actually become much better if we take the micro-specificity away and concentrate on sustainable financial services to a wider array of rural households and businesses. This increases institutional viability, reduces unit costs for services to the poorest and helps finance not only other poor but other important rural actors including – truckers, agribusinesses, side businesses, etc. all of which have an important role to play in rural development.

Rural entrepreneurs in commodity production and trade

Yet, the importance of non-agricultural activities notwithstanding, commodity production, processing and trade continue to be the backbone of the rural world in many developing countries. The commodity sector provides subsistence food, income, employment and opportunities for growth and development. One contributor reports that, "all the microeconomic data collected over the last 40 years in Nicaragua demonstrates that small land holders, family producers are more productive and more competitive than large and medium producers." From the US it is being reported that agriculture, in myriad forms of property, acts as an engine for economic growth. Eg, crops increasingly become the basis for products other than food or feed (eg, fibres

and fuels), and as research expands opportunities for value-added innovations increase; this in turn increases employment. Finance is essential in this commodity-dominated rural world. There are two sides in the financing of the commodity sector: (i) the demand side, with strategies for processors, producers and traders; and (ii) the supply side, with strategies for financial institutions. Closing the supply and demand gap is a daunting task, but not impossible. Two issues are crucial in combating poverty in a sustainable way: (i) on the demand side, a move is necessary from a sole emphasis on commodity production towards value creation through processing and marketing goods that respond to market pull; (ii) on the supply side, there has to be a shift away from charity and interest rate subsidies towards dynamically growing and sustainable financial services at commercial terms.

From this perspective, the challenge is how to turn effective (ie, creditworthy) demand for financial services into effective supply of financial services. The two sides have sometimes contradictory, but mostly complementary, though not identical interests. These are not two different worlds, but two sides of the same world: they can only grow together or fall together. Each contributes to the other's growth or failure: viable financial institutions provide financial services to producers, processors and traders, thereby contributing to their viability and growth; viable producers, processors and traders contribute to the viability and growth of financial institutions. Viability is crucial.

Short-term benefits of small entrepreneurs – gained, e.g., by running away with a loan – are of little benefit to them if this is the last loan they received. Squeezing collateral out of a small entrepreneur who cannot repay a loan is of little benefit to an MFI as this will be the last loan given to that customer. Sustainability is crucial: of producers, processors and traders on the one hand and of MFIs on the other hand.

A few high-quality loans to a few first-rate producers, processors and traders do little good: be it to the commodity sector or to the MF sector. Outreach is crucial.

Rural agro-processing

A broad spectrum of topics that can shape a strategy for rural enterprise development were discussed. Several examples of the potential and needs of rural agro-processing were presented in the SFD: cassava, leather, and preserved and processed fruits and vegetables.

In the past few decades, particularly during the heyday of agricultural credit, there has been a sole emphasis on production, regardless of costs, comparative advantage and opportunity. This has changed fundamentally. It is now realised that the viability and profitability of rural enterprise and rural microfinance institutions are intimately linked and mutually reinforcing in a virtuous circle. Profitability matters, not production. Of crucial importance are value-addition and quality at every link of the commodity chain to respond to strong market demand from rural and/or urban areas. There is a huge underutilised potential here.

Cassava processing in Ghana

In Ghana, as in numerous other countries, cassava processing offers highly profitable, diversified opportunities for production, processing, trade and investment. Eighty percent of farmers produce cassava, amounting to 10 million tonnes, which accounts for 22% of agricultural income and supplies 25% of calories consumed. The International Institute of Tropical Agriculture (IITA) in Nigeria exhibits 32 cassava products; very few of them are found on local markets, commercialisation being the bottleneck. In this situation, Feed & Flour (Ghana) Ltd. (FFGL) propose to set up a plant for the processing and marketing of high quality cassava flour, based on a modification of the gari-making process developed by IITA. Facing an estimated annual demand around 144,000 tonnes, there seems to be a good potential for a joint investment by local and external investors.

Quality matters

Quality is of crucial importance. Quality (together with standardisation and packaging) is crucial throughout the commodity chain and in the process of adding value. Each commodity has its own range of opportunities for adding value and improving quality. In the case of meat, hides, leather, this starts with the quality of

livestock and its veterinary care, which has a bearing on the post-processing of meat and leather. The major needs are training of producers in clean production and processing, quality awareness and quality management, capacity-building, access to finance, accurate information, and essential utilities and services. For a substantial improvement in the processing and marketing of leather, better cooperation between private producers, producer associations, commercial institutions, government agencies and donors is required.

Another example are perishable fruits and vegetables. Depending on seasonal and regional variation, many developing countries produce an excess of tomatoes, yet import large quantities of tomato concentrate. There may also be a seasonal abundance of fruit like mangoes, much of which, in the absence of processing facilities, is lost. The drying and processing of fruits and vegetables would offer solutions to these problems. The preservation and processing of fruits and vegetables adds value, generates employment and improves diet. Key issues are: Is processing worthwhile? And can farmers supply the material on a regular basis? Can economies of scale be achieved? Value creation requires the planning of diversified processing of several fruits and vegetables over the year to maximise plant utilisation; intermediate-scale processing through contract farming and the pooling of producers; the use of locally available raw materials and appropriate technologies to minimise capital expenditure and, at the same time, maximise product quality. Success factors are adequate training, the quality of raw material, and market analysis. The history of financing is full of failures. The sector needs experienced micro-entrepreneurs linked to farmers who are willing and able to grow fruits and vegetables, thereby guaranteeing:

- A steady source of supply
- Appropriate risk management, such as spreading production over several fruits and vegetables
- Good linkages between producers and processors
- Financial engineering comprising savings mobilisation as a basis for self-financing
- The provision of investment capital
- A balancing of individual and group lending technologies
- A legal framework for sanctions against defaulters

Strategies for financial institutions

Focus must be on sustainable financial institutions with sustainable financial services, combining credit with savings as a service to customers and as a source of loanable funds, thus moving away from credit-only provided through projects and programmes. Any MFI, bank or microbank striving for sustainability must: mobilise their own resources, apply appropriate lending technologies, provide attractive loan products with appropriate interest rates, have their loans repaid, manage their risks, make a profit, finance the growth of outreach from the growth of savings and profits, and through advocacy strive for a conducive policy and legal environment. Evidence to the contrary in the old world of development finance notwithstanding, sustainable MFIs, microbanks and AgDBs in the new world of development finance, with appropriate risk management technologies, have demonstrated their ability to lend to the agricultural sector including producers, processors and traders at low default rates and high profits. The number of such institutions has substantially increased in recent years: in all ownership categories, including government-owned banks, private and community-based rural banks, and various types of MFIs. Networks and associations of MFIs and banks have a crucial role to play in disseminating the positive experience and developing support strategies in cooperation with government and donor agencies.

Experience in several countries has shown that the informal financial sector is quite able to cater for small-scale financial needs, but not for larger loans; that rapid access to finance is more important to borrowers than cost; and that agricultural banks, as in Thailand and Bangladesh, are able to successfully diversify their portfolio by combining loans to both agricultural producers and non-agricultural small enterprises and processors.

Business development services (BDS)

BDS are of crucial importance to small and micro enterprises in various sectors of the economy, linking the strategies of producers, processors and traders with those of financial institutions. As reported in the SFD, to date more is to be learned from error than trial. Not only have many heavily funded BDS programmes broken down; it is being argued that it is the very fact of donor support which has undermined the market for BDS. Just as subsidised interest rates have undermined financial markets, so has donor support undermined the viability of BDS. This, however, can be turned around, as the experience with CEFE (Competency-based Economies through Formation of Enterprise) shows.

Provision of BDS as a private good
CEFE is a medium, small and micro enterprise development training concept and was developed in 1979 by GTZ, the German Technical Cooperation Agency. It is an action-oriented adult training tool, applied in numerous countries around the world, which helps micro- small- and medium-entrepreneurs developing a realistic business plan, which they implement at their own risk. To break the vicious circle between donor dependency and lack of viability, the proponents of CEFE have proposed a new paradigm, turning BDS as a public good into a private good. They argue that BDS should be provided by the private sector and governments should only facilitate the market development of BDS. Accordingly, the delivery of BDS has now been made a private business in various countries, including Sri Lanka. In Sri Lanka, 18 organisations are making use of CEFE as a fee-based BDS in different contexts and environments, 10 of them in the private sector.
To a good number of them, BDS is a major source of income. These organisations use CEFE for three major components of their portfolio: training & capacity development of BDS organisations; brand image development; and product packaging & marketing. Market orientation, marketing and diversification for agricultural producers, processors and traders is one of several products, with two major parts: market orientation and business planning.
The benefits include: sustainable increase in income, better ability to analyse production and marketing patterns, and the identification and use of opportunities for improved marketing. The CEFE team in Sri Lanka has also analysed most of the major microcredit schemes, which were all donor-driven, and found that most of them were not successful. They have already tested and introduced a new approach to link commercial BDS and commercial microfinance schemes operated by microfinance institutions and banks. The approach includes direct linking of CEFE training and microcredit and opening of CEFE training for microcredit customers on a commercial basis.

A different experience is reported from India, where Nabard, the National Bank for Agriculture and Rural Development, has promoted the establishment of about 1.6 million self-help groups (SHGs) of the rural poor and their linkages with some 36,000 bank branches. The approach, referred to as SHG Banking, is applied all over India: in marginal as well as high-potential areas. Numerous NGOs and government organisations are involved in social mobilisation and non-financial services. An example is Bharatiya Agro Industries Foundation (BAIF) Development Research Foundation an NGO which has helped some 13,000 tribal families, who are among the disadvantaged in India, to cross the poverty line: (i) through sustainable agri-horti-silvicultural production on 12,000 acres of rehabilitated lands and (ii) through commodity processing. Against a historical background of the direct sale of raw materials, six vertically integrated layers of production, processing and marketing were established in remote forest areas:
(i) individual farm households for basic production on wastelands, (ii) small farmer groups for procurement and grading, (iii) community organisations (Gram Vikas Mandals) for the establishment of community processing facilities, (iv) village planning committees for the organisation and coordination of activities, (v) regional cooperatives for finishing and packaging; and (vi) an apex organisation for federated marketing. BAIF acted as a resource and technology sourcing agency, introduced streamlined systems, provided managerial backup services, and facilitated credit and market linkages. The two major products where producers took control of the full commodity chain were mangoes and cashews. In the case of mangoes, procurement and grading alone added 20% value. In a second step, the raw mangoes are cut into pieces and semi-pickled at village level, which are then brought to the final pickling stage by cooperatives, where they packaged and forwarded to a Producer Company for federated marketing. Value addition through processing contributed substantially to a sustainable increase in employment and income.

Combined financial and non-financial services

Combining financial and non-financial services including BDS under a single institution is frequently advocated as a necessary strategy in poverty alleviation and rural development. The favourable role played by the Cameroon Gatsby Trust may serve as an example.

Financial and nonfinancial services to the commodity sector in Cameroon

Cameroon is a country where financial and non-financial services strategies for processors, producers and traders have developed over a period of almost 20 years. The process was spearheaded by the Gatsby Root Crops Project, 1985-93, with a focus on improved technologies for cassava, yam and sweet potatoes. It was replaced in 1994 by a sustainable financial institution, the Cameroon Gatsby Trust (CGT), which continued multiplying and disseminating improved varieties, but at the same time provided microcredit to the producers. During a third phase individual credit was replaced by group lending, comprising microcredit through solidarity groups and mesocredit to associations of small groups (at a satisfactory repayment rate of 96.5%). This also marked the cultivation of a most remarkable approach: building on pre-existing indigenous self-help groups including rotating and non-rotating savings and credit associations, which are ubiquitous in Cameroon and neighboring countries. A fourth phase started in 2003 by adding a range of nonfinancial services, comprising skill training in such fields as soap-making and tie-dye making, food conservation and tuber multiplication; group and association management training; financial management; and facilitation of local and regional trade fair participation. The trade mark of CGT is now the combination of financial services with business development services for three major market segments in the commodity sector: producers, comprising yam, cocoyam, sweet potatoes, plantains, corn and cassava as well as livestock farmers; cassava and textile processors; and traders in food, handicrafts, textiles and livestock. The CGT approach constitutes an option in which special emphasis is placed on (i) group and association formation on the basis of pre-existing indigenous group structures, (ii) internal financial intermediation based on savings, (iii) their upgrading to sustainable formal organisations, (iv) access to refinancing by CGT, (v) networking among associations, and (vi) linkages of associations with other institutions.

Drawing some lessons

Care has to be taken in generalising singular observations. In a multi-country evaluation of NGO programmes in francophone West Africa, it was considered important for such services for rural micro-entrepreneurs to be linked. Among the non-financial services were literacy training, group formation, organisational assistance, empowerment assistance, information dissemination, and skills training. Some NGOs had carried out both types of services themselves, some had created external MFIs, some had transferred the execution of financial services to existing MFIs. However, some similar weaknesses were found in most of the models: Social and business orientations were rarely separated, and/or the transformation from a socially oriented to a business-oriented design of the financial programmes proved to be very difficult and lengthy. MFI membership and credit approval was at least partially directed towards (former) beneficiaries of NGO programmes. Credit from donor resources, with strings attached, was frequently used to push technologies selected by the donor, which turned out to be inappropriate and restrictive of innovative indigenous entrepreneurship. All this led to inefficiencies, misallocations of funds, inappropriate groups (e.g. entrepreneurship organised around literacy or health training, groups not based on solidarity ties) and an overall lack of sustainability.

Credit offered on soft terms was found to undermine the sustainability of MFIs. Many NGOs depended on continual donor funding; typically, they were neither self-managed nor member-controlled. On the other hand, it appeared that many MFIs newly created with the help of NGOs were inclined to be ruled by a minority of better-off members which sought to get large amounts of credit at the detriment of weaker members. Among the conclusions drawn and lessons learned were: non-financial and commercial financial services must be institutionally separated; autonomy of MFIs in credit decisions is crucial; MFIs must diversify their portfolio in terms of clients, crops and sectors – including producers, processors and traders among their customers and not just one of these; service providers must take great care in assuring good practices; MFIs should be very careful in financing agricultural innovations pushed by well-meaning NGOs or other donors; new member-based MFIs need guidance for good practice and effective supervision; and, last but not least, institutional development takes a long time.

4. Women in Rural Entreprise

In terms of women's access to finance there seem to be three worlds of rural finance. There is first of all the old world of agricultural banks and agricultural cooperatives with a bias to land-holding farmers, most of whom are male; women enter into this world only as heads of households. Then there is a new world of mostly donor-driven credit NGOs and other MFIs with a widespread bias to women.
This world has been under the influence of institutions in South Asia, particularly the Grameen Bank in Bangladesh and the SHG programme in India, where women were targeted by donor and government agencies because large numbers of men worked as migrant labourers and had little scope for productive credit and no time for attending regular meetings. This is the case in India where the mainstreaming of microfinance has resulted in linking 1.6 million self-help groups (SHGs), 90% of which are exclusively women's groups, to some 36,000 banking units. Then there is a world of unbiased rural and microfinance institutions open to both men and women, in the formal, semiformal as well as informal financial sector. Depending on culture, choice and opportunity the percentage of women involved may vary widely. Note should be taken that empirical evidence is limited because the balance sheets of banks and MFIs do not report data separately for men and women; and that many MFIs which report figures on the number of clients implicitly refer to borrowers and ignore savers. There is some overall anecdotal evidence

that in situations of self-selection as MFI clients the percentage of women varies roughly around 40%, that women are more prevalent among savers than among borrowers; they tend to borrow smaller amounts for shorter periods; and they are the more reliable borrowers. In many cultures women are the petty traders, with a strong demand for short-term deposit and credit services.

In the SFD women appear to have been mostly subsumed under an undifferentiated clientele of MFIs, or simply as household members. Only few contributors explicitly refer to women. From Ethiopia it was reported that women's access to finance is restricted in "a male-dominated patriarchal societal system". From the Philippines it is reported that men usually tend the farm or look for employment either in the manufacturing or services sector. It's the women who are inclined to operate microenterprises. Even so, MFIs in the Philippines have patterned their microfinance programmes after that of Grameen Bank in Bangladesh, which adopts a mechanism for targeting women clientele. The strict credit discipline of Grameen Bank has led to repayment rates very close to 100%. As a result of that experience, many MFIs continue to target women as they are generally known to be responsible borrowers who repay their loans fully and on time. (B. Quiñones)

Three big challenges were presented by a female participant in the debate:

(1) The "sticking plaster' survival enhancement role is also due to the general failure of most MFIs to seriously address gender issues. MFIs need to provide products and services for women which enable them to get out of the debt management role. Availability of small loans mean they often become more and more responsible for household budgeting while men become less and less responsible for basics like school fees and child health care. Women have become stuck in a cycle of small group loans in order to maximise programme sustainability. MFIs need to consider much more seriously how they can integrate gender awareness and financial management training into mainstream service delivery to enable women, together with spouses where they are present, to think about household investment and financial management strategies over the longer term.

This includes linking with BDS.
(2) Unless gender issues are addressed, larger loans to male-owned businesses may either fail to have acceptable repayment rates (the reason why they were stopped before) or to lead to significant poverty reduction. Increasing male incomes does not in and of itself increase incomes actually going into households. In many cultures training/MF promotion for men needs to tackle issues of male responsibility for their families and reinforce household cohesion. In particular encouraging men to save rather than increase spending on their own indulgences. In Africa this is a particularly serious issue.

(3) How can the organisational base provided by microfinance in both rural and urban areas, (both individual and group credit and savings) be expanded for wider civil society development? MF groups and federations can provide a good basis for local communities to examine issues like local economic diversification, collecting information for local lobbying, increasing accountability of schools etc. Issues have to be decided by MF groups themselves, but the regular meetings around savings and credit provide an ongoing basis for discussion on a wide range of issues.

Another contributor suggests to make MFIs more women-friendly, eg, by offering deposit services with high confidentiality (supposedly vis-à-vis their husbands) and adjusting opening hours to women's schedules. In many countries door-step collection services have been an effective technology of reaching large numbers of women, enabling them to accumulate their savings and withdrawing them as needed as an alternative to periodic indebtedness.

Ultimately one of the most important factors for women is the enabling environment – land tenure laws, inheritance issues, etc. that discriminate against women. These affect not only financial access but their overall economic and social opportunities. Microfinance has been a catalyst in exposing and empowering women to begin to take collective actions in this regard.

5. What Would it Take to Foster Sustainable Access to Microfinance in Rural Areas?

The issue of interventions with the objective of building sustainable access to microfinance in rural areas has been taken up in the SFD in a comprehensive and systematic manner and put into the perspective of what matters in rural and microfinance.

1. First of all: client experience matters

Clients have experienced in donor projects that credit can make them poorer or richer:

- Starting with large loans and term finance, as has been common among donor-supported AgDBs, is a guarantee for failure
- Only small short-term loans allow them to experiment with investments at a reasonable risk; to test their ability to borrow, invest, repay and save; to change to more profitable investments as opportunities emerge; and to grow rapidly with growing internal and external resources
- Once they are successful, they need a banking partner which responds to their increasing financial needs. This allows them not only to move beyond the poverty threshold, but also to create employment for the poor

2. What matters in terms of origin, history and culture of rural and microfinance?

Poverty matters: Poverty has been at the cradle of rural and microfinance:

- The poor need financial services, savings more than credit

Informal finance matters: Informal financial institutions in various forms of ownership have been based, some for centuries, on the very principles that many credit NGOs find difficult to adopt: self-reliance, viability, outreach to the poor as owners or users, competition, market-driven innovations, demand-oriented financial products and appropriate risk management.

- Upgrading and mainstreaming through networking, driven by incentives, is one of many ways in which donors can support expansion of outreach and financial deepening of informal financial institutions

History matters: MFIs in Ireland, 1720-1950, have demonstrated how regulation makes and brakes savings-driven RMF. MFIs in Germany, 1778-2002, started from informal beginnings and evolved, through appropriate regulation and supervision, to cooperative banks and savings banks (Sparkassen) with outreach to the majority of the German population in rural and urban areas, accounting for 51% of all banking assets.

Among the lessons are:

- Microfinance is not a poor solution for poor countries
- Savings-driven microfinance institutions, in cooperative or community ownership, are equally feasible in rural and urban areas
- If properly regulated and supervised, they have great potential in poverty alleviation and development, both in rural and urban areas

Crisis matters: Financial innovations typically emerge as a response to crisis, which must be taken as a positive force:

- Learning from experience means: responding to crisis with innovations
- Many MFIs in crisis are kept alive, and prevented from reform, through donor support
- MFIs which fail to respond to crises constructively must be allowed to falter: close them or reform them!

Development matters: Microfinance is no panacea. It contributes to development, but requires a climate of broader development to be fully effective, both macroeconomically and at the local level:

- Agricultural and agrobusiness, land, trade, monetary, foreign exchange, educational and numerous other policies matter in generating a development climate in which microfinance can play its role
- The effectiveness of finance depends upon profitable enterprise and marketing to really make a difference
- Targeting the poor only and excluding the non-poor prevents the development of a village economy, diminishing the chances of employment, self-employment and economic growth of the poor
- Donors must respect the autonomy of RMFIs and refrain from imposing targeting

Culture matters: The enthusiasm over the new consensus in RMF has led to a neglect of cultural factors, which may be of crucial importance to the clients and corporate culture. E.g. a culturally sensitive approach may arrive at two fundamentally different approaches to development:

- Development from above, through the established authorities, is more effective in hierarchical or closed societies, which are oriented towards status, tradition and the preservation of stability
- Development from below, through participatory processes, is more effective in segmentary or open societies, which are oriented towards competition, experimentation, individual achievement and social change

3. What matters at the level of financial systems?

Financial systems matter: Well functioning financial systems must be in place if sustainable development and poverty alleviation are to occur. Governments and donors have to realise that financial systems and functioning networks of MFIs evolve over long periods of time:

- Donors can contribute to that evolution, but only in a long-range perspective
- And in a coordinated goal-oriented manner

Capital matters: The main functions of capital transfer from abroad should be:

- Bridging temporary shortages in loan capital through credit lines

- Investing in deposit-taking institutions, providing leverage for savings mobilisation

- Strengthening the capacity of RMFIs to generate their own resources: savings and retained earnings

- Shifting the emphasis from aid to investors (e.g., in Emerging Market Funds), encouraging thereby private entrepreneurship on both sides of the economic divide

…but capital transfer has undermined rural finance and development: Reliance on external resources, interest rate subsidisation and outside administrative control led to misallocation of scarce resources, corruption and external debts not matched by productivity increases.

- Under disbursement pressure, donors continue to provide credit lines in substitution of domestic savings, undermining the growth of self-reliant financial institutions

Savings matter: at three levels, provided inflation is low and does not erode the value of the savings of the poor:

- As a service to the poor, to deposit and accumulate their savings in a safe place

- As a source of loanable funds and self-reliance for (rural) financial institutions

- As the main source of domestic capital in the national economy

Savings and credit matter: which one comes first depends on the rate of return:

- Savings-first for subsistence and low-yielding activities

- Credit-first for high-yielding activities

Financial intermediation matters: Institutions, which offer both savings and credit services benefit twofold:

- They generate their loanable funds on a sustainable basis at a low cost

- They benefit from economies of scope; ie, the additional transaction costs of the second type of service are substantially lower than those of the first

Financial sector policy matters: The two main instruments of financial sector policy are:

- Interest rate deregulation, with interest rate autonomy on deposits and loans

- Institutional deregulation, to freely establish financial institutions and branches

The legal framework matters: Appropriate legal forms allow people to establish their own financial institutions in private, cooperative or community ownership:

- Donors should support the financial authorities in providing an appropriate framework

- The two most important legal forms are privately owned rural banks and financial cooperatives

Interest rates matter: Interest rates are of crucial importance:

- Caps on interest rates cut down on viability and outreach, rob savers and investors of the value of their resources, and ruin MFIs

- Interest rates above the inflation rate on deposits prevent the erosion of capital

- Rural market rates of interest must vary widely between institutions and countries, reflecting cost of funds, risks and services

- High interest rates force the borrower into investments with high returns

- Bringing down interest rates is an internal matter within institutions

Institutions matter (projects don't): Institutions are the social capital of a society, providing continuity and efficiency. Financial institutions fall into three sectors:

- The formal financial sector, which is regulated and supervised by financial authorities

- The semiformal financial sector of institutions officially recognised but not regulated

- The informal financial sector of institutions which are regulated through local norms and traditional law, but are not officially recognised nor regulated by the state

Donors may:

- Support a differentiated financial infrastructure with competitive institutions organised in networks

- Support the expansion of sustainable rural financial institutions and their outreach

- Provide opportunities and incentives for upgrading nonformal to formal institutions

- Abstain from perverse incentives which enable NGOs, AgDBs and others to maintain unviable operations

Competition matters: An emphasis on the creation of a competitive environment entails:

- Institutional diversity (eg, financial cooperatives, rural banks, AgDB branches)

- Pressure to perform, through effective supervision and enforcement of standards

- Procedures of bankruptcy for non-performing institutions

Prudential regulation matters: Regulation has failed in many developing countries, but is a prerequisite for financial market development. There are two controversial positions:

- Regulating deposit-taking MFIs only

- Regulating all MFIs, stabilising the system and protecting small investors

Effective supervision matters: Regulation is ineffective if not enforced by supervision. Donors should strengthen:

- The political will and institutional capacity to enforce standards of performance

- The restructuring or closing of nonperforming financial institutions, instead of preventing it through bail-outs – bankruptcy matters!

- Bank superintendencies or central banks and, under delegated supervision, networks and auditing apexes of rural banks, savings and credit co-operatives, and other RMFIs

Linkages matter: Through linkages with self-help groups or MFIs, commercial banks may provide the following services:

- Safe-keeping of deposits in a regulated and supervised institution

- Access to bank credit; channelling donor funds

- Liquidity balancing

- Equity participation

- Money transfer, check clearing, payments

- Capacity building

- Monitoring

Knowledge matters: The wealth of highly diverse institutional experience has largely escaped knowledge management: at the level of donor organisations, countries and regions:

- Donors will have to take up the challenge of establishing a system of knowledge management

4. What matters at the level of institutions?

Institutional reform matters: There are striking examples of successful reforms among different types of institutions, leaving no excuse for continual support to unviable institutions. The following lessons can be drawn:

- Financial sector policies such as deregulation of interest rates and the provision of legal forms for regulated financial institutions are conducive to financial innovations

- Any type of financial institution can be reformed, including credit NGOs and AgDBs

- With attractive savings and credit products, appropriate staff incentives, and an effective system of internal control, rural microfinance can be profitable

- The poor can save; rural financial institutions can mobilise savings cost-effectively

- If financial services are offered without a credit bias, demand for savings deposit services exceeds the demand for credit by a wide margin

- Incentives for timely repayment work

- Outreach to vast numbers of low-income people and sustainability are compatible

- Transaction costs can be lowered, profitability and outreach to the poor increased, by including the non-poor and their demands for widely differing deposit and loan sizes

Agricultural development banks matter:

- AgDBs are the largest providers of RMF services
- Unreformed AgDBs waste public resources, lack growth and outreach, undermine rural finance
- Reform may lead to sustainable outreach to all segments of the rural population through retail or wholesale services (linkages)

Donors may support:

- Regional reform policy seminars with financial authorities
- AgDB reform workshops
- Regular state-of-the-art reporting on AgDB reform

Ownership matters: Credit NGOs lack ownership; private ownership is most effective, but:

- Depending on culture, institutions can be sustainable and reach the poor under any type of ownership
- Individual or cooperative ownership by the poor as shareholders of MFIs, including transformed NGOs, deserve special support

Institutional autonomy matters: Management autonomy is more important than ownership. Donors should:

- Insist on management autonomy (vis-à-vis government and donor agencies)
- Refrain from targeting
- Respect management autonomy in customer selection and loan decisions

Viability, efficiency, sustainability and self-reliance matter: Donors should support the enhancement of:

- The mobilisation of domestic resources, such as savings, equity and borrowings
- Profitability, requiring adequate repayment and coverage of all costs from the margin

- Cost-effective microfinance products and services
- An adequate regulatory framework

Outreach matters – and so does truth in reporting: In contrast to a ubiquitous credit bias of donors and governments, both saver and borrower outreach matter, in both small and large institutions:

- Support both saver and borrower outreach
- Insist on the reporting of actual, not cumulative figures; the latter conceal the truth

Outreach and sustainability matter – together! There is strong evidence of the compatibility of outreach and sustainability, except under conditions of fixed interest rates:

- Insist on mutually reinforcing growth of sustainability and outreach
- Insist on adequate interest rates, allowing for profits above the inflation rate

Sustainable outreach to marginal rural areas requires recognition of, and support for:

- The primacy of savings and self-financing, due to the absence of markets
- Member-owned SHGs and cooperatives, operating at low costs

MFI portfolio diversification matters as a risk management strategy:

- Support portfolio diversification of both clients and MFIs
- Abstain from imposing loan purposes, which create undue risks

Lending technology matters – and should not be influenced by ideology:

- The poor can be reached by either individual or group technologies, if properly applied
- Group technologies with joint liability are more effective for small loans to the very poor
- Individual technologies offer opportunities for graduating to larger loans and sustainable movements out of poverty

Innovation and flexibility matter: Rigid replication of success stories is a recipe for failure.

- Support financial innovations and adjustments to local culture

5. What matters at the operational level?

Good practices matter (not best practices): The term best practices evokes notions of optimal solutions and leads to inappropriate replications:

- Support satisfactory culturally appropriate solutions

Institutional size matters, but not absolutely: RMFIs benefit from economies of scale, but there is no best practice in terms of size.

- Support both, small numbers of large, and large numbers of small, institutions; there is no minimum size of sustainable institutions (such as SHGs or cooperatives)

Profits matter:
Profits are a source of capital and a major determinant of growth of outreach.

- Support studies of profitability of different credit and savings products

- Support organisational efficiency, bringing down interest rates or increasing profits

Incentives matter: While profits are a source of incentive payments, incentives are at the same time a major determinant of profits. Donors may support:

- The transformation of branches into profit centers

- The introduction of systems of staff performance incentives

- Client incentives (rather than penalties) for timely repayment

Repayment matters:
There are many institutions of different types with repayment rates near 100%; however, enforcing perfect repayment may not be cost-effective and may even curtail outreach. Donors may support measures to attain adequate repayment based on:

- Appropriate terms like size, instalments, grace periods, purpose, timely disbursement

- Sound practices of loan enforcement, insisting on timely repayment

Information matters – in terms of computerised data and personal knowledge of clients.

- Support adequate Management Information Systems that provide timely information

Delivery systems matter: Institutions lower transaction costs; therefore:

- Support measures to bring the bank of MFI to the people, shifting transaction costs from clients to institutions, with cost coverage from the interest rate margin

Financial products matter:

- Support the development of demand-oriented and cost-effective savings and credit products

- Support efficient collection services (e.g., at doorsteps)

Loan protection matters:
Life (health, cattle) insurance is a service to clients, but also part of loan protection.

- Support the development of cost-effective insurance services by MFI, particularly to cover the default risks arising from AIDS/HIV

6. What matters to the poor?

Access to savings and credit matters – (far more than interest rates):

- Support institutions which offer both savings and credit

- Insist on the transformation of credit NGOs into institutions collecting voluntary savings

Rural enterprise viability matters:
The viability of RMFIs and rural farm and non-farm enterprises are mutually reinforcing.

- Promote linkages with agencies providing BDS in rural areas and to enterprising poor

Household portfolio diversification matters: Income-generating activities of poor households are usually highly diversified, managing the risks of diverse enterprises.

- Refrain from restricting small loans to single (productive) purposes

- Encourage loans to Income-Generating Activities (IGA) with high rates of return, including petty trading

- Stay away from financing group enterprises
- They have usually failed

The poor themselves matter…and so do the non-poor: Depending on culture and the financial infrastructure. Banking with both the poor and non-poor may increase outreach to the poor. In exploitative cultures, the poor may prefer access to financial services as a separate group

- Promote financial services to the poor and non-poor in separate or mixed MFIs depending on culture
- Instead of targeting, promote financial products for different market segments

Culture of labour division matters:
Depending on culture, men, women and RMFIs may opt for separate or mixed institutions.

- Refrain from targeting women
- Respect the autonomy of women and men and let them decide on separate vs. mixed institutions

Autonomy matters:

- Abstain from targeting and other impositions
- Respect the autonomy of the poor, women, local financial institutions and their owners
- Support self-selection through particular financial products and services

7. Donor policy and coordination matter

7.1 Transmitting policy to operational departments

There is an emerging consensus on RMF policy in the community of donors and microfinance practitioners. But transmitting policy to operational departments remains a major challenge:

- Examine the feasibility of a matrix structure, with operational responsibility in the operational units and responsibility for project design and performance in the financial sector & microfinance unit
- Create a mechanism for monitoring the effective implementation of policy

7.2 Cooperation, coordination and co-financing

The effectiveness of development assistance private sector cooperation can be infinitely increased through coordination:

- Synergies are created by stakeholder coordination at the national level, including cooperation in expert advice, policy dialogue and project supervision
- Bilateral technical assistance agencies can complement multilateral and bilateral financial assistance agencies with grant-financed expertise
- Private sector brings market orientation and business discipline
- Standardised reporting on MFIs will facilitate implementation of policy and donor coordination.

7.3 Opening markets

The total effect of development assistance is small compared to the importance of opening markets in the developed countries for products from developing countries:

- Donors should make every effort for abolishing agricultural subsidies and opening up markets for developing countries

8. Conclusions

(1) Sustainable development requires:

- Continued growth and diversification of the rural economy
- Access of all segments of the population including rural micro-entrepreneurs, farmers and the poor to sustainable financial services such as savings, credit and insurance
- Provided by self-reliant, sustainable financial institutions
- In a conducive macroeconomic policy environment

(2) Sustainable rural microfinance requires local initiative and careful donor support for the development of institutions, enabling them to:

- Offer both savings and credit services
- Mobilise their own resources
- Have their loans repaid
- Cover their costs from their operational income

- Finance their expansion to the poor and non-poor from their profits

(3) Governments, with careful donor assistance, have to provide:

- A conducive policy framework with deregulated interested rates
- An appropriate legal framework for competitive local and national financial institutions in private, cooperative, community and public ownership
- A system of prudential regulation and effective direct or delegated supervision

(4) Donors may contribute to the development of rural financial systems through:

- Experts for RMF units in central banks, RMF networks and leading RMFIs
- Capacity building in financial authorities, RMFI networks and RMFIs
- Policy dialogue
- Equity investments, clear ownership and an exit option
- Credit lines for bridging temporary liquidity gaps (no credit lines for other purposes!)
- Assistance for the transformation of MFIs into regulated bank or non-bank institutions
- Assistance for the promotion of ownership of financial institutions by the poor
- Making good use of the comparative advantages of multilateral and bilateral donors

(5) Supporting self-help groups in marginal areas through:

- NGOs helping to identify and promote existing, or establish new, SHGs as local financial intermediaries
- Networks or federations of SHGs
- Linkages of SHGs with regulated financial institutions

6. Frontier Issues and Recommendations

No single player can take the development of rural enterprise and microfinance fully into his own hands, as coordinated interventions are far more likely to be successful. Single players can sometimes achieve great things; but coordinated interventions are far more likely to be successful. Great care is to be taken that interventions do not do more harm than good. This can be the case with well-meaning interest subsidies which may undermine institutional viability; and grants which may discourage local resource mobilisation. The following recommendations therefore go beyond what the Syngenta Foundation can do by itself. But it may interact with other stakeholders in pushing a reform agenda, e.g., concerning the promotion of an adequate legal framework for local financial institutions, effective supervision or the restructuring of agricultural development banks.

1. Local resources mobilisation matters: Donor-driven vs. local initiatives

The importance of local resource mobilisation vs. capital transfer for self-financing, self-reliance, and growth

Source of funds: Internal (local savings, equity, retained earnings) vs. external

Risks: Donor funds discourage local resource mobilisation & growth

Opportunities: Savings mobilisation strengthens the self-reliance and self-financing capacity of rural entrepreneurs, at the same time freeing their credit absorptive capacity for larger loans and investments

Proposal: Capacity building in savings-driven local financial institutions, with a focus on MFIs in semiarid areas

2. Equity matters

Domestic resources can be effectively mobilised through equity instead of deposits by shareholder-driven RMFIs. Equity provided by external investors may bridge liquidity shortages and leverage own resources

Equity-driven RMFIs resources mobilisation through equity mobilised by local shareholders motivated by profit sharing and access to credit

Risks: Inadequate equity curtails growth

Opportunities:
1. Massive mobilisation of unequally distributed local capital in private hands
2. Donor equity leverages savings mobilisation and credit expansion

Proposal:
1. Support initiatives to build equity-driven local RMFIs
2. Invest in locally owned RMFIs

3. Legal framework for local financial institutions matters

A legal framework is important for establishing deposit-taking local financial institutions (microbanks) as self-reliant institutions which can grow dynamically on the basis of local resource mobilisation (savings, equity, retained earnings)

Such regulated financial institutions would be fully integrated within the formal financial sector.

Risks:
1. Non-formal: lack of deposit mobilisation and supervision
2. Formal: Inappropriate regulation and interference by rogue governments

Opportunities: Institutional sustainability and unlimited growth of saver and borrower outreach

Proposal: Support pilot projects in which RMFIs adopt an appropriate legal status

4. Effective supervision matters

The growth of sustainable RMFIs and sustainable financial services is contingent upon effective supervision

Supervision: Supervision of RMFIs, whether deposit-taking or equity-driven, is crucial; supervision must be effective, ie, able and willing to suspend or close non-performing RMFIs

Risks:
1. Ineffective supervision creates false confidence
2. Inappropriate supervision curtails the emergence of RMFIs

Opportunities: Appropriate and effective supervision is conducive to the emergence and growth of a healthy RMFI sector

Proposal: Support auditing of RMFIs by auditing apexes of RMF federations

5. Agricultural development banks (AgDBs) matter:

AgDBs are the largest providers of RMF services

Risks: Unreformed AgDBs waste public resources, lack growth and outreach, undermine rural finance

Opportunities: Reform may lead to sustainable outreach to all segments of the rural population through retail or wholesale services (linkages)

Proposal: Participate in policy dialogue on AgDB reform to expand deposit and credit services to rural entreperneurs

6. Informal finance matters

Informal group-based financial institutions (IFI) of ancient indigenous or recent origin are ubiquitous in much of Asia and Africa, but in contrast to the origins of microfinance in some European countries, they have rarely provided a basis for financial sector development

Informal finance: IFI are widespread and fulfill important functions; but their modern adaptations and their potential in RMF sector development is rarely recognised

Risks: Ignoring IFI as indigenous social capital leads to a continual existence of a dual financial sector and misses the chance of building an inclusive financial sector

Opportunities: Building a culturally integrated, inclusive RMFI sector through strategies such as upgrading IFI, linking IFI with banks, downgrading banks linked to IFI

Proposal: Support pilot projects of upgrading and linking IFI in remote and semi-arid areas

7. Linkages matter

Linkages Between banks and SHGs or MFIs

Risks: Discouraging savings mobilisation and growth

Opportunities: Linkages provide a full range of banking services, including safe-keeping of deposits, access to bank credit, liquidity balancing, equity participation, money transfer, check clearing, payments, monitoring and supervision

Proposal: Support model projects of horizontal networking among non-formal MFIs, incl. SHGs in remote areas (with incentives-driven upgrading), and vertical linkages with banks

8. Good practices matter; best practices risk turning into worst practices

The notion of best practices in RMF may lead to mechanical replication and to strategies which are not adapted to the cultural or economic conditions at a given time. Evidence is needed of the range of more variable and adaptable good practices and the process of their transformation over time.

Best vs. good practices: Only good practices may have the adaptability required in development situations widely varying over space and time

Risks: Insistence on best practices may lead to mechanical replication and inappropriate practices

Opportunities: Appropriate good practices may permit the development of viable RMFIs in rapidly changing or widely varying situations or in nonconducive policy environments

Proposal: Support a variety of good practices (e.g., group lending, individual lending, joint liability, capital injection in undermonetised rural economies) contingent upon socio-cultural situation and policy environment

9. Development matters

Given the emphasis on poverty alleviation, development has become the forgotten half of RMF. Does RMF lead to development and poverty alleviation; or does development as the result of good policy create an environment in which RMF will thrive and effectively contribute to poverty alleviation? Does RMF with its emphasis on the poor and the poorest sustain the poor in poverty or lead to sustainable poverty alleviation and development?

RMF and development: The relationship between RMF, development and poverty alleviation is complex

Risks: A sole emphasis on the poor and poorest undermines both development and the growth of outreach to the poor

Opportunities: Establishing a strong RMF sector for all segments of the population will in due course contribute to poverty alleviation once broader market-driven development processes set in

Proposal: Strengthen RMFIs with services to all segments of rural enterprise

10. Cooperation and co-financing matter

Co-financing of studies and programmes with research funding agencies and international development agencies would not only increase the flow of funds; it would also bridge the gap between basic and applied research; this would lead to more relevant and more systematic research as well as better communication and coordination between the worlds of research and development.

Co-financing of studies and programmes: Cooperation and coordination among research funding agencies and development agencies

Risks: Lack of coordination undermines the effectiveness of both research and development approaches and fosters uncritical and ineffective replications

Opportunities: Learning-based innovations in RMF

Proposals: Support cooperation between research funding and development agencies in RMF

11. Conclusions

- Include among the institutions eligible for support formal, semiformal and informal financial institutions – in private, cooperative, public, community or mixed ownership

- Place a special emphasis on support to small institutions which include people from the lower segments of the population as owners or customers
- Support the development of appropriate legal frameworks, conducive regulation and effective (delegated) supervision of self-reliant and sustainable RMFIs

- Provide incentives-driven schemes for upgrading institutions in terms of legal status, supervision, and outreach

- Support the injection of equity into RMFIs for bridging, leveraging and upgrading purposes

- Support linkages of informal and semiformal RMFIs, including SHGs in remote and marginal areas, with the banking sector and their up grading to the level of regulated institutions as seen fit

- Support RMFIs in establishing business associations with apex services to member institutions

- Support the development of sustainable BDS apex organisations in private ownership or in the hands of business associations of rural entrepreneurs

- Do not support temporary or ad-hoc solutions with no chance of institutional sustainability

- Initiate cooperation between research funding and development agencies in RMF; provide funding for longitudinal impact studies, e.g., of linkages and upgrading of RMFIs

Acronyms

ACSI	Amhara Credit and Savings Institution
AgDB	Agricultural Development Bank
BAIF	Bharatiya Agro Industries Foundation
BDS	Business Development Services
CEFE	Competency-based Economics through Formation of Enterprise
CGT	Cameroon Gatsby Trust
FFGL	Feed and Flour (Ghana) Ltd.
FI	Financial Institution
GTZ	German Technical Cooperation Agency
IFAD	International Fund for Agricultural Development
IFI	Informal Group-based Financial Institutions
IGA	Income-Generating Activities
IITA	International Institute of Tropical Agriculture
MF	Microfinance
MFI	Microfinance Institution
NBFI	Non Bank Financial Institution
NGO	Non-Governmental Organisation
PCFC	People's Credit and Finance Corporation
RB	Rural Bank
RFLC	Rural Finance Learning Centre
RMF	Rural Microfinance
RMFI	Rural Microfinance Financial Institutions
RoSCA	Rotating Savings and Credit Association
R&S	Regulation & Supervision
SACCO	Savings and Credit Co-operative
SFD	Syngenta Foundation Discussion
SHG	Self Help Group
SME	Small and Medium Enterprise
UN	United Nations