Making financial markets work for the poor

THE STATUS OF AGRICULTURAL AND RURAL FINANCIAL SERVICES IN SOUTHERN AFRICA 2011

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FinMark Trust is a non-profit independent trust, working across Africa, funded primarily by the UK's Department for International Development (DFID), and established in March 2002. FinMark Trust's purpose is 'Making financial markets work for the poor, by promoting financial inclusion and regional financial integration'. It does this by conducting research to identify the systemic constraints that prevent financial markets from reaching out to these consumers and by advocating for change on the basis of research findings. Thus, FinMark Trust plays a catalytic role, driven by its purpose to start processes of change that ultimately lead to the development of inclusive financial systems that can benefit all consumers.

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Background to the study

Access to financial services is an important contributor to enterprise productivity the world over. In Sub-Saharan Africa, where most people still live in rural areas and agriculture is the mainstay of the rural economy, access to financial services of all kinds still appears to be poor. Yet, relatively little is known about the demand for, supply of and effective level of access to rural and agricultural finance and about the policies, institutions and many other factors that determine them.

As part of its mission to 'make financial markets work for the poor' in Africa, FinMark Trust commissioned the Centre for Inclusive Banking in Africa in 2010 to undertake a study to examine the current state of rural and agricultural financial services in the Southern African region to enable the development of regional and country level policy frameworks and strategies that will significantly improve access to and the uptake of rural and agricultural finance. The specific objectives identified were:

- to conduct country and regional level assessments of the current state of agricultural and rural finance in Southern Africa
- to identify best practices in agricultural and rural finance in Africa and elsewhere
- to develop an overall policy framework and strategic approach to address agricultural and rural finance challenges at regional and country level
- to assist country level programmes towards operational action and impact in terms of access
- to provide a benchmark for agricultural and rural finance in Southern Africa and to develop a structure for long-term monitoring of progress, and
- to identify a small number of promising projects to assist.

This short report summarises the findings of the first phase of the work, namely, an assessment of the current state of rural and agricultural financial services in the region. The research was carried out in six countries – Botswana, Malawi, Mozambique, South Africa, Zambia and Zimbabwe – drawing mainly on secondary sources. It was completed in June 2011. Fully referenced individual country reports and a regional report are expected to be published in 2012.

1 By Mike de Klerk, Charles Machethe and Gerhard Coetzee, Centre for Inclusive Banking in Africa, University of Pretoria.

Acronyms

AFRACA	African Rural and Agricultural Credit Association
Agribank	Agricultural Development Bank of Zimbabwe
ASCA	Accumulated Savings and Credit Associations
ATM	Automated Teller Machine
BBS	Botswana Building Society
BDC	Botswana Development Corporation
BIFSC	Botswana International Financial Services Centre
BOSCCA	Botswana Savings and Credit Cooperatives Association
BSB	Botswana Savings Bank
CAADP	Comprehensive Africa Agricultural Development Programme
CEDA	Citizens' Entrepreneurial Development Agency
CEPAGRI	Centre for the Promotion of Agriculture
CGAP	Consultative Group to Assist the Poor
ESA	Eastern and Southern Africa
FAO	United Nations' Food and Agriculture Organisation
FEWSNET	Famine Early Warning Systems Network
FSC	Financial Services Company
FSTAP	Financial Sector Technical Assistance Programme
GDP	Gross Domestic Product
IFAD	International Fund for Agricultural Development
IPEX	Institute for Export Promotion
LEA	Local Enterprise Authority
MAFISA	Micro-Agricultural Finance Initiative of South Africa
MAMN	Malawi Microfinance Network
MARDEF	Malawi Rural Development Fund
MDG	Millennium Development Goals
MFI	Microfinance Institution
MFRC	Malawi Rural Finance Company
MSME	Medium, Small and Micro Enterprises
MUSCCO	Malawi Union of Savings and Credit Cooperatives
NACSCUZ	National Association of Credit and Savings Cooperatives
NDB	National Development Bank
NDP	National Development Plan
NGO	Non-Governmental Organisation
PACDE-MESE	Project to Support Private Sector Competitiveness and Development (PACDE) – Business Subsidy Mechanism (MESE) in Mozambique
PAFR	Program of Support for Rural Finance
POSB	People's Own Savings Bank
RBZ	Reserve Bank of Zimbabwe
RHLF	Rural Housing Loan Fund
ROSCA	Rotating Savings and Credit Association
SACCO	Savings and Credit Cooperative
SADC	Southern African Development Community
SAFEX	South African Futures Exchange
SAMAF	South African Microfinance Apex Fund
SEDCO	Small Enterprises Development Corporation
SEDOM	Small Enterprise Development Organisation of Malawi
SEF	Small Enterprise Foundation
SME	Small and Micro Enterprises
VLSA	Village-based Savings and Loan Association
WDB	Women's Development Businesses
ZBS	Zambia Business Survey
ZCFU	Zimbabwe Commercial Farmers Union

Introduction

Despite rapid urbanisation in recent decades, Sub-Saharan Africa's (SSA) population and economy are still predominantly rural and poverty is still primarily a rural phenomenon. The United Nations' International Fund for Agricultural Development (IFAD) reports that more than 70% of the continent's poor live in rural areas and depend mainly on agriculture for their livelihoods. Agriculture provides about 70% of employment and about 30% of the combined Gross Domestic Product (GDP) of SSA.

In Eastern and Southern Africa (ESA) the concentration of poor people is among the highest in the world. Most of the region's estimated 130 million poor live in rural areas and IFAD's research indicates that rural poverty is deepening. In 10 of the 21 countries in the region, average per capita income was less than US$1,10/day in 2009 – below what is generally accepted as the 'extreme poverty' level of income. Growth in the rural economy is slow, in part because arid or semi-arid land makes up almost 40% of the region's land base. Yet, while agricultural productivity is stagnating or decreasing, IFAD reports that more than 85% of the rural population live on land that has medium to high potential for increased productivity. It is the limited use of this natural resource base that leads to low productivity and low incomes in agriculture, which, in turn, limits the inclination of smallholder farmers to invest. This will make it difficult to attain Millennium Development Goals (MDG), especially MDG 1 – the halving of hunger and poverty by 2015 – and the 6% per annum increase in agricultural productivity aimed at by the Comprehensive Africa Agricultural Development Programme (CAADP).

The constraints on agricultural productivity are multiple and well recognized. Many are exogenous, brought about by policies and practices entirely beyond the control of farmers, including low public sector expenditure on agriculture and inadequate infrastructure, producer incentives, marketing structures, extension services, water management, research and development support, and financial services. Public sector expenditure on agriculture seldom reaches the 10% of national budgets agreed to in the 2003 Maputo Declaration. The low public sector expenditure on agriculture is caused partly by the decline in development aid. The collective impact reduces the returns on investment in agriculture to levels which are unattractive to most households and also aggravates the food security situation in the region.

But other constraints are endogenous. While most households that engage in small-scale farming are adequately supplied with labour, many will lack the technical and/or managerial skills to undertake anything but subsistence farming. Furthermore, few households will have the internal capital resources to produce more than occasional surpluses for the market.

It is in this context that the significance of access to financial services (transactional, savings, credit and insurance products and services) becomes clearest. Given the size of the outlays required to cover their annual, medium-term and long-term needs, most commercial farmers – especially annual crop farmers – find it necessary to borrow part or all of the funds needed. Whatever other improvements – for example, to infrastructure or water management – are made to raise the returns that agriculture offers and to encourage subsistence farmers to increase the volume of marketed output, most farmers will have difficulty in producing more for the market and improving food security without adequate access to and greater usage of borrowed capital and other financial services.

Although credit is emphasised above, a similar logic applies to other financial services, such as for savings, insurance, transmission and even foreign exchange. Savings facilities make it easier to accumulate internal capital and encourage less risk-averse behaviour by farmers. Insurance services also promote less risk-averse behaviour by both farmers and service providers. Transmission facilities make it easier to send and receive money, thereby reducing the cost and encouraging remote transactions, for example, to procure farming inputs. Foreign exchange facilities make it easier for farmers and traders to market output and buy other products across borders – a flourishing business in the region. Often the track record built up by using one or more of these facilities lays the foundation for borrowing.

Like advances made in easing any other constraint, improvements in financial services will probably not, on their own, bring about greater investment in productivity or income from agriculture or any other rural enterprise. However, if such improvements are insufficient on their own to ensure progress, they are clearly a sine qua non for such gains. Yet, of the many pre-conditions for agriculture and rural development, the provision of financial services remains one of the most poorly fulfilled across most of Africa and the nature, extent and causes of the deficiencies remain among the most poorly understood.

Objectives, ambit and methodology

Sponsored by FinMark Trust to further its objective of 'making financial markets work for the poor', the study examines the status of agricultural and rural finance in six Southern African countries: Botswana, Malawi, Mozambique, South Africa, Zambia and Zimbabwe. The study aims to understand the nature, extent and causes of the problems and challenges, and, ultimately, to derive a set of proposals for addressing these challenges. The nature and extent of the problems and challenges are gauged by analysing and comparing the demand for and the supply of finance in each country's rural economy. Insight into the causes of the problems and challenges is gained by identifying the factors that have either enabled or disabled progress in the provision of financial services to farmers, other businesses and households. The proposals aim at extending the enablers and eliminating or ameliorating the disablers. This report covers the first phase of the research. The next phase will identify best practices in agricultural and rural finance in the context of SADC. The final phase will develop country-specific policy frameworks and strategies that incorporate such practices, in collaboration with decision makers from the respective countries.

In assessing the gap between demand and supply, attention is paid not only to the effectiveness of rural enterprises' and households' access to financial services – or lack thereof – but also to the appropriateness and sustainability of the products and services offered in relation to their needs. Particular emphasis is given to agricultural financial services, since farming is the dominant economic activity and generator of income and jobs in rural areas. This is done without losing sight, on the one hand, of the importance of financial services for other types of rural business and for rural households' needs as consumers, and, on the other, of the growth of farming as an urban activity. For example, almost half of South Africa's small-scale farmers are now to be found in urban or peri-urban areas.

Bearing in mind the different levels at which policy and practice operate, the enablers and disablers are identified as macro, meso, micro or client level phenomena. An important group of disablers, largely unexplored in the secondary sources drawn on, relate to gender. The barriers faced by many women in the region, especially those in rural communities – which are more likely than urban to be governed by tradition – are highlighted in the Southern African Development Community (SADC) Protocol on Gender and Development, signed in 2008, but not yet ratified by all member states. Finally, while the analysis is conducted on a country-by-country basis and the proposals derived are formulated at country-level, consideration is also given to the implications for regional-level policy and practice in SADC. More detailed analysis of strategic options for the region will follow in a later phase. The information used in this study was obtained from secondary sources, and, in a few instances, from interviews with key informants and stakeholders.

Demand for and supply of agricultural and rural financial services

Demand

This section provides an initial, limited account of the current status of demand for rural financial services on a country-by-country basis.

The nature of secondary data obtainable varies widely, making uniformity in country analyses impossible. In each instance, the overall demand for rural financial services is outlined and, where the data allow, this is followed by an analysis by sub-sector and type. A summary of the evidence is provided at the end of the section. Conclusions about the gap between supply and demand and the effectiveness of access and inclusion are drawn on a country-by-country basis.

Botswana

As in all of the other five countries, the demand for formal sector financial services in Botswana is dominated by households and businesses in urban areas. Although many rural households use financial services supplied by formal institutions, the demand for financial services in rural areas is still overwhelmingly met by informal institutions. The most common form of loans from formal sources for rural people are medium-term loans for the purchase of non-farming assets, such as cars or household appliances, and short term loans for the payment of school fees. While farmers of all sizes and in all lines of production need short-term finance, it is almost exclusively large scale commercial, mainly livestock, farmers who borrow from formal financial institutions. As all but a few small farms are on land without freehold rights, the demand by small-scale farmers for long-term loans, for land purchase and fixed improvements, can be assumed to be relatively small. To the extent that such loans are advanced, it is again almost exclusively to large-scale commercial farmers.

By comparison, low-income households are able to access formal sector savings facilities more freely, despite the reluctance of banks to operate low-balance accounts. About 41% of Botswana's adults have a savings account. However, relatively few have transmission accounts, especially in low income rural communities, partly because of the high cost of transactions. Only 16% of adults have current accounts with commercial banks. Almost the same percentage (14%) have a life assurance policy and nearly 25% have some form of funeral insurance, but no information was found about how many policy-holders are located in rural areas. Agricultural insurance was launched in Botswana in 2010, but information is not yet available about the extent and nature of uptake.

Malawi

In spite of recent reforms, much of Malawi's population – which is overwhelmingly rural – remains effectively excluded from formal financial services. The Consultative Group to Assist the Poor (CGAP) estimated the demand for rural financial services in 2008 to be as much as five times the level of supply. While surveys by government, as well as the FinScope Survey indicate that much of this unmet demand relates to the need for savings and insurance (especially medical insurance) facilities, other information reveals a high level of apparent self-exclusion from available credit facilities by rural people, either on account of age, health or gender or because credit was felt to be too expensive. Recent nominal interest rates charged on formal sector loans to small and micro-enterprises (SMEs) have been close to, or even in excess of 50% per annum, leading to the dominance of informal sector lenders in this segment of the market. It is certainly also true that of the 70% of full-time farmers who are women, many are still effectively unable to seek loans because of domestic traditions which reserve transactions involving credit solely for men.

Mozambique

Most formal financial services are limited to urban areas. FinScope estimates that about 80% of the population is effectively excluded from access either because they reside in rural areas or because they are too poor. Of those that do have access, 12.7% use formal sector services and 9.6% informal. With less than 9% of adults in Mozambique in formal sector jobs and 42% receiving incomes of less than US$200 per annum, the costs of both formal and informal financial services are simply unaffordable to most. Small farmers in Mozambique, especially those who market a significant part of their output, need short and medium term credit, just as their counterparts in most other African countries do. But, in common with so many others, effective demand is limited by high transaction costs, risk aversion and lack of information and education. Furthermore, there appears to be a substantial, though unmeasured, demand for savings and transmission services. All are available in urban areas, but not in rural areas where the majority of the population still lives.

South Africa

The study draws on both the Consumer and Small Business FinScope surveys in 2010, at which point the rural population stood at 11.5 million with 2.4 million rural small business owners. Only 4.6% of rural individuals and 36.8% rural small business owners said that they used formal savings facilities. In respect of credit, 3.7% of the rural population and 3.2% of rural small businesses indicated that they had access to formal credit. Only 2.5% of rural small business owners borrow from the bank with 0.7% using other formal means of attaining credit. However, 3.3% of rural small business owners borrow from friends and family. In terms of insurance, 12.5% of rural small business owners indicated that they have formal insurance with just 9.5% of rural individuals' reporting that they make use of insurance. Medical aid, physical asset insurance and life cover were the main purposes for which insurance cover was obtained. Only 17.4% of the rural population and 36.4% of rural small business owners indicated that they have formal transactional accounts. It is clear that access to financial services in rural areas is more difficult than in urban areas, both for individuals and for small enterprises, including farms.

Zambia

The 2009 FinScope survey and the 2010 Zambia Business Survey (ZBS) provide a considerable depth of insight into the nature and particularly the constraints on the demand for financial services in rural areas in Zambia. The approach goes beyond merely equating usage with demand to investigate the degree to which the effective supply of the various types of service (determined by assessing the level of access) is matched by effective demand (measured by usage). Where the level of access is low, the surveys go on to diagnose the reasons for this and where demand falls short of supply, as it does in all instances, they identify what it is that is constraining demand.

About 62% of the country's adults live in rural areas and more than half of rural adults earn the greatest part, if not all, of their income from agriculture. Of the five countries in this summary for which FinScope collects data – only Zimbabwe is excluded – the level of usage of formal and informal financial services is second lowest in Zambia, exceeded only in Mozambique. About 18% of rural adults in Zambia use formal services of some kind, of whom less than half have bank accounts, while about 24% use informal services. The percentages are similar for farmers, a little lower for formal services and a little higher for informal, confirming the relative importance of the role of savings and credit groups for small farmers, as in most other countries in the region. Nearly two thirds of rural adults (66%) still do not make use of any kind of financial service, including 62% of farmers.

Of the services used, 14% of rural adults have savings accounts, 10% take advantage of transactional facilities and only 3% have some kind of insurance cover. Surprisingly, more than 20% of rural adults are the recipients of credit – significantly more than when the previous FinScope survey was conducted in 2005 and more than in urban areas (14%). For farmers, all of the comparative percentages are substantially lower: 3% for savings, 7% for transactions, 1% for insurance and only 9% for credit, suggesting that most rural people who borrow do so for consumption smoothing, not for agricultural production.

While this paints a picture of effective demand that is valuable on its own, it is in their assessment of the gap between the levels of actual usage and effective access and their diagnosis of the underlying causes of the gap that the two surveys are most revealing. In respect of products/services marketed by formal sector financial institutions, for what the ZBS adjudges to be the most accessible form of account as a benchmark for accessibility – the Xapit cell-phone based savings/transactions account marketed by Zanaco (formerly a state-owned institution established to enhance access to finance, particularly in rural areas) – the survey finds that as many as 34% of agricultural MSMEs and 38% of all rural MSMEs do not face any significant constraints to opening such an account. In relation to these levels of access, the ZBS records 27% of agricultural MSMEs and only 15% of rural MSMEs as being banked, that is, using any form of service offered by formal sector banking institutions. At least 7% of farmers and 23% of all rural entrepreneurs therefore choose not to open a bank account when they are well-positioned to do so. (Unfortunately, no comparable information is available for informal sector financial services).

What are the main reasons for self-exclusion and involuntary exclusion? Despite hundreds of thousands of individuals and MSMEs in Zambia's rural areas still being more than fifty kilometres from the nearest banking institution, the fact that more than 40% report being less than an hour's travel away from such facilities suggests than physical distance is no longer the key barrier to access for many. While still being the third most frequent reason given for not using a banking service, only 22% of MSME owners identified distance as a critical factor. By far the most important reason reported in the ZBS survey was that enterprises simply did not generate enough income to warrant opening a bank account that would be used mainly for cash storage (62% of respondents) and that they had no need for such accounts (34%). Low levels of education, poor command of English (when almost all documentation is in English) and general lack of financial literacy impose other significant barriers to access.

These are all fundamentally demand-driven constraints. By comparison, those that one might regard as being more supply-related – such as fees or minimum balances being too high – appear to be fairly minor reasons, as they were all reported by less than 10% of respondents. In addition, only small percentages of unbanked individuals expressed an inherent preference for using informal MFIs, suggesting that formal banking services would be preferred, if accessible.

While supply-driven constraints should in no way be ignored in designing policy to increase financial access, what is clear is that broad-based measures that will boost economic development and enterprise growth – and therefore the demand for financial services – are most important for increasing financial inclusion. Of course, greater financial inclusion would assist such growth, but, as the ZBS concludes: 'it is critical to acknowledge that, in the face of other significant barriers to business development, finance on its own is unlikely to engender growth'.

Zimbabwe

Although there is little recent statistical information on the demand for rural financial services in Zimbabwe, perceptive analysis of available material by the country specialist was able to generate considerable insight.

One of the few areas in which recent statistical data are available is on the demand for credit by Model A1 (largely subsistence resettlement smallholders) and A2 (commercialising resettlement small and medium-scale farmers) rural households respectively. In a 2010 field study, 45% of the former and 65% of the latter who were interviewed (including as many as 70-80% of medium-scale A2 farmers) said that they would take out agricultural loans, if financial institutions began to offer them. Credit offered at present – almost entirely by government – is only for short-term purposes and one can only guess at the level of unfulfilled medium and long-term demand. As in the instance of Zambia, there are reasons to expect that the uptake of medium-term credit for the purchase of machinery, livestock and some kinds of fixed improvement, such as fencing, would be considerable if available, while for long-term loans it would not be as great, given the predominance of traditional/communal land rights and the political instability in the market for freehold land. Such medium-term lending and leasing facilities, when available, are provided by formal sector institutions to commercial farmers.

However, in contrast to most other African countries, relatively little use is currently made of microcredit in Zimbabwe. Most formal and informal microlenders were wiped out either by the financial asset destruction caused by hyperinflation leading up to dollarization in 2009 or have found it impossible to compete with subsidised lending for agricultural inputs by government. The recent decline in the latter can be expected to regenerate demand for formal and informal microfinance institution (MFI) credit.

Conversely, the culture of saving is reported to be strong in Zimbabwe, difficult economic times notwithstanding. The demand for savings facilities is driven by non-agricultural 'seasons', for example, the need in January to pay school fees and buy school uniforms.

Because conventional money transmission services have, until recently, only been available in urban areas, rural demand has been met through the informal 'courier' services provided by bus and taxi drivers. As in many other countries in ESA, cell phone transmission services are now beginning to come on-stream. There is no data yet on the extent of uptake, but, if patterns elsewhere in the region are a guide, the demand for these convenient, relatively secure, low-cost services is likely to be substantial and largely eclipse the demand for alternative transmission facilities.

A feature of demand which is particularly prominent in Zimbabwe, but which is also known to exist in most other countries in the region, is the need by small, informal cross-border traders (some of who are farmers) for foreign exchange services. Informal cross-border trade in agricultural products, mainly maize, rice and beans, amounts to tens of thousands of tons or hundreds of thousands of US dollars in most months (FEWSNET, 2011) and the number of traders registered (excluding the many who are not) also runs into the tens of thousands. At present, this involves the carrying and keeping of substantial amounts of foreign exchange, with all of the attendant security risks, which better access to banking facilities could do much to reduce. In response, some Zimbabwean banks are understood to be experimenting with foreign exchange cards for such traders, but it remains to be seen whether the uptake will be substantial, given the exposure to taxation and to unexpected and unwelcome intervention by the country's monetary authorities, as well as to the deduction of transactions charges, that it will entail.

Summary

To the extent that valid generalisation is possible in the absence of better data and estimation techniques, the information available, together with overall patterns of demand in comparable low-income rural communities, suggests that:

- the demand for savings and transmission services is currently greatest and most widespread and would probably be near-universal, were facilities readily accessible;
- the demand for credit is perhaps not as pervasive, but is nevertheless substantial and widespread; it is also more seasonal and less price sensitive; taken over consumers' life cycles, it is likely to be almost universal as well; it is presently mostly of a short-term nature, though a significant and increasing proportion is for medium and longer-term purposes and is used for buying assets such as cars and houses; the proportion of demand for farming needs depends very much on the extent of commercial production in an area; regardless of scale, commercial farmers' needs are predominantly for short-term credit (of up to 12 months); the demand for medium-term loans is much smaller and is mainly for moveable asset (machinery and livestock) purchases; other than in freehold tenure areas, the demand for long-term loans is small and is mainly for fixed improvements;
- the demand for insurance is presently much smaller and mainly for non-farming purposes such as funeral, medical and life cover, followed by asset insurance – for houses and cars; other than in the large-scale commercial farming sector, little of the demand is likely to be for farming purposes, even in smallholder cash crop areas (coffee, cotton, sugar and tobacco are currently most important in the region); the demand for insurance among such smallholders can be expected to grow as transactions costs come down to more affordable levels; area-specific cover for climate risks should become significantly less expensive, following the development of automated rainfall and temperature data-capturing systems, experimentation with index insurance approaches, especially if small scale commodity producers become better organised;
- the demand for foreign exchange services by informal, small cross-border traders (some farmers) is already substantial and can be expected to grow as regional free trade policy takes effect.

Without question, the principle known in economics as 'Say's Law' (supply creates its own demand) applies to rural financial services: poor supply almost certainly suppresses or at least conceals demand. As rural communities' access to financial services improves, as the financial products on offer become better aligned with their needs and as transactions costs fall and the sustainability of such products and services grows, so demand that is not presently evident will grow. With the spread of mobile phones and other IT-based innovations driving these processes faster than was imaginable only a few years ago, it can confidently be expected that the demand for all of the products and services just referred to will expand and that it will respond positively to the development of products and services not yet on offer.

Supply

In this section, the current status of the supply of agricultural and rural financial services in each of the six countries is assessed. Key role players are identified and, where possible, details of the types, volumes and values of service are provided. In contrast to demand, the information available on supply is extensive.

Botswana

While Botswana has a well-established formal financial sector, the rural financial landscape is still dominated by informal suppliers, mostly located in small towns and larger villages.

The main focus of government intervention to date has been macro-economic stability and access to financial services by both commercial and subsistence farmers has been a low priority. However, in terms of the current National Development Plan (NDP 10), efforts are to be made to improve access to financial services for agriculture, to enhance food security and economic diversification. As part of the strategy, government aims to reduce the high costs of operating banking services in rural areas. Besides improving physical infrastructure, government intends to intensify consumer education, promote competition between suppliers of rural financial services and incentivise innovations in rural banking. Smartcard payments will also be encouraged.

The most important public sector financial institutions with some degree of rural outreach are:

- the Botswana Savings Bank (BSB), established in 1911;
- the National Development Bank (NDB), established in 1964 – about 20% of its loan portfolio is in agriculture;
- the Botswana Development Corporation (BDC), established in 1970 to invest in commercial and industrial projects, some of which are in rural areas, through the provision of loans and equity finance;
- the Credit Guarantee Scheme, a subsidiary of the BDC established in 1999 to assist small and medium enterprises access credit;
- the Financial Services Company (FSC), established as a subsidiary of BDC and NDB, mostly to offer property loans;
- the Botswana Building Society (BBS), originally established as a branch of the South African United Building Society in 1970 and incorporated in Botswana in 1977;
- the Citizens' Entrepreneurial Development Agency (CEDA), which provides development loans at subsidised rates mainly to rural entrepreneurs; and
- the Botswana International Financial Services Centre (BIFSC), established in 2010 to facilitate the delivery of a range of cross-border financial services to clients in other countries in the region.

Following policy reforms in 1990, nine commercial banks have established themselves in Botswana. Licensing does not require nationwide presence or rural branches. Consequently, branches are located only in major and a few smaller urban centres. An ongoing concern has been that commercial banks are poorly geared to provide financial services to lower income groups, but, following the mobile phone companies' lead in supplying money transmission services, several commercial banks are now offering transactional and other services on a mobile phone basis. FinScope's most recent survey showed that 29% of Botswana's population used mobile phone banking services in 2009, although it is not known what proportion of users were located in rural areas.

Of the various non-bank private sector financial institutions, only a few formal sector MFIs, such as the Women's Finance House, are likely to be significantly involved in the rural economy. However, registered and informal sector savings cooperatives are widespread in Botswana's peri-urban and rural areas. Many also provide limited credit facilities. Similarly, microlenders, or cash loan shops, abound and are now regulated by the Non-Banking Financial Institutions Act. On the other hand, particularly since Botswana was classified as a middle income country, few international donors and local NGOs have made grants for rural projects. Those that do provide grants have not focused on rural finance.

Support for formal and informal MFIs is provided by, among others, the Botswana Savings and Credit Cooperatives Association (BOSCCA) which assists cooperative societies in Botswana with auditing, training of staff and other business-related assistance, and the Local Enterprise Authority (LEA), a state-owned organisation which offers business planning and financial management training to MSMEs and potential clients.

Agricultural insurance was launched by a private sector service provider in Botswana in 2010 with the aim of facilitating the commercialisation of agriculture. While the company insures both crops and livestock and is understood to have designed its products to try to keep premiums as low as possible, in practice, its services are likely to be confined chiefly, if not exclusively, to large and medium scale commercial farmers.



Malawi

The eleven licensed commercial banks currently operating in Malawi provide a standard range of services including savings, credit and transmission facilities and foreign exchange and insurance services. In terms of physical accessibility, Malawi is ahead of many other countries in the region. Although most bank branches are located in larger or smaller urban areas, in relation to the geography and population distribution, branches are reasonably well spread across the various districts and mobile banks and agencies supplement brick-and-mortar branches.

However, bringing down transactions costs is still a challenge, especially for very small accounts. With some minimum savings balances starting at as little as US$3.50, even the relatively low charges involved in opening and maintaining accounts make costs of using commercial bank facilities prohibitive for many low-income potential clients. As the use of mobile phones spreads, outreach into rural areas will increase greatly and transactions costs should fall, both acting to bring commercial banking services within the reach of many more poor rural households and enterprises.

Given the historical limitations on access to commercial banks' financial services for the country's predominantly rural, agricultural, low-income households, the roles played by public sector financial institutions and formal and informal MFIs have been crucial. Chief among the public sector role-players have been state agricultural and development banks and the Post Office. The Malawi Rural Finance Company (MFRC) has an extensive network, including six branches and twenty sub-branches that have targeted mainly, but not only, small farmers. About 60% of its loans have been advanced to groups.

Institutions operating in similar fields include the Malawi Rural Development Fund (MARDEF), the Small Enterprise Development Organisation of Malawi (SEDOM) and PRIDE Malawi. MARDEF was set up and funded by government specifically to provide loans to rural groups, many of which are involved in agro-processing, while SEDOM's target market has been wider and the organisation has been supported by both government and donors. PRIDE provides standard working capital loans mainly to female borrowers engaged in urban activities. All struggle with sustainability, given the highly subsidised rates at which they lend and it remains to be seen whether they will survive the current fiscal crisis in the country. Especially because of the precariousness of public rural finance institutions, the ongoing role played by the IFAD-supported Rural Livelihoods Support Programme is crucial in providing loan capital and technical assistance to a range of agricultural and other rural development initiatives.

Insurance products and services, all provided by formal sector firms, are still geared mainly towards the urban, higher-income market. However, rainfall-indexed drought insurance for cash crop farmers, including options for seed and machinery finance, is now beginning to be offered. Affordability is a key issue for both insurers and low-income farmers, but so is the need to ensure greater understanding of what insurance products are and their benefits, especially in relatively poorly educated rural communities.

While Malawi has a well-established formal and informal MFI sector, some of whose members cater for the needs of rural clients, two constraints under which the sector currently operates limit its impact: the first is that, because MFIs are not yet regulated by the Reserve Bank of Malawi, they are prohibited from collecting voluntary deposits from the public, effectively precluding them from offering savings and transmission facilities; and the second is that, partly because of their financing structure, most of their lending is for periods of not longer than six months, making it difficult to finance many sorts of annual crops through MFI credit.

The inadequacy and exclusive nature of formal sector financial institutions, as well as the regulatory requirements, have led to the proliferation of informal services. The country's informal sector savings and credit cooperatives (SACCOs), village-based savings and loan associations (VLSAs), and individual moneylenders (*katapilas*) are less subject to restrictions on deposit taking. Unlike most other African countries, where they are more like traditional social structures embedded within strong social and economic networks, there are relatively few SACCOs in Malawi and fewer still that are rural-based. Most important from the perspective of access are ease of entry and flexibility as to the form of collateral for borrowing and the small minimum balances required for saving: entry involves payment of a small application fee and an initial minimum purchase of shares, which may amount to no more than US$7, while collateral may take the form of movable assets, including livestock. Minimum balances on savings accounts are sometimes as low as US$3.50. While the size of SACCOs varies considerably – from less than 100 members to almost 25 000 – membership is mostly between 1 000 and 5 000.

VLSAs are much smaller than SACCOs – typically only 15 to 25 strong – and are built on the rotating savings and credit association (ROSCA) model. Major advantages for the rural poor are that they operate in remote areas not served by other financial institutions and that they generally offer a return on savings higher than most other service providers, partly because, being operated on a voluntary basis, their costs are low. But because an end date is normally specified at the time of formation, the duration of many VLSAs may be too short for them to be well-suited to the needs of annual crop farming. No data was traced as to the number of VLSAs in Malawi, although many are given technical support by CARE International.

Katapilas provide short-term loans at short notice without necessarily requiring security, but at relatively high interest rates. Loans are typically payable within a few weeks or months and are generally repaid in a single instalment. Borrowers are usually known to moneylenders, who use familiarity as a substitute for collateral. Lending is based on ability to repay, with the lender taking little interest in the use of the funds, which, it can reasonably be assumed, is seldom for agriculture. Interest charged on loans is high compared to formal sources, but borrowers agree to this because of convenience and ease of access – loans are granted quickly and with hardly any questions asked – and because often no other alternative sources exist at the time of need. The number of katapilas is unknown, but they are known to operate in almost every community.

The two main support institutions, other than IFAD and CARE International, are the Malawi Union of Savings and Credit Cooperatives (MUSCCO) and the Malawi Microfinance Network (MAMN). MUSCCO is a 59-member apex body with a central finance facility to which its members have access. In addition to training and capacity building, it conducts monthly field visits and audits and requires members to submit monthly performance reports. MAMN is a formally incorporated professional association with 20 member institutions. It offers donor-funded training courses to develop and promote microfinance activities and ensures that good governance and practices, particularly in respect of loan portfolio management, are adhered to.

Mozambique

Mozambique's sixteen commercial banks, in common with most of their counterparts in the region, are only peripherally involved in agricultural lending and, to the extent that they are involved, provide services only to large-scale commercial farming enterprises engaged in producing sugar cane, tea, cotton and cashew nuts. The Land Bank, a public-private partnership, also offers commercial loans to all players in food and fibre value chains. Beyond this, it works with partners to assist associations of small farmers to develop their enterprises in order to position them to borrow and repay loans. About 120 MFIs have operating licences, but are thought to have no more than about 10% of the market at present.

The Bank of Mozambique provides incentives, such as lower reserve requirements for institutions with rural branches that engage actively in developing and marketing financial products and services geared to the needs of the rural population. Other public initiatives include:

- government's Program of Support for Rural Finance (PAFR), which has three components: institutional, policy and legislative support, an innovation and outreach facility, and support for community-based financial institutions such as accumulated savings and credit associations (ASCAs) and VSLAs; it also offers technical and financial support to financial institutions starting up in rural areas, partly through subsidising the cost of building new facilities;

- IPEX, the Institute for Export Promotion, which helps entrepreneurs, particularly in agriculture, to participate in international fairs to promote Mozambique's export products;
- CEPAGRI, the Centre for the Promotion of Agriculture, a recently established organisation which undertakes analyses of projects and sources of investment for the agricultural sector;
- PACDE-MESE, the Business Subsidy Mechanism, an instrument designed to strengthen small and medium enterprises, some of which are in rural areas;
- FSTAP, the Financial Sector Technical Assistance Programme, a lead financial sector development initiative, with backing from government and the World Bank.

While donor support is generally strong in Mozambique, not many multilateral and bilateral donor institutions are active in the rural economy. However, those that do are playing a leading role in developing rural financial systems, providing loan capital and educating enterprises and households on financial matters. Few of Mozambique's MFIs operate in rural areas, but informal institutions, such as ASCAs play an important role, even though the total value of their savings and lending is small.

Some recent innovations are the first weather-based index insurance products on offer for agricultural production, even though these will only be taken up initially by large scale commercial enterprises. Much more important for rural people at large, is the commencement of mobile phone based money transmission services, which will surely be followed, before long, by additional financial services, as has happened in neighbouring countries. Government has also recently launched a rural savings mobilisation campaign and the Central Bank has published a strategy to bring more banks to rural areas.

South Africa

South Africa has one of the most advanced financial sectors in the region providing financial services that are on par with those available in developed countries. The sector is dominated by a small group of large commercial banks whose business focuses mainly on urban areas and middle to high-income households and formal enterprises, including the country's 30 000 commercial farming units, to which it is now the major supplier of financial services. The financial needs of the extensive low-income sector of the rural economy, including an estimated 2.4 million rural business owners (this includes those who engage in some form of farming, mostly for domestic consumption), are catered for mainly by informal service providers, although the past decade has seen a number of developments that are now quite rapidly bringing low-income rural households and enterprises into the sphere of formal sector financial services.

A number of public sector institutions are also involved in supporting the development of the rural economy. The most important of these include:

- the Land Bank, which is mandated to provide financial services to all farmers, especially the historically disadvantaged; it has a network of 27 branches and 45 satellites and suites of products geared specifically to the needs of the large scale commercial agribusinesses which account for more than 95% of its loan book, on the one hand, and the small scale emerging farmers who account for the growing, but still small, balance, on the other;
- the Development Bank of Southern Africa, whose main activity is the financing of public sector infrastructure in the region, some of which is in rural areas and benefits agriculture more or less directly, for example water and energy reticulation, roads;

- PostBank, which through the country's extensive network of post offices, many in rural areas, has provided savings and transmission facilities for many years and is now beginning to offer some insurance products. The organisation has recently received permission from government to corporatize and is seeking a full banking licence;
- the South African Microfinance Apex Fund (SAMAF), launched in 2006 with the objective of increasing the outreach of the registered MFI industry more effectively into low-income rural areas through the provision of loan capital to industry members; it also facilitates management and systems development as well as other forms of capacity building and training;
- the Micro-Agricultural Finance Initiative of South Africa (MAFISA), an apex system which provides loan portfolio indemnity to accredited financial intermediaries to encourage the extension of credit to emerging farmers who have demonstrated the capacity, or are considered to have the potential, to service and repay loans, but who lack sufficient collateral; also launched in 2006, its implementation has been disappointingly slow, its beneficiaries few and its sustainability questionable;
- Khula Enterprise Finance, a state-owned national wholesaler of finance for enterprise development, which recently received approval from government to provide retail financial services to micro and small enterprises. This new venture is in a planning and testing phase. In the past, the organisation's wholesale and guarantee services struggled to gain traction in the market;
- the Industrial Development Corporation also finances agriculturally related activities. However it prioritises large scale operations focused on the export market and post harvest production activities in the agricultural value chain.

Initiatives (co-funded by donors) with substantial outreach in rural communities include:

- the Rural Housing Loan Fund (RHLF), which wholesales funding to accredited intermediaries to lend for the purchase or construction of houses in rural areas; after 15 years of operation in 2010, more than 300 000 rural home-owners had benefited and, despite some debt write-off, the Fund has still been able to show a significant re-investable surplus annually;
- the Small Enterprise Foundation (SEF), a non-profit microcredit institution operating in several of South Africa's poorest provinces; it targets groups of women, particularly in rural areas, using a Grameen-type model which requires that the groups have accumulated savings prior to receiving a loan; lending on average about R2 000 to groups consisting of about five individuals; at the end of 2010, the total value of loans advanced since inception in 1992 was R1.1 billion to more than 730 000 clients; with a debt write-off rate of less than 1% in most years and a current client portfolio of over 60 000 clients, it is firmly self-sustaining.

Another similar, but smaller, initiative is the Women's Development Businesses (WDB), a private sector and donor-funded trust. The trust follows the same methodology as SEF, but has found it difficult to establish adequate information systems. Estimated client numbers exceed 40 000, and like SEF, most of its activities finance rural micro enterprises. There are a number of similar suppliers operating in South Africa, with SEF, WDB and Marang Financial services being the largest (all with more than 20 000 clients each).

Given South Africa's middle income country status, there have not been many multilateral/bilateral donor-funded programmes to enhance access to and/or the appropriateness of financial services to low-income households and entrepreneurs in recent years. However, one example is the CARE International programme to help VSLAs, similar to its counterpart in Malawi. Another is the initiative undertaken jointly by the four largest commercial banks and Postbank to provide low cost Mzansi savings and transmission facilities, targeted at the low-income market. By 2009, more that 6 million such accounts had been opened, amounting to about 60% of the target market.

Popular informal ROSCAs, called stokvels, operate in low-income communities throughout the country, as do burial societies. Both have variants that make advances against members' savings.

Statutory regulatory bodies of most direct relevance are: the Banking Regulator, which focuses mostly on prudential requirements; the National Credit Regulator, which is tasked with ensuring that credit is not advanced beyond the means of borrowers, particularly to low-income groups; and the Financial Services Board, which supervises the operation of non-bank financial institutions and service providers.

Key non-bank private sector financial service providers of most direct importance to the rural enterprises are: the South African Futures Exchange (SAFEX), a derivatives market specializing in agricultural commodities, now widely used by commercial agriculture and agro-processors to manage price risks – its warehouse receipts are accepted by most commercial lenders as collateral; a number of insurance companies which offer crop and farming asset insurance products; a range of IT companies which provide MFI systems and service packages; and several for-profit and non-profit MFI training institutions.

Zambia

The main suppliers of financial services to agriculture and the rural economy at large, by value, are Zambia's five large and thirteen smaller commercial banks. Prior to the liberalisation of the financial sector in 1992, commercial banks were obliged to operate an extensive network of branches not only in urban but also in rural areas. After liberalisation, the number of rural branches dropped considerably, but has started growing again. At the end of 2009 there were 65 rural branches (BOZ, 2009), supported by about 400 urban and a smaller number of rural ATMs.

Commercial banks largely provide financial services to medium and large scale commercial enterprises and for crop marketing (mainly funding the Food Reserve Agency for maize marketing). However, one large commercial bank, Zanaco, does provide a range of financial services to smallholder farmers through the Lima scheme that it operates with the Zambia National Farmers Union. The scheme currently serves more than 2 000 farmers.

The role of commercial banks in the agricultural and rural sector is increasing as more banks are opening branches in rural areas and technological innovations, particularly mobile phones, are making it easier for them to extend their services in rural areas. Other initiatives include partnerships: for example, Zanaco recently partnered with Zambia Postal Services (Zampost) to utilise the postal services infrastructure to extend its rural presence.

Non-bank formal sector participation in rural financial service provision has been mainly in the form of supply chain finance. Generally, the supplier is a large lead firm that is able to purchase inputs in bulk. 'Outgrower' schemes that make use of such finance have developed in the cotton, tobacco and seed production industries. While the cotton schemes involve only smallholder farmers, the tobacco schemes work both with smallholders and with commercial farmers. For seed suppliers, the outgrower schemes are primarily with commercial farmers. Supply chain finance is a dominant source of production finance in all three instances.

The rapid spread of mobile phones has provided a new channel for expanding rural financial services. Among the institutions that have taken an early lead are, Zanaco, CelPay, Mobile Transactions Zambia and Airtel. Competition in the provision of mobile banking is growing rapidly, as is demonstrated by the impending entry of a fifth major mobile phone service provider, MTN.

Another consequence of liberalisation was the entry of MFIs into the rural, low-income market. MFIs' share of the market is growing but is still very small. The performance of MFIs in Zambia has generally been below expectation. However, the introduction of Microfinance Regulations in 2006 and subsequent assistance from offshore initiatives, such as the IFAD-supported Rural Finance Programme, appear to have had a positive impact. In at least one instance, they have facilitated the transformation of an MFI into a public liability company.

In the post-financial liberalisation period, informal financial service providers have become major suppliers of financial services to low income people in rural areas. FinScope's Zambia 2009 study found that 16% of rural adults used informal financial products as opposed to only 9% for formal non-bank products. Informal suppliers include money-lenders (known locally as kalobas), rotating savings and credit associations (ROSCAs) known as chilimbas, and accumulated savings and credit associations (ASCAs).

Most moneylenders offer short-term unsecured loans at high interest rates, typically 100% per month. Loans are used to finance a wide range of needs including school fees, medical fees, funeral expenses, small business assets, food, entertainment and even the servicing of MFI weekly repayments. Loan repayment is generally done via a single instalment. Prospective customers who are not known to a moneylender must be introduced by an existing well-known customer and are in most cases required to secure the loan with movable collateral (radios, bicycles, etc). 12.9% of Zambian adults borrowed from moneylenders in 2009, according to FinScope. Neither the number of moneylenders in Zambia, nor the percentage active in rural areas is known.

ROSCAs are popular among women in both urban and rural areas. ROSCA members make a periodic collection that is pooled and given to individual members in rotation. Slightly over 7% of Zambian adults borrow money from informal savings clubs such as ROSCAs and ASCAs (FinScope Zambia, 2009).

ASCAs are similar to ROSCAs but are more flexible and responsive to group members' demands. Groups typically consist of 15 to 30 members who make weekly contributions. After about one month, members can apply for a loan, with savers benefiting from interest paid by borrowers (typically 10% per month). Many such loans are known to be used for income generating activities. The Rural Finance Programme has made the spread of SACCOs and ASCAs one of its main thrusts since 2007.

Zimbabwe

The provision of rural finance in Zimbabwe has gone through a series of phases driven by developments in the political economy and their impact on macro and microeconomic policy. As the main function of this section is to outline the supply of financial services to the rural economy as it exists at present, reference to previous phases and political economic events, radical though their influence may have been at the time, is limited to those that still exert a significant influence on the present. The two major, interrelated historical developments that shape the current environment of agriculture and agricultural/rural financial services in Zimbabwe are the government's land acquisition policy that took effect in 2000 and hyper-inflation in 2007-8.

Following the fast track land reform from 2000 to the end of 2008, government, the Reserve Bank of Zimbabwe, through the almost-fiscal role that it played as a subsidiser and director of public rural finance resources until 2009, farmer contracting agencies and NGOs became the main suppliers of finance to rural smallholders and large scale farmers. The commercial banks, previously major players, have been able to provide little credit to either of these groups because of the lack of secure land-based collateral. Even the 99-year leases given to new land occupants by government have provided no substitute, being non-transferable. A further consequence has been a sharp reduction in the already small number of commercial bank branches in rural areas. Unique among the commercial banks is the Commercial Bank of Zimbabwe: as a small institution, it has focused on microlending to SMEs, but is now moving into microinsurance, microleasing and low-income housing finance. It is unknown what proportion of these activities is conducted in rural areas.

The Agricultural Development Bank of Zimbabwe (Agribank), a public institution that was also previously an important financial service provider, has struggled to source external capital for much the same reason, more so because of its mandate to lend for what most potential investors have seen as high risk farming activities.

The result has been an acute lack of liquidity, not limited to agriculture and rural finance, which government has been trying to find sustainable ways of countering since 2000, not helped by the reluctance of many of the major multilateral and bilateral donor agencies to become involved in a turbulent situation.

One component of a solution has been the reshaping of the public sector Post Office Savings Bank into the People's Own Savings Bank (POSB). It has the most extensive network of branches in the financial/communications sector – 185 at present – distributed throughout urban and rural areas. And, from being only a licensed deposit-taking institution, it has now entered the small loans market, using borrowers' savings and salary streams (which are required to pass through a POSB account) as collateral. A further new role that it is playing is that of wholesaler of funds to MFIs. While this is materially improving low-income rural clients' access to credit, a limitation from an agricultural point of view is that POSB's six-month repayment period is too short to make its loans suitable for financing many agricultural activities, most critically the annual grain crops which form the foundation of most households' diets. In addition, along with some commercial banks, POSB is now acting as an agent for some of the big international money transmission companies.

Another public institution which has played a role in providing loan capital for rural enterprises is the Small Enterprises Development Corporation (SEDCO). However, given its dependence on the tightly constrained national budget for capital and its high debt write-off rate, it is not clear how sustainable its role will be.

As in many other countries in ESA, multilateral and bilateral donor organisations have played a very important historical role in capitalising and providing technical support for MFIs in Zimbabwe, though, despite an acute need on the ground, their involvement in recent years has not been as great. In part this is very likely a consequence of the difficult political environment, but, as noted earlier, many MFIs were simply unable to survive the de-capitalisation brought about by hyperinflation and the competition of government-subsidised credit. Between 2003 and 2010, the number of registered MFIs fell from about 1 700 to barely more than 100, with the number of SACCOs which were members of the National Association of Credit and Savings Cooperatives (NACSCUZ) declining from more than 200 in 2006, to probably less than 100 that were functional at the end of 2010.

CARE International's programme of assistance to VSLAs in the region also operates in Zimbabwe and has continued in spite of the difficult political environment. It is not known how the external difficulties that afflicted MFIs and SACCOs have affected the number of VSLAs and ROSCAs. US and Danish aid has been used to provide the capital for revolving loan funds from which MFIs may borrow for on-lending. In partnership with a large commercial bank, a similar fund has also been created to meet the credit needs of smaller commercial farmers. The Zimbabwe Commercial Farmers Union (ZCFU) has been influential in mobilising other credit lines for its members – mainly the category A2 beneficiaries of land reform – from non-bank financial service providers, especially farming input supply companies.

Too recent for its impact to be measurable, the entrance of mobile phone based technology appears likely to revolutionise rural communities' access to financial services in Zimbabwe, just as it has done elsewhere in the region. Services already in operation or being tested include savings deposits and withdrawals, money transmission and bill payments and the direct deposit of the proceeds of tobacco and cotton auctions into farmers' bank accounts. With the choice to view such services as unwelcome competition or a new market opportunity, some banks have begun to form partnerships with mobile phone companies. Either way, rural enterprises and households will certainly benefit.

Not surprisingly, the agricultural insurance industry suffered seriously from land reform and hyperinflation, to the point that it almost stopped operating. While it is still struggling, the more favourable circumstances of the past two or three years have led to a revival and new products lines, targeted especially at smaller commercial producers, are now on offer. These include cover for crops, livestock, fixed and movable assets as well as goods in transit. A small commodity exchange has also been established and its warehouse receipts can be expected to provide a source of collateral for loans to emerging commercial farmers.

Finally, it was noted earlier that in response to the needs of informal small cross-border traders, some Zimbabwean banks are now known to be experimenting with card facilities for such traders.

Summary

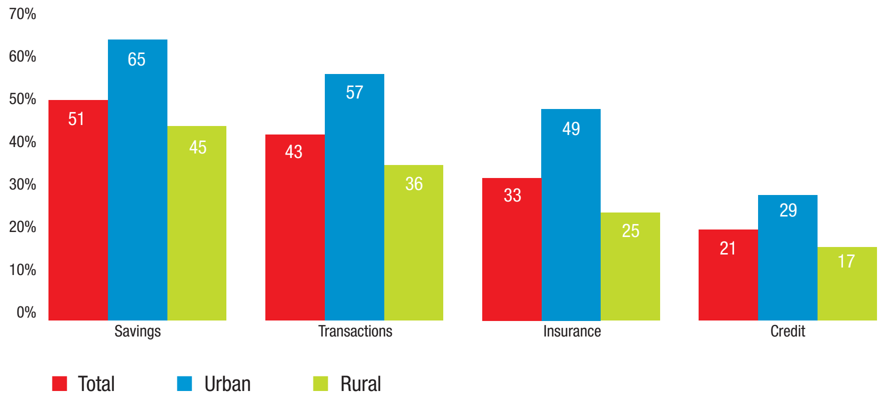
There are some clear common features among the six countries studied:

- The range of services provided by commercial banks and formal sector non-bank institutions to agriculture and the rural economy at large is similar to those available in other countries, whether more or less developed, but their availability is restricted almost entirely to medium and large-scale commercial agriculture. In Zimbabwe, given the uncertainty of land tenure, even long established commercial farmers are often unable to access standard financial services. However, the competition now being experienced from financial service providers partnering with mobile phone companies is putting increasing pressure on commercial banks to use mobile phone platforms to market their own products to low-income clients in rural areas. This is making them less expensive and more accessible to all users and is rapidly drawing low-income rural households and enterprises into the realm of formal sector banking, although other than in South Africa, the numbers are still quite small. It must be noted that the mobile based services are in almost all cases transactional and related services, with little if any credit provided through this platform.
- Public sector institutions are important in providing financial services to the rural economy, but decreasingly in the form of direct retail lending and grants/subsidies, and increasingly by way of creating an enabling and regulating environment, support services, the wholesaling of loan capital for on-lending and the provision of post office-associated savings facilities (which create the collateral foundation for adding credit services).
- Formal sector MFIs, often supported by multilateral or bilateral-financed NGOs, are significant suppliers of services that suit low-income rural households' and enterprises' financial needs. These NGOs have also played a crucial role in driving the growth and accessibility of rural – especially agricultural – financial services.
- Despite these developments, informal financial service providers – from voluntary savings and credit associations to individual moneylenders – still play a very important role in fulfilling low-income users' needs. This is primarily because they are the point of entry of most users into the greater rural financial services system, given the difficulty that most banks and formal MFIs experience in reaching out into rural areas. By number, though not by value, they are still the major source of financial services to this large category of users in most of the six countries, and the efforts that are being made to improve the services that they offer and their sustainability are in no way misplaced.

Access to and inclusion in rural financial services

The FinScope's 2009 survey of Botswana found that about 58% of adults in rural areas operated some form of formal or informal sector account. Of these, about 25% had a formal bank account of some kind, 22% used formal non-bank services and 11% informal sector services. While this was lower than the 76% in cities and towns, it is the highest rate of rural inclusion in the six countries in the study. Savings accounts are most widely used – 45% of rural people had one – followed by transactions accounts (36%), insurance (25%) and loans (17%). The percentages suggest that those who are banked use two or more of these facilities. Figure 1 compares the utilisation of the respective facilities in Botswana's rural and urban areas.

Figure 1: Access to formal financial services by area in Botswana (Napier, 2008)



In respect of loans made to rural people, the five most frequent sources were (in descending order): savings clubs, family/friends, formal sector bank personal loans, formal sector banks vehicle loans and public sector loans for business development. Clearly, at least where loans are concerned, even in relatively advanced Botswana, informal financial services are still the most widely used by rural people.

In Malawi, FinScope's 2008 survey found that only 45% of adults made use of any form of financial service, formal or informal, with women in rural areas the least likely to do so. Farmers found it particularly difficult to access credit: as the generator of close to 40% of GDP, agriculture accounted for only about 8% of total lending. Inclusion also appeared to be closely associated with levels of income, education and financial literacy.

Of the six countries in the study, financial inclusion appears to be lowest in Mozambique, where just 22% of the adult population use any form of financial service, a little more than half from formal institutions and the balance from informal. This places Mozambique lowest in the seventeen African countries in which FinScope surveys have been conducted or initiated. Urban-rural disparities compound exclusion for rural people: of the 12% that do use formal sector financial services, about 3% are located in rural areas. Only 2% of adults reported having borrowed from formal sector institutions, only 6% have formal sector savings accounts and only 5% have formal sector insurance cover.

In South Africa, rapid strides are being made to bring formal banking services to potential users. The FinScope 2010 survey shows that the percentage of the adult population of 33,4 million that use at least one formal bank service rose to 63%, substantially up from 47% in 2005. Bearing in mind the widespread barriers that women face in accessing financial services in SADC as a whole, it is significant that the percentage of adult women who use formal bank services is almost the same, namely 62%. In fact, when formal non-bank financial services are added, the percentage of women that use formal sector financial services as a whole (68%) is marginally greater than the percentage of men (67%) and the percentage of women using informal financial services (11%) is also greater than men (7%), bringing the inclusion rate to 79% for women and 74% for men.

In rural areas, the percentage using some form of formal banking services in 2010 was 49, rising to 56 if formal non-bank financial services are included. One of the biggest contributors to the increase between 2009 and 2010 was mobile phone based banking: in the country as a whole, the percentage using mobile phone banking services jumped from 5% to 13% during the year. The percentage of rural adults who used mobile banking services in 2010 was 6%. Among insurance services, burial insurance was the most widely used by rural people – 17% of rural adults in 2010 – followed by life cover (12%) and asset insurance (3%).

In Zambia, access and inclusion appear to be increasing, but are still at low levels. FinScope 2009 records almost 18% of rural adults as using one or more formal sector financial services, with non-banking services (about 15%) being considerably more widely accessed than banking (about 9%). Informal sector financial services are the most widely used by rural people (almost 24%). For farmers, the figures are similar – an indication of the importance of value chain credit from farm input suppliers and output processors. This leaves about 66% of rural adults unserved by any kind of financial institution. For farmers, the exclusion rate is a little lower (about 62%). What is crucial is that the overall usage rate, at least in respect of MSMEs, is significantly below the effective access rate to formal sector financial services, both for rural adults as a whole and for farmers as a key sub-group, indicating that there are important constraints on demand at play. The nature of these was explored earlier in this report.

Assembling the findings, despite data limitations, it seems clear that in terms of access to formal sector banking and non-banking services, the six countries divide themselves into two distinct groups: the two middle income countries, Botswana and South Africa, on the one hand, and the four low income countries, Malawi, Mozambique, Zambia and Zimbabwe, on the other. In the first, the banked percentage is well over 50% and increasing quite rapidly; in the second, it is much lower – the best reported being 14% of rural adults in Zambia (increasing to 23% if formal non-bank financial services are included) – and the rate of increase is uncertain. The gap is presently enormous, but it can be anticipated that the rapid spread of mobile telephony will bring about a substantial reduction in the disparity over the coming decade.

In respect of inclusion in formal MFI and/or informal financial services, there is no clear distinction between the middle and the low income countries. In fact, with the exception of Zimbabwe, where the impact of the period of hyperinflation is still being felt, there is a 'reverse gap', with poorer countries providing better MFI/informal networks and better access than their richer neighbours. As formal sector inclusion grows, the role played by the informal sector can be expected to diminish, although the latter will, without doubt, remain critical for a long time, especially for the poorest households in both rural and urban areas.

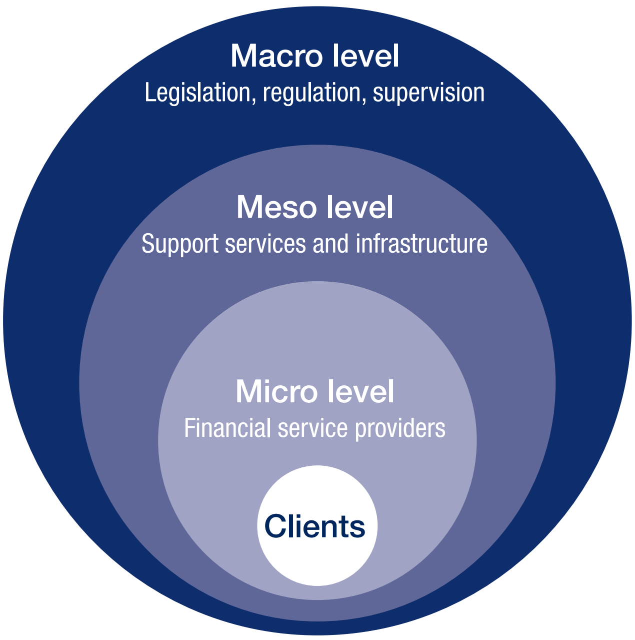
Disabling and enabling factors

If the overall objective is to steadily increase the level of access, ultimately to reach total voluntary inclusion, key questions to ask are: what makes it difficult or impossible to access financial services? And, conversely, what makes it easier or more possible to do so? The former identifies disabling and the latter enabling factors operating in financial services systems. Following many international analyses, it has now become standard practice to divide these into client, micro, meso and macro levels.

At the client level, in the context of this study, the focus is on the demand needs of individual rural households and enterprises, particularly those in lower income groups, and the supply impact of financial systems on them. At the micro level, it is on the retail financial service providers, formal and informal, that offer services to such clients; at the meso, on the financial systems, infrastructure (including support services such as auditing and credit bureaux), products and services; and at the macro, on the legislative, policy (including broad macroeconomic variables such as trade and foreign exchange regimes) and regulatory frameworks. Figure 2 illustrates the relationship between the levels.

In the summary that follows, influences that have, on balance, tended to assist the improvement of access to and/or the quality/appropriateness of financial products and services delivered in rural areas are categorised as predominantly enabling factors. The qualification of their description as enablers follows from the diversity of experience in the six countries: in some, the factors referred to have been unquestionably enabling, while in others their impact has been more ambivalent, perhaps even unfavourable in some respects. Where they differ fundamentally between countries, they are categorised in table 1 (on page 29) as both enabling and disabling. Factors that have tended, on balance, to influence access to financial services negatively are described as predominantly disabling.

Figure 2: Levels of the financial system and their interrelationship



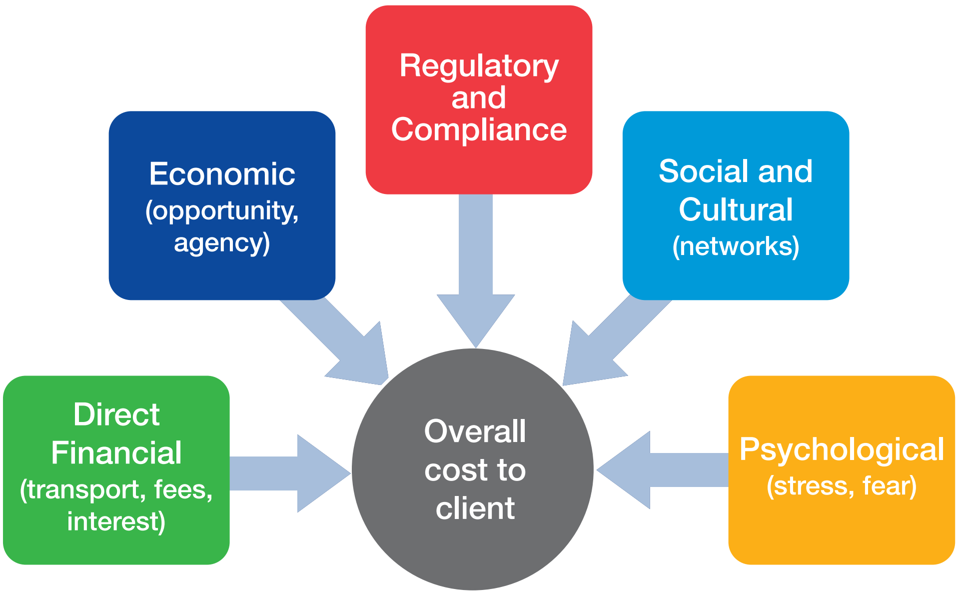
Predominantly disabling factors

Client level

Demand-damping concerns about financial services raised by low-income potential or actual consumers in rural areas include the high costs entailed in accessing formal services. These involve not only recurrent transactions costs and interest payments – but also the unseen, but very real, costs to rural residents entailed in travelling long distances to access formal sector services, such as fuel or bus/taxi fares and the opportunity cost of losing hours or days of work.

In Zambia, where most MSMEs appear to use bank accounts mainly as safe deposits, the low level and infrequency of income was found to be the biggest single constraint on demand for financial services. Other possible demand inhibitors include fear of asset seizure if loans are not repaid and fear of applications for services being rejected. To some extent, these may be the result of another demand inhibitor, namely, ignorance of how financial services operate and the conditions attached, that is, financial illiteracy. There may also be significant social costs, for example, if shifting to a formal from a local informal service provider involves 'closing an account' with a friend, relative or influential member of the community. The outcome is sometimes a preference for using an alternative, more familiar local service provider – usually in the informal sector and often considerably more expensive than a formal banking service – or simply forgoing the use of that service, that is, self-exclusion. Figure 3 illustrates the range of costs to clients that may accompany transactions with formal financial institutions.

Figure 3: Cost to clients to interact with formal financial intermediaries



Also a significant inhibitor of demand in some countries, though under-documented, not explored on a country-by-country basis in the study and therefore not included in Table 1 (page 29), is the gender-based disablement that many women probably suffer. Numerous studies the world over – some conducted in SADC countries – attest to the key role that women play in agricultural production and to the significantly better credit risk that they represent than men but, at the same time, to the disproportionately small share of credit that is advanced to them. A 1990 study of credit schemes conducted in five African countries, including Malawi, Zambia and Zimbabwe, found that women received less than 10% of credit directed to smallholders and only 1% of total agricultural credit. A leading analyst from the United Nations' Food and Agriculture Organisation (FAO) concluded that 'while (these findings are)… somewhat out-of-date, the pattern is still approximately the same today in many countries' (Norton, 2004, 329), although the 2009 FinScope study does reflect significant improvement in Zambia.

Among the reasons for the pro-male bias are:

- under some legal and customary systems, married (and often also unmarried adult) women are regarded as minors and cannot therefore apply for or make any decisions about loans on their own;
- women sometimes lack the literacy and numeracy to understand credit systems and financial transactions as they often have limited access to educational opportunities, compared to men;
- cultural barriers may limit women's ability to engage in financial transactions, especially in the formal sector, as well as sometimes restricting their mobility;
- credit is in some instances channelled through organisations to which women cannot belong.

As rural communities tend to adhere to tradition longer than urban communities, evidence from Zambia (despite recent improvements in gender equity) indicates that the incidence of these biases is higher in rural areas than in cities and towns. Slowness by some of the six countries to ratify, sign and implement the 2008 SADC Protocol on Gender and Development, aimed at removing or reducing gender biases, must be regarded as an important rural finance demand disabler.

Micro and meso levels

On the supply side, barriers to entry are raised by, among others, applying risk assessment criteria that are often difficult to meet, such as high minimum income levels and strict security requirements. Often, too, product design is not geared to the needs and circumstances of the low-income consumers who make up the great majority of rural residents in all six countries, especially farmers. Examples are high minimum savings balances (designed to offset high administration costs) and loan repayment periods that are too short to accommodate many agricultural cash flow cycles.

Another supply constraint is the high unit cost of servicing small-turnover, low-value client groups, widely dispersed in poor rural areas. This is at least partly responsible for the high charges and high interest rates that act as demand disablers, although poor public infrastructure and lack of competition also play a part. Costs are likely to be particularly high if local telecommunications systems are inadequate to operate financial services through mobile phones.

Macro level

Monetary and fiscal/exchange rate management – through steady improvements in almost all of the six countries, the macroeconomic environment has become more favourable for rural financial inclusion over the past decade or so; against this, a major ongoing weakness is continued dependence on foreign subvention of national budgets in all except Botswana and South Africa. Also, in some of the six countries, issues such as sub-market interest rate ceilings remain a disabler.

Financial regulatory systems – these have generally improved too, though much remains to be done, for example, to increase the stability of MFIs, to induce prudential structures that equip financial institutions to engage more sustainably in agricultural lending and to oblige financial institutions to collect and publish or submit sufficient data to the monetary authorities to enable the risks that they face and the competence of their management to be assessed adequately.

Road infrastructure – this has been slow to develop because of high costs and tight budget constraints; while this has been critical historically, it is becoming less so as mobile phone-based and other forms of branchless banking come on stream, for example, through using petrol stations and retail stores as agencies. On the other hand, road infrastructure is of the utmost importance to support the economic activities that underpin financial activities.

Energy or power infrastructure – this is critical for the development of the rural economy and the accompanying demand for financial services. It also enables rural financial service branches, agencies and automated teller machines (ATMs) to operate and banks to take advantage of branchless banking opportunities. The problem is alleviated by the substitutability of generators, solar panels and other power sources for grid electricity, all of which come at a cost.

Communication infrastructure – development has been limited historically by high fixed line installation costs and public sector budget constraints, but is now accelerating through the use of mobile phone, satellite and fibre optic technologies and the employment of private capital to fund installation costs.

Rural finance infrastructure – the physical infrastructure required, for example bank/agency buildings and ATMs, has been slow to develop or, in some instances, has regressed. However, the development of privately-owned communications infrastructure and accompanying changes in public policy and legislation/regulation have made it possible for mobile phone technology to be used as a platform for accessing financial services, where policy and legislation have adapted accordingly, thereby more than offsetting the lag in physical infrastructure.

Property rights – the traditional non-freehold land tenure systems that predominate in most of the six countries remove land as a source of collateral, thereby making access to credit more difficult; an offsetting advantage is that this also reduces the need for long term loans; alternative forms of security are steadily being developed, even if they are less than perfect substitutes for land.

Predominantly enabling factors

Political environment – with some exceptions, such as Zimbabwe, the political environment is generally more favourable than unfavourable, with most governments prioritising rural development – including rural financial systems – but implementation lags far behind policy in many countries.

Market liberalisation – in almost all six countries, the weakness of its own capacity to deliver rural financial services at retail level has been appreciated by government, the market has been opened and major reliance is now placed on private formal and informal suppliers; however there is much room for public-private partnerships to assist the entry of private sector.

Public sector rural finance support – the approach now emerging places the public sector primarily in an enabling environment generating role, through political and macroeconomic policy, market liberalisation and by formalising, regulating and, in partnership with multilateral/bilateral donors, supporting growing numbers of MFIs and informal rural finance groups with capital and technical assistance.

Social grants – at least three of the countries – Mozambique, South Africa and Zambia – have instituted social grant programmes to address the poverty in which much of their populations live, to the extent that their national budgets allow; rural communities, in particular, have benefited from these programmes and not only has this begun to stimulate the demand for financial services, especially savings facilities, but the need to ensure timely, secure, accurate distribution of the grants is prompting the development of financial transmission systems; in South Africa, nearly half of grants flowing into rural areas now do so through electronic transmission into the bank accounts that recipients have opened, making many banked for the first time; especially with the spread of mobile phones, these advances in financial access can be expected to extend into other countries in the region. Table 1 summarises the incidence of enablers and disablers in the six countries.

Table 1: Factors that are enabling (E) or disabling (D) for the development of agricultural/rural financial services in the six countries

	Botswana	Malawi	Mozambique	South Africa	Zambia	Zimbabwe
Macro/Environmental factors						
Income inequalities	D	D		D		
Fiscal and monetary policy	E	D	D	E+D	E	D
Credit act/regulation		D	D	E+D		
Exchange rate policy	E					
Property rights		D	D	D	E	D
Public sector capacity		D	D	D		
Political commitment to rural development		E	E	E	E	
Financial assistance policy	E+D					
National development plan	E		E			
Market liberalisation	E		E	E+D	E	
Public sector finance institutions	E	E	E	E	E	
Rural finance support institutions	E	E	E	E		E
Road infrastructure	D	D	D	E+D	D	D
Communication infrastructure	E+D	D	E	E+D	E	E+D
Electricity infrastructure	E+D	D	D	E+D	E+D	E+D
Financial sector infrastructure	E+D		D			
Micro/Meso factors						
Risk assessment procedures	D		D	D	D	D
Product design (terms and conditions)	D	D	D	D	D	D
Price			D	D	D	D
Service delivery (telecommunication)	E+D			E+D	D	E+D
Type of product	E		D	D	D	D
Client factors						
Concern about costs	E	D	D	D	E+D	D
Preference for alternative providers	D	D		D		D
Fear of being rejected	D	D	D	D		D
Ignorance	D		D	D		D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Recommendations

A review of the nature of demand and supply and of factors that inhibit or enhance them throws up a substantial list of actions that would help accelerate, broaden and deepen the delivery of financial services to low-income communities in rural areas and attune it more closely to their needs. While most are inherently national or local-level interventions, a number are also amenable to regional-level initiatives. The recommendations below are grouped accordingly. They focus mainly on public policy and practice, but also have implications for private sector and NGO action, and are in no way exhaustive. It is important to note that these are preliminary recommendations emanating from the first phase of research being conducted by FinMark Trust and that more specific recommendations for action will be provided after the second phase, will identify international best practices in rural and agricultural financial services appropriate for application in the SADC region.

Recommendations for national or local-level action

Demand-related

- Support further research and make fuller use of research findings to gain deeper insight into the nature and magnitude of the demand for financial services in low-income rural communities and to inform policy and strategy to expand demand.
- Focus on removing or reducing gender-based demand barriers to which many women are subject.
- Cut red tape wherever possible to facilitate the spread of mobile phone-based or other forms of branchless banking while protecting the integrity of transactions.
- Conduct financial literacy campaigns in communities with low average education levels (concentrated in rural areas), especially among commercialising small scale farmers and SMEs.
- Work with local groups that include formal authorities, traditional authorities and farmer/non-farmer community members to find consensual ways of enabling tenure systems to evolve to increase the use of land by farmers who wish to produce more for the market.
- Work with and incentivise established commodity organisations to assist the formation of smallholder commodity producer groups to boost market size and reduce unit transaction costs and risks (also supply-related).
- Prioritise reducing rural infrastructure backlogs, especially in respect of roads, power (and water) reticulation and communications (also supply-related).

Supply-related

- Give the development and accessibility of savings, transmission, insurance and foreign exchange facilities a higher profile, as foundation-layers for loans, in public and private sector strategies to enhance agricultural and other rural economic activities, including trade.
- Adopt a comprehensive value-chain approach – as opposed to an exclusively small farmer-focused approach – to the financing of agriculture.
- Explore the current extent and importance of supply chain finance and find ways of supporting its growth.
- Improve the quality and quantity of data collected and submitted to monetary authorities by financial institutions.
- Support the development of specialist agricultural units within banks.

- Strengthen rural finance knowledge management services to capture and disseminate information on best practices, to assist action research-based best practice innovation and to facilitate adoption into policy and practice through dialogue and advocacy.
- Re-examine and, if possible, lower the levels at which exclusionary risk-related client entry criteria are set.
- Consider and, if possible, extend the period of short term loans to accommodate small farmers' cash flow cycles.
- Enlarge the area of land available for freehold tenure by smallholder commercialising farmers.
- Intensify the search for and experiment with alternatives to land-based collateral, including non-collateral based group (and individual) lending techniques in use in other countries and also other collateral substitutes – such as warehouse receipt systems and equipment leasing.
- Develop and/or more actively enforce mechanisms to promote competition among rural formal sector financial service providers and to prevent their collusion to exclude new competitors, in particular those using mobile phone platforms to enter the rural financial services market.
- Facilitate and, where appropriate, collaborate with initiatives by multilateral/bilateral/other donor agencies to advance the outreach, appropriateness and sustainability of formal and informal rural financial services.
- Evaluate and, where appropriate, collaborate with donor initiatives to use loan guarantee mechanisms to underwrite and promote formal sector lending to small scale agriculture and other rural SMEs.
- Extend the regulation of and capital access support provided to formal sector MFIs.
- Use the platform created by existing sustainable public financial institution networks, such as post office savings bank services, to develop and offer an expanded range of rural financial services.

Recommendations for regional-level action

As noted above, most of the initiatives that should be implemented to promote the development of rural financial services are the prerogative of national and/or local-level institutions. However, there are some valuable potential roles for a regional-level body or bodies in promoting, supporting and coordinating these initiatives. Some roles call for a body that has banking powers, but most do not. The recommendations below are drawn from a recent report commissioned as part of SADC's preparations to formulate a Regional Agricultural Policy. [2]

Actions that could be carried out by a regional non-bank institution

- Promoting, supporting and coordinating across countries all of the initiatives mentioned above.
- Working closely with other organisations whose goals are to improve access to and the appropriateness of agricultural/rural finance services in the region, such as the Southern Africa chapter of the African Rural and Agricultural Credit Association (AFRACA) and, where opportune, broadening, deepening and accelerating activities aimed at achieving these goals; liaising with relevant agricultural/rural financial institutions abroad, such as the FAO and IFAD.
- Gathering and disseminating information on best practices in respect of norms, governance, risk management, regulation and monitoring/evaluation to national-level bodies/central banks, partly to assist policy and practice harmonisation (a prerequisite for regional financial integration).
- Developing regional training facilities to help national bodies educate and build the capacity of retail financial services providers to take advantage of innovations in agricultural/rural financial services; also to help smaller clients to understand and manage the use of financial services.

2 Note that these recommendations are based on the findings of FinMark Trust research, which were used to inform SADC's RAP formulation process.

- Facilitating the development of innovations to broaden outreach and/or reduce transaction costs (particularly those with cross-border potential), such as branchless banking by cell-phone or through regional retail store chains, petrol stations and supply chain based finance, but also drawing attention to the need for good public policy to govern such initiatives, for example, in respect of promoting competition and ensuring information/transaction security.
- Exploring the feasibility and advisability of a regional agricultural commodity exchange, with accompanying information dissemination and trading account based credit systems.
- Collaborating with multilateral and bilateral offshore and SADC national and local-level financial institutions in the design, phasing in and phasing out of subsidies and part-guarantees.
- Advising on and helping broker the formation of public-private financial services partnerships, for example, for private sector banks to make and manage loans partly underwritten by a regional/national body.
- Directing as many as possible of the activities that it engages in specifically towards assisting SADC member states to implement their undertakings regarding the elimination or reduction of gender discrimination.

Actions that could best be carried out by an institution with banking powers

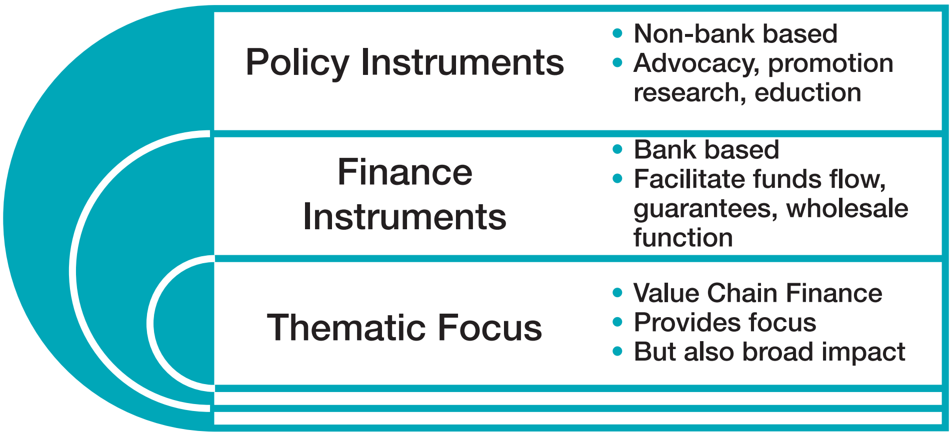
- Raising offshore resources and providing a conduit to national/local financial institutions to capitalize or subsidise the current costs of agricultural/rural financial service providers, especially for innovations.
- Acting as part-guarantor of national or local government-level loan facilities.

To provide a single focus for all of these actions, it may help to centre them on improving agricultural value chain finance, with all of the interventions at policy, industry, supply and client level that this entails. But, in essence, only two initiatives for the region are recommended:

- The establishment of a (non-bank) institution whose functions would be liaison, research and development (desk and action-based), education, dissemination, advocacy, brokering and advice – all with the goal of developing the supply of and demand for agricultural/rural financial services at the macro, meso, micro and client levels in SADC member states; the natural partners at national level for all of these activities would be the respective central banks; to save time and, quite likely, cost, these functions could be outsourced to an existing specialist agency or agencies.
- The inclusion of a specialist agricultural/rural financial services arm in whatever form of regional bank or development fund the region may decide to set up.

Particularly, if a regional development finance institution/bank does materialise before too long – and it is understood that consideration is being given to this – it is greatly in both initiatives' favour if they could be located relatively quickly and inexpensively in existing institutions: the first in one or more development research/facilitation agencies and the second in the regional development finance institution/bank. Figure 4 summarises the roles of a regional institution or institutions.

Figure 4: Roles of proposed regional institutions



This report summarises the forthcoming regional and individual country reports that will provide more detail on the findings of the six country studies. The publication of these reports will mark the conclusion of the first phase of FinMark Trust's programme to improve access to and the uptake of rural and agricultural financial services in the region. The findings and recommendations of these reports will serve to focus, contextualize and inform the forthcoming study of African and international best practices in agricultural and rural financial services – the second phase of FinMark's programme – and the development of corresponding regional and country-specific policy and strategy frameworks – the third phase.

FinMark Trust looks forward to working with stakeholders in the region to achieve the programme's goals.

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