Cooperative Finance In Developing Economies

2012 International Year of Cooperatives

Edited by
Onafowokan O. Oluyombo

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FOREWORD

Cooperatives are part of my family history. This is perhaps the main reason why I am so happy to write a foreword to this book published in 2012, the International Year of Cooperatives as declared by the United Nations General Assembly. This history started in January 1889 in Urmitz, my home village in Germany, when 15 people founded a cooperative savings and credit association, among them six farmers and six small entrepreneurs. Each member bought a share of 1 Mark (*approximately one day's wage at the time*) and contributed 2 Mark of savings. Annual interest rates were set at 3.5% on deposits and 5.5% on credit balances. At minimal costs and no loan losses, the association turned a profit from the first year onwards. Several factors contributed to its growth: forty years of prior history of a self-help movement, the existence of a federation from which the association borrowed 15,000 Mark, and the passing of a revised cooperative law in May 1889 which did away with greatly disliked joint liability. In 1934 credit cooperatives came under the banking law. Ever since, Urmitz had its own Raiffeisen Bank, where my family held its accounts. Today the village has its own industrial zone, with financial services provided by the Raiffeisen Bank, now a branch of a larger, impressive cooperative banking entity covering several neighboring villages.

The relevance of this history lies in its relationship to poverty, self-help, development and, last not least, legal recognition. The idea of cooperative self-help associations had come up during the famine of 1846/47 when many in Germany lost their property to moneylenders, or their life. The first initiative, by Raiffeisen, mayor of a small village across the Rhine from Urmitz, was charitable. But this was not sustainable, and limited in outreach. This is where a parliamentarian, Schulze-Delitzsch stepped in. He introduced the concept of self-reliant self-help groups, functioning as local banks. They were owned, managed and governed by their members, and self-financed from shares, savings and retained earnings. The first urban group, later called *People's Bank*, was established in 1850/52, followed in 1864 by the first rural group, later called Raiffeisen Bank. The groups soon formed federations and central funds for back-up services, including liquidity exchange, auditing, linkages with commercial banks, and advocacy. A crucial issue was legal status, at a time when any grassroots movement raised the suspicion of the Government. As a parliamentarian in Berlin, Schulze-Delitzsch was able to move the legislative process forward. This led to the first Prussian cooperative law in 1867, expanded nationally in 1871/73 and revised in 1889. By 1914 there were 19,000 credit cooperatives in Germany, backed up by a complex institutional infrastructure. Every village had its Raiffeisen Bank, every part of a city its People's Bank. Today, 30 million, out of a population of 83 million, have an account with a cooperative bank in Germany.

Here are the basic tenets as they evolved in Germany, replicable, on principle, in any country, albeit over a much shorter time period: self-help and self-reliance based on savings mobilization; self-determination and self-governance, keeping government at bay; local area outreach and local enterprise promotion, with lasting house-banking relationships; individual savings and credit accounts rather than group credit; limited liability (together with collateralized lending) having replaced joint liability (after 1889); a legal and regulatory framework integrating credit cooperatives into the formal financial sector; indirect (delegated

or auxiliary) prudential supervision[1] through auditing federations, enabling the central bank to effectively supervise large numbers of small institutions.

After 1889, as the movement spread around the world, these elements were generally applied in Western countries, like the Netherlands and Canada where champions of Raiffeisen introduced cooperative finance in 1896/97 and 1900, respectively. The most spectacular growth occurred in British India, where Sir Frederick Nicholson had been sent to Europe in 1894 to study solutions to the perennial problem of extortion by moneylenders and rural poverty. He came back with a report, summarized in two words: "Find Raiffeisen!" recommending the introduction of cooperative credit societies modeled after those in Germany. Several experiments were made (pilot projects in today's parlance) and evaluated by a committee. In 1904, this led to the passing of a *Co-operative Credit Societies Act* both in India (and also in Burma), the first of its kind in the colonies. Self-financing and self-governance kept the movement growing, resulting in some 50,000 societies within 25 years. As C. F. Strickland[2], registrar of cooperatives in India, noted in 1922: "The credit movement of British India is not working with official money: about 50 per cent of its capital consists of small shares contributed by the members and the surplus accumulated from the interest on their borrowings: another 10 per cent consists of deposits by the members themselves: the remainder is commercial credit.

The societies are not managed by government or by officials: they are in the hands of their members, subject to an audit prescribed by and carried out by non-officials under a decreasing official supervision". But in contrast to Germany and other Western countries, in India it was the government which had taken the initiative – a "pre-natal defect" in the words of a contemporary writer[3], followed eventually by state governments taking over the governance and financing of the credit cooperative system. Government was not kept at bay, and the result was disastrous. As of 2006, 51% out of 106,000 primary agricultural cooperative societies[4], and 26% out of 1,112 cooperative banks, incurred losses[5]. India is now struggling with a gigantic task: restructuring and reforming the credit cooperative sector, in a country where 135 million shareholders of credit cooperatives form a constituency of voters no state government is willing to ignore at election time. Over the past fifty years, many developing countries and their international donors have engaged in similar forms of irresponsible finance, mostly setting up state-owned agricultural or cooperative development banks and using credit cooperatives as channels of subsidized credit, thus undermining their self-reliance and sustainability.

How to proceed establishing a credit cooperative movement if no champions are forthcoming, like Schulze-Delitzsch and Raiffeisen 1847 in Germany, d'Andrimont 1864 in Belgium, Luzzatti 1865 in Italy, Desjardins 1900 in Canada and many others? In all these cases, the government has been kept at bay. Is there a role for government in credit cooperative development? The experience of India has been mixed: a positive limited role of government during the first third, and a rather negative, interventionist role during the second half of the

[1] Cf. Carlos E. Cuevas and Klaus Fischer, Cooperative Financial Institutions: Issues in Governance, Regulation, and Supervision. World Bank Working Paper No. 82. Washington D.C.: World Bank, 2006

[2] C.F. Strickland, An Introduction to Co-operation in India. London: Milford, and Bombay: Oxford University Press, 1922, p. 51

[3] Bernard Huss, People's Banks, or Use and Value of Co-operative Credit. Natal, 1924, p. 83

[4] PACS, functioning predominantly as credit cooperatives.

[5] NABARD, Annual Report 2006-2007. Mumbai: NABARD, 2007, p.87

20th century. A fresh start has been taken in Andhra Pradesh in 1995, with the passing of a new Mutually Aided Cooperative Societies (MACS)[1] Act, placing their governance fully in the hands of elected members and submitting them to their own rules and regulations, without an involvement of government; other states followed with similar laws. Since then 164,000 federations of self-help groups have been registered in India under such laws[2] – a hopeful fresh start for responsible cooperative finance.

The most inspiring case presented in this book[3] for a strong and constructive role of government in credit cooperative development has evolved since 1993 in Vietnam. The People's Credit Funds, seemingly a paradox, are a genuine self-help movement, yet one which has gained its strength and vitality from the government which has appointed the central bank as their regulator, training agency and supervisor, yet without undue interference. The government has not used them as credit channels, and has not spoiled them with subsidies. To the contrary, the PCFs pay income tax up to 28%, varying by province.

The experience of most developing countries with cooperative credit has been mixed, including Nigeria's, which in a way is also part of my personal history. As a student at Ibadan University (now University of Ibadan), I first came across the *esusu* in 1963/64, a ubiquitous savings and credit association, with different names in the various parts of Nigeria, which I later learned existed in many countries, and in Nigeria as early as the 16th century. They met all the tenets listed above as success factors of the German movement, except two: federation formation and a legal and regulatory framework. Strickland's verdict against them in 1934 was one reason why they were disregarded.[4] In 2012, they are still the most widespread financial institution in Nigeria, in terms of numbers and outreach; but the few efforts at *modernizing* them and bringing them into the formal financial sector have failed, as shown in this book.[5]

Moving away from German credit cooperatives, the *esusu* inspired me to my first book publication, on *Indigenous Cooperatives in Africa*.[6] They also made me an advocate of *upgrading informal financial institutions such as self-help groups (SHGs)*, or, where this was not feasible, linking them to banks[7], propagated as *SHG linkage banking* by APRACA in Asia Asia and AFRACA in Africa, including Nigeria. In India, SHG banking has enabled 7.5 million SHGs, informal cooperatives with 100 million members, to open bank savings

[1] In contrast to *government*-aided cooperatives.
[2] N. Srinivasan, Microfinance India, State of the Sector Report 2010. New Delhi: Sage Publications, pp. 29-30.
[3] Seibel and Thac, Growth and Resilience of Credit Cooperatives in Vietnam
[4] C.F. Strickland, Report on the Introduction of Cooperative Societies into Nigeria. Lagos: Government Printer, 1934
[5] Marx and Seibel, The Evolution of Financial Cooperatives in Nigeria
[6] H. D. Seibel and Michael Koll, Einheimische Genossenschaften in Afrika/Indigenous Cooperatives in Africa. Bertelsmann Universitätsverlag, 1968
[7] Seibel and Marx, Mobilization of Personal Savings: through Cooperative Societies or Indigenous Savings and Credit Associations? Case Studies from Nigeria. Third International Symposium on the Mobilization of Personal Savings in Developing Countries, Yaoundé 1984. New York: United Nations, 1985; Seibel, Saving for Development: A Linkage Model for Informal and Formal Financial Markets. Quarterly Journal of International Agriculture (Berlin) 24/4, 1985: 290-298; Seibel, Old and New Worlds of Microfinance in Europe and Asia. Pp. 40-57 in: Aditya Goenka and David Henley, eds., Southeast Asia's Credit Revolution: From Moneylenders to Microfinance. London: Routledge, 2010

accounts; 4.8 million SHGs have a bank loan outstanding (31/3/2011), paralleled by the emergence of 164,000 cooperative SHG federations.[1]

Perhaps there are lessons to be learned by Nigeria and other countries when it comes to cooperative finance. What has been missing in cooperative development? Where are the dividing lines between *due* promotion and *undue* interference? In a diverse country like Nigeria, are these to be determined in each particular case, do they gradually evolve, or are they to be defined categorically and for all cases? We hope that this book will inspire researchers, policy makers and practitioners to find answers to such questions.

We have not yet reached the boundaries of the wide field of cooperative innovation.

Prof. Emeritus. Hans Dieter Seibel
University of Cologne,
Germany
22 April 2012

[1] Seibel, SHG Sector Own Control: an Approach towards Self-reliance and Sustainability of the SHG Sector in India, MicroFinance Review (Lucknow) IV, 1, 2012; N. Srinivasan: Microfinance India, State of the Sector Report 2011. New Delhi: Sage Publications, 2012

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Finally, all glory and honour to the highest God for the gift of life, for the completion of this book and for the salvation of my soul through His son, Jesus Christ.

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Chapter 1

INTRODUCTION

Onafowokan Onabanjo **OLUYOMBO**

THE BEGINNING

The United Nations General Assembly passed a resolution 64/136 on December 21, 2009 declaring **year 2012 as the International Year of Cooperatives**[1]. This is to showcase the contribution and impact of cooperative to the socio-economic well-being of the participants among other reasons.

It was in view of the above that a call for papers was made in 2011 by the editor after receiving an approval, reference number 20110809002 on August 9, 2011 from the International Year of Cooperatives Secretariat at the United Nations, USA. We also have the privilege of using the 2012 International Year of Cooperatives logo (see the book cover) for the call for papers, cover of the book and other documents for this book project. The papers, which should be original and should not have been published, submitted, or under consideration for publication elsewhere were to focus on challenges, impacts and prospects of cooperative finance and microfinance arrangement in developing nations.

I have the good pleasure of informing you that the outcome of the above call for papers is this book - **Cooperative Finance in Developing Economies** - which contains papers from notable members of the academia from **four continents** - Africa, Asia, Europe and North America. Specifically, **twenty nine authors** from **nine countries** namely Canada, France, Germany, Italy, Nigeria, Senegal, Spain, United Kingdom and Vietnam contributed to this work.

The scope of the book includes all forms of cooperative and microfinance arrangements such as Cooperative Society, Cooperative Bank, Informal Microfinance, Credit Union, Thrift and Credit, Multipurpose Cooperative, NGO, Farmers and Traders Cooperative.

THE BOOK

The book covers both the theoretical and empirical research in different areas of Cooperative and Microfinance arrangement which include but not limited to: Capital formation and loan administration, Corporate governance, Country comparison and analysis, Financial intermediation and social capital, Financial sustainability, Impact assessment and evaluation, Integration into formal financial system, Management and members – relationship and conflict, Micro and small scale enterprise development, Poverty

[1] I would like to thank the International Year of Cooperatives Secretariat at the United Nations, USA, for the approval to use the 2012 International Year of Cooperatives logo for the call for papers, cover of the book and other documents for the book project.

reduction and economic development, Products and services delivery models, Regulation, policy and control, Risk management and insurance, and Women empowerment and gender issues.

PLAN OF THE BOOK

This book is organised into **nineteen chapters**. The **first chapter** is the introduction written by **Oluyombo**. **Chapter two** by **Marx** and **Seibel** is titled the Evolution of Financial Cooperatives in Nigeria: Do They Have A Place in Financial Intermediation? Their paper looks at the evolution of financial cooperatives in Nigeria, compares them with other financial service providers, and looks at some causes of their success and failure. They started by juxtaposing informal beginnings of microfinance centuries ago: in Germany, where appropriate regulation and legislation eventually turned them into savings banks and cooperative banks as a major part of the banking sector, and in Nigeria, where a similar approach was discussed but discarded early on, and formal and indigenous informal financial institutions (esusu) have continued to operate side by side. The main focus of the paper is on the rise of financial cooperatives, their decline due to both government intervention and neglect, and the differential experience of financial cooperatives with and without an indigenous base. This includes the historical experience in Nigeria with three strategic approaches to indigenous savings and credit associations: transformation to cooperatives, institutional upgrading, and bank linkages. They conclude with a discussion of whether or not there is space for financial cooperatives in Nigeria, and whether substantive results could be expected in case substantive policy changes would be made.

The focus on **chapter three** by **Ighomereho, Dauda** and **Olabisi** is Making Cooperatives Effective for Poverty Alleviation and Economic Development in Nigeria. The authors argue that cooperatives are veritable tools for poverty alleviation and economic development because they enhance individual savings and access to investment credit. Cooperatives improve macro and micro level incomes, create employment, enable the procurement of commodities, increase productivity and ensure food security. However, they noted that performance of cooperatives in Nigeria has been hampered by numerous challenges such as: poor governance, limited management skill, inadequate fund, limited access to investment credit, ineffective implementation of government policies, resistance to change, inadequate education in cooperative operation and inadequate marketing activities. Several solutions have been proffered to making them vibrant and relevant in developing economies, but the peculiarity of the challenges confronting the subsector in Nigeria call for a need to align them to address the issues of poverty alleviation and economic development in the country. This paper proposed cooperative marketing, cooperative management and cooperative financing with government assistance as relevant solutions.

The Role of Informal Microfinance and Cooperatives in Poverty Alleviation and Economic Development written by **Pedzinski** and **Odoemenam** in **chapter four** contend that insight into the role of microfinance in poverty alleviation and economic development is relegated to an analysis of formal institutions, largely because of the recent exponential growth of formal Microfinance Institutions (MFIs) and the difficulties in measuring informal sector activities. Nevertheless, especially in the case of large developing economies like Nigeria where as much as 70% of economic activity occurs in the informal sector, the inability of formal institutions to reach the vast majority of the unbanked population necessitates a look into the realm of informal microfinance, not as an alternative, but as a continuation of a long history

of transactions rooted in traditional social networks. This paper uses secondary sources and analysis of three disparate case studies on informal cooperatives completed in Nigeria between 2008 and 2009 to identify the role of informal financing mechanisms in contributing to poverty alleviation and economic development in a local context. Their findings reveal that the significance of informal microfinance in Nigeria is aligned with the inherent strengths of social capital vis-à-vis strong kinship networks and mutual dependence. These characteristics contribute to the grassroots relevance of informal institutions, a key element lacking in formal MFIs, especially as they commercialize and stray from their social bottom line. They recommend that the informal microfinance should be re-evaluated for its strengths in reaching those who are still excluded from 'inclusive financial systems', i.e. those at the bottom of the pyramid.

Ikomi's paper in **chapter five** is on the Role of Insurance in Managing Microfinance Program Risks. The paper reveals that many of the microfinance institutions accept deposits directly or indirectly like commercial banks. As a result of the acceptance of deposits and granting of credits, the MFIs are exposed to the risks associated with this type of trade, because MFIs give out loans without asset based collaterals. The above fact makes it very imperative for MFIs to set up sound risk management techniques that will be very efficient in forestalling possible loan default. Considering the popularity of MFIs operations across nations, the paper examines different types of risks that exist in microfinance program and what the insurance companies can do to support the microfinance in order to mitigate the risks. This can be done by setting up an intelligent and professionally driven risk management system that will apply modern techniques in dealing with all the types of risks inherent in microfinance business endeavours. In **chapter six**, **Founanou** and **Ratsimalahelo** discuss Regulation and Supervision of Microfinance Institutions: An Example of Cooperative Credit Society. They studied the optimal regulation of a cooperative credit society which has private information on the intrinsic quality of its loan portfolio (adverse selection) and where the cooperative's choice of effort to improve this quality cannot be observed by the regulator (moral hazard). The paper characterizes the optimal contracts offered by the regulator to the credit cooperatives. Their paper reveals that the optimal contracts depend on three main factors namely: the accuracy of the supervisor's signal, the likelihood of facing a high quality credit cooperative, and the cost of supervision.

The Place of Cooperatives in Nigerian Microfinance is the focus of **chapter seven** by **Oluyombo**. The paper creates a clear understanding of some basic and essential aspects of microfinance and cooperatives across the world with special emphasis on Nigeria. Discussion and clarification of contextual aspects of microfinance and cooperatives in the chapter enables the author to provide working definitions and explanations of different terms used in these areas of study which may be different from the way it was used by other studies. The paper also provide a microfinance definition model that is useful for creating a niche in the delivery of micro and cooperative finance services to both the rural and urban dwellers. This is important, because the author used this background information to explain and discuss the different types of formal and informal microfinance service providers in Nigeria and their operations. Determinants of Microfinance Banks Sustainability in South-Western Nigeria by **Fajonyomi** and **Jegede** in **chapter eight** employed secondary annual panel data collected from 80 microfinance banks in Lagos and Ondo States over a period of six years from 2005 to 2010. Generalized Least Squares Method and Panel Ordinary Least Square Method were employed to analyze the relationship between determinants of sustainability of the sampled microfinance banks. Their study finds that microfinance sustainability is positively and

significantly determined by loan delivery method, average loan size and amount of funds available to the microfinance bank. The result observes that poor sustainability precipitated the collapse of microfinance banks in south western Nigeria. Microfinance banks are encouraged by the authors to put emphasis on the identified determinants starting with loan delivery method and average loan size followed by debt-equity capital. Microfinance banks must also focus on the real effective lending rates for improved sustainability.

An empirical study on the Performance of Microfinance Banks in Financing Agricultural Cooperative Societies in Rural Nigeria by **Onugu** is in **chapter nine**. His study used Anambra State as a case. Eighteen rural based Microfinance Banks (MFBs) and one hundred and twenty Agricultural Cooperative Societies (ACSs) linked with the banks and drawn from the three geo-political zones in Anambra state were used for the study. Data was collected through structured questionnaire and group-focused interview. Descriptive statistic tools, simple and multiple percentages and means were used for the analysis of data. The study found that the main source of financing the ACSs, are through share capital, annual reserve, thrift and savings of members and the MFBs. The key financial product targeted at ACSs includes group-savings and group-credit. The ACSs certified they had access to funds from the MFBs, though its impact in enhancing their farming activities was not very satisfactory. Notable challenges to the funding of the ACSs include: poor monitoring and supervision of loans; insufficient fund to meet the needs of the societies; inadequate credit staff; and high interest rates on loans. The researcher recommended that efforts should be made to raise the financial resources available to the MFBs. Equally; the non-banking service functions of MFBs should be emphasized to develop the ACSs, and aid their effectiveness. Finally, there is need to sustain the training of credit officers of the MFBs as well as re-orienting their focus to field operations.

Financial Services Cooperatives, Public Policy and Financial Inclusion: A Perspective From Latin-America is the focus of **chapter ten** by **Buendía-Martínez** and **Tremblay**. They argue that the 2008 international financial crisis highlighted the greater stability of financial services cooperatives (FSC) and its contribution to lower the systemic risk of financial systems in countries in which they have a significant share of the financial market. This phenomenon has resulted in a resurgence of attention in the cooperative form of financial organisation and its contributions to other economic challenges such as local development and financial inclusion. Globally, FSC are increasingly viewed by public policy makers as contributors to the needed diversity of actors in the financial sector. Their paper provides an updated vision of FSCs in the Latin-American region, with particular attention to the Brazilian and Mexican cases as remarkable examples of public policy applied to reducing financial exclusion through cooperative institutions. Financial inclusion is a major issue in public policy agendas as a consequence of its effects, namely, reducing social exclusion and enhancing economic growth. In the Latin-American region, the profile of FSCs in the banking industry is heterogeneous. The authors note that there is an important disparity among the various countries owing to the variety of forms of institutionalization of FSCs in financial systems. Brazil and Mexico are ahead of others in the implementation of financial public policy, in as much as FSCs are key institutions in facilitating banking services for more than seventy million people.

In **chapter eleven**, **Balogun, Akinlade** and **Campbell** empirically examined the Impact of Microfinance on Rural Households. A multistage sampling was employed for the study. Ekiti and Osun states were randomly selected from the six states in Southwest Nigeria. This was

followed by random selection of two Local Government Areas (LGAs) from each senatorial district of the states. Thirty Microcredit Groups (MGs) were randomly selected from each of the selected LGAs. Three hundred and ninety nine respondents were randomly selected from the MGs. Data on household demographic characteristics and microcredit variables were collected with structured questionnaire. The data were analysed using descriptive statistics. Their study identified five microcredit sources patronize by rural households namely Commercial Bank; Cooperatives; Governmental Agency; Local Money Lenders and Friends/Family. They found that the average microcredit granted by these sources was ₦15,739.35 ± ₦1,026.81 representing only 44.2% of the total credit needs of households. The time lag for credit was 4.65 ± 3.35 weeks with a payback period of 7.30 ± 4.63 months. Half of the amount requested as loan from credit sources was granted and this required that credit delivery needs to be strengthened. Impact of Microfinance on Occupational Choice and Performance of Women Entrepreneurs by **Oyetayo** in **chapter twelve e**mpirically assessed the extent to which microfinance; formal and informal has been able to reach out to clients especially female entrepreneurs. As an intervention program, female entrepreneurs' membership of either formal or informal microfinance is expected to help co-ordinate their business activities and help overcome constraints to business productivity. In the study, neither formal nor informal microfinance in terms of capital (external) provided, has made a significant impact on the business activities of the women studied. Although informal has a high probability to impact on business productivity at ($t= -1.95$, $p< 0.05$), while the capital for formal is insignificant at ($t= 0.53$, $p> 0.05$). However, in their separate categories, the author found that each of them has been able to help mitigate some of the constraints to business productivity. She recommended a synergy between formal and informal microfinance, while women entrepreneurs are encouraged to belong to both programs to enjoy their complementaries

Seibel and **Thac** examine the Growth and Resilience of Credit Cooperatives In Vietnam in **chapter thirteen**. The paper reveals that credit cooperatives first emerged in the mid-1850s in Germany as savings-led self-help organisations, without government subsidies. As they spread around the world, governments in many developing countries used them as credit channels, thus undermining their self-reliance and self-governance. The authors argued that there is a dearth of developing countries that may serve as models for a sustainable self-reliant credit cooperative movement. Vietnam, with its People's Credit Funds (PCFs) is one such country. The PCFs are a paradox: a genuine self-help movement, yet one which has gained its strength and vitality from the government which has appointed the central bank as their regulator, training agency and effective supervisor, without undue interference. The paper presents the origin and evolution of the PCF system and examine how its two segments, the rural PCFs and their central fund (CCF), the latter with rural wholesale and urban retail services, have performed during the recent global crisis. **Lawal's** paper in **chapter fourteen** is devoted to the Impact of Cooperative Finance on Capital Formation. He examines the role of cooperative societies in business financing in Nigeria, using primary and secondary data. It is argued that capital formation is a major challenge to doing business in Nigeria and many developing economies. All the various types of business organisations are faced with the problem of inadequate funding. This situation frustrates business and in most cases leads to business failure, unemployment, loss of potential output, and loss of potential tax revenue that would have accrued to the government. The Harold-Domar (neo-classical) theory stresses the importance of savings as a major source of raising fund for investment purpose so as to enhance macroeconomic growth and development. Data were collected using structured questionnaires and were analysed using descriptive statistics and multiple regression

technique. His result shows that cooperative credits and thrift association is a veritable source of raising, mobilization and channelling of capital for ordinary people. Thus, cooperative financing should be encouraged in Nigeria.

Chapter fifteen is on Impact of Cooperative Societies on Members Business by **Nzekwe**. The paper stated that the major objectives of cooperatives was to provide support, render services, and provide mutual and self help to the members through the surplus/profits realized by the society from their activities. The population of the study area was two hundred and four (204) farmers of eight (8) registered cooperatives in Idemili North Local Government Area of Anambra State, Nigeria. 192 respondents were selected using Yaro Yarmene formula. The sampling technique used was purposive and simple random sampling method. One hundred and fifty (150) respondents returned their questionnaires. The data was analyzed using mean rating, standard deviation, gross margin and net return. Two hypotheses were designed and tested using t-statistics. The findings revealed that cooperatives engaged in different business activities which enabled them met the expectations of members in the society, thus raising profit for their members. Consequently, the study recommended that enhancing marketing efficiency by supplying and marketing of farmers input and output, using integrated approach, mechanization and so on will improve members' socio-economic well being as their businesses record more profit. Government and Anti-Poverty Programmes in Nigeria: The Way Forward is the focus of **Ogundele** and **Abiola's** paper in **chapter sixteen.** Their paper looks at poverty as a situation of extreme wants of basic life's support and as a product of an environment that is not able to provide the life's supporting resources. They probe into why there is continued lack of sustainable development in Nigeria in spite of institutional structures and various government efforts. The paper also examines the effects of corruption as a result of the level of poverty in Nigeria. The study found that poverty reduction initiatives of the government in Nigeria since 2005 are yielding positive international result in form of debt relief to the tune of $18 billion, but of which its internal benefit is of little effect. The study is of value to policy makers in developing countries and Nigeria in particular, in propagating effective poverty eradication programme. The paper comes up with some recommendations which are of value for successful implementation of poverty eradication programmes with the need to strengthen the existing poverty eradication institutional framework.

Chapter seventeen by **Akinbobola** examines Personality and Leadership Style as Predictors of Intent to Escalate Commitment in Financial Institutions. The empirical study utilized an ex-post facto design. Participants were 348 Banking and Finance graduate students of a university in Nigeria, who were engaged in decision making in some corporate organisations. Standardised psychological scales used to measure transformational / transactional leadership style, self efficacy and the need for achievement as personality attributes and intent to escalate commitment were administered on the participants. Data obtained were subjected to hierarchical regression and zero order correlation. The hierarchical regression analysis showed that demographic variables jointly accounted for 4% variation in intent to escalate commitment ($p<0.01$). The inclusion of leadership style resulted in 29% change in variance with transactional leader behaviour significantly predicting ($\beta = 0.37$; $p< .01$) intent to escalate commitment. Further inclusion of personality factors resulted in 3% change in variance with self efficacy ($\beta = -0.14$; $p< .01$) independently significantly predicting intent to escalate commitment. Importance of transactional leader behaviour and self efficacy has implication for escalation of commitment. The author recommended that management should

be tactical in engaging individuals with such dispositions for transactional leader behaviour in decision making involving initial loss.

In **chapter eighteen**, **Okeke** focuses on Human Resource Management (HRM) Practices in Cooperative Organisation using the Household Utensils Dealers Multipurpose Cooperative Society (HUDMCS) to determine the effect of human resource management on workers and members of cooperative. The study population was 1810 from which a sample size of 328 was selected using systematic random sampling technique to select the sample size from the entire population. The t-statistics was used for testing the hypotheses. The study found that the HUDMCS have good HRM practice and this has reflected in their activities. However, they are confronted by some problems. The hypotheses tested revealed that there was no significant difference in the perception of members and workers based on the HRM practices, effects and problems of HUDMCS. Based on the findings, the researcher made some recommendations such as; having a well written policy on HRM practices by cooperatives, need for regular promotion and recognition as it will help to boost the morale and enthusiasm of both members and workers. **Ishola** and **Abianga's** paper on Corporate Governance Role in Family and Cooperative Business is the last chapter - **chapter nineteen**. This paper discusses corporate governance in a family, cooperative or microfinance business. The general concept is broad but connotes having policies and practice of owners and managers of the business. They examine corporate governance as a key to maintaining focus of an organisation's goals and objectives. Corporate entity, be it family or non-family should be based on required adopted policies and rules that guide the procedure and process of practice. The concept is cited as the 'value side' of management and organisation. The paper identifies culture and other informal approach as dominance on issues in family and cooperative business. The study views the need for family as well as cooperative business to operate a system or an association that has a reliable framework based on policies. Research and general observations infer that poor corporate governance has been the 'Achilles' heel' in many businesses especially family or cooperative because of their simplistic build-up. Microfinance initiatives are to be supported in other to add-value to family and cooperative financial needs. The paper advocates for proper policy guideline in the management of family and cooperative business especially in a developing nation.

CONCLUSION

This book is our modest contribution to the field of cooperative and micro finance, and for the recognition and celebration of year 2012 as the International Year of the Cooperatives. It is our sincere desire that readers – students, researchers, practitioners and policy makers will get new insight of knowledge from the pages of this book.

I therefore wish you a happy reading.

Chapter 2

THE EVOLUTION OF FINANCIAL COOPERATIVES IN NIGERIA: DO THEY HAVE A PLACE IN FINANCIAL INTERMEDIATION?

Michael T. **MARX**
Hans Dieter **SEIBEL**

INTRODUCTION

Over the past three decades, a few innovations have had a major impact on the lives of Africans, among them mobile phones, minibuses, and microfinance. In some countries, microfinance has reached about 15-20% of the adult population[1], while in others, it is much less prominent. For Nigeria, the EFINA Access Strand Survey 2010 has provided data on access to the different types of financial services. Of the total adult population, 30% operate a (deposit or loan) bank account, 6% use other formal financial institutions in microfinance including credit cooperatives, insurance, pension schemes or remittances[2], and 17% reportedly use informal institutions (most likely underestimated) such as ajo, adashi or esusu, moneylenders or informal remittances. This leaves almost half the adult population, or almost 40 million persons, excluded from financial services.

This paper looks at the evolution of financial cooperatives in Nigeria, compares them with other financial service providers, and looks at some causes for their success and failure. We start by juxtaposing informal beginnings of microfinance centuries ago: in Germany, where appropriate regulation and legislation eventually turned them into savings banks and cooperative banks as a major part of the banking sector, and in Nigeria, where a similar approach was discussed but discarded early on, and formal and indigenous informal financial institutions (*esusu*) have continued to operate side by side.

The main focus of the paper is on the rise of financial cooperatives, their decline due to both government intervention and neglect, and the differential experience of financial cooperatives with and without an indigenous base. This includes the historical experience in Nigeria with three strategic approaches to indigenous savings and credit associations (*esusu):* transformation to cooperatives, institutional upgrading, and bank linkages. We conclude with a discussion of whether or not there is space for financial cooperatives in Nigeria, and

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1 Such as Kenya, Benin, Mali, Burkina Faso and Senegal. The country with the highest share of microfinance in total loans outstanding that we are aware of is Kyrgyzstan in Central Asia with 42%. (Marx, 2011).

2 The data indicate that the vast majority of respondents in this category used remittances and vehicle and life insurance products.

whether substantive results could be expected in case substantive policy changes would be made.

ORIGINS OF MICROFINANCE

European Origins of Microfinance

Revolutions in rural and microfinance seem to be recurrent events. One such revolution started in the 1970s, when Shaw and McKinnon (1973) at Stanford University propagated, pertaining to financial systems, the crucial importance of Money and Capital in Economic Development; and a group of scholars around Dale Adams (1984) at Ohio State University, pertaining to rural financial systems, exposed the dangers of Undermining Rural Development with Cheap Credit.

An earlier revolution, truly in microfinance, urban and rural, started in Germany some 160-230 years ago from small informal beginnings as part of an emerging self-help movement: with the first thrift society established in Hamburg in 1778; the first community savings bank in 1801; and the first urban and rural cooperative credit associations in 1850 and 1864, respectively. The provision of legal status, prudential regulation and effectively delegated supervision played a crucial role in their further development, starting with the *Prussian Savings Banks Decree* in 1838 and the Cooperative Act of the German Reich in 1889, the first cooperative law in the world. Their success has been spectacular. These two types of (micro) finance institutions now comprise about half of all branches/points of sale and 38% of all banking assets in Germany (*Dec. 2010 data*) and seem healthier than many of the big national banks (Deutsche Bundesbank, 2011; Seibel, 2003a, 2008).

The story of Germany is preceded by an earlier, yet sadder, story of the Irish charities or Irish funds, respectively, which emerged in the 1720s in response to a tremendous prior increase in poverty. They started with interest-free loans from donated resources. After a century of slow growth, a boom was initiated by a special law in 1823, which turned the charities into financial intermediaries by allowing them to collect interest-bearing deposits and to charge interest on loans. Around 1840, about 300 funds had emerged as self-reliant and sustainable institutions, with interest rates on deposits and loans higher than those of banks. They were so successful that they became a threat to the commercial banks, which responded with financial repression: getting the government to put a cap on interest rates in 1843. The Loan Funds lost thus their competitive advantage, which caused their gradual decline, until they finally disappeared in the 1950s (Seibel, 2003a).

Microfinance is thus not a recent development, and it is not just a temporary solution for poor countries. It seems every now developed country has its own history of microfinance. It is important to recognize this because it presents a view different from that of many in the microfinance community who associate microfinance with credit NGOs, or believe that microfinance was invented in Bangladesh in the 1970s. Attributing the origin of microfinance to recent initiatives misses not only its historical depth and scale, but also centuries of experience, which means: learning from trial and error, failure and success. The beginnings in Europe and Africa, notably in Nigeria, were all informal and small-scale. What distinguishes a country like Germany from many developing countries is not the prevalence of self-help and informal finance at an earlier time. Community and member based as well as other informal financial institutions are exceedingly widespread throughout the world. The major difference

seems to be the legal recognition given to informal finance in Germany and the protection of the institutions through prudential regulation and effective supervision, which enabled them to eventually turn into banks.

African Origins of Microfinance

Centuries ago, a microfinance revolution must have taken place in Nigeria. The earliest evidence of financial institutions in Africa dates back to the 16th century: to *esusu*, a rotating savings and credit association (RoSCA) among the Yoruba. As a form of social capital, the *esusu,* a financial self-help group, was transported during the slave trade to the Caribbean Islands (Bascom, 1952:69), where both the institution and the term still exist today and are now carried by a new wave of migrants to major American cities. Its origin were probably rotating work associations, in which labour as a scarce commodity was accumulated and allocated to one member at a time; and then, with the spreading of commercial transactions, replaced by money, such as cowries, pounds and Naira.[1] Nigeria is one of the countries where informal financial institutions continue to play an important role. There may be only few adult Nigerians who are, or were, not a member in one or several of them. Numerous adaptations and innovations have sprung from the RoSCAs: one is the transformation into non-rotating savings associations with a permanent loan fund. Both the name, susu, and the institution, have spread as far as Liberia (and beyond), where in the 1960s they were the only effective financial institutions existing in the countryside (Seibel, 1970; Seibel and Massing, 1974). The other one is daily deposit collection at doorsteps or market stalls. This seems to have originated among the Yoruba (where it is known as *ajo*) from where it has spread all over West and Central Africa during the past half century.

These informal financial institutions are immensely popular in Nigeria. Virtually every ethno-linguistic group has its own institutions and proper names (*adashi,* in Hausa, perhaps the best-known besides *esusu/isusu/osusu*); and most adults are members in one or several. Yet their importance and potential have been controversially discussed. In 1934 C.F. Strickland, a former British cooperative registrar in India, examined the *esusu* as a possible basis for modern cooperative societies in Western Nigeria. Having previously worked on the rotating *chit funds* in India, he speculated that the esusu must have been imported from India at some unknown time; he found them “improvident” and “fraudulent”, and concluded that he was “not hopeful of the reform of the Esusu.” (Strickland, 1934:14) The consequences of his judgment were far-reaching: the Cooperative Societies Ordinance, introduced in 1935, was modeled after British-Indian cooperatives and became the blueprint for the British colonies in Africa.

However, informal financial institutions of various types continued to be rediscovered in Nigeria by scholars (e.g., Green 1947/64; Bascom 1952; Ardener 1953, 1964; Isong 1958; Seibel 1967; Seibel and Marx 1984; Ottenberg 1968, 1973; Okorie and Miller 1976; Chukwu 1976) and practitioners, who were intrigued by their development potential. At various times,

1 Financial institutions accumulate scarce resources and make them available in lump sums: either as one’s savings at the end of a period of depositing small amounts; or as a loan at the beginning of a period of (usually) small payments; or as a mixture of both, savings and credit, somewhere during that period. In the process, financial institutions manage risks, decrease the costs of transaction between individuals, and increase efficiency. Historically, labour has been a scarce resource in Africa. Rotating group work has been one of the forms of accumulating and allocating that scarce resource. With the emergence of a cash economy, money was gradually substituted for labour: a process which is still going on in some countries. (Seibel and Damachi 1982; Seibel 2006).

two approaches were tested: (i) upgrading informal rotating or non-rotating savings and credit associations to registered cooperatives; and (ii) linking them to banks.

EVOLUTION OF INFORMAL AND FORMAL COOPERATIVE FINANCE IN NIGERIA

Evolution of Financial Cooperatives in Nigeria [1]

On the basis of the 1934 Strickland report cited above, the colonial administration started to introduce cooperatives in Nigeria in 1935. The most prominent type of cooperatives were the Cooperative Thrift and Credit Societies, which began to grow in numbers and membership during the 1940s and 1950s. Growth occurred much more in the Southern parts of Nigeria, where this form of social organisation fitted more neatly into the prevailing indigenous value systems, behavioral norms and patterns of decision making, and provided an alternative approach to managing household finances.

All financial societies were based on the classical, simple financial intermediation model: membership rights were granted upon admission as member and purchase of the minimum prescribed share, which obliged the member to make regular savings at meetings. The cooperative would then grant loans to members on a demand basis, with mostly shares and savings as prime collateral, and often by observing a maximum credit limit (MCL) of three times one's savings. Very few societies had their own buildings or offices, and meetings of members were mostly conducted at the residence of the chairperson.

In the late 1940, secondary cooperative societies started to emerge, which were established and controlled by their member societies. Their business model also followed the classical intermediation model of the cooperative sector: member cooperatives had to contribute the share capital of the secondary society and deposit a certain share of their own savings with it. In return, the more creditworthy primary societies could avail of loans from the secondary union, often by applying a similar MCL as in the primary societies. According to our studies carried out in the mid 1980s on the cooperative sector (Seibel and Marx, 1984), the model seems to have worked pretty well up to the 1970s in many areas as the demand for loans was either not very high or artificially suppressed by stiff regulations, as banks were not always around to deposit excess liquidity, and as the entire system was well monitored by cooperative inspectors, most of which were well educated. In fact, the cooperative legislation provided for compulsory audit by the cooperative auditor prior to the distribution of any dividends to members. This provision was apparently strictly enforced until the early 1960s, and the number of cooperative auditors was sufficient to audit many or most societies. Our data on some secondary financial cooperatives in the Western Region, the Delta and the South-East indicate that both primary and secondary societies were functioning relatively well, were able to recover their loans and cover their expenses from self-generated revenues.

Like in many other developing countries, politics in Nigeria discovered the potential of the cooperative sector as instrument of rural and economic development, and later as compensatory mechanism to share the national wealth deriving from oil exports. The approach taken by consecutive governments was not to stimulate self-help, thrift, prudent lending, organic growth, prudent expansion, self-control, careful selection of members, but to

1 The term financial cooperatives is used here interchangeably with savings/thrift and credit cooperative societies and credit unions.

provide external subsidies to make the cooperatives more attractive. The distribution of stockfish, tinned milk and cheap loans through cooperatives in the 1970s up to the mid-1980s permitted rapid quantitative and geographic expansion over and beyond the areas where cooperatives had previously existed. This went in line with a tighter hands-on policy of the administration in the internal affairs of the cooperative sector, lesser procedures for granting of loans, lower recovery rates, a partial or total consumption of the nominal share capital, lower attendance rates at general meetings, lower savings propensity, and the predominance of external loans in total liabilities, among others.

The growth in number of societies was not paralleled by growth of capacity in the state cooperative departments. While more efficient monitoring systems and means of transport allowed inspectors to attend meetings of societies, the number of cooperative auditors remained more or less stagnant. As a consequence, cooperative auditors were unable to audit primary societies as frequently as before. This impacted negatively on the quality of records kept by cooperatives and prevented societies from declaring dividends. As cooperatives were prevented by legislation to get their accounts audited by private auditors, they were effectively barred from borrowing from commercial banks.

The secondary unions established during the 1970s, Cooperative Financing Agencies (CFAs), were only nominally established by the primary societies. In many regions, they replaced the former secondary cooperative unions, which had become obsolete in the view of primary societies. The main source of capital of the CFAs came from government sources, including state budgets and the Nigerian Agricultural and Cooperative Bank (NACB). As members of the primary societies regarded the government loans as their 'share of the national cake', they had little intention to repay their loans to their primary society, which in turn affected the ability of primary societies to pay back their loans to their state CFA. The entire three-tier conduit system, from NACB to state CFAs and primary societies, fell gradually apart because none of these institutions was able to recover loans due; they consumed their share capital and ultimately became insolvent. By the late 1990s, all except two CFAs had disappeared, as had the old NACB. In the mid 2000s, the two last existing CFAs, in Bauchi and Gombe States, had changed their business model. Their prime activity was to run school feeding programmes funded by their respective states, and they had stopped all financial intermediation. They had lost all capital sources for lending, had realized that they did not have the expertise to survive in a rapidly changing market, were not assessed as creditworthy by banks, and were no longer privileged by their former financiers.

LINKAGES BETWEEN INDIGENOUS SAVINGS, CREDIT ASSOCIATIONS AND FINANCIAL COOPERATIVES

Transformation of the Indigenous Savings and Credit Associations to Cooperatives

In Eastern Nigeria, in the 1940s colonial officers with an anthropological background recommended the transformation of *osusu* or *isusu* (the Igbo term) to financial cooperatives as well as the continuation of *isusu* practices within modern cooperatives (i.e., those registered under cooperative law). In 1954, the Eastern Region Cooperative Department (1954) stated in its annual report:

> "The Isusu (Esusu, Susu, Osusu) is a widespread indigenous system of thrift and credit… On the whole, the Esusu seems to be fairly well managed; although in some areas… the

> Isusu has degenerated into a notorious money-lender-controlled ‘racket’. There are vast numbers of Isusu Clubs in the region and the total amount of money involved must be very large. Some local Government Bodies have recently instituted a system of registration of Isusu Clubs.”

During the 1950s, when self-government was introduced, definitions of what constitutes “development” changed; and so did attitudes to local culture and institutions. This is indicated by the “modernization” of one esusu in Ondo Province initiated in 1952 by a Nigerian civil servant, J. T. Caxton-Idowu. He prepared by-laws, “regularized” its activity, imparted cooperative education, and registered the esusu as a proper cooperative society. At that time, there existed four Cooperative Thrift and Credit Societies of the type imported by the British, to which the esusu was added as a fifth cooperative, but of indigenous origin. Within a ten-year period, the number of such cooperatives grew from 5 in 1952 to 94 in 1962, including converted esusu. Their proportion of *modernized* esusu in terms of total number of financial cooperatives in the area had risen from 20% in 1952 to 44% in 1962; their working capital and savings from 20% to 52%, and their membership from 23% to 58%. Adeyeye (1970), a learned observer, concluded:

> “… the Ondo experiment has demonstrated… that the ‘Esusu’ may yet represent a source of immeasurable strength… With the renewed pride in our traditional heritage, we in the developing nations will definitely find the idea of institutional adaptation a most welcome experiment. It will offer opportunities to modernise without necessarily destroying the essentially indigenous character.”

In the early 1980s, donor countries realized that capital transfer through development banks had failed to bring about the desired modernization and shifted their interest to domestic resource mobilization. As a contribution to the Third International Symposium on the Mobilization of Personal Savings in Developing Countries, 1984 in Yaoundé, the Federal Ministry of Economic Cooperation (BMZ) of Germany commissioned a comparative study of modern cooperatives and indigenous savings and credit associations in Nigeria. At the time, cooperatives of all kinds in Nigeria had 1.6 million members. There were no figures on the membership in esusu-type groups; but membership was conservatively estimated at 12-25 million. At a time when Nigeria had a differentiated banking sector and a booming oil industry, the question came up again whether traditional and modern cooperatives had a major role to play in financial sector development; and what had happened to the earlier approach of converting indigenous to modern cooperatives. Was it a thing of the past, or did it still have promise? In Eastern Nigeria, it was estimated at the same time that approximately 40% of all cooperatives had been established on the basis of pre-existing isusu, the majority of which had previously evolved from rotating to non-rotating associations with permanent loan funds.

In 1984, Seibel and Marx studied a total of 64 cooperatives in five states in Nigeria: Anambra, Imo, Cross River, Oyo and Benue, comparing cooperatives with and without esusu origin. The case studies are not statistically representative; and the results can only be indicative. There are two striking results: one concerning the difference between cooperatives with and without an indigenous esusu origin; the other concerning the difference between cooperatives and unconverted esusu. The following typical example is from the former Anambra State (now Enugu State), where all cooperatives operating in one selected rural district, Isi Uzo LGA, were studied. All 15 cooperatives were found comparable with regard to size, age, occupation (mostly farmers) and sex. The esusu-based cooperatives outperformed the other

cooperatives by a wide margin: higher monthly contributions (2.5 times), higher entrance fees (83 times), and higher income from business ventures (6.3 times) enabled these cooperatives to give out a larger volume of loans (4.8 times) at greater frequency (8.4 times). Similar results were found in the other states. (Seibel and Marx, 1984, 1986, 1987)

The conclusion was thus that cooperative societies, based on indigenous savings and credit associations were more effective in mobilizing personal savings and in terms of all other economic indicators than cooperatives without such a basis. However, it would be premature – and in fact a *non sequitur* – to therefore recommend to convert esusu into cooperatives. Several observations stand in the way of such a conclusion: (i) In most esusu associations the regular contributions per member were reduced to almost half when registering as a cooperative society; (ii) most members of a cooperative society continue to join informal esusu; and (iii) confidence in state controlled cooperatives is limited; personal benefits are restricted as individual members have no control over the use of what some of our respondents called "useless funds".

Upgrading Indigenous Savings and Credit Associations

Our studies in the Nsukka area in 1984 evoked considerable interest, first in our motivation for doing so, next in developing an approach that avoided the weaknesses of both, isolated isusu and government-controlled cooperatives. A number of isusu in the Isi-Uzo LGA decided to form an association, later renamed NALT United Self-Help Organisations (NUSHO), and to experiment with linkage banking. But banks failed to respond; they could simply not imagine lending to an informal association[1] without status of a body corporate, and could not understand the value that comes along with financial discipline of the *isusu*. The *isusu* groups then decided to build central functions of financial intermediation and liquidity exchange at the association level. For some years starting in 1986, the association received financial support from EZE, a German Protestant church organisation, as well as technical assistance since 2000 from UNDP. By the end of 2000, NUSHO served about 900 groups with 15,000 members in seven zones. Loans outstanding amounted to ₦23.77 million (≈ USD 0.2 million at the then prevailing exchange rate); savings accounted for 18% of loans outstanding. There is no write-off policy; and arrears stand at 21%. Interest income was 28%, and net result 3% of loans outstanding (Marx, 2001:44). While NUSHO was probably one of the first three microfinance associations[2] in Nigeria, it has not been able to keep pace with the evolution of the microfinance sector elsewhere, as it was not able to adjust its business model over time and did not invest sufficiently into sound management information systems and capacity building. By 2010, NUSHO had lost the drive of a leading MFI in Nigeria.

The approach of upgrading self-help groups together with capacity-building and liquidity exchange through their own associations has however spread to several other parts of Nigeria, including Farmers Development Union (FADU) in Ibadan, which by the mid 1980s comprised 350 self-help groups. By 2000 its membership had surged to 50,000 societies with a total of 458,000 individual members, 87% of them women; only 12% of the members were active borrowers. By December 2000, loans outstanding amounted to ₦153.65m (≈ USD 1.56 million), with an arrears ratio of 1.3%.

1 Despite the advantages that come along with a joint liability, compared with the limited liability of registered credit unions.
2 In addition to DEC Bauchi and FADU

Linking Microfinance Institutions to Banks

Apart from upgrading informal institutions to cooperatives, linking informal and formal financial institutions, or self-help groups and banks, is another strategy with its own history in Nigeria. The experience of "modernizing" an *esusu* in Ondo by Caxton-Idowu opened the way for broader replication in Lagos, where Caxton-Idowu had been promoted to the rank of Registrar of Cooperative Societies. In cooperation with First Bank of Nigeria, the Cooperative Department, between 1968 and 1970, mobilized ten *esusu* clubs of market women, who have a daily income. He combined the rotating collection and allocation of funds of the *esusu* with the doorstep savings collection of the *ajo*. Itinerant collectors paid by the bank collected daily savings and deposited them in the bank as collateral for loans to *esusu* members. The Cooperative Department registered the *esusu* as cooperatives and provided training and auditing services; the bank created a special department for the administration of the deposit collection and loan disbursement. Traditionally, members would either have to wait for their turn to receive the total amount of contributions at a given time, or they could apply to the *esusu* to receive the total out of turn. Under the new terms, anyone could apply to the bank for a loan at any time. By 1973, it was obvious that the *esusu* had lost their traditional autonomy and self-reliance; the combined bank and government intervention had disrupted internal controls, with disastrous consequences for their finances:

> "…the accounting procedure laid down by the Cooperative Department was generally flouted with impunity… the accounts of a good number of the Societies were in the red…. By 1980,… the Societies had, without an exception, been wound up." (Adeyeye 1981:8-9)

Why did linkages between bank and esusu, or formal and informal finance, fail? Adeyeye (1981) attributed the failure to outside interference into a well-functioning system: establishing associations of women of different origins who did not know each other; and de-linking loans from savings by lending to participants before they had made their first contribution. Another effort was made by the Central Bank of Nigeria (CBN). Since the mid-1980s, under conditions of economic and political instability interrupted by a spell of financial deregulation in 1994, the CBN has channelled an increasing part of its agricultural loan guarantees to commercial banks through local self-help groups. These were frequently formed for the sole purpose of accessing loans from commercial banks at controlled interest rates. As they were guaranteed under the Agricultural Credit Guarantee Scheme Fund (ACGSF), many farmers considered the loans as free money. As the loans were unsecured and unsupervised, most, at a rate of 60%, turned out to be unrecoverable. Banks were not impressed by linkage banking. Meanwhile, a linkage approach had been worked out under the German technical cooperation agency GTZ (now GIZ) auspices, initially in west and central Africa around 1983-85 as a model, then, when there were no takers, since 1986 in southeast and south Asia, where the first projects had been initiated through the Asia-Pacific Rural and Agricultural Credit Association (APRACA).

Around 1990, the African Rural and Agricultural Credit Association (AFRACA), with support from GTZ, followed suit with intermittent technical assistance. The Central Bank of Nigeria was one of four institutions in Africa to join a pilot project carried out with its own technical staff in the Agricultural Finance Department. It issued a *Model for Linking Savings and Credit Associations/Informal Groups and Banks*; and by 1993, eight commercial banks had been won to participate, with 54 branches in 22 states. 313 groups were linked to banks, comprising 137 cooperatives and 176 informal groups. As agricultural lending was

compulsory for commercial banks, they had no interest of their own, but found the AFRACA approach more effective and efficient than other approaches. UBA, one of the major banks, was impressed by the initial results and declared it would convert all its lending through 8,000 farmer groups to the AFRACA model. However, the program seemed to be stagnating in 1993; and the deregulation of the financial sector on 1 January 1994, with interest rate ceilings far below the inflation rate, killed any spark of enthusiasm among the banks. In stark contrast to its vast outreach in India sanctioned by the Reserve Bank of India (RBI) and promoted by the National Bank for Agriculture and Rural Development (NABARD) (Srinivasan 2012; Tankha 2011), linkage banking in Nigeria remained a special project of minute dimensions, not integrated into the banks' regular operations. A 1994 evaluation concluded that linkage banking through community banks, which were partially owned by local self-help groups, might be infinitely more effective than through commercial banks. As far as we are aware, only few community banks adopted the linkage approach.

CONCLUSION AND IMPLICATIONS FOR POLICY REFORM

Conclusions

Apart from a relatively small number of primary financial cooperatives mostly found in the Western, South-Eastern and North-Eastern zones, which have developed their own business models and maintained financial discipline, there is not much left of the former system. Even the former cooperative banks have disappeared as such, either merged with other banks to meet new minimum capital requirements, or disappeared from the market. Even in the absence of data, one would conclude that their ability to provide meaningful services to their members and have an impact on their income, assets and business prospects is less than marginal.

Cooperatives in general do not have a good reputation in Nigeria today. Few people would entrust their savings to them where other deposit facilities existed within reach. Credit cooperatives would hardly be considered as creditworthy by commercial banks if strict banking criteria were applied. It is therefore no surprise that not one single community bank, as promoted during the 1980s and 1990s, was established as a cooperative community bank, as happened in other countries with similar legislation (e.g. Sri Lanka, the Philippines, Indonesia).

Not much is left of the capacity of state administrations to serve, guide, advise, monitor, supervise and audit financial cooperatives. At the same time, the ability of the few cooperative schools and colleges to provide relevant and up-to-date training along solid curricula and through qualified teaching staff has very much declined. Nigeria does not have a single training institute providing standard microfinance technology. The national apex body of financial cooperatives, NACCUN, has long disappeared, and for the time being there does not seem to be much access for credit cooperatives to financial or other support services.

The microfinance evolution which has happened outside Nigeria has mostly left Nigeria untouched. Only few MFIs have emerged, and of these, only a few are operating profitably along business models that would carry them through at least in the medium run. The successful credit union models of Eastern Africa, as practiced in the SACCOs (Savings and Credit Cooperatives) in Kenya and Tanzania, and in the Coopératives d'épargne et de crédit (COOPEC) of francophone west and central African monetary zones, have not been

understood and absorbed yet in Nigeria. First, they are based on sound regulation, regular reporting, tight supervision, and strict application of sanctions, all under the direct mandate and auspices of the respective central banks and their branches. Second, transactions are carried out in designated offices or own buildings, and not in the presence of all during monthly meetings at the home of the chairperson. This simple measure has created visibility and customer privacy and permitted better marketing of their services, provided for professionalism through hired professional staff, and allowed members to make and withdraw deposits more conveniently, all of which impacted positively on their ability to mobilise deposits and increase loan amounts.

Third, many governments have supported these SACCOs and COOPECs because of their merits and achievements, without undue interference, and left much of the promoting work in the field to the secondary cooperative unions and national MFI apexes. They have facilitated the provision of technical assistance and training by semi-commercial service providers and actively encouraged donors to support microfinance through projects. In fact, in the UEMOA zone, new credit cooperatives would only get an operating license when affiliated to a network organisation providing the relevant support and monitoring. Fourth, legislation, policy and administrative support, and donor interventions created the scope for economies of scale. Given the high operating costs of microfinance, compared with that of commercial bank, credit unions (serving only members and not the general public) can only reduce their transaction costs if they serve large numbers of clients, certainly more than the typical 100 members traditionally served by Thrift and Credit Cooperative Societies in Nigeria.

The differences to Ghana, which has followed similar business models for its credit unions as Nigeria, and to Western Cameroon, where the strict supervision model applies, could not be more revealing. In the absence of any substantial government and donor support, the credit unions in Ghana under the Credit Union Association (CUA) survived where they concentrated on salaried members, the mobilisation of deposits as prime source of funds, the application of simple tried and tested business principles and the provision of loans at competitive rates. They managed this because they used primarily members to run, supervise and internally audit the operations. Furthermore, they remained largely outside the formal financial system and did not borrow extensively from governments, development banks or donor institutions. In Cameroon, the Cameroon Cooperative Credit Union League (CamCCUL) has become the biggest and most widespread provider of microfinance in the country. Before the adoption of the PARMEC law in the early 1990s, the network, then operating only in the anglophone parts of the country, followed the strict, traditional above-mentioned patterns of financial cooperatives that had prevailed up to the 1960s in Nigeria. To avoid any contamination from the government-led COOPECs prevailing in the francophone zones, it used the term ‘credit union’ instead of ‘cooperative’. Third, it did not accept credit lines offered by the government or donors, but remained self-reliant on member deposits[1]. When the PARMEC law introduced new requirements, the network adjusted accordingly, but opted to change its business model and shifted its focus from rural lending to urban microfinance, a decision that the network is currently correcting. Both, CUA in Ghana and CamCCUL in Cameroon, have identified their respective market niches, responded to changes, adapted their operational and business models, ensured client satisfaction, complied with reporting requirements and prudential regulations, kept a selective distance to government offers, and thus survived and remained

1 The league maintained its resistance to external credit lines until the mid 1990s, but realized that it lost money in most of its operations. Its biggest mistake was to deposit vast surplus liquidities in government-owned banks, which went bankrupt in the mid-1990s.

profitable. The main question hereafter is therefore whether the provision of financial services through a cooperative sector would be possible and advisable in Nigeria. This in turn requires answers to the questions whether: (i) financial cooperatives do have advantages over other forms of social organisation around finance; (ii) there is still a market niche in today's Nigeria for financial cooperatives; and (iii) this option would constitute the most promising avenue for the federal and state governments and social investors.

Do Credit Unions Have A Comparative Advantage Over Indigenous Savings and Credit Associations?

Generally, most indigenous forms of savings and credit allow for the fast mobilization and use of funds, but not for their accumulation. Both the rotating savings and credit association (ROSCA) and the accumulating savings and credit association (ASCA) permit a saver to preserve a stipulated amount of cash from the pressures of one's family and neighbours, and use the flow in such a manner that the desired objectives could be reached, such as paying school fees, replenishing one's store, purchase of household goods, or building/construction material. Both models have in common that at the end of the cycle, contributors are almost as poor or rich as they were before, while starting the next cycle. ROSCAS without internal credit funds do not permit access to emergency loans. These deficits are at the same time their strengths: operations are simple, do not require elaborate mechanisms of record keeping and supervision, are understood even by adolescents and illiterate people, and entail almost no operating costs. While indigenous systems do not respect confidentiality, their transactions are socially accepted by everyone, and a contribution to one's *esusu* is an accepted excuse for not assisting a spouse, child, relative or neighbour. Against this, cooperatives permit to take out any excess liquidity not immediately needed out of one's pocket and preserve it outside the realms of one's social environment. The many small deposits are intermediated into larger loans. However, organisation, management, record keeping, reporting and auditing are often heavy burdens for communities with low educational levels. Costs of operations are quite substantial, and often exceed 20% of the amount of loans outstanding. Against this, the interest charged by many informal groups are a multiple of what cooperatives charge, 5-10% per month are not an exception. However, few cooperatives pay dividends, and these are mostly marginal, following a business model that favours the borrower, not the depositor.

In our research findings in 1984, after having first established the superiority of *esusu*-based cooperatives over other financial cooperatives and then having cast some doubts on the advantages of a conversion of *esusu* into cooperatives, we studied unconverted *esusu*-type savings and credit associations, which is the vast majority of such institutions in Nigeria. In our small sample in four states, the savings of adults being members of both the indigenous ROSCA or ASCA and a credit union, were much higher in the informal sector. We also observed that almost all informal groups kept records, although less complex than those of cooperatives, but in any case providing adequate documentation and evidence of all financial transactions. We further found that a majority of the *isusu* had bylaws, maintained a functional separation of major offices (chair, vice-chair, treasurer, secretary). There is also evidence that some ROSCAs and ASCAs reconstitute cycle after cycle, at times over a period of 20 years and more. This dispels the myth of a generally short-lived existence of the esusu; the fact that funds are distributed over a given cycle in a rotating manner or, in associations with permanent loan funds, at the end of the year does not mean that the association is disbanded, though this may be the time for some turnover in membership. Our second tentative conclusion was that indigenous informal savings and credit associations are more

effective in mobilizing personal savings for lump sum allocations to individual members than cooperative societies, and far superior to cooperatives without an *esusu* base.[1] [2] We also observed many of these patterns in many other countries, in Asia and Africa.

Whilst there are no clear-cut overall advantages for either the cooperative or the indigenous system, both have their respective pros and cons. In Nigeria and in other countries in Africa and Asia, people do use both systems in parallel to widen their financial management options. However, there is no doubt that throughout its history heavy state interference has undermined its self-reliance and growth and has curtailed opportunities for indigenous savings and credit associations, which are genuine informal cooperatives in spirit. This has practically forced Nigerians to rely either on their indigenous informal institutions[3] – or on bank accounts kept with commercial banks.

Do Financial Cooperatives Still Have A Market Niche in Today's Nigeria?

The FinScope surveys[4] and central bank data have clearly shown the expansion of the banking sector in Africa, both in terms of volumes and outreach, and a corresponding regression of the semi-formal sector, including credit unions and non-bank financial institutions. It is however not entirely clear whether the informal sector, ROSCAs, ASCAs and others, has been shrinking, given the particular methodology and presentation of the surveys. Despite the strength and expansion of the commercial/universal banks, the reinvigorated microfinance banks emerging from the former community banks, and the expansion of some MFIs and microfinance banks, the chances of a cooperative sector to attract a sizeable proportion of deposits in urban and semi-urban areas are very slim. However, financial sector penetration rates in rural areas are still low, with 46% of adults not using any financial service, and this would certainly constitute an opportunity for cooperative finance. Ideally, their competitive advantage could be proximity and accessibility, more so than affordability of services.

Does Cooperative Finance Constitute The Most Promising Avenue For Donors?

State governments have continued, in many different ways, to support financial cooperatives, whereas support from federal government agencies has dwindled. The peak of donor support, which has never played an important role in Nigeria, to the cooperative sector has passed more than a decade ago, and it is doubtful that it would resume and reach former levels. The approach used in Eastern and Southern Africa to promote access to financial services through informal *ASCA*s[5] (at times referred to as Village Savings and Loan Associations, or VSLAs) is unlikely to become an option in Nigeria, as these systems are likely to have originated from here, are practiced and known by each and everybody, and would hardly be considered as an improvement on access to finance. The most important alternatives to promoting access to financial services through the cooperative sector would be the commercial banks and the

1 We should add that cooperatives do have a comparative advantage vis-à-vis indigenous informal institutions: cooperatives are best at mobilizing state funds for cooperative investments.
2 Similarly, Nwabughuogu (1984:55) stated that no other institution, "not even the cooperative thrift and credit societies", offered the opportunity of accumulating relatively large sums and at the same time made allowance for emergencies.
3 In the mid-1980s, many Tiv farmers in Benue State were forced into cooperatives, which misused their members' funds. Our survey revealed that farmers put on average over 30 times more savings into their bam, the Tiv variety of ASCA, than into their cooperatives (Seibel and Marx 1987: 74-76).
4 For Nigeria, see EFInA 2010, with reference to the more recent results elsewhere in Africa.
5 E.g. in Kenya, Tanzania, Lesotho and Mozambique as well as in other countries.

microfinance banks. Learning from India, the Philippines and Indonesia, a well-conceived linkage programme closely associated to the original concept would most likely remain the most feasible policy and support option, in terms of total costs, effectiveness of outreach, and efficiency. Some commercial banks, such as Union Bank of Nigeria and First Bank of Nigeria, have over periods longer than a decade operated group lending approaches profitably[1], and there are no principal reasons why banks could nowadays not repeat this successfully. The options to revitalize financial cooperatives in Nigeria are slim. In the system of household finance, the indigenous institutions play a unique role in the sense that their functions can hardly be substituted by other financial arrangements. To the contrary, cooperative finance has to compete with other service providers: some state governments offer cheaper loans, commercial banks offer better access to deposit services through branches and ATMs, and many microfinance institutions have their comparative advantage in customer-orientation and friendly relations.

However, we see a role for cooperatives in services, marketing and trade for small and medium enterprises; in case a cooperative status would grant tax exemption privileges to the members up to a certain threshold (say a turnover of NGN 20-30 million). This would in turn require that all efforts to promote cooperatives through government agencies would be stopped, the function of the registrar of cooperatives be transferred to the registrar of companies, the cooperative units dissolved, the tax regulations be amended, and cooperatives be forced to get their accounts audited by private auditors once a certain scale of operations would be exceeded. SMEs in the agricultural, trade and services sectors might then be more attracted by the unique features of the cooperative business model and do real business under this legal status.

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Chapter 3

MAKING COOPERATIVES EFFECTIVE FOR POVERTY ALLEVIATION AND ECONOMIC DEVELOPMENT IN NIGERIA

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Jayeola **OLABISI**

INTRODUCTION

One of the challenges of developing countries is finding successful solution to poverty and economic underdevelopment (Gunga, 2008:1). Most developing countries, particularly those that fall within the continent of Africa are overburdened by high level of poverty and low macroeconomic performance. These over the years have continued to inform various policy measures aimed at bringing about growth and development of these economies for better and improved well-being of the citizenry (Yusuf and Ijaiya, 2009:74; Oshewolo, 2010:272). However, facts of various economic indicators in these countries have shown that the policy measures seem not to be yielding the desired result going by low level of economic growth, worsening security condition, high level of poverty, increased mortality and morbidity occasioned by high level of communicable diseases, bad governance, and political instability (IMF, 2011; Tradingeconomics.com; WDI, 2011). Cooperatives, which by design and operation are expected to help improve the economic well-being of its members, and therefore a country as a whole is one of the vehicles that could be used to foster growth and development of economies of nations.

Conceptually, a cooperative is “an autonomous association of persons, united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise” (ICA, 1995 and ILO, 2002). This paper defines cooperative as a form of organisation in which a group of individuals who have common interest mutually agree to come together to promote their interest in the area of economic activities such as production, distribution or marketing of goods and services as well as provision of other welfare benefits to their members. With these activities, cooperatives are able to alleviate poverty, particularly in developing countries where a high level of poverty prevails. In Nigeria, it is reported that about 70% of the population estimated at 156.05 million by Global Finance (2011) is still living in abject poverty (Oshewolo, 2011:2). Global Finance (2011) reported that 83.91 percent of the Nigerian population is living on less than US$2 a day and that the inequality of wealth distribution is 42.9 percent. This is a pointer to the fact that, cooperatives are yet to impact more positively on the economy of the country. Azeez (2011) has argued that the challenges inherent in the

cooperative movement have made it impossible for them to impact positively on the economic well-being of Nigeria and so, efforts to make them more vibrant and strategic for development process must be put in place.

Making cooperatives relevant for economic development has been a global concern (ICA, 1995; ILO, 2002; UN, 2009) and maximizing the potentials of the subsector for poverty reduction has been focal point of theorization and discussion among academics and development practitioners. To this end, researchers have suggested several strategies to making cooperatives more functional and relevant for development in our contemporary days. Mwelukilwa (2001:13) suggests a government transparent strategy for rebuilding the cooperative movement and a change of mindset and governance practices by cooperators to enable them function adequately as tools for poverty reduction. Torgerson (2001:1) suggested New Generation Cooperatives (NGCs), which he maintains are a relatively new cooperative structure. NGCs have peculiar characteristics that differentiate them from traditional cooperatives. These characteristics include: value-added processing of members' commodities, a significant equity contribution by members, obligation of product delivery based on equity contribution, and the ability to trade equity shares and delivery rights. These features notwithstanding, NGCs are still similar to traditional cooperatives in terms of earnings, which are based on member patronage, and one-member, one-vote. Birchall (2003:65) opines that human resource development, which provides effective management and good leadership in cooperatives are vibrant in reducing poverty. This study examines the cooperative movement in Nigeria and provides strategies to making the organisations more effective for poverty alleviation and economic development.

DEVELOPMENT OF COOPERATIVES IN NIGERIA: SOME HISTORICAL FACTS

Cooperatives came to Nigeria through agriculture (Agbo, 2009:169) and this began when few individual cocoa farmers formed the Ibadan Agricultural Society and Agege Planters Union in 1904 and 1907 respectively (Agbetunde, 2007:44). The objectives of these groups were to extend credit to members, impact knowledge of improving the quality of their cocoa and to provide infrastructure and where possible organize direct sales of their products to the world market. Other associations sprang up later in different areas of South Western Nigeria. The widespread nature of the associations, the pressure they exerted on the government for improved cocoa prices coupled with the unstable world cocoa market and the exploitation of the various foreign cocoa firms attracted government attention and these gave cooperatives some form of official recognition. FDC (2007) reported that the government established fermentaries, which became the nuclei of modern cooperative organisation in Nigeria and this made it obvious that cooperative associations in the country were now been accorded better recognition. By 1928, the fermentaries were upgraded to marketing societies by the Department of Agriculture. This development encouraged the farmers such that, at the end of the first year, there were 4,850 members and the quantity of cocoa handled was 1,600 tones. To give them a legal backing, a Cooperative Society Ordinance was passed in 1935, accompanied by bye-laws on the recommendation of the Strickland commission. The bye-laws stipulated the following objectives: Arranging for the sale of members' cocoa to the best advantage; Encouraging members to produce the highest quality cocoa; Advancing loans to members; Encouraging thriftiness among members by accepting their deposits; and Promoting the cooperative spirit among members.

Furthermore, a Cooperative Division was established in the Department of Agriculture to handle cooperative issues. Agricultural cooperatives were mostly promoted and registered to extend production credit, supply farm inputs and export quality produce to European industries. The first registered cooperative society was Gbedun Cooperatives, Produce and Marketing Society Limited, named after a village near Ibadan in 1937 (Agbetunde, 2007:45). Thereafter, thrift and credit societies and consumer cooperatives were registered. It can be deduced therefore, that the acceptance by the Colonial Administration of Strickland's Report on the prospects of cooperatives in Nigeria in 1935 marked the beginning of modern cooperative movement in the country and the transformation of traditional cooperatives to modern cooperatives. Modern cooperatives are formal, well structured, organized and well coordinated unlike the traditional cooperatives that were primitive and informally operated. In the post civil war period (1970-79), a Cooperative Development Act was promulgated and the Federal Ministry of Cooperative Development and Supply was established to promote consumer cooperatives as part of the reconciliation and reconstruction process. The policy thrust in the '80s, which focused on Structural Adjustment Programme (SAP), hindered the growth of the cooperative movement. In 1991, the Federal Government of Nigeria in collaboration with the World Bank evolved a new policy directive by carrying out sector review. In 2002, a comprehensive Cooperative Development Policy was formulated with the assistance of International Labour Organisation (ILO). A draft policy implementation strategy, which clearly defined roles for cooperatives in Agriculture and Rural Development and other primary sectors, was prepared. The review recommended that cooperative policies should be comprehensive, friendly and participatory to facilitate bottom-up development. It further envisioned a cooperative sector that is strong, autonomous, operationally independent and economically viable, competing effectively in the private sector of the economy (FDC, 2007).

COOPERATIVES AND POVERTY ALLEVIATION

Poverty entails a complex interconnection of descriptors surrounding the livelihood status of people in a society. It is a global phenomenon and a relative concept. The poor are those with lower standards of living than a country specific poverty line and people who lack access to the wherewithal to improve their conditions of living. Bamiduro (2011:4) defines poverty as "deprivation, lack, insufficiency, inability, inequality and disparity, non-availability, deficiency and shortage in essentials of well-being."

According to Wanyama, Develtere and Pollet (2008:17), poverty deprives individuals the basic necessities for existence such as: food, water, shelter, clothing and other fundamentals to life namely: health, education, security, opportunity and freedom, which could exclude the individual in the society as a result of inadequate capability to function and exercise freedom of choice. Citing some of the highlights of the 1995 World Summit for Social Development held in Copenhagen, Mwelukilwa (2001:3) noted that poverty could manifest in various ways, such as: lack of income and productive resources required for sustainable livelihoods; hunger and malnutrition; inadequate access to education, high rates of morbidity and mortality, homelessness, inadequate housing; unsafe environments; and social discrimination and exclusion as well as lack of participation in decision making. Another major manifestation of poverty in Nigeria is inefficient functional power supply. The epileptic power supply has aided mass poverty as many able and willing Nigerians have been put out of job since many companies could no longer sustain their operations because the cost of procuring, operating and maintaining generating sets has been on the increase and it is becoming unbearable for

most business organisations operating in the country with some of them already relocating to the neighbouring countries, such as Ghana and Benin Republic.

The fight against poverty in Nigeria has been expressed in many intervention programmes with promotion of cooperatives as one of such progammes suitable to combat poverty mostly within the Millennium Development Goals (MDGs). Oshewolo (2010:272) examined poverty alleviation programmes in Nigeria and concluded that most of the programmes by successive governments aimed at tackling the menace of poverty among the population have failed to halt the problem. This failure according to Bamiduro (2011:5) could be attributed to poor targeting, lack of adequate funding, inadequate coverage and management capacity, and lack of political will by national and sub-national governments, discontinuities and poor monitoring. These inhibiting challenges notwithstanding, consensus exists among many actors, including the United Nations (UN), International Labour Organisation (ILO), International Cooperative Alliance (ICA) and the European Union (EU) that the cooperative enterprise is one of the few forms of organisations that could combat all dimensions of poverty. Cooperatives have the advantages of identifying economic opportunities for the poor, empowering the disadvantaged to defend their interests and providing security to the poor by allowing them to convert individual risks into collective risks (Wanyama, Develtere and Pollet (2008:6).

Yusuf and Adedayo (2004:123) argued that the failure of the poverty alleviation programmes initiated by different tiers of government in Nigeria indicate that there is a socio-institutional dimension to the problem and as such, an institutional approach should be considered in the design and implementation of poverty alleviation programmes in the country. This according to them should begin with an examination of the institutions and organisations that govern access to assets, finances and services in the creation of wealth. In other words, for cooperatives to be result-oriented in Nigeria, there is need for a re-examination of their activities and operations as well as the role of government in its promotion. Birchall (2003:3) maintained that for cooperatives to play the role of poverty alleviation, a number of conditions must be met. There should be an appropriate environment that enables cooperatives to be true to their principles. In addition, serious promotional efforts by different social actors as well as strong focus on human resource development should be accorded strategic place for cooperatives to thrive better and contribute to the growth and development of the Nigerian economy. Promoting and encouraging effective cooperatives is imperative if Nigeria is to be successful in reducing the misery and poverty faced by millions of people in the country. Effective cooperatives could also be important tools for poverty alleviation in most African countries, considering the level of poverty in these economies and the percentage of their populations that reside in the rural areas, who engage in agriculture and informal business activities as well as small and medium scale enterprises.

COOPERATIVES AND ECONOMIC DEVELOPMENT

Economic development, which has to do with a qualitative change that takes place in all facets of a given society seems to be very difficult to achieve as against economic growth- a sustained increase in the level of real gross domestic product (GDP) of an economy. This therefore calls for a deliberate and concerted efforts geared towards achieving this lofty goal in the society. Effective cooperatives could be very vital, considering the important roles they play in the development process going by the various areas in which they contribute to the growth of the economies of many countries. Although, cooperatives directly

benefit their members, they also offer positive externalities to the society, which has a transformational impact on the economy (GSDRC, 2011:5). Therefore they are able to promote economic capacity and bring sustainable development.

According to Dogarawa (2005:8), cooperatives play an increasingly important role in facilitating economic growth and social development. Most of the services they render underscore their importance in fostering growth and development in our contemporary economies, particularly in low income countries of Africa. Hence, he suggested that the promotion of cooperatives should be considered as one of the pillars of national economic and social development. In addition, the United Nations (UN) takes a 'cooperative' approach to development. It insists that development must be community-driven, with funds channeled directly to community groups, and with capacity building of self-help groups being the key to success (Birchall, 2003:17). In a report on the socio-economic impact of cooperatives, UN (2009:19) posited that "leveraging the contribution of cooperatives to development requires the promotion, formation and growth of cooperatives in a manner that is sustainable and respectful of their autonomy". This implies that for cooperatives to have a significant impact on economic development, they must be properly organized, coordinated and managed.

ROLES OF COOPERATIVES IN POVERTY ALLEVIATION AND ECONOMIC DEVELOPMENT

The contributions of effective cooperatives to economic growth and development processes cannot be overemphasized, particularly in low income countries like Nigeria, where a large number of the citizens still live below US$1 per day. Some of the strategic roles cooperatives could play in alleviating poverty and bring about economic development of any country are discussed below.

Promotion of Savings

Cooperatives encourage their members to form the habit of saving without being extravagant. They mobilize savings and pool available resources from the members, utilize the same in the best possible manner and share the benefits among members. Consequently, they can be set up in poor communities, where access to savings and credit at non-exploitative terms is of greatest importance (Adekunle and Henson, 2007:678). UKAid reiterates that cooperatives enable poor people to access financial services, credits, as well as insurance and remittances, which go a long way to reduce vulnerability since the poor could accrue savings, own assets and smooth out consumption by virtue of their participation in the association. In Nigeria, the credit and thrift cooperative has been a major avenue for the working class to save part of their incomes because such savings are deducted directly at source, and this seems more convenient than bank savings that attract virtually 0% interest.

Access to Fund

The stringent conditions attached to loan by formal financial institutions and the inability of funds made available by existing banks to reach the poor segment of the population have increased the relevance of the informal financial institutions (Yusuf and Ijaiya, 2009:71). This underscores the relevance of cooperatives in the provision of funds to members at affordable and low interest rate. Elhiraika (1999:355) has noted that lending by traditional formal financial institutions to small borrowers in developing countries is often limited due to

collateral requirement and high interest rates. Cooperatives assist their members financially by providing loans at low interest rate for start-up capital or for business expansion thereby promoting entrepreneurial activities. The interest rate charged by them is usually lower compared to what obtains in the formal financial institutions. Since members do not require any collateral securities to access loans, (it is assumed that a member's shareholding is his/her collateral) loan procurement is made easier and almost stress free. The staff cooperatives in most organisations are formed to bridge this gap and help members have access to credit, which enable them to acquire the basic necessities of life and to improve their standard of living (Azeez, 2011), to start a business, pay medical bills, further their education or sponsor education of their children (Wanyama, Develtere and Pollet, 2008:27).

Employment Generation

Various cooperatives such as the agricultural, thrift and credit, producers', consumers' and multipurpose cooperatives have provided employment to many people across the world. The Department for International Development (DFID) of the UKAid cited an ILO study and reported that cooperatives, which have more than 800 million members globally, provide employments for over hundred (100) million people, which according to the report is more than the number of people employed by the multinational corporations globally. According to this study, which was authored by Hertig and Elena in 2008, the number of jobs created by cooperatives all over the world is 20 percent more than the one provided by multinational corporations. It further noted that cooperatives are the largest employer in Switzerland and Quebec province in Canada, the second largest employer in Colombia, generate more than a million jobs in France and Italy and also provide 71 percent of all jobs in the state of Wisconsin, USA. It furthermore maintained that the Indian dairy cooperatives employed about 12.96 million families. These are all facts of how important cooperatives are in contributing to growth and development process in the economies of the world.

Wanyama, Develtere and Pollet (2008:19) identified three different ways cooperatives contribute to employment. These according to them include direct wage employment, which is provided for those people who work in primary and secondary cooperatives as well as in government cooperative support institutions (Ministries, Departments and Cooperative Colleges) whose existence is mainly on account of cooperatives, self-employment to members and indirect employment, which is obvious in the spillover effects of their activities on non-members whose income-generating activities are only viable through the transactions they have with cooperative. In addition, low interest loans given out to members assist in investment activities including the establishment of small and medium scale enterprises, which in turn provide employment for the owners and the employed workers. They also offer youths in their base communities short and long-term employment positions. Students could also be employed on casual-appointment basis during long vacations (Dogarawa, 2005:8). Through these, cooperatives contribute to poverty reduction and economic development.

Improvement in Members' Incomes

Cooperatives are specifically seen as significant tools for the mobilization of resources for income generation. ACDI/VOCA has maintained that cooperatives help to improve members' incomes through various activities aimed at securing better prices for any product they purchase on behalf of members, low input costs, strengthening of bargaining power, gaining greater control of market channels and thus offering a better chance to be profitable. The

agency reiterates that when members' incomes are improved, it tends to increase demand for goods and services, attracts traders and other business support entities (including credit institutions), encourages communications and travel and reduces isolation.

Increased Productivity

Increased productivity is the bedrock of growth and development in any economy, which consequently could result to a reduction in the level of poverty since income level in the economy eventually will increase. The activities of cooperatives, which manifest in form of production, distribution and consumption, tend to increase productivity at the societal level. UKAid reports that the combined turnover of the top 300 global cooperatives stands at 1.1 trillion US Dollars. It further noted that cooperatives contribute about 9 percent to the GDP in Vietnam and 45 percent in Kenya. The agency cited the report of the Cooperative Bank of Kenya for its 2008/2009 year turnover put at over £900 million with the combined assets of all Kenyan savings and credit cooperatives as 2.7 billion US Dollars. In addition, the agency maintained that the 2008 global recession notwithstanding, an Indian dairy cooperative named Amul reported a turnover of £750 million for the 2008/2009 year with sales growth of 27 percent. Information made available on the Kathmandu Post (2011) revealed that there are 20,000 cooperatives in Nepal and their contributions to the improvement of the economy of the country have been very significant. In fact, the report states that cooperatives contribute 10 percent to the financial sector in the country and that the financial transaction carried out through cooperatives worth over 100 billion with the share capital of cooperatives working in different sectors reaching a record of Rs. 9.36 billion. It further stated that the accumulated savings and investment courtesy cooperatives in the country were Rs. 58 billion and Rs. 61.54 billion respectively. These facilities help to raise the members' standard of living, boost their productivity and contribute to the growth of the entire economy.

Ease of Commodity Procurement

To overcome the constraint of access to more goods and services occasioned by low level of income, cooperatives encourage and assist their members to acquire durable assets. These according to Yusuf and Adedayo (2004:129) include but not limited to houses, motor cars, motor cycles, electronics, grinding and milling machines, sewing machines and others which may include landed property and computers. With this, cooperatives have been very strategic in enlarging members' access to a variety of commodities at affordable prices through collective negotiation, loans and other facilities, which are important for their well-being.

Food Security

One of the core problems confronting most African countries is food insecurity. Countries such as Somalia, Niger and some parts of Kenya have been battling with extreme famine due to insufficient food. To tackle problems of this nature, cooperatives could be considered as one of the veritable tools. In the period when many countries in Africa are experiencing famine, the role of cooperatives in ensuring food security cannot be underestimated. Agricultural cooperatives are very instrumental not only in the production and distribution of food necessary for survival but also as agents to support food security. In a report on cooperatives and development, GSDRC (2011) revealed that "in India, there are some 150,000 primary agricultural and credit cooperatives serving more than 157 million agricultural/rural producers." In the same vein, Cooperative League further asserts that

corporative helps members in farming to reduce overdependence on government by cutting farm costs and adding to income in order to help the rural communities to survive and prosper by refunding retail and manufacturing margins to customers. They normally respond to market demands, improve technical and managerial capabilities and address the needs of the farmers thereby increasing the production of food for the populace. Deji (2005:147) states that membership of a cooperative could be one of the strategies to improve adoption of agricultural innovations, and this could lead to increase in food production.

Agent of Social Change

In addition to the conventional functions, cooperatives could serve as agents of social and economic change, and are therefore vibrant civil society actors. In this regard, cooperatives are unique institutions that balance and negotiate relationships between their members, communities, traders, the state and national community. Today, governments expect cooperatives to inform policy making and engage in advocacy while the cooperatives themselves seek a more pronounced, active and permanent role in decision-making (Gunga, 2008:3).

COOPERATIVE VALUES AND PRINCIPLES

For cooperatives to function effectively and efficiently, they must be governed by universally accepted values and principles. Cooperative values are general norms that cooperators, cooperative managers and staff should share and which should determine their way of thinking and acting. The values, which are articulated by ILO in a statement in 2002, include but not limited to self-help, self-responsibility, democracy, equality, equity and solidarity. In articulating the values of personal and ethical behaviour that cooperators should actualize in their enterprises, it further stated that a cooperative is meant to embody ethical values of honesty, openness, social responsibility and caring for others.

These principles are also guidelines by which cooperative enterprises put their values into practice. The principles rest on a distinct philosophy and view of society that help members judge their accomplishments and take decisions. The first set of cooperative principles was developed by the Rochadale Society of Equitable Pioneers established in 1844 in England. In 1937 and 1966, ICA made formal statements of cooperative principles to guide cooperatives globally (Dogarawa, 2005:5). ICA (1995) reviewed the principles and identified seven important ones that should guide the formation, organisation and activities of cooperatives in the 21st century. These include: Voluntary and Open Membership (VOM); Democratic Control of the Business Enterprise (DCBE); Members Economic Participation (MEP); Cooperatives are Autonomous and Independent (CAI); Education, Training and Information (TI); Cooperation among Cooperatives (CC) and Concern for the Community (CfC).

The principles imply that membership of a cooperative should be voluntary and should be open to all those who have common interest with free entry and free exit. To be able to form a cooperative in Nigeria, the Cooperative Societies Act specifies that a minimum of ten members who are 18 years and above are required. However, it did not specify the maximum number but after formation, members may specify the maximum number (Agbetunde, 2007:7) and after establishment, the organisation should be managed on democratic rules.

Cooperatives are usually managed by a group known as "Board of Directors" whose members are the elected representatives. Every member is expected to actively participate in the cooperative activities, policy formulation and planning. Decisions are taken at general meetings and each member has a single vote, irrespective of the number of shares held. Furthermore, members are expected to contribute capital equitably while the enterprise provides benefits and services, which help to enhance members' ways of living. Cooperative arrangement is based on the powerful idea that together, a group of people can achieve goals that none of them could achieve alone (Dogarawa, 2005:2). In addition to providing services to its members, cooperatives also generate some profits while conducting business and such profits are distributed among members on the basis of the number of shares held and as well as on members' participation in the business of the cooperative. For example, in a credit and thrift cooperative, only a small part of the profit is distributed to members as dividend on their shares; a major part of the profit is paid as purchase bonus on the basis of goods bought by each member and the amount of loan procured.

In addition, cooperatives should be autonomous and independent, which must be clearly spelt out, and they should also be left entirely to the members for proper management and control. If they enter into agreement with other organisations or governments, such should be based on terms that ensure democratic control and the sustainability of their autonomy. Also, members should be given continuous education and training for effective and efficient participation in cooperative activities. In addition, cooperatives thrive on the principle of mutual help and cooperation. They convert the weaknesses of members into strength by adopting the principle of self-help through mutual cooperation. It is only by working jointly on the principle of "each for all and all for each", that the members can fight exploitation, show concern for the community and secure a place in the society. These values and principles make cooperatives possess some attributes that distinguish them from other associations and make them well suited for poverty alleviation, economic growth and development.

THE STATE OF COOPERATIVES IN NIGERIA

The current state of cooperatives in Nigeria seems not to be different from what obtains in most African countries. In spite of the important roles they play in development process and poverty alleviation, a good number of them are still bedeviled with many problems and this continue to prevent them from taking advantage of the enormous potentials inherent in them. In fact, the numerous upheavals, which are multifaceted in nature, operate like 'giants' steering them in the face prevent them from recording successes in terms of poverty reduction and development in most developing countries. The major challenges inherent in the cooperative movement in developing countries include lack of proper management, inadequate financing, poor cooperative integration, government unfavourable policies, resistance to change, illiteracy and lack of training facilities (DCFS, 2011); over-control and regulation by government, limited access to credit and inability to penetrate markets (GSDRC, 2011:1). The economic situation of Nigeria continues to impact negatively on the operations of cooperative enterprises, and as such it becomes increasingly difficult for most of them to meet the goals for which they were set up. To critically x-ray the current condition of the organisations in the country, we consider it more appropriate to look at the various challenges that militate against their operations and objectives. These are discussed below:

Poor Governance and Limited Management Skills

Cooperative is a vital avenue for building wealth but lack of good managerial skill on the part of many proponents hinders this objective and where such skill exists, it is from time to time grossly under-utilized (Azeez, 2011). (Agbo, 2009:173) argued that cooperatives in Nigeria are not adequately alleviating poverty because of mismanagement of the existing ones while the managements of some of the organisations lack vision and the will to exploit the potentials in cooperatives. Also, when the governance of a cooperative is not built on fairness and transparency but on selfishness and corruption, then it will not be able to contribute much to development.

Inadequate Fund and Limited Access to Investment Capital

In Nigeria, savings of members are usually very small due to low income status of the population (Yusuf and Ijaiya, 2009:80) and as such, majority of the cooperatives do not have enough fund to give out as loans to their members. Some give less than what members request for, which may not be sufficient for the project such member intends to utilize the loan on. Yusuf and Adedayo (2004:127) in their study reported that about 31 percent of cooperative members in Nigeria claimed that the loan is usually inadequate for the purpose it is intended. Bamiduro (2011:5) identified lack of adequate funding as one of the inhibiting factors for the inability of most poverty alleviation strategies to yield results. (Agbo and Sand, 2010:1) in their views stated that one of the major challenges of cooperative is limited access to investment credit. They observed that even when fund is made available for cooperatives by the government, it is still very difficult for members to access such fund.

Ineffective Implementation of Government Policies

Poor monitoring of government policies has also been the bane of effective poverty alleviation programmes in Nigeria (Bamiduro, 2011:4). The government has intervened several times to inject credit into the cooperative sub-sector of the economy over the years, but it is saddened to note that such monies ended up in wrong hands for wrong purposes, living crippled, the activities of cooperatives in the country. In 1976, the government decided to change the Nigerian Agricultural Bank Ltd to Nigerian Agricultural and Cooperative Bank Ltd so as to give special attention to cooperative activities, but yet not much has been seen in terms of assistance to cooperatives from this bank. Furthermore, in the year 2000, the government renamed the Nigerian Agricultural and Cooperative Bank (NACB) Ltd as the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB) Ltd to reflect the rural nature of cooperative activities in the country. In 2005, the Federal Government domiciled the sum of fifty billion naira (₦50 billion) with the NACRDB Ltd to lend to Agricultural cooperatives at concessionary interest rates. Agbo and Sand (2010:2) reported that an evaluation of the patterns of disbursement of the ₦50 billion intervention funds showed that more than 75 percent of the funds went to private farmers and other farmers' organisations that were not cooperatives. As such, to recover the loan became a major problem.

Resistance to Change

Dogarawa (2005:15) posited that inability to adapt to changes in the environment is a challenge to cooperatives. A cooperative is a business enterprise (Agbetunde, 2007:5) whose

activities and operations are also affected by the business environment in which they operate. The elements of the business environment could be opportunities (when they are favourable) or threats (when they are unfavourable). It is expected that when there are changes in the business environment, the business enterprise has to adapt appropriately. However, most cooperative organisations in Nigeria find it very difficult to adapt to changes that are required to make them more viable and efficient.

Inadequate Education in Cooperative Operation

In a study carried out by Agbo (2009) on farmers' perception of cooperative societies in Enugu State, Nigeria, it was discovered that poor cooperative education and illiteracy has been one of the greatest hindrances to growth of cooperatives in the state. Adeyemo and Bamire (2005) also found out in their study that cooperative farmers in southwestern Nigeria are mostly males, literate and of average age of 47 years. Educating, training and re-training of members in general and officers in particular have been a challenge to cooperatives in Nigeria (Dogarawa, 2005:16). Agbetunde (2007:222) stated that cooperative awareness is high in Nigeria but knowledge of the cooperative principles, values, ideas and practices is very low. As such, issues are handled as they come without proper knowledge and skill necessary to handle them. In fact, some of them lack appropriate documentation, which continue to breed corruption within the organisation.

Inadequate Marketing Activities

Cooperatives are expected to create and develop income-generating activities and sustainable decent employment (ILO, 2002). Marketing activities enable a cooperative to generate fund and contribute significantly to the community where it operates. However, cooperatives in Nigeria are not adequately involved in marketing activities. In a study conducted by Agbo (2009:172), it was stated that most of the farmers that joined cooperatives did so to attract services from government, thereby perceiving cooperatives as government agency rather than as autonomous business outfit. The study found that only 0.35 percent joined cooperatives for the purpose of marketing their products. All the challenges considered above have continued to hamper the performance of cooperative organisations in Nigeria, and addressing them will go a long way to make them effective and efficient tools for poverty alleviation and economic development.

STRATEGIES FOR COOPERATIVE EFFECTIVENESS IN NIGERIA

Asides adhering to the values and principles stated above, how can cooperatives in Nigeria perform efficiently their roles in the society? There is no doubt that Nigerians are aware of the importance of cooperatives (Yusuf and Adedayo, 2004:125; Agbo, 2009:172, Agbetunde, 2007:222). The consumers' cooperatives, producers' cooperatives, agricultural cooperatives and the savings and credit cooperatives in the country are evidences pointing to the fact that cooperatives worth the while in the economic transformation and poverty alleviation. It is important to state categorically that the problems besetting cooperative enterprises in most developing countries in general and Nigeria in particular are both internal and external. As such, there is the need to realize that both internal and external strategies are required to tackle these problems and challenges. It should be appreciated that the internal strategies of cooperative marketing, cooperative management and cooperative financing with external strategy of government assistance are necessary for cooperatives to be

able to function effectively and to achieve its objective of poverty alleviation and economic development. It should be noted that for the government to assist, there must be some form of control and regulation, but care must be taken to avoid excessive control and overregulation, which may hamper cooperative autonomy and prevent them from being true to their values and principles. On that note we propose the following:

Cooperative Marketing

Cooperative marketing involves collectively producing, pricing, distributing, promoting and selling products to achieve desired goals. It also includes offering members an assured market for their products. Cooperatives could assemble the products of a number of producers into larger lots to facilitate more efficient handling and more competitive sales, and then grade and market these products or they may be directly involved in the production of the products. Majority of the cooperatives in Nigeria only encourage savings by members and granting of loans. If this continues, it will be difficult for them to make a significant impact on poverty reduction and economic development. This accounts for the depreciation of the contribution of the Agricultural sector to GDP in Nigeria. Cooperatives must strive continuously to be productive with the available resources at their disposal. A particular percentage of the cooperative fund (between 1 percent and 5 percent) should be allocated for marketing purposes. They should invest in productive activities that will enhance the dividend of their members. They can also be involved in the provision of services such as laundries, restaurants, filling stations, transportation, housing, health care services and schools. Although, cooperatives are not set up for the purpose of profit making, they make decisions that balance the need for profitability with the welfare of their members and the community, which they serve. It was reported in UN (2009:5) and GSDRC (2011:10) that in Bangladesh and US, rural electricity cooperatives were set up to meet communities' own needs in the absence of any external private firm seeing it as a viable market opportunity.

In Bangladesh, rural electric cooperatives provide service for 28 million people. In the United States, 900 rural electric cooperatives serve 37 million people and own almost half of the electric distribution lines in the country. With this, they are able to create jobs, generate profits, which can be used to increase members' incomes, increase funds for loan and improve productivity. In the privatization process that has been going on in Nigeria, cooperatives have not been able to acquire any of the services. Cooperative marketing is indispensible in Nigerian cooperative movement because it will ultimately help members to improve on their living conditions and pull them out of poverty. Therefore, efforts should be directed at encouraging multipurpose cooperatives so that they can be involved in such marketing activities. The role of government in cooperative marketing is to provide enabling environment that creates economic conditions favourable to profitability and a regulatory system favourable to business success. When this is in place, it will become easier for cooperatives to venture into the activities mentioned above.

Cooperative Management

The strategy (cooperative marketing) discussed above is very critical for effective management system. If this is adopted it will be easier to sustain cooperative movement. Cooperatives need democratic, fair and transparent management and good governance for better operation and performance. Effective management system involves carrying along members in all decision processes. This gives members the opportunity to determine how the

proceeds of the cooperative can be utilized. When members are involved and informed on the direction the organisation is going, they are more willing to invest and patronize the cooperative, increase their feeling of ownership and responsibility for its success.

They should also be involved in planning and good record keeping. Planning entails developing a vision and mission statement, appraising the future, assessing the external and internal business environment, defining desired goals with stated objectives, and developing a course of action to reach them. In addition, cooperatives must develop and install a double-entry accounting system, prepare financial reports including operating and capital improvement budgets and report to the members in a clear and timely manner. They should also account for members' contributions and purchases as these determine dividend allocations from net earnings. The management must prepare periodic operating statements and balance sheets to inform the board and members on how the cooperative is performing and its financial condition. Reports should come often so that the board can satisfactorily monitor their activities, take appropriate actions and keep members informed on how their cooperative is progressing. An annual independent audit should also be carried out to serve as an outside appraisal of the cooperative's financial condition to act as a check on the business and accounting procedures. These will also help to promote transparency.

In the area of cooperative management, the government could assist in training and capacity building to enhance managerial ability. The government through its ministries and departments should be more effective in their responsibilities. They should regularly organize seminars, workshops and lectures to help enlighten members on the roles of cooperatives in poverty alleviation and economic development. They should also instruct cooperators and cooperative officials on values, principles, laws, book-keeping and practices of modern cooperative. The impact is that it will inculcate in cooperators and cooperative officials the right attitudes, skill and character required for effective and efficient operation.

Cooperative Financing

Cooperative financing is the process by which cooperatives raise funds needed to finance their operations. The sources of their funds include contributions by members, incomes from business activities, loans from governments and financial institutions. Virtually all cooperatives require some level of member financing, usually in the form of stock purchases or membership fees. Member financing not only provides equity for the cooperative, it also provides a financial base that helps other investors, particularly banks, feel more secure in investing in the cooperative (Dogarawa, 2005:13). Although, Agbo (2009:174) suggests that government should not interfere in the activities of cooperatives, but where this is deemed necessary, such intervention should be limited only to the provision of enabling environment for cooperative businesses to thrive. For cooperatives to be useful tools for poverty alleviation and economic development, governments all over the world should encourage them through financial assistance and direct loans. Cooperative banks are the channels through which government gives aids to cooperatives. They are established to offer greater access to savings and borrowing facilities for cooperative enterprise and their members at relatively low interest rates. By increasing cooperatives' access to finance, the challenge of inadequate fund will be overcome. Another aspect that the government has to look into is the effective implementation of any financial assistance. Government should ensure that all policies and intervention programmes are controlled and monitored to achieve the stated objectives.

CONCLUSION

Cooperatives are organized to improve the standard of living and general welfare of the members by meeting the economic, social and cultural needs and aspirations of members and the society. In spite of the tremendous roles of cooperatives, a lot of them are still bedeviled with many challenges in developing countries. As such, they are not able to adequately contribute to economic performance and poverty alleviation. Making cooperatives in developing countries in general and Nigeria in particular to be more effective is imperative for poverty alleviation and economic development. Their operations and management must be geared towards making them to contribute significantly to the economies where they operate. Also, regardless of a cooperative purpose or membership size, adherence to the values and principles of cooperation is relevant in shaping the way of thinking and behaviour of cooperators, cooperative leaders, cooperative staff and cooperative regulators.

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Chapter 4

THE ROLE OF INFORMAL MICROFINANCE AND COOPERATIVES IN POVERTY ALLEVIATION AND ECONOMIC DEVELOPMENT

Alexandra **PEDZINSKI**

Franklin **ODOEMENAM**

INTRODUCTION

The idea of inclusive financial services for the poor rests largely on the assumption that such systems bring about genuine economic growth and poverty reduction by granting access to resources that can be used to enhance the productivity and boost incomes of micro and small entrepreneurs. However, little focus is placed on the duality of the financial sector between the formal and informal. Especially with the exponential rise of formal institutions dedicated to providing 'pro poor' services and with the transformation of microfinance NGOs into commercial banks, the role of informal micro financing is reduced to something secondary and diminishing. Nevertheless, the informality of developing economies remains strong and is even experiencing a rapid resurgence in countries like Nigeria (Yusuf et al., 2009), where the convergence of ineffective government financial and monetary policies exacerbates the inability of formal financial institutions to reach the poorest of the poor.

The prevalence of informal economic systems amongst the growth of the formal microfinance sector exposes the inherent strengths of traditional cooperative financing mechanisms for rural development, especially in Nigeria's array of villages that still adhere to strong kinship networks. Familiarity, trust and convenience (in terms of proximity) characterize most informal transactions, while unregulated lending terms are generally conducive to the uptake of financial services by the poor. Ultimately, the greatest illustration of the strength of Nigeria's informal economy is the fact that it provides services for 65% of the economically active population and is responsible for 90% of new job creation (Meritime Securities, 2009). As such, figures like the recent finding by Microfinance Information Exchange that 80 million adult Nigerians remain unbanked (MIX, 2011) must be taken with the proverbial 'grain of salt'. In other words, statistics depicting the state of formal financial inclusion in the country don't take into account the dynamic activities of the informal sector in such a large developing economy that may have a prominent role in poverty reduction and economic growth.

The following analytical study seeks to describe the role of informal microfinance, particularly through cooperatives, in poverty alleviation and economic development in Nigeria. The literature review outlines key barriers to the country's socioeconomic development and conceptualizes poverty, economic development and microfinance through

the lens of the capability and asset-building approaches. It then goes on to detail the trajectory of microfinance in Nigeria and the distinction between formal and informal financing for micro entrepreneurs. The methodology and data presentation are contingent upon case studies of informal cooperatives in Enugu, Imo and Ekiti State, respectively. The data analysis and conclusions extract broader insights into the particular strengths of informal microfinance and touch upon further research endeavors in these areas.

LITERATURE REVIEW

As arguably the largest market in Africa, in the sense of being the most populous country on the continent with over 150 million inhabitants, Nigeria presents countless opportunities for financing economic activities. However, systemic development challenges have squandered the hopes of millions of poor Nigerians to access the resources needed to boost local economic growth and improve their livelihoods. It is estimated that an unprecedented 70 percent of Nigeria's population is living below the international poverty line of $1.25 per day (CIA World Factbook, 2007) and the country was recently rated in the category of "least human development", ranked 156 out of 187 developing countries by the UN's Human Development Index (UNDP, 2011). Other than extreme poverty, Nigeria's development challenges include an undiversified economy, bad governance characterized by corruption and lack of transparency and accountability, and income inequality.

With the advent of oil discovery in the 1960s, Nigeria's economy has undergone appreciable distortions in sector dominance. Today, approximately 95 percent of Nigeria's revenue comes from the oil sector (USAID, 2010). In turn, the country has gone from being a model breadbasket for other developing African countries to facing a food import bill of $4.2 billion per annum (*Nigerian Tribune,* 2011). Since the oil boom, Nigeria's agricultural sector has been ravaged by inconsistent government subsidy policies, neglect of indigenous farmers and local markets, harsh climate changes and extensive rural-urban migration. The convergence of these forces gradually transformed Nigeria from an agricultural export powerhouse into a net importer for the last 40 years, increasingly dependent on external sources for its food security and sustainability. Even today, although agriculture accounts for 41% of GDP, 38% of economic growth and employs about 70% of the population, agricultural exports account for only 2.6% of Nigeria's total exports (USAID, 2010).

This trend has had an indelible effect on smallholder farmers and agricultural cooperatives, groups that also fall into the category of the marginalized rural poor. Although the demand for financial services for these groups remains high, formal institutions lack the incentive to overcome the high costs associated with reaching the rural poor. In fact, only 500,000 smallholder farmers in Nigeria have access to insurance (MIX, 2011), a vital buffer for the inherent volatility of the agricultural sector. It is evident, especially in Nigeria, that a rise in informal and private sector intervention in the economy can be attributed to government incapacity to bring financial services to the population at large, let alone those at the bottom of the pyramid. In Nigeria's case, current day corruption and bad governance can be traced back to the discovery of vast quantities of crude oil and natural gas in the 1950s. Although it was not until the 1970s that oil came to dominate the economy, transforming into an oil-rich country in a short amount of time jump-started Nigeria's trajectory as a state inflicted by the Natural Resource Curse. Such a characterization is applied to countries that are rich in natural resources (i.e. oil in this case) and yet their people continue to suffer from low socioeconomic development (Frankel, 2009:3).

Nigeria's high economic growth generated by the oil sector in the past decades is a façade for a country mired in poor resource management, rampant corruption and patrimonialism, an extreme lack of transparency and accountability, and weak or nonexistent institutions, all of which fall under the umbrella of bad governance. This precarious combination has rendered the government virtually incapable of responding to the needs of the people, particularly the millions of those living below the poverty level. In lieu of this void, informal financing mechanisms have been strengthened while formal institutions have emerged to respond to the exponentially growing demand for inclusive financial services.

Nigeria's oil curse has also contributed to an endogenously evolving wealth gap between those leveraged to reap the benefits of a corrupt system and those 'left behind'. Besides a high Gini Coefficient, pervasive income inequality has manifested in great disparities in the financial services sector. Perhaps, more pressing is the recognition that institutions created to address the circular problem of poverty and economic exclusion, namely microfinance NGOs, banks, and non-bank financial intermediaries, are increasingly experiencing mission drift as they expand and commercialize. In this transformation process, their social mission of reaching the poorest of the poor is shifted to targeting middle income clients in order to meet new regulations and collateral requirements. The ultimate result is a widening wealth gap that increasingly marginalizes those at the bottom of the pyramid.

The broad notions of poverty and economic development in relation to microfinance as a practice are, for the purpose of this paper, conceptualized within the theoretical framework of the capability approach (Sen, 1999) as well as the asset-building approach (Sherraden, 1991; Oliver and Shapiro, 2001), both of which are central to sustainable development theory. Both approaches challenge conventional measurements of the relationship between poverty and economic development vis-à-vis income or consumption. Within the context of this paper, this approach creates a framework for answering guiding questions such as: What are the causes of prevailing and widespread poverty in Nigeria? Does self-help based financing present a strategy to poverty alleviation through empowerment and enhanced livelihoods? Much of the current day relevance of the capability approach can be attributed to a reconstitution of poverty, including a shift in perceptions of the poor and a new understanding of their financial habits and needs (Pedzinski, 2011). What was once considered a static state of living affecting a homogenous group, "poverty" is now understood as a dynamic categorization grounded in a variety of endogenous and exogenous factors affecting a diverse group of individuals with complex livelihoods. Poverty, in the nuanced sense, is not just a state of living demarcated by a figure determined by multilateral institutions, but rather a state of physical, social and other deprivations that limit the choices that the poor can make in their daily lives.

Within the framework of the asset building and sustainable development model, economic development is categorized on a variety of levels (individual, family, communal, national) and measured in a number of ways. It is not enough to say that economic development is simply economic growth. For the purpose of this paper, economic development can be considered any or all of the following besides just GDP growth: Job creation, Reduction in absolute poverty count, Narrowing income differentials, Economic empowerment, Enhanced financial literacy, Reduction in vulnerability and exposure to financial risk, and Wealth creation/Increase in assets. Standard definitions of microfinance describe it as a method to offer poor people access to basic financial services such as loans, savings, money transfer services and micro insurance (CGAP, 2012). Nevertheless, as the sector expands, institutions

are discovering and developing more diversified products, services and methods of delivery. For the sake of the topic at hand, a clear distinction needs to be made between formal microfinance and informal microfinance.

CGAP defines formal financial providers as "those that are subject not only to general laws but also to specific banking regulation and supervision (development banks, savings and postal banks, commercial banks, and non-bank financial intermediaries) (CGAP, 2012)." Semiformal providers are registered entities that are subject to commercials laws but are not necessarily regulated or supervised by banks, including financial NGOs, credit unions and cooperatives, although these may also fall into the category of informal groups.

Informal microfinance, on the other hand, refers largely to traditional methods of trading and financial exchanges that emerge organically and are shaped by cultural values and norms. It can be defined as a method to offer poor people access to basic financial services, but through the *informal sector*, or outside the purview of government regulation (Ekpo et al, 2012). Informal economic activities encompass a wide spectrum of small-scale, self-employment and subsistence activities, such as petty trading, smallholder farming, repair services, etc., as well as unregulated remittances. Unlike the structured formal sector, informal activities are difficult to measure, but it is evident that they are "highly dynamic and contribute substantially to the general growth of the economy and personal or household income (Ekpo et al, 2012)."

NIGERIA'S MICROFINANCE SECTOR

Evolution of Microfinance in Nigeria

Before the spawn of Nigeria's formal microfinance industry, indigenous microfinance practices dominated the way that people accessed financial resources and made financial transactions. In Nigeria, although not exclusively, informal sector finance was and still is distinguished along traditional tribal lines, with varying characterizations by the Hausas in the north, the Yorubas in the west and the Igbos in the southeast. Indigenous microfinance arrangements assumed names like *esusu* to describe rotating savings and credit associations and *ajo* to describe daily contribution schemes, or pooling (Oloyede, 2008). The evolution of indigenous microfinance practices into formalized microfinance institutions parallels the growth of a variety of channels and influences that have determined the current day characteristics of Nigeria's financial sector. These include mainly the rise of NGOs, government initiatives and private sector actors. As ascertained by Ehigiamusoe (2011), "Non-governmental Organisations played a pioneering role in the development of modern microfinance in Nigeria (64)". Before government policy took root in formalizing indigenous microfinance practices, NGOs with a strict social mission to address poverty began setting up a framework for the provision of affordable financial services to the rural poor, especially women. Microfinance gradually became an autonomous extension of the health and other social services provided by NGOs. Some early pioneers of community-based credit and savings initiatives include Lift Above Poverty Organisation (LAPO), Farmers Development Union (FADU), Community Women and Development (COWAD), Development Exchange Centre (DEC) and Community Development Foundation (Ehigiamusoe, 2011).

Much of the support given to the flourishing of NGOs and emerging microfinance institutions (MFIs) came from foreign foundations and multilateral agencies in their attempt to address

growing concerns over poverty and the evidence of extreme wealth disparities between what was then labeled as the First world and Third world. A critical source of support came from the United Nations Development Program (UNDP) and United Nations Capital Development Fund (UNCPF) in their implementation of the Micro-Start Program modeled after ASA Bangladesh. From 1998 to 2004, the program provided eight promising MFIs throughout the country with targeted technical assistance in line with international best practices for the provision of 'pro poor' financial services. Other key players in the burgeoning of Nigeria's microfinance sector were the Ford Foundation, Grameen Foundation and Oxfam-NOVIB (Ehigiamusoe, 2011).

Motivated by the rise of non-governmental actors in the financial sector, the Government of Nigeria attempted to gain control by enacting a number of initiatives dedicated to rural development beginning in the 1970s. In particular, the National Agricultural and Cooperative Bank (NACB) and the Rural Banking Scheme (RBS) were founded in order to facilitate financial access to farmers. Subsequently, an Agricultural Credit Scheme Fund was developed to provide a financial cushion for farmers facing risk from natural disasters. Finally, the Export Financing Rediscount Facility was established to formalize and standardize rural credit markets. Despite these measures, it became increasingly evident that such governmental policies failed to grant financial access to those most in need (i.e. the rural poor) and that the programs were largely unsustainable. In 1989, the programs promulgated in the 1970s were abolished in favor of the establishment of The Peoples Bank, with a mandate to lend to the poor. When this also failed, community banks were established to provide non-sophisticated loans to rural areas. Eventually, the Central Bank of Nigeria (CBN) released the "Microfinance Policy, Regulatory Framework (MPRF) for Nigeria," which capitulated the government's direct involvement in the trajectory of Nigeria's microfinance evolution. This policy encouraged many of the community banks to reconstitute themselves as MFIs, and led to a marked increase in non-bank institutions (i.e. microfinance NGOs).

Like the duality of the cooperative movement, private sector actors in the evolution of Nigeria's microfinance sector have evolved from informal, to semi-formal and formal actors working simultaneously in a variety of ways to provide 'pro poor' financial services. Prior to the enactment of the MPRF, private sector intervention in informal lending had traditionally been dominated by moneylenders and itinerant savings collectors. Such options were characterized by private capitalization and seen on the one hand as exploitative due to high interest charges and, on the other hand, as convenient alternatives to commercial loans and savings due to flexibility and lack of collateral requirements. Upon the release of the MPRF in December of 2005, private sector initiatives took on a whole new dimension, as MFIs proliferated throughout the country and individuals and private institutions were allowed to capitalize microfinance banks. Today, there are over 900 MFIs throughout Nigeria. However, with the growing trend to commercialize, private sector actors are losing their autonomy to the purview of the government while simultaneously subjecting themselves to mission drift. Nevertheless, in lieu of an extensive record of government incapacity to bring financial services to those excluded from the sector, private sector-led microfinance plays a crucial role in filling this void.

Formal versus Informal Microfinance in Nigeria

Microfinance as an approach to granting access to financial services to those excluded from the commercial banking sector in Nigeria, has fragmented since the rise of formal MFIs in the

1990s. What was once dominated by informal financing mechanisms is now a sector inundated with a variety of actors seeking to supply a part of the huge market demands. Formal microfinance in Nigeria is notionally under regulation by the Central Bank of Nigeria (CBN) although, in practice, lax enforcement means that many institutions operate autonomously (Marx, 2004:6). Under the umbrella of formal financial institutions lie a number of actors, some of which are specific to the Nigerian context. The most prominent of these are commercial and merchant banks (today known formally as universal banks), which control approximately 90 percent of total bank sector assets (Osabuohien and Duruji:27). Second are state-owned non-bank financial institutions and federal agricultural banks that act as arms of the Nigerian Agricultural, Cooperative and Rural Development Bank, or NACRDB (Marx, 2004:7). Another source of formal micro financing is through registered cooperatives which, despite a long history of significance in the sector, are now virtually defunct (Ehigiamusoe, 2011:91; Marx, 2004:8). Finally, community banks spawned out of a government decree in 1992 that attempted to address the inability of commercial banks to reach rural areas. Although community banks have a commendable motive, their actual penetration in Nigeria is low, accounting for only about 0.6 percent of total bank sector assets (Marx, 2004:15).

The informal microfinance sector, on the other hand, gains its relevance from the large informal economies of developing countries. Indeed, Marx asserts that "Nigeria has a very dynamic informal financial sector, which is certainly among the most dynamic ones on the African continent (2004:5)". Furthermore, Hans Dieter Seibel argues that informal microcredit systems existed in Nigeria as far back as the 15th and 16th centuries (2003:10-12) implying that the country's experience with informal microfinance is far from being replaced by the rise of formal providers. Instead, it is largely recognized that formal and informal financing schemes operate side by side in countries like Nigeria (Anyanwu, 2004:5). The predominant sources of informal financing in Nigeria come from variations of traditional savings and credit associations, or cooperatives. In the north, the rotating savings association meets the needs of most petty traders with a relatively stable source of income that discourages the take up of micro loans. Throughout the country, the rotating savings and credit association (ROSCA) is the preferred mechanism for many micro entrepreneurs. The 'rotating' component refers to a fund that is created from the pooled resources of members, which is then distributed as the groups deem fit. Most smallholder farmers concentrated in the south of the country prefer the non-rotating savings and credit association, in which savings are used for lending purposes and are repaid, plus interest, to the members after a determined time period (Marx, 2004:8-9). Despite various versions, the basic premise of these types of informal lending and savings schemes is that traditional groups work together for mutual benefit, and to meet the common financial needs of the members (Anyanwu, 2004:4; Ehigiamusoe, 2011:82).

Informal microfinance schemes in Nigeria operate under tribal-based distinctions between the three main ethnic groups. *Esusu, adashi* and *etoto* are all terms to describe informal microfinance arrangements by the Yorubas in the west, the Hausas in the north and the Igbos in the east, respectively (Anyanwu, 2004:4). Such informal arrangements are concentrated in rural areas, but are also present in urban communities (Ehigiamusoe, 2011:58).

Measuring the Informal Microfinance Sector

All in all, an analysis of the informal microfinance sector in Nigeria is significantly hampered by the inability to measure the penetration rates of informal arrangements, especially on a national scale. Various studies have attempted to quantify the strength of informal financing in Nigeria: A 2004 study by the Food and Agriculture Organisation (FAO) "estimated that 25 percent of all Nigerians access some informal source of financing (CGAP, 2009:10)". A 2005 study by USAID estimated that a majority of financing for MSMEs comes from informal microfinance such as personal savings and informal lending schemes (CGAP, 2009:10). A 2008 study by FinScope estimated that informal sources were the predominant mode of financing for 24 percent of those surveyed.

Moreover, mechanisms posing as sources of formal microfinance which are supposed to be regulated by the CBN are most often not accounted for by the government when asked to do so. For example, a 2007 study on formal savings and credit cooperatives implemented by the Cooperative Department in the Ministry of Agriculture found over 27,000 of such groups registered at the national level and yet no information was available as to their individual financial details or activities. A CGAP *Access to Finance in Nigeria* report concluded that "In comparison to neighboring countries, savings and loans cooperatives are conspicuously invisible on the landscape of formal financial intermediaries in Nigeria (2009:13)."

Gender Dimension of Informal Microfinance

In Nigeria, as in other developing countries, the clientele of microfinance is dominated by low-income women, especially rural women, inasmuch as they are recognized as the most vulnerable and marginalized demographic group. It is largely qualified that deep rooted structural inequalities (Opata and Nweze, 2009:2) and pervasive gender biases prevalent in developing economies underline the social and economic vulnerability of women in these patriarchic societies. In addition to the provision of inclusive financial services to poor women, microfinance institutions seek to empower this target group through opportunities to better their lives and those of their family. Nevertheless, the high costs of rural financing mean that most women still lack access to financial services and therefore are subject to initiate and build upon informal mechanisms within their communities. In a study on informal women's cooperative microfinance societies in Enugu State, Nigeria, Opata and Nweze found that both systemic gender inequality and lack of access to credit for rural dwellers converge to encourage women to "organize their own forms of microfinance institutions (MFIs) which are peculiar to their own needs (2009:2)."

METHODOLOGY

This paper uses secondary case study analysis of three disparate case studies completed between 2008 and 2009 in various parts of Nigeria. The studies focus on financing of informal cooperatives in Imo state, Enugu state and Ekiti state. All three case studies used qualitative field surveys and/or interviews from a random sample of the target group, i.e. the rural poor, in order to assess variable social impact indicators. The analysis is supported by a causal linkage and theory-building framework as well as exploratory research in relevant fields.

DATA PRESENTATION

Case Study: Enugu State

In 2009, a study by the Department of Agricultural Economics at the University of Nigeria was done to analyze the role of informal women's groups in Enugu State in southern Nigeria (Opata and Nweze, 2009). The study was designed to determine whether or not these women's groups have contributed to poverty alleviation and economic development in a local context through the accumulation of financial assets. The data was sourced from a sample population randomly selected from local women's cooperative groups as well as secondary sources. The study asserted that, faced with gender-induced exclusion from financial services, rural women in Nigeria organize themselves into informal cooperative groups in order to facilitate credit and savings from each other as well as from external actors such as NGOs, donors and development agencies. Utilizing multiple regression model analysis, the study found that informal women's cooperative MFIs have significantly increased the volume of credit and savings of their members and that there is a statistically significant relationship between socioeconomic determinants of these services and the volume of services taken up by the members. In other words, the socioeconomic marginalization of rural women (in terms of gender biases that perpetuate their financial exclusion) and the inability of the government and the commercial financial sector to address these development barriers explain the rise and strength of informal women's cooperatives to identify their own particular needs and to enable them to mobilize credit and savings from local NGOs.

Ultimately, the study shows how poor rural women are able to adopt informal financing mechanisms within cooperative groups to support their income-generating activities and, as such, to leverage increasing access to credit and savings as a result of high repayment rates. In turn, the financial resources are used by the women to overcome gender barriers, increase their incomes and build their financial assets as a way to enhance and sustain their livelihoods. Overall, the study asserted that "Although the road to gender equality and poverty alleviation is rough and challenging, this study has shown that informal women's cooperative MFIs have played a key role in addressing issues of poverty alleviation and gender inequality (21)."

Case Study: Imo State

A 2008 study from the Department of Economics from the University of Uppsala was conducted to determine whether informal lending schemes present a viable poverty reduction strategy in the Obazu community of Mbiere in Imo State, Nigeria. The study analyzed the Obazu Progressive Women's Association, a longstanding NGO of approximately 350 members offering informal financing options to rural women in order to enhance their capacity to contribute to self-induced, sustainable, socioeconomic development in the community. The members include petty traders, smallholder farmers and other micro entrepreneurs living in the outskirts of Owerri, the capital city of Imo State.

From the data collected through interviews and questionnaires, the study was significant with respect to two main independent variables: amount of loan and years of membership. It found that the women who received higher loan amounts (of 40,000 Naira or more) and had been members of the organisation for at least seven years benefitted economically, politically and socially within their community, although all recipients benefitted to some extent. The data

was interpreted using qualitative livelihood indicators portraying the effect of informal lending on poverty alleviation and economic growth at the individual, family and community level. Ultimately, the study found that the women surveyed were empowered economically through increased incomes, socially through enhancing their leverage in the community and politically by strengthening their voice in decision-making processes. It concluded that local community organisations involved in informal lending play a key role in lifting its members out of poverty and contributing to their socioeconomic development.

Case Study: Ekiti State

In a 2008 study published in the *African Economic and Business Review*, Ekiti State was the case study used to determine the effectiveness of the informal financial sector in mobilizing savings for productive investment and rural development in Nigeria (Oloyede, 2008). Ekiti is one of Nigeria's smallest states, situated in the west and consisting of mainly Yorubas involved in petty trading and subsistence farming. According to Oloyede (2008), "The major types of informal financial institutions found in Ekiti State of Nigeria include the rotating savings and credit associates (*esusu*), the daily contribution scheme (*ajo*), moneylenders, traders associations, social clubs, youth clubs, town unions, religious organisations and cooperative thrift and credit societies (36)."

The data of the study was generated through descriptive questionnaires administered to a randomly selected group of over 1,000 respondents within villages throughout the state. An analysis of the data reveals the strength and significance of informal financing for the respondents. A majority of the group (58.6%) patronized the informal financial sector as opposed to the formal and many respondents claim to utilize more than one mechanism, the most popular being the 'periodic contribution (*Ajo*)' group. Ultimately, the study found that most funding for informal financing comes from members' contributions and that these funds are effectively allocated into income-generating activities and/or for sectors directly related to socioeconomic development, particularly education. Moreover, it found that funds are hardly ever used for consumption purposes, largely due to the fact that most respondents are engaged in some level of agricultural activity. The conclusion was that "Informal financial institutions help greatly in improving the rural community by providing funds for activities such as business, agriculture, that accelerate rural development (60)."

DATA ANALYSIS

The examined case studies reveal the significance of informal microfinance for cooperatives in facilitating an environment conducive to poverty alleviation and economic development in the Nigerian context. The qualitative indicators from the individual case studies can be extrapolated from inherent strengths of informal microfinance versus its formal counterpart. The ability of informal financing to address the needs of its recipients is rooted in social theory, or the "idea that social relationships are resources that help people act effectively (Serageldin, 1999:ii)." In the context of microfinance, social theory translates into social capital, or the idea that members of informal arrangements are mutually dependent on each other in order to reap the benefits of the financial services. This is the case when members of informal cooperatives are organized into self-help groups and essentially guarantee the loan for each other, so that if one person in the group has trouble repaying, the other members can mobilize to support them. This mutual dependence also works in creating "positive pressure" to contribute to repayment lest the others suffer from default.

It is clear from the case study data that the experiences that people gain from microfinance operations and micro-entrepreneurial activities are more productive if they build relationships which are based on trust. In other words, people achieve more results if they collaborate in building networks with other people who share the same values and interests in running their enterprises. The central argument of social capital is that social networks have value. Social capital in this context refers to the collective value of social networks and the tendency that emerges from these networks to do things for each other, i.e. the norms of reciprocity. In practice, social capital is used as a form of intangible collateral for guaranteeing loans as an alternative to physical collateral required by commercial banks which poses the gravest barrier for the poor in accessing financial services. It is largely recognized that social capital is a much more effective tool for informal mechanisms to guarantee repayment and protect against risk because of the trust, reciprocity, information and cooperation that are associated with strong social ties. In this case, all members have a stake in the success of each member's enterprise in order to maintain their flow of access to credit and savings to grow their ventures. Social capital is also used as leverage for effective mobilization of savings as a form of repayment and asset accumulation. In a study comparing cooperatives in Anambra State, Seibel asserts that "Cooperative societies based on indigenous savings and credit associations are more effective in mobilizing personal savings in terms of all other economic indicators than cooperatives without such a basis (2004:5)."

The virtues of social capital translate into the Nigerian case studies as evidenced by the qualitative data from the interviews and questionnaires. In the Enugu study, the authors assert that the social stigma attached to not being creditworthy influences members to pay back and that the trust, social cohesion and mutual dependence inherent in social capital explain why informal microfinance overcomes the problems of commercial banking such as information asymmetry, transaction costs and moral hazard. The Ekiti State study also highlights the unique characteristics of informal microfinance that enable it to address the needs of the poor where formal institutions are incapable. It finds that "The economic, social and educational advantages to be derived from cooperation between individuals with limited resources are generally taken for granted" (Oloyede, 2008:48). From an interpretation of the data, the study asserts that cooperation in the form of social capital is vital to rural development through informal means that are best equipped to understand the needs of the rural communities. In the Imo State study, the recognition by respondents that their uptake of financial services through their membership in the Obazu Progressive Women's Association led to significant improvements in their standard of living rests on the strong social ties established through trust and longtime membership in the cooperative.

CONCLUSION

This paper sought to address the role of informal microfinance and cooperatives in the socioeconomic development of Nigeria. Through a review of secondary sources and case study analysis of experiences with informal financing in different parts of the country, a clear relationship was found between social capital and improvements in living standards. In all cases, the strong social ties and kinship networks between members of the community served as a source of effective usage of informal financial services and thereby established a positive relationship between members and providers for reliable and increasing flows of credit and savings. Moreover, the flexibility, convenience and familiarity of informal microfinance contributed to the uptake of services by the poor. Most importantly, by overcoming access barriers to financing and being able to leverage the mutual needs of

members, ROSCAs and other types of informal group mechanisms overcome the exclusionary aspects of formal microfinance and thereby more effectively serve the poorest of the poor.

Despite the strong association between social capital and effective use of microfinance in the case studies of Enugu, Imo and Ekiti states in Nigeria, it is difficult to ascertain the quantitative effect of informal microfinance on poverty alleviation and economic development throughout the country. However, it is evident from these cases that at least at an individual, family and community level, participation in informal cooperative microfinance schemes enhances the possibility of poor micro entrepreneurs to reap the spillover benefits of boosted incomes and asset building. It is also evident that most of Nigeria's poor, especially poor rural women, still lack access to formal microfinance due to collateral requirements and other access barriers. In this case, informal microfinance presents a viable and necessary alternative to inclusive financial services for the poor.

It is widely argued, however, that formal and informal microfinance are not mutually exclusive, but rather that they work side-by-side in their provision of financial services. Through the case study analysis, one can see how the inherent strengths of informal cooperatives present a model for microfinance banks to better address the needs of the poor. Indeed, Opata and Nweze (2009) suggest that "An impetus for the rethink is the increased recognition of the rural informal savings and credit associations especially informal women's cooperative micro finance institutions and their persistence and long term sustainability and how they could be linked to formal rural credit schemes (4)." Further research in this area would contribute to a more nuanced understanding of inclusive financial systems tailored to the diverse livelihoods of the poor.

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Chapter 5

THE ROLE OF INSURANCE IN MANAGING MICROFINANCE PROGRAM RISKS

Folorunso Moses **IKOMI**

INTRODUCTION

In order to survive in this very competitive new landscape and fast changing socio economic environments, businesses and banks in particular must learn to live with risks as risk taking is closely associated with profitability. This can be done by setting up an intelligent and professionally driven risk management system that will apply modern techniques in dealing with all the types of risks inherent in their business endeavours. It is a known fact that banking business all over the world is exposed to more risks than any other class of business. This is so because of the nature of their trade which deals with money market instruments.

Many of the microfinance institution (MFI) accept deposits directly or indirectly like commercial banks. As a result of the acceptance of deposits and granting of credits the MFIs are exposed to the risks associated with this type of trade, because MFIs give out loans without asset based collaterals. The above fact makes it very imperative for microfinance institutions to set up sound risk management techniques that will be very efficient in forestalling possible loan default. Considering the popularity of MFIs operations across nations, this paper examines different types of risks that exist in microfinance program and what the insurance companies can do to support the microfinance in order to mitigate the risks.

CONCEPTUAL FRAMEWORK

Otero and Rhyne (1994) defined microfinance as a revolution that involves the large scale provision of small loans and deposit service to low-income people by secure, conveniently located and completing commercial institutions thereby generating the process needed to democratize capital. This definition means that the numbers of microfinance institutions should be enough to meet the needs of low-income earners in the nation through the provision of loan facilities and to give room for healthy competition among them. The Central Bank of Nigeria - CBN - (2005) defined microfinance as the provision of financial services to the poor who are traditionally not served by the conventional financial institutions. The three features that distinguish microfinance from other formal financial products are: smallness of loan advanced and or savings collected, the absence of asset based collateral, and Simplicity of operations.

Asian Development Bank (2000) defined microfinance as the provision of a broad range of financial services such as deposits, loans, payment services, money transfer and insurance to

poor and low-income households and their micro enterprises. Ledgerwood (2000) described microfinance as an economic development approach intended to benefit low-income women and men. This definition implies that the purpose of microfinance is to reach the urban and rural areas with financial services that will empower them to create wealth without any discrepancy as to the sex of such individual. Ndiaye (2005) opined that access to improved financial services and access to more and better ways of turning savings into lump sums helps poor people from sliding deeper into poverty and also assist them in laying foundations for their desire to better their lots and that of their families.

According to ADB (2000), CBN (2005) and Oluyombo (2007), the distinguishing features of the operations of microfinance institutions from those of other financial institutions are that the loans granted to customers are very small, no asset based collateral is required before loans are granted, simple operational modus operandi, banking operations are taken beyond economic considerations to socio-cultural upliftment of the people, establishment of a good inter-personal relationship between the MFI and its customers because of the intimacy of operations procedure, and the provision of insurance policies to poor and low-income household and their micro enterprises.

Insurance

Scholars over the years have contended about what insurance is and whether its essential nature is transfer, pooling, or some combination of the two together. The process of attaching an insurance label in a legal context has not been an easy one. There are series of questions to be answered, such as: What constitute doing an insurance business? The legal meaning of insurance; what constitute insurance within the meaning of the law? Delimitation of insurance field and what is a contract of insurance? The above controversies notwithstanding, authors have tried to define insurance based on their understanding of the subject matter. Hensel (1987) defines insurance as a social device providing financial compensation for the effects of misfortune, the payment being made from the accumulated contribution of all parties participating in the scheme. A close look at this definition reveals four concepts: The insured - the person who gets the compensation, Premium - the amount paid by the insured into the accumulated fund, Insurer - the organisation that receives, accumulate and pays compensation and, Indemnity - this is the restoration of the insured into the “same position” he occupied immediately before the occurrence of the event insured against.

According to Mehr and Cammack (1976) in the book “Principles of Insurance”, an adequate definition of insurance must include either the accumulation of a fund or the transference of risk, but not necessary both. In addition, it must include a combination of a large number of separate, independent exposure units having the same interrelated group. They then proceeded to define insurance as a device for reducing risk by combining a sufficient number of exposure units to make their individual losses collectively predictable. The predictable loss is then shared proportionately by all units in the combination. This definition implies that uncertainty is reduced and that losses are shared. These are the important characteristics of insurance. Dickson (1980), defined insurance as a means whereby group of people facing similar risk can club together for protection against certain financial losses, each individual transfers his risk to the club by paying premium. Bickel Harupt (1983) defined insurance from five perspectives as follows.

Economics: from economic perspective, he defined insurance as reduction of uncertainty by transferring and accumulation of funds.

Legal: from legal perspective, he defined insurance as a transfer of risk through payment of premium by insured to insurers in a contract of indemmity.

Business: from business perspective he defined insurance as sharing of risk by transferring risk from individual and business organisations to a financial institution that specializes in risk management.

Social: from social perspective, he defined insurance as a collective bearing by all members of a group.

Mathematics: from mathematical perspective, he defined insurance as a means of predicting and distributing losses by actuarial estimate based on principles of probability.

In summary, insurance can simply be described as an agreement by which one party called the insurer agrees to make good by payment of compensation to another party called the insured should an event happens that causes the insured to suffer a financial loss.

Risk

Risk is a concept with several meanings depending on the context and the scientific discipline in which it is used. For people who use the term loosely, the concept of risk means exposure to adversity or danger. Mathematicians are interested in the behavior of phenomena and define risk as a degree of dispersion of values in a random chance pattern. The larger the degree of dispersion, the greater is the risk. Herald Crener, a pioneer in risk theory in his book on the Mathematical Theory of Risk (1930) explains that the object of the theory of risk is to give a mathematical analysis on the random fluctuation in an insurance business and to discuss the various means of protection against their inconvenient effects. Herald Crener's (1930) explanation can be extended to the banking industry and in particular to microfinance institutions and it will read thus; "The object of the theory of risks in a microfinance institution is to give a mathematical analysis of the random fluctuation in the microfinance institution and to discuss the various means of protection against their inconvenient effects". The above definition is also collaborated by that given by Home (1983) which defined risk as the probability that the actual return will deviate from that which was expected. Kalaitzanakes and Valdivia (1996) defined risk as the chance of loss or the loss itself. Microfinance institution been an enterprise is subject to all the risks that affect any enterprise. However, the effects of those risks vary from enterprise to enterprise depending on their peculiarities. For example, the effect of risk on microfinance institutions will differ from those of commercial banks because of their mode of operations.

RISK FACTORS OF MICROFINANCE INSTITUTIONS

According to Oluyombo and Olasbisi (2008), the factors responsible for the difference in risk between microfinance institutions and conventional banks are as stated below:

i. MFI services and products are designed for the poor and low-income earners in the society.

ii. Most clients of MFI do not have physical assets (house, land, automobile, plant and machinery) and financial assets (shares, bond, stock and debenture certificates) to pledge as collateral for loans and advances collected.
iii. There is no supportive regulatory and supervisory policy framework on the part of some government which lead to physical and economic challenges for MFIs.
iv. Where regulatory framework exits, the peculiarity of MFI business in most cases is not taken into consideration in such country. MFIs and other banks are regulated under the same policy.
v. The ownership structure of MFIs is dominated by donors. In Nigeria however, MFI are dominated by private ownership.

It is pertinent to examine the nature of risk inherent in microfinance business. Berenbach and Churchill (1997) and Ledgerwood (2000) identified four main areas of risk that are peculiar to MFI as portfolio risk, ownership and government risk, management risk and new industry risk. Adewunmi (2005) on the other hand recognized risks such as credit risk, operational risks, interest rate and liquidity risk as those affecting financial institutions Oluyombo and Olabisi (2008) held the view that liquidity risk, credit risk, foreign exchange risk, ownership return risk and operational risk are the five major risks affecting the operation of MFIs. According to Aroy (2001), there are four categories of risks namely hazard risk, financial risk, operational risk and strategic risk. These risks affect all businesses irrespective of their stock in trade.

Hazard Risks

These are the risks that have traditionally been addressed by insurers. They include fire, thief, windstorm, liability business interruption, pollution, health and pensions. All businesses have fixed and moveable assets that should be insured against fire, theft and/or windstorm. Also, all businesses are subject to some form of liability especially public liability which should be insured. Pollution risk may however not applicable to MFI but it could affect their creditors in the production industry. Business interruption can apply to some clients of MFI in the manufacturing and product business. Health and pension are applicable to the personels of MFI.

Financial Risks

Financial risks cover potential losses due to changes in financial markets, industry interest rates, foreign exchange rates, commodity prices, liquidity risks and credit risk. Financial risks became an important source of uncertainty for firms for two major reasons. In the 1970s, the refusal of the major developed countries to continue with the Bretton woods agreement which had kept foreign exchange stable for three decades and the agreement by Organisation of Petroleum Exporting Country (OPEC) to reduce production to raise prices led to instability in foreign exchange rates and high inflation rates in developed countries. During the later part of the same decade, a policy shift by the U.S Federal Reserve to focus on fighting inflation as a result of the increases in oil price had a negative result. Instead of stabilizing interest rate, it led to a rapid rise and increasing volatility of interest rates in the United State and had a spill over effects in other nations as well. Thus, volatility in foreign exchange rates, prices and interest rates caused financial risk to become an important concern to institutions

Unlike foreign exchange, interest rate and commodity price, liquidity risk is defined as the inability of MFI to meet its financial obligation to its customers as a result of short fall in the value of cash at hand. The situation can arise in the under listed ways:

a. Where MFI gets funds from mandatory legal deposit from banks and government at various levels. A change in government or government policy can affect such MFI that depend upon this type of deposit for their funding. For example the Central Bank of Nigeria (CBN) encourages each state government to dedicate not less than 10% of the annual budget for such purpose.

b. Liquidity problem can also arise when funds given by donors are recalled for whatever reasons. This type of situation makes MFI to be uncapable to meet its financial obligation to its customers.

Credit risk is a child of default. Some debtors are unable and/or unwilling to make repayment of the loans granted them for a wide varieties of reason such as adverse trading experience, loss of property to fire, windstorm, thief and other natural or man-made disasters, death or disability leading to non-continuity of trade or business, and death or inability of guarantors to meet the financial obligation when a default has arises. The implication of such situation is that the MFI will receive less funds than projected for and this can lead to liquidity problem. According to Oluyombo and Olabisi (2008) credit risk is not limited to unpaid loans and advances alone but can be extended to those loans applications that were turn down by MFI because they may hinder the growth of the lender and cause reduction in earning and profitability of the MFI.

Operational Risks

Adewummi (2005) defined operational risks as the risk of loss resulting from inadequate or failed normal process, people and system or from external events which is in agreement with that given by the enterprise risk management. However, Oluyombo and Olabisi (2008) identified operational risks in MFI as having to do with employees who work in such organisations. They further stated that in most nations, bank employees earn more than many other sectors of the economy and if the employees of MFI see themselves as bankers and with this mind set, it may create disorder and operational breakdown. It is expected that the above will lead to agitation for better welfare package and may tend towards unionism. Operational risks cover wide variety of situation including customer satisfaction, product development, product failure, trademark protection, corporate leadership, information technology, management fraud and information risk. All the risks aforementioned under operational risk are relevant to MFI operations except perhaps trademark protection.

Customer satisfaction has to do with service delivery and the attitude of MFI employees towards their customers. An efficient service delivery mechanism, if put in place by MFI and their staff on their part, are able to establish good interpersonal relationship with the clients will lead to customers' satisfaction. Anything to the contrary will certainly have negative effects on the overall performance of the MFI product development is necessitated to the changing socio-economic situations at most economies. Any institution including the MFI that are unable to develop products that will meet the realities of the day will certainly find itself going out of business. There is therefore need than ever before for MFI to continually design products that will be able to meet the current demand of their clients if they are to

remain in business. Products failure is a direct consequence of faulty designs and wrong audience. If the design of a product is faulty, it will not be able to meet the purpose for which it was made and therefore lead to dissatisfaction. On the other hand, if the product is sold to the wrong audience, the outcome is also the same. Dissatisfaction will arise and consequently product failure. Information risk involves divulging official secret to wrong set of people who may take advantage of such information and work against the progress of the institution. There is need to treat this type of risk with the greatest caution as information is vital for the healthy operations of any MFI.

Strategic Risks

Strategic risks include competition, customer preferences, technological innovation and regulatory or political impediments. Customers are always given the freedom to make choices as to what product they prefer. Preferences are influenced by socio-economic changes, product design, marketing, and Advertisement and research. Once a product is able to meet the needs of the society, they in turn will of necessity prefer such product.

Technological innovation involves the development of new technology which makes the old ones obsolete and due for replacement. Any MFI using old technology is bound to have some serious drawback in its service delivery mechanism. This will adversely affect the rating and preference the microfinance product. The enactment of wrong regulatory or political policy can make or mare the operations of MFIs. For example, if a government decides to close her doors to external donors, this will adversely affect the MFI that have been operating on donor's funds. Regulatory or political policies can create the right or wrong environment for MFI to strive.

RISK MANAGEMENT

Risk management has been practiced for several years. Early lenders must have quickly learned to reduce the risk of loan defaults by limiting the amount loaned to any individual and by restricting loan to those considered most likely to repay their loans. Mehr and Hedges (1963) were widely acclaimed the fathers of risk management. They enumerated the following steps as being necessary for risk management process: Identify loss exposures, Measure loss, Evaluate the different methods for handling risk which include; Risk assumption; Risk transfer; Risk reduction, Selection of the appropriate method to use, and Monitoring results. Mehr (1977) in his book "Life Insurance Theory and Practice" defined risk management as an efficient pre-loss arrangement for an effective post-loss balance between available and needed resources. Baffa (1990) defined risk management as the planning and controlling of all the conceivable elements of risks which are inherent in operations of an organisation in order to ensure the organisation's continued existence as well as the realization of its set goals and objectives. Meyer (2000) opined that in managing risk, banks must decide which risks to take, which to transfer and which to avoid. The above opinion also applies to MFI who gives out loans without any asset based collaterals.

The traditional risk manager dealt with only pure or static risks while speculative or dynamic risks were ignored. This development was not surprising because those who pioneered risk management either taught or worked in the insurance industry, so that the focus was on risk which insurers would be willing to underwrite. Another reason is that in many cases, these represented the most serious short term threats to the financial position of an organisation at

that time this field was founded. Finally, there were simply not a lot of reasons or options for dealing with financial risks such as interest rate changes, foreign exchange rate movement or equity market fluctuations when the field was first developed.

During the emergence of the risk management as a field of study, interest rates were stable, foreign exchange rates were internationally maintained within narrow bands and inflation were at yet a concern to most organisations. Financial risks were not a major issue for businesses. The field of finance was primarily institutional at that time. Although Markowitz had proposed portfolio theory (Markowitz, 1952), but the Capital Asset Pricing Model had not yet been developed. The mathematics for qualifying financial risks were not sufficient to put these risks in the same framework as pure risks. The primary risks at the time were hazard risks, the risk of fire, windstorm or other properly damage or liability. Environmental risks were still in their infancy. With the ever turbulent socio-economic environment, other forms of risks such as operational risks and strategic risks were identified. This led to the evolution that took place in the field of risk management which eventually brought about the birth of Enterprise Risk Management. Precursors to this term are corporate risk management, business risk management, holistic risk management, strategic risk management and Integrated risk management.

The Casualty Actuarial Society(CAS) (2001) defined Enterprise Risk Management as “the process by which organisation in all industries assesses, control, exploit, finance, and monitor risks from all sources for the purpose of increasing the organisational short and long term values to the stakeholders”. The CAS enumerated the type of risks subject to Enterprise Risk Management as hazard, financial, operational and strategic risks. The compositions of the various classes have been given in the previous section.

ROLE OF INSURANCE IN MICROFINANCE INSTITUTIONS

The provision of insurance for the poor and low-income households and their micro enterprises is an essential part of the services to be rendered by the microfinance institutions. In enumerating the roles insurance can play in the management of risks in microfinance institution, a distinction between the microfinance institution and its clients will be drawn.

All MFI have fixed and moveable assets such as buildings, furniture, fittings and vehicles etc. that are subject to hazard risks. The type of assets can be insured adopting the approach of a traditional risk manager. Since the recognition of financial risks in the 1970s the tools used in managing them include forwards futures, options and swaps. These techniques were not developed by the traditional risks mangers who have set very high standards for managing hazard risks. Although these techniques followed similar fashion like those developed by traditional risk managers, they cannot be classified as insurance contract. However, insurance could be of help in the area of credit risk management by insuring the lives of their clients against premature death before the expiration of the loan granted. The MFI becomes the beneficiary of the contract. Premiums should be paid by the clients along with his/her periodic repayment of loan. Considering the value of the loans granted, their repayment period is always less than one year. As a result of the above, a yearly renewable group term assurance will be very appropriate for this purpose.

Of all the risks covered by operational risks, management fraud can be managed via insurance contract in addition to other internal control mechanism that should be put in place. Fidelity guarantee by MFI to cover all staff involved in handling cash or granting of loans. The amount fraudulently removed by any covered staff will be paid by the insurance company while the insurers recover their financial outlay from the guarantee of the staff involved.

The clients of MFI are either in the retail trading business or in the manufacturing business. For those in the retail business, goods are moved from the point of purchase to the selling point and they can be involved in accidents or theft. A group of goods in transit policy can be taken on each cooperative unit within the spectrum of clients. At the point of sales, hazards such as fire windstorm, flood, theft e.tc. can occur and should be insured. If this step is not taken, it can lead to default in loan repayment should these events listed above happen. As aforementioned in the MFI insurance needs, the clients should obtain life insurance policy to cover premature death which is one of the reasons for loan default.

Those clients involved in manufacturing need to cover their business against, public liability, product failure, business interruption, workmen compensation, goods-in-transit and life insurance for themselves. These covers can take the form of a group cover for similar businesses within the same geographical location. All Premium payable should be built into the periodic repayment to be made by the clients. Those policies will not only guarantee loan repayment but the continuity of such businesses should the clients be involved in any of the hazards listed above. MFIs should also take workmen compensation policy to cover their staff for any injury sustained while on duty.

CONCLUSION

From the preceding section, it is apparent that insurance can be a very useful device in managing risks associated with the microfinance institution business. As already stated, all hazards risks could be handled using the traditional risks managers method. Some aspect of the financial risks and operational risks could adopt insurance policies in their management. So far in the operations of MFI in Nigeria, the provision of insurance policies as contained in the definition provided by the Asian Development Bank (2005) is yet to be embraced. It is the belief of the author that the adoption or provision of insurance policies for the clients of MFIs will be of immense assistance to both MFIs and their clients in ensuring the progress and continuity of the businesses of both parties.

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Chapter 6

REGULATION AND SUPERVISION OF MICROFINANCE INSTITUTIONS: AN EXAMPLE OF COOPERATIVE CREDIT SOCIETY

Mathurin **FOUNANOU**
Zaka **RATSIMALAHELO**

INTRODUCTION

Microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers, and insurance to poor and low-income households and, their microenterprises. Microfinance institutions now reach well over 100 million clients and achieve impressive repayment rates on loan (Cull, Demirgüç-kunt and Morduch, 2009a). Microfinance services are provided by three types of sources: formal institutions, such as rural banks and cooperatives; semiformal institutions, such as non-governmental organisations; and informal sources such as money lenders and shopkeepers. Microfinance institutions are defined as institutions whose major business is the provision of microfinance services. (Institutional microfinance is defined to include microfinance services provided by both formal and semiformal institutions).

The interest in microfinance has burgeoned during the last three decades: multilateral lending agencies, bilateral donor agencies, developing and developed country governments, and nongovernment organisations all support the development of microfinance. A variety of private banking institutions have also joined this group in recent years. As a result, microfinance services have grown rapidly during the last decade, although from an initially low level, and have come to the forefront of development discussions concerning poverty reduction. The rapid growth of microfinance has brought increasing calls for regulation, but complying with prudential regulations and the associated supervision can be especially costly for microfinance institutions (Cull, Demirgüç-kunt and Morduch, 2009b). Christen, Lyman, and Rosenberg (2003) speculate that compliance with prudential regulations could cost a microfinance institution five percent of assets in the first year and 1 percent or more thereafter.

In discussing tradeoffs in regulation of microfinance, Christen, Lyman, and Rosenberg (2003) draw an important distinction between prudential and non-prudential regulation. According to their definition, regulation is prudential when "it is aimed specifically at protecting the financial system as a whole as well as protecting the safety of small deposits in individual institutions". The assets of microfinance institutions remain substantially less than those of formal providers of financial services, most notably banks, and thus they do not yet pose a risk to the stability of the overall financial system in most countries. However, an increasing

share of microfinance institutions take deposits from the public, and many of the depositors are relatively poor. Protecting the safety of those deposits provides a rationale for improved regulation and supervision of microfinance institutions. We investigate the role of prudential regulation on the profitability and self-sustainability of credit cooperatives. Credit cooperatives as formal financial institutions originated in nineteenth century Germany. These associations operate democratically; each member has one vote. Leadership is voluntary and unpaid, although professionals may be hired for day-to-day operations. Members contribute equity in the form of an initiation fee and regular capital contributions. The amount a member can borrow is based on his or her capital contributions. Profits are distributed to members in the form of dividends based on their equity contribution or retained to increase the organisation's capital. This ensures that benefits go to members rather than to external intermediaries and their shareholders.

Cuevas and Fischer (2006) observe that "lack of knowledge of cooperative financial institutions governance, regulation and supervision has been a recurrent obstacle in development finance, resulting in widespread neglect of the cooperative financial institutions sector in spite of its pervasiveness and potential". In addition, there are topics related to organisation, governance, legislation, regulation and supervision of cooperative financial institutions over which there is no agreement but over which one is needed if we are to facilitate the growth of these institutions and realize their potential for serving the poor. The issues refer to fundamental questions such as: what are the main strengths and weaknesses of cooperative financial institutions, what is the role of the legal framework in doing this, should the legal framework be a specialized one covering uniformly all cooperative financial institutions or should the system be tiered, should cooperative financial institutions fall under banking authority supervision? Most agree that yes, it should - but then how? Direct, delegated or auxiliary supervision, see Cuevas and Fischer (2006). What are differences between these schemas, and the effects they have on performance of cooperative financial institutions?

Delegated monitoring is probably the hottest point of the debate and disagreements on regulation and supervision of cooperative financial Institutions (CFIs). The argument that regulation and supervision in microfinance are less important because of its small economic role misjudges the exceptional sensibility of this segment and its possible contribution to financial systems development. Banks and other financial intermediaries are major players in modern economies by exerting a strong influence on risk sharing, capital allocation and economic growth. This important role in the economy stresses the need to safeguard the stability and soundness of the financial system. Recent financial crises in many countries have triggered renewed interest in the structure and conduct of banking regulation. The existence, type and scope of banking and prudential supervision have become topical issues and main subjects of intense academic and policy debates. The regulation and supervision of Microfinace Institutions (MFIs) should be subsumed in the overriding goal of developing a market-based financial system (Staschen, 1999). Target group demand is not limited to borrowing; it also includes other financial services such as savings, insurance, transfer facilities, etc. Savings facilities are a particularly important question when considering a prudential regulation of MFIs. The prospective target group is many times larger in deposit business than in lending (Staschen, 1999). Where the poor have no access to savings facilities MFIs should also take up deposit business. Another reason for regulating this sector is that MFIs'available funds cannot keep pace with their lending business. To reach as many

prospective borrowers as possible, MFIs also need to have access to external finance in addition to their own resources and finance from donors.

There are three typical regulatory approaches to Microfinance institutions sector (see e.g. Staschen (1999), and Berenbach and Churchill (1997) for a similar classification): the regulation of MFIs by existing banking legislation, regulation by a special MFI law and self-regulation. Statutory regulation and self-regulation differ as to who lays down the rules and how they are stipulated. In government regulation this is the task of the legislator or subordinate administrative agencies. The distinction in statutory regulation between regulation by banking law and by a special MFI law is not a methodological necessity, but it is very helpful to give existing regulatory approaches a structure. In self-regulation the institution to be regulated set their standards themselves, not each on its own (this would be internal self-regulation), but as a group (e.g. through an association), and these are equally binding on all. Self-regulation and statutory regulation are the two extremes demarcating a continuum of regulatory methods. Pure self-regulation (i.e. without any government influence), is rare. More frequent is indirect influence through government bodies (e.g. via state licensing of regulatory institutions. This approach is also termed: indirect supervision or delegated monitoring.

Indirect supervision is a regulatory regime that is unique to cooperative financial institutions (CFIs). In this regime an agent (the delegated or auxiliary supervisor) performs certain tasks associated the supervisory function on behalf of the state authority (the principal supervisor). The agent may be (and usually is) a body specially setup by the network of CFI, but could potentially be any other independent party like an auditing firm or a rating agency. The ultimate responsibility of the functioning of the regime rests squarely with the principal supervisor, and no indirect supervision regime should be expected to work without a commitment of the later to make it work. This is government regulation with delegation of supervisory tasks to a private institution CGAP (2003). Historically this regime grows from the experiences in Germany (and then Europe), starting in the second half of the XIX century, throughout modern times, where it is still the dominant supervision regime.

There is no theoretical or empirical work from which we can draw clear guidelines. The little theoretical work that touches tangentially on the subject provides only arguments why these kinds of arrangements might work. On the empirical side, although there is vast experience out there of the successes and failures of systems that work with and without delegated/ auxiliary monitoring, this information has not been processed in an orderly fashion allowing drawing inference. We are reduced to the fact that there are systems of CFIs that employ the approach and work well. The same can be said of systems operating under direct supervision. Auxiliary/delegated monitoring is also employed in other networks such as those of savings and loans banks (German, Scandinavian countries, and Spain for many years before switching to a direct supervision schema), insurance (Quebec) and health insurance (France, Belgium). Microfinance institutions (MFIs) can be classified into three rough categories depending on the structure of the liabilities side of their balance sheets. This classification is given by Van Greuning, Gallardo and Randhawa (1999). First category comprises all MFIs which depend on other people's money to finance their lending business. These MFIs are described as credit-only institutions and they include financial NGOs. In the second category, member's deposits are used to grant loans exclusively to members. Classic examples of this are saving and credit cooperative and/or credit unions. The latter category comprises all MFIs that use the public's money to finance their lending business. These do not include financial

institutions that employ forced savings components to secure their lending transactions, however, as long as their clients are net borrowers.

Another type are formal banks with a microfinance window. The regulations of banking legislation automatically apply to their microfinance portfolio, but these are usually poorly adapted to the requirements in this area. This problem has not yet been solved. Each institutional type stands out for an idiosyncratic risk of its own, which has a bearing on the best regulatory framework to choose. Cooperative financial institutions, albeit highly pervasive in most countries, are among the poorly understood entities that comprise the existing institutional base for financial intermediation. CFIs include diverse member-owned financial intermediaries' referred to as credit unions, savings and credit cooperatives, cooperative banks, and other terms that differ across regions of the world. For example, Savings and Cooperatives in East Africa; "Caisses populaires or Caisses d'épargne et de crédit" in West and Central Africa; "Cooperativas de ahorro y crédito" or "Cajas de ahorro y crédito" in Latin A merica; credit unions in the UK, USA and parts of Canada (see, Cuevas and Fischer, 2006). Their institutional structure and governance, legal and regulatory status, and scale and services portfolio also vary widely across regions and especially between industrialized countries and developing economies. A most basic common denominator is that they collect deposits and do business often solely with members (see Cuevas and Fischer (2006)). CFIs serve many poor people, even though middle-income clients are also among their membership, a feature that in fact allows CFIs to reach poor segments of the population without necessarily compromising their sustainability.

In deposit business there is an asymmetric distribution of information available to the depositors on the one hand and the financial institutions on the other. The focus of this is on the debate associated with indirect supervision, i.e., delegated and auxiliary supervision mechanisms. We examine the role of prudential supervision and information disclosure as a regulatory instrument, and analysis its effects on performance of CFIs concerning incentives and effort. Here, information disclosure refers to the optimal monitoring scheme by the supervising agency taking into account all costs and benefits of such a scheme.

PREVIOUS LITERATURE

Previous research on microfinance regulation and prudential supervision focuses on the relationship between financial performance and regulation, treating outreach as a secondary concern (see Cull, Demirgüç-kunt, and Morduch, 2009b). Ndambu (2011) and many others have analyzed the impact of regulation on financial intermediaries (including MFIs) worldwide, deriving potential implications of microfinance supervision in a consistent manner and moving one step beyond countries' anecdotal evidence. Hartarska (2005) finds that regulated microfinance institutions in Central and Eastern Europe and the Newly Independent States have lower return on assets relative to others, and weak evidence that the breadth of outreach may be related to regulation. After controlling for the endogeneity of regulation, Hartarska and Nadolnyak (2007) have conducted a research using a positive approach to assess if regulated MFIs achieve better sustainability and outreach than unregulated MFIs. They find that regulation has no impact on financial performance and weak evidence that regulated microfinance institutions serve less poor borrowers. As a policy implication, they concluded that MFIs' transformation into regulated financial intermediaries might not lead to improved financial results and outreach. However, they fund institutions

collecting savings reaching more borrowers, thus suggesting that regulation might have an indirect benefit if it is the only way allowing MFIs to collect deposits from the public.

Cull, Demirgüc-kunt and Morduch (2009b) examine the implications for the institutions' profitability and their outreach to small scale borrowers and women. The tests draw on a new database that combines high-quality financial data on 245 of the world's largest microfinance institutions with newly-constructed data on their prudential supervision. Ordinary least squares regressions show that supervision is negatively associated with profitability. Controlling for the non-random assignment of supervision via treatment effects and instrumental variables regressions, the analysis finds that supervision is associated with substantially larger average loan sizes and less lending to women than in ordinary least squares regressions, although it is not significantly associated with profitability. The pattern is consistent with the notion that profit-oriented microfinance institutions absorb the cost of supervision by curtailing outreach to market segments that tend to be more costly. By contrast, microfinance institutions that rely on non-commercial sources of funding, are thus less profit-oriented, do not adjust loan sizes or lend less to women when supervised, but their profitability is significantly reduced. Ndambu (2011) discusses the potential impact of regulatory on microfinance in Sub-Saharan Africa using cross section data from the mix market of 192 microfinance institutions from 32 different countries. The results do not show sufficient evidence that the regulatory status increases the sustainability of MFIs nor does the deposit intermediation. However, after controlling for the regulatory capacity, there is clear evidence that countries with a high Official Supervision Power have more sustainable MFIs and it is only after integrating the Official Supervision Power in the model that the deposit intermediation coefficient becomes significant and positively associated with the Operational Self sufficiency. Though these results are intuitive from an economic perspective, it remains an open question whether the benefits of supervision in terms of better protection of depositors' funds and improved stability in the MFI sector outweigh the reductions in outreach.

This study considers the optimal regulation of a single bank that has private information on the intrinsic quality of its loan portfolio. The credit cooperative is able to raise its total quality above its intrinsic quality by exerting costly managerial effort. Higher overall quality enhances the distribution of returns on the bank's loan portfolio and therefore its expected profits. However, the choice of effort is unobservable to the regulator and cannot be verified. So, in this setting the regulator faces adverse selection and moral hazard which has important consequences for designing the optimal contract. A similar approach is taken in for example Giammarino, Lewis, and Sappington (1993) and Rochet (1992). Our study extends Giammarino, Lewis and Sappington's focus on incentive compatibility requirements by analyzing the regulator's concern for social welfare. The regulator offers the bank a menu of contracts from which the cooperative chooses depending on its characteristics and on the profit sharing scheme between the regulator and the cooperative. In this way contracts are not rigidly imposed on all banks, but induce self-selection by cooperatives through incentive compatibility.

Information asymmetry due to the bank's private information about its costs of operation (selection adverse) and about hidden actions that managers of bank (moral hazard) induce a loss of control for the regulator and limit the effectiveness of its regulatory policy. This loss of control may be mitigated by collecting bank specific information, creating the need for active prudential supervision. Supervising agency acting on behalf of the regulator may be

able to resolve the information asymmetry between the regulator and the bank, depending on its competence and ability to gather information. We assume that the supervisor retrieves a signal imperfectly correlated with the bank's intrinsic quality and that it is able to improve this signal at certain costs. These costs reflect on the one hand the direct costs of devoting more resources to the supervisory task, but on the other hand also the costs attached to increased public concern about the soundness of the inspected bank, when the disclosed information turns out to be bad. In the event that the bank's management is caught shirking, the regulator may react by imposing a punishment to correct this undesired behaviour. The regulator must optimally weigh the costs and benefits of an active prudential supervision policy, which defines an optimal monitoring scheme. The purpose of this paper is to characterize the optimal contracts offered by the regulator to the credit cooperatives. It is shown that these contracts depend on the accuracy of the supervisor's signal, the likelihood of facing a high quality financial intermediary, and the cost of supervision.

THE MODEL

Our analysis sets out from the viewpoint that members of the cooperative credit society need to be protected and represented by a regulator. To protect the interest of members, cooperative societies are placed under state control through registration. While getting registered, a society has to submit details about the members and the business it is to undertake. It has to maintain books of accounts, which are to be audited by government auditors. We consider a regulator-cooperative society two-player hierarchy as a stylized model of a regulated microfinance sector, where the state authority (the principal supervisor) may require the help of a supervising agent (the delegated or auxiliary supervisor) to collect information. The model heavily builds on Giammarino, Lewis and Sappington (1993), Laffont and Tirole (1993) and Dewatripont and Tirole (1994). In Giammarino, Lewis and Sappington (1993), the bank retains its own profits, and the regulator is modelled as presenting a menu of options to the bank, these options linked to the required capital structure depending on the bank's type. Our designed incentive contracts are so to say the "monetary equivalent" of these options.

The specific details of our model are as follows. There are four classes of risk-neutral players: (1) members/depositors that seek loans to finance projects, (2) cooperative credit society that provide intermediation services, (3) an auxiliary supervisor performing certain tasks associated to the supervisory function on behalf of the state authority, and (4) a regulator (the principal supervisor) who is required to insure deposits issued by the cooperative credit society.

The regulation environment is such that the principal supervisor is the residual claimant of the imposed (vertical) hierarchical structure. Every cooperative society in addition to providing services to its member also generates some profits while conducting business. Profits are not earned at the cost of its members. Profit generated is distributed to its members not on the basis of the shares held by the members (like the company form of business), but on the basis of members participation in the business of society. In our model, regulation and supervision of cooperative financial institutions refers to the extent of profit sharing between the regulator, members and cooperative society. In particular, it is assumed that the regulator captures all the profits of the cooperative and compensates the cooperative's management for its exerted effort by offering a contract which specifies a monetary transfer from the regulator to the cooperative society. The cooperative credit society employs the deposits they receive to

finance projects promising a random return, depending on the overall quality of the cooperative's loan portfolio. The cooperative society is able to enhance this overall quality of its loan portfolio by exerting costly effort. The regulator does not know the cooperative society's exact type in terms of the exogenously given intrinsic quality nor observes its exerted effort. We now turn to each player in more detail.

The Players

Members/Depositors

We assume that each member has access to an investment project. The member is unable to finance the project alone and thus requires an outside source of funding. For simplicity, we assume that cooperative credit society is the only source of funds. Although each investment project requires the same amount of funding from the cooperative credit society, projects differ in their expected returns. We denote by R the average rate of return on all projects financed by the cooperative credit society. If the cooperative society lends a total of L to members who collectively generate an average return of R, the cooperative credit society earns an overall return of RL.

The Cooperative Credit Society

The cooperative credit societies are formed to provide financial support to the members. The society accepts deposits from members and grants them loans at reasonable rates of interest in times of need. Village Service Cooperative Society and Urban Cooperative Bank are examples of cooperative credit society. At the beginning of the period $t = 0$ initial deposits D are used to finance loans L, normalizing $L = D$. In a cooperative society capital is contributed by all the members. However, it can easily raise loans and secure grants from government after its registration.

The cooperative society owns no equity. Cooperative is not formed to maximize profit like other forms of business organisation. The main purpose of a cooperative society is to provide service to its members. The cooperative credit society offers a standard debt contract to its members at a reasonable price by retaining a small margin of profit. The cooperative credit society offers an interest rate r to depositors at maturity at $t = 1$. Deposits are not insured and pay zero before maturity. The investment provides an average gross return of RL . The net return on the loans is influenced by the operating economies achieved by the cooperative credit society. We denote by $C(L)$, an increasing, strictly convex function, the cost of processing L of risky loans. Hence the net return on risky loans is $RL - C(L)$. The average gross rate of return R on the loans is random, but its distribution depends on the overall quality q of the loan portfolio. More precisely, higher levels of q shift the distribution of returns in the sense of either first-order stochastic dominance (i.e., reduce the likelihood of low returns) or second-order stochastic dominance (i.e., reduce the variance of returns).

Formally, it is assumed that R is modeled as a random variable with smooth distribution function $G(R/q)$. Technically, we assume the underlying density function has positive support on $\left[\underline{R}, \overline{R}\right]$ and: The overall quality of cooperative credit society's loan portfolio consists of an exogenous and endogenous part. For simplicity, we assume: $q = q_0 + e$, where

q_0 denotes intrinsic quality (exogenous) and e denotes (endogenous) effort exerted by the cooperative's management. We assume the cooperative credit society knows the exact level of intrinsic quality, while the regulator views intrinsic quality as a random variable on the interval $\left[\underline{q}, \overline{q}\right]$ with density function $f(q_0)$. And let $F(q_0)$ be the corresponding distribution function, with $\frac{d}{dq_0}\left(\frac{1-F(q_0)}{f(q_0)}\right) \leq 0, \forall q_0 \in [\underline{q}, \overline{q}]$.

The cooperative credit society is able to raise its overall quality above its intrinsic quality by exerting managerial effort e which is costly. We assume that the cooperative management's disutility is given by $\psi(e)$. The reduction in disutility by lowering effort may represent either the manager's valuation for a low-pressure job of selecting loans or the private benefit received by distributing loans among friends rather than to the best borrowers. A central feature of our model is the cooperative credit society's private information about its influence on the return it receives from the risky projects it finances. The information asymmetry in this model concerns that neither the exact type of the cooperative q_0 nor the exerted effort e is observable to the regulator, but only known to the cooperative. The expected gross profits on its loan portfolio of a cooperative society are given by:

$$\pi(q_0) = \int_{R}^{\overline{R}} [RL(q_0) - C(L(q_0)) - L(q_0)]g(R/q)dR \qquad (1)$$

Note that negative gross profits induce default (bankruptcy) since it is assumed that the cooperative society has no own equity. The probability of cooperative society failure as a function of effort is given by

$$p(e) = \int_{\underline{R}}^{R} g(R/q(q_0)dR.$$

Finally, realized profits at $t=1$ directly accrue to the regulator. In return the cooperative is compensated for its effort by means of a monetary transfer T. The cooperative societies expected utility U_C amounts to:

$$U_C = T - \psi(e) - P \qquad (2)$$

this can be written by

$$U_C(q_0) = T(q_0) - \psi(q - q_0) - P(q_0) \quad (3)$$

Where P denotes the possible punishment imposed on the cooperative society's management by the regulator, whenever suspected of shirking. However, the penalty imposed cannot exceed the net transfer, reflecting the limited liability of the cooperative society's management. We impose $P(q_0) \leq T(q_0)$.

The Delegated Monitoring and Auxiliary Supervision

Generally it is seen that, cooperative society does not function efficiently due to lack of managerial talent. The members or their elected representatives are not experienced enough to manage the cooperative society. In our regulatory game the supervisor has the ability to detect false reports of the cooperative society management. In this sense it may prevent the cooperative from shirking since the cooperative faces a penalty if caught lying. Consequently, the costs of regulation may drop and better incentives for low quality cooperative societies may result. Obviously much depend on the supervisor's accuracy to detect shirking behavior. Moreover, it is assumed that the regulator is unable to perform the supervisory task itself. Indirect supervision is a regulatory regime that is unique to cooperative financial institutions. In this regime an agent (the delegated or auxiliary supervisor) performs certain tasks associated to the supervisory function on behalf of the state authority (the principal supervisor). This could well be the case because supervision comprise of complex monitoring and auditing activities which require specific skills. Like the regulator the supervisor is uninformed about the cooperative society's true type q_0, but receives a signal θ which is imperfectly correlated with the cooperative society's exerted effort.

The supervisor reports a signal $\theta \in \{q_0, \emptyset\}$ to the regulator. With probability μ the supervisor finds out the true q_0 and with probability $1-\mu$ it finds no new information. This probability μ reflects the signal's precision or accuracy. The supervisor may improve its accuracy, but only by incurring costs. It is assumed that these costs are increasing and convex in μ,

$$\gamma(\mu) = \frac{\mu^2}{2}. \quad (4)$$

The Cooperative Regulator

The inadequacy of capital and various other limitations make cooperative societies dependant on the government for support and patronage in terms of grants, loans subsidies, etc. Due to this, the government sometimes directly interferes in the management of the society and also audits their annual accounts. The regulator's task is to provide deposit insurance while maximizing social welfare. It captures all profits from the cooperative society and designs the contract which it offers to the cooperative's management to compensate for the exerted effort. The contract specifies a monetary transfer T from the regulator to the cooperative, to which the regulator is irrevocably committed to pay just after the returns on the loans materialize at $t=1$. The critical information asymmetry in our model centers on the costs of enhancing the quality of the cooperative credit society's loan portfolio. The functional form of $\psi(e)$ and the relationship between quality and the cooperative society's' efforts ($q = q_0 + e$) are common knowledge. The regulator cannot observe the realization of q_0 nor can the regulator monitor the level of discretionary resources that the manager devotes to quality enhancement. The informational asymmetry implies that no written contract can be contingent on effort directly, but instead must be geared to observable realized total quality of the loan portfolio q.

Without loss of generality, we model the regulator as presenting a menu of linked options $\{q(.), T(.), L(.), P(.)\}$ to the cooperative credit society. The cooperative society is permitted to choose one of these options after observing the environment in which it is operating. Nature

chooses the cooperative's type q_0. The cooperative society learns its type. We will denote by $\{q(q_0), T(q_0), L(q_0), P(q_0)\}$ the particular contract that the cooperative will select in equilibrium when q_0 is the realized level of its intrinsic quality. After announcing the contract it has selected, the cooperative society raises the required amount of issues deposits. The funds raised are used to make loans. The cooperative society chooses effort e which determines total quality of the loan portfolio. The supervisor monitors this procedure and prevents the cooperative from operating if the specified quality level is not achieved. If the quality level is achieved, the cooperative remains in operation until $t = 1$. The cost of government involvement in the regulation and supervision of cooperative financial institutions is captured by the assumption that the social cost of public funds used to finance the insurance program is $(1+\lambda) > 1$.

Social welfare in our model reflects cooperative credit society profits less the social costs generated by financial distress and social cost of government intervention in the regulation and supervision of cooperative financial institutions. The costs of financial distress are given by the expected negative payoffs during bankruptcy plus the social costs of financial distress which are assumed to be proportional to these losses.

$$C_d(q_0) = (1+b)\int_{\underline{R}}^{R} [RL(q_0) - C(L(q_0)) - L(q_0)]g(R/q(q_0))dR \qquad (5)$$

The regulator maximizes expected social welfare W, where

$$W = E[\pi(q_0) - (1+\lambda)(C_d(q_0) + T(q_0) + \gamma(\mu) - P(q_0))] \qquad (6)$$

The problem of designing optimal regulation of a single cooperative credit society that has private information on the intrinsic quality of its loan portfolio can be written as:

$$\underset{q,T,L,P}{Max} \int_{\underline{q}}^{\bar{q}} [\pi(q_0) - (1+\lambda)(C_d(q_0) + T(q_0) + \gamma(\mu) - P(q_0))] f(q_0) dq_0 \qquad (7)$$

subject to, $\forall q_0, \hat{q}_0 \in [\underline{q}, \bar{q}]$:

$$U_C(q_0, q_0) \geq 0 \qquad (8)$$

$$U_C(q_0, q_0) \geq U_C(\hat{q}_0, q_0) \qquad (9)$$

The inequalities (8) describe the individual rationality constraints of cooperative society ensure that, for all realizations of intrinsic quality, the cooperative society expects to have non-negative utility.

The incentive compatibility constraints (9) identify $\{q(q_0), T(q_0), L(q_0), P(q_0)\}$ as the contract the cooperative will select when its intrinsic quality level is q_0.

The Full Information Benchmark

In this case, there are no informational asymmetries. The regulator is able to observe and verify the exact cooperative society's type and its exerted effort. Supervision costs are normalized at zero. The regulator maximizes social welfare in presence of bankruptcy costs.

This is the policy that the regulator would implement if he shared the cooperative society's private knowledge of its intrinsic quality level (so that the incentive compatibility constraints were not relevant), and if $\lambda = 0$. Equation (7) can be written:

$$W = \int_{\underline{R}}^{\overline{R}} (-b)[RL(q_0) - C(L(q_0)) - L(q_0)]g(R/q(q_0)dR - \psi(q(q_0) - q_0) - U_C(q_0) \quad (10)$$

The maximizing problem leads to the following proposition.

Proposition 1. Suppose first-order stochastic dominance (FOSD) or second-order stochastic dominance (SOSD) hold. Then the optimal contract under symmetric information is characterized by:

(i): $\forall q_0 \in [\underline{q}, \overline{q}],\ T(q_0) = \psi(q(q_0) - q_0)$; (11)

(ii): $$\int_{\underline{R}}^{\overline{R}} (-b)[RL(q_0) - C(L(q_0)) - L(q_0)]\frac{d}{dq}(g(R/q(q_0))dR) - \psi'(q(q_0) - q_0) = 0 \quad (12)$$

(iii): $$\int_{\underline{R}}^{\overline{R}} (-b)[R - C'(L^*(q_0) - 1]g(R/q^*(q_0)dR = 0. \quad (13)$$

Equation (11) states that at the first-best level of effort, marginal gains of effort and marginal costs of effort are equated. Higher effort induces higher expected utility and lowers the probability of bank failure, but increases the disutility of effort and therefore the required transfer for the cooperative society. The regulator pays the cooperative society just enough to make it accept the contract.

Equation (12) identifies the first-best level of quality for the cooperative's loan portfolio. Increases in quality increase the expected cash flows of the cooperative and reduce the probability of failure. At the first-best level of quality, these marginal gains are equal to the marginal costs of additional quality $\psi'(.)$. The optimal level of loan activity reflects the usual trade-off between the expected benefits from debt and the social costs of bankruptcy.

OPTIMAL REGULATION UNDER INCOMPLETE INFORMATION

In this case, it is assumed that the regulator faces adverse selection and moral hazard. In designing the contract, the regulator cannot condition on effort directly, so transfers have to be made a function of total realized quality (q) of the cooperative's loan portfolio. The regulator is concerned with limiting the cooperative society's information rents because these rents are paid with the distortionary tax system. The regulator must now weigh the gains form inducing optimal effort against the costs of leaving a rent. Using the revelation principle, we may restrict ourselves to so-called direct revelation mechanisms which have to fulfil the incentive compatibility constraints. The Envelope Theorem to applied to the maximization of (7) with respect to $\hat{q}_0$ implies that

$$\left.\frac{dU_C}{d\hat{q}_0}\right|_{\hat{q}_0 = q_0} = \psi'(q(q_0) - q_0) \quad (14)$$

From (14), $U_C(q_0)$ is strictly creasing in q_0. So the individual rationality constraint is satisfied if $U_C(\underline{q}) \geq 0$. Integrating (14) yield:

$$U_C(q_0) = U_C(\underline{q}) + \int_{\underline{q}}^{q_0} \psi'(q(\tilde{q}), \tilde{q})d\tilde{q} \quad (15)$$

Using (15), the regulator's objective function can then be written:

$$W = \int_{\underline{q}}^{\bar{q}} [\pi(q_0) - (1+\lambda)(C_d(q_0) + \int_{\underline{q}}^{q_0} \psi'(q(\tilde{q}) - \tilde{q})d\tilde{q} + \psi(q(q_0) - q_0) + \gamma(\mu))]f(q_0)dq_0$$

$$- (1+\lambda)U_C(\underline{q}) \quad (16)$$

Because $U_C(\underline{q})$ may be set equal to zero without loss of generality, and $F(\underline{q}) = 0$, after integrating by parts (16) can then be written:

$$W = \int_{\underline{q}}^{\bar{q}} \left\{ \int_{\underline{R}}^{\bar{R}} [RL(q_0) - C(L(q_0)) - L(q_0)]g(R/q(q_0)dR \right.$$

$$- (1+\lambda)[(1+b)\int_{\underline{R}}^{\bar{R}} [RL(q_0) - C(L(q_0)) - L(q_0)]g(R/q(q_0)dR + \gamma(\mu) + \psi(q(q_0) - q_0)] \quad (17)$$

$$\left. - (1+\lambda)\psi'(q(q_0) - q_0)\frac{1 - F(q_0)}{f(q_0)} \right\} f(q_0)dq_0$$

The optimal incentive contract is the solution of the pointwise maximization of W with respect to q and L. The results to follow are similar of those Giammarino, Lewis, and Sappington (1993).

The Optimal Incentive Contract Without Supervision

The next proposition reports how the information asymmetry and the social cost of government financing combine to induce departures from the first-best solution.

Proposition 2. Suppose first-order stochastic dominance (FOSD) or second-order stochastic dominance (SOSD) hold. Then the optimal contract under asymmetric information without supervision is characterized by:

(i): $T(q_o) = \psi(q(q_0) - q_0) + P(q_0) + \int_{\underline{q}}^{q_0} \psi'(q(\tilde{q}) - \tilde{q}) d\tilde{q}$; (18)

(ii)

$$\int_{\underline{R}}^{\overline{R}} [1-(1+\lambda)(1+b)][RL(q_0) - C(L(q_0)) - L(q_0)] \frac{d}{dq}(g(R/q(q_0))dR)$$

$$-(1+\lambda)\psi'(q(q_0) - q_0) = (1+\lambda)\psi''(q(q_0) - q_0)\frac{1-F(q_0)}{f(q_0)} \quad (19)$$

(iii): $\int_{\underline{R}}^{\overline{R}} [1-(1+\lambda)(1+b)][R - C'(L^*(q_0) - 1] g(R/q^*(q_0) dR = 0$. (20)

Proposition 2 shows a familiar result in incentive theory (Laffont and Tirole (1986), (1993)). The informational rents of the cooperative cannot be completely eliminated when the cooperative has private knowledge of q_0 (see equation (19)). Proposition 2 reports how the information asymmetry and the social cost of government financing combine to induce departures from the first-best solution. The departures are designed to limit any gains the credit cooperative might anticipate from understating its intrinsic quality level by choosing from the menu of contracts one that, in equilibrium, will be selected by the credit cooperative when a smaller value of q_0 is realized.

Equation (18) identifies the primary deviation from the first-best solution that the regulator implements is a reduction in the final level of quality that the credit cooperative will achieve for all but the credit cooperative with the highest realization of intrinsic quality. Quality distortions are common in incentive problems of this type. The reduced quality limits the gains to the credit cooperative from understating its intrinsic quality.

The Optimal Incentive Contract With Supervision

Supervision can either be financed through contributions by the financial institutions under supervision or from the national budget. An advantage of the latter option is that the financial institutions cannot use their contributions to pressure the supervisory agency. Employing a supervising agency enables the government to reduce the costs of regulation which are caused by leaving the high quality cooperative credit society an informational rent. Reducing this informational rent consequently leads to a smaller distortion in the effort level of the low quality cooperative, which in turn reduces the probability of credit cooperative failure. The regulator obtains a truthful report from the supervisor who is able to retrieve a signal about the cooperative's exerted effort. Because of the possibility that new valuable information is retrieved with probability μ , the incentive compatibility constraint must be modified.

$$T(q_0) - \psi(q(q_0) - q_0) \geq (1-\mu)(T(\hat{q}_0) - \psi(q(\hat{q}_0) - q_0) + \mu(T(\hat{q}_0) - \psi(q(\hat{q}_0) - q_0) - P(\hat{q}_0)) \quad (21)$$

Obviously, since the supervisor cannot collude with the credit cooperative, the optimal punishment is the maximal one, that is $P(\hat{q}_0) = T(\hat{q}_0)$. Moreover there is no use in supervising

when observing a high overall quality. In equilibrium, high overall quality reflects high effort under incentive compatibility. We do not consider the possibility of sending the supervisor on a random basis when observing low overall quality; see Kofman and Lawarrée (1993) on this topic. Given μ, the maximizing problem becomes:

$$\max_{q,T,L,P} \int_{\underline{q}}^{\bar{q}} [\pi(q_0) - (1+\lambda)(C_d(q_0) + T(q_0) + \gamma(\mu) - P(q_0))] f(q_0) dq_0 \tag{22}$$

subject to:

$$T(q_0) \geq \psi(q(q_0) - q_0) \tag{23}$$

$$T(q_0) - \psi(q(q_0) - q_0) \geq (1-\mu)(T(\hat{q}_0) - \psi(q(\hat{q}_0) - q_0) - \mu(\psi(q(\hat{q}_0) - q_0)) \tag{24}$$

The Lagrangian of this program reads:

$$L(q, L, T, P) = \int_{\underline{q}}^{\bar{q}} [\pi(q_0) - (1+\lambda)(C_d(q_0) + T(q_0) + \gamma(\mu) - P(q_0))] f(q_0) dq_0$$

$$+\eta(T(q_0) - \psi(q(q_0) - q_0) \tag{25}$$

$$+\kappa[T(q_0) - \psi(q(q_0) - q_0) - (1-\mu)(T(\hat{q}_0) - \psi(q(\hat{q}_0) - q_0) + \mu\psi(q(\hat{q}_0) - q_0)]$$

A solution to this problem is giving in the following proposition.

Proposition 3. Suppose first-order stochastic dominance (FOSD) or second-order stochastic dominance (SOSD) hold with $T(\hat{q}_0) = P(\hat{q}_0)$. Then the optimal incentive contract with supervision is characterized by:

(i): $T(q_o) = \psi(q(q_0) - q_0)$; (26)

(ii): $P(\hat{q}_0) = T(\hat{q}_0) = \dfrac{1}{1-\mu}\psi(q(\hat{q}_0) - q_0)$; (27)

(iii): (28)

$$\int_{\underline{R}}^{\bar{R}} [1-(1+\lambda)(1+b)][RL(q_0) - C(L(q_0)) - L(q_0)] \frac{d}{dq}(g(R/q(q_0))dR)$$
$$-\eta\psi'(q(q_0) - q_0) + \kappa[-\psi'(q(q_0) - q_0) - (1-2\mu)\psi'(q(\hat{q}_0) - q_0)] = 0$$

(iv): $\int_{\underline{R}}^{\bar{R}} [1-(1+\lambda)(1+b)][R - C'(L^*(q_0) - 1]g(R/q^*(q_0)dR = 0$. (29)

From Proposition 3 it immediately follows that the effort level is increasing in the probability μ (see Equation 27). Hence, as the accuracy of supervision improves, the distortion of the effort becomes smaller. Obviously, we have
$\psi(q(q_0)-q_0)=\psi(q(\hat{q}_0)-q_0)$ for $\mu=0$ (no value of supervision).

CONCLUSIONS

In this paper, we introduced a framework for designing and analyzing the properties of the optimal regulation of a single credit cooperative that has private information on the intrinsic quality of its loan portfolio (adverse selection) and where the cooperative's choice of effort to improve this quality cannot be observed by the regulator (moral hazard). In designing the contract, the regulator faces a trade off between inducing proper incentives and the costs of regulation as a consequence of informational asymmetries. This may create a demand for information gathering. If observed overall quality is low, the regulator may decide to use a supervising agency. The supervisor collects information and retrieves a signal about the cooperative's intrinsic quality, however not with perfect certainty. By incurring costs, the supervisor is able to punish the cooperative's management if caught lying. In designing optimal contracts the regulator trades off incentives for efficient cooperative against costs of regulation.

Our analysis here of the optimal contracts specifies monetary transfers from the regulator to the credit cooperative. These monetary transfers are not commonly observed in practice. In the first-best solution, the regulator is able to observe and verify the exact cooperative society's type and its exerted effort. Supervision costs are normalized at zero. The regulator maximizes social welfare in presence of bankruptcy costs. Higher effort induces higher expected utility and lowers the probability of bank failure, but increases the disutility of effort and therefore the required transfer for the cooperative society. The regulator pays the cooperative society just enough to make it accept the contract. Increases in quality increase the expected cash flows of the cooperative and reduce the probability of failure. At the first-best level of quality, these marginal gains are equal to the marginal costs of additional quality. The optimal level of loan activity reflects the usual trade-off between the expected benefits from debt and the social costs of bankruptcy**.**

The informational rents of the cooperative cannot be completely eliminated when the cooperative has private knowledge of intrinsic quality of portfolio. Proposition 2 reports how the information asymmetry and the social cost of government financing combine to induce departures from the first-best solution. The departures are designed to limit any gains the credit cooperative might anticipate from understating its intrinsic quality level by choosing from the menu of contracts one that, in equilibrium, will be selected by the credit cooperative when a smaller value of intrinsic quality is realized. Quality distortions are common in incentive problems of this type. The reduced quality limits the gains to the credit cooperative from understating its intrinsic quality.

The probability of cooperative financial institutions failure is the same for all realization of intrinsic quality (Compare equation (13), (20), and (29)). Our study abstracts form several factors that could be included in future research. First, although the interaction between regulator and credit cooperatives is not repeated, qualitative conclusions will continue to hold in many settings with repeated play. Second, we characterize information disclosure by the optimal monitoring scheme. However, the decision whether or not to bring out the

information found by the supervisor to the public is not really modelled. The optimal regulation policies in these situations merit further investigation.

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Chapter 7

THE PLACE OF COOPERATIVES IN NIGERIAN MICROFINANCE

Onafowokan Onabanjo **OLUYOMBO**

INTRODUCTION

Inadequate access to formal banking services in the rural areas of developing countries is an issue of major concern. This may be due to lack of basic infrastructural facilities in rural areas that could be used as a platform for providing this service and the perceived low level of education among rural dwellers especially in sub-Saharan Africa as a result of prolonged civil war, military rule, the *sit-down* syndrome of some rulers in the continent and several military coups – successful and unsuccessful. These events have brought untold hardship to rural dwellers and, as such, the formal banking system in most cases may be outside the reach of the poor and the poor may have to patronise any available alternatives in such locations (Oluyombo, 2010). However, there is no doubt about the existence of poverty across nations, and the likely negative consequences of poverty to individuals, households, enterprises and nations of the world. The desire to reduce the effect of poverty worldwide is not in contention but the modalities on what to do, how they should be implemented and the reason for the choice of such action differs from one nation to another.

The objective of this paper is to create a clear understanding of some basic and essential aspects of microfinance and cooperatives across the world with special emphasis on Nigeria. This is important to enable the researcher to explain and discuss the different types of formal and informal microfinance service providers in the country and their operations. Discussion and clarification of contextual aspects of microfinance and cooperatives would enable the researcher to provide working definitions and explanations of different terms used in these areas of study which may be different from the way it was used by other studies.

DEFINITION OF MICROFINANCE

Microfinance is the provision of small scale financial services to people who lack access to traditional banking services which includes very small loans to low income clients for self employment, often with simultaneous collection of small amounts of savings (Karlan and Goldberg, 2007). There are people who cannot patronise conventional banks but still need to enjoy small scale financial services that cannot be provided by the traditional bank. The focus in the study by Karlan and Goldberg (2007) are individuals who earn income which is neither enough for them to start any enterprise nor move them out of poverty level. They therefore see microfinance (MF) as an avenue through which such people can access loans to become self employed and probably escape poverty.

Microfinance is the supply of loans, savings and other basic financial services to the poor (Iganiga, 2008). Microfinance includes the provision of savings opportunity for the participants which may not occur in all situations because some projects are financed exclusively to alleviate the economic situation of the participants.

The inaccessibility to traditional banking services put forward by Karlan and Goldberg (2007) may not be tenable because there is no clear cut definition of what traditional banking services are. How do we then explain an individual who declines to patronise a bank based on his or her background, educational attainment or because of some other personal predicaments? Is such a person not served by the traditional bank? There is a need to properly define small financial services, traditional banking services and small loans. This brings us to the institutional definition by the Central Bank of Nigeria - CBN (2005) that microfinance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions. It went further to provide three features that distinguish microfinance from other formal financial products. These are (i) the smallness of loans advanced and/or savings collected (ii) the absence of asset-based collateral, and (iii) simplicity of operations. Microfinance is an intervention based on social intermediation in which poor people can mobilise their savings, link them with credit and finally become self employed (Singh, 2004). The social intermediation in microfinance includes training of MF clients on different areas of vocations, health, literacy, business record keeping and management skills as found necessary. Social intermediation also include support for clients in trouble such as sickness and those having essential social function to perform such as burials and weddings. The concept of microfinance was defined as

> *"small-scale financial services, primarily credit and savings-provided to people who farm or fish or herd; who operate small enterprises or micro enterprises where goods are produced, recycled, repaired or sold; who provide services; who work for wages or commissions; who gain income from renting out small pieces of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries both rural and urban"* (Robinson, 2001: 9).

The definition is specific as it fully indicates the beneficiaries of microfinance institutions (MFIs) and also suggests that developing countries need more MF than developed countries. This has been refuted in part by Singh (2004) that MF is applicable wherever poverty exists. Poverty can be relative or absolute. Relative poverty has to do with the living standard of the poor when compared to the standard of living that is applicable elsewhere in the same society where the poor lives. Absolute poverty refers to poverty measurement which shows the lack of basic items such as food, clothing and shelter for survival. Absolute poverty seems to be more pronounced in developing nations, it can therefore be reasoned that the higher the extent of poverty, the greater the need for a financial intervention such as microfinance.

Robinson (2001) argues that microfinance is meant for both the rural and urban dwellers. Microfinance services cannot be totally restricted to the poor people in rural areas alone because as there are poor people in the rural areas, so they are in the urban centres (Oluyombo, 2011). Though this group of people in the city may not be easily identified, but they are poor and need microfinance services since the conventional or commercial banks do not have any product or service to benefit them as identified in CBN (2005). The establishment and provision of MF is not restricted to a particular group of people living in a particular location, but it is all about the availability of financial services that is beneficial to

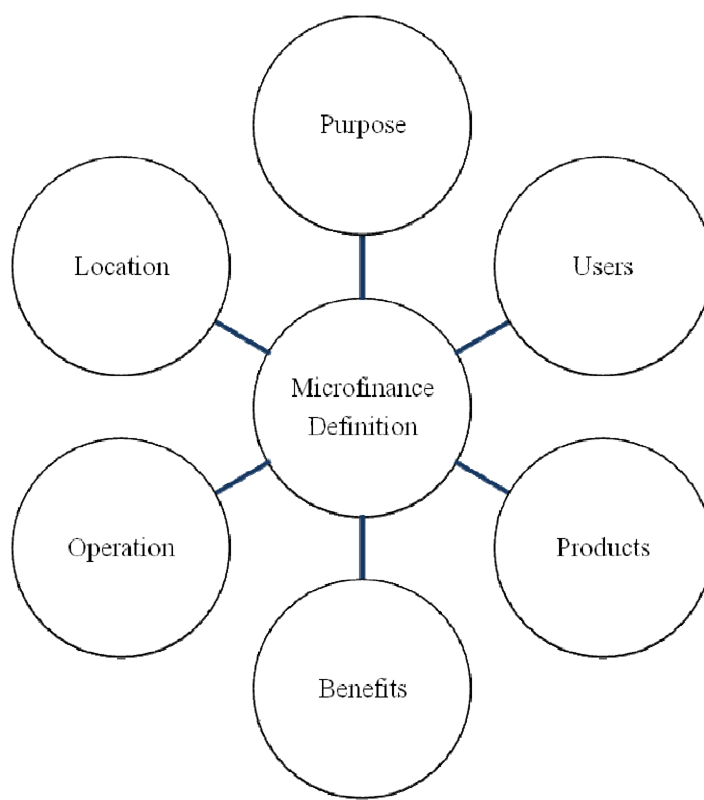
the poor people irrespective of where they live or what they do to earn a living in as much as it is intended to serve as a financial leverage out of poverty circle (Oluyombo, 2010). Otero and Rhyne (1994) describe microfinance as the provision of small loans and deposit services in large scale to low income people in a secure and convenient location through competing commercial financial institutions thereby generating the process needed to democratise capital. The number of MFIs should be large enough to meet the needs of low income earners through the provision of deposit and loan facilities and to give room for healthy competition among them. These definitions (Otero and Rhyne, 1994; Robinson, 2001) recognise that any attempt to draw the low income earners into the formal banking system may fail because they do not have what it takes to be the clients of commercial banks.

Ledgerwood (1998) sees microfinance as a development approach with economic undertones which is intended to benefit low income men and women. This is to reach the low income earners with financial services that will enable them to create wealth without any discrepancy as to the gender of such person. This is because some studies (Mawa, 2008; Akingunola and Onayemi, 2010; Idowu and Salami, 2011) present microfinance as relevant to the female gender alone. Microfinance is one of a range of innovative financial arrangements designed to attract the poor as either borrowers or savers (Montgomery and Weiss, 2005). For a microfinance program to be innovative, it implies that it has to be dynamic in operation. The ability of MFIs to change suggests that there should be an avenue through which feedback can be received from MF users to determine how satisfied they are with the system.

Microfinance enables low income people to access financial and non financial services that are packaged in a manner that enables those who are unable to access formal financial services to access comparatively small loans, saving schemes and other services for working capital and income generation (Nathan et al., 2004). Park and Ren (2001) note that microfinance programs are united in aiming to provide financial services to individuals traditionally excluded from the banking system. Microfinance can be seen as a holistic approach designed to improve the lot of individuals and enhance micro and small scale entrepreneurs both in the rural and urban areas in accessing fund as at when needed, from microfinance services providers depending on the amount involved.

The review of different definitions of microfinance above led to the development of the "microfinance definition model" in figure 1 below by the researcher. This model captures the essential elements of a working definition of microfinance.

Figure 1. Microfinance Definition Model (MDM)



Microfinance is therefore defined as a deliberate economic approach to the delivery of financial services by formal and informal microfinance providers in form of savings, loans and financial advisory services to those that are hitherto unreachable due to their income and/or location at a fee that is affordable and economical to the users of such services. And also, using funds from the providers of these financial services to generate adequate returns for the users, thereby building up their enterprises and creating employment opportunity which has the potential of reducing the poverty level in an economy.

The model in figure 1 above and the microfinance definition provided by this study above (below figure 1) are further explained in table 1 below based on the various definition of microfinance examined in this section.

The main objectives of microfinance based on various definitions examined above can be summarised as the provision of savings and credit services to low income earner, bringing banking services to those that are hitherto unbanked, economic empowerment of poor entrepreneurs, accessibility to credit under less stringent conditions, integration of the poor into the financial system by creating and developing banking habit among the poor and low income earners, and provision of financial services to rural and semi-urban centres.

Table 1 Summary of Microfinance Definition

Purpose	• Encourage savings • Access to credit or loan • Raise entrepreneurs
Users	• Low income earner • Poor people • Irregular income earner
Operation	• Low scale financial services • Formal and informal ways
Location	• Rural and Semi-urban centres • Areas not served by conventional banks
Benefits	• Poverty alleviation and/or reduction • Financial empowerment of entrepreneurs
Products	• Savings • Loan • Other financial and non-financial services

HISTORY OF MICROFINANCE

Microfinance business is likely to have commenced in the primitive age of trade by barter as an informal sector, long before the advent of paper money, based on the economic needs of the people in different household. The actual date is not certain, but Easton (2005) stated that the lending of uncollaterised loans to the poor originated from the non-governmental organisations (NGOs). Opportunity International, an NGO began lending in Colombia in 1971, while ACCION International gave its first micro loan in 1973. Grameen Bank commenced micro loan in Bangladesh in 1976. Mawa (2008) recorded that Grameen Bank started in 1974 without any brand or registered name when it launched its $27 project in a village called Jobra, but was later called Grameen Bank in 1983. Ledgerwood (1998) stated that MF arose in the 1980's as a response to the need for subsidised credit to poor farmers, because the poor required cheap credit as a way of promoting agricultural product by small land holders or peasant farmers. Consequently one could arguably state that the need to provide cheap loans to the low income farmers brought about microfinance.

According to Robinson (2001), Indonesia commenced microfinance in the formal sector in 1970 with the opening of Bank Dagang in Bali providing micro savings and loan services to the poor in the rural and urban areas. Westover (2008) reported that microfinance started in Bangladesh around 1976 through the Grameen Bank. Microfinance commenced in Bangladesh in the 1970's (Montgomery and Weiss, 2005). The earliest account, until it is proved contrary, is by Robinson (2001). It revealed that microfinance might have commenced on or before 1970. For most African countries, independence had taken place about a decade before. This signifies the learning period in creating and transferring governance to Africans and the lack of skilled personnel in such nations. The evolution of microfinance organisations compiled by the researcher based on the literature is in table 2 below. The table shows the names of the microfinance institutions, country of location and year of establishment.

Table 2 Evolution of Microfinance

S/N	Organisations	Country	Year
1.	Bank Dagang	Indonesia	1970
2.	Opportunity International	Colombia	1971
3.	Grameen Bank	Bangladesh	1976
4.	National Development Foundation	Jamaica	1981
5.	Association for Development of Micro Enterprises	Dominica Republic	1983
6.	Bank Rakayat	Indonesia	1984
7.	Kenya Rural Enterprise Programme	Kenya	1984
8.	Agence de Credit Pour'L Enterprise Privee	Senegal	1986
9.	Foundation for the Promotion and Development of Micro Enterprises	Bolivia	1986
10.	Instituto de Desarrollo Hondurando	Honduras	1987
11.	Banco Nacional del Pequeno Comercio	Mexico	1992

THE FINANCIAL SECTOR IN NIGERIA

The structure of the Nigeria financial system consists of supervisory/regulatory authorities, banks and other non-bank financial institutions (Oluyombo, 2007b) as stated below.

a. The supervisory authorities are: Central Bank of Nigeria, Securities and Exchange Commission, Nigeria Deposit Insurance Corporation, Federal Ministry of Finance, National Insurance Commission and Federal Mortgage Bank of Nigeria.

b. Banking institutions are: Universal Banks, Microfinance Banks, Mortgage Banks and Profit and Loss Sharing Banks.

c. Development banks: Bank of Industry, Urban Development Bank Plc, Nigeria Export - Import Bank and Nigerian Agricultural, Cooperative and Rural Development Bank.

d. Non-bank financial institutions are: Nigerian Stock Exchange, Insurance Companies, Bureau-de-change, Discount Houses, Financial/Investment Companies, Pension Fund Managers, Issuing Houses and Stock Brokers.

Microfinance Policy and Regulation in Nigeria

The formal microfinance institutions in Nigeria is named 'The Microfinance Bank', it was so named as a result of the transfer of the regulation and control of the former community banks from the National Board for Community Banks to the Central Bank of Nigeria in 2005. The survival of microfinance institutions in any country depends largely on the overall political and economic environment of such nation because MFI exists within the wider economy of the particular country where it operates. The practice of microfinance has grown over the years across the globe either as formal or informal institutions. The regulation of these

institutions is a function of the roles they are expected to perform in such economy vis-a-vis the level of poverty in such a nation. According to Oluyombo (2007b), the adoption of microfinance banking concept in Nigeria, which is expected to result in grassroot development and poverty reduction, might have opened up more opportunities in the Nigerian financial system while creating new challenges for supervisory and regulatory authorities in the country. In essence, MFIs need to be regulated and supervised to monitor their safety and soundness so as to ensure that the hard earned savings of low income earners are properly kept and utilised so that the poor do not become very poor as a result of the failure of these MFIs. If MFIs are expected to act through it products and services as a channel through which many could be lifted out of poverty in an economy, it should be regulated. But the regulation should be carried out in a way that does not encourage a run on the MFIs or discourage the low income earners from patronising these MFIs. Irrespective of the regulation of MFIs, there are some informal microfinance providers such as the rotational savings scheme that cannot be regulated because they operate on personal trust over time among familiar and related individuals.

Conversion of Community Banks to Microfinance Banks

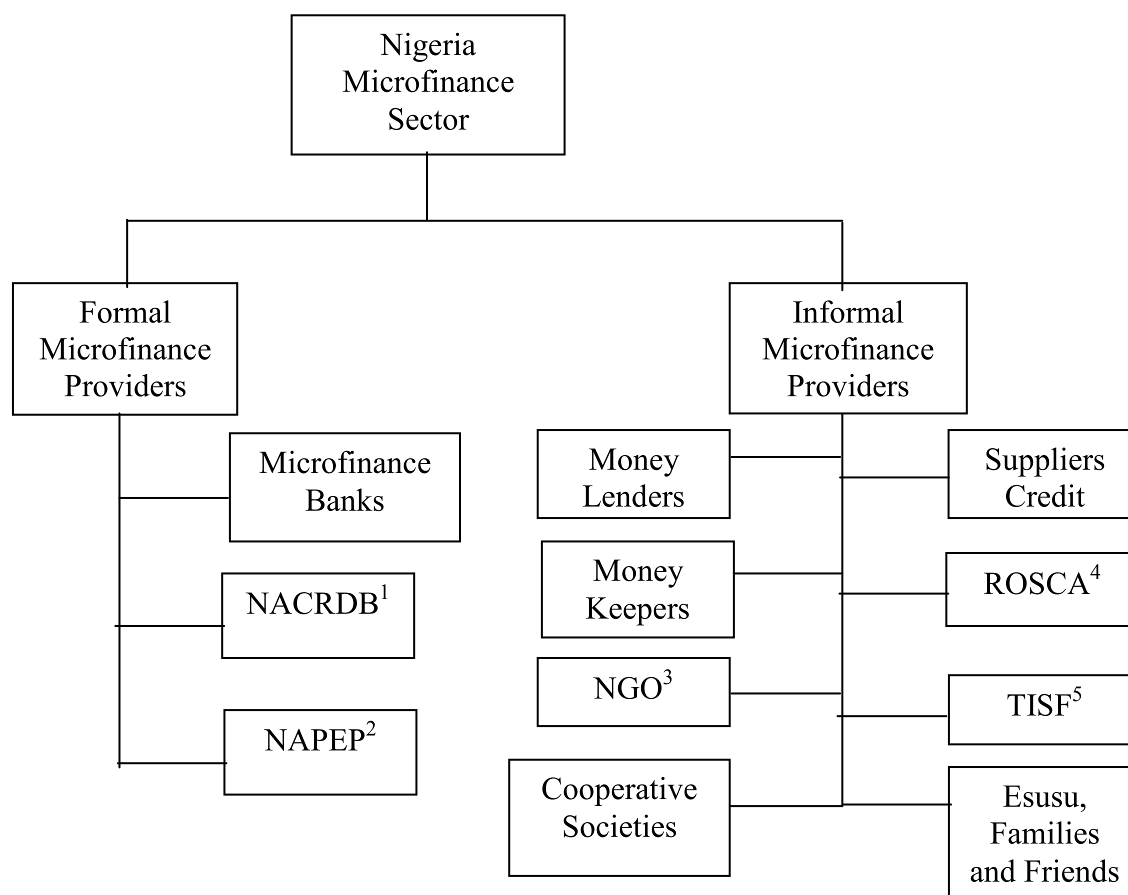
Community banking in Nigeria relates to those banks that are established to serve a community or group of communities operating under a unit banking structure that is not expected to open any branch outside the community(ies) it intends to serve. These banks are owned and managed by the community with the purpose of providing different types of banking services at the grassroots level. In the administration of loans, they are to rely more on self recognition of the borrower instead of availability of collaterals like other banks. According to Agene (1995), a community bank is a self-sustaining financial institution owned and managed by a community or group of communities for the purpose of receiving deposits, providing credits and other banking and financial services to its members, largely on the basis of self-recognition and credit worthiness. This borrowing strategy has changed drastically as a result of many community banks that were distressed in the 1990s.

In pursuance of the establishment of Microfinance Banks in Nigeria, the CBN (2006) issued a circular referenced OFIC/DO/CIR/Vol.1/450 on February 3, 2006 on the requirements and procedures for the conversion of Community Banks to Microfinance Banks (MFB). The operation of MFB in Nigeria is grouped into two by the CBN. The first group operates as Unit Microfinance Bank while the second group operates as a State-wide Microfinance Bank. The implication of this can be seen from the prescribed capital requirements of ₦20 Million ($133,333) for Unit MFB and ₦1 billion ($6,666.667) for State-wide MFB. The license fee payable to the CBN is ₦170,000 ($1,133) and ₦400,000 ($2,666) for Unit MFB and State-wide MFB respectively. The unit MFB operates within a local government council and can open branches or cash centres within the same local government after seeking approval from the CBN. The State-wide MFB are allowed to open branches or cash centres within the state after seeking the CBN approval. The CBN directive is a way of bringing the informal financial sector under the control and influence of the CBN, thereby promoting monetary stability and sound financial system in the country. The CBN policy is the official commencement of MFB in Nigeria.

The author’s perspective about the current position of the Nigeria microfinance sector is shown in figure 2 below which shows that the sector is divided into two, namely formal and

informal microfinance providers. The informal microfinance providers are discussed thereafter.

Figure 2. Nigeria Microfinance Sector



INFORMAL MICROFINANCE PROVIDERS IN NIGERIA

The informal microfinance providers are microfinance outlets that operate outside the regulatory and supervisory authorities of the financial system regulatory bodies. The informal MF providers are more than formal providers in rural areas and semi-urban centres as a result of the exclusion of poor people from financial services by government regulated financial institutions because of high transaction costs, high risk, lack of infrastructural facilities and lack of adequate/acceptable collateral (World Bank, 2000; Oluyombo, 2007a). The pattern and nature of informal microfinance in developing countries differs substantially, though similar in their operation. According to Buckley (1997), most entrepreneurs make use of the informal sectors financial intermediaries in Africa. The informal financial sectors are those financial providers that cannot be classified or regarded as

[1] Nigerian Agricultural, Cooperative and Rural Development Bank
[2] National Agency for Poverty Eradication Program
[3] Non Governmental Organisation
[4] Rotational Savings and Credit Association
[5] Trade and Input Supply Financing

a separate legal entity since they are neither controlled nor regulated by the government. In most cases, they operate outside the financial system hence the cooperative society and rotational saving scheme can be regarded as institutional finance provider for entrepreneurs in informal sectors of rural areas, while the individual arrangement for informal microfinance include, friends, family, money collectors and money lenders.

The World Bank (2000) reported that in virtually every part of Nigeria, people have used their personal savings and small loans from family and friends and other informal associations, to carry out their businesses. The same report affirms that rural dwellers still patronise and show preference for the informal sector due to the high degree of certainty and flexibility in sourcing for, and repaying loans from informal lenders. It is easy and faster to source for credit from these informal financial service providers in Nigeria than the commercial banks (Oke et al., 2007; Oluyombo, 2010; Idowu and Salami, 2011). This is because a prospective borrower can access the lender and the financial deals completed within few days. With an average maturity of three months, the informal sector ruled out becoming involved in the provision of the medium to long-term credit necessary for term investment in long gestation crops, livestock and agro-processing (World Bank, 2000).

Types of Informal Microfinance Providers

About 90% of the rural sector financial needs were satisfied by informal rural finance providers (World Bank, 1994). The report specified that the informal sources provided the bulk of rural dwellers credit needs for five active occupational groups, namely: farmers, artisans, market women, traders and local manufacturers. There are different types of informal microfinance providers in the world, some of these operate in groups as associations and unions within a particular community, profession, clan and companies. World Bank (2000) and Akingunola and Onayemi (2010) identified informal rural finance providers in Nigeria to include: trade and input supply financing, cooperative societies, non-governmental organisations, *esusu's*, families, friends and money lenders. Informal microfinance providers identified by Buckley (1997) include supplier's credit, money lenders and rotational savings scheme. Iganiga (2008) identifies NGOs, money lenders, friends, relatives, savings collectors, rotating savings and credit association, credit unions and cooperative societies as main providers of informal finance in Nigeria.

The informal microfinance providers in India are the traditional money lenders, pawn brokers and trade specific lender (Singh, 2004). Nathan et al. (2004) reported that the informal microfinance sector in Uganda include cooperative and credit societies, government credit scheme, NGO, money lenders, commercial firms employers, relatives and friends. The informal microfinance providers shown in figure 2 above are discussed below.

Suppliers Credit

This is an arrangement whereby goods are supplied to an entrepreneur on credit for a particular period of time. This is possible as a result of long time business relationship between the supplier and the buyer. The amount of goods supplied includes an element of interest that is neither disclosed to the buyer nor stated in his invoice. Suppliers' credit stands between the money lender and friends/relatives, and this is usually for a short term and flexible (Buckley, 1997).

Money Lenders

Money lenders are those individuals who spend a significant part of their time lending money, usually for short periods and sometimes unsecured by collateral (Buckley, 1997). The provision of collateral security for loans is one of the distinguishing features of informal microfinance from formal finance providers. Whereas the banks will seek for tangible and adequate collateral (financial assets and physical assets) that can compensate them in case of default, a money lender is not in a position to take collateral because the loan is expected to be paid in most cases within a few weeks or months. The money lender does not see the need to ask for collateral, this is the main reason why the interest rate charged by money lenders is always higher than the bank interest rates (Singh, 2004; Oluyombo, 2010). The high interest rate is to compensate for the risks of default as an alternative to taking collateral. The interest rate is not uniform and the ability of money lenders to craft loan contracts that are unusual is one of the major advantages that money lender finance has over formal finance (Buckley, 1997). Interest charged by money lenders is a function of many parameters such as the amount, duration, purpose and season of the year such as harvesting time and festival period. It also includes the borrowers profile and the fund available to the money lender at that particular period.

Rotational Savings and Credit Scheme

A rotational savings and credit scheme or association (ROSCA) is an arrangement whereby people who know each other come together to form an economic team of providing savings and credit opportunity for each member of the group. The operation requires that each member is expected and committed to save an agreed amount at a particular period for a fixed term (Iganiga, 2008). The savings by the members are given on a rotational basis to a member of the group until the last person in the group has benefited. ROSCA varies in size and practices, but the principles that define them remained fairly constant (Buckley, 1997). Participants in ROSCA are free to use their credit for whatever business they like and there is no restriction as to how the money can be used. Moreover, members are saved the burden of payment of interest on their credit since all members jointly raise the fund.

Money Keepers

The money keeper's arrangement in developing nations including Nigeria has to do with a person serving as a financial intermediary between a saver and a financial institution (World Bank, 2000). The arrangement requires the money keeper to move from one house, store, shed, kiosk etc to another to collect individual savings on a daily basis. The record keeping is carried out by the money keeper in his ledger opened for each saver and a saving card held by the contributor which the money keeper endorses on a daily basis signifies that fund in term of savings has been kept with him. Each saver is expected to contribute usually for a month and at the end of the month, the money keeper then gives the saver the total amount saved for the month less a day saving which serves as the benefit for the money keeper's services rendered.

This type of arrangement is common in the rural and semi urban areas where the dwellers found it extremely difficult to patronise commercial banks either as a result of their lack of education or the distance of banks to such communities. One of the outstanding benefits of the money keeper is that it encourages a saving habit among the rural poor (World Bank, 2000;

Singh, 2004). Though the savers pay for the service, yet it reduces transaction cost of the savers transporting themselves individually to a commercial bank venue before they can save into or withdraw from their account.

Trade and Input Supply Financing

They are concerned with the provision of funds for the purchase, handling, transportation, processing, storage, and selling of various commodities. It involves short term funding to carry stocks of inputs and produce at various stages of production and marketing. This financing arrangement is common in the rural and urban areas among commodity traders (World Bank, 2000).

Non Governmental Organisations

The non-governmental organisations operate partly as a result of programs sponsored by development organisations and donor agencies to support poverty eradication and rural development (Singh, 2004). The mandate of most NGOs is to promote rural development and increase the standard of living of the poor rural communities by providing credit and technical assistance.

Esusu, Family and Friends

The main informal lenders that mobilise deposits are the *esusu's* and the money keepers, while money lenders are seldom involved in accepting deposits. In terms of volume and coverage, the savings collectors have the highest rates of savings mobilisation. Family and friends also provide small amount of loan with short term duration as an informal finance (World Bank, 2000) but availability of fund from them is not usually guarantee.

Cooperative Societies

Sizya (2001) opines that cooperatives provide an opportunity for pooling financial resources of people of limited financial means together in order to achieve commonly identified development needs of their members. Cooperative societies are avenue through which cheap credit is channelled to the rural areas and especially when it is supported by international donors and governments (Huppi and Feder, 1990). Cooperatives are based on the members' ideology and need, hence there is a need to reduce government intervention in cooperatives to the barest minimum especially in areas where financial demand is placed on them since the formation and funding of the cooperatives is from the members with or without government subvention or grant. Cooperative societies are a major part by which developmental activities are carried out in rural communities via individual member's participation. Financial cooperatives was described by Larocque et al. (2002) as an avenue for those without access to commercial banking services to gain access to financial services that may include savings deposit, productive credit, consumer credit and loan.

Cooperatives have been the leader in development interventions that aim to alleviate the poverty level of the poor in the rural areas (Sizya, 2001). The rural people take solace in the little financial service that is provided by the cooperative. Sizya (2001) stated further that cooperatives are the most significant forms of participation in financial markets available to

the rural Tanzanians. The importance of cooperatives has been identified by Larocque et al. (2002) as an avenue for the introduction of formal banking to rural areas in Burkina Faso. This shows that the rural people first have a good knowledge of the benefits of financial services by participating in financial cooperatives and thus suggests that the failure of access to formal banking system in the rural areas is a major boost for the growth of financial cooperatives.

COOPERATIVE SOCIETIES IN NIGERIA

The early cooperative societies in Nigeria were established to facilitate cocoa farming which led to the establishment of the Cooperative Registrar of the Colonial Government in 1935. Later, these cooperative societies began providing financial intermediation between members (World Bank, 2000). Eventually, multi-purpose cooperative societies were designed to simultaneously solve several problems facing members, such as input supply, farming and marketing of farm produce. When purchases increase in volume or value, traders often approach their informal thrift and savings associations for loans. Cooperatives with track records of prudent management and cohesive membership stand to play a major role in the development of rural financial markets in Nigeria (Oke et al., 2007).

The existence of employee cooperatives in some organisations reduce the burden of loan request from their employers and also serve as a common platform for owning household equipments and other assets at a reduced interest rate with loan repayment spread over a particular period of time (Oluyombo, 2010). A study by Oke et al. (2007) show that more clients of microfinance institutions in South Western Nigeria are members of cooperative societies. Cooperative members in other microfinance organisations and programs believe that the cooperative is a very good alternative source of finance in form of saving and loans for them (Oluyombo, 2010). Oke et al. (2007) observed that improvement in payment of loans in microfinance program by 7.05% is caused by cooperative society's members. Cooperative credit or loan processing is faster than the formal banking sector because assets are not required as collateral, and a loan can be given for any activities and there is less administrative work. Oke et al. (2007) and Oluyombo (2010) notes that the interest paid on a cooperative loan is lesser than those charged by the formal MFIs in Nigeria. Larocque et al. (2002) found that it is not possible to get a low interest rate in the banking system as it is available within the cooperatives societies.

CONCLUSION

Microfinance and cooperatives are related in Nigeria in term of their purpose, but the regulatory framework differentiates between the two whereby the microfinance institutions are formal financial providers, while the cooperatives are the informal. In Nigeria, most cooperative societies are financially sustainable because of their ownership base which is restricted to cooperative members alone and the operational modality is approved by the cooperative members. Interest rate on loan are jointly agreed upon by the members and implemented by their executives elected by members at their annual meetings.

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Chapter 8

DETERMINANTS OF MICROFINANCE BANKS SUSTAINABILITY IN SOUTH-WESTERN NIGERIA

Olubanji S. **FAJONYOMI**
Charles Ayodele **JEGEDE**

INTRODUCTION

One of the central problems confronting most economies, developed or developing, is that of sustainable economic growth. In Nigeria, successive governments from independence in 1960 have laid emphasis on the need, not only to consolidate the country's political autonomy, but more importantly to achieve economic independence through the indigenization and modernization of small and medium enterprises aimed at accelerated socio-economic development. Among the factors that are theoretically expected to promote rapid economic development in an economy is finance. Finance has also been regarded as an important ingredient in enhancing growth and development of micro and small enterprises (Levy, 1993). Indeed many studies have found a direct and positive relationship between finance and growth of Micro and Small Enterprises (Foster and Gupta, 2003; Kenji and Yuji, 2006; Radji and Ajani, 2007).

Since the existing financial banks structure could not meet the required credit need of the poor and the fact that Nigeria, like most other developing countries, is in serious need of sustainable economic growth. The Nigerian government has vigorously pursued poverty reduction programmes through direct and indirect involvement in micro finance banks, to cater for the financial needs of the so-called deprived groups. It has however been observed, that inefficiencies as well as over indebtedness of credit granted to the clients led to collapse of these publicly owned micro finance banks (Sanusi, 2003; Okereke, 2005).

Following the poor performance and collapse of publicly owned micro finance banks, the Nigerian government in August 1991, introduced Community Banks (CBs) to address the inefficiencies of the public sector-led micro finance banks. However, it was disappointing to note that, the number of Community Banks which stood at 1,355 in 1995 declined to 634 in 2005 (Mohammed and Hassan, 2008). Furthermore, by the beginning of 2005, the Central Bank of Nigeria reported that no fewer than 700 Community Banks had collapsed as a result of poor management skills of the operators and weak capital base. Consequently, microfinance banks were introduced to replace the remaining surviving Community Banks. The capital base of the newly introduced microfinance banks was increased from ₦5 million to ₦30 million by the Central Bank of Nigeria so as to remain liquid, strong as well as to reach out to more clients and be able to perform on long-term basis without relying perpetually on government subventions for their operations. But, it has been observed, that one of the challenges currently faced by micro finance banks in Nigeria is that of sustainability (Soludo, 2008). The report by Central Bank of Nigeria (2005) survey revealed that, existing microfinance banks in Nigeria

serve less than 1 million people out of 40 million that need its services and account for about 0.2 percent of Gross Domestic Product (GDP) and less than 1.0 percent of total credit to the economy. This was further corroborated by the study of Soludo (2008) which submits that the existing microfinance banks in Nigeria will benefit only 35 percent of the nation's population, particularly medium and small scale enterprises (MSEs), due to uneven spread of the banks across the 36 states and the federal capital territory.

There are however virtually little or no research efforts conducted on the determinants of microfinance banks sustainability in Nigeria. Most studies conducted are mainly on impact analysis of microfinance banks, on poverty alleviation (Akanji, 2001; Magnus, 2005; Folake, 2005; Okerenta, Orebiyi and Adesope, 2007) with the exception of a few studies. Another major controversy addressed in the literature is whether microfinance banks are sustainable or not. While some studies reveal that these banks are sustainable (Hulmes and Mosley, 1996; Rhyne, 2002; White and Champion, 2002), others indicate that they are not (Morduch, 2000; Hartarska and Nadolnyak, 2007). Most microfinance banks owned by governments have been found to be highly unsustainable (Murduch, 2000) while those owned and controlled by NGOs and private sectors are found to be highly sustainable (Hulmes and Mosley, 1996, Rhyne, 2002). The evidence from these studies shows that the issue of what determines the sustainability of microfinance banks has not been extensively addressed in the literature. Hence, the continued disappointing performance of microfinance banks sustainability in Nigeria calls for investigation and therefore, this study hopes to achieve the following specific objectives:

i) To ascertain the extent of the sustainability of microfinance banks in Southwestern Nigeria.
ii) To determine the factors affecting microfinance banks'sustainability in Southwestern Nigeria.
iii) To examine the role of microfinance banks as financial intermediaries.

CONCEPTUAL FRAMEWORK

The sustainability of microfinance banks has manifested in diverse definitions, depending on the interest of individuals or organisations. Robinson (2001: 128) defined "microfinance as small-scale financial services, primarily credit and savings, provided to people who farm or fish or herd; who operate small enterprises or micro-enterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages and commissions; who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and other individuals and groups at the local levels of developing countries, both rural and urban area".

Microfinance is usually conceived of as the provision of small units of financial services to low income clients who are usually excluded from mainstream financial intermediation, which primarily focuses on alleviating poverty through the provision of financial services to the poor or owners of microenterprises (Ehigiamusoe, 2008). The objectives of microfinance banks include: (i) promotion of rural development through financial intermediation, (ii) stimulation of productive activities in the rural sector, (iii) development of banking habits in rural dwellers and ensuring the development of an integrated national financial system, and (iv) improving the economic status of small scale producers in the rural and urban areas. Similar definition is provided by Akanji (2001). Ledgerwood (1999) posits that microfinance

"is the provision of financial services (generally savings and credit) to low-income clients. The clients are often identified as traders, street vendors, small farmers, service providers (hairdressers, rickshaw drivers), and artisans and small producers, such as blacksmiths and seamstresses." Microfinance pertains to the lending of extremely small amount of capital to poor entrepreneur in order to create a mechanism to alleviate poverty by providing the poor and destitute with resources that are available to the wealthy albeit at small scale. According to Aklilu (2002) and Christen and Drake (2002) from the perspective of household sector, microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers, and insurance to poor and low-income households and their micro-enterprises. The definition; low income households' as well as those below the poverty line are employed since there are a significant number of low-income households that are not below the poverty line, but have limited access to financial services, especially in rural areas.

In practice, microfinance means more than delivery of small units of financial services. It goes beyond disbursement and collection of loans. It refers to the flexible structures and processes by which affordable financial services are delivered to the owners of micro-enterprises on a sustainable basis. Microfinance includes a range of financial services such as savings, credit, money transfers and insurance, among other things for poor and low-income people. For credit to be of help to people, the recipient should have the capacity to service the credit, in addition to having an intention to do so. For example, Robinson (2001) points out that, extremely poor households living in small, isolated communities in areas that lack basic infrastructure and markets may be unable to use credit in any way that would enable them to repay loan principal and interest. Haan and Lipton (1998) also believe that credit should be a lubricant for the engine of feasible and profitable activities: if the lubricant is mistaken for the engine, the borrower may end up in a debt trap. Thus, financial services do not create economic opportunities; they only enable people to take advantage of the economic opportunities created through other interventions (Fernando, 2004).

Access to financial services enables the poor to increase their household incomes, build assets and reduce their vulnerability to crisis that they face in their daily lives. Financial services can put power into the hands of poor households, allowing them to progress from hand-to-mouth survival to planning the future, acquiring physical and financial assets and investing in sustainable livelihood initiatives. When such resources are effectively utilized, they lead to expansion of business activities, enhanced productivity and employment of additional labour as a result of business expansion. Microfinance bank stimulates savings and asset accumulation. Empirical and anecdotal evaluation of many microfinance banks reports, conclusively from the clients' perspective, that learning to save and having a safe place to keep those savings are principal benefits of the microfinance banks (Odejide, 1997). Thus, microfinance has demonstrated ability to build up capacity of people and communities; as well as make a significant and social development in developing countries.

Nature and Measure of Microfinance Sustainability

The world of microfinance has dramatically changed over the past decades from a subsidy oriented focus to a focus on sustainability; from a project approach to a focus on building sustainable microfinance banks; from a perception of poor as beneficiaries to treatment of people as partners, from providing credit only to providing a range of financial services. The term sustainability is widely used interchangeably with other concepts such as profitability, self-sufficiency, financial self-sufficiency, self-sustainability, financial

sustainability, financial efficiency, operating self-sustainability (Yaron, 1992; Rhyne and Otero, 1992; Christen, Rhyne, and Vogel, 1995; Hulme and Mosley, 1996; Christen, 1997; Ledgerwood, 1999; Meyer, 2002). Ledgerwood (1999) defined sustainability as the continuous service provision to clients profitably as a going concern without relying on subsidies. Sustainability in the opinion of Meyer (2002: 102) is "the ability of the organisation to grow and provide services on a long-term basis with either its own resources or debt secured from commercial sources, which the organisation must have ability to repay and without relying perpetually on subsidies. To reach the majority in the long-run requires being self-reliant and sustainable by securing revenues through expanding its outreach and increasing its volume of service".

Christen (1997) concludes that in most discussions, sustainability is taken to mean full cost recovery or profit making, and is associated with the aim of building microfinance banks that can last into the future without continued reliance on government subsidies or donor funds. Therefore, sustainability is a question of self-reliance in the medium to long-term, or as Meyer (2002) argues, that sustainability means, the ability of the organisation to grow and provide services on a long-term basis with either its own resources or debt secured from commercial sources, which the organisation must have ability to repay.Woller andSchreiner (2006) argue that bank sustainability is determined by the extent to which microfinance banks are efficient in using resources and turning them into services. Yaron (1994) identifies four necessary conditions for microfinance banks to become sustainable:

i. The bank should have positive on-lending interest rate high enough to cover non-subsidized financial costs (for a subsidized bank) to maintain the value of equity in real terms.
ii. Second, the bank has to achieve a high repayment rate.
iii. Third, the bank has to offer deposit interest rates high enough to ensure that voluntary saving becomes increasingly significant in financing the loan portfolio.
iv. Lastly, the bank must be efficient (including low transaction and administrative costs) in its delivery mechanism which includes the screening process, processing loans, collecting repayments, and mobilizing and servicing savings to ensure that lending rates do not become prohibitive.

Several classifications have been developed concerning the level of sustainability attainable by micro finance banks; however, Robinson (2001) argues that most of the world's microfinance banks are categorized in the first category basically sponsored by government. Christen (1997) divides the level of sustainability into three categories:

i. The first category comprises banks in which revenues from interest and fees do not cover operating costs.
ii. The second category identifies banks in which revenue covers operating costs but does not cover the commercial costs of loanable funds. This second category refers to microfinance banks in which fees and interest charges cover nonfinancial costs, but still depend on subsidies to varying degrees for the cost of loanable funds. Most non-governmental Organisations (NGOs) microfinance banks fall under this category.
iii. Fully self-sufficient banks that cover all costs and risks and generate profit are in the third category which refers to microfinance banks (private sector sponsored) whose revenues cover both non-financial and financial costs calculated on a commercial basis.

Ledgerwood (1999) on the other hand classified sustainability into four dimensions; these are (i) continued benefit flows, (ii) longevity or survival, (iii) ability to meet recurrent costs, and (iv) bank capacity and performance. It is about ensuring effectiveness, building and maintaining capacity, and realizing that capacity into tangible results (Brown, 1998). The measures of sustainability according to Woller and Schreiner (2006) are operational self-sufficiency (OSS), financial self-sufficiency (FSS), and profitability (Natilson and Bruett, 2001). Operational self-sufficiency measures the capacity of microfinance banks to cover operating expenses, financing costs, and allowance for bad debts from operating revenues. Financial self-sufficiency measures the ability of microfinance banks to cover all direct and indirect costs without subsidies taking adjustments to operating income and expenses (Ledgerwood, 1999; Fisher and Sriranm, 2002; Barres, 2006). Financial self-sufficiency shows cost recovery regardless of size of operation and gives a quick synopsis of the general performance of the bank. It gives a clue on the sustainability of the bank considering the impact of subsidies into account. Relating to profitability, sustainability is an adjusted measure of profitability in an accounting sense, generally defined as the difference between total revenue generated by an organisation from its operations and the total associated costs.

The Role of Microfinance Banks as Financial Intermediaries

The search for a development strategy, which could lead to significant improvement in the socio-economic conditions of members of poor household, led to the focus on credit. Microfinance banks have made array of contributions, especially in poverty reduction and economic development of the country. For instance, the greatest constraint of small businesses and other actors in the informal sector is constrained access to affordable bank crisis. The existence of vibrant microfinance banks has sufficiently addressed the challenge. Microfinance banks provide credit on affordable conditions to enhance income-earning capacity of the beneficiaries.

Microfinance is foremost a poverty alleviation tool. Ehigiamusoe (2008) observed that the rapid spread of microfinance in developing countries is attributed to its capacity to impact positively on poverty alleviation. As observed by Morduch and Hoshemi (2003), sustainable access to micro finance helps alleviate poverty by generating income, creating jobs, allowing children to go to school, enabling families to obtain health care, and empowering people to make the choices that best serve their needs. He states further that the stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is savings, credit or insurance and the great challenge is to address the constraints that exclude people from full participation in the financial sector. According to him, micro finance should be one of the key driving mechanisms toward meeting the millenium development goals (MDGs).

Microfinance has also been demonstrated to have enormous capacity to boost economic development through support for micro, small and medium scale businesses. On a general note, injection of new funds on appropriate conditions into small businesses take them from the vicious cycle of small investment little returns small investment to the vicious cycle of prosperity of little capital-injection of funds (credit)-greater output greater investment. They provide micro-insurance service to the poor to assist them address the problem of vulnerability. Vulnerability is the bane of persons with limited means. Microfinance banks

provide the hedge against enormous risk faced by poor. Microfinance also involves in provision of cash transfer and micro investment.

Determinants of Microfinance Sustainability

There have been several determinants of microfinance banks sustainability in literature. Most of these determinants include: sources of funds; subsidies; governance; savings mobilization; average loan size; lending interest rate; repayment rates; delivery mechanism; cost of loan disbursement; age of the bank; ownership status; economic, social and political environments; population density and human capital development and level of inflation (Ledgerwood, 1999; Jensen, 2003). Sources and amount of funds available to microfinance banks have implications for outreach and sustainability. Indeed, a significant amount of literature on microfinance has placed much emphasis on the sources of funds as a major determinant of sustainability and outreach (Christen and Drake, 2002; Fernando, 2004; Chu, 2006; Ledgerwood and White, 2006).

Another factor that has been identified in the literature as one of determinants of sustainability and outreach is subsidy. Inboden (2005) states that most microfinance banks started as non-governmental organisation, hence external financial intervention was needed which normally come from both domestic and international political actors. Yunus (2002) observes that, Grameen Bank in Bangladesh was able to promote access to financial services for the poor to enhance their participation in productive activities mainly through donor support. Chaves and Gonzalez-Vega (1996) report that subsidies contributed to the success of rural finance bank in Indonesia. The bulk of funding for non-governmental organisations (NGOs) tends to come from donors in the form of grants or proceeds from concessionary loans (Chu and Otero, 2002). Greuning, Gallardo and Randhawa (1999) identify three broad types of microfinance banks according to their main sources of funds for operations and loans.

(i) those using member's money in the form of grants and donations, limited deposits, and concessionary and commercial borrowing;
(ii) those using people's money in the form of contributions and savings deposits; and
(iii) those using the public's money in the form of retail deposit, saving deposit wholesale funds and commercial borrowing.

The study of Chu (2006) corroborates the findings of Yunus (2002) and Chaves and Gonzalez-Vega (1996) that subsidies play a key role to re-orient and expand programmes of microfinance banks. In a recent study, conducted by Hudon and Traca (2008), on 138 microfinance banks operating in European countries, the study reveals that a high number of microfinance banks still depend on subsidies to achieve their outreach and sustainability goals. The researchers further argue that, the social objective of microfinance banks would be undermined if the bank is not subsidized.

A repayment rate is defined as that proportion of the loan lent out that is eventually recovered (Ledgerwood, 1999). The repayment rate is the inverse of the default rate. Either of the rates indicates the extent to which a microfinancebank is able to recover its loan portfolio. For example, a repayment rate of 100% or a default rate of 0% means that the microfinancebank can fully recover the money it lends out. Cull *et al.* (2006) observe that one of the remarkable developments in the microfinance industry across the world is the high repayment rates. In

this sense, microfinance banks often insist with their clients that repayment on time will guarantee future access to loans. They insist that arrears or default not only will force them to reject any future credit application, but that this behaviour may prevent delinquent borrowers from creating new credit relationship with other lenders. Similarly, population density and adequate infrastructure are other determinants of microfinance banks sustainability mentioned in the literature. Rhyne (2001) shows that, population density plays a positive role in microfinance banks, outreach and sustainability, which could explain why the sector is still underdeveloped in rural areas. With regard to an adequate infrastructure (that is good interconnectivity between regions, availability of electricity, communication and sanitation networks). The study of Schreiner and Colomber (2001) argue that, the absence of an adequate infrastructure plays a hindering role for the development and performance of microfinance banks. Moreover, Yaron and McDonald (1997) see the absence of good infrastructure and sparely populated settlements as some of the main factors hindering the microfinance banks outreach and sustainability goals due to high cost of transaction and monitoring.

Economic, social and political environment have been identified in the literature as another determinants of microfinance banks sustainability and outreach. Indeed, the viability of financial market depends on the economic viability of the clients it serves. Zeller and Sherma *(*1998) find that in most developing countries, and more especially in the agricultural sector, the capacity of the people to save and invest is very low mainly, because of low returns on the economic activities. Consequently, the demand for financial services is low, a situation that is often not improved by low, and sometimes inappropriate, investment in agriculture and other rural activities Different types of organisations provide microfinance services, including private, public, state and non-governmental organisation (NGOs). In addition, these banks use different lending technologies. Some studies reveal that microfinance banks that operate under bankist paradigm are more sustainable than those that operate under welfarist paradigm (Seibel and Perhusip, 1998; Ryne, 2000; Schadwinkel, 2000; Mommartz and Schor, 2002; Mog, 2004). Another microfinance banks sustainability and outreach determinant identified in the literature is the age of the bank. Natilson and Bruet (2001) identify maturity of the bank as one of the three key factors that influence the level of activities and operational costs. Others are turnover of loan portfolio and average loan size. Literature identitied information asymmetry as one major source of costs to the bank providing financial services. For example, Steel et al. (1997) argue that problems of imperfect information characterise low-income economies where economy-wide information flows are united and financial information is lacking or costly to obtain. Poor information systems raise the cost to formal banks of acquiring information on the clients.

A delivery mechanism can be defined as a bridge between a provider of a product/service and the recipient of the same (Yunus, 2002). It is widely documented that, the traditional financial banks in developing countries, have failed to adequately meet the demand for financial services by low-income earners and micro and small enterprises on account of underdeveloped financial market, information asymmetry, high cost of information gathering and lack of physical collateral (Robinson, 2001, Bose, 1997; Hoff and Stiglitz, 1990; Vaessen, 2001; Schreiner and Woller, 2003; Gine and Karlan, 2001). To a financial bank, lending interest rate is that rate charged to the bank when borrowing money or the rate the bank charges when lending money to its clients (Smithen, 2005). According to Ledgerwood (1999), three types of lending rates can be distinguished: nominal, effective and real. The nominal interest rate is usually explicitly quoted by a financial bank, while an effective lending rate

includes the nominal interest plus other charges that are directly associated with the loan granted.

Empirical evidence from literature suggests that, subsidized and directed credit programmes perform poorly, partly because their loans sizes are attractive to non-targeted clients. For example, figure from Bangladesh Rural Advancement Committee's 1995 impact study indicates that 10 percent of members were from non-target groups (Johnson and Rogaly, 1997). In Nigeria, the study of Obadah (2001) indicates lack of targeting mechanism for the poor and the fact that most of the programmes do not focus directly on the poor led to the failure of most government sponsored microfinance banks. The term saving is widely used to mean income not spent on consumption but put aside for future spending (Jensen, 2003). It is often assumed that savings arise from the surplus income available for current consumption. However, in most developing economies savings may not occur in the form of income not spent on current consumption, but on non-financial assets. Moreover, according to Robinson (2001), savings may not necessarily be the result of surplus income, but a genuine sacrifice of current consumption for either investment to produce goods and services for future consumption or for an unforeseen eventuality. If saving has occurred and is placed in a financial bank, it becomes a financial product offered by their financial bank.

McGuire (1999) observes that, as a microfinancebank reaches a larger number of clients, manages increasing volume of financial resources, borrows substantial amounts from financial markets, and starts to earn profit, governance becomes an important requirement. He further observes that what makes governance of microfinance banks different and more challenging than that of other types of banksare four unique attributes, namely: the dual mission of microfinance achieving profitability and maintaining a social objective; the ownership of microfinance banks; the fiduciary responsibility of the board; and risk assessment in microfinance banks. Most microfinance banks are promoted by non-governmental organisations (NGOs) with donor support and start with the social objective of reaching out to the poor.

THEORETICAL FRAMEWORK

The theoretical framework adopted for the paper involved the theory of the firm, the bank capital channel model and model of lending behaviour based on an agency framework. The theory of the firm addresses the issues of the existence, the boundaries and the internal organisation of the firm. The theory of the firm study the behaviour of firms in respect of: (i) the inputs they buy; (ii) the production techniques they adopt; (iii) the quantity they produce; and (iv) the price at which they sell their output. Understood in this manner, knowledge of the way firms behave is essential in determining such major variables as investment, employment of factor inputs, wages, and output levels and prices (Samuelson and Nordhaus, 1996).

The bank capital channel views change in interest rate as affecting lending through bank's capital, particularly when banks'lending is constrained by a capital adequacy requirement. Thus, an increase ininterest rates will raise the cost of banks' external funding, but reduce banks'profits and capital. The tendency is for the banks to reduce their supply of loans, if the capital constraint becomes binding. However, banks could also become more willing to lend during certain periods because of an improvement in their underlying financial condition. This

bank behaviour is explained by the capital constraint models. Basically, banks are subjected to both market and regulator imposed capital requirements. For prudential purposes, banks regulators generally require banks to maintain capital at not less than a stated fraction of the bank's total assets. For instance, banks are expected to meet the capital adequacy requirement of the Basel Accord of ten per cent. Also in Nigeria, banks are expected to maintain a minimum of 40 per cent liquidity ratio of total deposits. Thus, the ability of banks/microfinance banks to grant loans is constrained by the amount of financial resources at their command, based on the capital requirements.

The agency theory is concerned with how agency affects the form of the contract and the way they are minimized, particularly, when contracting parties are asymmetrically informed. Fundamentally, the problem arises because lenders are imperfectly informed about the characteristics of potential borrowers, and it may be impossible, as a result, for lenders to distinguish 'good' borrowers from 'bad' ones (Fraser, 2004). As observed by Akerlof (1970), and cited by Kitchen (1972), a systematic bias may arise in small and medium scale enterprises (SMEs) financing, because of the theory of the market for "lemons". Akerlof (1970) argues that small businesses, especially in developing countries, are regarded as "high-risk", and the level of risk associated with the riskiest small business tends to affect all small businesses. Therefore, the problem of information asymmetry highlights the importance of relationship between lenders and borrowers. As Fraser (2004) observes, longer and broader relationship increases the amount and the flow of information to lenders, enabling good borrowers to obtain better access to finance over time. Therefore, information asymmetries lead to sub-optimal flow of finance available to smaller firms compared to larger firms (Cook, 2001). The implication of the lack of adequate funding is that small and medium scale enterprises (SMEs) are caught up in a vicious cycle of low investment, low incomes, low profits and savings for investment.

EMPIRICAL LITERATURE

Many researchers has examined the sustainability of microfinance banks in developed and developing countries. Microfinance sustainability, having been examined at the institutional, group and individual levels, has been linked to organisational, managerial and financial levels. Empirical evidence on the sustainability of microfinance in literature is mixed across countries. MIX et al. (2006) cited in Ganesh (2010) conducted a study on sample of 101 Asian MFIs (from five countries, namely, Bangladesh, Cambodia, India, Philippines, and Pakistan) to assess their performance and identify challenges and opportunities facing them. The findings show that MFIs in Asia depend heavily on external funds to continue their expansion. In South East Asian countries, savings mobilization plays an important role in raising fund. MFIs in India secure significant quantities of debt in borrowing, as they are not allowed to mobilize savings. NGOs continue to depend on soft funds from public institutions (e.g., PKSF in Bangladesh).

Bogan (2009) investigated the optimal capital structure for MFIs, using panel data on MFIs in Africa, East Asia, Eastern Europe, Latin America, the Middle East and South Asia for the years 2003 and 2006. The results show that Africa has the highest percent of unsustainable MFIs (37.70%), the highest percent of portfolio at risk (7.02%), and the lowest average return on assets (0.43%). The East Asia and Pacific region has the lowest percent of unsustainable MFIs (6.56%). The Eastern Europe and Central Asia region has the highest return on assets (5.25%), the lowest percent of portfolio at risk (3.16%), and the highest average cost per

borrower (US$273.27). South Asia has the lowest average cost per borrower (US$36.31). Hulme and Mosley (1996) conducted a comprehensive study of 13 micro credit schemes in Asia, Africa and South America and found unanimously that the benefits of the micro credit schemes understudy were not scale neutral - the upper and middle income poor tended to benefit more than the poorest of the poor. Morduch (2000) found that Grameen model was able to reach poor borrowers but was not financially self-sufficient. According to Morduch, the bank reported profits of $1.5 million between 1985 and 1996; these profits depended on $16 million of direct grants, $81 million of implicit subsidies through soft loans, $47 million of implicit subsidies through equity holdings, and $27 million in delayed loan loss provisions. Parveen (2009) analyze sustainable development as well as performance of Rural Development Scheme (RDS) of Islamic Bank Bangladesh Limited (IBBL) using panel model. The empirical analysis of the study reveals that Rural Development Scheme (RDS) of Islamic Bank Bangladesh Limited (IBBL) has been sustainable in reaching very poor section of the society and also maximizes clients' welfare.

Oluyombo (2010) examined the effects of microfinance banks on rural development in Nigeria from 1992 to 2006. The study revealed a major downward trend in the value of credits to rural people compared to the deposits mobilized from them. It identified that there is a net outflow of finance from the rural poor, thereby jeopardizing the sustainable development of the rural areas. Using simple statistical tools, i.e. inferential statistics, the study found that, between 1992 – 2006, Nigerian microfinance banks gave larger percentage of their loans (i.e. 39 percent) to "other sectors", and only 9 percent was made available to rural people in agriculture and agricultural related businesses. This lopsided arrangement does not justify the basic reasons for the establishment of microfinance banks in the rural areas of Nigeria. However, Webster and Fidler (1995) and Bennett et al. (1996), cited in Ganesh (2010) have shown it is very difficult for MFIs in the world to achieve financial self-sufficiency, particularly if they have to serve the poor in remote, rural areas. There may be a justification for well-managed programs to receive some level of subsidy if they can be shown to be as effective as or more effective than alternative strategies to reduce poverty. For example, Khandker (1998) reported a cost-benefit ratio of 0.91 with respect to improvements in household consumption via borrowing by women from the Grameen Bank, compared to the ratio of 1.71 for the World Food Programme's Food-for-Work scheme, and 2.62 for CARE's similar program. However, this argument of selectively subsidizing MFIs to reach the poorest of the poor does not question the imperative for MFIs to achieve as high a degree of financial self-sufficiency as possible by reducing operational costs and charging market rates of interest. The higher the degree of self-sufficiency, the greater the extent to which an MFI can leverage donor and government funds to expand outreach.

MATERIALS AND METHOD

This study made use of both descriptive and econometric analysis. The econometric analysis is the generalized least squares method. This was specified to examine the determinants and trend of outreach of microfinance banks. The study adopted purposive and stratified sampling techniques. All the microfinance banks operating in Lagos and Ondo States chosen as the study area were considered as the study population. The selection was based on the concentration of microfinance banks in these states. For instance, Lagos State has the highest concentration of microfinance banks, 140 out of 720

microfinance banks operating in the country (Central Bank of Nigeria, 2010) and is an urban and industrial state. Also, the three-tier microfinance banks were present in the state. On the other hand Ondo State has 21 registered microfinance banks (Central Bank of Nigeria, 2010). Ondo State is an agrarian state, albeit, not having the lowest concentration of microfinance banks but has the present of three-tier microfinance banks. The total population of the study is 161 microfinance banks made up of 140 and 21 microfinance banks in Lagos and Ondo States respectively.

Source of Data

The study employed secondary data. The data were collected from the portfolio and savings registers, balance sheet and income statement of70 and 10 surveyed microfinance banks in Lagos and Ondo States respectively, for a period of six years from 2005-2010.

Model Specification

The general econometric model used for the paper, i.e. sustainability (OSS) is pool panel model. The model is specified as:

$$OSS_{it} = \alpha + X_{it}\beta_{it} + \delta_i + \gamma_t + \varepsilon_{it} \ldots\ldots 1$$

Where OSS_{it} is the dependent variable, $X`_{it}$ is a K-vector of regressors stated in equation 1 above, ε_{it} are the error terms for i=1, 2…M cross-sectional units observed for dated periods t=1, 2…T. The α parameter represents the overall constant of the model while δ_i and γ_t represent cross-section or period specific effects (random or fixed). However, to estimate the determinants of sustainability of microfinancebank, the following panel model is specified:

$$\begin{aligned} InOSS_{it} = {} & \alpha + \beta_1 InDER_{it} + \beta_2 InTA_{it} + \beta_3 InWL_{it} + \beta_4 InALz_{it} \\ & + \beta_5 LDM_{it} + \beta_6 InLRR_{it} + \beta_7 OS_{it} + \beta_8 InCLD_{it} + \beta_9 SP_{it} \\ & + \beta_{10} InRELR_{it} + \beta_{11} InAGE_{it} + \varphi_i + \psi_t + \varepsilon_{it} \ldots\ldots 2 \end{aligned}$$

Where α parameter represents the overall constant of the model while φ_i and ψ_t represent cross-section or period specific effects (random or fixed), α_1-$\alpha_{11}$are estimated parameters which represent the coefficients of all the estimated variables, OSS= Operational sustainability measures, DER = Debt-equity Ratio, GM = Management skill proxy with Value of Total Assets (TA), SP = Providing savings product (SP takes the value 1 if the microfinance banks provides savings product and O, if does not), WL = Salary/wages and benefit of staff, RELR = Real effective lending interest rate, ALZ = Average loan size, LDM = Loan delivery method (LDM is a dummy which takes the value 1 if the dominant delivery mechanism is group-based lending and 0 if otherwise), LRR = Loan repayment rate, OS = Ownership status (OS is a dummy which take value 1 if microfinancebank is privately owned and 0 if otherwise), CLD = Cost of loan disbursed, AGE = Age of the microfinance banks, ε_{it} are the error terms for i=1, 2…M cross-sectional units observed for dated periods t=1,2,…T.

Given the assumed relationship, based on apriori reasoning between sustainability (OSS) and the various determinants, the expected sign for the parameter estimates are α1, α2, α7, α8, α9 >0, while α3, α4, α5, α6 are expected to < 0. Thus, positive relationships are

expected between debt-equity ratio, management skill, loan repayment rate, cost of loan disbursed, age of the microfinance banks and sustainability, which implies that the higher the explanatory variables, the higher the sustainability (OSS). However, negative relationships are expected between provision of savings product, salary/wages, real effective lending interest rate, average loan size, loan delivery method and sustainability, meaning that the higher the variables, the lower the sustainability (OSS) of microfinance banks.

RESULTS

Table 1. Result of Trend of Microfinance banks' Sustainability (OSS) in Southwestern Nigeria

Dependent Variable: OSS

Explanatory Variable	GLS
Constant	-1.12811
	(0.00001)
Trend	0.31736
	(0.00001)
No of observation	417
Number of groups	80
Time series length: Min.	3
Max.	6
'Within' Variance	2.26173
'Between' Variance	0.212318

Source: Data Analysis

Table 2. Result of Random-Effects Model for Sustainability (OSS) estimated
Dependent Variable: OSS

Expl. Variable	GLS 1	GLS 2	GLS 3
CONST	-3.0943	-3.1810	-3.3500
	(0.0015)	(0.0004)	(0.00016)
RELR	0.1881	0.1939	0.1947
	(0.01)	(0.00001)	(0.00001)
LDMg	-0.5508	-0.5844	-0.5497
	(0.0012)	(0.0006)	(0.00104)
LALZ	0.2942	0.3793	0.3749
	(0.0034)	(0.00001)	(0.00001)
LCLD	-0.2340	-0.2328	-0.2239
	(0.01)	(0.00001)	(0.00001)
LDER	0.3431	0.3582	0.3714
	(0.01)	(0.00001)	(0.00001)
LWL	0.0578		
	(0.2297)		
LSP	0.1661		
	(0.2188)		
LTA	-0.0938		
	(0.5786)		
LAGE	0.3391	0.3265	0.3374
	(0.0420)	(0.0351)	(0.0386)
LRR	0.0094	0.0102	0.0102
	(0.0045)	(0.0018)	(0.00177)
OS	-0.1012	-0.0866	
	(0.0967)	(0.1474)	
No of observations	431	431	431
Number of groups	80	80	80
R-Sq: Within	0.568	0.566	0.577
Between	0.081	0.081	0.081
Breusch-Pagan Test:			
Chi-square	0.712	0.461	0.789
Hausman Test:			
Chi-square	23.549	22.602	18.533

Source: Author's Calculation

Therefore, the OSS model for microfinance banks in Southwestern Nigeria's for the period 2005 to 2010 can be specified as (in parentheses are p-values)

LOSS = 3.3500 + 0.91947 RELR – 0.5497 LDM + 0.3749 LAIZ – 0.2239 LCD + 0.3714 LDER + 0.3374 LAGE + 0.0102 LRR
(0.00016) (0.0001) (0.00104) (0.00001) (0.00001) (0.00001) (0.00001) (0.00177) ……………………………………… 3

DISCUSSION OF RESULTS

The result in Table 1 shows the trend of Microfinance Banks' Sustainability (OSS) in Southwestern Nigeria. The probability statistics of the trend statistics is significant at 5 percent level, indicates that there has been an increase in the trends of sustainability of the sampled microfinance banks in Southwestern Nigeria in the periods under this study. Table 2 shows the result of random-effects model for sustainability (oss) estimated in Southwestern Nigeria. The panel data estimation under the Random-Effect (RE) log-Linear Generalized least squares (GLS) model reveals that seven explanatory variables are statistically significant (in parenthesis are p-values). These explanatory variables are the real effective lending rates (RELR), the loan delivery methods (LDMg), the loan repayment rates (LRR), the average loan size (LALZ), the cost of loan delivery (LCLD), the debt equity ratio

(LDER) and age of the microfinance bank (AGE) are significant at 5% level. With the exception of real effective lending rates and loan delivery method the coefficients of the other statistically significant variables have the expected signs. The positive sign of loan repayment rates (LRR) is in tandem with the findings of Oke, Adeyemo and Agbonlahor (2007) which argue that the high repayment rates recorded by NGOs microfinance banks in Nigeria contributed significantly to their success.

Moreover, the result in Table 2 shows that loan delivery method is negatively related with sustainability with coefficient value of -0.5508. Although, this coefficient has counter-theoretical sign, the negative coefficient could be explained by the fact that group formation is a difficult process and most microfinance banks in Nigeria preferred individual lending methodology for easy processing of credits. This is also plausible in Nigeria with the fact that individual lending methodology offers dynamic incentives, regular repayment schedules and collateral substitutes to help maintain high repayment rates. This result, supports the findings of Gonzalez-Vega (2003), that individual lenders are more robust along the business cycle and lead to better long-term repayment records, because they can avoid better the covariance of the members' returns.

Generally, as can be seen from the results in Table 2, sustainability (OSS) of the studied microfinance banks in Southwestern Nigeria is driven significantly by the debt equity ratio (DER), the average loan size (ALZ), the real effective lending rates (RELR), the unit cost of loans disbursed (LCLD), the loan repayment rates (LRR), loan delivery methods (LDMg) and the age of the microfinancebank (LAGE). Based on the level of statistical significance, the real effective lending rates (RELR), the loan delivery method (LDMg), the debt equity ratio (LDER), the average loan size (LALZ), the cost of loan delivery (LCLD) and age of the microfinancebank (AGE) are highly important, while loan repayment rates (LRR) is moderately important. This implies that for microfinance banks to improve their sustainability, they must put emphasis on the identified determinants.

To further investigate the relevant explanatory variables in the OSS model, a stepwise regression approach was adopted. This procedure was followed until the final model considered to be explaining sustainability of microfinance banks in Southwestern Nigeria was arrived at (see equation 3). The finding reveals that cost of loan delivery (LCLD) is negatively related with sustainability. The results is consistent with the study of Steel *et al*. (1997) which argues that cost of loan disbursed reduces the net income of microfinance banks and hence the sustainability of the bank. The result also shows that age of the microfinance bank is positively related with sustainability and is significant at 5% with positive coefficient of 0.3374. The result indicates that the age of an bank affects sustainability through accumulated experience from learning by doing. Overall, the result indicates that poor sustainability precipitated the microfinance banks in Southwestern Nigeria.

CONCLUSION AND RECOMMENDATIONS

From the analysis above, the study reveales that there has been an increase in the trends of sustainability of the sampled microfinance banks for the study period. However, the main core area of the rural people (agriculture) was neglected for the six years period because loan and advances to agriculture occupies the fourth position and represents less than ten percent of the total loans disbursed. The findings

further indicate that outreach is driven by the debt equity ratio (DER), the average loan size (ALZ), the real effective lending rates (RELR), the unit cost of loans disbursed (LCLD), the loan repayment rates (LRR), loan delivery methods (LDMg) and the age of the microfinancebank (LAGE). Based on the contribution to the proportional change in the variations in sustainability (OSS), loan delivery method (LDMg) and average loan size (LALZ) are the most important determinants of sustainability, followed by the amount of funds available to the microfinancebank.

The findings suggest that for microfinance banks to improve their sustainability, they must put emphasis on the identified determinants starting with loan delivery method and average loan size followed by debt-equity capital.Microfinance banks should focus on the real effective lending rates for improved sustainability. This recommendation thus calls on the Central Bank of Nigeria, not only to maintain market-based interest rates policies but also, to continue with the current strategy of keeping inflation rate low through prudent fiscal and monetary policy management. Also, since sustainability is usually an outcome of a strong governance structure, microfinance banks should strengthen the governance structure to achieve the sustainability objective, outreach will be achieved simultaneously. The Central Bank Nigeria also needs to promote consumer education to empower potential clients to identify efficient and sustainable microfinance banks, and negotiate for better interest rates. Accordingly, it is imperative that appropriate policies, legal regimes and infrastructure be put in place to reduce the cost of doing business for the microfinance banks. The high priority placed by the government on energy and infrastructural development as well as information, communication and technology is an important policy strategy that will benefit all the sectors of the Nigerian economy including the microfinance industry.

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Chapter 9

THE PERFORMANCE OF MICROFINANCE BANKS IN FINANCING AGRICULTURAL COOPERATIVE SOCIETIES IN RURAL NIGERIA

Charles Uchenna **ONUGU**

INTRODUCTION

The importance of agriculture to economic growth and development cannot be over-emphasized. Agriculture is the backbone of the rural economy at least providing by far the largest source of rural employment and also the mainstay of the majority of households in Nigeria (World Bank 2006; Ekundayo, 2008). The National Bureau of Statistics (NBS) stated that the environment of agricultural sector in Nigeria is such that 60% - 70% of the population is engaged in agriculture related activities and that small-holder farmers constitutes 80% of all farm holdings (NBS, 2008). This distribution implies that financing smallholder farmer needs to take pre-eminence in Nigerian agriculture. The benefit of the agricultural sector to Nigeria economy include: the provision of food to feed the teeming population, provision of income for particularly the rural dwellers, contribute to the nations Gross Domestic Product (GDP), provision of employment, and provision of raw-material for agro-allied industries and generation of foreign earnings. These aforementioned benefits make it imperative that funding of the agricultural sector is essential for overall national growth, poverty reduction and food security. Agricultural sector in Nigeria are predominantly occupied by peasant farmers who produce primarily for their personal use and the excess, which they sell to earn income. The lack of capital is largely a constraint in the advancement from subsistence to commercial agriculture (ljere, 1992). These peasant farmers therefore come together to form agricultural cooperative societies in order to achieve what they could not do as individual such as input supply, product distribution, processing and marketing (Umebali, 2006).

Agriculture Cooperative Societies have been used over the years as a veritable instrument to achieve increase in the food production and also to improve the living standard of the rural populace. Ijere (1988) noted that Agricultural Cooperative business provides suitable channel for the delivery of input and other services to a multitude of small scale farmers and also small scale entrepreneurs whose economies are interwoven with the farmers. Resources are pooled together by these cooperatives members who have easier access to credit than individual farmers. Collectively they procure equipment, machineries, improved seed and animal varieties and also agro- chemical etc. Agricultural Cooperative societies are still facing difficulties in financing some of their agro-project, due to inadequate capital because the contribution from their earnings is minimal. Okorie (1991) opined that banks see agricultural

enterprises as very risky ventures in which they should not commit depositor's fund. Beside these, the difficulties acquiring land especially in the south-eastern part of Nigeria and inadequate infrastructure constitute a hindrance to Agricultural Cooperatives.

According to Umebali (2006), in Nigeria effort have been intensified in order to improve the agricultural production by the government by establishing various programmes ranging from Agricultural Development Projects (ADP), Agricultural Credit Support Scheme (ACSS), Operation Feed the Nation (OFN) and others. World Bank (2005) had reported that on-lending schemes to agricultural cooperative operated by most levels of government in Nigerian had only tended to increase level of loan disbursement but failed to achieve adequate level of loan repayment and as a result proved unsustainable. Although the program resulted into increase in level of credit disbursement and gains in agricultural production and other activities, the effect were short lived due to the unsustainable nature of the programmes. The failure of the programmes to achieve the desired result (Ketu, 2008) led to the emergence of Microfinance Banks (MFBs) which are aimed at extending micro credit to micro enterprises and encouraging Micro entrepreneurs especially in semi-urban and rural-areas. Micro Finance Banks are institution constructed as a company licensed to carry out business of improving financial services, such as Micro-Saving and other deposit instrument, micro credit provision, micro leasing, money transfer and payment services to particularly the active poor and group such as cooperative societies who are not served by conventional financial institution (CBN 2005). Micro Finance Banks gives out small loans to the active poor in developing countries to allow them improve their business without having to pay unmanageable interest rate and also provide non-financial services that will enable them expand their agricultural and non-agricultural project which help to enhance their income level and hence, reducing poverty. Government enters into partnership with Micro Finance Banks to raise bank loan to be disbursed to the beneficiaries. In so doing, the bank are increasing and sustaining the numbers of people going into small scale businesses. Micro Finance Banks according to (Ketu, 2008) has been a key factor that contributed immensely to the development of agricultural Cooperative societies in Nigeria, African and the word at large.

Statement of Problem

Agricultural Cooperative Society has been encouraged among Nigeria farmers as a measure to curb poverty and hunger in the society. There is no doubt that agricultural cooperative have tremendously contributed to the economic growth in Nigeria. It is expected, that cooperative business will help farmers pool resources together to increase production, to generate more income and improve their living standard. But today, the reverse is the case; there is a wide gap between the demand and supply of food in the country as the prices of local food item have continued to rise in the market beyond the reach of the common man (Mba, 2008). This Agricultural Cooperative Societies are facing difficulties among which finance is the *major* factor militating against enhanced production (Ugbajah and Orji, 2006). Umebali (2006) support this view further by stating that agricultural product in Nigeria is faced with numerous problems including poor financial status of the farmer, inadequate agricultural education and extension services, high incidence of disease and pest, lack of mechanization etc. This inadequate capital and poor financial management have led to the demise of many cooperative societies including agricultural cooperative.

Agricultural cooperative needs finance to boast their production and be able to finance their activities. Many attempts have been made to address the challenge of Agricultural finance in

Nigeria. CBN (1986), in a study conducted identified shortage of primary production credit as one of the major causes of declining agricultural production. This shortage was attributed to reluctance by the banks to provide credit for real sector activities, especially agricultural production. The reason for the reluctance were inherent risks associated with agricultural production, high cost of administration of agricultural loans and inability of farmers to provide the necessary collateral. This prompted the establishment of rural banking scheme, agricultural credit guarantee scheme, the Community Bank among others (CBN, 2005). The un-sustainability of such programmes has caused government in December 2005, through CBN to review their operations in order to ensure sustainability. The CBN hence demanded that community banks be converted to Micro Finance Banks and the capital base be increased from ₦5million to ₦20million by the end of 2007. This enable the Micro Finance Banks have adequate fund to operate and reach the vast needs of the micro enterprises and rural poor in terms of deposit mobilization and credit provision.

In spite of government effort to finance Agricultural Cooperative Societies and micro enterprises in rural areas, the impact of these banks have not been adequately felt by the target group (USAID, 2005). This is as a result of some constraints which include inadequate experienced credit staff, internal control challenges, economic and political instability, illiteracy of client, inadequate financing facilities, insufficient information on awareness creation, poor infrastructural facilities among others that have impaired the effective operations of MFBs in delivering its mandate to the rural dweller and micro enterprises (Owuala, 2002). The challenge of this study is whether micro finance banks indeed finance agricultural cooperative societies and if they do, how adequate are the loans provided to the societies? Equally, to what extent has micro finance banks fund helped in enhancing the activities of agricultural cooperative societies? Do the micro finance banks, render non-financial service to support agricultural cooperative societies? What are the opinions of cooperative members on the performance of micro finance banks in financing their activities? What challenges pervades in financing agricultural cooperative societies and what remedies are available for strengthening the effective finance of agricultural cooperative societies in Nigeria?

Objective of The Study

The general objective of the study is to appraise the performance of microfinance banks in financing agricultural cooperative societies in rural Nigeria, with focus on Anambra state. The specific objectives are to:

i. Identify the source of fund of the agricultural cooperative societies in Anambra state.
ii. Ascertain the financial and non-financial products available in microfinance banks for agricultural cooperative societies.
iii. Find out if the microfinance banks do finance the activities of the agricultural cooperative societies.
iv. Ascertain whether credit provided by microfinance banks are adequate and if it did enhance the performance of the agricultural cooperative societies.
v. Examine the challenges of financing agricultural cooperative societies by microfinance banks.

LITERATURE REVIEW

Cooperative has long been one of the platforms in the drive to make the rural areas functional economically and socially. Most communities are today populated with various types of cooperative societies engaged in both group as well as supporting individual activities. Cooperative as described by ILO (1986), is an association of human beings who have voluntarily come together and agreed to work collectively at their common risk and with resources contributed by all towards an improvement of common socio-economic interest, which working singularly they cannot achieve. Also, ICA (1995) captures the concept of cooperative as the autonomous association of person united voluntarily to meet their economic, social and cultural needs and aspirations through jointly owned and democratically controlled enterprises. Equally, Okoli (2006) saw cooperative as a free and voluntary organisation jointly owned by people with identical economic needs and having equal voices in its management and deriving proportionate service and benefit from it. Onuoha (1998), identified the basic concept of cooperative as enunciated in its principles set by the International Cooperative Alliance (ICA) review 1995 as: Open and voluntary membership. Democratic member participation. Member economic participation. Autonomy and independence. Education, training and information. Cooperation among cooperative. Concern for community.

Different types of cooperative societies abound most common among them are; agriculture, thrift and credit, consumer, housing, marketing, transport insurance and multipurpose cooperative societies. However, the Nigeria cooperative movement is composed largely of agricultural cooperative, (ljere, 1992). The reason is not far-fetched when one realizes that most of its population earns their living from Agriculture. This has led to the formation of cooperative in the agricultural sub-sectors of crops and animal production, processing and marketing, fishery and forestry. According to Ihimodu (1988), cooperative is a vital framework for solving many rural problems. In the rural area were civilization and development facilities are low, the impact of cooperative societies can be enormous. The areas of impact include the following among others; Mobilization of saving, provision credit, expansion of cultivated land area mechanization, increasing output, supply of inputs, marketing of farm products, provision of raw material to industries, improved level of income as well as standard of living. Cooperatives offer excellent opportunity for both individual and group economic empowerment.

According to ILO (2007), over 100 million jobs have been generated by cooperative around the world. Agriculture remains the major source of income and employment in rural area and majority of cooperative are found in the sector. Cooperatives are therefore significance in providing jobs to rural communities. They tend to be vital providers of easier financial services. So far, cooperative societies in Nigeria are plagued with challenges, which have affected its optimal performance in economic development. These challenges include; dishonesty among society's officials, mismanagement, lack of finance, inadequate infrastructure facilities, government interference, lack of cooperation and technical education, lack of member loyalty, lack of regular inspection of cooperative society, (Onugu and Uneze, 2008). In spite of this, cooperative societies are playing relevant roles in community development and self help project (Berko, 2010).

Agricultural Cooperatives and Importance to Nigeria Economy

Agriculture is an important sector of the Nigerian economy, being particularly important in the area of employment generation, export earning and contribution to its Gross Domestic Products (Olayemi and Akinyosoye, 1989). A sectoral analysis in 2006 of the real Gross Domestic Product (GDP), indicated that agricultural sector in Nigeria contributed to about 42 percent of the GDP (World Bank, 2006). Though the growth rate in the agricultural sector in Nigeria increased from an average of about 3 percent in the 1990's to about 7 percent in 2000. The food security status of Nigeria continues to decline (Adeoti, 2002). Indeed, over the past two decades, agricultural yield have stayed the same or declined (Philips, Nkong, Pender and Dim, 2008).

Agriculture cooperatives come in as a key organisation in supporting and strengthening the productivity of small holder farmers who dominate the agricultural sector in Nigeria. According to Onwuchekwa (1985), agricultural cooperatives are those types of cooperatives organized fundamentally to assist member farmers in rural areas to improve their productive and marketing activities. Staatz (1987) describes agricultural cooperatives as a business with farmers as stakeholders and major users of the firm services, having a democratically structured governance and with it net margins distributed to these stakeholders in proportion to their patronage rather than their equity participation in the firm. Following cooperative doctrine, Agricultural cooperatives can be defined as an autonomous association of persons united voluntarily to meet their economic, social and cultural needs and aspirations through jointly owned and/or individually controlled agricultural enterprise. They are societies that are essentially agricultural and/or agricultural related enterprises owned and democratically controlled by their members with the aim of achieving mutually agreed socio-economic goals in accordance to cooperative value and principles. The fundamental functions of agricultural cooperative include agricultural input supply, storage of farmer produce, processing of produce, bulking up, marketing, provision of credit, training and member education. Agricultural cooperatives are formed in different types. They include rice farmers cooperative societies, group farming cooperative society, arable farming cooperative society, farm settlement cooperative society, livestock farmers cooperative society, agricultural cooperative credit and marketing society, fishermen multipurpose cooperative society and village multipurpose agricultural cooperative society (Ijere, 1992). Equally, Okechukwu (2006) highlighted four groups of cooperatives that can be formed under the agricultural sector to include farmer production cooperative, forestry cooperative, livestock cooperative and fishery cooperative.

Agricultural cooperatives in Nigeria have played key roles in its economic development through championing farmers productivity in the abovementioned area. Bob-Igwe and Ugwuanyi (2006) cited the land acquisition and utilization cooperatives as witnessed in the farm settlement as well as the esthwile National Land Development Authority (NALDA) as success stories. The effectiveness of the Bauchi State Cooperative Finance Agency (BSCFA), in its micro-lending and agro-input supply, programme according to Abubakar Umar (1986) is worth noteing. A commonly cited advantage of agricultural cooperative is their ability to reduce the variability of farmers income through polling of growers returns and expenses across products, time and space (Staatz, 1987). The formation and registration of agricultural cooperative has been encouraged by government. This in the words of Uneze (2011), is because of their increasing use in agriculture and rural development programmes of the

country. Ijere (1992), had earlier noted the extensive use of agricultural cooperative in River Basin Development Authority (RBDA); state-wide Agricultural Development Programme (ADPs); Family Economic Advancement Programme (FEA) as well as individuals and partnerships operating with billions of naira in Nigeria. In recent times as observed by Uneze (2011), the World Bank Fadama Development Program, National Poverty Eradication Programme (NAPEP), Federal Government Agricultural Credit support schemes under the Bank of Agriculture (BOA) are current programs in Nigeria that have utilized agricultural cooperatives as agency for delivering their economic mandates.

Microfinance and Role in Meeting the Financial Needs of Agricultural Cooperative Societies

Microfinance is the provision of financial services to the poor and low income household without access to formal financial institution (Anyanwu, 2005). The microfinance revolution evolved out of the failure of mostly government directed agricultural credit in reaching the poor. The semiformal microfinance providers, particularly the Non-Governmental Organisations (NGOs), credit unions and cooperatives emerged, targeting the unbanked poor. According to Nagarajan and Meyer (2005), the Microfinance Institutions (MFls) eventually revolutionized traditional views by showing that the poor are bankable, but that the conventional approach fails to serve them. Indeed, the MFls modified the informal lending services found in rural and urban areas with respect to interest rates, collateral and collection methods. The strength and success of microfinance as emphasized by Ledgerwood (2002), Ehigiamusue (2005) and CBN (2011) lies on its services which involve: Small loans, Informal approval of borrowers and investment, Collateral substitutes, Access to repeat and larger loans depending on the repayment performance, Streamline loan disbursement and monitoring, Demand-driven and varied financial services, Secure savings products, Effective outreach.

The Nigerian government in attempt to enhance flow of financial services to the rural areas, has in the past initiated several publicity-financed rural credit programmes mainly directed to the agricultural sector and non-farm activities. Among such programmes are the Rural Banking Scheme (RBS), sectoral allocation of credit, concessionary interest rate; and the Agricultural Credit Guarantee Scheme (ACGS). There were also institutional establishments such as the Nigerian Agricultural cooperative and Rural Development Bank (NACRDB) now re-named Bank of Agriculture (BOA); the community Bank as well as the National Poverty Eradication Programme (NAPEP). Though there was evidence of growth in credit provision and gains in agricultural production as well as other economic activities, the effects wee short-lived, due to the unsustainable nature of the programme (World Bank, 2005).

Since the 1980s, microfinance institutions, particularly the credit administered NGO's have emerged in Nigeria to pivot the support of micro and rural entrepreneurs. Notable amongs them are Country Women Association of Nigeria (COWAN) in Ondo state, Community Development Trust Fund (CDTF) in Lagos state, Farmers Development Union (FADU) in Oyo State, Women Farmers Association (WOFA) in Kano state, Development Exchange centre (DEC) in Enugu State and Life Above Poverty Organisation (LAPO) in Edo State.

By the end of 2007, COWAN and LAPO, the two largest NGO's reported loan portfolio of ₦2.2 million and ₦2 billion respectively. Alltogether, the active lending NGO's had ₦4 billion in portfolio with 550,000 credit clients, with average loan balance ranging from

₦1300-₦15,000 (Isern, Akpakoba; Flaming; Mantilla; Pellegrini and Taranzi, 2009). The approval and success of the MFls according to Uneze (2011), has generated the need for the Nigeria government through the Central Bank of Nigeria (CBN) in 2005 to develop a National Microfinance Policy Framework. The policy targets as stated by CBN (2005) are:

- To cover the majority of the poor but economically active population by 2020 thereby creating millions of jobs and reducing poverty.
- To increase the share of micro credit as percentage of total credit to the economy from 0.9 percent in 2005 to at least 20 percent in 2020, and the share of microcredit as percentage of GDP from 0.2 percent in 2005 to at least 5 percent in 2020.
- To promote the participation of at least two third of states and local governments in micro credit financing by 2015.
- To eliminate gender disparity by improving women's access to financial services by 5% annually and

To increase the number of linkages among universal banks, development banks, specialized finance institutions and microfinance banks by 10% annually.

The licensing and operation of Micro Finance Banks in Nigeria commenced in 2007 for the purpose of providing financial services to the economically active poor and low income earners to help them start or expand income generating activities. Micro Finance Banks since then, has played an important role in financing agricultural cooperative society. Ketu (2008) observed that MFBs here disbursed more than ₦800 million micro credits to over, 13,000 farmers across the country to empower their product capacities which will increase the output of the farmer and improving the farm capacity. Micro Finance Banks have been an intermediation between the government and also the foreign investor to reach the farmers. They make fund available through the Micro Finance Bank and these fund is available to the farmer that join a recognized cooperative society. This fund help the farmers have access to modern farm inputs like quality seeds and fertilizers, processing equipment which help the farmers to improve their efficiency, output and add value to their products.

METHODOLOGY

Anambra State, the area of the study is one of the thirty six (36) states of Nigeria. It was created on 27th August, 1991 and comprise of twenty one (21) local government areas. The total population of the state is estimated at four million, fifty thousand and forty eight (4,055,048) according to the 2006 census (NPC, 2006). The predominant occupations in the state are farming, trading and public service. The cultural and political background of the people of the state is decentralized as each community has its own traditional ruler; "Igwe" and his council of chiefs, cultural practices and festivities. The people are predominantly Christian, with few traditionalist (pagans). There are about eighty six (86) licensed MFBs in Anambra state and about seventy percent (70%) are rural based. The rural based MFBs, based on researcher interaction with operators of the banks, have an average of ten (10) farmers cooperative societies (NAMB, 2011).

With about seventy percent (70%) of the eighty-six (86) MFBs in Anambra State rural based, it translates to a population of sixty (60) MFBs. Employing a judgmental method in determining the sample size, it translates to eighteen (18) MFBs at twenty (20%) of the population. To determine the sample size of the Agricultural societies at twenty (20%),

translates to one hundred and twenty (120). To ensure a representation of the state, the study was designed to draw sample based on the three (3) geo-political divides of the state; Anambra North, Anambra central and Anambra South senatorial zones. With this in mind, six (6) MFBs and forty (40) Agricultural cooperative societies were drawn respectively from each of the zones. A structured questionnaire was the major instrument used for data collection. Institutional information from each of the 18 MFBs were provided by the Managing Directors and Head of credit Administration of the banks. For the ACSs, the data was sourced through 'group-focused' interview guided by the questionnaire. Their leaders (president, secretary, a committee members) represented each of the agricultural cooperative societies. To effectively collect the data, the researcher trained three (3) of his final year students in the department as enumerators. Each of the enumerators covered a geo-political (senatorial) zone of the state. The Managing Directors of the MFBs assisted in arranging group-focused interviews with the ACSs. Data collected from the questionnaire were arranged in a tabular and itemized according to the response sought from the respondents. Descriptive statistical tools (means, likert-scale, simple and multiple percentages) were the instrument used for data analysis.

RESULT AND DISCUSSIONS

Sources of Financing the Activities of Agricultural Cooperative Societies

Each of the one hundred and twenty (120) Agricultural Cooperative Societies were asked to state their sources of financing their farm activities. From the result (Table 1), there are nine (9) sources of internally generating funds, however, three (3) of such source are important. They include share capital contribution (41.6%); annual reserve (20.8%) from gross profit, and through their Thrift and Savings (16.7%). Also, the table showed that they raise funds through external sources; commercial banks (8.3%), MFBs (69.2%); Government grants (12.5%); and Trade credit (10%). Based on the researcher interaction at the focused-group interview, microfinance banks because of their rooting in the communities are very vital to the financial needs of the societies.

Financial Products Available For Agricultural Cooperative Societies

The operators of the MFBs represented by the Managing Director and Head of Credit were asked to indicate the financial products they have for Agricultural cooperative societies. As shown in table 2, though six (6) products, were listed, but four (4) stands out. They include; Savings Accounts (100%), Current Account (100%), Fixed Deposit Account (100%) and, Microcredit (100%). Further interaction in course of the research reveals that within some of the products, particularly savings accounts, that there are sub-products, targeted at ACSs such as group savings and group credit products. Micro leasing products though not very pronounced is found among MFBs located in key agricultural communities of the state, such as Aguleri and Ogbaru areas where the banks lease tractors to Agricultural cooperative societies. The cost of this service is either paid outright to the MFBs or incorporated as part of the credit provided by the bank to the societies. The micro insurance where only 3 of the MFBs are involved are done in collaboration with private insurance companies, as well as the Nigeria Agricultural Insurance Cooperation (NAIC); a government parastatal.

Non-Financial Products Available for Agricultural Cooperative Societies

An often-neglected element of credit administration is support services, which are non-financial but are important in enhancing the effective utilization of credit facilities from banks. In line with this, the researcher sort to ascertain if such product exists in the MFBs. The operators were therefore asked to identify from the list of such products contained in the questionnaire the ones provided by their banks. Based on their multiple responses (Table 3), it can be stated that the only meaningful non-financial service rendered to ACSs are financial advisory services (7.5%) monitoring and supervision (10.8). Further inquiry by the researcher reveals that even the monitoring and supervision is mere visitation to remind or demand for loan repayment.

Financing of Agricultural Cooperative Societies

In accessing financing of agricultural cooperative societies by MFBs, the researcher sought to find out the number of times in the last five (5) years the ACSs got credit from the banks. The study also determined the highest amount of loan accessed as well as the ease at which they access credit from the MFBs. As indicated in Table 4, most (83%) of the ACSs have collected loans for between 1-3 times, while the rest (17%) got between 4-6 times. The average number of times in last 5 years was found to be 3. It was also found that the highest amount of credit obtained by ACSs (Table 5) are mostly between ₦51,00- ₦100,000 (29.2%) and ₦101,000-₦ 300,000 (39.2%). The average highest credit given to the societies in the last 5 years stood at ₦260,708.3. This implies that the group credit availed to the ACSs which they share among their members are indeed microcredit in form. Finally, table 6 revealed most (68.4%) of the ACSs certifying their access to finance in the last five years from the microfinance banks.

Performance of The MFBs In Promoting Business Activities of The Agricultural Cooperative Societies

The opinions of the ACSs on how credit facilities obtained from the MFBs had promoted their business activities were sought. Table 7 indicated majority (70%) agreeing that it was either very adequate or just adequate. When asked if the credit enhanced their farming-activities, 43(35.9%) were in affirmative, while the rest 77(64.1%) were not (Table 8). What this implies is that there is most likely a missing service-function between the availability of adequate funds from the MFBs and its effective utilization to advance the farming-activities of the ACSs. This missing-gap could be traced to weakness in supporting the societies through non-financial services by the MFBs.

Challenges of Financing Agricultural Cooperative Societies

A list of possible challenges of financing Agricultural Cooperative Societies were presented to both their leaders and operators of microfinance banks. Their multiple responses are as represented in table 9. From the result, there are fourteen (14) of such challenges. However, prominent among the challenges include: poor monitoring/supervision of Loanees (96%); weak organisation/leadership of ACSs (94%); High interest on loan (94%); insufficient fund (89%), non/poor training of ACSs (88%); and inadequate credit staff (67%). Beyond the high interest on loan and insufficient fund, the rest of the challenges identified are traceable to non-

existence or very poor regards to implementing non-financial services from the MFBs. That would have ensured that the ACSs are well organised and managed to utilize credit profitably and be able to pay back.

CONCLUSIONS AND RECOMMENDATIONS

Nigeria agriculture has degenerated to such an extent that food security has become a serious treat and hence a topical issue. This is happening inspite of the nations enormous agricultural resources and a large population of small-holder farmers. Agriculture is very vital to the growth of any nations economy particularly in Sub-Saharan Africa where if well developed should account for massive employment, productivity and growth of our economy. Nigeria agricultural is indeed in a bad state and need revamping. Whatever policy initiatives and actions must focus on the small-holder farmers otherwise it will fail as others. Financing and expanding their farm-holdings is important and that is where reaching them through the group platform is important.

This study has revealed that the main sources of financing of the activities of the agricultural cooperative societies in Anambra State are through their share – capital, annual reserve, thrift and savings, as well as microfinance banks. It must be emphasized here that considering the large number of Microfinance banks in the country, its spread and rooting in the communities, that these factors should be seen as an advantage. Particularly of interest are the financial products of the MFBs, microcredit, micro lease and micro insurance. Even though microcredit appears to be the well established in the banks, products like micro lease of farm machines and tractors as well as micro insurance should be developed and promoted amongst microfinance banks in the country. The biggest challenges of financing small-holder farmers as revealed in this study is the non-recognition of the development component of credit administration; that is through effective employment of non-financial services. Services such as group organisation and leadership; financial advisory service; monitoring and supervision; pre-loan and post-loan trainings in such areas accounting and record keeping, business management and marketing are vital. There is positive indication from the study that MFBs are financing agricultural cooperative societies. Though the financing has not gotten to its peak due to paucity of funds as indicated by operators of the banks, it is still a great departure from what prevailed in the commercial banks and other credit delivery programmers of government.

The ACSs from the study affirmed that credit from MFBs are accessible, adequate, but though have not so much advanced their business activities. This calls for development support from credit officers of MFBs through their non-financial functions. The challenge of funding agricultural cooperative societies as identified in the study is indeed many. However, beyond insufficient fund, inadequate credit staff and high interest rate on loan, the rest are traceable still to non-implementation of non-financial service by the microfinance banks. Based on the out come of this study, the underlisted recommendations aimed at strengthening the effective financing of small-holder farmers in Nigeria through agricultural cooperative societies are made.

State and local government councils are encouraged to provide the MFBs with 1% of its budget as provide by the CBN microfinance policy document to assist them have sufficient fund to deliver their services to rural communities as well to the agricultural cooperative

societies. The Central Bank of Nigeria in the spirit of the banking sector reform and re-vamping the economy should set-up a microfinance development fund. Criteria should be made for accessing the fund and MFBs who meet it should be given. The re-structured Nigeria Agricultural Cooperative and Rural Development Bank, now re-named Bank of Agriculture (BOA) should finance agriculture through 'whole-sale' financing of MFBs for on-lending to farmers by ACSs. The various federal and state government credit based poverty alleviation programes should focus on agriculture. They should extend such funds through micro finance banks that have the structure and are better placed to lend it to farmers through their groups. Because of the risk-nature of agricultural activities the federal government through the Nigeria Agricultural insurance cooperation (NAIC) and the CBN Agricultural Credit Guarantee Scheme (ACGS), should effectively collaborate to provide insurance cover to the MFBs. This will motivate them to finance agriculture.

The Central Bank of Nigeria, through its monetary policy guideline should provide a mandatory 'percentage' exposure of credit of MFBs to the agricultural sector. It should be followed by stringent regulatory and supervising visits to the banks to monitor compliance. Microfinance banks should take seriously their 'development role' to the agricultural cooperative societies. This they must do through emphasis on deploying non-financial services, particularly training of the societies on group organisation and leadership, good accounting and record keeping, business management and marketing. They should also step-up the monitoring and supervision of their activities. The executive capacity of the credit department of the MFBs should be up scaled. Emphases in this regard should be on employing personnel in the department that has the disciplinary background in vocational studies as well as the requisite experience. Also, the right number of staff and the logistic needs to effectively follow with the 'field-nature' of the department should be engaged. There should be a re-orientation and sustained training of credit staff. The 'seat-tight' or 'arm-chair' banking mentality witnessed in the old-generation (government owned) banks is no longer fashionable. Besides, microfinance banks because of the characteristic of its customers base are expected to emphasize developmental functions. This requires the operators and particularly the credit staff to see themselves as credit extension personnel and hence be field-focused. Secondly, there should be sustained training of the credit staff in broad-area of microfinance operation as been done presently through the CBN microfinance certification programmme. Beyond that, specific targeted training in agriculture, group formation, organisation and leadership, entrepreneurship and business management, accounting and record keeping, basic health and home management, as well as agro-produce marketing should be promoted. Credit Officers should see themselves as trainers since they are expected to transfer knowledge and skill gained from training exposure to their clientele. Microfinance banks are encouraged to emphasize group lending especially for small-holder farmers through ACSs. This allows them to: take advantage of group pressure, reduce credit administrative cost, easily conduct training and utilize other collateral substitutes to reduce the incidence of loan default and irregular repayment.

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APPENDIX

Table 1: Distribution of ACSs, According to Sources of Finance

Sources	No of Respondents	Percentage (%)
Internal sources		
Share capital	50	41. 6
Entrance fee	5	4.2
Reserve	25	20.8
Fines and levies	5	4.2
Thrift and savings	20	16.7
Donation	10	8.3
Interest on loans	3	2.5
Loans from members	2	1.7
Total	120	100
External sources		
Commercial Banks	10	8.3
MFBs	83	69.2
Government Grants	15	12.5
Trade credit	12	10
Foreign Aid	-	-
Loan from non-members	-	-
Total	120	100

Source: field survey, August 2011

Table 2: Distribution of Respondent According to Financial Products of MFBs.

Options	No of Respondents (N=18)	*Percentage (%)
Savings accounts	18	100
Current accounts	18	100
Fixed (time) deposit account	18	100
Microcredit	18	100
Money transfer	-	-
Micro lease	7	39
Micro insurance	3	17

*Multiple responses

Sources: field survey, August 2011

Table 3: Distribution of Respondents According To Non-Financial Products of MFBs.

Option	No of Respondent (N=18)	*Percentage (%)
Financial advisory service	9	7.5
Monitoring/supervision of loanees	13	10.8
Pre-loan training	4	3.3
Post-loan training (health, Nutrition management etc)	-	-
Agricultural extension services	-	-
Group organisation/development	2	1.6
Agro-input service	3	2.5
Ware-housing/marketing service	3	2.5
Agro-equipment (tractor) lease service	3	2.5

*Multiple Responses

Source: field survey, August 2011

Table 4: Distribution of ACSs According to the number of times MFBs loans have been accessed.

Options	No of Respondents	Percentage (%)
1 – 3 times	100	83
4 – 6 times	20	17
7 – 9 times	-	-
10 times and above	-	-
Total	120	100

Source: Field Survey, August 2011

Table 5: Distribution of ACSs According To The Highest Amount Obtained From MFBs

Option	No of Respondents	Percentage (%)
₦20,000 – ₦50,000	-	-
₦51,000 – ₦100,000	35	29.2
₦101,000 – ₦300,000	47	39.2
₦301, 000 – ₦500,000	23	19.2
₦501,000 – ₦700,000	11	9.2
₦701, 000 – ₦1million	4	3.2
₦1million and above	-	-
Total	120	100

Source: Field survey, August 2011

Table 6: Distribution of ACSs According To Access To MFBs Credit.

Options	No of Respondent	Percentages (%)
Very accessible	29	24.2
Accessible	53	44.2
Somewhat accessible	38	31.6
Seldom accessible	-	-
Not accessible	-	-
Total	120	100

Source: Field survey, August 2011

Table 7: Distribution of ACSs on Adequacy of MFBs loans

Options	No of Respondent	Percentage (%)
Very adequate	13	10.8
Adequate	71	59.2
Somewhat adequate	22	18.3
Not adequate	10	8.3
Very inadequate	4	3.3
Total	120	100

Source: Field survey, August 2011

Table 8: Distribution of ACSs on the extent MFBs credit did enhance their business activities

Options	No of Respondent	Percentage (%)
To a very great extent	11	9.2
To a great extent	32	26.7
To some extent	50	41.7
Seldom	20	16.7
Not at all	7	5.8
Total	120	100

Source: Field survey, August 2011

Table 9: Distribution of Respondent on challenges of financing ACSs

S/N	Challenges	ACS		MFBs	
		Frequency (N=120)	*Percentages (%)	Frequency (N=18)	*Percentage (%)
1	Insufficient fund	33	26	16	89
2	Inadequate credit staff	-	-	12	67
3	Poor monitoring/supervision of loans	115	96	13	72
4	Poor member/group repayment	43	36	10	56
5	Dishonest members/group	49	41	9	50
6	Inadequate training of credit staff	-	-	11	61
7	Non/poor training of ACSs	105	88	14	78
8	High interest rate of loan	113	94	-	-
9	Lack of awareness on MFB service.	73	61	-	-
10	Delays in accessing credit	61	51	2	11
11	Poor attitude of credit staff	57	46	-	-
12	Collateral demands	33	28	4	22
13	Weak organisation/leadership hip of ACSs	-	-	17	94
14	Weak managerial ability of ACSs	-	-	15	83

*Multiple: Response

Source: Field survey, August 2011

Chapter 10

FINANCIAL SERVICES COOPERATIVES, PUBLIC POLICY AND FINANCIAL INCLUSION: A PERSPECTIVE FROM LATIN-AMERICA

Inmaculada **BUENDÍA-MARTÍNEZ**
Benoît **TREMBLAY**

INTRODUCTION

Although financial inclusion is not a new issue, the financial crisis has put it back on the public policy agenda. From a macroeconomic perspective, the reduction of financial exclusion has positive effects on economic growth. Research shows that the relationship between financial development and economic growth is mutually causal. Moreover, this relationship cannot be generalized across countries because of the specificity of economic policies and the efficiency of financial institutions (Ang, 2008; Choong and Chan, 2011; Demetriades and Hussein, 1996; Khalifa Al-Yousif, 2002; Suntsova, 2011). From a micro perspective, globalization obliges all organisations to rapidly evolve in terms of their strategies. For financial institutions, whose activities have for quite some time been strongly regulated, strong competition and the internationalization of their activities impose even more radical changes. Paradoxically, although the financial sector is characterized by considerable dynamism and a great ability to innovate, the level of profitability required in a very competitive context makes them less accessible to part of the population if their activities are not sufficiently profitable.

This issue remains a concern in developed countries alike in developing ones. In OECD countries, 84% of adults are financially included although this percentage varies widely from one country to another. For example, the last available data show that 12.7% of US households do not have a bank account (Aizcorbe et al., 2003). This percentage drops to 10% in 15 European and increases to 47% if we consider the new member states (European Commission, 2008). In Canada, the problem of access to the banking system is much less pronounced. Research on this subject shows that between 2% and 4% of Canadians do not have an account in a financial institution (Les Associés de recherche Ekos, 1998). In contrast, in developing countries almost 70% of the adult population lack access to basic financial services. The regions with the largest share of unbanked populations are Sub-Saharan Africa and South Asia, where only 12% and 24%, respectively, are banked (Stein, Randhawa and Bilandzic, 2011; World Bank Group, 2009). In light of this situation, some international initiatives have been developed in recent years. In 2008, the Alliance for Financial Inclusion (AFI) was created by the Bill and Melinda Gates Foundation and administered on behalf of its members by the German International Cooperation (GIZ). Composed of public and private agents from developing countries, this information interchange network seeks to support the

development of financial inclusion policies. Another initiative is the Global Partnership for Financial Inclusion (GPFI). Created at the 2010 G20 summit in South Korea, the objective of this international platform is to work on financial inclusion by putting the Principles for Innovative Financial Inclusion into practice. These principles seek to foster an enabling policy and a regulatory environment for growing financial inclusion (International Finance Corporation, 2011).

These international guidelines have to take the concrete form of actions by financial institutions. Expanding financial access requires a focus on various dimensions of exclusion, such as products, features and channels (Stein, Randhawa and Bilandzic, 2011), using different mechanisms: voluntary codes, government intervention, and market approaches (European Commission, 2008). Voluntary charters and codes of practice are banking industry instruments for developing various strategies to bring large strata of society within the ambit of the banking sector. Financial institutions are increasingly concerned with being viewed as ethical and socially responsible enterprises. This desire reflects a willingness to satisfy the demands of society and leads to the introduction of activities viewed as socially responsible (Dembinski, 2000). This trend has given rise to a spectacular development in voluntary codes driving financial institutions to adopt sustainable and social orientations, including financial inclusion actions. However, despite the convenience and flexibility these instruments offer enterprises in terms of self-regulation (Saurwein, 2011; Schwartz, 2001), lack of initiative may lead to interventions by government authorities to impose regulations framing socially responsible activities. State-driven interventions using statutory enactments have been used by some countries to force institutions to face the problem of banking exclusion (Barr, Viña, Personick and Schroder, 2000). As examples we can cite the Belgian law instituting a basic banking service, the Community Reinvestment Act (CRA) in the United States, and Bill C-8 in Canada. Market approaches against financial exclusion drive us to analyse financial services providers. Developing social products and services and giving access to financial services to individuals and small and medium size enterprises (SME) are specific practices that the banking industry adopts to tackle financial exclusion (Prior and Argandona, 2009; Zeegers, 2000). However, this service portfolio is constrained by considerations of service profitability. The self-financing proportion limits the real capacity to include excluded individuals in an unprofitable economic relationship (Vienney, 1994, p.68). For this reason, financial institutions work in partnership with not-for-profit organisations or governments to increase access to affordable financial services.

For over a century citizens-consumers-entrepreneurs, unsatisfied by available banking services, have been creating financial institutions to satisfy their own needs. Financial services cooperatives (FSC) are among these alternative financial service providers. Lack of accessibility to financial services was the main reason for their creation a century ago. Based on specific values and principles and their structural integration of the community interest, the dynamics of FCSs have allowed them to meet the needs of social groups, communities, and regions inadequately served by conventional banking institutions (Buendía Martínez, Lapointe, Roy and Tremblay, 2006). If in addition we include the higher stability afforded during the financial crisis compared to commercial banking institutions (Groeneveld, 2011), we can understand the resurgence of the cooperative enterprises. FSCs help to increase the diversity of the banking sector, both in terms of business models as well as in terms of ownership structure, thus contributing in a significant manner to improving the financial system (Ayadi et al., 2010). In Latin America, although the weight of FSCs is small in terms assets (1.5 % of the financial system of the region (Durán, 2011)), they play a key role in

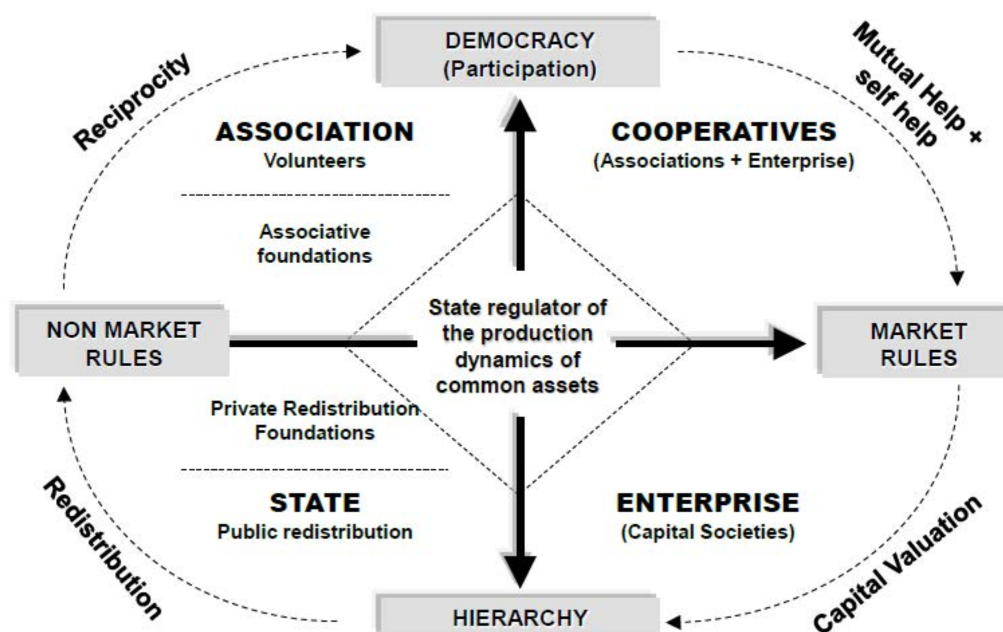
facilitating banking services for more than seventy million people. With 55% of the population considered to be financially excluded, national governments and financial authorities are becoming increasingly proactive in incorporating financial inclusion as one of their priorities. Mexico and Brazil can be highlighted as recent examples in moving towards better financial inclusion (Stein, Randhawa and Bilandzic, 2011) through their use of cooperative institutions as one of the instruments to this end. Research on financial exclusion in Latin America is scarce due to the region's lower index of financial exclusion compared to other regions. For this reason, this paper seeks to increase knowledge about FSCs from a financial inclusion perspective for this region. Firstly, the particularities of FSCs and financial inclusion are analyzed, followed by a study of Brazilian and Mexican cases as remarkable case studies of public policy in supporting efforts by cooperative institutions to reduce financial exclusion.

FINANCIAL INCLUSION AND FINANCIAL SERVICES COOPERATIVES: NEW DEVELOPMENTS IN AN OLDER RELATIONSHIP

More than a century has passed since the creation of the first FSC which largely contributed to access to savings and credit for consumers, farmers, craftsmen and SME in the countries in which they prospered. The model of institutional forms for activity financing (see Figure 1) from Malo and Tremblay (2004) enables us to place FSCs in the market's financial activities. Historically, FCSs have been a form of social banking used by more or less marginalized individuals and micro-enterprises to mobilize resources to reorganize the relationship between their activities and markets through this new form of organisation. In developed countries where FSCs have succeeded in securing a significant market share, they influence not only their members' financial situation but the whole financial system by increasing the intensity of competition and limiting the profitability of all financial institutions (see PA Consulting Group, 2003). In situations such as these, their obligation to maintain profitability in the market place limits their capacity to play their fundamental role of reintegrating people and/or SMEs excluded by economic and societal transformations into the market without the help of the state or voluntary organisations. Additionally, the transformation of FSCs into universal banking institution implies a shift from a membership base that hinders initiatives requiring strong solidarity on the part of their constituents. Nevertheless, FSCs have succeeded in maintaining their distinctive characteristics: a strong orientation towards their domestic market, a large margin for strategic interventions afforded to local decision makers and greater social and geographic accessibility for their members entailing a certain equalization favoring their outlets in more remote regions (Malo and Tremblay, 2004).

Additionally, a review of state intervention mechanisms and the growing number of private foundations shows that FSCs have experienced a multiplication of associative forms. Some of them have a similar composition, rules and activities to those of cooperatives. For the most part, these associations emerge at the heart of solidarity movements characterized by a strong capacity for voluntary engagement and financial support from third parties. FSCs become financial partners that take advantage of their social capital of proximity, which highlights the fact that this option puts into practice what they have a hard time doing in their market oriented banking dynamics.

Figure 1. Model of institutional forms for activity financing



Source: Malo and Tremblay, 2004

Although FSCs' contribution of granting access to financial services is acknowledged (European Association of Cooperative Banks, 2005; HM Treasury, 1999; Jones, 2007; Mayo and Mullineaux, 2001; Mckillop, 2011), they have a clear ability to stimulate local development in both urban and rural areas not only with their financial resources, but also with their philosophy and organisational expertise (McCarthy, Briscoe and Ward, 1999, p.8). In this regard, in his report to the 47th session of the General Assembly (United Nations, 1992), the Secretary General of the United Nations acknowledged that FSCs have a strong potential for mobilizing local savings and providing credit to members and are particularly important in capital-scarce conditions, thereby encouraging thrift and entrepreneurial activity and hence stimulating local multipliers.

From a financial point of view, Douthwaite (1996) argues that conventional banks reduce purchasing power in a community since the money deposited with them leaves the community and is employed elsewhere. Furthermore, once money leaves the community, it only returns at interest rates determined by the world market. Credit unions, on the other hand, keep local money in the community by encouraging the pooling of local savings for local lending. Loans are made to members for personal or business development purposes. However, lending to business in general has been weak. McCarthy, Briscoe and Ward (1999) estimate less than 10% of total FCS lending is to local enterprises. Although FCSs have emphasised personal lending due to a legislative requirement to lend to individual members, they are allowed to lend to individuals for business purposes. There is enormous scope for FCSs to become more involved in business lending particularly in light of the fact that many of them experience less success with lenders. Gormley (1993) argues that by assisting in local development, FCSs can actually reduce local migration and emigration, and thereby sustain

the population and demographic health of local communities. From an organisational perspective, one of the most valuable contributions FCSs make to local development in their communities is by demonstrating the principle of co-operation. Generally speaking, involvement in local development FCSs to extend their vision of social justice both to the individual members and to the larger community in which they work and reside, as directed by their operating principles. FCSs are a means by which a community's financial resources in particular can be mobilised for the benefit of the community as a whole (Buendía Martínez, McCarthy, Briscoe and Ward, 2001). In most Latin American countries, banking institutions are not responsive to the majority of the population's needs. Given that widespread financial services require specific government policies (Solo, 2008), Mexico and Brazil are among the leading countries with a public policy to tackle financial exclusion. They are also working on developing a strong financial service cooperative movement by establishing an enhanced legislative environment accompanied by tighter regulations. In doing so, they are following the modern approach to financial regulation in order to minimise systemic risk and ensure consumer protection.

FINANCIAL SERVICES COOPERATIVES IN BRAZIL: TWO DECADES OF CONSOLIDATION

The economic reforms of the early 1990s were a turning point in Brazil's development. The introduction of the Real in 1994, the reduction of inflation, and the opening up of the economy gave rise to a process of transformation and strengthening of the financial system in which state banks and saving banks were the most affected as they entered a process of privatization, transformation, and/or liquidation. This situation opened the door to foreign banks who acquired privatized entities as one of the quickest means to increase their market share. However, beginning in 2000, they gradually lost a part of their market share to local commercial banks.

For the first time in Brazil's history, the cooperative financial sector has been defined as a key pillar of public policy on financial inclusion. Moreover, financial authorities believe that a part of the country`s development depends on FSCs' ability to increase access not only to financial services, but to credit as well (Henriques Pinheiro, 2008). Over the past 15 years, the movement went from 980 to 1370 entities, an increase of 40% despite the merger process among locals FSC that has occurred in recent years. This tendency is reflected not only in the number of FSC, but also in the their market share of the banking sector: their participation has increased sevenfold with respect to assets, fivefold in credit, and eightfold in deposits (see Table 1).This growth has been a consequence of the Central Bank of Brazil's (CBB) policy of allowing FSCs to take charge of new banking activities and at the same time to strengthen their regulatory framework. This monitoring of the legal environment relative to the efficiency, performance and professional response of each of the components of the financial cooperative system has been an important success factor for FSC (Soares and Melo Sobrinho, 2008, p.92). Brazil is the only country in the Latin-American region with a financial cooperative sector structured into three levels: local, central and confederation. At the local level, FSCs have a long history. In 1964, their legislative competencies were transferred to the CBB. Their creation had to be based on two common bonds: members had to earn their livelihood in areas related to agriculture, fishing or mining; and workers in a specific profession or activity or belonging to specific companies (Henriques Pinheiro, 2008).

Table 1: Brazilian FSC Evolution 1995-2010

	1995	**2000**	**2005**	**2010**
EVOLUTION OF INSTITUTIONS IN THE BANKING SYSTEM				
Multiple banks	205	163	138	137
Commercial banks	35	28	22	19
Savings banks	2	1	1	1
FSCs	980	1.235	1439	1370
EVOLUTION OF THE MARKET SHARE (%) OF BANKING INSTITUTIONS				
Market share (%) of total banking assets				
Private banks with foreign investors	8,39	27,41	22,89	17,92
Private banks	39,16	35,23	43,12	52,70
State banks	21,90	5,62	5,09	2,02
Savings banks	16,40	15,35	12,05	9,40
Bank of Brazil	13,91	15,63	15,36	16,35
FSC	0,24	0,76	1,49	1,61
Market share (%) of total banking credits				
Private banks with foreign investors	5,72	25,16	26,37	19,40
Private banks	31,79	34,53	40,84	64,37
State banks	23,46	5,12	4,05	1,81
Savings banks	22,63	23,00	8,01	2,81
Bank of Brazil	15,96	10,95	18,46	9,21
FSC	0,44	1,24	2,27	2,40
Market share (%) of total banking net worth				
Private banks with foreign investors	13,08	28,31	24,56	17,77
Private banks	49,21	50,33	54,15	39,41
State banks	12,41	5,66	4,74	3,05
Savings banks	12,04	3,82	4,39	14,07
Bank of Brazil	11,82	9,89	9,30	23,26
FSC	1,44	1,99	2,86	2,44
Market share (%) of total bank deposits				
Private banks with foreign investors	5,4	21,14	20,27	15,99
Private banks	36,4	33,93	41,61	48,96
State banks	16,07	7,36	5,98	2,44
Savings banks	24,33	19,49	14,26	11,84
Bank of Brazil	17,59	17,05	16,51	19,11
FSC	0,21	1,03	1,37	1,66

Source: BBB

Removing the common bond restrictions was a demand by the FSC sector which viewed it as a limitation to the creation of FSCs and their ability to act as promoters of territorial economic development. To alleviate some of the consequences of this state of affairs, Resolution 3.058

was promulgated in late 2002 to allow for the creation of FSCs by small and micro entrepreneurs working in industrial, commercial, and services activities, including those in rural areas (Banco Central do Brasil (BCB), 2002). This modification made it possible to achieve a balance between urban and rural businessmen. Under the previous legislation, members had to be in the same field of activity, something which was possible only in the big cities where it was feasible to group a sufficiently large number of businessmen in the same activity sector to obtain minimal scales of operation (BCB, 2003).

Less than six months after the relaxation of the legal framework, another regulation allowed the creation of free-admission FSCs, though subject to different levels of population density. After several modifications, the level was limited to areas with populations no greater than two million. The legislation also permitted the transformation from rural and mutual FSCs to free-admission FSCs requiring a minimum of three years of operations (BCB, 2010).

The second level units of the Brazilian financial cooperative sector are Central cooperatives; they represent the pillar of their model. Requiring a minimum of three local FSCs for their constitution, their functions are focused principally on prudential supervision, monitoring the application of their regulations, and technical-professional training of its affiliates. Prior to Resolution 3859/2010, FSC affiliation with a central cooperative depended on their typology and was mandatory for every FSC created after 2003. For independent FSCs, this regulation has increased the required level of capital and equity to operate. Of note was the reduction by 50% of the established minimum limits for new FSCs in the north, northeast, and central regions (BCB, 2010). This initiative seeks to promote the creation of entities in the poorer regions with the greatest difficulties of access to banking services.

The third level of integration is composed of the confederations. Created by central cooperatives, their objective is to orientate, coordinate and carry out support activities (Brasil, 2009). This level also includes cooperative banks owned by the local FSC through their central cooperatives. Their role is to act as their FSC group's treasurer and as its financial agent on domestic and international markets. It offers financing, banking and international services to institutional organisations and to large and medium-sized businesses (Soares and Melo Sobrinho, 2008). The authorization for their creation did not take place until 1995 as a response to the development and growth needs of various FSC groups. The operating equivalence to the rest of commercial banks took place in 2000 through several regulatory changes including that which made it possible for foreign investors to participate in the capital stock (BCB, 2000). After 15 years of operation, the two existing cooperative banks, Bancoob and Bansicredi, have experienced massive growth in terms of loans, deposits, and assets. The combinations of these three levels of financial cooperative organisations have generated a set of structures with different origins and composition. In effect, slightly more than 80% of local FSCs and central cooperatives belong to one of six networks: Sicoob, Sicredi, Unicred, Ecosol, Cresol, and Crehnor. The first three have similar profiles and incorporate the majority of FSCs and centrals whereas the other three represent the so-called solidarity credit sector created after the mid-1990s to address serious problems of access to credit by a part of small Brazilian farmers due to the volatility of agricultural production and its limited financial magnitude (Bittencourt and Abramovay, 2003; Machado Padilla and Nunes da Silva, 2010). Although Brazilian FSCs have accomplished notable development based on a progressive strengthening of their foundations, yet they are facing several challenges. Firstly, the merger process among local FSCs that has taken place in recent years is a clear sign of their willingness to strengthen their ability to offer a full range of financial services to their

members on a competitive basis. Secondly, the last legislative reform of 2010 will present significant qualitative management-related challenges because it will be mandatory to professionalize executive managers and to separate their role from that of the board of directors. Those changes are the result of a long discussion process between the monetary authority and the cooperative movement (Ventura, 2009). Thirdly, the sector's future growth could be higher with less intersystem competition and the establishment of new ways of integration both from a national and a regional economic perspective (Buendía Martínez, 2010).

REBUILDING FINANCIAL COOPERATIVE SECTOR: THE MEXICAN CASE

The process of normalizing the Mexican financial cooperative sector began at the beginning of the new millennium and represents an unprecedented challenge in Latin America. Its situation differed from the region's other countries in two respects: 1) the multitude of institutions with different legal status belonging to the financial cooperative sector (savings and loans institutions – SAP, credit unions - UC, savings and loans cooperatives – CAP, solidarity unions - CS), and their size, inasmuch as this movement was among those with the greatest number of members and assets, but had a low market share (Buendía Martínez and Tremblay, 2002).

This state of affairs was the result of the movement's erratic development throughout its 50 years of existence. Given the absence of a specific legal framework and public monitoring, the sector was largely self-regulated and structured around the Mexican Confederation of Credit Unions (CMCP), to which the provincial federations were affiliated. Local FSCs were incorporated in the provincial federations (Rojas Herrera, 1997). The Organisations and Credit Auxiliary Activities Act (LGOAAC) and the Cooperative Societies Act (LGSC), enacted respectively in 1991 and 1994, introduced a new legislative environment for the sector. Unfortunately, there was no shortage of confusions. Firstly, the SAP option was adopted by many local FSCs and the majority of institutions were integrated into the CMCP, which subsequently merged to give rise to the sector's largest entity—the Caja Popular Mexicana (CPM). Secondly, for the first time in the Mexican history, the new legislative framework recognized the credit cooperative society (CAP) as a type of cooperative. Differences in operating requirements between the SAP and CAP led to a massive transformation of the SAP into a credit cooperative society (Imperial Zuñiga and Ramírez Guerra, 2001).

To complete the profile of financial cooperatives, we have to add another two legal entities: the CSs and UCs. Defined as civil associations/societies, CSs were created under the protection of the National Social Business Support Fund (FONAES), in operation since 1993, to facilitate access to credit by agricultural producers with the fewest resources (Développement International Desjardins, 1998). Farmers with difficulties accessing financial resources are also targeted by the UCs, which since 1996 have been able to accept deposits from their members in addition to being active in product sales, purchases and processing (Conde Bofil, 2000). Created under limited corporation status, the history, goals and the democratic governance of a subgroup of UCs in the social sector allow us to view them as part of the financial cooperative movement (Buendía Martínez and Tremblay, 2002). The early 2000s was marked by a serious crisis in the sector resulting from a fraud perpetrated on thousands of individuals who lost their savings through the creation of a false FSC. This event resulted in the mobilization of public authorities and the financial cooperative movement,

represented by the newly created Mexican Council of Popular Savings and Credit (COMACREP), to establish an appropriate legal framework not only to protect against cases of fraud but also to promote its development (Imperial Zuñiga and Ramírez Guerra, 2001). On June 4th, 2001, the Popular Savings and Credit Act (LCAP) went into effect and led to the global regulation of popular savings and credit entities (EACP) as financial intermediaries under two legal statuses: cooperative societies of savings and loans (SCAP) and popular financial societies.

The new legal framework was an inflexion point in the sector and had three basic orientations: a) the definition of a formal process for the creation of entities; b) the recognition of SCAPs as banking intermediaries, which meant that they had to be supervised and contribute to the financial deposit protection fund; and c) an increase in the authority of representative entities – the federations were responsible for auxiliary supervision while confederations were responsible for managing the protection funds (Buendía Martínez and Tremblay, 2002). However, the process of transformation was not without its difficulties. In June 2009, after several legislative reforms to address the different problems of the entities, the Regulation of Activities of Cooperative Societies of Savings and Loans Act (LRASCAP) was enacted as the new regulatory framework for FSCs. Its objective was to solve three significant limitations: the inefficiency of the supervisory system as consequence of the free affiliation of the local entities; the conflict of interest of the federations which were allowed to supervise and to provide technical assistance services; and the governance complexity of federations as a consequence of the affiliation of both kinds of popular entities, cooperatives and non-cooperatives.

Although the core orientations of the financial cooperative sector were maintained in the new regulation, it is important to bear in mind certain aspects that have led to an important change in direction. Firstly, FSCs were classified into two large groups: those with assets of less than 2.5 million investment units (UDIs) with authorization to perform basic operations but without the obligation of financial supervision or contribution to the deposit insurance; and those with assets over 2.5 million UDIs, which themselves were classified into four groups, with each one having an authorized level of operation involving differing levels of prudential regulation. Secondly, the federations and confederations no longer have authority in terms of supervision or administration of the guaranty fund and are thus regulated by the LGSC. Thirdly, the regulatory and supervisory authority is now the National Banking and Stock Commission (CNBV), which has the power to authorize, regulate, supervise and sanction. Lastly, a guaranty fund was created with four functions: auxiliary supervision, deposit insurance management, preventive monitoring, and management of the national register, which registration is compulsory for all FSCs (Estados Unidos de México, 2009).

CONCLUSION

Although financial exclusion is not a new problem, its negative consequences are much better understood than they were in the past. The deregulation process, which has resulted in more intense competition, the impact of economic and financial crisis in the banking industry, the relationship between financial access and social exclusion, and the economic effects on growth and communities deprivation have all placed financial inclusion as a policy concern on the public agenda.

Tackling financial exclusion is a complex matter because its causes and nature are varied and multifaceted. Focusing on financial providers, public policies are building on a set of initiatives that must be implemented as much for mainstream as for alternative institutions. The latter insitutions vary greatly from country to country, pay special attention to marginal segments, and act in compliance with rules and regulations. These institutions often adopt an organisational dynamic of a low integration network and in many instances their development receives support from the state, private funds or even from large commercial banks. Before the development of these alternative financial providers, citizens-consumers-entrepreneurs who were unsatisfied with available banking services participated in the development of FSCs as a means of meeting their own needs. Defined as organisations committed to responding in an alternative manner to the banking service needs of their communities, FSCs have succeeded in maintaining their distinctive characteristics: a strong orientation towards local, regional and national markets; a large margin of strategic intervention in the hands of local decision makers; and greater geographic and social accessibility for their members. In addition, their specific organisational form, which enhances reciprocity and redistribution practices a cooperative nature, offers an alternative governance model to the purely commercial one.

In Latin American region, where the role of public banks was drastically reduced and where there is concentration of private, national and foreign banks, FSCs play a key role in facilitating banking services for more than seventy million people. The analysis of the Brazilian and Mexican cases reveals that FSCs are well situated in the financial services industry to have a positive impact on financially excluded communities. However, this role cannot be accomplished without adequate government policy and regulatory framework and supervision. While Mexican authorities came to this conclusion later than those in Brazil, they are now enacting public policies quite similar in nature to those which have been implemented in Brazil. Brazil and Mexico are clearly ahead in the implementation of financial public policy to increase financial inclusion through FSCs. The impact of those policies in the medium term could turn out to be more far reaching in terms of contribution to local and regional development, higher competition in the financial sector and more financial stability than other countries have experienced.

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Chapter 11

IMPACT OF MICROFINANCE ON RURAL HOUSEHOLDS

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INTRODUCTION

Despite rapid urbanization and convergence in poverty rates between rural and urban areas, rural poverty remains an important welfare problem in the rural areas in developing countries of the World. In most Latin American countries, rural poverty has resulted in a number of welfare problems such as wastage of human resources, a frequent source of political destabilization and a cause of environmental pressure (De Janvry and Sadoulet, 2000). In recent times, as other continents continue to register sustainable economic growth and development, Africa is not only lagging behind, it is also trapped in a vicious circle of borrowing and donor dependency syndrome which some critics point out as one of the causes practically sabotaging real development. Africa has perpetually failed to focus its development efforts on the optimum utilisation of the immense natural resources many of it countries are endowed with, turning it into wealth, to propel their economies and people towards a high level of economic and social development, and as a consequence eliminate pervasive poverty (Matovu, 2006).

Nigeria represents one of the many paradoxes of development in which case the nation is rich but her people are poor (Nwaobi, 2003; Omotola, 2008). Available statistics indicate that poverty has become endemic in Nigeria and is on the increase. As the most populous and one of the largest countries in sub-Sahara Africa, the issue of poverty in Nigeria is of concern not only in itself but also as a challenge for poverty reduction mandate in the entire African continent (Okunmadewa, 2001). For instance, poverty increased from affected 18 million people in 1980, to 35 million people in 1985; 39 million people in 1992; 67 million people in 1996; and 74 million people in 1999. At present, about two-third of the Nigeria's population (about 150 million) are poor. The 2010 Human Development Indicator of the UNDP indicates that 70.8 per cent and 92.4 per cent of Nigerian population live below US$1 (₦117) and US$2 (₦234) a day respectively. Nigeria, as a major oil exporting country, enjoyed massive windfall from the oil boom of the 1970s.

Statistics from the National Bureau of Statistics (NBS) indicate that the poverty situation in the country which has been increasing since 1960 (15.0 percent), 1980 (28.1 percent), 1985 (46 percent), 1992 (42.8 percent), and 1996 (65.5 percent) respectively, dropped to 54.4 percent in 2004. At the 2006 International Day for the Eradication of Poverty (IDEP) event in Abuja, tagged 'Working together out of poverty', Magnus Kpakol, National Coordinator of National Poverty Eradication Programme (NAPEP) affirmed that poverty rate in Nigeria was as high as 54.4 percent, identifying the North East region of the country as the poorest with

72.2 percent incidence of poverty. It is followed closely by the North West zone with 71.2 percent; North Central, 67.0 percent, South-West 43.0 percent, South-South 35.1 percent, and South East 26.7 respectively. Table 1 shows poverty situation in south west geopolitical zone, Nigeria which is the study area.

Table 1. Poverty Situation in South West Geopolitical Zone, Nigeria

State	Percentage of National Population	Poverty Incidence P_o	Poverty Gap P_1	Poverty Severity P_2
Ekiti	1.33	42.27	0.1181	0.0479
Lagos	6.41	63.58	0.3473	0.2200
Ogun	2.62	31.73	0.1023	0.0422
Ondo	2.92	42.14	0.1539	0.0694
Osun	2.42	32.35	0.0757	0.0533
Oyo	3.86	24.08	0.0585	0.0244
South West	19.55	43.01	0.1821	0.1024

Source: National Bureau of Statistics, (2007)

Government Anti Poverty Policies in Nigeria

Between 1988 and 1999, elaborate poverty-eradication programmes were initiated in Nigeria. The initiatives focused on food and agricultural production, social mobilization, employment and skills improvements. The programmes have aimed at improving basic infrastructure and housing facilities for rural and urban population, extending access to credit and farm inputs, and creating employment, but they all failed to achieve the desired goals (Obadan, 2001; Garba, 2006; Elumilade et al.,2006; Iroegbu, 2009; Oshewolo, 2010). It was during the period that institutions such as Directorate of Food, Roads and Rural Infrastructure (DFRRI) and National Agricultural Land Development Authority (NALDA) were established. All these programmes and institutions were put in place to bring about rural development, increase productivity of rural households and improve their income levels. Other programmes are: Better Life for Rural Women and Family Support Programme. World Bank report in 1999 indicated that Nigeria's Human Development Index (HDI) was only 0.416 and that about 70.0 per cent of the population was below the poverty line, despite the plethora of poverty alleviation programmes which past governments had initiated and implemented. These alarming indicators prompted the government to review the then existing poverty alleviation schemes and established an emergency Poverty Alleviation Programme in 2000 which later metamorphosed to the National Poverty Eradication Programme (NAPEP) in 2001. Nevertheless, it is important to note that most of the poverty alleviation programmes adopted in Nigeria are focused on rural areas and on agricultural sector (Ogwumike, 2002). The reason is because poverty in Nigeria is essentially a rural phenomenon—majority of those in poverty are disproportionately located in the rural areas, where they are primarily engaged in agricultural production and allied activities (Omonona, 2009).

One dominant response to tackling the issue of poverty has been to evoke a market mechanism of microcredit support. The idea is to make credit available through less access restrictive credit schemes or institutions and hope that the poor can use it to establish, grow and improve their income generation avenues and subsequently get out of poverty (de Soto, 2000; Odigie, 2007). Hence, the clamour for microcredit as a strategy to lift the poor out of poverty is seen more as a belief that the poor can use to access market opportunities and take steps to engage in economic activities that will enable them to generate their own incomes (Bredow, 2002). For this to materialize, the people must develop the capacity to generate and maintain their means of livelihood and produce excess that will eventually lead to savings

(Iheduru, 2002). In spite of the spirited efforts, poverty in South-western states, as in other parts of Nigeria, is a matter of urgent policy concern.

Overview of Financial Sector in Nigeria

The economy of Nigeria is highly dominated by the agricultural sector, which contributes about 35% of Gross Domestic Product (GDP) and employs over 70 per cent of the population (Oxfam, 2007). Rural sector, on which the bulk of agricultural output is hinged, has not provided a base for improved livelihoods as its potential is not fully exploited. A number of factors, including limited access to credit services, poor infrastructure, small land holdings, and the nature of land tenure systems, have been identified as limiting the full exploitation of the agricultural potential in Nigeria. It is emphasized that, access to micro-credit is important for investment to increase agricultural productivity and support off-farm enterprises. It is also recognized that the poor have diverse financial needs including credit for the purchase of small capital assets, working capital and consumption. Accessibility to formal financial system, especially by Small and Medium Enterprises (SMEs) is very limited. On the supply side, banks are not expanding SMEs loans due to imperfect information, high transaction cost of dealing with small loans, geographical dispersion of the SMEs and large number of borrowers and low returns from investment. On the demand side, SMEs are reluctant to obtain loans because of the collateral security, high interest rate and untimely delivery of credits. The identified problems of SMEs notwithstanding their enormous depth, breadth and intensity, is only fair and proper to acknowledge the fact that the government did not fold its arms to watch the SMEs wallow in the gamut of problems. Doubtless, the government fully appreciates the opportunities SMEs create for employment, their contributions to economic growth and development, despite the constraints and difficulties in their operating environment. These explain why in the past forty-five years or so, the government has established various support institutions and relief measures, specially structured, to render assistance and succour to minimize the constraints SMEs typically face if not to eliminate them. The support institutions established by the government range from specialized banks, designed to focus on the funding of SMEs to, agencies and departments all meant to give a flip to the fortunes of SMEs (Onugu, 2005). It is also pertinent to note that government policies behind the establishment and operations of the SME support institutions had not been effective and productive.

Past programmes and institutions established and directed at SMEs development by government include: Mandatory Credit Guideline in respect of SMEs (1970); Small Scale Industries Credit Guarantee Scheme (1971) and Agricultural Credit Guarantee Scheme (1973). The main objectives of the scheme are to increase output, generate employment, diversify Nigeria's revenue base, raise the level of foreign exchange earnings and provide input for manufacturing and processing on a sustainable basis. Others are Nigeria Agriculture and Cooperative Bank (1973); Nigerian Bank for Commerce and Industry (1973); Rural Banking Scheme (1977); The World Bank Assisted SME I (1985) and The World Bank Assisted SME II (1990).Second – Tier Security Market (1985); Peoples Bank (1989); National Economic Reconstruction Fund (1992); Small and Medium Scale Enterprises Loan Scheme (1992); Family Economic Advancement Programme (1997); African Development Bank – Export Stimulation Loan Scheme (ADB-ESL) in 1988. The merger of the National Economic Industrial Development Bank (NIDB), the Nigerian Bank for Commerce and Industry and National Economy Reconstruction Fund (NERFUND) by Nigerian Government in October 2001, resulted into the Bank of Industry. Its major aim is to provide necessary

financial assistance and incentives for the establishment of large, medium and small scale projects, and the expansion and diversification of existing industries. It engages in fund mobilization, project appraisals, financing, implementation and investment activities: The Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB) established in the year 2002, is a merger of the defunct Nigerian Agricultural and Cooperative Bank (NACB), People's Bank of Nigeria (PBN), the Family Economic Advancement Programme (FEAP) and Small and Medium Enterprises Development Agency of Nigeria (SMEDAN). SMEDAN was established in 2004 to promote and develop the country's micro, small and medium-sized enterprise (MSME) sector. The organisation's mission is "to establish a structured and efficient micro-, small and medium-sized enterprise sector that will enhance sustainable development of Nigeria". SMEDAN helps MSMEs access the resources required for their development and provides technical assistance as needed.

In spite of the various measures put in place, funds flow into SMEs has been on the decline. Table 2 shows the declining ratio of commercial loans to small scale business in (rural and urban) Nigeria. Trend in the commercial bank total credit and loans to small scale enterprises in Nigeria shows there was an increase in total credit of commercial bank (₦48,056.0 millions) to small scale enterprises (₦15,462.5 million) in 1993 to ₦8.791 billion and ₦15,825.2 million in 2008 respectively. During these periods, ratio of commercial bank loan to small scale enterprises continue declining steadily from 32.2% in 1993 to about 0.2% in 2009. Bank loan to SMEs in early 1990s shared about 50% of the total bank credit availability. However, this was not the case in the 2000s after the abolition of mandatory 20% bank credit allocation to SMEs. However, this decline points to the fact that entrepreneurs, especially in Nigeria, do not have easy access to credit for their entrepreneurial activities and as such have low business performance. Commercial banks were reluctant to give loans to the private sector, especially SMEs, not because the sector is not viable, but due to the perceived risky nature and lack of government guarantee schemes. This implies that financial liberalisation policy in Nigeria has not generated enough funds for the development of private sector-led economy and government objective of using private sector as a catalyst of development may not be easily achieved.

CONCEPTUAL FRAMEWORK AND LITERATURE REVIEW

Microfinance is the provision of small loans (micro credit) and other financial services to low income clients to help them engage in productive activities or grow their small businesses. According to Ledgerwood (2002), the term, microfinance, refers to the provision of financial services to low income client including self employed. It differs in key concepts from conventional banking in that it employs different collateral substitutes to deliver and recover loans. Such collateral substitutes include group lending, dynamic incentives which allow the loan size to increase over time upon satisfactory repayment, mandatory savings, and regular repayment schedules. These collateral substitutes are important for both the poor borrowers who usually lack enough collateral and available credit history, and for lenders operating in countries with weak law enforcement. Adeyemi (2008) however, documents that despite decades of public provision and direction of provision of microcredit, policy reorientation, and the entry of new players, the supply of microfinance in Nigeria is still inadequate in relation to demand. This suggests that there is some inefficiency in microfinance operations in Nigeria due to some institutional inadequacies such as low credit volume, inefficient management and control. Studies (Conning and Kevane, 2002; Aryeetey and Udry.1997) on informal finance in Africa show

that, informal finance providers will do well so long as the level of economic activity demands increasing financial services for groups that cannot be reached by the formal financial institutions (Chipeta and Mkandawire, 1994). The emergence of demand for short-term credit especially among traders and farmers will most likely lead to the development of an informal unit to meet households demand for credit.

Table 2. Ratio of Loan to Small Scale Enterprises to Total credit (rural and urban) by Nigerian Bank

Year	Commercial Bank Loans to Small Scale Enterprises (₦'Million)	Commercial Banks Total Credit(₦'Million)	Commercial Banks Loan to Small Scale Enterprises as Percentage of Total Credit %
1992	20,400.0	41,810.0	48.8
1993	15,462.9	48,056.0	32.2
1994	20,552.5	92,624.0	22.2
1995	32,374.5	141,146.0	22.9
1996	42,302.1	169,242.0	25.0
1997	40,844.3	240,782.0	17.9
1998	42,260.7	272,895.5	15.5
1999	46,694.1	353,081.1	13.3
2000	44,542.3	508,302.2	9.7
2001	52,428.4	796,164.8	6.6
2002	82,368.4	954,628.8	8.6
2003	90,176.5	1,210,033.1	7.5
2004	54,981.2	1,519,242.7	3.6
2005	50,672.6	1,899,346.4	2.7
2006	71,896.5	1,847,822.6	3.9
2007	26,981.0	3,155,029.7	0.7
2008	18,824.2	5,453,188.2	0.4
2009	15,825.2	8,791,800.9	0.2

Source: Central Bank Nigeria Statistical Bulletin Dec.2006 and 2010

The failure of many government-subsidized credit programmes to reach the targeted groups has prompted the emergence of alternative means of administering rural credit so as to reduce the access problem (Braverman and Huppi, 1991). Informal credit markets have developed in rural areas, providing faster services to their clients. That informal finance has been proven to be of more importance than formal finance by different approaches used to measure its magnitude in different countries, namely Chipeta and Mkandawire (1992) for Malawi and Aryeetey and Gockel (1991) for Ghana. Important lesson learned from informal financial institutions is its degree of flexibility and creativity which accounts for the high degree of success. Financial services are useful instruments in overcoming constraints faced by households and in risk management and also influence household decisions by making it possible to exploit productive opportunities that would otherwise not be exploited. The Central Bank of Nigeria, (CBN) (1999), reported the significance of credit and other inputs to rural household's output and submitted that the provision and use of these inputs in the right proportion are crucial to increasing output and productivity in Nigeria. Availability and proper usage of credit has also been empirically proved to enhance productivity level of rural households in Nigeria (Okoruwa and Oni, 2002). In order to purchase inputs, rural poor need to be able to obtain production loans. The rural poor typically have little awareness of where to obtain credit for their production activities. Even when they are aware of formal credit sources, high interest rates and difficult terms for such loans discourage them (Chemonics International Inc, 2003).

Opara (2010) investigated the extent to which microfinance institutions have helped in the alleviation of poverty in Nigeria. They employed data collected by National Bureau of Statistics using factor analysis. The result of the analysis identifies five factors: low profit, prices of commodities are too high, hard economic times, lack of finance to start or expend their business, and business not doing well, as critical factors causing poverty. The analysis also reveals that the impact of microfinance on poverty in Nigeria can be explained in two phases. The first phase, the take-off stage, sees poverty as increasing though at a decreasing rate as microfinance credit increases. In the second phase, precisely starting from the year 2001; persistent increase in microfinance credit reduces drastically the poverty index in Nigeria. The researcher therefore, calls on the monetary authorities to put in place the financial superstructure necessary for making mandatory the establishment of microfinance banks in every community, if poverty will be aggressively fought. In another study, Yahaya (2011) examined the effectiveness of microfinance banks in alleviation of poverty in Kwara state Nigeria. The data collected were analyzed through the use of t-test and Analysis of Variance (ANOVA). Findings revealed that microfinance has significant role to play in the economy, as it helps reduce poverty by providing financial services to the active poor, help in generating employment and also provide small loans to grow small businesses.

MATERIALS AND METHODS

The south-western part of Nigeria comprises six states: Ekiti, Oyo, Osun, Ogun, Ondo and Lagos. The total population is 27,581,992 and predominantly agrarian and more than 96% of the population is Yoruba (National Population Commission, 2006). The region is bounded in the North by Kogi and Kwara States, in the South by Atlantic Ocean, in the West by Republic of Benin and in the East by Edo and Delta States. Agriculture is the dominant economic activity and main source of employment in the states providing employment and income for more than 75.0 per cent of the population. The people are predominantly farmers, while women engage in food processing and trading in addition to farming. The states have distinct wet and dry seasons, which characterize their humid tropical climate, with the dry season extending from November to March. Annual rainfall varies from about 500 mm in the northern belt to 1,100 mm in the forest belt. Primary data were collected for the purpose of this study using structured questionnaire. Some of the data include: socio economic and demographic characteristics, membership of associations, participation in the local level institution activities, credit financing activities of the households, productive activities and household expenditure details in the last one-month prior to study in these states. The list of micro credit groups was collected from States' National Poverty Eradication Programme (NAPEP) and other relevant information was also collected from publications of the Central Bank of Nigeria, Nigeria Agricultural Cooperative and Rural Development Bank and National Population Commission (NPC). A multistage sampling technique was employed for this study. Ekiti and Osun states with poverty incidence of 42.3% and 32.4% respectively were chosen for the study based on fact that the poverty situations in the two states are among the highest in southwest zone though they are agrarian in nature. The non selection of Lagos state with highest incidence of poverty (63.6%) in the region was because of the metropolitan nature of the state and also Ondo which is next to Ekiti state in poverty figure not selected because of homogenous nature of the two states (Ekiti was carved out of Ondo state in 1992). In each state, two Local Government Areas were randomly selected from each of the senatorial areas of the states. This was necessary for equal representation of the households of the microcredit groups. At the next stage, there was a random selection of microcredit groups in each of the selected local government areas depending on the number in each LGA. Hence,

the number of microcredit groups chosen is a function of the number of microcredit groups available in a particular local government area (probability proportionate to size). The proportionality factor used in the selection of microcredit groups is stated as:

Xi = n/N*30 ……………………………………………….................… (i)

Where Xi= number of microcredit groups to be sampled from a local government

n = number of micro credit groups in the particular local government area

N = total number of micro credit in all the local government areas

The desired total number of microcredit groups for the two states is 30

The last stage of sampling involved the random selection of households in each of the selected microcredit groups. In all, a total of four hundred and sixty-five (465) microcredit households were interviewed. However, only three hundred and ninety nine have meaningful information for analysis. Table 3 shows the sampling procedure and the map of the two states. This study employed descriptive statistics such as tables, frequencies, mean and percentages to profile socio-economic and social capital variables.

Table 3. Sampling Procedure for the Selection of Microcredit Households

State	Senatorial District	LGA	Town/village	Population of Microcredit Group	No of Sampled Microcredit Group	No of Questionnaire Distributed	No of Questionnaire Retrieved and Completely Filled
Ekiti	Ekiti South	Ikere	Aba Igbira, Aba Ayede, Agamo	25	2	30	30
		Ekiti East	Ilasa, Isinbode, Oruju, Araromi	19	2	30	30
	Ekiti Central	Ado Ekiti	Ajebamidele, Araromi, Ago Aduloju	50	5	75	55
		Ekiti West	Erio, Ikogosi, Ipole	22	2	30	30
	Ekiti North	Ikole	Ijesa Isu, Oke Ayedun, Itapaji, Irele, Ipao	26	2	30	30
		Moba	Erinmope, Igogo,	39	3	45	41
Osun	Osun Central	Ifelodun	Obagun, Eko Ende, Iba	40	4	60	39
		Boripe	Iragbiji, Ada, Aagbaorowuro	25	2	30	29
	Osun East	Ife Central	Modakeke, Ikoyi	30	3	45	30
		Atakunmosa East	Iperindo, Iwara, Ipole	24	2	30	28
	Osun West	Isokan	Apomu, Ikoyi	22	2	30	27
		Ayedaade	Ode omu , Orile Owu	26	2	30	29
Total				348	30	465	399

Source: Field Survey, 2011

RESULTS AND DISCUSSIONS

Table 4 shows that 48.9 per cent of the household's sourced credits from Cooperatives as their most available source of credit for their businesses and consumption needs, 15.5 per cent obtain credit from banks and 23.8 per cent use personal savings annually. The local money lenders accounted for 4.0 per cent, while the friends/family constituted about 4.5 percent. Government agencies are used by about 3.3 per cent. The implication of more households sourcing credit from cooperatives is based on the belief from members' assurance of flexible credit in terms of interest rate, social and spiritual benefits. Table 5 shows the credit characteristics of the households in the study area. The result shows that average interest rate in the study area was 10.6 per cent. The distribution of interest rates charged by the microcredit sources shows that commercial banks charged the highest interest rate, and the least is credit from friends/family. The result supports the finding of Yahaya (2011) that microfinance has significant role to play in the economy. Households' heads travel an average distance of 1.16 kilometres to get to the financial institutions for credit. The farthest credit source to households is commercial banks. The demand for credit is expected to decrease as distance increases. Households travelled a distance of about 3.0 kilometres to get to the nearest commercial banks.

Table 4. Credit Sources of Households per year

Credit source	Percentage
Bank	15.5
Cooperative	48.9
Governmental agency	3.3
Local money lender	4.0
Personal savings	23.8
Friends/ family	4.5
Total	100.0

Source: Field Survey, 2011

Payback period for loans was about seven months. Government agency credits have the longest payback period of 9.15 months while other credit sources have payback period of less than six months. The implication is that these loans are short terms and borrowers are expected to invest their loans in business activities that are capable of yielding quick returns. The time lag for credit is the period between when a loan is applied for and when money is given. The lag period is used to process the loan application, or wait for the next meeting of the loan approval committee, or wait for the next revenue drive which may be the next meeting day, or the period used to investigate the borrower and market situation (Agom, 2001). The time lag for credit was four weeks and five days on average. Commercial banks were found to have longest time lag (5.32 weeks) among the credit sources while the least was governmental agency (3.61 weeks). In order to purchase inputs, the rural poor need to be able to obtain production loans as when due (Okoruwa and Oni, 2001). An average of ₦31,068.42 was requested as loan while the average amount granted was ₦15,739.35. The Granted/Requested ratio is 0.44 (gap in credit request). Following from this, credit demanded is not commensurate with credit supplied as less than half of the amounts requested as loan from credit sources are granted. The result supports the finding of Opara (2010) that rural household's lack of finance to start or expand their business.

The various uses of credit are shown in Table 6. About 57.0 per cent of the households used loan to expand their businesses while 7.8 per cent used it to take care of their health and education needs. The result agrees with the finding of Opara (2010) that a rural household lacks finance to start or expend their business. Only 24.8 per cent of respondents used their credit to purchase inputs (agricultural or non-agricultural) and 9.8 per cent of the respondents purchased consumer goods and assets with their credit. The result showed that a greater proportion of the household microcredit was used for non-agricultural businesses across all the credit sources. However, spending on agricultural inputs was done by less than 25.0 per cent of households in all the microcredit sources with the exception of governmental agency and local money lenders which had 38.5per cent and 31.3 per cent respectively. It was observed that local money lenders and friends/family did not give microcredit for consumption purposes, whereas, households that obtained credit from banks, cooperatives and governmental agency spent 16.1%, 10.3% and 15.4% respectively on consumer goods.

Table 5: Credit Characteristics of Households

	Bank		Cooperative		Governmental Agency		Local money Lenders		Friends / Family		All Households	
Variable	Mean	SD	Mean	SD	Mean	SD	Mean	SD	Mean	SD	Mean	SD
Interest charged (%)	15.40	2.68	9.53	3.95	8.61	2.62	11.72	3.61	7.72	4.61	10.60	2.35
Credit Distance (Km)	2.58	0.25	1.13	0.66	0.97	0.03	0.76	0.15	0.34	0.11	1.16	0.37
Payback period (month)	5.00	3.05	7.93	2.57	9.15	3.56	5.44	3.22	6.44	1.22	7.30	4.63
Time lag (Week)	5.32	4.77	4.49	1.36	3.61	1.33	5.11	2.25	5.11	2.25	4.65	3.35
Amount Requested (Naira)	31779.03	19923.16	29594.87	18320.34	27692.31	19106.65	40312.50	18568.02	32777.78	18568.02	31068.42	23247.22
Amount Granted (Naira)	15987.78	772.15	16226.67	940.72	11538.46	898.71	13125.75	998.91	17611.11	998.91	15739.35	1026.81
Gap=G/R	0.50		0.55		0.42		0.33		0.54		0.44	

Source: Field Survey, 2011

Table 6. Uses of Credit by Households

	Bank	Cooperative	Governmental agency	Local money lenders	Friends / Family	All Households
Credit Use	%	%	%	%	%	%
Non –agric business	56.5	60.0	46.2	43.8	72.2	57.6
Human Capital development	4.8	7.7	0	6.3	11.1	7.8
Agric inputs	22.5	22.1	38.5	31.3	16.7	24.8
Consumer goods	16.1	10.3	15.4	0	0	9.8
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Field Survey, 2011

Table 7 presents the constraints faced by rural households in sourcing microcredit. The major constraint among the households is credit delivery. Majority of households (45.9 percent) identified non-availability of credit as at when needed (especially for purchasing production inputs). On the other hand, 19.3 percent of the households interviewed were unable to cope with credit protocol, thereby limiting their sourcing from formal credit market. Collateral requirement is also an important constraint in credit demand among rural households. Small asset endowment is an impediment to credit and it limits what households can pledge as collateral in the study area. High interest rate charged (12.5 percent) was the reason why households could not demand for credit. Furthermore, 10 percent of the household heads were unable to access credit information while 1.8 percent of households' could not get guarantors to secure them in the credit market. However, credit information was identified as a major constraint by 6.5%, 16.4% and 11.1% of households that patronised banks, cooperatives and friends/family respectively. As for protocol being a constraint in credit market, an interesting result was observed among the households that applied for loan from all identified credit sources. The result reveals that a higher level of paper work and politicking was required to secure loan from governmental agency (76.9%), cooperatives (31.8%), friends/family (11.1%) and banks (3.2%) respectively whereas local money lenders involved little or no paper work. Collateral as constraint in credit markets shows that only 56.5%, 3.1% and 7.7% of households were hindered by their inability to provide the required collateral for the banks, cooperatives and governmental agency respectively. High interest rates accounted for 32.5%, 6.2%, 15.4% and 6.2% of low demand among the households that applied for microcredit from the banks, cooperatives, governmental agency and local money lenders respectively.

Table 7: Household's Constraints in Credit Market

	Bank	Cooperative	Governmental agency	Local money lenders	Friends / Family	All Households
Reasons for Credit rejection	%	%	%	%	%	%
Information	6.5	16.4	-	-	11.1	10.0
Protocol	3.2	31.8	76.9	-	11.1	19.3
Collateral	56.5	3.1	7.7	-	-	10.5
Guarantor	-	3.1	-	-	-	1.8
High Interest	32.5	6.2	15.4	6.2	-	12.5
Delivery	1.6	39.5	-	93.8	77.8	45.9
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Field Survey, 2011

Table 8 shows sources of loan repayment by rural households in the study area. About 11.5 percent of the households repaid the loan through money realised from the sales of their produce while 32.3 percent of respondents who invested in productive activities were able to repay from their profit/dividends. About one-quarter of respondents repaid from salaries from paid jobs. Remittance from children and relatives was the source of repayment by 4.5 percent. The remaining 5.8 percent of the respondents were unable to pay back the borrowed loan (defaulted). The result also shows that 37.1%, 43.0%, 53. 8%, 12.6% and 11.1% of households that obtained microcredit from the banks, cooperatives, government credit programmes, local money lenders and friends/family respectively were able to repay borrowed credit and interest charged fully from profit realised from sales of produce. Salaries from paid employment represented about 29.0% and 43.8.1% of credit repayment from the banks and local money lenders respectively while only 15.4% of microcredit from governmental agency was repaid through this source. On the other hand, in a situation of high indebtedness by the households, the sales of assets and other properties were the last option. In the study area, the highest payment which was 25.0% was done by households disposing of their valuable assets. The rate of default was very small in all the microcredit sources with the local money lenders and governmental agency having the lowest. These findings have confirmed the earlier and long-held belief that local money lenders have high loan recovery rate.

Table 8. Household Sources of Loan Repayment

	Bank	Cooperative	Governmental agency	Local money lenders	Friends / Family	All Households
Sources of Loan repayment	%	%	%	%	%	%
Default	4.8	6.7	0	0	5.6	5.8
Sales of produce	37.1	43.0	53.8	12.6	11.1	11.5
Salary from paid job	29.0	22.6	15.4	43.8	16.6	24.8
Remittance	6.5	3.6	7.7	18.8	5.6	4.5
Sales of property	22.6	24.1	23.1	25.0	11.1	21.1
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Field Survey, 2011

Table 9 shows collateral requirement for loan by credit sources. Majority of the respondents (74.2 %) obtained credit without mortgaging anything. The remaining 25.8% has to provide one valuable material or another in case of default. In all the sources, 29.0% and 2.6% of microcredit from banks and cooperative respectively required guarantors before it could be approved, whereas 6.5%, 29.2%, 38.5%, 12.5% and 11.1% of households that sourced their credit from bank, cooperatives, governmental agency, local money lenders required sales or future harvest as collateral. About 4.8%, 12.5% and 11.1% of microcredit from banks, local money lenders and friends/family respectively required land as collateral, while the remaining did not ask for any. However, 3.2% and 11.1% of microcredit from banks and friends/family respectively made buildings mandatory collateral for microcredit to be released.

Table 9. Collateral Requirements for Loan

	Bank	Cooperative	Governmental agency	Local money lenders	Friends/Family	All Households
Collateral	%	%	%	%	%	%
None	56.5	68.2	61.5	75.0	66.7	74.2
Guarantor	29.0	2.6	0	0	0	5.5
Sales/future harvest	6.5	29.2	38.5	12.5	11.1	17.5
Land	4.8	0	0	12.5	11.1	1.8
Buildings	3.2	0	0	0	11.1	1.0
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Field Survey, 2011

CONCLUSION

The basis of this study is centred on the significant role of microfinance in transformation of the rural financial system in Southwest, Nigeria. Based on the empirical evidence emanating from both descriptive and inferential statistics employed for this study, it could be concluded that formal and informal credits coexist in rural Nigeria. It is evident from the results that the credit markets are functioning below their potential as the credit demand of households are not being satisfied since less than half (44.1%) of their credit needs were met. Findings in this study therefore have significant policy implications for addressing the credit demand and supply in rural Nigeria. The results further show that friends/family and cooperatives sources offer households greater access to credit in terms of volume, pay-back period and interest rates. It is suggested that the involvement of both private and government organisations in credit delivery should be strengthened in the area of volume and coverage.

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Chapter 12

IMPACT OF MICROFINANCE ON OCCUPATIONAL CHOICE AND PERFORMANCE OF WOMEN ENTREPRENEURS

Oluwatosin **OYETAYO**

INTRODUCTION

Since the last two decades, women have entered the field of entrepreneurship in greatly increasingly numbers. The routes women followed to take leadership roles in business vary and most of them have overcome or worked to avoid obstacles and challenges in creating their businesses (Aderemi et al., 2008). Whether they are involved in small or medium scale production activities or in the informal or formal sectors, their contribution to output and value added in the manufacturing sector is substantial, even though it remains partly invisible in official statistics. Women entrepreneurial activities are not only a means for economic survival but also have positive social repercussions for the women themselves and their social environment (UNIDO, 2001). The growth of their businesses has also contributed to the global economy and the economies of their immediate communities and countries (Gundry and Welsh, 2001). Women entrepreneurship in Nigeria is common in the informal sector and activities in this sector seem to be invisible, along with their contribution and needs. Despite government programs aimed at reaching small scale entrepreneurs, women as a group are not considered for assistance. A major reason for this is that most of the enterprises women engage in, such as petty trading, dressmaking, hairdressing, food processing, and small scale manufacturing, fall outside the census of production surveys. These surveys normally include enterprises employing 10 or more people (Soetan, 1995). Women have limited access to critical resources like education, land, technology and credit. Hence, the notion of informal sector captures certain peculiarities such as informality of business organisation, use of rudimentary technology, lack of separation of consumption and production, ease of entry and exit, reliance on family labour and apprentices and small requirements for capital.

By the tradition of some cultures in Nigeria like the Yoruba, Ibo, Hausa, Bini, women are not expected to be involved in occupations that will take them outside their matrimonial homes; they are rather expected to manage the family and "be submissive to their Husbands" (Ehigie and Idemudia, 2000). However, in the recent times, women are increasingly expected to work when they complete either their vocational training or educational careers, hence there is a decline of domestic work as an occupation (Ehigie, 2000). Thus, the number and percentage of wives and mothers in the labour force are increasing (Menaghan and Parcell, 1990). However, husbands opt for their wives to engage in less demanding occupations, especially non-career occupations, characterised by micro and small scale businesses in Nigeria. The South Western Nigeria basically made up of the Yoruba speaking tribe, has at its centre, Lagos which co-incidentally is the commercial hub-nub of the country. The state has

witnessed the evolution of the highest number of women entrepreneurs (UNDP, 1996). Their activities cover areas in small and medium scale manufacturing, processing and service industry. The activities of these women has had a spiral effect on the commercial activities of women in nodal towns to Lagos as they are either involved in producing the raw materials needed to feed the major city or are receiving the ones produced from the major cities for onward distribution to consumers in their location

Microfinance Institutions consist of organisations and agents that engage in relatively small financial transactions using specialised, character-based methodologies to serve low-income households, small farmers and others who lack access to the conventional banking system. They may be informal, semi-formal (that is legally registered but not under the Central Bank regulation), or formal financial intermediaries (Steel, 2006). Previous scholarly research and development reports have shown that women entrepreneurs form a good percentage of the total clientele of the microfinance institutions. Microcredit summit campaign report (2000) reveals that women comprise nearly 74% of the 19.3 million of the world's poorest people now being served by Microfinance Institutions, Banks, NGOs and Traditional/ Non-Bank financial intermediaries. It is reported that women entrepreneurs are more prudent, effective and display a sound knowledge of financial management when it comes to small businesses. This is evidenced by the commitment they display in their membership of microfinance programs; attending meetings regularly, remitting their savings and making on –time repayment of loans. It is argued that women see microfinance as their last and only hope of access to the much desired external finance needed to grow their business and as such will do all they can to keep it. Several NGOs, Rotating Savings and Credit Societies of trade associations, Community and Religious Cooperative societies and the recently introduced Microfinance banks have all emerged with a special focus on women owned businesses. Activities of Country Women Association of Nigeria (COWAN), Family Economic Advancement Programme, Lift Above Poverty (LAPO) all give credence to the aforementioned.

At an international conference in 1998, donor agencies and governments reviewed their commitments to advancing women, regenerating environmental resources and providing sustainable livelihood for all using the vehicle of microfinance (Iheduru, 2002). It is believed that microfinance programs constitute and provide the drive to develop a "broad access" to the financial resources crucial to the poor (among whom women comprise the majority), in order to provide the basic requirements for sustainable development. As a result, the World Bank, United Nations Development Program (UNDP), United States Agency for International Development (USAID), Development and Peace of Canada, EZE of Germany and the Catholic Agency for International Development of the Netherland have all made funds available to microfinance ; non-governmental organisations in Nigeria with varying levels of success.(Anyanwu, 2004). A survey by the special unit on microfinance of the United Nations Capital Development Fund (SUM/UNCFD) of 29 Microfinance Institutions revealed that approximately 60% of these Institutions' clients are women. Six of the 29 focused entirely on women. Of the other 23 mixed sex programs, 52% of clients were women. However, the percentage of women clients decreased when "only individuals' loans" or "relatively high minimum loan amounts" were offered. Similarly, according to the USAID's annual Microenterprise Result Report (2000), approximately 70% of USAID- supported micro financial Institutions in Nigeria are Women driven. The expected outcome of any intervening program is to smoothen the consumption pattern, encourage financial independence and growth in the businesses of their clients. This is brought about by higher productivity which

makes them to contribute to the economy of their immediate community and the country as a whole. Women entrepreneurs are faced with a number of constraints in making the decision of the type of business activity to go into which have been mentioned in the background to the study. How then can the microfinance programs they belong to, help to co-ordinate the businesses of these women in order to overcome those constraints hindering their higher productivity and providing the opportunity and environment for women entrepreneurs to harness areas of business prospects? Specifically, this research addresses the following questions; Does membership in a microfinance program or not, affect the choice of business ventured into by women entrepreneurs in the area? Can the Microfinance Institutions (informal and formal) operating within the rural financial market bring about higher productivity in the businesses of the women entrepreneurs?

THEORETICAL AND CONCEPTUAL ISSUES

Schumpeter (1934) was of the view that financial institutions are necessary condition for economic development. This view has been variously corroborated by other scholars like Goldsmith (1969), Cameron et al. (1972) and Patrick (1966). Other theories reviewed for this study considers female empowerment through access to business loans in an environment where informality is the only affordable avenue for operating a business venture. The aim is to examine the choices of activity informal female entrepreneurs make when faced with patriarchal forms of business regulations that substitute for the absence of legal means for enforcing contracts in the informal economy. Basic economic theory supporting the empowerment potential of microfinance targeted at women emphasizes access to credit and the resulting opportunity for earning an independent income as the theoretical links to female empowerment through microfinance. In other words, involvement in income-generating activities should translate into greater empowerment for women. But, female empowerment is about improved ability to bring about changes that enhance women's well-being at the household, community, and national levels. Bringing about such well-being requires that women first acquire the power to change their social environment. Whether women can gain such power at individual, community or national levels obviously depends on a number of factors, including social, political, institutional, as well as purely economic, such as access to microfinance services. How these factors interact to affect female empowerment, therefore, warrant consideration.

First, in many developing countries, business formalization in order to access legal means for enforcing contracts is often a privilege available only to politically powerful entrepreneurs, given the prevalence in these countries of high costs of legality. For the vast majority of these countries' micro-entrepreneurs—including women— who cannot afford these high cost of legality (bribes collection by public officials are an example), the informal economy becomes a "gateway"–a framework for producing and/or selling legal goods albeit using illegal means.
Second, in the informal economy, patriarchal forms of business regulations substitute for the absence of legal means for enforcing business contracts and often emphasize the use of threat and violence as an enforcement mechanism (De Soto, 1989). Relative to men, this institutional feature of the informal economy put women at a comparative disadvantage for accessing certain lucrative markets (Gibbon 1995; Kabeer, 2001). For example, relative to male entrepreneurs, women may face limited access to crucial input markets necessary to effectively operate a high-productivity business venture. Example include labour markets– where lack of legal mechanisms for resolving contract disputes may exposed female micro-entrepreneurs to male employees' violence, and fertilizers markets which are often controlled

by male-only cooperatives. Due to these patriarchal practices, developing countries women still face trade-off that cause them to make decisions that are arguably disempowering, such as clustering in low-productivity activities, and/or relying on male family members (often their husband) as contract enforcers (Kabeer, 2001). Notwithstanding the above, intra household bargaining models have demonstrated that female empowerment is positively associated with the level of a woman's fall-back option, which, in turn, is shown to rise with her relative earned-income (Anderson and Eswaran, 2005; Basu, 2005). Yet, in the informal economy of developing countries, women continue to earn less than men, even when controlling for differences in literacy and education. In Bangladesh–a country that pioneered MFIs targeted at women–, there is evidence that self-employed men earn more than three times the income earned by self-employed women, while male informal micro-entrepreneurs earn about four times more than their female counterparts (Dasgupta and Barbattini, 2003).

Most of this disparity reflects the extent to which women enterprises differ from men's in terms of scale, items sold by traders, extent of diversification, access to effective networking (Kabeer, 2001). Given the prevalence of patriarchal practices in the informal economy, networking among female entrepreneurs may play an essential role in overcoming transaction costs induced by compliance with such practices. Understanding constraints to the emergence of large enough networks of female entrepreneurs can therefore shed light on the issue of female empowerment through microfinance. In the game-theoretic model developed by Sylvain and Jacques (2006), the study highlighted coordination failure that hinders the emergence of networks of female entrepreneurs necessary to overcome patriarchal business practices that limit female entrepreneurs' access to high productivity informal activities. In the model, women's entrepreneurship is assisted by an MFI which provides loan and training to all their clients. They focused on women's demand for venture capital and choice of activity as jointly determined by their ability to mitigate the transaction costs that limit their access to more productive business activities. A female entrepreneur must jointly choose the type of business activity she plans to operate informally and its size as determined by the amount of capital borrowed from the MFI of her choice. Operating a high-productivity informal activity puts a higher demand on a woman to link up with other women operating the same type of activity in order to generate collective resources necessary to overcome obstacles created by patriarchal business practices.

In his promotion of regional entrepreneurship, Pages (1993) advocates for "entrepreneurial ecosystems" which include networks of entrepreneurs as well as service providers. Key features of the entrepreneurial ecosystem he maintained are a "business culture that embraces start-ups (higher risk tolerance and entrepreneurs vs. Large firms" and the creation of a "vicious cycle of civic/ philantrophic leaders and mentors/ angels. Pages (1993) summarised his works by identifying entrepreneurial network as the hub of the entrepreneurial ecosystem having peer learning as the central role and four key activities: training, mentoring, investment screening and matching. Doub and Edgcomb (2005) maintained that in an entrepreneurial community, entrepreneurs constitute a sub-community based on a network of relationships through which support, resources and business techniques flows. It provides its peers with the conditions necessary to grow their firms. Jacques (2004) describes networking as involving how entrepreneurs blend tacit knowledge from experience with knowledge gathered from their personal and formal networks to "fine tune their opportunity perceptions". Sylvain and Jacques (2006) therefore posited that the more there are female entrepreneurs operating in such a network, the more able will this network be in enhancing women's success at operating high-productivity activities. Consequently, an essential feature of the

environment underlying women's entrepreneurship in the informal economy is the complementarity of their respective business strategies: a female entrepreneur's decision to tap into the range of high-productivity activities increases other female entrepreneurs' marginal gain from following suit. In the absence of a mechanism for inducing coordination of women's decision to link up in such a network, the non-cooperative game these women play admits two pure-strategy Nash-equilibria: a high-income equilibrium where all of them operate high-productivity informal activities, and a low-income equilibrium where they all remain confined into low-productivity ones, despite access to credit. Therefore, when the low-income Nash-equilibrium obtains despite women's improved access to credit, it must be that microfinance assistance to female entrepreneurship has failed to act as a coordination mechanism for the emergence of large enough networks of female entrepreneurs operating high-productivity activities.

Relationship between Source of Capital, Choice and Performance/Growth in Women Owned Businesses

Growth and performance of new business ventures are dependent upon strategic direction, access to resources, and execution of strategic and tactical decisions (Doub and Edgcomb, 2005). Right from the 1990's a number of papers have addressed such issues as Factors Influencing Business Growth. In much of the literatures, researchers identify a set of factors inherent in business owners (characteristics and behaviours) that appear to influence business success. Academics and practitioners like Reynolds (1997), Rogoff (2004) and Lichtenstein and Pages (2005), examine factors such as growth goals, human capital (education, work and business experience), financial capital and demographics (gender, marital status, state of parenting, ethnicity/race). Doub and Edgcomb (2005) further expatiated on the factors influencing business growth. They identified eight growth factors that influence business performance and growth. The growth factors were divided under the internal and external environment. The growth factors under the internal environment include (i) entrepreneurs' business growth goals, (ii) human capital (iii) personal assets (iv) demographics (v) business growth management skills and resources. The growth factors under the external environment include (vi) growth sectors and industries (vii) business regulation and financial support systems (viii) entrepreneurial communities and systems. They further identified business growth practices expected of micro-entrepreneurs and the intervening programs which they classified into two main categories: (a) Owners' business growth goals and life cycle stage; (i) increasing entrepreneurial education in the training curricula of intervening programs (ii) providing more intensive focus on key management issues that affect growth (or survival)- during core training and after core training and in program design. (b) build bridges to the business world by ;(i) connecting individuals to mentors', experienced business consultants and coaches (ii) incubating businesses with supportive and productive facilities and services (iii) building network of entrepreneurs (sector or industry based networking, networking across sectors beyond the small network of the bridging program, (vi)providing access to markets for fledging entrepreneurs that in turn, build networks and connections (v) improving personal and business financial readiness and fund availability for entrepreneurial clients

Strategic Choice

Carter, Williams and Reynolds (1997) argued that strategic choice is shaped by experiences to which individuals are subjected and that females and males have fundamentally different socialization experiences. Assuming that a different socialization experience would result in the development of unique capabilities that could compensate for a deficient set of founding

resources, they investigated performance differences of men and women-owned businesses.. The authors found that women-owned firms had higher odds of discontinuing, fewer resources at start-up (including industry specific experience in retail), and were launched on a smaller scale. They reported equal access to credit from formal lending institutions for men and women. Their findings supported the hypothesis that women used unique strategies to offset initial resources limitations. Another study of strategy found that women were more likely than men to develop strategies that emphasized product quality and less likely to emphasize customization or cost efficiency (Chaganti and Parasuraman, 1996). Women also used a relational strategy when working with employees and clients, focusing on creation and development of teams, mutual empowering, achievement, and perseverance. Relational theory evidenced potential as a framework for identifying and explicating women entrepreneurs' interactive style in their own businesses (Buttner, 2001).

Self-efficacy offered another possible explanation for women's choice of smaller retail and service (traditional) businesses rather than those in high technology, construction, and manufacturing (non-traditional). Anna et al. (2000) proposed a model a Combining venture efficacy, career expectations, and individual context as determinants of Industry selection. Women in traditional businesses had higher venture efficacy for opportunity recognition and higher career expectations of life balance and security and placed more importance on the financial support received from others. Non-traditional owners had higher venture efficacy for planning and higher career expectations for money or wealth. Barrett (1995) reported that men were more likely to choose businesses with a female image than were women to choose a business with a male image. Different business outcomes had long been a point of concern. Kalleberg and Leicht (1991) conducted a study analyzing the relationship between the owner's gender and personal characteristics, choice of industry, choice of organisational structure, and the survival and success of the business. The authors found that women-led businesses were no more likely to go out of business or be less successful than those led by men and there were no gender differences in earnings growth. This study stands in contrast to those showing women-owned businesses had lower sales volumes and lower incomes as a result of positioning in less profitable industries, as well as lack of access to capital, and inability to secure government contracts (Loscosso and Robinson, 1991; Loscosso et al. 1991). Another study found women business owners to have smaller annual sales and employment growth but no gender differences in return on assets (Chaganti and Parasuraman, 1996).

Initial resources

Several researchers examined the impact of human capital, risk preferences, and characteristics of the firm's operations on the capital structure of small firms, looking specifically at the ratio of debt to total capitalization. Male owners were found to use significantly more debt. The authors offered both supply and demand side explanations for this finding. They postulated that lenders may discriminate or that female entrepreneurs may be more risk averse (Scherr, Sugrue, and Ward, 1993). Coleman (2000) reported that lenders did indeed discriminate, but on the basis of firm size, preferring to lend to larger and more established firms, thereby limiting their involvement with women-owned firms which were generally smaller. Female owners tended to prefer internal sources to external financing. However the owner's sex was not an issue in predicting the choice of equity versus debt financing (Chaganti, DeCarolis, and Deeds, 1995). No difference was found by gender in the use of financial management services (Cole and Wolken, 1995), but, using data from Britain, Carter and Rosa (1998) found several significant gender differences in business financing.

Men used larger amounts of capital at start-up. Women were less likely to use financial instruments such as overdrafts, bank loans, and supplier credit. Coleman (2000), in a comparative study of men and women utilizing bank debt, found that access to financing did not differ by sex. Another study found that women-led businesses that used bank loans as a primary source of start-up capital outperformed those that used alternative funding sources. The authors stressed the importance of having a relationship with a bank in place at the time of the business launch (Haynes and Helms, 2000).

REVIEW OF EMPIRICAL STUDIES

From an empirical point of view, there is a case that women's attempt to access high productivity business activities may be subject to strategic complementarities. Available evidence reveals that most women who receive loans from microfinance institutions tend to be confined into low-productivity, low-capital activities, despite access to credit, and often despite having equal managerial credentials as men. In a case study of Bangladesh, Kabeer (2001) reports that while access to credit succeeded in increasing the rate at which women participated in economic activities, it failed, however, to increase the range of economic activities they have access to.

Lairap-Fonderson (2002), in a case study of Cameroon and Kenya, finds similar evidence. She argues that women micro-entrepreneurs are clustered within a narrow range of activities that offer virtually no opportunity for innovation, or for upgrading to more-lucrative ventures. This includes street-vending, operating food kiosks, selling second-hand clothes and unprocessed food, which are relatively low-capital, low-productivity activities, but which, in addition, face strong competition from cheap imports. She concludes that microfinance fail to lift women out of the confine of such low-capital activities. In a case study of Zimbabwe, Gibbon (1995) finds that rural women business activities tend to remain at a survival level, despite assistance from microfinance institutions. Anderson and Eswaran (2005) developed an intra household bargaining model which demonstrates the relative ability of earned income to nurture empowerment for women within the household. The model is tested to rural Bangladeshi data, which provides support for their model's prediction. McIntosh and Wydick (2005) develop a model of competition among potential entrants in the microfinance industry that highlights the misgivings of increased competition in terms of the performance and viability of microfinance institutions. Carter and Fletschner (2004) build a model of women's demand for entrepreneurial capital that explicitly incorporates into women's decision-making the effect of social norms prescribing gender behaviour. They use this model to argue that microcredit programs that relax women's capital supply constraints may have benefits that extend well beyond the direct beneficiaries. In Nigeria,

This research therefore builds around these literatures by emphasizing the need to explicitly organize female entrepreneurs in large enough business networks strong, effective and capable of mitigating patriarchal business practices that confine women in low-productivity activities through the co-ordination of a microfinance system adapted to the dynamism of the rural market. Consequently, based on the literature reviewed, the following hypotheses are formulated to serve as a guide;

1. External capital would independently influence the choice of business of the women entrepreneurs
2. Access to external capital would bring about increased level of business productivity which is a function of increased and better networking, increased demand for products,

reduction in trade barriers and patriarchal activities, increase in the positive perception of the business for women entrepreneurs.

METHODOLOGY

For the purpose of this study micro-entrepreneurs were divided into two types: (i) Micro-Entrepreneurs that are members of Informal Microfinance program such as Credit Cooperative and Thrift Societies in the past five years (ii) Micro-entrepreneurs that are members of Formal Microfinance programs such as Microfinance Banks. Three Microfinance banks; (CMFB microfinance, Olive microfinance and LAPO microfinance), Ten Credit Cooperative and Thrift Societies; (Orelope Busari (Iloye), Ayomikun (Iloye), Ogo-Oluwa (Adiyan), Ibukun Oluwa (Ajayi Egan, Atan-Ota), Alubarikaloju (Sango), Otitodun (Temidire), Agbelere (Sango), Olorundafepo (Ajibode), Itesiwaju (Ota), Irewole (Adelemo), were selected from the study area due to availability and financial constraint. These Microfinance Banks and Cooperative Societies represent others in the area since based on the theory of "in depth interview" all Cooperative Thrift and Credit Societies have somewhat similar mode of operation (Adeyeye, 2003). The sampling frame for the three Microfinance Banks drawn from their membership lists was 350 (this represents the total number of female micro-entrepreneurs who are their members), and the sampling frame for the ten Credit Cooperative and Thrift Societies also drawn from their membership list was 420, (this also represents the total number of female micro-entrepreneurs who are their members. From these sampling frames, selection of female micro-entrepreneurs for the study was done

The female owned microenterprises selected for this study were enterprises in the food and agricultural processing, local manufacturing (Adire and Batik; tie and dye), petty trading and service; hairdressing and tailoring sectors. Each selected enterprise had at most five employees. Hence, the cooperative societies and microfinance bank members were selected based on simple random sampling within the known and defined sampling frame. The simple random sampling for microfinance members was achieved by using the most basic method. A combination of questionnaires and structured interviews was administered to bank customers (female micro-entrepreneurs) at random. The number desired (100) for the sample was then drawn from the total number of questionnaires and result of interviews conducted. The same was done for members of Credit Cooperative and Thrift Societies and 100 members were drawn from the sample. Only the micro-entrepreneurs who fit into the criteria for selection were selected. In addition to the criteria for selection, it was ensured that these female owned businesses was not managed and funded with equity from other sources, also that the businesses must have been in existence since at least five years ago. The questionnaire and structured interviews used had eight sections. The specific areas in Ota I, II, and III covered are Oju-Ore, Dalemo, Toll-Gate, Joju, Estate, Iyana-Iyesi. For each of the eight sections, the scale adopted for measurement followed the five-point Likert or the Yes/ No format. The study assumed that in all the categories surveyed, female micro-entrepreneurs' membership of microcredit programs was exclusive i.e members do not belong to two programs at the same time.

Before the final administration of the questionnaire, a pre-test of the questionnaire on the three groups was undertaken. A total of fifteen respondents selected judgementally and equally from each category was used for the pre-test. Judgemental sampling is a non-probability sampling technique useful where the population is homogenous. A non-

probability sampling technique is frequently used in pre-testing the data collection instruments or procedures to be used in a larger research project (Raymondo, 1999).

Variable and Model Specification, Data Analysis

It's been established that constraints that determine the choice of the business will also, to a large extent, determine the success of the business (Jacques, 2005). The constraints form the independent variables while the expected business outcome which comes as result of the choice of business made forms the dependent variable. Of all the constraints, access to external source of finance which in this study is regarded as microfinance is singled out to perform a co-ordination role between the other constraints and the expected business outcome of the women entrepreneurs being considered. The variables are further specified below;

Integration into the larger market through networking
Measured by the number of social organisations belonged to by the entrepreneur which provide contacts for sale and purchase for the business at little or no cost.

Availability of demand for a product or service
This is measured by the quantity of stocks purchased and quantity sold at different periods.

Start up capital available to the entrepreneur (internal source of finance)
Measured by the amount of personal capital; personal savings, aid from family and friends at the start of the business.

Trade barriers (becoming a member of and be committed to a trade association)
Measured by the amount paid to become a member, length of productive hours spent within a year attending trade association meetings and the percentage of profit paid as association dues within a year.

Demographic details of the entrepreneur
Measured as the age, marital status, number of children (parenting), Gender, ethnicity/race (Doub and Edgcomb, 2005), location of business premises and the location of residence (distance-in between), place of birth, level of education (primary, secondary, tertiary), number of years spent as apprentice in a trade or vocational study).

Entrepreneurs perception of the venture
Measured as the level of success pre-empted and the suitability of venture to natural abilities and skills which usually influences the choice of business. This bothers on psychological variables like self-concept, managerial competence, business commitment, perceived work stress which determines perceived business success (Ehigie and Umoren, 2003).

Level of Business productivity
Percentage change in sales volume and revenue, % of stocks bought with cash/stocks bought on credit, % change in gross profit .

ACCESS TO EXTERNAL SOURCE OF FINANCE

This measured as the volume of credit received by the female entrepreneurs under study, the mode of operation, loan strategies adopted by the Microfinance Bank for their women entrepreneurs. Basically classified into outreach and sustainability, Gallardo Joselito et al. (1997) gives outreach scales as; amount of loans, average loan amount, number of borrowers, interest rate per year, loan recovery, credit technology, deposit balances, number of accounts while the scales for sustainability are given as operating efficiency (ROCE), deposit/loans, administration expenses/assets. It is established in literature that access to microfinance bank should provide a forum for bringing women together to foster networking, provide access to better marketing and technical innovation to boost demand and supply of their products, overcome patriarchal activities and reduce trade barriers, improve the skills and training acquired and also bring about improved and positive perception of the business for the women entrepreneurs. Hence; the impact of microfinance on choice and success of women entrepreneurs can thus be modelled as;

Level of Business productivity = f (Networking, Demand for goods or service, Internal Capital, Trade Barriers, Demographics, Perception, **External capital**)

Choice = f (Networking, Demand for goods or service, Internal Capital, Trade Barriers, Demographics, Perception, **External Capital**)

Where; networking, demand for goods or service, internal capital, trade barriers, demographics, perception and external capital are variables explaining choice (Aderemi et al., 2008). The model developed by Ehigie and Umoren (2003) for the analysis of psychological factors influencing perceived entrepreneurial success among Nigerian women in small-scale businesses is adopted in this study. They considered self-concept, perceived managerial competence, work stress and business commitment as important psychological variables for perceived entrepreneurial success among female entrepreneurs. Analysis was done using multiple regressions to show the joint prediction of perceived entrepreneurial success of female entrepreneurs by self –concept, perceived managerial competence, work stress and business commitment. Also, inter-correlation and partial correlation analysis of perceived entrepreneurial success, self –concept, perceived managerial competence, work stress and business commitment among female entrepreneurs

$$\text{Business Productivity} = \beta + \beta_1\text{Networking} + \beta_2\text{Demand} + \beta_3\text{InternalCapital} + \beta_4\text{TradeBarriers} + \beta_5\text{Demographics} + \beta_6\text{Perception} + \beta_7\text{External Capital} + \varepsilon_i \quad \text{.......... (1)}$$

A priori Expectation

It is expected that external capital will have a major influence on choice and business performance as the intervening variable. The other explanatory variables i.e networking, demand for product, internal capital, perception and demographics are all expected to have a positive relationship with the independent variable which is business productivity except for trade barriers. Trade barriers are expected to have negative relationship with business productivity. Trade barriers hinder business productivity as a result, the lower the trade barriers, the more business productivity we expect. Therefore for this study it is expected that;

(i) $\beta>0, \beta_1>0, \beta_2>0, \beta_3>0, \beta_4<0, \beta_5>0, \beta_6>0, \beta_7>0$

(ii) $R_{BUSP,\ EXTC} > 0$

Data Analysis

Aggregate scores were used to rank the questions in each section representing each variable specified in the model from most important to least important and the Yes or No according to each group. The first hypothesis was tested using the inter and partial correlation of choice, external capital and other independent variables.

Inter and Partial correlation of Business Productivity, Networking, demand for goods/services, internal capital, trade barriers, demographics, perception and external capital among female entrepreneurs

Informal

	BUSP	DEM	DMD	EXTC	PEC	NET	STRC	TRB
BUSP	1.000000	-0.018532	0.2090004	-0.056007	-0.119616	0.017758	0.545667	0.369214
DEM	-0.018532	1.000000	-0.137887	-0.295908	-0.185147	-0.088473	-0.301109	-0.177224
DMD	0.209004	-0.137887	1.000000	0.134735	-0.108369	-0.294321	0.345440	0.096177
EXTC	-0.056007	-0.295908	0.134735	1.000000	0.279033	0.081557	0.246816	0.003981
PEC	-0.119616	-0.185147	-0.108369	0.279033	1.000000	0.011038	-0.168414	-0.194760
NET	0.017758	-0.088473	-0.294321	0.081557	0.011038	1.000000	0.058003	0.418347
STRC	0.545667	-0.301109	0.345440	0.246816	-0.168414	0.058003	1.000000	0.286153
TRB	0.369214	-0.172246	0.096177	0.003981	-0.194760	0.418347	0.286153	1.000000

Formal

	BUSP	DEM	DMD	EXTC	NET	PEC	STRC	TRB
BUSP	1.000000	-0.032197	0.347893	0.255283	0.226243	0.134604	0.095309	0.386742
DEM	-0.032197	1.000000	0.123296	0.001035	-0.121219	0.003419	0.023902	-0.246447
DMD	0.347893	0.123296	1.000000	0.282608	0.258556	-0.016782	-0.025737	0.057458
EXTC	0.255283	0.001035	0.282608	1.000000	0.286350	0.155095	-0.043320	0.111759
NET	0.226243	-0.121219	0.258556	0.286350	1.000000	-0.080242	-0.043761	-0.207916
PEC	0.134604	0.003419	-0.016782	0.155095	-0.080242	1.000000	0.065023	0.055242
STRC	0.095309	0.023902	-0.025737	-0.043320	-0.043761	0.065023	1.000000	0.046289
TRB	0.386742	-0.246447	0.057458	0.111759	-0.207916	0.055242	0.046289	1.000000

DISCUSSION OF RESULT

In the formal category, the result reveals that external capital has a positive relationship with all other variables determining choice and business performance with the exception of start-up capital. It means therefore that the presence of external capital, put differently, female micro-entrepreneurs' involvement in a microfinance program (in this case formal) positively influences the workings and performance of other variables. External capital's negative relationship with start-up capital reveals that most micro-entrepreneurs that have adequate capital to run their business may not bother to be members of microfinance programme and vice-versa. In the informal category, the result reveals that external capital has a positive relationship with all other predictor variables except for demography. It is also observed that external capital has a negative relationship with the outcome of choice and business performance. It means that in this category the older female micro-entrepreneurs, more educated, more experienced and married may not be subscribing to external capital and vice-versa. The negative relationship between external capital and final output of choice and business performance shows that access to external capital in this category does not translate

to business success. This could be as result of shortcomings in process and style of distribution, inadequate loan capital or loan diversion.

The second hypothesis was tested using the multiple regression analysis to determine the joint influence of the independent variables on the dependent variable. Multiple regression showing the joint prediction of Level of Business Productivity by networking, demand for goods/services, internal capital, trade barriers, demographics, perception and external capital

Result Estimate

Informal

BUSP = 6.084618 + 0.3216TRB + 0.197570DEM – 0.31247EXTC + 0.11839DMD + 0.30084NET + 0.480751PEC + 2.864920STRC

t-statistic =	(1.4755)	(3.19327)	(1.90833)	(-1.95435)	(0.07629)	(-1.18210)	(1.33648)	(6.12180)
Std.Error =	(4.1237)	(0.10072)	(0.10353)	(0.15988)	(0.15518)	(0.25453)	(0.35971)	(0.46798)
Prob. (Sig) =	(0.1435)	(0.0019)	(0.0595)	(0.0537)	(0.9394)	(0.2402)	(0.1847)	(0.0000)

R^2 = 0.41871
R = 0.647
D.W = 1.02094
F-statistic = 9.467079
Prob.(F-statistic) = 0.0000

Formal

BUSP = -6.781406 + 0.321075TRB + 0.185332DEM + 0.104662EXTC + 0.546973DMD + 0.804169NET + 1.001795PEC + 0.71712STRC

t-statistic =	(-1.56040)	(4.627990)	(0.814009)	(0.532789)	(2.573548)	(2.720935)	(1.413305)	(1.005189)
Std. Error =	(4.34592)	(0.06937)	(0.22767)	(0.19644)	(0.21253)	(0.29554)	(0.70883)	(0.71341)
Prob. (Sig) =	(0.1221)	(0.0000)	(0.4177)	(0.5955)	(0.0117)	(0.0078)	(0.1609)	(0.3174)

R2 = 0.342807
R = 0.585
D.W = 2.10117
F-statistic = 6.855630
Prob.(F-statistic) = 0.000001

Informal

Almost all the coefficients of the specified variables have positive relationship with business productivity as expected even though perception, networking and demand are insignificant at 0.185, 0.248, 0.939 respectively. Start-up capital has a strong effect on business productivity (2.865) with a strong predictive strength in the level of significance of (0.0000). This is explained by the nature of women entrepreneurs in this category. They are mostly less educated, coming into the business as means of survival with little or no choice, access to loans at the initial stage is almost impossible hence they rely more on their personal capital built over time. Trade barriers with a coefficient of (0.322) even though not negative as expected shows that members involvement in informal microfinance programme and access to loan has reduced the effect of trade barriers on business productivity to a minimum degree. The level of significance of trade barriers in this category (0.002) shows its high predictive strength on entrepreneurs' business productivity. External capital's coefficient of (-0.312) shows a negative effect of funds sourced from informal microfinance (credit cooperative societies). However, external capital's level of significance of (0.054) reveals a high strength of this variable in determining business productivity. Negative effect could be as result of failure in disbursement mechanism and repayment structure, diversion of capital received into

some other things like consumption smoothening other than for business. Demography with a coefficient of (0.198) shows a positive effect but at a very low percentage even though it's predictive strength is significant at (0.059). This implies that age, marital status, experience and level of education is actually an important factor but it has very minor effect on the business productivity of the women entrepreneurs studied in this category. Generally, the R-squared for the estimate is low at 0.419. This can be explained by the low probabilities of some of the variables. The R (0.647) also reveals general positive relationship between dependent and independent variables. F-statistic of 9.467 at (0.000) level of significance reveals that the fitted line is a good and sufficient measure for estimating business productivity of women entrepreneurs in this category.

Formal

All the coefficients of the variables estimated have positive relationship with business productivity as expected, even though start-up capital, external capital, demography and perception all have very low and insignificant probabilities of 0.3174, 0.5955, 0.4177 and 0.1609 respectively. Just like in the informal category, Trade barriers with the coefficient of 0.3210, is also significant at 0.0000. The coefficient even though not negative as expected shows that members' involvement in formal microfinance programme and access to loan has reduced the effect of trade barriers on business productivity to a minimum degree. Level of Demand for product (DMD) with a coefficient of 0.1853 is also very significant at 0.011 indicating that the demand for product is an important factor determining business productivity in this category. Even though level of demand only explains about 18 percent of changes in business productivity for this category. Most of the women entrepreneurs that are members of the formal microfinance programme sell goods or services that are demand sensitive. Networking with a coefficient of 0.8042 and a level of significance of 0.007 reveals that this variable not only explains about 80 percent of changes in business productivity, but is also important factor determining business productivity in this category. This can be explained by the fact that formal microfinance brings together large network of women entrepreneurs unlike the pockets of associations involved in credit societies located in different areas. The formal microfinance programme provides a better platform for different trade and social associations to meet and interact, makes it possible for entrepreneurs to access some other advantages like training and seminars on effective or innovative methods of production of some of their products and also give entrepreneurs access to collective loans which is usually substantial when compared with loans from credit cooperative societies. This factor will also help reduce trade barriers.

Trade barriers just like in the case of informal even though not negative is reduced (0.3210) with a level of significance of (0.0000). This implies that trade barriers have affected about 32 percent of business productivity and is also an important factor determining productivity in this category. External capital's low coefficient (0.1046) and insignificance at (0.5955) can be explained by the fact that most of the entrepreneurs in this category have not subscribed to loans from their microfinance institution even though they have access to it. Generally, the R-squared for the estimate is low at 0.3428. This can be explained by the low probabilities of some of the variables. The R (0.585) also reveals general positive relationship between dependent and independent variables. F-statistic of 6.856 at (0.00001) level of significance reveals that the fitted line is a good and sufficient measure for estimating business productivity of women entrepreneurs in this category.

SUMMARY AND RECOMMENDATIONS

This study has revealed the differences and similarities in the impact of microfinance (formal and informal) on the occupational choice and business performance of women entrepreneurs in a local economy. From the result discussed, both sources of microfinance have been able to reduce trade barriers but not to a satisfactory level. It is also interesting to note that external capital which represents the main contribution coming from these institutions, have had little or no impact on the businesses of women entrepreneurs in both categories. In the case of informal, women in this group rely more on their personal funds as start up capital. Demography is also an important factor determining business productivity in this category. In the formal category, level of demand is an important determining factor for business productivity even though its estimated effect is not much. Networking is estimated to be a highly important factor determining business productivity and has actually had a high effect on business productivity.

From the above discussion, it is clear that women entrepreneurs' involvement in microfinance programs either formal or informal has its benefits. Their involvement in microfinance institutions is expected to give them access to loans and also help them overcome factors that are constraints to choice and business productivity. In both ways, some of these constraints have been mitigated while some persists. There is need for restructuring the mode and process of loan disbursement in both categories. It is observed that the strength of benefit derived in each category complements the other; therefore it is recommended that there should be a synergy in the mode of operation of the two classes of microfinance institutions placing emphasis on outreach and sustainability. The informal have their strength in outreach (i.e they have a larger clientele base and are closer to the entrepreneurs). While the formal are more organised more conscious of efficiency in their mode of operation. Women micro-entrepreneurs are encouraged to belong to both programs to enjoy their complementarities, Informal microfinance institutions (credit cooperative societies can become members of formal microfinance institutions to access more capital and benefit from the training and seminars offered by formal institutions. These they can pass on to their members, which will in turn bring about higher productivity and making good decisions on choice of business.

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Chapter 13

GROWTH AND RESILIENCE OF CREDIT COOPERATIVES IN VIETNAM

Hans Dieter **SEIBEL**

Nguyen Tam **THAC**

INTRODUCTION: DOES THE GLOBAL MELDOWN AFFECT SAVINGS-DRIVEN MFIs?

"The $32-billion microfinance sector has been pounded by the worst economic slowdown since the Great Depression," writes Joseph Rosta in the American Banker (1 Sep 2009); "default rates at MFIs are rising… And growth has pulled back significantly, with MFIs hampered by the capital constraints endemic to the financial market meltdown." Statements like this are not based on a random sample of microfinance institutions (MFIs). In fact, many MFIs which make headlines and are found on the *MIX Microfinance Information eXchange* have enjoyed disproportionate support from international investors and donors. MFIs which rely on their own resources – equity, deposits and retained earnings – and do not have a donor paying for their participation at international gatherings, among them credit cooperatives in particular, are less conspicuous. Paradoxically, least conspicuous are those savings-driven MFIs which occur in numbers too large to be individually listed, such as 4,600 Microbanking Units of Bank Rakyat Indonesia, 1,350 Lembaga Perkreditan Desa in Bali and 1,015 People's Credit Funds in Vietnam, to mention just these three subsets in Southeast Asia, totalling 7,000 MFIs. Have they been equally affected by the global meltdown? Does it make a difference in terms of resilience to crisis whether MFIs rely on their own resources rather than on those of donors and international investors?

In this paper we present a network of rural savings and credit cooperatives in Vietnam and examine how it's two segments, the rural People's Credit Funds (PCFs) and the Central People's Credit Fund (CCF), the latter with wholesale and urban retail services, have performed during the global crisis. At the same time this is a case study of the successful establishment of a network of savings and credit cooperatives as part of the formal financial sector, regulated and supervised as well as guided and trained by the central bank. Source of quantitative data on PCFs and CCF is the State Bank of Vietnam through CCF unless otherwise stated. This paper is based on field research in 2008; updates have been provided by CCF.

Credit cooperatives are a type of microfinance institution (MFI) which are, on principle, self-governed and self-financed. This at least is how they emerged in Germany in the mid-1800s (Seibel 2003), spreading from there to numerous countries around the world around the turn

of the 19th to the 20th century. In Europe, North America and a few other countries such as South Korea they retained their character as self-help organisations and became part of the formal financial sector. In Communist countries they became part of the command economy and lost their self-help character. In many developing countries they are held in high esteem by the government – so much so that the government has taken their governance into its own hands and generously supplied them with financial resources. This has rarely been to their advantage. In South and South-East Asia, respectively, India and Indonesia are two countries where the government, with well-meaning interference, has undermined the health of a century-old movement, resulting in a lack of services to members and the loss of member savings. There is a dearth of developing countries that could serve as models for the construction or reform of a sustainable self-reliant credit cooperative movement: Vietnam is one such country.

Within less then two decades Vietnam, emerging from the collapse of its command economy, succeeded in creating a conducive policy environment, captured some of the lessons of credit cooperative history and build a strong credit cooperative system. Yet, while Vietnam may serve as a model, it would be fatal if the Vietnamese credit cooperative system were simply duplicated. Every country faces the challenge of finding its own way in a given economic, cultural and political environment. In Vietnam, the Government examined the options, benefited from the experience of other countries, but replicated none. Instead it came up with its own innovation: People's Credit Funds (PCFs), self-help organisations under state control, seemingly a contradiction. The case of Vietnam shows that the world of cooperatives is more complex than indicated by the simple dichotomy of successful self-help movements vs failing state-supported systems. The newly established PCFs are self-managed and self-financed; yet they are part of a movement in which the State Bank of Vietnam (SBV), the central bank, has been in the driver's seat from the beginning. SBV has been in charge of designing the new system; it prepared its regulatory framework, integrated the network into the formal financial sector, supervised its progress and enforced prudential standards. Yet SBV has abstained from undue direct interference and from using, or abusing, the PCFs as credit channels or for other politically motivated purposes.

The PCF system has mastered several challenges since its establishment in 1993, including the closing of nearly 100 poorly performing PCFs by the central bank at the conclusion of the pilot phase. It is now facing a new challenge: a test of resilience under conditions of a global financial and economic crisis, which presents a real threat as Vietnam has been increasingly integrated into the world economy. There are two aspects to this test: the first pertains to the PCFs as local financial institutions with a rural membership of predominantly small savers and borrowers. The second aspect pertains to their apex, the Central People's Credit Fund (CCF), which manages liquidity exchange for the PCFs, but in order to make a profit also provides financial services to the general public, including companies and better-off individuals mostly in urban areas. One may expect that the two types of institutions differ in their exposure to the global crisis and perhaps in their resilience.

CREATING A CONDUCIVE ENVIRONMENT

Since 1976 rural credit cooperatives were part of the command economy of Vietnam. By the mid-1980s, there were about 7,200, covering most of the communes, each of which covers some three to four villages. Their main functions were to collect small deposits and to provide credit to production cooperatives, farm households and small state-owned

enterprises (SOEs). (Boi and Hung, 1992: 17-19) Yet, the continual decline in the production of rice and other commodities and, finally, a period of hyperinflation led to the collapse of the economy, which included the credit cooperatives.

The Government responded to the crisis with a new policy, *Doi Moi* ("renovation"), aiming at the introduction of a market economy. Structural reforms were geared to dismantling the extensive system of controls; financial reforms focused on the consolidation of public finances and the reduction of inflation. In 1988 the mono-tier banking system was transformed into a central bank (State Bank of Vietnam, SBV) and four state-owned commercial banks (SOCBs). This was followed in 1989 by a policy of monetary restraint, with a dual focus on limiting the supply of credit to state enterprises and increasing interest rates to positive real terms. Economic reforms included a return to private household farming and a reduction of restrictions on private sector activities. At the same time, Vietnam abandoned its policy of international dissociation and entered into economic relations with the convertible area. The impact on output growth and monetary stability was dramatic (IMF, 1990: 26; WB 1991: i) – achieved under an American embargo and without significant external support.

The 1989 reforms revealed the weaknesses of the financial system, the four SOCBs being but arms of the SBV, and the SBV failing to carry out its central bank functions. The Government thus moved on to new reforms. In 1990 the Ordinance on Banks, Credit Cooperatives and Finance Companies was passed, providing a legal framework for a differentiated financial infrastructure, comprising SBV as the monetary policymaker and financial regulator, universal banks in government, private and partially foreign ownership, limited-service financial institutions and credit cooperatives. This was followed by a banking decree in 1991, which accorded SBV supervision authority over the banking sector. Note should be taken that a legal framework was created for credit cooperatives before the first steps were taken of establishing them. Of crucial importance for the future members of rural credit cooperatives was a new land law passed in 1993, which provided for land use certificates that can be sold, leased, inherited and mortgaged – in a country without private land ownership. (IMF, 1990: 18-27, 58; Seibel, 1992: 48-57; World Bank, 1991, 1993)

With ups and downs, there has been remarkable growth over the past two decades. Private enterprise is now the backbone of the economy. Out of 12,000 SOEs, around 10,000 have been fully or partially privatized, including one of the SOCBs. Most impressive has been the impact of Vietnam's new agricultural policy. Private land use rights have replaced collective agriculture; and free input purchasing and produce marketing have replaced administrative factor allocations. Harnessing the power of millions of smallholders as private entrepreneurs, the result has been an agricultural miracle, happening almost overnight. In 1989 Vietnam turned from a net importer to an exporter of rice; in 1993 it became the world's third-largest, and in 1996 the second-largest, rice exporter. It is now also a major exporter of coffee and other farm, forest and fisheries produce. Economic performance has been paralleled by social performance. Between 1990 and 2004 the percentage of the population living on $1 or less per day (at purchasing power parity) declined from over 50% to below 10%. Today 94% of households have electricity; almost all children attend primary school; nearly two-thirds stay on to upper secondary level. Free enterprise, free trade and sensible state finances have been the key factors of transformation. Huge problems remain, among them a poor infrastructure, pervasive corruption and, as The Economist (2008: 4, 9) stated, "the glacial speed of legislative and bureaucratic processes".

DESIGNING A CREDIT COOPERATIVE SYSTEM

As part of a stated financial sector reform policy, the financial institutions law of 1990 provided a legal framework for the establishment of a rural credit cooperative system; subsequently they were placed under the law on cooperatives of 1996, the law on credit institutions of 1997 and the decree on the model statute and operation of the PCF of 2001, amended in 2005. In 1991 a team from SBV and several government agencies was formed to examine the options. Its first decision was to rule out the option of credit cooperatives as local agents of rural shareholding banks or of the state-owned Vietnam Bank for Agriculture (VBA), arguing that, as agents, they would lack autonomy and responsible management and would therefore not evolve into viable institutions. In a second step the team visited the Grameen Bank in Bangladesh, cooperative banks of the Raiffeisen and Schulze-Delitzsch type in Germany and the Caisses Populaires Desjardins, or credit unions, in Canada, which are a spin-off, in 1900, of the German credit cooperative system. This resulted in a dialogue with Développement international Desjardins (DID) and the decision for a pilot project for the period 1993-2000, aided by DID (2008). To avoid any resemblance to the defunct system which had given cooperatives a bad name in Vietnam, a new name had to be found: People's Credit Funds (PCFs) – cooperative in nature but not in name. The PCF network was designed to comprise three types of institutions: (a) primary societies (PCFs) established in 1993; (b) a Central People’s Credit Fund (CCF), established in 1995 together with Regional People’s Credit Funds (RCFs); and (c) the Vietnam Association of PCFs (VAPCF), established in 2006.

At inception a steering committee was formed with the task of establishing a network of PCFs and guiding them throughout the duration of the pilot project. The committee comprised SBV as the lead agency, the Ministries of Finance, Planning and Investment, Government and Cooperatives, and the Vietnam Cooperative Alliance. Its executive committee was placed in the SBV and consisted of officials of the SBV. To implement the establishment of PCFs, steering committees were formed at all levels of the administrative structure: central, provincial, district and commune. This was paralleled by a focal involvement of a newly established People’s Credit Institution Division of SBV in Hanoi and in all its branches. DID provided technical support services during the start-up phase. In 1996 the Asian Development Bank (ADB) approved a loan to the PCF network, comprising $14.8 million for refinancing and $1.395 million for equipment and training. SBV provides a regulatory framework for the PCFs and licenses them. Through its branches it supervises their performance and compliance. SBV has the authority of closing non-performing PCFs. Prudential standards include a minimum capital requirement of D100 million (equivalent to $16,977 in 1993, around $6,000 in 2008; increased to D500 million in the provinces for new PCFs and D1 billion in Hanoi and HCMC in 2008), a risk-weighted capital adequacy ratio of 8%, a fixed asset ratio of at most 50% of equity, reserve requirements (placed interest-free at SBV) of 1% of Dong deposits and 8% of US$ deposits, a single borrower limit of 15% of equity (up from 10% at inception), adequate maturity matching (at most 10% of short-term deposits used for term loans) and observance of SBV’s provisioning rules.

PCFs are subject to three types of oversight: daily internal control; regular random inspections by the SBV branch; and remote supervision by the SBV supervision department. PCFs send their financial and credit reports to the SBV branches as well as to the CCF branches. The SBV branches forward them to the PCF Division of the Supervision Department and the Credit Cooperative Institutions Department (CCI) of SBV. Online reporting is expanding, but

not yet universal. Based on the monthly report, an SBV branch may intervene directly in case of irregularities or poor performance. SBV provides a mandatory training program free of charge. Two units are involved: the People's Credit Institution Department (PCID) and the Center for Banking Research and Training (CBRT), which designed the curriculum and training materials. The actual training proceeds in two steps: CBRT trains the officers of the SBV branches; and the SBV branches train the PCF board members and staff. This is followed by training-on-the-job and monitoring by SBV officers instructing the PCF staff in all practical affairs.

PCFs are voluntary organisations, initially with at least12, since 1997 30 members living in the same commune. They are based on the principles of self-help, self-reliance, self-management and democracy. More concretely, they are formed by their members; self-financed through shares, deposits and retained earnings; professionally managed by a team of qualified employees under the control of a board; and the board is democratically elected by the members, all with equal voting rights. Unlike the former credit cooperatives, they are part of a network, which functions as a nation-wide system of mutual support. It provides model bye-laws and various apex services, including access to liquidity exchange and refinancing by a central fund. 95% of the PCFs are rural; given the ample supply of financial services in cities, SBV discouraged the establishment of urban PCFs. After an initial two tax-exempt years, PCFs are subject to income tax up to 28%, varying by province. The board of directors consists of three to nine persons elected by the general assembly for a five-year term. Board members are usually experienced and respected citizens who played a leading role as founding members. The board decides on capital increases, interest rates within the range set by SBV, recruitment and expenditure. It also appoints the managing director, to be approved by the general assembly and confirmed by the local SBV branch. The chairman of the board may also serve as managing director. The credit committee decides on loans exceeding the managing director's lending authority. Internal control is placed in the hands of a supervision committee elected by the general assembly.

In the early years the Local People's Committee (LPC) took considerable influence. Establishing viable and sustainable financial institutions was a major concern of local government, aiming at the recycling of local financial resources and preventing their siphoning off to urban areas. The LPC first helped carrying out a feasibility study, preparing a business plan and organizing the establishment process including the application for a license. Subsequently it took joint responsibility with SBV to avoid a repetition of cooperative failure. Direct influence on management and business decisions has reportedly subsided with increasing experience of management and staff and growing confidence in cooperative self-management. The LPC still has a role to play when problems arise, to facilitate collection in case of defaulting, or to provide land for the premises of the PCF. Management and staff have to be qualified and are remunerated for their work. SBV has a training program in bookkeeping, loan appraisal, loan administration, internal control and cooperative management. Mandatory and voluntary training continue life-long, provided by SBV, CCF, VAPCF and other institutions. Deposits are mobilized from members and non-members, individuals and organisations. PCFs offer attractive conditions: proximity which entails lower depositor transaction costs; diversified products including demand, term, regular and discount deposits (with prepaid interest); higher interest rates than in banks; and term deposit insurance under the Vietnam Insurance Company (BAOVIET). As a result deposits usually account for three-quarters or more of loans outstanding: a solid basis of self-reliance. Surplus deposits are

placed at the central fund. Other financial services include bill payments and remittances. PCFs may also act as trustee agencies for development programs.

Lending is restricted to members in good standing. PCFs may lend up to 10% of their portfolio to poor non-members. About 30% of the borrowers are women. The portfolio of PCFs is generally diversified, comprising loans for agricultural production and processing, crafts, services, trading, consumption and emergencies. The emphasis is on productive loan purposes, particularly in agriculture, the main occupation of most of the members. Loans for socioeconomic organisations and small enterprises are mainly for equipment, modernization and expansion. Procedures are kept simple. The appraisal process, collateral, loan loss provisioning, record-keeping and reporting are regulated by SBV. Most loans are secured, except small loans and loans to the poor. The most common collateral is land use and house ownership certificates – largely a formality as these are difficult to alienate. Both loans and deposits are mostly short-term (up to one year). Interest rates were liberalized in 2002; but PCF boards felt morally obligated to keep lending rates low. As inflation rose from 6.6% in 2006 to 12.6% in 2007 and 22% in 2008, SBV returned to a restrictive interest rate policy, in an ill-guided effort to fight inflation. In May 2008, SBV set ceilings for PCFs at 21% p.a., lowered in December to 16.5%. Deposit rates were around 8% to 9% p.a. in 2008, leaving an extremely narrow margin which requires great efficiency of the PCFs.

GROWTH OF THE PEOPLE'S CREDIT FUNDS

The pilot project establishing PCFs started in July 1993 and was to cover a seven-year period. The first 179 PCFs were set up during the second half of 1993 and in 1994. Overall the network has evolved in three phases, which are not sharply divided, as the number of PCFs, their membership and the volume of financial transactions did not evolve at exactly the same pace.

The start-up phase, 1993-1996, is marked by rapid growth in the number of PCFs and members, resulting in 847 PCFs with 378,978 members by the end of 1996. Total loans outstanding reached $91.2 million, deposits $60.3 million (66% of loans) and equity $9.05 million. Disbursements in 1996, the first year for which data are available, exceeded loans outstanding by more than 100%, indicating very short loan periods. The second phase, 1997-2002, is marked first by a slowing-down of growth over a two-year period, followed by consolidation based on an evaluation after which SBV closed nearly 100 non-performing PCFs. By the end of 2002 the number of PCFs had fallen from a peak of 977 in 1998 to 888, while growth in the number of members was only slightly affected, reaching 850,781 in 2002. Loans and deposits continued to grow at a low rate, reaching $207 million and $154.0 million, respectively, at the end of 2002. Equity grew only slightly to $13.0 million. Borrowings from the central fund (CCF), the newly established refinancing apex of the network, started in 1997, with $18.4 million (16% of loans outstanding), and grew to $40.0 million (20% of loans) in 2002. The current phase, since 2003, is characterized by three trends: cautious growth in the number of PCFs, with SBV closing about 3 PCFs per year until 2007 (none were closed since 2008); continual growth in membership; and rapid growth in loans and deposits, indicating the members' trust in their cooperatives. By the end of 2008, the network covered 1015 PCFs with 1.35 million members. Total assets stood at $982.2 million, loans outstanding at $833.0 million, total deposits at $726 million – the main source of loanable funds, accounting for 87% of the portfolio. Equity had increased to $45.9 million, equivalent to 5.5% of the portfolio. At $131.8 million, borrowings fell back to 16% of the portfolio.

Disbursements in 2008 exceeded loans outstanding by 56%, indicating that average loan periods continued to stay under one year – see table 2.

Highlights of the evolution of the PCF network are summarized in Table 1.

Table 1: Highlights of the evolution of the network of PCFs

July 1993	Start of the pilot project establishing People's Credit Funds; first 179 PCFs established during 1993-94
1995	Central People's Credit Fund (CCF) established, together with a growing number of Regional People's Credit Funds (RCFs)
1997	Slow-down of expansion
1999	Assessment and subsequent consolidation of the network; nearly 100 PCFs closed in 1999-2002
2000	Official conclusion of pilot phase in March 2000; network reorganized into two tiers, PCFs and CCF; RCFs converted into CCF branches
2002	Growth of loans and deposits resumed
2003	Cautious expansion of the network resumed
2006	Vietnam Association of PCFs (VAPCF) established
2010	CCF expected to be converted into a commercial bank
2020	1700 PCFs expected to cover about 6,000 communes

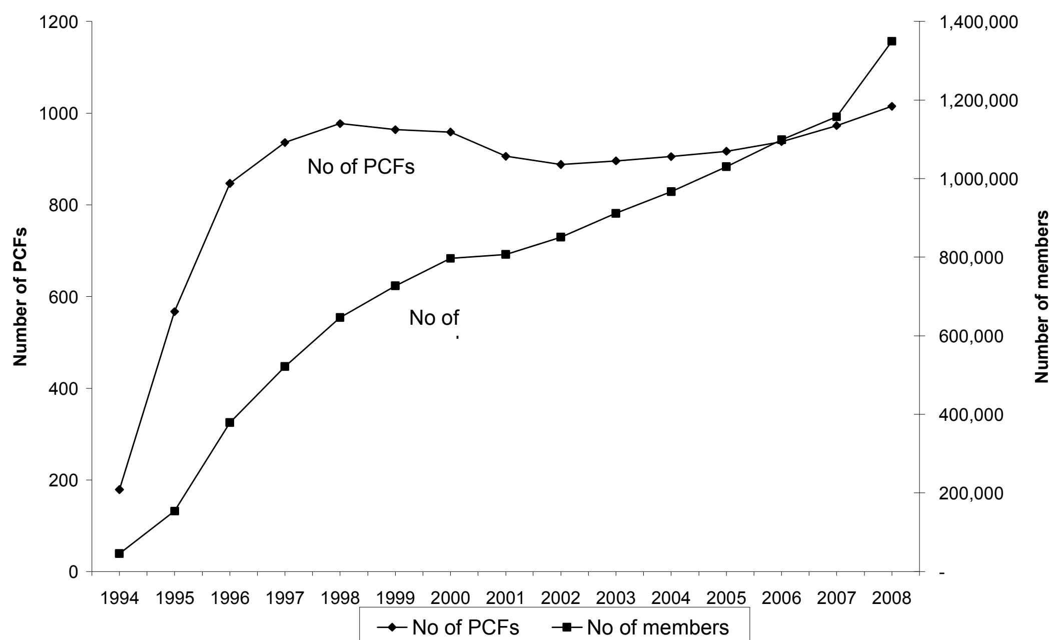
Table 2: The development of PCFs, 1994-2008 (amounts in million US$)

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
No of PCFs	179	567	847	936	977	964	959	906	888	896	905	917	938	973	1015
Growth in number p.a.		*388*	*280*	*89*	*41*	*-13*	*-5*	*-53*	*-18*	*8*	*9*	*12*	*21*	*35*	*42*
No. closed by SBV	0	0	0	0	0	0	5	53	24	3	3	4	4	2	0
No of members	46,045	153,901	378,978	522,080	646,701	727,098	797,069	807,546	850,781	911,926	966,540	1,029,987	1,098,754	1,157,416	1,349,804
Av. no of members/PCF	*257*	*271*	*447*	*558*	*662*	*754*	*831*	*891*	*958*	*1,018*	*1,068*	*1,123*	*1,171*	*1,190*	*1,330*
No of borrowers				677,717	734,796	746,481	711,769	661,443	660,361	663,757	661,663	670,933	732,774	785,638	785.698
Balance sheet															
Total assets	7.6	40.67	120.81	128.91	133.74	163.39	184.2	196.15	232.14	303.11	371.01	458.74	585.98	850.71	982.17
Av. total assets/PCF	*0.042*	*0.072*	*0.143*	*0.138*	*0.137*	*0.169*	*0.192*	*0.216*	*0.261*	*0.338*	*0.41*	*0.5*	*0.625*	*0.874*	*0.97*
Loans – gross	6.59	34.9	91.16	114.61	116.17	140.46	161.9	169.64	200.66	259.09	322.5	404.44	511.3	731.11	833.04
Growth p.a. in percent		*430*	*161*	*26*	*1*	*21*	*15*	*5*	*18*	*29*	*24*	*25*	*26*	*43*	*14*
Disbursements	n.a	n.a	193.47	230.69	227.33	258.02	274.83	264.19	318.3	395.85	496.42	603.63	569.49	1,131.37	1,215.60
Deposits	5.01	24.69	60.26	80.86	85.63	107.39	117.85	129.41	153.97	205.23	250.05	299.75	389.65	582.47	726.24
Growth in percent		*392*	*144*	*34*	*6*	*25*	*10*	*10*	*19*	*33*	*22*	*20*	*30*	*49*	*25*
Borrowings				18.39	19.62	20.44	22.34	35.92	39.77	51.88	63.36	85.96	106.7	152.98	131.83
Equity	0.98	4.32	9.05	12.01	11.03	11.28	11.96	11.8	13	15.64	19.53	24.44	28.52	38.55	45.88
Av. equity/PCF	0.005	0.008	0.011	0.013	0.011	0.012	0.012	0.013	0.015	0.017	0.022	0.027	0.03	0.04	0.05
Net profit after tax*	0.26	1.15	3.13	3.52	2.76	3.55	3.18	3.96	4.89	5.8	7.19	8.79	10.54	10.24	10.81
Financial ratios (in %)															
CAR (not risk-weighted)	14.9	12.4	9.9	10.5	9.5	8	7.4	7	6.5	6	6.1	6	5.6	5.3	5.5
Overdues (≥1 days)	0.74	0.51	1.24	3.53	3.84	3.72	3.42	2.17	1.36	0.84	0.66	0.53	0.53	0.5	0.53
ROAA*							1.17	1.37	1.43	1.38	1.4	1.38	1.3	0.87	0.79
ROAE*							15	18	20	20	21	18	19	14	11
Loans-to-deposits	131	141	151	142	136	131	137	131	130	126	129	135	131	126	115
Deposits-to-loans	76	71	66	71	74	76	73	76	77	79	78	74	76	80	87
US$ exchange rate	*11,003*	*11,020*	*11,037*	*11,175*	*13,887*	*14,019*	*14,540*	*15,086*	*15,395*	*15,630*	*15,776*	*15,906*	*16,056*	*16,025*	*16,977*

Source: Based on data from SBV

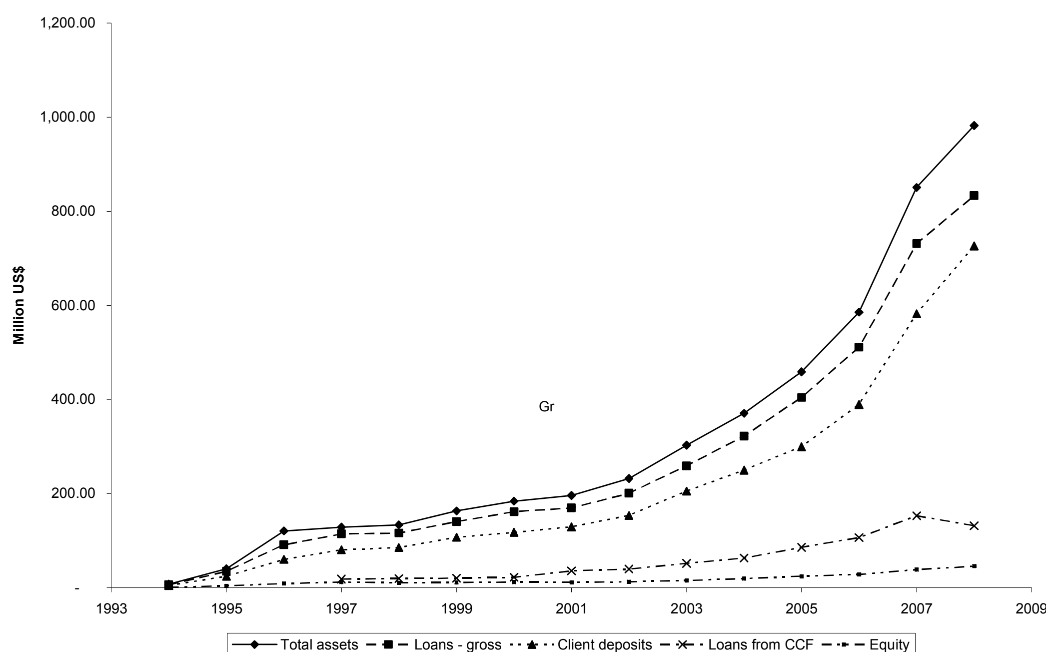
Figure 1 shows the exponential growth in the number of PCFs until 1996, the decline in the rate of increase in the following years when SBV closed a number of institutions, and slow growth since 2003. Membership grew rather steadily, with a flattening of the curve in 2000 and a sharp incline in 2008. PCFs have grown more than five-fold in average membership, from 257 per PCF in 1994 to 1330 in 2008.

Figure 1: Number of PCFs and members, 1994-2008



Since inception, total assets, loans outstanding and client deposits as the main source of funds have grown virtually in unison – figure 2. From 1994 to 1996 the three almost parallel curves grew steeply, followed by a flattening. 2002 marked a turn-around to an increasingly steep incline, with total assets, loans and deposits more than doubling in US$ terms during the last three years. Borrowings virtually stagnated at a very low level until 2000, after which they increased modestly until 2004. In 2005-07 they grew somewhat faster; but the rate of growth as indicated by the incline remained far behind that of total assets, loans and deposits. In 2008 they fell back, not only in US$ dollar terms (by 13.8%) but also in national currency (by 9.8%9). Equity has remained at a low level, its growth far behind that of the other curves – perhaps a source of weakness which might make it difficult for PCFs to cope with external shocks.

Figure 2: Total assets, loans outstanding, deposits, borrowings and equity of PCFs, 1994-2008 (in million US$)



Broadening of outreach has been accompanied by financial deepening. Average deposit balances per member increased from $109 in 1994 and $155 in 1997 to $538 in 2008. Average loans outstanding per borrower increased from $169 in 1997 (the first year the number of borrowers was reported) to $1060 in 2008.

Overall the PCFs have performed extraordinarily well, both in quantitative terms of growth and in qualitative terms of repayment and profitability, the latter reduced however by the recent restrictive interest rate policy of SBV designed to regain macroeconomic stability. In 1994 and 1995 overdue (≥ one day) ratios were well below 1%. In 1996 they climbed to 1.2% and went up to rates ranging from 3.4% to 3.8% between 1997 and 2000. During the second part of the consolidation period they started to decline and stayed at 0.5% during the last four years up to 2004 – proof of the effectiveness of consolidation. Information on return on average assets (ROA) and equity (ROE) is available from SBV since 2000. Between 2000 and 2006 ROA fluctuated between 1.2% and 1.4%. In 2007 it declined to 0.87 and in 2008 to 0.79. The drop in profitability in 2007 and 2008 is not due to an intrinsic weakness of the PCFs, but is a result of interest rate restrictions newly imposed by SBV. Similarly, ROE started at 15% in 2000, climbed to rates between 18% and 21% and subsequently fell to 14% and 11%, respectively. No doubt, it is not only the PCFs which have performed well, but also SBV as a supervisor.

GROWTH OF THE CENTRAL PEOPLE'S CREDIT FUND (CCF)

CCF was licensed by SBV in 1995 as the apex cooperative financial institution of the PCF network. The CCF is a joint stock financial institution under the law of cooperatives, the law of credit institutions and the decree (of 2001) on PCF which also pertains to CCF. It is supervised by SBV. It is expected to be transformed into a commercial bank. CCF provides financial services to PCFs and the general public, including SMEs,

farmers and CCF staff. In addition it provides technical assistance to PCFs and has been acting as focal point for the network in its external relations. There are 25 branches which operate as profit centers. Performance incentives may effectively double one's salary. CCF is owned by the PCFs, four state banks and the Government as a special member represented by SBV, which also form the general assembly and the board of management. The legal capital as of 31 December 2007 amounted to $7.0 million, 73.2% of which were held by SBV. In early 2008 SBV injected D600 billion, bringing its share to 95.8%. The Government plans to increase legal capital to D2.0 trillion in 2009. There is a permanent supervisory board of three and an executive committee of six members. The accounting system is largely in line with international standards. Reporting is based on a format issued by SBV. The accounting department prepares a daily balance sheet, which is sent to all departments. The branches submit their data daily, with automatic overnight inclusion in a consolidated report. Risk management pertains to four major risks: credit, liquidity, market and interest rate risk. An internal auditing department is under construction.

CCF has s deposits from PCFs since 1998 and from the general public since 2001. As of 31 December 2007 15% of total deposits came from PCFs, 40% from banks and 45% from other clients. CCF has been lending to PCFs since 1995. Lending to SOEs started in 1998, in an effort to contribute to their viability. In 2001 CCF introduced consumer lending to individual clients. 52% is extended to PCFs, 7% to SMEs and 41% to individuals. 73% of the loans are short-term, 25% medium-term and 3% long-term. 84% of the portfolio is financed from own resources, 16% from donor credit lines. The feasibility of a life insurance product for loan protection is under study. Interest rates in August 2008 stood at 4.8% p.a. on current accounts and 19.24% to 17.52% on term deposits. Lending rates varied from 16.8% to 21.0% on loans from own funds and from 13.2% to 19.8% on loans from project funds. The net interest rate margin was 2.95%. PCFs pay the lowest, individuals the highest interest rates on loans. Due to interest rate uncertainty long-term loans (with an overdue ratio of 0.9%) were more expensive than short-term loans (with an overdue ratio of 1.5%).

There are two major phases in the evolution of CCF: a first phase of slow growth from 1995 to 2000, the end of the pilot project, during which the refinancing function of the CCF was paralleled by Regional Credit Funds (RCFs); and a period of rapid growth from 2001 to 2007, initiated by the merger of the RCFs with the CCF and the provision of retail financial services to the general public, which has laid the institutional foundation for the transformation of CCF into a commercial bank which is under discussion. The trend changed in 2008, which is discussed in the final chapter. During 1995-2000 average annual growth rates of total assets and loans outstanding were 40% and 69%, respectively; during 2000-2007 these rates were almost 150%. Deposit-taking started in 2000 near zero; hence meaningful percentages of growth cannot be calculated. In 2007 deposits accounted for a remarkable 96% of loans outstanding. Equity almost stagnated, growing during the two periods at an average of 0.3% and 7%, respectively. Growth rates of borrowings declined by 9/10th, from 513% to 54%, largely replaced by deposits in Table 3.

Table 3: CCF: Increases of core balance sheet parameters, 1995-2000 and 2000-2007 (amounts in million US$, average annual growth rates in percent)

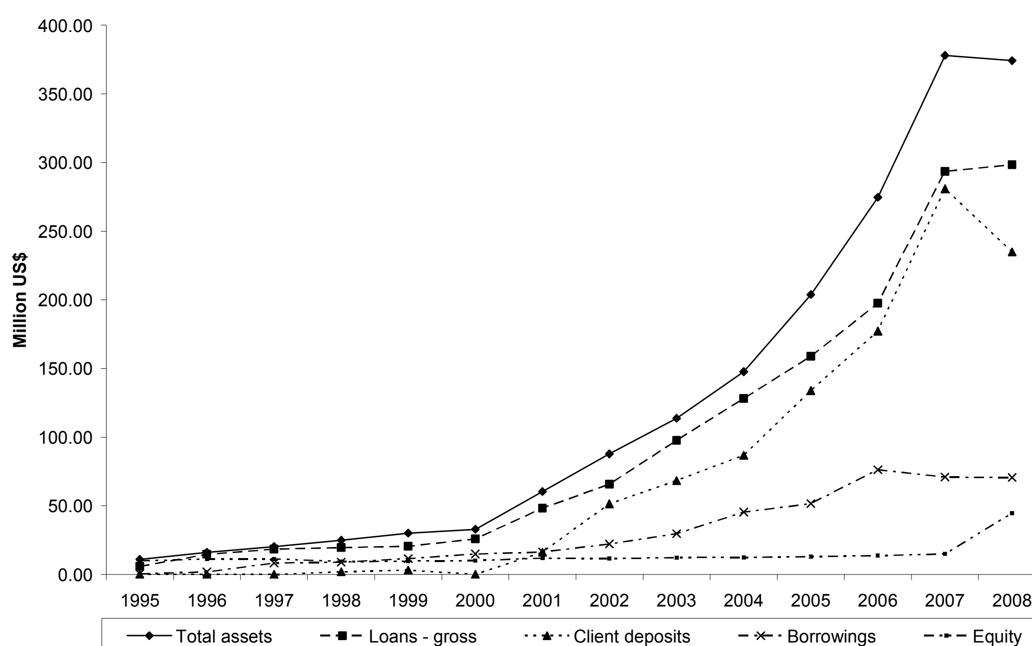
	Balance sheet data (in million US$)			Av. annual growth rates (in %)	
	1995	2000	2007	1995-2000.	2000-2007
Total assets	11.00	32.99	378.04	40	149
Total loans gross	5.78	25.79	293.51	69	148
Total deposits	0.00	0.15	280.83		
Total borrowings	0.56	14.91	70.98	513	54
Total equity	9.98	10.11	14.89	0.3	7

Source: Based on CCF data

The turn-around of CCF led to a fundamental change in the structure of the balance sheet. Comparing percentages in terms of total passiva in 2000 and 2007, deposits surged from 0.5% to 74%, borrowings fell from 45% to 19%, and total equity dropped from 31% to 4%. This is paralleled by a decrease in the percentage of loans outstanding to PCFs in terms of total activa from 68% to 40%, and an increase of loans to other clients from zero to 37%. The overall result of the transformation has been a savings-driven institution with a diversified portfolio. Self-reliance through deposit mobilization has been the most outstanding outcome. By the end of 2007 CCF stood at 44% of the total asset size of PCFs.

Graphically the turn-around is shown in figure 3. All curves are nearly flat up to 2000, indicating very low growth rates. In sharp contrast, during 2001-2007, there has been a more than ten-fold surge in total assets and loans outstanding (measured in US$); deposits grew from 7% of loans outstanding to almost 100%. Only the curve of total equity remained flat, with a growth of less than 50% over the seven-year period until 2007 (but over 400% by 2008 after a capital injection by SBV).

Figure 3: Total assets, loans outstanding, deposits, borrowings and equity of CCF, 1995-2008



The performance of CCF has been mixed but satisfactory overall. Overdue ratios have been moderate: they were near zero during the first three years for which data exist, 1998-2000, when CCF only lent to PCFs and RCFs. Due to the adoption of lending to the general public in 2001, the overdue ratio (≥1 day) of CCF surged from 0.25% in 2000 to 2.05% in 2001 and oscillated subsequently between a low of 1.0% and a high of 2.9%. In terms of profitability the best-performing years were 1996 and 1997: a liberal era in which the net interest margin was above 8%; the ratio of operational expenses over operational income was around 40%; and return on average assets was above 7%, which is exceptionally high. Since then the net interest margin, restricted by SBV policy, has been a modest 3% to 4% and stood at 2.95% in 2007, the lowest ever. From 2000 to 2007 net interest income grew by more than 900%; but efficiency went down as costs surged, as indicated by the increase in the ratio of operational expenditure over operational income from 57% in 2000 to peak of 91% in 2002; in 2007 it stood at 68%, which is quite satisfactory. Return on average assets has come down substantially. In 1998-2000 it roughly oscillated around 2%. Between 2000 and 2007 net profit after tax only doubled; return on average assets declined from 2.2% to 1.2% in 2001 and stagnated at 0.4% during 2005-07 due to a repressive interest rate policy. This ratio is far too low for an otherwise well-performing institution, particularly in light of its expectation to be transformed into a commercial bank. In the inflationary environment of 2008, SBV does well to impose a tight money policy and raise interest rates. But a cap on interest rates – in an effort to keep inflation low – is the wrong instrument. This puts the health of an otherwise sound credit cooperative sector at risk.

GROWTH AND RESILIENCE DURING THE GLOBAL CRISIS

The global financial crisis began in July 2007 in the US with a loss of investor confidence in securitized mortgages; it spread and intensified throughout 2008 and turned into a global economic crisis. Vietnam's export-driven economy was affected by a downturn of global demand and inward investment. The economy was not shattered, it expanded by 6.18% in 2008; but this was the lowest level in almost a decade. During the first quarter of 2009 Vietnam was one of the few countries with positive growth; yet its GDP growth of 3.1% was the lowest on record.

Over the past year concerns have been voiced that the crisis might seriously affect the microfinance industry worldwide. We surmise that effects will vary widely, depending, among other factors, on the self-reliance of institutions and their exposure to the inflow of external capital. Field work for this study was done in August 2008, before the impact of the global crisis was fully felt. As the crisis spread, the question arose whether and how it affected the PCFs. PCFs are financed through member deposits as their main source of funds (74% of passiva, 87% of loans outstanding in 2008). Other sources of funds comprise member shares and retained earnings. At 13% borrowings from CCF are but a fraction of passiva. When requesting an update until December 2008, our hypothesis was that impact would be quite limited. However, economic reality is complex, and there are other factors at work which might influence the growth and performance of the PCF system. Inflation in Vietnam increased from 6.6% in 2006 to 12.6% in 2007 and surged to 22% in 2008 according to SBV. As in many other developing countries, this was initially due to rising food and energy prices, which were unrelated to the crisis. Subsequently inflationary pressures might have been increased by the crisis, particularly in light of the fact that food and energy costs declined in the second half of 2008. The possible impact of inflation on the PCFs has been exacerbated by the central bank's attempt to stem inflation with a ceiling on interest rates, a policy which

diminishes profitability. As a result, interest rates in 2008 turned negative in real terms, last seen in 1989. The question of resilience is thus a wider one: how did PCFs fare under the onslaught of global crisis, inflation and financial repression?

With regard to CCF, the central fund of the PCFs, the situation might be different. CCF derives only 13% of its passiva from PCFs; the main source of funds is deposits by other, mostly urban, clients (50% of total passiva). Borrowings account for 19% and equity for 12% of passiva (2008). Both types of institutions, PCFs and CCF, are savings-based; but they differ in that PCFs fully rely on local rural markets, while CCF is to a considerable extent integrated into urban markets and thus more exposed to global as well as wider domestic influences. Does this show in its performance?

The PCF network expanded by 4.3% in 2008, more than in the preceding years; and for the first time since 2000, no PCF was closed by SBV. Membership grew by an unprecedented 16.6%; but the number of loans outstanding stagnated. (Table 1, Figure 1) In US$ terms growth continued at an impressive rate as visualized in Figure 2. Total assets grew by 15.5%, loans outstanding by 13.9%, deposits by 24.7% and equity by 19.0%. Yet the growth rates in 2008 are lower than those of 2007, which were exceptionally high compared with already high growth rates in preceding years. Thus, growth continued to be strong in 2008, but at a lower rate than in 2007 and 2006. Borrowings had increased by 43.4% in 2007 and decreased by 19.0% in 2008: mostly due to lesser loan demand. At the same time this is a sign of self-reliance as indicated by the increase in the deposit-to-loan ratio from 76% in 2006 to 80% in 2007 and 87% in 2008 – table 2. The decline in borrowings is not due as one might suspect to a drying up of international funds channeled through CCF; in fact, these increased by 16.9%, far more than in previous years.

Table 4: Growth rates of PCFs, 2005-2008 (in percent, amounts based on US$)

	2005	2006	2007	2008
Outreach:				
No of PCFs	1.3	2.3	3.7	4.3
No of members	6.6	6.7	5.3	16.6
No of borrowers	1.4	9.2	7.2	0.0
Balance sheet				
Total assets	23.6	27.7	45.2	15.5
Loans - gross	25.4	26.4	43.0	13.9
Deposits	19.9	30.0	49.5	24.7
Borrowings	35.7	24.1	43.4	-13.8
Equity	25.2	16.7	35.2	19.0

Source: Based on table 2

The overall economic situation apparently did not have an impact on the ability and willingness of PCF members to repay their loans: for the past four years, including 2008, the overdue ratio (≥ 1 day) stayed at 0.5%. In 2007 performance of the PCFs declined, a trend which continued into 2008: ROA (unadjusted for inflation) declined from 1.30% in 2006 to 0.87% in 2007 and 0.79% in 2008; correspondingly, ROE fell from 19% to 14% and 11% in table 2. The decline in profitability in 2007 was due to two factors which depressed earnings: a more conservative provisioning policy and stronger competition which kept PCFs from lowering their deposit interest rates. As a result net income after tax stagnated and failed to keep pace with portfolio growth. Compared to that, interest rate restrictions as of May 2008

had surprisingly little additional impact in 2008. From 2001 to 2007 the growth pattern of CCF has been overwhelmingly positive and similar to that of the PCFs, with rates of growth of CCF overall somewhat higher, as visualized in figure 2 and figure 3. The pattern in 2008, however, is different. The growth of total assets, at 37.7% in 2007 (and similarly high rates in the years before), came to a standstill in 2008, at an unprecedented -1.0%. Similarly, the growth of the loan portfolio fell from a spectacular 48.6% in 2007 to 1.7% in 2008. Deposits fell even more dramatically: from 58.4% to -13.8%. The two client groups of CCF reacted differently to the recession: the PCFs deposit more in the CCF and borrow less; other clients deposit less and borrow more. More specifically, from 2007 to 2008 the share of the PCFs in the deposit portfolio grew from 15% to 20%, while their share in the loan portfolio fell from 52% to 44%. Correspondingly, the share of other clients in the CCF's deposit portfolio fell from 85% to 80%, while their share in the CCF's loan portfolio grew from 48% to 56%. The changes in the growth rates of the various balance sheet parameters since 2005 are given in table 5. From 2007 to 2008 the growth rates of deposits by PCFs fell from 90.2% to 14.1%, compared to respectively 53.9% and -21.8% of other clients; growth rates of loans to PCFs fell from 43.4% to -13.8%, while growth rates of loans to other clients fell from 54.7% to 18.5%.

Unrelated to the crisis, the rate of growth of equity surged from 8.6% in 2007 to an astronomical 199.2%. This is owed to a substantial investment of SBV, which brought equity up from $14.9 million in 2007 to $44.55 million in 2008, in preparation of a transformation into a commercial bank. CAR (risk-weighted) surged from an all-time low of 10.1% to 30.9%. There was no drying up of donor credit lines in 2008, as might have been feared by observers of the global microfinance industry. These have risen continuously since 1997. During the last three years they not only rose in absolute terms, but their growth rate also went up: from 9.1% in 2006 and 12.3% in 2007 to 16.9% in 2008, reaching $65 million. This was accompanied by a reduction of domestic credit outstanding over the past three years, which declined from $20.6 million in 2006 to zero in 2008. See table 2 and table 5.

Table 5: Growth rates of CCF, 2005-2008 (in percent, amounts based on US$)

Balance sheet	2005	2006	2007	2008
Total assets	38.0	34.7	37.7	-1.0
Total loans gross	23.9	24.4	48.6	1.7
Loans to PCFs	*35.7*	*24.1*	*43.4*	*-13.8*
Loans to other clients	*12.5*	*24.7*	*54.7*	*18.5*
Total deposits	54.4	32.4	58.4	-16.4
Deposits of PCFs	*1.7*	*43.7*	*90.2*	*14.1*
Deposits of other clients	*65.6*	*30.9*	*53.9*	*-21.8*
Total borrowings	13.7	47.6	-6.8	-0.4
Domestic borrowings	*-93.3*	*9,266.1*	*-54.9*	*-100.0*
Donor credit lines	*26.4*	*9.1*	*12.3*	*16.9*
Total equity*	4.3	5.7	8.6	199.2

Overall impact of the turmoil in 2008 on the financial performance of CCF has been moderate. Since CCF started lending to the general public overdue ratios (≥1 day) have been fluctuating between 1% (2004) and 2.9% (2005). In 2007 CCF had succeeded in bringing the overdue ratio down to 1.3%; but in 2008 it jumped to 3.1% - evidence of repayment problems, but still at a moderate level given the strictness of the definition. Efficiency as measured by the ratio of operational expenditure over operational income declined slightly,

from 68% to 73%. Under pressure to charge “affordable” interest rates, ROA, unadjusted for inflation, has been historically declining from 7.8% in 1996 to values significantly below 1% after 2001, stabilizing at 0.43% between 2005 and 2007. In 2008 ROA further declined slightly to 0.37%.

CONCLUSION AND UPDATE

By way of conclusion, credit lines have played only a small role in the financing of PCFs and CCF; and there has been no drying up of donor funds in 2008 which might have affected the network during the global crisis. In 2008, at the height of the global crisis, PCFs with their purely local rural clientele proved resilient. Total assets, loans outstanding and deposits continued to grow almost unimpeded at high rates. Only the number of loans stagnated, as some members worried about the future. Also, members honored their repayment obligations, with overdue ratios constant at a level near zero. The central bank’s attempt to control inflation (related to the prior rise in food and energy prices) by imposing interest rate ceilings in 2008 depressed the profitability of the PCFs only slightly. Earnings had been more affected in 2007 by the introduction of a more conservative provisioning policy and by competition, the latter preventing the PCFs from lowering their deposit rates and thus increasing their margin. It also appears that PCFs are more concerned with low lending interest rates for the benefit of their members than with profit maximization. As a result, deposits remain their main source of funds, not retained earnings.

From December 2008 to June 2011 the PCFs have continued to grow (calculated at the respective exchange rates to the US$: 16,977 as of 31 December 2008 and 20,570 as of 30 June 2011): The number of PCFs from 1015 to 1064, without any closures during that time; the number of members by 33%, from 1.35 million to 1.80 million; total assets by 57%, from $982.2 million to $1542.4 million; deposits by 65%, from $726.2 million to $1196.9 million; loans outstanding by 54% from $883.0 million to $1282.0 million; their deposit base has strengthened, with the deposits-to-loans ratio up from 87% to 93%.

CCF serves not only PCFs but also urban corporate and individual clients, relying largely on their deposits. Since CCF began serving the public, in 2001, its growth has been spectacular, exceeding even that of the PCFs, but only until 2007. In 2008, under the impact of the global crisis, growth of total assets and loans outstanding came to a standstill; deposits, which are mainly mobilized from clients other than PCFs, declined. Compared with previous years, in 2008, PCFs deposited more in CCF and borrowed less, while other clients deposited less and borrowed more. Exposure to urban markets, previously the strength of the CCF, now turned into a liability, disrupting the previously unabated growth pattern. As a result, total asset size of CCF relative to the PCFs declined from 44% in 2007 to 38% in 2008. Yet, in terms of financial performance CCF has coped rather well with the impact of the global crisis and inflation on its clients. Overdues went up, but not to an alarming degree. Efficiency went down slightly, and so did profitability. But more serious than external threats has been an overall culture of interest rate moderation which is characteristic of many credit cooperative systems – quite the opposite of many other types of microfinance institutions – and the re-enactment of interest rate controls. One may hope that due to their self-reliant growth over a long period, both PCFs and CCF possess the inner strength to also cope with economic and policy challenges in the future.

Growth rates of the CCF between 31 December 2008 and 30 June 2011 have been as follows: total assets by 78%, from $374.2 million to $664.7 million; deposits by 78%, from $234.8 million to $418.8 million; borrowings by 29%, from $70.7 million to 91.5 million; loans outstanding by 14%, from $298.4 million to $340.8 million; given the continually low growth of its loan portfolio, presumably a consequence of the global crisis, the deposits-to-loans ratio has surged from 79% to 123%. Vis-à-vis the PCFs the CCF has recovered its relative pre-crisis total asset size, 43% as of June 2011 (44% in 2007), up from 38% in 2008. Yet, its national outreach and exposure to the urban SME economy has made the CCF more vulnerable: its non-PCF deposits have declined from 80% in 2008 to 59% as of June 2011; and the growth of its loan portfolio, at a rate of 14% compared to 54% of the PCFs, continues to be low. This might change once the CCF is converted into a full-fledged cooperative bank, which is expected in 2012.

In sum, there are four outstanding characteristics of the credit cooperative sector as it has evolved in Vietnam since 1993: (i) resilience to the recent global crisis, which we attribute to a large extent to a savings-based self-reliance of the network; (b) a difference in resilience between the PCFs, which are focused on a rural local area economy, and CCF, with a partial focus on an urban economy, the former more shielded from, the latter more exposed to, the global economy and the global crisis; (iii) the crucial role played by government through the central bank as a regulator, supervisor, guidance and training agency, insisting on good performance by enforcing regulatory compliance; (iv) the existence of a strong central fund which until recently, in addition to liquidity exchange, has served the functions of a national federation, providing advocacy, external relations, training and other services, while the actual federation, VAPCF, established in 2006, is only now gaining in strength. Credit cooperatives in various European countries have derived their strength from self-help as a structural characteristic of the movement, keeping Government at bay. For instance, in Germany, there is no cooperative ministry, department, or desk; instead, there are strong self-organized associations and federations. In contrast, in many developing countries (as in India, Indonesia and many African countries) the state (or the Government) has played a negative role through undue interference in ownership, resource mobilization and governance, stifling self-help, self-governance and self-reliance. This has created a big problem for emerging economies: how to start a cooperative movement in the absence of prime movers like Raiffeisen and Schulze-Delitzsch (in Germany) or Desjardins (in Canada). In this respect Vietnam has shown the way how Government, through the central bank, can play a constructive role in building a people-owned, self-managed and self-governed network of local credit cooperatives in rural areas, providing the necessary regulation, supervision and human capacity building inputs, without destroying the spirit of self-help and self-reliance.

Many countries in the South could benefit from that experience, not blindly and mechanically replicating what might appear as *best practices*, but making the necessary adjustments to their own sociocultural and economic environment and thus arriving at their own *good practices* in each case. Donors should be encouraged to assist the Vietnam Association of PCFs (VAPCF), together with the PCFs, the CCFs and the SBV, to establish an international credit cooperative exposure training program.

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Annex 1: CCF financial data, 1995-2008 (in million US$)

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Balance sheet														
Total assets	11.00	16.04	20.24	24.84	30.14	32.99	60.39	87.83	113.69	147.67	203.80	274.59	378.04	374.16
Total loans gross	5.78	14.63	18.39	19.62	20.44	22.34	48.29	65.70	97.63	128.14	158.82	197.53	293.51	298.39
Loans to PCFs, RCFs in %	*100%*	*100%*	*100%*	*100%*	*100%*	*87%*	*74%*	*61%*	*53%*	*49%*	*54%*	*54%*	*52%*	*44%*
Total deposits	0	0	0.02	1.89	3.07	0.15	16.24	51.46	68.35	86.71	133.91	177.28	280.83	234.75
Deposits of PCFs in %			*100%*	*100%*	*100%*	*100%*	*29%*	*12%*	*20%*	*17%*	*11%*	*12%*	*15%*	*20%*
Total borrowings	0.56	1.87	8.31	8.96	11.57	14.91	16.38	22.18	29.74	45.38	51.62	76.19	70.98	70.72
Donor credit lines in %	0%	0%	78%	100%	94%	84%	89%	83%	95%	79%	88%	65%	78%	92%
Total equity*	9.98	11.25	11.31	9.46	9.65	10.11	11.91	11.77	12.13	12.44	12.97	13.71	14.89	44.55
Profit/Loss														
Net interest income	0.48	1.39	1.66	1.01	1.09	1.17	2.02	2.49	3.12	4.27	7.01	8.37	10.79	13.09
Net profit before tax	0.36	1.06	1.36	0.72	0.76	0.84	0.81	0.75	0.75	0.92	1.06	1.42	1.94	1.86
Net profit after tax	0.36	1.06	1.36	0.39	0.64	0.71	0.55	0.51	0.52	0.66	0.76	1.02	1.40	1.34
Financial ratios (in %)														
CAR, risk-weighted	n.a.	n.a.	n.a	35	37	32	36	35	34	25	17	13	10.1	30.9
Overdues, ≥1 day	n.a.	n.a.	n.a	0.06	0.09	0.25	2.05	2.06	1.24	1.02	2.9	2.3	1.3	3.06
Return on average assets**		7.81	7.49	1.75	2.33	2.23	1.18	0.69	0.51	0.51	0.43	0.43	0.43	0.37
Return on average equity**			12.05	3.79	6.69	7.14	4.99	4.29	4.33	5.40	5.99	7.64	9.79	4.57
Net interest margin	4.35	8.67	8.18	4.08	3.61	3.73	3.46	2.97	2.88	2.99	3.55	3.15	2.95	3.76
Op.exp./op.income	24.34	38.97	41.61	61.19	70.08	56.65	84.86	91.16	74.16	74.68	58.56	66.32	68.17	73.29
Deposits-to-loans (in %)	0	0	0	10	15	1	34	78	70	68	84	90	96	79
US$ exchange rate	11,020	11,037	11,175	13,887	14,019	14,540	15,086	15,395	15,630	15,776	15,906	16,056	16,025	16,977

* Equity for 1995 is estimated.

** After taxes, calculated over the average of beginning and end of year

Chapter 14

THE IMPACT OF COOPERATIVE FINANCE ON CAPITAL FORMATION

Adedoyin Isola **LAWAL**

INTRODUCTION

No one has a prescribed answer as to when cooperative society began in the world as different authors have traced its origin to different time. For instance, Godly (et al 2011) traced the origin of co- operative society to the eighteen century in England. According to them, cooperative was formed as a result of human sufferings and degradation during the industrial revolution and the need for the poor to improve on their conditions of living. This argument was supported by Ukpere (2010) and Brace (1996). It was argued that human sufferings motivated the idea of cooperative movement that was envisioned by Robert Owen. This led to the formation of the Rochdale Pioneers (a group of workers) in 1844, who organised themselves into a movement for a new humanism, based on self help and group actions (Abia, 2000; Ahmad, 2005). In another view, Taylor (1974) traced the origin of cooperative society to the credit system formed by Herman Schulge-Delitzsch in 1851 to provide credit facilities to debt ridden peasant farmers in Germany. Ahmad (2005) traced the origin of cooperative society to 1750 in France, where local cheese makers in the community of Franche-Comte established a producer cooperative society. This led to increase in their volume of trade and economic well being, and motivated the growth of cooperative societies in France, United Kingdom, United States and Greece. The origin of cooperative society in Nigeria can be traced to 1935 following the acceptance of Mr. C. F. Strickland's report that supports the establishment of a cooperative society in Nigeria. This led to the enactment of the first cooperative legislation known as Cooperative Society Ordinance No.6 of 1935 (Godly, 2011; Adekunle et al., 1965). Ijere (1977) observed that early cooperative societies in Nigeria were deliberately those of farmers' societies for cocoa farmers in the South-Western Region, palm farmers in the South-Eastern Region and ground-nut farmers in the Northern Region.

Classification of cooperative societies

Cooperative societies can be broadly classified into four which are:

1. Periodic Savings and Credit Unions (PSCU): This is a self-help group formed when a group of people with common background come together to make regular contributions to a common fund, which is then pooled as a source of credit. This is more/less an informal microfinance institution like Esusu (common in the eastern part of Nigeria) that promotes savings and micro/very small scale business financing.

2. Solidarity Based Cooperative System (SBCS): This class of cooperative is based on peer group influence, and loans are made to the individual in groups. It is usually small in size and comprises of about six (6) to eight (8) members who collectively guarantee loan repayment. Credits are pooled together and advance to members after a reasonable amount has been realized. Only one third (1/3) of the member can access the initial loan, and after re-payment another (1/3) benefits from the societies in the form of loan accessibility, and the process continues. Nyele (2011) and Godly et al. (2011) all agreed that this type of cooperative society has contributed immensely to broader social benefits because of the mutual trust arrangement at the heart of the group guarantee system, and that the group itself often becomes building block to a broader social network. However, caution has to be taken, and measure must be put in place to ensure that repayment of loans is achieved.

3. Rural Banking System: This approach usually consists of between twenty five (25) to fifty (50) people who are low income earners and are seeking to improve their lives through self-employment activities. According to Chuku (2010), the core of this system lies in the promise that group stand behind each loan, and each loan is backed by moral collateral. The group is democratic and self governed in nature. The major role of this type of system is financial intermediation, recycling funds from surplus spending units (SSU) and channelling same to the deficit spending unit (DSU) Godly et al (2011).

4. Kibbutz System: This is a blend of both socialism and Zionism idea to economic life whereby people come together to raise a common fund by pooling their resources together so as to improve their socio-economic life. Most businesses of Jewish origin were founded based on Kibbutz system. Kibbutz interest includes funding agriculture and allied products, manufacturing etc. (Wikipedia, 2011)

The impact of cooperative society can never be over-emphasised as it contributes greatly to economic development of the nations where they are found. For instance, in the year 2003, the top US cooperatives had combined ventures of USD 117 billion. In addition, over 30% of farmers products in the US are marketed through 3,400 farmer-owned cooperatives. 270 telephone cooperatives provide services to over 2 million households. About 10,000 US credit unions have over 84 million members and assets in excess of USD 600 million (ICA,2011). In Brazil, cooperative societies are responsible for 72% of wheat production, 44% of barley, 43% of soya, 39% of milk, 38% of cotton, 21% of coffee production and 16% of maize production. On the aggregate, agriculture cooperative society export is over USD1.3 billion (Rohit Mishra, 2011). In Korea, agriculture cooperative have an output of over USD11 billion. Japan record shows that cooperatives contributes over USD90 billion. In Singapore, cooperative had a record of over USD 700 million contributions to the national economy. In Bolivia, cooperatives handled over 25% of the savings in 2002. In Belgium, cooperative pharmacies have a market share of 19.5%. Records from Benin Republic Shows that, FECECAM, a saving and credit cooperative federation provided USD 16 millions in rural loans in 2002. Cooperative societies provides job to over 700,000 people in France, over 440,000 people in Germany in year 2004. Credit sourcing is a major challenge in many developing countries, Nigeria inclusive. It has a lot of negative implications such as business failure, loss of potential output, and increase in the rate of unemployment, deteriorating standard of living etc on the economy (Godly et al., 2011; Elumilade et al., 2005).

The dearth of capital required to combine other factors of productions for productive purpose has lead to unemployment and other untold hardship on Nigerians (Nieman et al., 2003). Various efforts have been put in place by the government to ensure that adequate funding are made available to business by providing enabling environment to do business in the country (Goodluck, 2011). A major source of finance available to common man for business formation and financing is the cooperative credit and thrift society (Godly et al., 2011). Poor access to finance has negatively affected many businesses in Nigeria leading to their collapse. This is responsible for high rate of declining standard of living in Nigeria; a major negative implication of inadequate financing for business is unemployment. This paper examines cooperative societies as significant sources of capital formation, mobilization and channelling of funds to profitable investment within a country. This work attempts to answer the following questions: What is the level of membership of cooperative societies among small scale businesses? What relationship exists between membership of cooperative society and owning a small scale business? What role does membership of cooperative societies play on the rate of business turnover and employment generation?

LITERATURE REVIEW

Co-operative society had been defined by many authors depending on the authors' background and views. The term co-operation is derived from the Latin word "co-operari", where the word 'co' means 'with' and *operari* means 'to work'. Thus, co-operation means working together. So those who want to work together with some common economic objective can form a society which is termed as "cooperative society". It is a voluntary association of persons who work together to promote their economic interest. It works on the principle of self-help as well as mutual help. The main objective of cooperative society is to provide support to the members. Owojori (2005) explained that Cooperation and cooperative derive their origin from the idea of mutual understanding, respect and dependence. It is derived from the French words "Espirit de corps" which means working together. Asaolu (2001) believed that the word 'cooperative' was derived from a Latin dictum, "OPERARE" meaning to work and the prefix "co" meaning together. Two major approaches have been used to describe cooperative societies: these are economic and social aspect, and social and cultural background of the movement. The major emphasis in cooperative is on self-help, thus people cooperate because they realize that it is extremely difficult to achieve some goals by working alone. In a related development, Reeves (2003) observed that the best way of overcoming the limit of economic problem of scarcity is by working together by pooling your resources together with the main objective of accessing such facilities with a soft but reliable pay back mechanism. This is because more can be accomplished when people coordinate their efforts with each other and take concerns and talents of other into considerations. Nobody joins a cooperative society to earn profit.

People come forward as a group, pool together their individual resources, utilise them in the best possible manner, and derive some common benefits (Guraji, 2006). It can also be defined as an association of person who pool their resources together on mutual basis to solve specific socio-economic problems, which may include income generating activities (Godly et al., 2011). Abia (2000) defined cooperative as self-help organisation formed by either producers or consumers of goods and services usually by initiative ideas of one or two people who plays advocacy role and enlist other people to the cooperative. According to Owojori et al. (2009) Cooperative society is one of the microfinance institutions (MFIs) that promote entrepreneurship and industrialization desirable for economic development. Epetimehin

(2006) described cooperatives as a business owned and controlled by the people who use its service. They finance and operate the business or service for their mutual benefit.

Roy (1964) saw cooperatives as voluntary organisation established for the pursuance of economic, social and political interest of members. The International Labour Organisation (ILO) in its studies and report series, No 57 of 1960 on cooperative management and administration viewed cooperatives as an association of person usually of limited means, who have voluntarily joined together to achieve a common economic end through the formation of a democratically controlled business organisation, making equitable accepting a fair share of the risk and benefit of the undertaking. Onuoha (1986) observed that cooperatives are business of patrons whose motive is to obtain the goods and services they require at a cost through their joint undertakings. The International Cooperative Alliance (ICA) which is the world apex body of cooperative movements at its centennial congress and General Assembly in Manchester, 1995, defines cooperative as 'an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.' In a related development, UWCC, (2002) observed that cooperative society is a business enterprise voluntarily owned and controlled by its member patrons and operated for them and by them on a non-profit or cost basis. Laidlaw (1974) was of the opinion that cooperative societies are business enterprises that aim at complete identity of the component factors of ownership, control and use of service, which are the three distinct features that differentiate cooperatives from other business. Adeyemo et al. (2005) observed that cooperative societies are informal financial institutions that provide its members with the opportunity to market their products and serve as avenues for mobilising savings and credits facilities. He explained that, cooperative society is more preferable because of its easy accessibility, smallness of scale and informal nature of transactions. Ahmad (2005) explained that in an era when people feel powerless to change their lives, cooperative societies are formed to meet peoples' mutual needs based on the understanding that powerful ideal that cannot be achieved individually can only be achieved by a group of people with strong, vibrant and viable economic alternatives offered by cooperative societies.

In a study on mobilization of rural savings and credit extension by pre-cooperative organisation in Southwest, Nigeria, Osuntogun and Adeyemo (1981) examine the interrelationships between the value of members' savings in the group and some other features. Using Pearson correlation matrix they found that, the larger the membership strength of the group, the higher would be the number of members striving hand to make their savings, which invariably increase the capital base of the societies. They also observed that there is a positive correlation between the value of members' savings and frequency of savings. In another development, Adeyemo and Bamire (2005) examine the saving and investment patterns of cooperative farmers in South-western Nigeria. With four hundred respondents, the study shows that about 40% of total capital borrowed was expended on farm work and a mean annual total investment was about ₦75, 043:00 with cooperative farmers earning more than three (3) times the investment made. Ahmad (2005) adopts the use of time series approach in examining the role of cooperative societies in economic development. He observed that for over 160 years, cooperative have been an effective way for people to exert control over their economic livelihood as they play an increasingly important role in facilitating job creation, economic growth and social development. In a study by Saka et al. (2008), on the effect of group participation on access to micro-credit among rural women in Osun and Oyo states, Nigeria, observed that 85.6% of rural women belonged to micro credit group through which

42.3% were able to source credit. They observed that cooperative societies granted higher volume of credit than the local groups while women farmers had access to greater volume of credit than women traders, and that micro credit was yet to have significant impact on poverty status on the women. Otto and Ukpere (2011) carried out an empirical study on the contributions of cooperatives societies in Nigeria as a potential source of capital formation and employment. The work identified cooperative credits and thrift associations as a veritable source of capital formation which is required for investment purposes. It further explained that the thrift cooperative as a micro finance agency is also a direct source of employment for those engaged in its management or coordination. The scope of operation of a cooperative society is based on the size of its capital and membership. Godly et al. (2011) identified three levels of cooperative society as: the primary level whose operation is within a classified community, secondary level which operates within a local government and tertiary level whose operation covers a number of local governments but within a state. This paper essentially focuses on issues relating to credits and thrift cooperative societies whose activities centres on improving access to credits at a relatively low and affordable cost to its members, making savings convenience, borrowing easy with soft pay back mechanism. Otto (2006), argued that cooperative societies make borrowings easier for members than the traditional commercial banks. Abia (2000), Elumilade et al. (2005), and Godly et al (2011) all agreed that it is the bedrock of capital formation for business financing in Nigeria.

RESEARCH METHODOLOGY

The study deals with a survey of views and experiences among the Yoruba in Kwara South Senatorial District on the utility of cooperative financing as a source of capital formation. Seven Local Government Area covered by the study are Irepodun, Ifelodun, Offa, Oke-Ero, Isin, Oyun and Ekiti in Kwara South Senatorial districts. The local government areas were divided into two groups: Group A which comprises of those LGAs in urban areas such as Irepodun, Offa and Ifelodun; Group B comprises of those LGAs in the rural areas comprising of Oke-Ero, Isin, Oyun and Ekiti LGAs. A total of eighty five cooperative was covered, forty five from group A and forty from group B. Data for the study were generated mainly through the use of structured questionnaires, oral interviews and focus group discussion which were developed after the review of relevant literature. Twenty One (21) trained research assistant were detailed to cover the LGAs, three (3) per LGA. Data collection lasted between September and November 2011. A hundred and fifty five (155) respondents were eventually interviewed randomly from the business community in the LGAs. Capital formation was the dependent variable while membership of cooperative societies and profitability level were the independent variable. We adopted the use of descriptive statistics and multiple regression analysis to infer the relationship between the dependent variables and the independent variables of the study, while correlation matrix was used to examine the direction of relationship among selected socio-economic features of the respondents and membership of cooperative societies.

The regression analysis is express as follows:

$$Y_i = \beta_1 + \beta_2 X_{2i} + \beta_3 X_{3i} + U_i$$

Where

Y_i = Capital formation / numbers of co-operators that access credit facilities

X_{2i} = numbers of co-operators that own a business

X_{3i} = rate of increase in business profit (profitability level)

U_i = random error term

To test whether the data contain any evidence suggesting *y* is related to x_2, we test the null hypothesis

$H_o : \beta_2 = 0$

against the alternative hypothesis

$H_1 : \beta_2 / 0$

and

$H_0 : \beta_3 = 0$ and $H_0 : \beta_3 = 0$

RESULT AND DISCUSSION

Table 1 below shows the demographic character of the respondents, one can deduce that about sixty one percent (61.2%) of the respondents fall between the ages of 15-35, forty- seven respondents representing forty-nine (49.47%) are male between the ages of 15-35. Ninety-five percent of the respondents between the ages 15-35 are Yoruba. On the aggregate, seventy one (71) of the respondents are female representing about forty five (45.81%), one hundred and forty nine (149) respondents representing about ninety six (96.13%) are Yoruba. From the above, one can see that those within the work active age (15-60) constitute a large member of respondents. This represents about ninety six percent (96.13%) of the respondents. This is in line with the findings of some authors like Deji (2005), Elumilade et al (2005) and Otto (2009).

Table 1: Demographic character of the respondents

Age		Sex		Ethnicity	
	Frequency	Male	Female	Yoruba	Non-Yoruba
15 – 35	95	47	48	90	5
36 – 45	30	10	20	29	1
46 – 60	25	5	20	25	-
61 – 75	5	2	3	5	-
75 – above	-	-	-	-	-
Total	155	64	71	149	6

Source: Field survey

Table 2: Distribution of respondents by ownership of business and membership of cooperative societies

Year	Numbers of respondent that start business (X)	% of the respondents
2005	2	1.2
2006	14	9.03
2007	9	5.7
2008	21	13.6
2009	42	27.1
2010	67	43.2
Total	155	100

Source: Field survey

Ownership of a business and membership of cooperative societies

It was found that 100 percent of the respondents owned their own business. About 1.29 percent started in year 2005, 14 percent in 2006, 5.7 percent in 2007, 13.6 percent in 2008, and 27.1 percent n 2009. The 2010 had the highest record of 43.2 percent of the population under the study. The result shows that a very large percentage of the respondents owned their own business, an indication that they played vital role in wealth and job creation, hence reducing unemployment. Studies (Adeyemo et al, 2005; Adeyemo, 1982) have shown that sourcing fund through cooperative membership to establish business is crucial to fighting unemployment.

Result of Regression Analysis

Effect of Cooperative Societies on Capital Formation: Based on the R^2, F value, t-tests and 'a priori' expectation of the variables (Pindyck and Rubinfeld, 1998), the linear function was chosen for the analysis. The result of the linear multiple regression analysis is presented below:

Table 3: Distribution of respondents by membership of cooperative societies, ownership of business, profitability level and average numbers of employees.

Year	No of co-operator that access credit facilities	No of co-op. that owns a bus.	Profitability level*	Average number of employees
2005	2	1	5	2
2006	14	7	7	5
2007	9	6	9	10
2008	21	13	4	10
2009	42	25	6	15
2010	67	32	8	20
Total	155	84	39	62

* The level of profitability was deflated by 10% to make the data easier for computation.
Source: Authors Field Survey

From table 3 above, one could deduce that a total number of 84 co-operators own their business in the period under review, the profitability level in the year 2009 was about 60%, and the number of employees employed averaged about 15 employees. One can also see that as membership of cooperative increases, the numbers of co-operators that open their own business began to increase. The same thing apply to the numbers of employees employed in the study area, it increases as more business are opened.

Table 4: Results of the Regression and Inter-Correlation analysis between variables

Variables	Coefficient	Std. Error	t- Statistic	Prob.
Constant term (β_1)	-2.173	0.665913	-3.2632	0.000
X_2	1.9925	0.028392	7.018	0.000
X_3	0.022	0.03032	0.7257	0.008

$R^2 = 0.97234$ SSE= 89.124 $\hat{\sigma}=0.58634$ $t=1.96$ $\alpha=0.05$

From the above, it could be deduced that 7.018 >1.96, thus, we reject the H_0 (for H_0: $\beta_2 = 0$); the data supports the conjecture that membership of cooperative societies enhances capital formation in business financing. The same test outcome can be obtained, using the *p*-value. In this case we reject the Ho because 0.000>0.05. Also, since 0.72566<1.96 we reject the H_0:β_3=0 and conclude that there is evidence from the data to suggest that capital formation depends on profitability level. Using the *p*-value to perform the test, we reject the Ho because 0.000<0.05. The interpretation of R^2 is that 97.23% of the variation in the level of capital formation is explained by the variation in the membership of cooperative society and by the variation in the level of profitability. It means that only 2.77% of the variation in the capital formation of the respondents is left unexplained and is due to variation in the error term or to variation in other variables that implicitly form part of the error term.

IMPLICATION OF THE RESULT

The result of this paper shows that membership of cooperative societies could be one of the strategies to improve capital formation needed to finance a business, thus adequate provision of loan to the business owners/ co-operators will enhance their investments, and this will invariably increase their income and ability to generate employment, as corroborated by Adeyemo and Bamire (2005). On this note, this paper submits that regular enlightenment campaign and education should be organized by the government and other Non-Governmental Organisations (NGOs) for business owners especially the small scale business, on the advantages of joining cooperative societies. This could have a multiplier effect on business expansion which will in turn reduce aggregate unemployment and increase aggregate output in the economy.

CONCLUSION

Cooperative financing remains the vibrant economic technique of capital formation, wealth creation, job creation and business financing. There are various problems militating against the performance of cooperative societies in Nigeria. Some of these factors include the alarming level of indiscipline and corruption in the country which affects almost all sectors of our economy, cooperative society as a sub-sector inclusive. Another major challenge of cooperative society lies on the attitudinal behaviour of Nigerians towards consumptions. Nigerians like most third world people have a high taste for consumption rather than investment (Oyedepo, 2006). The fear is money borrowed for investment purpose could be diverted to consumption purpose like taking another wife, buying new cars and other downward investments. Hence, those who are interested in running cooperative business should be willing to confront these challenges. Agbo (2009) explained that the major problems facing cooperative societies in Nigeria are poor cooperative education, mismanagement of existing cooperative societies, illiteracy, political instability, overdue loans, lack of patronage of existing cooperative societies, bad projects, diversion of farm inputs meant for all by few and unfulfilled promises by the government. Also the changing world of technology poses great challenges to the efficiency of cooperative societies in Nigeria most cooperative societies are operating with inadequate capital to cope with the need of business financing, not to talk of IT needs for their operation, in view of this, the following recommendations are suggested.

The government and the various multinational NGOs should finance research suitable for planning; more effective cooperative education and training programmes for committees,

members and employees of cooperative societies should be encouraged so as to be able to cope with the changing socio-economic environment. Government should liberalize cooperatives by loosening its grip on cooperatives to allow for self-help and self-responsibility principles of cooperativeness. There should be aggressive Investment in Information and Communication Technology (ICT), as this has become imperative for a success-driven cooperatives. On-line update of members' passbooks, loan application, etc should be incorporated into the business of cooperatives so as to bring timely delivery and allow for wider coverage. Just like the government through the CBN introduce recapitalization exercise to the banking sub-sector, the cooperative sub-sector of the economy should be re-capitalized so as to prevent crisis in the sector. The government, NGOs and commercial banks should encourage cooperative societies by channelling funds for sustainable business well-being especially among the micro, small and medium scale businesses through cooperative societies.

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Chapter 15

IMPACT OF COOPERATIVE SOCIETIES ON MEMBERS BUSINESS

Abumchukwu Ifeanyichukwu **NZEKWE**

INTRODUCTION

The Rochdale society of equitable pioneers, founded in 1844, is usually, considered the first successful cooperative enterprise, used as a model for modern cooperatives following the "Rochdale Principles". According to Hoyt (1996) the major objectives of cooperatives is to provide support, render services and provide mutual and self help to the members. Dambiec (1997) in his own view said that cooperatives help people work together and move forward in a collective way.

According to Okonkwo (1992) the origin of Cooperative in the world is traced back to late eighteenth and early nineteenth century in England. He maintained that cooperative was the device adopted by the suffering working classes of the Industrial revolution to alleviate their pitiable conditions. He also stressed that origin of cooperatives in Nigeria can be traced back to 1935 when cocoa farmer's cooperative was formed in Western Nigeria. Cooperatives in Nigeria today have greater economic activities to play in order to improve the socio-economic well being of the members. In line with this, Hoyt (1996) suggested that the roles of cooperatives include: "employment creation, provision of retail services, production activities, enhancement of rural income, rural market development and provision of social activities to members". Cooperative started in Nigeria in early 1930s. Then, cocoa farmers were organized into miniature cooperative societies in Western Nigeria (Okonkwo, 1992). In 1933, a cooperative expert, Mr. C.F. Strickland was appointed to study and report on the desirability of establishing cooperative societies in Nigeria. After investigation, he issued a report in April 1934. The report contains the following fact; that Nigeria was fit for the introduction of cooperative society. The nature, objectives and types of cooperative societies which are most suitable in Nigeria were outlined. On the foot note of this favourable report recommendation was made for formation of cooperative society in Nigeria. Therefore, in 1935, the Nigerian cooperative society ordinance was enacted, and in 1936 regulations were drawn up to guide the running of cooperative societies in Nigeria. This paper therefore is to assess the impact of cooperatives on the members' business activities. In an attempt to achieve this, cooperative societies in Idemili North Local Government Area of Anambra State were studied by the researcher. The research questions postulated to guide the study are: What are the major business activities of Cooperatives under study? To what extent have Cooperatives in your area met the expectation of members by providing farm-input-supply, storage, marketing and credit function? How profitable are members' business in view of their membership of cooperatives? Two hypotheses were formulated to guide the study.

$H0_1$: Cooperatives in the study area have not met the expectation of their members in terms of farm input supply, storage, marketing and credit functions.

$H0_2$: There is no significant difference in the profitability of members business on gross margin per hectare (Gm/ha) and net return (NR/ha).

LITERATURE REVIEW

According to Chavez (2003) "cooperative society is an autonomous association of persons united voluntarily to meet their common economic, social, cultural needs and aspiration through a jointly owned and democratically – controlled enterprise. It is state chattered" business voluntarily organized, operating at cost owned, capitalized and controlled by member – patrons as users sharing risks and benefits proportionately to their participation". Also Rhodes (2010) was of the opinion that cooperative is a special type of business firm owned and operated for mutual benefit by the users/member patrons (Rhodes, 2010). Okechukwu (2001) in his own view, saw cooperative as an organisation of individuals who have voluntarily come together to contribute towards solving a common socio - economic problem which they cannot achieve on individual basis, reaping the benefits as well as bearing the risk collectively. Chavez (2003) identified seven internationally recognized cooperative principles which are: voluntary and open membership, democratic member control, member economic participation, autonomy and independence, education, training and information, cooperation among cooperatives and concern for community or social responsibilities.

Cooperatives play vital roles in improving the socio economic well being of the members'. According to Hoyt (1996) and Onoh (2009), the roles of cooperatives include: employment creation to individuals/ members of the society, sourcing and accessing funds for projects implementation, enhancement of cooperative society's management capacity for increased productivity, thereby contributes significantly to the rapid socio-economic development of the country, provision of retail services activities, provision of social activities to the members example is cooperatives education, provision of housing to members, political activities, and empowering women and men to participate in decisions that affect their lives and that enables them to build their strengths and assets. Kolawole (2006) provided the following as cooperative potentials and advantages. Cooperatives stand on behalf of small farmers and transact business in a cost effective manner, it locates the ability for the supply of required inputs, so that the production done timely enhances productivity, it also provide an ensured market for commodities produced by isolated, small farmers in rural areas, with collective action cooperative societies like agricultural cooperative can capture the benefit of value added, because of bulking and take advantages of introducing grade and standards allowing agro processing value addition for its members, and Cooperatives are responsible for stimulating poor farmers to make entry into markets enhancing demand for standards and grades for perishable commodities such as bananas, onions, tomatoes. According to Resource (2010) and Pomerleau (2006) the benefits of cooperatives are greater, most benefits are evaluated in economic terms but some also may be social. In several major ways, cooperatives benefit members and often non members through employment creation, rural market development, enhancement of rural incomes, improvement of access to social services, ownership and democratic control, increase farmers income, improve services, improving quality of supplies and production. In attempt to improve the socio-economic well being of members, Mudiobor (2005) identifies the followings as problems of cooperatives. Poor capitalization, dishonesty on the part of member's management and board of directors,

lack of regular inspection of cooperative societies by the government, inadequate infrastructural facilities due to lack of finance by the cooperatives, mismanagement of societies business, lack of cooperatives technical education on the part of members, board of director and management, poor cooperative corporate governance, inadequate human resources, limited regulations and supervision, low marketing and innovation, poor information technology, and high taxation. From the foregoing, the following problems may be added: Ineffective linkages or lack of networking, government interference and poor conflict management in the cooperatives by the leaders

The importance of cooperatives in boosting the economic well-being of the people cannot be over emphasized. Cooperative Society is an invention of necessity and originated from the evils of industrial revolution in early 18th and 19th century in England (Okonkwo, 1992). It is a vital tool for solving many rural problems. Black (2010) says that no matter how sophisticated a community is, cooperatives cannot be ignored. This is because it is a dependable source of food, money, meat, shelter etc. Despite the importance of cooperatives, there seems to be some problems jeopardizing cooperative activities and profitability of members' business. This may have increased the level of economic and food crises, we notice in our domain. Such problems are poor capitalization, lack of infrastructural facilities, high cost of transportation, lack of land to mention but a few. The broad objective of the study is to assess the economic impact of Cooperatives on members' business activities in Idemili North Local Government Area of Anambra State. In order to achieve this objective, the researcher identified the business-activities of Cooperatives in Idemili North Local Government Area of Anambra State; examined the extent to which the Cooperatives in the area have met the expectation of the members in terms of farm input-supply, storage, marketing and credit facilities; and assessed the profitability of members' business.

METHODOLOGY

The researcher adopted a survey and descriptive research design in carrying out the investigation. The study was conducted in Idemili North Local Government Area of Anambra State, Nigeria. This has 273 registered cooperative societies. At the time of this study 265 societies were moribund, while 8 of them were viable with a total membership of 204 and this formed the population of the study. Purposive sampling techniques were employed to ensure that some of the executives were interviewed. Simple random sampling techniques were also used in order to select the respondents to be interviewed. The sample size of 192 was drawn from the 8 viable registered Cooperatives in the study area using Yaro Yarmene formula because the population was not equal. However, after distributing the questionnaire to the respondents, only 150 were returned and found properly filled. The 192 sample size are from the following cooperative societies.

(1)	East-Niger Dist. F.C.S Ltd	24
(2)	Throne of God (Omagba I)	19
(3)	Maria Assumption Ogidi Emcs Ltd	37
(4)	Amafor West Nkpor F.M.C.S Ltd	30
(5)	Udo Amaka Nkpor M.C.S Ltd	19
(6)	Mustard Seed (Nkpor) F.M.C.S Ltd	20
(7)	Immaculate Women Nkpor F.M.C.S Ltd	19
(8)	The Nobles Nkpor F.U.G.C.S Ltd	24

The major instrument for the study was structured questionnaire made up of 41 items statements with four point scale format of Strongly Agree (SA), Agree (A), Disagreed (D) Strongly Disagree (SD) and Very Large Extent (VLE), large extent (LE), Small Extent (SE) and Very Small Extent (VSE) with 4, 3, 2 and 1 point rating respectively. Oral interview was also employed. The data collected were analyzed using the arithmetic mean and standard deviation. The assessment of impact of cooperatives was taken from three perspectives all at members levels; analysis of members' perceptions of the impact of cooperatives on economic activities of the members, the extents cooperatives met members' expectations and a profitability analysis of the member business. These perceptions were analyzed using four point Likert (1932) type response categories of very large extent (VLE), large extent (LE), small extent (SE) and very small extent (VSE) etc. The mean rating that ranges from 2.5 and above were regarded as large extent or agreed while the mean rating that fall below 2.5 were regarded as small extent or disagreed. The profitability analysis was employed to determine the effect of cooperative activities on the profitability of the business unit of the members. This was analyzed using gross margin (GM) and net return (NR) analyses.

Gross Margin

GM = TR – TVC

Net Return

NR = TR – TC

Where;

TR = Total Revenue
TVC = Total Variable Cost
TC = Total Cost

Hypotheses 1 is tested using t-statistic, to test the perception of the members as to whether their expectations have been met in relation to service received from the society. Hypotheses II was also tested using t-statistics to determine the profitability of members' business on gross margin per hectare (GM/ha) and net return per hectare (NR/ha).

DATA PRESENTATION AND ANALYSES

The results of the data analysis are presented below following the research questions:

Business Activities of Cooperatives

The analysis of the business activities of Cooperative were carried out to enable the researcher identify actually the real economic activities of these societies to their members.

Table 1: Business Activities of Cooperatives

S/N	Items	Mean	Standard Deviation	Decision
1.	Marketing of product	3.2745	0.58143	Agree
2.	Supply of agricultural inputs	3.2402	0.53096	Agree
3.	Production of crops and other consumer products	3.2745	0.58985	Agree
4.	Provision of credit and loans to member	3.5784	0.5335	Agree
5.	Processing of agricultural product and other related goods	5.4951	0.05121	Agree

Source: Field Survey, 2011

The data in table 1 indicates that respondents agreed with items 1 – 5 as business activities of cooperatives. This implies that Cooperatives market their members' farm products, supply farm inputs to their members, produce crop and animals that are required for consumption and even process these produce to different uses. The implication of this result is that if the government assists these societies financially and provides them with farming tools, there will be tremendous increase in total quantity and quality of production by the societies.

The Extent to which Cooperatives have Met the Expectations of Members in Terms of Farm Input, Supply, Storage, Marketing and Credit Functions.

The analyses of the extent to which Cooperatives have met the expectations of the members in terms of farm input-supply, storage, marketing and credit functions were analyzed to have knowledge on the impact of the society on the socio-economic needs of the members.

Table 2: Members Expectations from Cooperatives

S/N	Items	Mean	Standard Deviation	Decision
6.	To supply feeds, seeds and fertilizer that give farmers maximum gain or yield in your local government	2.7598	0.64031	Large Extent
7.	To provide members with dependable sources of reasonable price supplies especially during shortages or emergencies.	3.6373	0.48197	Large Extent
8.	Provide storage equipment or store products, when they will be available for steady supply.	3.455	0.58974	Large Extent
9.	Marketing of farm product for the members by cooperative marketing experts.	2.6716	0.78469	Large Extent
10.	Provision of credit facilities to the members	3.5736	0.53405	Large Extent

Source: Research Field Survey, 2011

The data in table 2 indicates that members' expectations from the society in areas of farm input-supply, storage, marketing and credit functions are satisfied to a large extent. This revealed that Cooperatives have to a large extent met the expectations of their members by providing farm feeds, credits, storage facilities and marketing of farm inputs etc for their members. This indicates that with government sponsorship of these societies, there will be

increase in food production, improved socio-economic condition and standard of living for the members and public.

Profitability of Members' Business

The profitability analyses of members' business activities were carried out in order to assess the profit realized by members from the cooperatives.

Table 3: Profitability Analysis

S/N	Variables/items	Mean	Minimum	Maximum	Std.Deviation
11.	Total Revenue (TR)	382352.94	200000.00	750000.00	172816.00723
12.	Total cost (TC)	220799.69	120000.00	380000.00	80455.19390
13.	Total Variable Cost (TVC)	153215.69	20,000.00	260000.00	62717.54297
14.	Total Fixed Cost (TFC)	675833.33	0.00	120000.00	38984.24485
15.	Gross, margin per hectare (GM/ha)	183377.45	45,000.00	490000.00	99635.68950
16.	Net return per hectare (NR/ha)	128455.88	26,000.00	370000.00	84201.10231
17.	Farm size	1.3333	1.00	2.00	0.47256

Source: Field Survey, 2011

The profitability analysis was presented on table 3. From the findings it was revealed that the cooperatives total revenue (TR) was N382, 352.94, total cost (TC) N220, 799.02, total variable cost (TVC) N153, 215.69 while total fixed cost (TFC) was N67, 583.333 for the year. The gross margin per hectare (GM/HA) was established at N183, 377.45 while the net return per hectare (NR/HA) was N128, 455.88. The minimum total cost and maximum total cost were N120, 000.00 and N380, 000.00 as against the minimum and maximum total revenue of N200, 000.00 and N75, 000.00 of the members. The table also indicated that the total revenue was more than the total cost incurred by the respondents. This showed that membership of Cooperatives was generally profitable in the study area. All things being equal greater effort in Cooperatives will enhance the income of the members.

Test of Hypotheses

Hypotheses I

$H0_1$: Cooperatives in the area have not met the expectations of their members in terms of farm input-supply, storage, marketing and credit functions.

The statistical hypotheses were tested using t-test. Data analyzing the hypotheses is presented in table 4.

Table 4: Test of Members' Expectations from the Cooperatives

	Test Value					
	N	Mean	Sig.2-tailed	T	df	Std.deviation
Mean performance rating	150	3.2200	0.000	169.386	148	0.27148

The t-statistics of 169.386 shown in the above table was found to be significant at 0.000 level. Therefore, we reject the hypothesis and conclude that the cooperatives have indeed met the expectations of the members by providing farm input – supply, storage facilities marketing and credit functions.

Hypotheses II

$H0_2$: There is no significant difference in the profitability of members on gross margin per hectare (GM/ha) and net return (NR/ha)

The statistical hypotheses are tested using t-test. The data analyzing the hypotheses is presented in table 5. To test the above hypotheses mean summary statistics of the responses of the members as regards to the profitability of cooperatives in the study area are presented as follows:

Table 5: Test of Profitability

	Test Value = 0					
	N	Mean	Sig.(2-tailed)	T	df	Std.deviation
Gross margin/ha	150	183377.5	0.000	26.287	148	99635.68950
Net Return/ha	150	128455.9	0.000	21.790	148	84201.10231

From the above table the t-test for GM/ha and NR/ha were 26.287 and 21.790 respectively. These values were found to be significant at 0.000 levels. Therefore, we reject the hypothesis and conclude that there is significant difference in the profitability of members business on GM/ha and NR/ha. Which means that members GM/ha and NR/ha are not the same.

DISCUSSION OF THE RESULTS

The result of the study revealed that cooperatives engage in different business activities such as; marketing of products, supply of input, granting of credit, crop production, animal rearing, processing of products and so on. This result is in line with the view of Willamson (2010) that Cooperatives involve in a series of inter-connected activities, such as; planning, growing of crops, harvesting, grading, packaging, transport, storage, food processing, distribution and sales of crops, fruits and livestocks etc. This result also agreed with opinion of Umebali and Agu (2009) who maintained that cooperatives involve in actual farm production, processing and marketing of farm products. This implies that cooperatives engage in different activities for their members' well being.

The result of the findings also revealed that the societies have met the expectations of their members by providing farm input to members, supply raw materials, storage facilities, marketing of cooperative products and credit functions for the members to a large extent. This result agreed with Pickard (2004) view where he said that the purposes of Cooperatives societies include: marketing of farm product, purchasing, home supplies, and provision of credits etc. The implication of this result is that, if other Nigerian cooperatives would be able to provide these services to their members, there will be general improvement in economic well being of the Nation. The result of profitability analyses indicated that, members' business units were found to be profitable since the total revenue was more than the total cost incurred by the members in the society. This therefore implies that joining Cooperatives will

increase the profit of members because the result indicated that it is a profitable venture for the members.

Finally, it is also interesting and quite instructive to observe that gross margin estimate of the cooperative members are higher than those reported by Adeyemo, Okeke and Akinola (2010) and Kolawole (2006). This concurred with Chambo (2007) who opined that cooperatives maintains higher level of income, thereby enabling small farmers to construct decent houses and send their children to school and provide health insurance to sustain rural livelihood. Pomerleau (2006) submitted that the benefit of belonging to cooperatives is judged by its net margins or savings. Therefore, our conclusion here is that Cooperatives have indeed raised the profitability of members business.

CONCLUSION AND RECOMMENDATIONS

Cooperative is a voluntary association of group of individuals who come together in order to meet the members' common social, economic, political, cultural needs and aspiration through a jointly – owned and democratically control business unit of their choice. The totality of this study revealed that Cooperatives improve the pitiable conditions of their members. They play greater role in meeting the members' expectations and improve the general well-being of the members through production of crops, raw materials, rearing of animals, processing, marketing of products, increase of members' business profits, gross margin or income etc. The result of their activities were general improvement in socio-economic well -being of the members more especially in the rural areas. Hence, Cooperatives remain the strong inevitable tool for economic growth and development of any nation.

Based on the result of the analysis of this study, it is obvious that any assistance/contribution rendered to these societies will strengthen their business effort and increase the members' economic business unit. Therefore, from this result the researcher recommends that the government and capitalists should assist these societies by providing cooperatives education, extension services and free education to members to increase their level of knowledge on the importance/needs of cooperatives in the society. Supplying and marketing of agricultural input and output to the cooperatives, providing cooperative farmers' hectares of land for extended farming practices thus boosting the quantity of crop and animal production in the area. Mechanization of agriculture to enhance specialization, increase in quantity and quality of production of farm products and other related products, standardization, grading and exports. Providing subsidies and loan to cooperatives for production efficiency. Organizing seminars, workshops and conferences for the Cooperatives. Encouraging integrated approach of cooperatives, providing basic infrastructural facilities for members and the societies. Encouraging cooperative corporate governance at all levels of management for openness and transparency in the organisation. Finally, it is also very pertinent to recommend that for improved performance, formation of more effective and efficient Cooperatives will lead to stabilization and or general improvement of the socio-economic well-being of the members.

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Chapter 16

GOVERNMENT AND ANTI-POVERTY PROGRAMMES IN NIGERIA: THE WAY FORWARD

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James O. **ABIOLA**

INTRODUCTION

This paper examines the various regions in Nigeria under Civilian and Military government since independence and how corruption of the ruling elites have succeeded in worsening the poverty level in Nigeria. Poverty is defined in terms of human conditions of varying grades and shades. Governance for the purpose of this paper is the exercise of rule or control over human and material resources. The developmental challenges facing Africa and African nations are enormous and cut across several fields. Two of them are examined in this paper. These are governance, especially in public administration and poverty, which is a serious deficiency affecting the African continent. Our specific focus is governance and poverty in Nigeria environment. After explaining what poverty as a construct means we discuss some of the causes of poverty in any given situation. The various regimes since independence were examined on the extent to which they were able to minimize or escalate the poverty situation within their term intenure of office. The various analyses showed that Nigeria has consistently moved from 'fair', to 'bad', and to 'worse' situation in area of minimizing or controlling the painful effects of poverty on the people. It is noted that poor governance has largely contributed to worsening poverty situation in Nigeria, because of its direct and significant impacts on several causes of poverty. Lists of recommendations are outlined as guides for implementation by our political leaders.

CONCEPTUAL FRAMEWORK

We attempted to define poverty and provide the list of it causes in any given society. We also discuss how Governance influences behaviour and the environment. The multidimensional nature of poverty has rendered it a controversial concept. However we shall present a few of the several possible definitions of poverty. In broad term, poverty presents a condition of human deprivation, extreme want or denial in respect of the primary life sustaining goods - food, shelter, and clothing. It represents a situation of imbalance in several domains of human existence ranging from lack of healthcare, education, and capacity to meet varying social obligations. Johnson, (1974) defines poverty as a situation or condition whereby the resources of individuals or families are insufficient to provide a socially acceptable standard of living.

Aluko (1975) defines poverty as lack of command over basic consumption needs such as food, clothing and shelter. Such lack of resources to meet the basic necessities incapacitates the individual in protecting himself/herself against social, economic and other deprivations. Therefore, when people have limited and insufficient food, poor clothing, live in crowded and dirty shelter, cannot provide medical care for self and family, cannot meet family and community obligations and other necessities of life, all are indicants of poverty. Contextually people are poor, when their incomes, even if sufficient for survival fall seriously behind the average attainable in their immediate community. Asama (2005) notes that poverty can be seen from two different perspectives (1) lack of money, which means both insufficient cash and chronic inadequacy or resources of all types to satisfy basic human needs such as nutrition, rest, warmth and body care and (2) powerlessness meaning those who lack opportunities and choice open to them and whose lives seem to be controlled by forces and persons outside their influences (e.g. people in position of authority, perceived ‘’natural’’ or ‘’evil force’’ or ‘’hard luck’’). Hamok (1999) notes that poverty is a symptom of imbedded structural imbalance, which manifests in all domain of human existence. It is therefore considered to be highly correlated with social exclusion, marginalization, vulnerability, powerlessness, isolation and deprivation. This multi dimensionality has given rise to conceptual debates which now characterized the concept of poverty. Ajakaiye and Adeyeye (2001) note that the dimensions include; the lack of access to basic needs/goods as a result of lack of, or impaired access to productive resources, outcome of inefficient use of the perception. There is the agreement that in conceptualizing poverty, low income or low consumption represents its symptom. Thus the World Bank (1990) definition of poverty line is based on the expenditure necessary to buy a minimum standard of nutrition and other necessities. Poverty is seen in this paper as lack of or the want of basic supporting goods and services.

Governance

In our discussions of poverty and the modes to be presented below, we have linked poverty with governance. Cornell et al.,(2004:6) conceptualised governance as ‘establishing rules we can depend on to coordinate our actions and achieve our goals in addition to making decisions and establishing policies in order to get things done’. Recent globalisation underlines the increased importance of international environment which in turn exerts demand on national government. As a result, the traditional conceptualisation of public sector, according to Peter and Pierre (1998) has come under increasing strains. Governance is therefore considered in terms of capacity of the state to continue to govern as it has in the past and to continue developing alternative mechanisms for exerting control over society (Peter and Pierre, 1998). Akinkugbe, (1999**)** states that governance is a concept that could be subjected to varied and diversified interpretations and beliefs and such may be difficult to measure to any degree of reliability. The World Bank (1997) defined governance as the manner in which power is exercised in the management of a country’s economic and social resources for development. Thus good governance is said to be synonymous with sound development management, since it is important in creating and sustaining enabling environment which promotes strong and equitable development, it is an important complement to good economic policies (Akinkugbe, 1999). As noted by Akinkugbe (1999**),** poor governance exists when following signs become noticeable in a country: Failure to make clear distinction between what is public and what is private, hence a tendency to divert public resources for private use: Failure to establish predictable framework of law and government behaviour conducive to development or arbitrariness in the application of rules and laws. Excessive rules, regulations, licensing

requirement etc, which impede the functions of markets and encourages rent-seeking. Priorities inconsistent with development, resulting in mis-allocation of resources. Excessively narrowly based and non-transparent decision making.

Akinkugbe (1999**)** states that when all the symptoms are sufficiently severe and occur together they tend to create an environment hostile to development and thus poor government. That governance from this perspective can be conceptualized as involving three interrelated dimensions of governance (1) influence the way public decisions and authority are exercised (2) the enactment of laws, policies and regulations that effect the allocation of resources i.e. expenditure and investment which affect incentives for other actors in the economy and (3) the corrective interactions of government when Market failures are noticeable or for inability to achieve development objectives. Therefore, the capacity of governance in modern state is defined by the existence of system of rules, institution and mechanisms when there are universal and predictable. The state is thus defined as a set of institutions that posses the means of legitimate coercion, exercised over a defined territory and its population referred to as society. The state consequently monopolizes rule making within defined territory through the medium of an organised government (World Bank, 1997). The states in the sub-Saharan African have gone through a path of negative growth and economic stagnation. The search for an explanation of lack of development in sub-Saharan African has continued to focus on the role of the state (Akinkugbe, 1999)**.** Akinkugbe (1999) notes that the non-development or anti development thrust has manifested in the mismanagement, inefficiency, and pervasive corruption of the public sector, including political instability and the ability to prevent widespread evasion of taxes, laws and regulations. Government of the state is one explanatory variable for the massive economic problems in Nigeria and other sub Saharan countries. Other includes hash international economic climate, natural calamities-drought and desertification, low saving and capital formation capacity, decline in foreign direct investment unmanageable external debt situation. The focus of this paper is however on governance i.e. the role of the state or institutional framework. We now examine some of the challenges that have contributed to poverty situation in Nigeria.

Causes of Poverty

Several factors have contributed to increased poverty for example in Nigeria. We shall examine them briefly in this segment of the paper.

Underdevelopment: A major cause of poverty is underdevelopment. Underdevelopment represents a situation where the capacity to meet the basic needs and desires of individual and social groups are grossly inadequate and unsatisfactory. Jhingan, (2003) notes that ‘due to underdevelopment a large percentage of Indian population has to go without even the most essential needs to daily life because total national income and hence aggregate consumption is too small relatively to the enormous size of the population’. The situation in Nigeria is not anyway markedly different.

Inequality: Another important factor is the extreme inequality of income in Nigeria. Akinjide (2004**)** notes that this inequality has produced two classes of Nigerians, the very rich and the very poor. He notes that the middle class who is the engine of development has been destroyed in Nigeria. Hence, Jhingan (2003), states that underdevelopment and inequality are the twin causes of poverty.

Macro-Economic Problems: There are several macro-economic problems which are part of the causes of poverty in Nigeria. For example in Nigeria, there is poor macro-economic and monetary policies which had resulted in low economic growth rate and continuous fall in the value of Naira. One reason for the failure of planning to make a major dent on poverty has been the growth rate.

Low per Capital Income: Poverty is reflected in Nigeria in the low per capital income. Torado and Smith (2003**)** state that the per capital income as at year 2000 in Nigeria was U.S $1,570.00, South Africa $3,020.00 and Egypt $3040 for the same period. Nigeria presents very poor picture of low per capital income, reflecting deep rooted case of poverty.

Inflation: Continuous rising prices are another cause of poverty. When prices rise the purchasing power of money falls and they lead to the impoverishment of the lower middle and poorer sections of the society. These inflationary pressures in Nigeria have further increased the number of poor people.

High Growth Rate of Population: The population growth rate has been very high in the third world countries against the growth rate of their economy. Torado and Smith (2003) notes that the birth rate in the less developed countries are generally very high, on the order of 30 to 40 per 2,000 whereas those in the developed countries are less than half that figure. There is also the **dependency burdens** in the sense that the older people and the children which are the unproductive members of the society represents about one-third of the populations of the developed countries but almost 45% of the population of the less developed countries, Nigeria inclusive. The result of the high growth rate of the population vis-a-vis low economic growth rate and the dependency burden equals aggravation of poverty in Nigeria.

Unemployment: Poverty is on the increase as a result of rise in the number of the unemployment. In Nigeria, Aliyu (2003) notes that unemployment assumed crises levels in the 1980s and early 1990s especially among the secondary school leavers and graduate of tertiary educational institutions, it is estimated that Nigeria's educational systems turn out annually about 5million unemployed people. These unemployed individuals worsen the already high level of poverty in Nigeria.

Low Availability of Essential Commodities: The poverty situations in the third World countries like Indian, Nigeria, Kenya and others have been deepened by low availability of essential commodities which is reflected in low standard of living.

Social Factors: This refers to requirement for fulfilling social obligations. Jhingan (2003**),** notes that in Indian, people are caught in the vicious circle of poverty due to the prevalent socio-cultural institutions. In order to fulfil social obligation and observe religious ceremonies form childhood to old age, people spend extravagantly. In Nigeria there are several ceremonies e.g. death, annual religious rites, marriage, house warming etc, in which people embark on wasteful spending in a situation of low income people will either dis-save or borrow. Consequently, high level of indebtedness due to borrowing is both the cause and effect of poverty.

Corruption: There are several dimensions of corruption in developing countries**.** Ogundele and Opeifa (2004) identified sixteen global causes of corruption in Nigeria based on empirical study. They range from economic, political, psychological, socio-cultural, family, leadership,

religious, legal/judicial, management slack, training and development, education, modernization values related and motivational cause. Aliyu (2003) earlier notes that in Africa, 'illegal take-over of government through military coups, embezzlement, nepotism, looting, bribery, vote buying and abuse of office are very common corrupt practices'. Through corrupt practices substantial amount of the nations wealth in the Third World Countries have been taken over by a privileged few to the disadvantage of the majority who are under condition of abject poverty.

Low Productivity: Low productivity refers to declining performance of the primary and manufacturing sectors of the economy. The reasons responsible for this feature include poor economic policies, political instability, weak private sector, and breakdown of societal values and lack of appropriate harnessment of internal resources.

Capital Deficiency: This stems from low availability of capital and low rate of capital formation. The rate of capital formation in the Third World Countries is below the level for the rapid grow of their economy. This deficiency is another cause of poverty in Nigeria.

Low Technology: Another factor that is responsible for poverty in Nigeria is the low level of technology. This means that the manufacturing process, agricultural production and marketing skills. The capacity of organize production units and financial marketing are far below the standards in developed economy (Jhingan, 2003). As a result of low technology, per capita productivity remains at a low level. This consequently keeps Nigeria economy in a poor state.

Political Leadership: Ogundele (2005a) notes that bad political leadership at the managerial levels in both the public and private sectors over the years had been a major cause for poverty in Nigeria. Aliyu (2003), states that the lack of development in Nigeria in the past years was due to bad governance.

Lack of Entrepreneurial Ability: Appropriate level of entrepreneurial development is lacking in Nigeria. Entrepreneurship is inhibited by several of the factors listed above, other include low level of education in the society, the social system, lack of business know how, legal constraints, lack of adequate motivation by government, lack of skills, constraints on opportunities for creativeness and several other factors. All these affect enterprise development which is important in the process of economic development, the lack of entrepreneurial ability is therefore one of the causes of poverty in the Third World Countries.

Globalisation Effects: The main feature of the process of globalisation are liberalisation of trade, free movement of capital, accelerated development in information technology, removal of control on interest and exchange rates, terms of trade, tariffs etc. (Aliyu, 2003). These features constitute problems for Nigeria for it lacks what it takes to be relevant or even adapt and cope with the requirements of globalization. Consequently, Nigeria remains at the receiving end of globalization, which further aggravate poverty situation.

Debt Burden: Debt burden is one of the major problems to development in the Third World Countries. Aliyu (2003) notes that around 40% of Nigeria national income goes to debts payments. That this high debts services ratio translates into resources constraints for infrastructures, utilities and productive sectors like agriculture, industry and manufacturing. The results are low productivity, low capacity utilisation, under employment, and low purchasing power thereby throwing the majority of the people into abject poverty (Aliyu,

2003). The outline causes of poverty represent serious challenges to the Third World Countries and Nigeria.

PAST AND PRESENT DEVELOPMENT PROGRAMMES IN NIGERIA

Nigeria seems to thrive on apparent contradiction. She is the 7th largest producer of crude oil in the world which should put the country in the group of prosperous and rich nation. This global expectations and the country's economic reality has been going in opposite directions for years. This is a case of wealth as paradox of poverty (Adeloye, 2005). The main reasons for this contradiction are bad governance and corrupt leadership. Ribadu (2005) states that Nigerian past rulers stole or misused a whopping $220 billion. This was squandered between independence and the return to civilian rules in 1999. That corruption on such a scale was made possible by the country's possession of 35 billion barrels of proven oil reserves. There were a number of development plans in Nigeria, particularly in the post independence era. These include, the first 1962-1968, the Second 1970-1974, the Third 1975-1980, the Fourth 1981-1985, the Fifth National Development plan ending in 1989, and three yearly National Rolling plans from 1990-1999, the rolling plan culminated in the vision 2010 for Nigeria (Ogundele, 2004a).

The First and Second and Third Development Plans

In the first and second national development plans, the criteria that were used include: Focusing on investment with greatest growth potentials, Ensuring the feasibility of various government proposals, Emphasizing economic desirability of projects, and Ensuring the achievement of maximum growth rate. Olayide (1976) notes that the planners of these two plans were conservative in their target rate of growth. All they planned for was the maintenance of normal growth rate of the economy which was the 6.7 percent between 1962 and 1971. This could have produced a great and dynamic economy.

The Fourth National Development Plan 1981-1985

Yesufu (1996) notes that judging by the actual performances of the economy, the period 1981-1985 proved to be relatively the most dismal since the economic development was introduced in 1954. The growth rate of GDP per annum was only 1.25%. Only agriculture, government services, real estate and business and housing sectors recorded positive growth rate per annum. Some of the factors that militated against the implementation of plan were large scale corruption, high level of inflation, lack of coherent policies lack of effective data base, period lag in feedback, simplistic and optimistic projection, over invoicing and over-valuation of contracts and high level of indiscipline. The problems listed above compounded the poverty situation in Nigeria, in that period. Anyanwu et al. (1997), note that by 1986 it was realized in Nigeria that adopting a five-year planning model has become unrealistic in Nigeria situation. The government then decided to adopt a three-tier planning system for better economic management. This includes: A 15 to 20 years perspective plan which will provide clear vision of where the economy should be at the end of the period. The three-year national rolling plan and one year annual budget.

Performance of the Economy from 1999 to Date

Fadeyi and Ogundele (2005) examine the performance of the economy based on one indicator that appears to capture many of its aspects i.e. growth rate of GDP. It was 2.7 in 1999, 3.5 in 2000, 3.5 in 2001, 3 in 2002, 7.1 in 2003, 6.2 in 2004, 6.9 in 2005, 5.3 in 2006 6.4 in 2007, 5.3 in 2008, 5.6 in 2009 and 8.4 in 2010. Currently, there is the report that the GDP is showing some positive improvement over last year's level. The lack of any appreciable level of development in Nigeria since independence is the result of lack of developmental vision. Past National Plans were based on ideas of a few self interested individuals or borrowed models from other parts of the world. A look at the definitions of vision and development and the core values and objectives of development show that Nigeria seriously falls short of meeting the set of criteria put forward. The basic reason is the application of inappropriate models in the developmental process of Nigeria economy. This, coupled with the strive to comply with the conditionality imposed by International Monetary Fund (IMF) and World Bank, have never produced positive development in all the less developed countries where they have been applied. Akinjide (2004) notes that 'Nigeria economy now lives on artificial respiration'. That bad economic management has been persisting because Nigeria leaders listen to the IMF and World Bank. That IMF and World Bank are not building contractors but demolition contractors. Their interest and ours are different; nations which control the IMF and World Bank control them for their own nations. This calls for a new and more relevant vision for Nigeria economic development. It is at this point that NEEDS, with its vision of Nigeria development will be examined.

The Various Anti-Poverty Programmes Since Independence

The first civilian administration at the national and regional levels carried out various entrepreneurial development initiatives aimed at combating poverty in Nigeria. These were in addition to the development plans discussed above. Among the institutions established to combat poverty in Nigeria are the Industrial Training Centres in Oshogbo, Zaria and Owerri and several trade centres all aimed at developing people with requisite skills for entrepreneurial career and also providing them with some forms of financial and materials supports. The anti poverty relating objectives during 1962-1985 periods were: To increase per capital income, to ensure more even distribution of income, to reduce the level of unemployment, and to increase the supply of high level manpower.

Obadan (2001) and Ogwunike (2001) note that subsequent development plans were to follow with poverty-alleviation related goals, with emphasis on boosting agricultural production, increase in real income of the average Nigerian, in addition to reducing income inequality among others. Apart from development plans the government in its fight against poverty, established a number of institutional mechanism. These include River basin Development Authority (RBDA), Agricultural Development Programme (ADP), Agricultural Credit Guarantee Scheme (ACGS), and Rural Banking Programme (RBP). The schemes were designed primarily to care for such objectives as employment generation, enhancing agricultural output and income generating ventures to stem the tide of rural-urban migration which will affect poverty reduction (Ogwunike, 2001). There was also the Operation Feed the Nation Revolution of 1980. The SAP era witnessed the worsening of the socio-economic and political situation in Nigeria.

Various programmes were targeted at various dimensions of poverty by the government such as Family Support Programmes (FSP), Community Bank (CB), Directorate of Food and Rural infrastructure (DEFRI), National Directorate of Employment (NDE), Better Life Programme (BLP) and Family Economic Advancement Programmes (FEAP). These anti-poverty programmes recorded achievements in the area of good production, primary health care, education, environment, mass transit programmes and financial services through the people's Bank of Nigeria and Community Banks (Obadan, 2001). Omotola (2005) notes that yet the level of poverty in Nigeria has attained unprecedented height of 70 percent, showing the inefficiency of the strategies and programmes. The programmes failures have been attributed to lack of targeting mechanism for the poor, political and policy instability, inadequate coordination of various programmes, several budgetary, management and governance problems, lack of accountability, overextended scope of activities of most of the institutions, and lack of mechanism for sustainability of most of the programmes (Nemedia, 2001). The Poverty Alleviation Programme (PAP) was introduced in 2000 as a temporary anti-poverty scheme. The programme essentially seeks to reduce the level of unemployment and hence raise effective demand in the economy. Though the programme was able to recruit some unemployed youth at inception it has not been able to make much impact on poverty in Nigeria. The ineffectiveness of PAP and the inadequacy of a policy that aims at alleviating people's poverty instead of eradicating it informed the government to come up with National Poverty Eradication Programme **(**NAPEP) initiative in 2001. NAPEP essentially aims at the provision of strategies for eradicating absolute poverty in Nigeria. It is complemented by the National Eradication Council (NAPEC) which is to coordinate the poverty related activities of all relevant ministries, parastatals and agencies (Obadan, 2001).

THE WAY FORWARD

The poverty reduction initiative of the present government together with its other economic reform packages are already yielding positive result at the global level. It has earned Nigeria a debt relief of N18 billion which the president referred to as dividend of democracy. Amaefule et al. (2005) report that Nigeria Minister for Finance highlighted the fact that the "debt relief package was an endorsement of the implementation of the country's economic reform package the National Economic Empowerment and Development Strategy, which the creditors recognized externally. But for Nigeria to reap full benefits from the programme in terms of its poverty eradication effects we want to provide a number of recommendations so that all the poverty reduction initiatives of the present administration will really and substantially reduce poverty to a considerable degree and provide a stable environment for development. The key strategy for fighting is that of accelerated pace of socio-economic growth and increase in general level of productivity in the country.

Therefore the necessary actions that should be taken to change the poverty situation in our environment include faithful implementation of NEEDS and other supportive programmes which are macro and micro-economic policies and programmes designed to fight poverty, (Soludo, 2004). There should be appropriate framework to determine target of interventions. The studies of poverty have shown it to be overwhelmingly a rural phenomenon in Nigeria, (World Bank, 1996, 1999; Wiseyila, 1999; Ajakaiye et al., 2004) it is therefore reasonable to concentrate more on rural institutions such as Community Development Association. Ensure full and proper implementation of Universal Basic Education (UBE) and other structural levels of our educational policy to harvest from the NEEDS policy thrust. There should be massive mobilization and orientation of the populace. The practice of ad-hoc arrangement is

one of the strong factors causing high motality of government programmes in Nigeria. Involving targeted people is very important for the success of any programme. Poverty alleviation programmes have failed in this country because the people for whom it was meant were not involved in the design and execution of such ideas. NEEDS documents are still been extensively discussed in seminars and conferences (Ogundele, 2004, 2005a; Ogundele and Oghojafor, 2005, and Fadeyi and Ogundele, 2005a). Promote awareness in the community with regards to NEEDS and other supporting programmes. The government still needs to intervene in critical sector of the economy to fight poverty, given Nigeria's level of development. It may have to intervene directly in the areas of technology for agriculture and other food production and their marketing related processes. There is also need for institutionalization of democratic political culture and citizenship at all levels. It is only within such a framework that the idea of good governance, transparency, accountability and control can be effectively nourished and consolidated (Omotola, 2005).

There is also need for intensive skills development among the populace so that they will be able to respond effectively to the wide ranging opportunities in Nigeria economic environment (Ogundele and Oghojafor, 2005). Effective leadership with culture of discipline, honesty, transparency and community centre is a must (Ogundele, 2005a). Management in terms of various aspects of their functioning in private and public sectors must be more development in outlook.

CONCLUSION

This paper has argued that poverty is a condition of deprivation which hinders development. The nature and pattern of poverty, based on government actions, from independence till today are examined. It is concluded that past anti-poverty programmes have failed based on the approach and the process of implementation and massive corrupt practices. We pointed out that NEEDS and other initiatives by the current administration seem promising. In the final analysis if the current initiatives at combating poverty must yield desired results, the role of the state in the development process must be revisited, that is, the state will have to take a leading position and other recommendations outlined above should be incorporated into the functioning of NEEDS so that real poverty reduction could be attained. This is because governance has been shown in this paper as the major influencing factor in controlling poverty positively or negatively.

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Chapter 17

PERSONALITY AND LEADERSHIP STYLE AS PREDICTORS OF INTENT TO ESCALATE COMMITMENT IN FINANCIAL INSTITUTIONS

Olusola Iyabode **AKINBOBOLA**

INTRODUCTION

Decision making is inevitable in organisations including the financial institutions where decisions are made mostly in relation to disbursement of funds. Financial institutions diversify into capital market, insurance, pension and banking industry to provide financial services. The banking industry incorporates mortgage banks, investment banks and commercial banks. Commercial banks such as cooperative banks are retail, and are organized on cooperative basis. Cooperatives are people and not capital oriented as other commercial banks; provide financial services to low income clients who traditionally lack access to banking and help people out of poverty through provision of credit services to poor clients in developing economies. The result of decisions made in financial institutions may be favourable or unfavourable. When decisions are unfavourable, decision makers in order to justify a losing previous decision, have a heightened need for continued commitment to the initial course of action (Drummond, 1994; Staw, 1982). There is tendency to persist with a losing course of action termed escalation of commitment. Intent to escalate commitment is the individual's predisposition and tendency to stick to an initial course of action despite convincing proofs received from negative feedback that the initial decision was ineffective. Fishbein and Ajzen (1975) proposed that behaviour can be preceded by intention specifically intent to escalate commitment predicted escalation of commitment behavior (Akinbobola, 2008). Staw (1976) propounded in his theory of escalation of commitment that decision makers persist on a losing initial course of action because of self justification for ego defense and external justification for face saving. Escalation of commitment is an irrational commitment and most probably has a magnitude effect on the organisation. Kahneman and Tversky (1979) used an alternative approach of framing of preferences into gains and losses to further explain escalation of commitment. Decision makers tend to exhibit risk seeking or risk averting behaviour to the framed outcomes. Decision makers who become risk seeking when they receive negative consequence will increase commitment to a losing course of action and undergo risk of further losses (Kahneman and Tversky, 1979; Schoorman, Mayer, Douglas and Hertrick, 1994). Decision makers who become risk averting when they receive negative consequence will decrease commitment to a losing course of action. Wong (2005) reported that risk taking behaviour is associated with escalation of commitment.

The banking industry in Nigeria in 1985 (Kayode and Odusola, 2002) and cooperative banks in developing countries in the 1990's (Birchall, 2001), experienced distress with the introduction of Structural Adjustment Programme (SAP). Distress became a perennial

phenomenon in the banking industry in Nigeria (Soludo, 2004) and led to the collapse of some banks. The apex bank, the Central Bank of Nigeria (CBN), against this background advocated the banking sector's reforms (CBN, 2004). The global stock market in 2008 (Crawford and Young, 2009) dropped due to problems in the mortgage market which led to a worldwide credit crisis culminating in financial institutions failure in Europe and the United States of America. Azmi (2011), ILO (2002) and ILO (2008) advocated cooperative financing which is social and economic reforms for developing economies. Birchall, Hammond Ketilson (2009) commented that cooperatives in developing economies endured the financial distress better than their commercial bank counterparts; nevertheless cooperatives are still developing (Pollet, 2009). Furthermore, only few studies viewed distress in financial institutions from an escalation of commitment perspective. Most studies viewed financial institutions distress from an economic point of view. This study therefore seeks to highlight escalation of commitment and the challenges of financial institution distress, from a psychological perspective.

Decisions made by financial institution staff lead to financial institution distress. Certain psychological factors in the individual may influence him or her to make decisions that lead to distress. However, in organisations, decisions are mostly made by its leadership. Continued commitment to a losing initial course of action may be a function of leadership. Some researchers, such as Miller and Toulouse (1998) explored escalation of commitment and suggested that leadership style of decision makers could be a source of inappropriate persistence within an organisation. Some approaches to leadership are trait, behavioural, contingency and contemporary styles.

Transformational/transactional leadership is one of the most recent researched approaches to conceptualizing leadership (Bass, 1990; Pawar, 2003). Transactional leadership refers to a leader who manages, sustains and controls achievement of already established goals in the organisation. McKenna (2000) explained that transactional leadership is appropriate under stable conditions in an environment characterised by risk aversion in decision making. Transformational leadership on the other hand refers to a leader who brings about changes in people and organisation by creating, communicating and modeling a vision and inspiring the organisation to strive for the vision and goals. Such leader also brings the organisation to a greater awareness of its environment and the understanding of established views and decisions, which are necessary to keep the organisation aligned with its outside environment. In another view, Conger and Kanungo (1994) found that transformational leaders have a strong personal commitment to their goals and are prepared to take high risks and incur significant costs to support their vision. When financial institutions such as few Nigerian banks in 1985 and global stock market in 2008 collapsed, the management of the institutions was believed to be one of the factors that contributed to such failure (Azmi, 2011; Udegbe, 2005; World Bank, 1993). Managers in general including those of financial institutions perform leadership and decisional roles. They make decisions on disbursement of funds such as credit cooperative financing, microfinancing, mortgage loans financing and bank loan financing. They exhibit escalation of commitment behaviour in some decisions as they become locked unto an escalation situation (Staw, 1981). The escalation of commitment is partially responsible for the worst financial losses experienced by organisations (Kreitner and Kinicki, 2000).

The success and failure of an organisation depends on the quality of its leadership. Researchers such as Kisfalvi (2000), Miller and Toulouse (1998) did not agree with Bass's

view of the omnipotent transformational leader. Bass (1990) believes that transformational leadership is the solution to organisational success. However, no empirical study was conducted to verify this opinion. Other schools of thought (for example, Pfeffer, 1992) earlier down played the role of leadership style in organisational outcomes. Little attention has been given to the role of transformational/transactional leadership style on escalation of commitment. It has therefore become imperative to conduct an empirical study on the influence of leadership style on escalation of commitment. Leaders bring personality attributes to the organisation which is regarded as being of key significance in their decision-making. Decision makers also experience a number of personal limitations that make it difficult to identify problems and opportunities, choose solutions and evaluate decision outcomes. Personality factors such as self efficacy and need for achievement may predispose a leader to behave in certain ways, including decision making and the escalation effect (Schaubroek and Williams, 1993).

Other researchers, such as Seijts, Latham and Whyte (2000), Whyte, Saks and Hooks (1997) reported that high self-efficacy subjects have a tendency to persist especially in economic task and therefore escalate commitment. McClelland, (1965) propounded that people have a need for achievement and an attitude towards risk. Lack of adequate commitment to a losing course of action might be due to some personality factors such as self efficacy and need for achievement. It is pertinent to determine in this study if self efficacy and need for achievement will influence intent to escalate commitment. Demographic factors may also play role in persistent behaviour (Datta and Rajagopalan, 1988), but in this study they are controlled for. According to Barnes (1984), Schwenk (1988), being a male or a female may influence escalation of commitment. Finkelstein and Hambrick (1996) and Kilsfalvi (2000) found that top management team demographic heterogeneity, which is variation in sex, age and job tenure of leaders who are open-minded with wider range of ideas, influence escalation of commitment.

The objective of this study is to highlight the influence of leadership style and personality factors on intent to escalate commitment among decision makers who work in financial institutions in Nigeria and who are Banking and Finance graduate students of a university in Nigeria. These factors must be understood if solutions to leaders' problem on commitment to investment decisions leading to financial distress are to be adequately considered. Findings from this study will provide information not only on personality and leadership style of decision makers but also on the problem of commitment to investment decisions leading to financial distress. Findings may eventually be useful for policy formulation and implementation for Millenium Development Goals (MDGs) in developing economies. Based on the foregoing, the hypothesis stated was that leadership style, self efficacy and need for achievement will independently and jointly predict intent to escalate commitment while controlling for sex, age and job tenure.

METHOD

The study adopted an expost facto design; the variables were not under the direct manipulation of the reseacher. The independent variables were transformational leader behavior, transactional leader behavior, self efficacy and need for achievement. Demographic variables sex, age and job tenure were controlled for. The dependent variable was intent to escalate commitment. A total of 348 participants who were Master of Business Administration (Banking and Finance) graduate students of a University in Nigeria took part

in the main study. These participants were randomly selected and comprised 210 (60.3%) male and 138 (39.7%) female, whose average age was 37.62 with standard deviation of 6.16. Tenure on the job had average of 11.36 and standard deviation of 6.14. The participants were working, with 185 (53.2%) in banking, 26 (7.5%) in financial institutions and 115 (33.0%) in finance and accounts departments of non-financial organisations. Following Biyalagorsky, Boulding and Staelin (2001) pattern of study in choice of participants; the MBA students used for this study were logically and significantly generalized to the population of senior level managers as utilized by Boulding, Morgan and Staelin (1997) who normally make major investment decisions. Biyalagorsky, Boulding and Staelin (2001) using MBA students replicated Boulding et. al. (1997) study, the results of these studies showed no substantial differences and that increased researchers' confidence that findings of MBA students' can be generalised to the population of senior managers. The participants indicated their willingness to participate in the present study. A questionnaire was used and divided into sections. In Section A is contained the intent to escalate commitment scale developed for the purpose of this study. The scale comprised 27 items, Likert format and rated as strongly agree 5, to strongly disagree 1. Content validity was established by giving the 34 items to experts on the basis on which 27 items were picked. The 27 items were subjected to item-total correlation and the items had coefficient that ranged between 0.37 and 0.94. The reliability for the whole scale is coefficient alpha of 0.97. Following this, a factor analysis was carried out using the varimax rotation leading to three factors accounting for 71.9% of the total variance. Based on literature review, the three factors were named external justification, ego defense and biased belief update. The coefficient alphas for the respective factors were: 0.97, 0.96 and 0.84. Section B of the questionnaire measured transformational leadership style.

The 28-item scale was developed by Podsakoff, Mackenzie, Moorman and Fetter (1990). Olaseinde (2005) used the scale on Nigerian subjects and reported coefficient alpha of 0.79. The scale comprised seven dimensions. The higher the score on the first six dimensions, the higher the participants transformational leader behaviour. The higher the score on the seventh dimension the higher the participants' transactional leader behaviour. The reliability coefficient for the respective dimensions as reported by the authors were: articulate vision 0.90, provide appropriate model 0.97, foster acceptance of goals 0.83, high performance expectations 0.78, individual support 0.90, intellectual stimulation 0.91 and the seventh leadership dimension that measures transactional leadership 0.92. The result in the present study showed that the reliability coefficients for the respective dimensions were: 0.88, 0.87, 0.88, 0.76, 0.80, 0.87 and 0.74. Section C of the questionnaire contained a 10-item self-efficacy scale developed by Bandura (1997) measuring the respondents' belief in their ability to complete a task successfully. The higher the score on the scale the higher the participant's self efficacy. The author reported a coefficient alpha of 0.76. This study reported a coefficient alpha of 0.83. Section D of the questionnaire consisted 9-item need for achievement scale developed by Oyefeso (1988) which is the modified version of Edward's (1954) 15-item scale. The scale measures respondents' drive to excel, to achieve and to strive to succeed in whatever they do. Oyefeso (1988) reported a split-half reliability coefficient of 0.85 among Nigerian samples. The higher the score on the scale the higher the participant's need for achievement. This study indicated coefficient alpha of 0.92.

Section E of the questionnaire consisted of items measuring the personal demographic data of the respondents such as age, sex and job tenure. The systematic sampling procedure was used by picking the 3rd name from the class list and the students were selected for the study. A pilot study was conducted using 190 bankers for the purpose of establishing reliability. During the

main study, the instructions were duly explained to the participants. The questionnaire was given to the participants in the auditorium. A total of 348 copies of the questionnaires were administered to the participants

RESULTS

Data collected were analysed using zero order correlation summarised in Table 1 below, and hierarchical regression analysis with demographic variables, serving as control variables. The analysis was run on overall score on intent to escalate commitment as well as the score on the 3 subscales. The result in Table 2 below showed that the demographic variables which were entered in model 1 jointly accounted for variance on intent to escalate commitment ($R^2 = 0.04$; $F(3,340) = 4.90$; $p < .01$). Only sex independently significantly predicted intent to escalate commitment ($\beta = 0.16$; $p < .01$), indicating that female participants are higher than male participants on intent to escalate commitment.

The inclusion of leadership style entered in model 2 jointly accounted for variance ($R^2 = 0.33$; $F(10,333) = 16.30$; $p < .01$). The result specifically revealed 29% change in variance ($\Delta R^2 = 0.29$; $p < .01$). Only transactional leader behaviour independently significantly predicted intent to escalate commitment ($\beta = 0.37$; $p < .01$). Further inclusion of personality variables entered in model 3 jointly accounted for variance ($R^2 = 0.36$; $F(12,331) = 15.07$; $p < .01$). Only self efficacy ($\beta = -0.14$; $p < .01$) independently significantly predicted intent to escalate commitment. For the 3 sub-scales, result in Table 3 below revealed that the demographic variables jointly accounted for variance in the first subscale, external justification for escalation of commitment ($R^2 = 0.03$; $F(3,340) = 3.09$; $p < .05$). Only sex independently significantly predicted external justification for escalation of commitment ($\beta = 0.11$; $p < .05$). The inclusion of leadership style entered in model 2 jointly accounted for variance ($R^2 = 0.26$; $F(10,333) = 11.65$; $p < .01$), resulting in 23% change in variance ($\Delta R^2 = 0.23$; $p < .01$).

Among the six dimensions of the transformational leader behaviour only “provide appropriate model” independently significantly predicted external justification for escalation of commitment ($\beta = 0.19$; $p < .05$). Also, transactional leader behaviour significantly predicted external justification for escalation of commitment ($\beta = 0.38$; $p < .01$). This means that transactional leader behaviour contributes more than “provide appropriate model” in the explained variation in external justification for escalation of commitment but both contributed positively. Further inclusion of personality factors in model 3 jointly accounted for variance in external justification for escalation of commitment ($R^2 = 0.28$; $F(12/331) = 10.82$; $p < .01$). Only self- efficacy significantly predicted external justification for escalation of commitment ($\beta = -0.14$; $p < .01$). This means that the higher the self efficacy the lower the external justification for escalation of commitment.

For the second sub scale, which is ego defense for escalation of commitment, Table 3 revealed in model 1 that only sex significantly predicted ego defense for escalation of commitment ($\beta = 0.12$; $p < .05$). The inclusion of leadership style in model 2 jointly accounted for variance ($R^2 = 0.21$; $F(10/333) = 8.63$; $p < .01$). The result also revealed 19% change in variance ($\Delta R^2 = 0.19$; $p < .01$). Only transactional leader behaviour independently significantly predicted ego defense for escalation of commitment ($\beta = 0.31$; $p < .01$). Further inclusion of personality variables entered in model 3 accounted for variance ($R^2 = 0.21$; $F(12,331) = 7.32$; $p < .01$). However, the personality variables did not independently predict ego defense for escalation of commitment.

For the third subscale, biased belief update for escalation of commitment, Table 3 revealed that the inclusion of leadership style entered in model 2 jointly accounted for variance (R^2 = 0.22; F (10,333) = 9.29; p< .01) resulting in 20% change in variance (Δ R^2 = 0.20; p< .01). Only transactional leadership behaviour independently significantly predicted biased belief update for escalation of commitment (β = 0.33; p< .01). Further inclusion of personality factors entered in model 3 significantly accounted for variance (R^2 = 0.23; F (12/331) = 8.09; p< .01). However, only self efficacy independently significantly predicted biased belief update for escalation of commitment (β = -0.10; p< .05). This indicated that the higher the self efficacy the lower the biased belief update for escalation of commitment.

DISCUSSION

From the result, it could be seen that sex, transactional leader behaviour and low self efficacy significantly predicted intent to escalate commitment. Female participants exhibited intent to escalate commitment higher than male participants. The findings from the present study confirmed earlier findings by Datta and Rajagopalan (1988), who found that demographic factors played major role in persistent behaviour, escalation of commitment is a type of persistent behaviour. Other researchers like Barnes (1984) Schwenk (1988) also reported that being a male or a female influenced escalation commitment. Empirical explanations for this outcome could be found in the results on the subscales of intent to escalate commitment. Research revealed that females are more ego defensive than males because of stereotype. Stereotypes define people by the demographic and organisational groups they belong. Theoretically, according to Babalola and Olapegba (2005) and Katz (1960), ego defense makes the individual to hold back self knowledge, seeks only to express and acknowledge his/her commitments. The individual protects himself/herself from acknowledging his/her deficiencies and defends his/her self concept. These may explain why a female will escalate commitment higher than a male. Miller and Toulouse (1998) suggested that leadership style of managers could be a source of inappropriate persistence within an organisation. The study revealed that leadership style significantly accounted for variance in intent to escalate commitment. However, among the six transformational leadership behaviour dimensions examined, only one dimension, “provide appropriate model” contributed significantly in the joint influence. “Provide appropriate model” contributed significantly in a subscale of intent to escalate commitment, which is external justification. The more inclined a leader is in providing appropriate model for subordinates the higher his or her intent to escalate commitment. Conger and Kanungo (1994) have described leaders who provide appropriate model as high risk takers. Such leaders would believe that one of the ways subordinate could respect a leader is if a leader takes a decision and is able to stand by the decision without change. This might also be responsible for the result of such persistence in decision made for risky actions and Wong (2005) reported that risk taking behaviour is associated with escalation of commitment. Moreover, in the prospect theory, Kahneman and Tversky (1979) explained that people who escalate are risk takers. This confirms the description of leaders who provide appropriate model as risk takers.

The result revealed that transactional leader behaviour also contributed significantly to intent to escalate commitment and the three subscales which are external justification, ego defense and biased belief update. This might not be unconnected to transformational leadership theory by Bass (1990) that the transactional leader sustains status quo thereby maintaining persistent behavior of escalation of commitment. The result in the hypothesis further revealed that self–

efficacy independently predicted intent to escalate commitment. Specifically, it was found that the higher the self efficacy the lower the intent to escalate commitment. This is contrary to the findings of other researchers such as Whyte, Saks and Hooks (1997); Seijts, Latham and Whyte (2000) that high self-efficacy subjects have a tendency to persist especially in economic task and therefore escalate commitment. Kisfalvi (2000) found that self-efficacy is a predictor of escalation decisions.

IMPLICATION AND RECOMMENDATION

For effective reforms in the financial institutions' perennial distress, the following shall be considered as implications of the present finding. There should be involvement of managers with transformational leader behaviour and preference for managers with high self-efficacy in decision making, to prevent and to curb intent to escalate commitment budding into escalation of commitment behaviour. Management should recruit leaders and members of staff with heterogeneous personal demography to attain broad strategic alternatives in financial decision making and disbursement of funds such as credit cooperative financing, microfinancing, mortgage loan financing and bank loan financing. It is important that psychological perspective of financial distress be taken seriously. It is recommended that government should start to use the services of psychology experts if they are sincere in the realisation and implementation of the financial reforms, interventions and MDGs. Psychological determinants of escalation are used in the present study, future research should include social and project determinants.

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Table 1: Zero-order correlation matrix showing the relationship between the independent variables and the dependent variables specifying dimensions

Variables	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**	**14**
1. Age														
2. Job Tenure	.72**													
3. Articulate Vision	-.93	-.15**												
4. Provide Appropriate Model	-.13*	-.16**	.68**											
5. Foster Acceptance of Goals	-.14**	-.13*	.65**	.77**										
6. High performance Expectation	-.09	-.11*	.58**	.69**	.74**									
7. Individual Support	-.10	-.10	.29**	.44**	.43**	.37**								
8. Intellectual Stimulation	-.13*	-.13*	.61**	.71**	.73**	.69**	.45**							
9. Transactional leadership Behaviour	-.09	-.11*	.45**	.66**	.67**	.64**	.53**	.69**						
10. Self efficacy	.10	.09	-.14**	-.32**	-.30**	-.25**	-.20**	-.32**	-.27**					
11. Need for Achievement	.02	.09	-.23**	-.25**	-.27**	-.22**	-.14**	-.23**	-.26**	.22**				
12. Biased Belief Update	-.10	-.08	.26**	.39**	.39**	.40**	.36**	.38**	.49**	-.23**	-.11*			
13. Ego Defense	-.08	-.03	.26**	.39**	.38**	.37**	.33**	.40**	.47**	-.20**	-.15**	80**		
14. External Justification	-.10	-.11	.27**	.44**	.41**	.39**	.31**	.42**	.53**	-.29**	-.22**	.74**	.84**	
15. Intent to Escalate Commitment	-.12*	-.08	.20**	.40**	.39**	.35**	.27**	.37**	.49**	-.32**	-.23**	.60**	.61**	.67**

**P<.01 *P<.05

key: Zero-order correlation matrix in Table 1

1 = Age
2 = Job tenure
3 = Articulate vision
4 = Provide appropriate model
5 = Foster acceptance of goals
6 = High performance expectations
7 = Individual support
8 = Intellectual stimulation
9 = Transactional leadership behaviour
10 = Self efficacy
11 = Need for achievement
12 = Biased belief update
13 = Ego defense
14 = External justification
15 = Intent to escalate commitment

Table 2: Hierarchical regression of intent to escalate Commitment on leadership style and personality factors

Variables	**Model I** Beta	**Model II** Beta	**Model III** Beta
Step 1: **Control Variables**			
Age	-0.12	-0.11	-0.11
Sex	0.16**	0.15**	0.14**
Job Tenure	0.01	0.08	0.09
Step 2: **Leadership Style**			
Articulate Vision		-0.09	-0.08
Provide Appropriate Model		0.14	0.11
Foster Acceptance of Goals		0.06	0.06
High Performance Expectation		0.02	0.03
Individual Support		0.05	0.04
Intellectual Stimulation		0.04	0.02
Transactional Leader Behavior		0.37**	0.36**
Step 3: **Personality Variables**			
Self-Efficacy			-0.14**
Need for Achievement			-0.07
F	4.90**	16.30**	15.07**
R	0.20	0.57	0.59
R (square)	0.04	0.33	0.36
Change in R (Square)	0.04**	0.29**	0.03**
Adjusted R (Square)	0.03	0.31	0.33
Df	3/340	10/333	12/331
SE	22.91	19.38	19.08

**P<.01 *P<.05

Table 3: Hierarchical regression of 3 subscales external justification [A] ego defense [B] and biased belief update[C] on leadership style and personality factors

	A			B			C		
	Model I	**Model II**	**Model III**	**Model I**	**Model II**	**Model III**	**Model I**	**Model II**	**Model III**
Variables	Beta	Beta	Beta	Beta	Beta	Beta	Beta	Beta	Beta
Step 1: **Control Variables**									
Age	-0.01	-0.00	-0.01	-0.10	-0.09	-0.09	- 0.06	-0.06	-0.05
Sex	0.11*	0.92	0.08	0.12*	0.11*	0.10*	0.09	0.08	0.08
Job Tenure	-0.11	0.05	-0.04	0.04	0.10	0.10	-0.05	0.01	0.01
Step 2: **Leadership Style**									
Articulate Vision		-0.10	-0.09		-0.07	-0.07		-0.08	-0.06
Provide Appropriate Model		0.19*	0.15*		0.14	0.12		0.08	0.06
Foster Acceptance of goals		0.01	-0.02		-0.01	0.02		-0.03	0.02
High Performance Expectatio		-0.01	-0.00		0.04	.03			
Individual Support		-0.03	-0.04		0.04	0.03		0.10	0.10
Intellect. Stimulation		0.04	0.01		0.04	0.03		0.08	0.07
								-0.05	-0.07
Transaction Leader Behavior		0.38**	.37**		.31**	.31**			
								0.33**	0.36**
Step 3: **Personality Variables**									
Self-Efficacy			-.14**			-0.05			-0.10*
Need for Achievement			-0.07			-0.03			0.03
F	3.09*	11.65**	10.82**	2.39	8.63**	7.32**	2.31	9.29**	8.09**
R	0.16	0.51	0.53	0.14	0.45	0.46	0.14	0.47	0.48
R (square)	0.03	0.26	0.28	0.02	0.21	0.21	0.02	0.22	0.23
Change in R (Square)	0.03*	0.23**	0.02**	0.02	0.19**	0.00	0.02	0.20**	0.01
Adjusted R (Square)	0.02	0.24	0.26	0.01	0.18	0.18	0.01	0.20	0.20
Df	3/340	10/333	12/331	3/340	10/333	12/331	3/340	10/333	12/331
SE	14.16	12.49	12.33	8.98	8.98	8.17	5.99	5.41	5.40

**P <.01 *P <.05

Chapter 18

HUMAN RESOURCE MANAGEMENT PRACTICES IN A COOPERATIVE ORGANISATION

Chinwe Susan **OKEKE**

INTRODUCTION

Cooperative organisations just like every other organisation, engage in different economic activities. They do this by employing the services of both material and human resources in their capacity. These resources, especially the human factor should be managed well because they are the brain behind the functioning of the material resource. They manipulate the technologies for production purposes. Therefore, they ought to be recognized and motivated in other to retain them in the organisation. The technological changes, global competitiveness and challenges demands that organisations should move towards good human resources management (HRM) practices. Human resources are human beings and by nature are prone to changes. This peculiar characteristic of the human resource requires a follow up to attune their minds in helping to attain organisational goals. It is therefore not an overstatement to say that no organisation can exist without quality human resource to exploit the material resource for surplus, survival, growth and diversification. This paper basically is to investigate on the HRM practices in a cooperative organisation as well as determining its effects on both workers and members. The objective of the study is to investigate into the human resource management practices in Household Utensils Dealers Multipurpose Cooperative Society (HUDMCS). This will help to determine the HRM practices in HUDMCS, and examine the problems and effects of human resource management practices in HUDMCS.

CONCEPTUAL AND THEORETICAL ISSUES

Business organisations are set up with stated goals which people in organisation thrive to attain. These people are usually given different tasks to perform and all work cooperatively together, towards attainment of the desired goals. Onwuchekwa (2002) sees organisation as being economic oriented with the basic objectives of making profits. For organisations to attain their stated goals, they must be managed well. This means that management is very relevant in organisations. Management involves utilizing both human and material resources through planning, organizing, directing, coordinating, controlling and evaluating, to achieve set goals. Ramu (2008) is of the view that human resources have a significant bearing on the profitability, efficiency and overall organisational effectiveness. According to him, human resource is the most important asset of any organisation. They are needed to make the capital and material resources functional. But these human resources are dynamic in nature; they differ from one another in their complex behaviour patterns and psychological make up. Such differences obviously multiplied when they interact with one

another in organisations. This generates different management styles, values, feelings, beliefs and opinions of the employees. For these human resources to be able to take risks, think innovatively and handle new problems, they must be groomed very well.

Human resource management therefore, is inevitable for the success of any organisation. Armstrong (2006) sees human resource management (HRM) as the strategic and coherent approach to the management of an organisation's most valued assets-the people working there who individually and collectively contribute to the achievement of the objectives of the business. He simply puts HRM to mean employing people, developing their resources, utilizing, maintaining and compensating their services in tune with the job and organisational requirement. Hills (2003) states that human resource management entails activities organisations carry out to use its human resource effectively. According to him, when these activities are embarked upon, the character, development, quality and productivity of the organisation's human resource will be enhanced. Also Osuala and Okeke (2006) assert that human resource management (HRM) comprises the managerial activities involved in planning for recruiting, staffing, training and maintaining human resource. Donald et al. (2002) maintain that the effectiveness of every organisation depends, to a great extent, on how well its human resource are utilized which largely depends on management policies and practices. Many modern organisations set good human resource policies that direct their recruitment and selection, training and development, promotion and compensation etc. All these, help to boost the morale of their employees and enable them face the competitive pressure in the business environment. This means then that human resource management is very important in the modern business operations, since it helps employees to face new challenges and global competitiveness. Based on this, employees of any business organisation stand as the key factor deciding the success or failure of the organisation and cooperative organisations are not left out.

Ramu (2008) is of the view that cooperative organisation approach human resource management from the wrong perspective and this usually affects their financial performance. In his words, 'cooperatives, instead of focusing on how to execute strategy through the performance of their employees, make cost control their first priority'. This incidentally affects the functions of the human resource. He stressed further that cooperative organisations have been in existence for many years; yet human resource management has been a neglected field. Hence poor image of the employees in the cooperative organisations affects their morale. In his words, "not much attention is given to this function of human resource management".

Human resource management practices are those things done by the organisations to see that they have quality human capital that can face the changes in today's business environment. It comprises of elements like recruitment, training and development, incentives and allowance or compensation etc. According to Ejiofor (1988), the elements of human resource management are employment, training, development, salary administration, industrial and labour relations while encyclopedia Britannica (1989) lists these elements; organisational management, personnel administration, manpower management and industrial management. Noe Hollenbeck, Gerhart and Wright (2002) identify planning, recruitment, selection, training and development, compensation, performance management and employee relations as the HRM practices in organisations. In line with this, Ramu (2008) highlights that there are four broad HRM practices and they are; acquisition, development, rewarding and maintenance of human resource. Indeed, these practices generally help organisations to attain their objectives.

The importance of human resource in organisations cannot be overemphasized. According to Adeyeye (2009), the effect of good HRM practices include sales growth through training and development, increases in the financial strength of an organisation, operational efficiency through cost reduction in hiring and firing, innovation. and workers commitment that enhances productivity and profitability. Jones and George (2000), points out that HRM practices increase knowledge and skills of workers through training and development. In their words, it will make them effective performers. Ramu (2008) however adds increased productivity, high morale, reduced supervision, organisational stability and flexibility as effects of good HRM practices. Some obstacles are encountered while managing the human resource. According to Ewium and Ubochi (2007), these problems include selection and placement. Through paternity management, the best quality of workers may not be hired or placed in their right position. Lacks of facilities for manpower development - most organisations are economically incapable of establishing training facilities except for some multinationals. Incompetence of the trainees - many at times, trainings are unproductive and ineffective to the organisation. This may be because the particular staff did not grasp anything or trainer lacks basic expertise.

RESEARCH METHODOLOGY

The study was carried out on Household Utensils Dealers Multipurpose Cooperative Society (HUDMCS) located at Ogboefere in Ogbaru Local Government Area of Anambra state, Nigeria. Ogbaru people are traditional fishers, farmers and warriors. Ogbaru people and clan are stretched into three Nigerian states, namely Anambra State, Delta State and Rivers State. Ogbaru Land is neighbored by Onitsha, a major commercial city in South Eastern Nigeria located at Anambra State. This neighbourhood has influenced the commercial activities of the Ogbaru people and has resulted into three big markets namely: electronics market, relief market and Ogboefere market. The cooperative society under study is in Ogboefere market which happens to be a big market in Ogbaru Local Government Area. Three hypotheses were considered for the study as follows: There is no significant difference between the perception of members and workers on the HRM practices in HUDMCS. There is no significant difference between the perception of members and workers on the effects of HRM practices in HUDMCS. There is no significant difference between the perception of members and workers on the problems affecting HRM practices in HUDMCS.

The population of the study consisted of the entire workers and members of the HUDMCS. The members are 1800 from which 328 participants were selected. The researcher used a systematic random sampling technique where every 6th element or person from the register was chosen as a respondent. This resulted in having 293 members and 35 workers for the study. The research instrument used for the study was questionnaire. The researcher structured and administered thirty five item questionnaires which were divided into four (4) sections. Section A, dealt with socio-economic profile of the respondents. Section B, was on human resource management (HRM) practices while sections C and D, dealt with the effects and problems of HRM practices respectively. In section A of the questionnaire, information solicited from the respondents included age, gender, educational qualifications, marital status, work/business experience, work/business status and income. Sections B to D followed the likert type comprising four (4) response ratings of strongly agree (4), agree (3), disagree (2) and strongly disagree (1). The respondents were requested to indicate their level of agreement or disagreement with each of the items in sections B to D. A theoretical mean value of 2.5 was taken as a criterion to judge the means for items in the respective selections. Any item in

the instrument which has a mean equal to or higher than 2.5 was regarded as agree while items with less than 2.5 was regarded as disagree. All 328 copies of the administered questionnaires were properly filled and returned since the researcher personally administered and waited to collect after they were filled by the respondents. The instruments used for analyzing responses from the respondents were descriptive statistics like frequency distribution table, percentage, mean and standard deviation. For the hypotheses posed, t-test or t-statistics was used to draw if there was any significant difference between the perception of the workers and the members based on HRM practices, effects and problems. All calculations and estimates were obtained through the use of version 17 of the statistical package of social science package.

DATA PRESENTATION

Table 1: Human Resource Management practices in HUDMCS

S/N	HRM Practices	N	Mean	Standard Deviation	Decision
1.	Staff are employed by direct recruitment	328	3.2741	0.59135	Agree
2.	Staff are employed by taking persons on deputation from other government ministries or agencies	328	3.4593	0.50019	Agree
3.	Staff welfare is given utmost priority	328	3.7926	0.42490	Agree
4.	Promotions are given regularly to deserving staff	328	3.2222	0.43480	Agree
5.	A well written down policy on HRM practice	328	1.7185	0.58145	Disagree
6.	Staff are provided with appropriate and adequate facilities/tools/ equipment	328	3.2889	0.63324	Agree
7.	On the job training/workshops are regularly provided	328	2.7259	0.52447	Agree
8.	Staff are paid living wages/salaries, allowances and other incentives	328	38074	0.39580	Agree
9.	Staff and members are given health care support as need arises	328	3.2370	0.50678	Agree
10.	Staff and management have cordial relationships	328	2.9181	0.36756	Agree

Source: Field survey, 2011

Table one above revealed the mean scores and standard deviations for all items on the Human Resource Management Practices. The study showed that in Household Utensils Dealers Multipurpose Cooperative Society, HRM practices is not a new thing because they are quite aware of the importance of human factor. They virtually agreed to all the items except that of item five (5) where they disagreed that there is a well written down policy on HRM practice.

Table 2: Effects of human resource management practices in achieving maximum productivity

S/N	Effects of HRM Practices	N	Mean	Standard Deviation	Decision
1.	Increased service delivery and productivity of staff	328	3.252	0.529	Agree
2.	Increase effectiveness and efficiency of staff	328	1.719	0.581	Disagree
3.	Prepared staff in expectation of higher responsibilities/jobs	328	3.289	0.633	Agree
4.	Boosted staff morale and increase job satisfaction	328	2.726	0.524	Agree
5.	Increased capacity to adopt new technologies and methods	328	3.807	0.396	Agree
6.	Reduce employee turnover and enhanced cooperative's image	328	3.238	0.507	Agree
7.	Reduced waste, accident, lateness and absenteeism of staff	328	2.919	0.368	Agree
8.	Reduced staff misunderstanding of management's policies and intentions	328	3.030	0.546	Agree
9.	Increased staff skill, knowledge and techniques of handlings a job	328	3.259	0.610	Agree

Source: Field survey, 2011.

The mean scores from table 2 above showed that HRM practice has many positive effects. This reflected on the mean scores which showed that both members and workers agreed to almost all the items as effects of HRM practices. However, they disagreed on the second items that HRM practices increased effectiveness and efficiency of staff. This signifies that there are other variables that can lead to effectiveness and efficiency and not just HRM practices.

Table 3. Problems of Human Resources Management (HRM) practices in Household

S/N	HRM Practices	N	Mean	Standard Deviation	Decision
1.	Low level of formal education	328	3.333	0.529	Agree
2.	Poor cooperative education	328	3.459	0.500	Agree
3.	High levy imposed by the government as subvention	328	3.793	0.424	Agree
4.	Impracticability of training programs by cooperatives	328	3.237	0.443	Agree
5.	Poor salary structure which has influenced choice of staff	328	1.740	0.572	Disagree
6.	No written policy on HRM practices in cooperative organisations	328	3.303	0.626	Agree
7.	The mode of recruitment	328	2.733	0.521	Agree

Source: Field Survey, 2011

The mean scores above reveal that the respondent agreed to all the items as problems of HRM practice in the cooperative organisation. However, they disagreed that item five (5) is a

problem. This signifies that HUDMCS feel their salary structure is not poor compared to what is paid as minimum wage to workers in the state government.

Test of hypotheses

Table 4. Test of Equality of variance

Equal variance Assumed	Mean	Std deviation	T	Df	Sig (2 tailed)
1	3.148	0.156			
2	3.134	0.126	0.469	326	0.640

1 = members (N = 293) 2 = workers (N = 35)

The t statistics of 0.469 as shown in table 4 above was not significant at the conventional 5% level. Therefore we fail to reject the null hypothesis that there is no significant difference between the perception of members and workers on the HRM practices in HUDMCS. We therefore conclude that there is no significant difference between the perception of members and workers on the HRM practices in HUDMCS.

Table 5: Test of Equality of Variance

Equal variance Assumed	Mean	Std deviation	T	Df	Sig (2 tailed)
1	3.020	0.202			
2	3.044	0.202	0.615	326	0.540

1 = members (N = 293) 2 = workers (N = 35)

From the table above, the t-statistics was 0.615 and this is not significant at the normal level of 5%. Therefore, we fail to reject the null hypothesis. Thus, we conclude that there is no significant difference between the perception of the members and workers on the effects of HRM practices in Household Utensils Dealers Multipurpose Cooperative Society.

Table 6. Test of Equality of Variance

Equal variance Assumed	Mean	Std deviation	T	Df	Sig (2 tailed)
1	2.686	0.178		326	
2	2.722	0.162	-1.073	326	0.285

1 = members (N = 293) 2 = workers (N = 35)

Test Result: The t-statistics -1.073 as shown in table 6 above was not significant at the conventional 5% level. Therefore, we fail to reject the null hypothesis and therefore conclude that there is no significant difference in the perception of members and workers on the problems of HRM practices in HUDMCS.

DISCUSSION OF FINDINGS

The study revealed that HUDMCS has good practice of human resource management. This seems to be in line with Hollenbeck, Gerhart and Wright (2002) where they identified the human resource management practices in organisation as planning, recruiting, selection, training and development, compensation, performance and employee relations. Also Osuala and Okeke (2006) assert that human resource management comprises

the managerial activities involved in planning for recruiting, staffing, training and maintaining human resource. The study also revealed that HRM practices have positive effects such as, having helped to prepare staff in expectation for higher responsibilities or jobs, increased capacity to adopt new technologies and methods, reduced employee turnover and enhanced cooperatives image etc. These findings seem to agree with Ramu (2006) where he maintained that organisations train and develop employees to achieve increased productivity, high morale, reduced supervision, organisational stability and flexibility. However, findings showed that HRM practices have not increased effectiveness and efficiency of staff. This disagrees with what Adeyeye (2009) found, that HRM practices leads to operational efficiency. On the issue of the problems affecting HRM practices, finding revealed that cooperative organisation studied does not have written down policy guiding HRM practices. This was pointed out by Ramu (2008) where he said that a set of written policies enhances employees understanding of cooperative rules and expectation.

CONCLUSSION AND RECOMMENDATIONS

It is obvious that the Household Utensils Dealers Multipurpose Cooperative Society have good human resource management practices. The study was able to show that when there is good management of human resources, many positive changes will be felt in the cooperative organisation. However, HUDMCS are faced with some problems which have limited the HRM practices such as low level of formal education, no written policy on human resource management practices and the mode of recruitment. Based on the findings and conclusions, the researcher recommends the following. Though, the cooperative organisation studied has good HRM practices, there is no written down policy on HRM practice. Therefore cooperative organisations generally as a matter of urgency should have a well written down policy that will cover human resource management practice. There is need for regular promotion and recognition of members and workers who perform very well. This will help boost their morale and enthusiasm at work. Regular seminar should be organized for both members and workers in order to increase their cooperative knowledge. Every member or worker should be given opportunity for training. Trainees on the other hand should implement what they learnt.

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Chapter 19

CORPORATE GOVERNANCE ROLE IN FAMILY AND COOPERATIVE BUSINESS

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INTRODUCTION

Corporate governance is the broad range of policies and practices that enables a business- be it small or big, family or cooperative- to actualize its objectives. It refers to how an organisation (family or cooperative) is governed. Its relevance in family or cooperative business where culture and other informal approach to issue seem to be dominant. Sentiments are expected to be phased out when crucial decisions are to be taken. Family and cooperative businesses start simple and graduate into enterprises which are essential for economic growth and development by making use of both human and other resources. Hence, the expected focus on the need to align this group of business with corporate governance. The developing economy requires sustainability. Family businesses and cooperative societies are essential for economic growth and development which tend toward new start-ups and growth of existing small and medium enterprises. A family business is one that is owner-managed. The objectives of setting up and managing the business are the personal objectives of the owner and need to be checkmated by guidelines. This is intriguing because most businesses in Nigeria are family businesses, set up to meet the wishes of the owner (Ihekwoba, 2007). Cooperative action occurs when many individuals of same lineage mostly extended family pool their meager resources in an effort to obtain what is needed by all. This is an example of small business not requiring large sum of money to start it up. This is why this article is of prominence because with the level of resources development most families and cooperators will require effective financial and management acumen to survive the modern day competition to survive.

The purpose of this paper is to discuss corporate governance in a family and cooperative business and place them in their proper perspective. Over the years, family and cooperative business were based on cultural norms and family affiliations. The essence of this paper is to emphasise the need for them to develop acceptable policies, procedures and process base on corporate governance principles as guide to owners and managers of businesses. This study is based on the use of secondary data, basically from research work on family business, cooperatives society and microfinance initiatives. Family business, cooperatives society and microfinance initiatives are abound in most countries including developing nations including Nigeria but not much focus is given to corporate governance- a growing area of management research especially in the above named area. This study would be useful to the managers of these category of businesses that it cannot be business as usual- that there has to an adherence to policy, rules and regulations to direct affairs. The study focuses on the operations of family

business, cooperatives society and microfinance initiatives stating different authorities and comparing views as per their researches.

CONCEPTUAL AND THEORITICAL FRAMEWORK

The review of literature seeks to provide an understanding of the conceptual and theoretical framework of corporate governance role in family and cooperative business. As a secondary dependence research the following sub-headings are followed: Corporate governance, Family business, and Relevance of cooperative and microfinance

Corporate Governance

Corporate governance has been a growing area of management research especially among large and listed firm. However, less attention has been paid in the area with respect to small and medium enterprises (Adeniyi, 2011 quoted Akor et al. 2011). That is why this work is of importance because it is considering a less focused area- family and cooperative business in terms of development financing. According to Amole (2005), corporate governance is the system by which business corporations are directed and controlled. The phenomenon specifies the distribution of rights and responsibilities among different participants in corporation such as the board of directors, managers, shareholders and other stake holders and spell out the rules and procedures for making decision on corporate affairs. This provides the structure through which the business objectives are set and the means of altering these objectives and monitoring performance. Agbaeze (2011) defined the field of corporate governance as the study of the processes by which the resources suppliers-reduced to the only financial investors-guarantee the profitability of their investment. Also Magdi and Nadereh (2002) stated that corporate governance is about ensuring that business is run well and investors receive a fair return 'build on due processes. These are done through structures in the form of policies and implementation.

Pandey (2005) puts it that corporate governance implies that the company (business organisation) would manage its affairs with diligence, transparency, responsibility, accountability and would maximize shareholders wealth. According to him, good corporate governance requires firms to adopt practices and policies which compromise performance accountability, efficient management control by board of directors and constitution to include the board committee as part of internal controls mechanism. According to Chrisman et al. (2008), corporate governance refers to the way that boards oversee the running of an entity by its managers and how the members of the board are held accountable to the share holders and the business. This concept is a strong barometer ensuring the different types of family businesses and the manner in which strategy is formulated and implemented. It is concerned with holding the balance between economic social goals and between individual and communal goals. The corporate governance framework is there to encourage the efficient use of resources, regulate accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and (cooperative) societies.

Corporate Governance Forum of Japan (1997) explained that corporate governance rests with the conduct of the board of directors chosen on behalf of the shareholders US Business Round Table White Paper on Corporate governance (1997) agreed that "corporate governance is not

an abstract goal, but exists to serve corporate purpose by providing a structure within which stockholders, directors and management can pursue most effectively the objectives of the corporation." This exposition includes family and non family business because they were all established with the aim of achieving goals and objectives. This is as a result of congregational hearing in the United State. This was set up by the Harvard Business Review- A working group on corporate governance in 1990. "Institutional shareholders (including family /cooperative members) were recommended to see themselves as owners, not just investors in a company, but should refrain from getting involved in the company's day-to-day activities. Shareholders also evaluate the performance of directors regularly. They need to be properly informed about the company's activities in order to carry out this evaluation"

Chrisman et al. (2008) corroborated that "collectively the articles explore and elucidate some of the most common variables associated with strategic performance: response to a changing environment, industry dynamics, governance, firm level characteristics, behavior and of course, economic performance". Amole (2005) went on to classify that a good corporate governance entails the realization of organisational goals and objectives which are usually targeted at huge profits accuracy from small input of different scarce resources. It is the responsibility of management to ensure these scarce resources are synergistically projected to achieve organisational goals and objectives. In the corporate domains today, be it family or cooperative, where the stakes are comparatively high in virtual competition, the same vales constituting a culture bond have come to force to propel organisation to profit. Oyejide and Soyibo (2001) buttressed that "corporate governance as a concept, can be viewed from at least two perspectives: a narrow one in which it is reviewed merely as being concerned with the structures within which a corporate entity or enterprise receives its basic orientation and direction" and "a broad perspective in which it is regarded as being the heart of both a market economy and a domestic society".

Olakesusi, (2000) stated that "governance is the set of values, policies and institutions by which a society manages economic, political and social processes at all levels through interaction among the government, civil society and private sector". It is the way of achieving mutual understanding, agreement and action. It comprises the mechanism and processes through which …groups articulate their interests, mediate their differences and exercise their legal rights and obligations. It is, in other words, the framework of rules, institutions and practices that sets limits and provides incentives for individuals, organisations and businesses. Good corporate governance is the glue that holds together responsible business practices, which ensure positive workplace management, marketplace responsibility, environmental stewardship, community engagement and sustained financial performance. It instills in companies the essential vision, processes and structures to make decisions that ensure longer-term sustainability.

More than before, we need companies that can be profitable as well as achieving environmental, social and economic value for society. It is now beyond the conventional role of approaching work through other people to the one with strong visionary leaders who manage by inspiring strong norms and values into management and staff at all levels. The above authorities stress the need for businesses to establish strategies through rules and regulations for the owners and managers to be guided in dealings of the business. It also emphasizes "the transaction at the heart of corporate governance is an investment in a corporation that is simultaneously met not with payment but with a promise of future returns". We so far identify the basic function of corporate governance as an engine room of

investment (business) helps to clarify thinking (projections). It helps to allocate risks by providing information and manage problems correctly. This is at the heart of analyses of governance system because asymmetries in information discourage investment by increasing the probability of adverse selection and moral hazard. Corporate governance institutions determine the extent and timeliness of information disclosure as well as the incentives to engage in monitoring (Dyck, 2000).

These are the advantages of having well drawn corporate governance. It guides by showing the way to prosperity and pitfalls. This will keep the owners of the business on guide as they enquire of the business state of affairs. Where the regulations are kept in managing the excesses of the family members will be kept on check. Dyck (2000) further emphasized that the adoption of various economic reforms programmes in Africa in the last two decades in which privatization of government-owned enterprises form main focus thus heightening the corporate governance concern and need in the continent. When remembering the bitter experience of massive governance in some Eastern Europe countries like Russia and Czech Republics that rushed into large-scale privatization without the necessary corporate governance “infra-structure”, suggest that Africa needs to take stock of it corporate governance capacity. Oluwagbam (2002) also corroborated that corporate governance system covers all the mechanisms that govern the managers’ behavior and delineates their discretionary latitude. Ahunwan (2002) noted that as it affects the macro level of Nigerian economy so does it apply to the micro level (family business?) with vertical and horizontal implications of corporate governance being the arbiter of decision making especially in modern age of relying on policy and procedure.

In the narrow view of corporate governance in the area of shareholders protection, management control and agent of economic theory should include the proponent of wider perspective uses like the resultant effects of keeping family firms in check. Good Corporate governance ensures business ethics. This is the base for morals and propels the business toward optimal level of achieving the set goals and objectives. This is a pointer to the caliber of professionals be involved in the management of any family business. With some outstanding family business graduating to big organisations, efforts are put in place appropriate corporate governance policy which will enable the business to sustain its growth and development positively. This being the case, proper employment opportunity is created, material is sourced, and funds is properly managed and utilized with guided principles, socio-economic problems which include peculiar welfare approach like the corporate social responsibilities which takes many forms to affect the immediate community. Memorandum of Association is the constitution of a corporate body to enable it fulfills its economic and social functions within its set objectives and business environments. The fundamental framework in the business is to operate as set out in the memorandum clauses, which include the name of the business, the registered office address, the object clause of the business, the liability clause, the shareholders and the list of subscribers or members.

In Nigeria, the articles of association of the business that amplifies the memorandum by enumerating the internal management rules of the business. It expresses the voting, meetings, powers of directors, use of company seal, proceeding of directors and the winding up, among other things (Companies and Allied Matters Act (CAMA), 1990). This enhances control in the business organisation as a going concern and Oluwagbam (2002) defined control as the capacity to choose directors. As a colliery, it carries capacity to influence the board of directors and possibly to dominate it.

Family Business

Cater and Schwab (2008) stated that family firms share many aspects common to all firms, but the embeddedness of business relationships in family relationships creates some unique organisational characteristics. The management literature has generally recognized these characteristics but has only started to explore their implications. According to him, in our study, we investigated how the unique characteristics of established small family firms affect their ability to implement turnaround strategies when facing an organisation crisis. This category of business has gradually to the limelight and has contributed to sustainable economic development of most of the nations. It is a stool on which cooperative society seat to develop into colossus. Family business has been a 'burning issue'. Chrisman et al. (2008) stated that "during the last decade, family business academics have established models of family business that integrate different mainstream theories and allow for an analysis of the distinctions between family and non-family firms as well as among family firms of different types". The basis of family business is trust from another angle as Sundaramurthy (2008) viewed trust as fundamental for the competiveness of social organisations given the increased levels of complexity and uncertainty. He referred trust to mean a person's belief that individuals engaged in exchanges will make sincere efforts to uphold their commitments and will not take advantage of the given opportunity; in other words, it is ones willingness to rely on others. He believes that within family firms this component is even more significant because family businesses have ready access to resources such as the social capital and stewardship behaviors that stem from common ancestry and showed family identity.

As expressed by Pieper and Klein (2007), the family business field is not only advancing rapidly but is also constantly gaining relevance within and beyond the business research field. As in any unknown and fast- changing area, navigating without a roadmap, results in losing your way. A guiding framework (in form of corporate governance) can help to effectively and efficiently reach the final destination. In the family business field, many useful and important models have been developed to structure and explain the complex intersection of the family and the business. However, a holistic model able to illustrate the interrelations between family business components at various levels of analysis is lacking. Such a family business research roadmap may contribute to advancing the family business field by enhancing the structure and design of theory- building research questions.

Family businesses are essential for economic growth and development which tend toward new startups and growth of existing family firms. There seem to be little doubt, world, family businesses are critical in spurring economic development and growth by creating and funding new businesses as well as growing existing firms Kellermanns, Eddleston, Barnett and Pearson (2008). Family business enjoy both formal and cultural wave of work, with emphasizes on the former explicitly nowadays. It is very essential to appreciate the cultural linage of the family regarding the family business but not at the expense of formal structure in place for the running of the business. This is the focus of corporate governance for the days of the rule of thumb in the form of family link are maintained. Previously, in family business, the family was the 'be all and end all' but with the CAMA (1990), the Corporate Affairs Commission if notified will inquire the registration status and midwife the corporate stand of the family business and also advise as appropriate to ensure industrial peace.

According to Okike (2007), it is generally believed that poor corporate governance has been the Achilles' heel of many corporations in both rich and poor nations. This is particularly true

of Nigeria. Family businesses are essential for economic growth and development through initiatives of different families. His is entrepreneurship in action and it is pertinent at this point to ensure cultural respect with respect for led down laws for processes and procedures. The growing importance of corporate governance in organisations owes much to the impressive study of changing structure of companies performed through adequate implementation. Kellermanns et al. (2008) stated that the family firm is a business governed and/or managed with the intention to shape and pursue the vision of the business held by a dominant coalition controlled by members of the same family or a small number of families in a manner that is potentially sustainable across generations of the family or families.

In another sphere, the family business was defined by Chrisman et al. (2005) as a business governed or managed with the intention to shape and pursue the vision of the business held by a dominant coalition controlled by members of the family or a small number of families in a manner that is potentially sustainable across generations of the family or families. Family business field developed and advanced from the crude stage of non-formal agreement in the developing countries. Hence, constant relevance issues are carried out within and beyond the business research field to give necessary correction and direction in the area of management. Guided framework like the memorandum of association and articles of association can help effectively and efficiently to reach the stated objective of the business. Attitude of family business members made it expedient to place these rules and regulations to control their behavior towards the management, financial control etc. This is so because of the alarming rate of failure in the in the family enterprise (business). The euphoria of establishing family business is always jettisoned because of the moribund situation of a supposed to be viable initiative. This is attributable to family interference which leads to ‘putting square peg in round holes’ – the bane of family business. This connotes personal aggrandizement at the end of the day. It could be on grounds of settling family imbalance. Human capital is always the issue. Family inclinations influence the staffing disposition of the business from the board composition to the least on the payroll of the organisation. Appointments to represent certain family interest are made without considering the know-how of the person so appointed. This appointee may now become the cog in the wheel of progress of the family business and this may lead to malfunctioning of the outfit like abuse of office and misappropriation of fund etc.

With corporate governance in the mainstream of affairs of the family business, the staff will be guided. If he acts ultra vice will not be part of the management team. The board will be worse off if that character is tolerated to run the business. The early years of family business in Nigeria witnessed a lot of prangs which led to misconduct within the limbs and bounds of the nation. The family business environment then witnessed little or no focus because every member of the family contributed to the management whether it was relevant or not. Employees and managers especially if not linked to the family play second fiddle no matter their intellectual level. From the above empirical works family business researchers continue to seek ways to describe how family firms are differentiated from other organisational forms. In search for ways in which the family firm context is unique to organisational science, the construct of “familiness” has been identified and defined as resources and capabilities that are unique to the family’s involvement and interactions in the business (Person, Carr and Shaw, 2008). This research also tends to ‘anchor’ that the management of a family business needs to be protected. Before this research, they always fall prey to the ‘hire and fire’ syndrome characterized by the leadership of the family. It is a common scene for the family/cooperative heads to find faults in the management style of CEO, which may tapper into sack threat. The behavioral pattern will not arise if there is guided principle in place, with corporate

governance to ensure due process for a registered family/cooperative business. The degree of family influence in the firms, as indicated by the number of generations involved in the business (Kellermanns et al., 2008).

For every business, be it family or cooperative lacking transparent control can collapse quickly as the owner's confidence collapses. There is also the need for mutual cooperation between the management and family members of the firm in developing the need capacity to ensure effective corporate governance with a focus to ensure the achievement of the family firm's objectives. This is the basis of collaboration and partnering with the family members for the firm to be a going concern and transcending many generations like the ford family business still going strong.

RELEVANCE OF COOPERATIVE AND MICROFINANCE

As a link, there is relationship between cooperative business and family business. With the characteristics of the later which are based on trust, family affiliation, and ancestral links could readily become the base for the former. As explained by Ihekwoaba (2007) that cooperative society is one of the early forms of business organisations in Nigeria. From ancient times, family members, societies and guilds have been known to cooperate in production, marketing or supply goods and services. According to him cooperative society is an association of group of people who agree to pool their resources together, for the benefit of their members and in order to make profit. There are different types of cooperatives: namely: Producers Cooperative Society, Consumers Cooperative Society, Farmers Cooperative Society, Thrift and Savings Cooperative Society, and Fishermen's Cooperative Society.

The basic feature of cooperative societies is that membership is voluntary. There is free entry and exit from the society. It serves as a training ground for individual members in small business management. Of all the types of cooperative society listed above the thrift and savings emphasizes financing and credit arrangement for its members and the immediate community. Today, the government has established Nigerian Agricultural Rural and Cooperative Bank with the objective of helping cooperators among other things. The microfinance banking institution has also been introduced to add-value to the financing needs of family and cooperative society business. The economic importance of cooperative society is pronounced in the rural areas based on family and ethnic ties because of the extended family system in Nigeria.

What started in simple modality is now wearing a global look in the form of International Cooperative Alliance (ICA) (Ebunu, 2006). This phenomenon called cooperative society is even practiced in rural communities in Europe, Manchester, Ireland etc. where its management has reached an evitable point. The purchasing power of the rural people affects the community development. Social life almost not available, the educational outburst is poor but with local community rallying to form cooperatives, will ginger members into empowerment and entrepreneurship. This will add value to their income and other volunteer workers of the cooperative will follow suit because they will be remunerated at one point or the other. Thrift and loan will be introduced to bring pep and succor to the members. This is the principle of cooperative movement cooperation. Accordingly, Okoli and Abianga (2009) stated that in cooperative development, cooperatives have significant employment potentials which should be encouraged in all the project areas. Labour intensive types of cooperatives

like labour contracting cooperative networks in the informal sector like agriculture need to be exploited although it has been tested and proved successful in other parts of the world.

According to Ayano (2010), looking forward into the new millennium, the quest for cooperatives selling farm supplies will be as it has always been; faster, better and cheaper. This is because cooperative is a team and the more hands (members) the better in stock piling, purchasing and selling through the society. They enjoy synergy by supplying to members at lower profit margin and to non-members at higher profit margin. Many farm supply cooperative will continue to operate with this philosophy. Some will look to technology and improved market to prosper since cooperatives are owned by their users who are members, so, the desires of the farmer owners are reflected. Understanding membership's business and their expectations for cooperative is essential to its survival. As there is need for emphasis on rural development cooperatives will be sustained to provide a more changing role. The cooperative will provide extensive scouting services and problem solving in term of human capital, financial, social and economic terms. To add value to development finance stride of cooperative society especially the thrift and savings type, microfinance are established to assist family and cooperative business. This is new remedy in place to tackle poverty-The microfinance initiative. The aim of this microfinance initiative is to support micro-enterprise development. Small business or small scale enterprises are supported through training, giving of small loans and creating jobs to fight poverty. With this the individual entrepreneurs are helped to economically independent and to be able to sustain the families of their employees. Okorie (2011) defines microfinance as financial services for the poor and low income clients. Otiti (2007) outlined the roles of microfinance service as to: Provide efficient and effective financial services such as credit deposits, commodity/inventory collateralization, leasing and innovative transfer/payment services. Undertake appropriate recruitment and retention of qualified professionals through transparent and competitive processes. Adopt continuous training and capacity building programmes to improve the skills of staff; and strictly observe their fiduciary responsibility and remain transparent and accountable in protecting savers deposit.

Microfinance and Small scale enterprises in Nigeria indicates that war against poverty as discussed by the roles of government during launching of microfinance policy, regulatory and supervisory framework for Nigeria, Dr Ngozi Okonjo Iweala, the then Minister of Finance in Nigeria has this to say; Over the years, successive governments in Nigeria have made several attempts to address the issue of access to finance by poor Nigerians for micro and small scale economic activities (CBN 2005). In recent years, international economic pressures have induced the country (Nigeria) to adopt a programme of economic liberalization and deregulation. Advocates of reforms tout their potential not only for generating greater economic growth, but also for contributing the more responsible corporate governance. There is no saying that the activities of microfinance banking institutions reflect their unique role as the engine of growth in any economy (Bello, 2011). They remain crucial to the growth and development of entrepreneurs-(cooperatives and family members) and their operations provide solid backing viable and profitable ventures.

CONCLUSION AND RECOMMENDATIONS

This paper has viewed the importance of corporate governance in business firms including family business and cooperative societies. Corporate governance is established as the system by which business organisation are directed and controlled.

Family business has gradually come to the limelight and has contributed to sustainable economic development of most of the nations. It is the basis on which cooperative society seat on to develop. The thrift and savings cooperative help in loan and credit. Microfinance initiative has been recognized and supported by government with the necessary framework to formalizing them. All these finance windows are of great importance for sustainable economic development of any nation. From the forgone, the following recommendations are proffered for corporate governance role in family and cooperative business: That corporate governance should be encouraged to be part of any business-family, cooperative and microfinance; Family businesses need to be promoted to continue to add value to the entire economy as they adhere to corporate governance principles in the effort of contributing to entrepreneurial stride; Cooperative society should inculcate corporate governance as a cradle of business as the support sustainable economic development of the nation; Microfinance initiative should be encouraged as the government has provided enabling corporate governance. With the initiative, the barriers of conventional banks are broken, giving the window out for micro-venture (family and cooperative) to liaise effectively.

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Cooperative Finance in Developing Economies contains papers from notable members of the academia from **four continents** - Africa, Asia, Europe and North America. Specifically, **twenty nine authors** from **nine countries** namely Canada, France, Germany, Italy, Nigeria, Senegal, Spain, United Kingdom and Vietnam contributed to this work.

The book covers both the theoretical and empirical research in different areas of Cooperative and Microfinance arrangement which include but not limited to the following: Capital formation and loan administration, Corporate governance, Country comparison and analysis, Financial intermediation and social capital, Financial sustainability, Impact assessment and evaluation, Integration into formal financial system, Management and members – relationship and conflict, Micro and small scale enterprise development, Poverty reduction and economic development, Products and services delivery models, Regulation, policy and control, Risk management and insurance, as well as Women empowerment and gender issues.

This book makes significant contributions to current research in cooperative finance. It is also an attempt to celebrate year 2012 as the International Year of the Cooperatives as declared by the United Nations.