



Microfinance in marginal and upland areas

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In the aftermath to Asian Financial Crisis, donors like IFAD are taking a fresh look at the relevance and potential of microfinance for the sustainable development of marginal and upland areas in Asian countries. Three major points will be presented below, after having defined what is meant by microfinance:

Microfinance comprises microsavings, microcredit and other financial services such as microinsurance and microleasing. Small amounts of savings are collected: daily, weekly, at market days, after harvests or irregularly. They are then transformed into microloans which are repaid in microinstalments: this is microcredit. I call any institution that provides such microfinancial services a microfinance institution. This includes financial self-help groups, savings and credit cooperatives, rural banks, branches of Agricultural Development Banks and some commercial banks, furthermore moneylenders, deposit collectors, credit NGOs and rotating savings and credit associations. A small number of them is donor-supported. Sustainable rural financial institutions are a prerequisite of sustainable rural development in any country and any region.

1. Impact of the Asian financial crisis

The Asian financial crisis has brought out the strengths and weaknesses of the Asian miracle and of the financial sector in particular. In Indonesia, the hardest-hit country, deregulation which started in 1983 had produced a diversified financial sector. The crisis has affected the sector in different ways:

- (a) The banking sector was almost obliterated. Deregulation had brought it up; political interference and lack of supervision had brought it down.
- (b) The crisis brought out the strength and resilience of rural and microfinance:
 - ✓ In the 3600 units of Bank Rakyat Indonesia (BRI), a government-owned agricultural development bank, 1.3 million new savings accounts were opened in the units at village and sub-district level during a single three-month period immediately after the peak of the crisis, June to August, 1998. With the demand for credit stagnating, the BRI units generated more than one billion dollars in excess liquidity. The BRI Mi-

crobanking Division, with 20 million savers and 2.5 million borrowers, has made BRI the only profit-making government-owned bank.

- ✓ There are over 2200 rural banks, which have emerged since October 1988 when a new law permitted the establishment of rural banks with an equity capital of what was then \$25,000. Several hundred of them have come under distress, particularly around Jakarta; but the sector as a whole has survived
- ✓ There are also some 10,000 semiformal financial institutions, which are to be upgraded to rural banks.

2. Pre-crisis spillover of growth to marginal and upland areas

To a limited extent, economic growth has spilled over to some marginal and upland areas, as it has enabled governments to finance special rural and microfinance programs:

- ✓ P4K is a microfinance project for the very poor in marginal areas in Indonesia. With assistance from IFAD, 50,000 small farmer groups have been formed by field extension workers of the Ministry of Agriculture. At their own initiative, these groups have organized intergroup associations which collect microsavings and transform them into microloans. They are now being upgraded to cooperatives and perhaps rural banks.
- ✓ *Linking banks and self-help groups* has been spreading in many Asian countries and to marginal areas. In India, Indonesia, Thailand and the Philippines, more than 60,000 self-help groups, close to 2000 banks and bank branches, and numerous NGOs as facilitators have been involved.
- ✓ In Nepal, IFAD has helped the Agricultural Development Bank to establish the Small Farmers Development Project, channeling credit through some 25,000 small farmer groups in marginal and upland areas. These are now being transformed into autonomous local financial institutions (SFCLs) owned and managed by the farmers.
- ✓ IDT is a special program in Indonesia of which Prof. Mubyarto, the moderator of our panel discussion, is one of the architects. 27,000 poor villages have received the resources for establishing financial self-help groups and, with World Bank assistance, for rural infrastructure projects.

3. The neglect of marginal and upland areas

While economic growth has trickled down in some countries, it has mostly failed to produce sustainable institutions and sustainable development in marginal and upland areas. The examples given above have remained exceptions, albeit important ones as they are proof of the potential for financial innovations in those areas.

In most countries, marginal and upland areas have been largely neglected. Little effort, if any, has been made to build sustainable institutions. As a result of the crisis, poverty has been aggravated, with severe effects in some areas.

4. Conclusions

Marginal areas need sustainable local financial institutions. This requires a major effort of support. Assistance to build a physical infrastructure needs to be complemented by assistance

to build a lasting institutional infrastructure, including a financial infrastructure. Experience shows that without a sustainable institutional infrastructure which mobilizes the local self-help potential, the physical infrastructure will not be maintained.

Building an institutional infrastructure does not have to start from scratch. The poor in marginal areas possess a capacity for self-help; and they possess their own community-based self-help organizations. Without those, they would not have survived. In virtually all tribal and marginal areas, we can build on the existing institutional knowledge, which is cast in financial self-help groups such as the arisan in Indonesia, the paluwagan in the Philippines, the hui in China and Vietnam – to name but a few. Self-help and self-reliance are their basic principles. They mobilize their own resources, cover their costs, and have adjusted to changing circumstances. Yet, barred by public neglect from upgrading into higher-level financial institutions and integrating into wider financial markets, most have remained small and isolated. These institutions, together with innovative approaches to rural and microfinance by NGOs and government agencies, can provide a basis for the systematic development of a sustainable financial infrastructure in marginal and upland areas.

A multitude of different approaches to the development of rural and microfinance should be promoted, adjusted in each case to local culture and socio-economic conditions. There is no single best way that could be mechanically replicated. The initiatives of the local people should be strengthened; the local knowledge embedded in local traditions should be utilized; financial innovations should be disseminated; linkages to national support structures should be promoted.

With international assistance and IFAD's involvement, the Asian financial crisis might spark off the development of sustainable local financial institutions in marginal and upland areas – just as the hunger year of 1846/47, some 150 years ago, had sparked off a world-wide movement of savings and credit cooperatives which have been of vital importance to sustainable rural development in many of the now developed countries.