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Accessing Financial Services in Rural Areas

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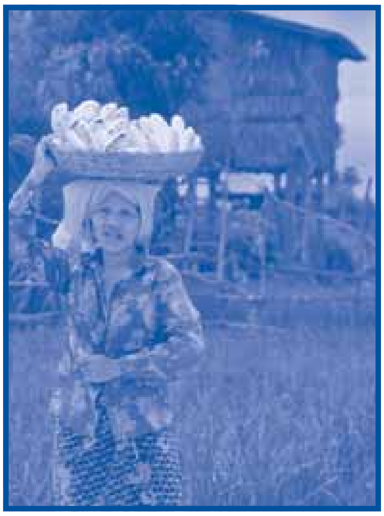

Woman leaving her house (in the background) to go to the market, about a five-minute walk. The market is simple, a set of stalls along the main road where everything seems to sell 2 for 1 US$ – all sells for US currency in rural Cambodia. (Photo: Jeremy Andrulis, 2005, Siem Reap (Cambodia), "CGAP Microfinance Photography Contest").

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Irina Illiescu and her family live in the rural district of Edine in the Republic of Moldova. Irina grows some crops and fruits that she sells on the local market. The income she generates is not enough to support the family, so Irina's husband spends most of the year working on construction sites in Russia. Despite this additional income, the family remains vulnerable to risks such as fluctuations in the prices of grapes and apples, weather-induced low harvests, or the changing demand for construction workers and increasing costs of living in Russia.
Recently a bank installed a mobile office in the region – a small minibus that visits the local market once a week. Irina seized the opportunity to open a savings account, where she now deposits the family's small income after the harvest. In addition, her husband can now directly transfer his remittances to the savings account through a bank in Russia. Unexpected family expenses such as doctor's bills can now be covered from these savings. Irina is also considering the possibility of taking a small loan to purchase a cow and generate additional income by selling the milk.

This example has been witnessed by the author of the present issue of InfoResources Focus.

Overview of financial services for rural areas:

Financial Services for the Rural Poor
www.cgap.org/gm/document-1.9.2394/DonorBrief_15.pdf
(See ref. CGAP, p. 13)

Formal and informal financial services

Rural finance is about providing financial services – secure savings, credit, money transfer and insurance – in rural areas. Indeed, financial services can play an important role in rural development:

- **Savings and insurance schemes** assist the rural population in reducing vulnerability to risks, planning more reliably for the future and saving for upcoming investments, as well as smoothing out irregular income flows and covering unexpected expenses. The latter is particularly important in rural areas where income depends on agricultural cycles.
- **Loans for investments and working capital** are crucial elements that enable rural entrepreneurs to make investments, seize economic opportunities, and purchase agricultural inputs and working capital. Short-term consumption or emergency loans can help households to avoid difficult situations that might have forced them to sell an asset. However, loans are not always favourable: some poor borrowers experience difficulties in repaying their debts, due either to circumstances beyond their control (e.g. sickness, theft, natural disasters) or to a lack of knowledge and wrong investment strategies.
- **Money transfer services** make it possible for people who leave rural areas to work in cities or abroad to send home their remittances safely and at reasonable costs.

In addition to fostering rural development, rural finance is increasingly used as an incentive to promote sustainable use of natural resources, use of alternative energies, and environmentally sound behaviour. In recent years, several banks and microfinance institutions have attempted to achieve not only financial and social, but also environmental sustainability, which has been dubbed the "triple bottom line".

Despite the significant demand for financial services in rural areas, institutions offering financial services – such as banks, credit unions, microfinance institutions (MFI) or insurance companies – are typically reluctant to serve rural areas. As a result, the majority of the developing world's rural population does not have access to the formal financial system. Confronted with this lack of access, households, farmers and small entrepreneurs rely on informal ways of accessing financial services.

Experience has shown that poor people do save. In fact, for the rural poor, secure and flexible savings schemes are more important than access to credit. On the role of savings, see:

Mobilizing Savings. Key Issues and Good Practices in Savings Promotion
www.deza.admin.ch/ressources/resource_en_24283.pdf

Through the Biogas Microfinance Capacity Building Program, USAID promotes microcredit for farmers to install biogas plants in Nepal.

The Dutch Triodos bank, for example, aims at investments that benefit both people and the environment and promote sustainable development. www.triodos.com

For an analysis of different institutional forms of rural finance, see:

Models of Rural Finance Institutions
www.microfinancegateway.org/files/20074_20074.pdf

Documents mentioned in the margin are annotated in the list of references.

* **Lending among relatives, neighbours and friends:** entrepreneurs usually rely on family savings or borrow money from friends to make small investments, and in emergency situations people tend to borrow from acquaintances. Such loans are usually repaid without interest.
* **Moneylenders and pawnbrokers:** in the absence of formal institutions people typically rely on moneylenders to obtain loans. Moneylenders often ask for usurious interest rates and sometimes try to recover the loans by violent means. On the other hand, moneylenders can provide loans rapidly in an emergency, and they do not ask for collateral.
* **Community self-help schemes** such as self-help groups (SHG), rotating savings and credit associations (ROSCAs), community-based savings and credit mechanisms are useful instruments to encourage savings, provide small-scale insurance and avoid debt at exorbitant interest rates.
* In the absence of banks and official money transfer agents, **money transfer** is frequently carried out by bus drivers or small shops collaborating with a network of migrants abroad. These services are cheaper than official money transfer providers, but they are not always as secure and reliable.

On community-managed financial institutions, see:

Community-managed Loan Funds: Which Ones Work?
www.cgap.org/gm/document-1.9.2577/FocusNote_36.pdf
(See ref. CGAP, p. 13)

While the existence of informal services highlights the general demand for financial services, informal services are usually not sufficient to seize economic opportunities in rural areas to the full. Family and group savings are often too small to pay for important investments. Moreover, they are not always available in cases of emergency. This is particularly true for emergencies caused by natural disasters: if the whole region is affected, no neighbour will be able to help out. Furthermore, most loans from moneylenders are too expensive to be profitable, and debt can lead to dependency of borrowers on moneylenders.

More information on these issues can also be found in documentation related to microfinance.

The following websites provide information on microfinance:
www.cgap.org
www.lamicrofinance.org (in French).

Formal institutions can offer a broader range of financial products. Formal services such as microfinance cannot replace loans from friends and family, but they do complement them and enable the rural population to access a wider range of services. Moreover, formal financial institutions belong to the economic infrastructure of a country or region and can thus help to foster economic development.

Challenges of rural finance

Many obstacles still make it difficult for rural households and enterpreneurs to access financial services. Accordingly, both service users and financial institutions offering services in rural areas are confronted with a broad array of challenges:

- **High transaction costs:** provision of financial services in rural areas is associated with high unit costs both for institutions and for their clients. This is due to the fact that infrastructure for transport, communication and information technology is less developed in rural areas, as well as to the remoteness of these areas. Clients frequently have to travel long distances to deposit savings or repay a loan. As they usually travel on foot, this can cost them an entire working day. Rural financial institutions face additional costs for ensuring security and managing liquidity. High unit costs are usually passed on to the clients, with the result that users in rural areas frequently pay higher interest rates than people in urban areas.
- **Higher risks:** credit risk is higher in rural areas both for borrowers and for rural financial institutions. The revenues of rural households, whose incomes mostly depend on seasonal agricultural and livestock production, are volatile due to fluctuating weather conditions and pests or diseases. In addition, price fluctuations are high in the agricultural sector. Generally, rural households depend on one or two sources of income only, increasing the risk of credit default. Many households either entirely lack collateral or do not have a legal title to their house or land. Financial institutions thus have no means of securing their credits against defaulting. Defaulting clients run high risks as well: financial institutions will typically impose punitive interest rates for delayed payments and might even confiscate assets of defaulting clients.
- **Higher rates of illiteracy:** in developing countries illiteracy rates are particularly high in rural areas. Poorly educated people face an additional challenge in accessing financial services: it is difficult for them to analyse credit risks and the profitability of a loan or savings scheme, to provide all documents and information (such as a business plan) required to apply for a loan, and to understand conditions and contracts. Some institutions fail to communicate interest rates and commissions in a transparent manner, and small prints in contracts can contain additional costs for borrowers. On the other hand, financial institutions that want to expand into rural areas experience difficulties in finding, hiring and keeping well-trained staff that is willing to work in a rural region. Lack of experienced staff, in turn, leads to poor institutional capacity among rural financial institutions.

For more information about the challenges of rural finance, see:

Rural Finance – What Is So Special About It?
www.deza.admin.ch/ressources/resource_en_24697.pdf

For more details on the particularities of agricultural finance, see "Agriculture production and financial services" on page 9 of the present issue of InfoResources Focus.

Addressing the difficulties

SDC's policy for financial sector development highlights the importance of promoting financial services in rural areas, in particular.

Policy for financial sector development: Update 2007
www.deza.admin.ch/ressources/resource_en_159783.pdf

Revolving funds are funds provided to an organisation or group for on-lending. The idea is that such funds will grow over time and remain available over a long period of time. However, experience has shown that revolving funds hardly ever yield satisfactory results: most revolving funds are not managed professionally, and bad repayment rates has often led to a loss of the entire fund. See:

11 Reasons for the possible failure of a Revolving Fund
www.intercooperation.ch/finance/download/divers/reasons-failure-revolving-fund-eng.pdf

On how subsidised credit can be harmful for rural development, see:

Undermining Rural Development with Cheap Credit
www.microfinancegateway.org/content/article/detail/1661

Ways of introducing rural finance into urban microfinance institutions are described in the following case study:

Introducing Rural Finance into an Urban Microfinance Institution: the Example of Banco Procredit, El Salvador
www.fao.org/ag/rurfinconference/docs/papers_theme_3/introducing_rural_finance.pdf

Institutions that are successful in offering loans in rural areas normally follow a lending strategy based on an integrated analysis of all economic activities of a household in order to understand its cash flow throughout the year. An example of this type of methodology is given in:

Rural Finance for Small Farmers: An Integrated Approach, appendixes 2–5
www.swwb.org/files/pub_lang_Rural%20Finance_Focus_Note.pdf

Promotion of rural finance remains a priority of many governments, donors and NGOs, since several challenges still need to be addressed. Rural finance can be promoted by supporting informal schemes such as community-based savings groups, as well as by fostering formal institutions through technical assistance (supply-side measures) and assisting poor households and small enterprises in accessing financial services (demand-side measures). In addition, donors can support the development of favourable policy and regulatory frameworks.

Various approaches have been developed over the last decades to address the challenges of rural finance. In the 1970s and 1980s, governments channelled subsidised credits through centrally managed development banks; NGOs and development projects promoted access to credit through so-called revolving funds. The objective of these initiatives was to increase the availability of funds for rural and, in particular, agricultural credit. None of these approaches turned out to be financially sustainable, and the majority of the rural population remained excluded from access to financial services.

In the mid 1980s, a shift occurred towards a more demand-oriented approach, with the aim of building inclusive and sustainable financial systems. This approach takes the demand of farmers and rural entrepreneurs for savings, loans and insurance as an entry point. Indeed, when institutions offer financial products tailored to the needs of the rural population, low-income households do use saving schemes, are willing and able to pay interest rates, and buy insurance to cover their risks. Moreover, experience has shown that financial institutions only increase their outreach – to rural areas, but also to poorer clients – if they can cover their costs. Several financial institutions (such as Bank Rakyat in Indonesia, BAAC in Thailand, and FDL in Nicaragua) have demonstrated that it is possible to operate in rural areas and be financially sustainable. Key lessons learnt in recent years include the following:

- **Need orientation:** rural households and small entrepreneurs have specific needs which may vary from those of urban clients. An institution thus has to offer a variety of financial products and flexible services that are adapted to rural clients. For instance, in rural areas most households depend on agricultural cycles. Monthly or even weekly deposits for loan repayment and savings accumulation, as they are promoted by urban microfinance institutions, are simply not tailored to the needs of rural clients. It is therefore important that financial institutions understand the cash flow of rural households and offer adapted loan repayment and savings collection schemes. For example, such a scheme can involve monthly interest rate payments, while the capital is paid back in two or three instalments after the harvest.
- **Innovation:** financial institutions need to be innovative to reduce costs. Innovative distribution channels such as mobile branch offices or banking counters located in rural post offices and shops can help to reduce the fixed costs of an institution. Moreover, the use of information technology such as handheld computers or mobile phones is a helpful way of cutting transaction costs. A reduction in costs can improve access to financial services for rural borrowers and savers, as well as leading to a reduction in interest rates and transaction costs.

- **Minimizing risks:** while financial institutions in rural areas often lack collateral or the possibility to legally enforce contracts, they can use social links (for example through group savings and lending) to reduce their risks. The so-called linkage model combines informal systems such as self-help groups with formal banks. Groups are linked to the bank through a group contract, so the bank does not have to deal with each client separately. This way the bank or microfinance institution can reduce its risks and transfer transaction costs to the self-help group.
- **Building on existing institutions:** wherever possible, promoters of rural finance should build on existing institutions rather than create new ones. One way of doing this is to provide commercial banks with technical assistance to extend their services into rural areas (so-called "downscaling"). Furthermore, donors can support existing institutions in reducing costs and, thus, interest rates by helping them to develop more efficient distribution mechanisms and new products and to increase their efficiency through training, but also by assisting poor households and small enterprises in accessing financial services.

Unfortunately, even if financial institutions offer their services at reasonable costs, interest rates for loans remain high in rural areas. There is generally little or no competition among financial institutions in rural areas, and, consequently, the pressure to reduce interest rates is low. Competition needs to be fostered by attracting more financial institutions to rural areas. This, in turn, requires a favourable legal, economic and political environment.

The microfinance institution SafeSave (www.safesave.org) has achieved a reduction of costs by means of handheld computers. SafeSave operates in an urban environment, but has recently also begun to offer its services in rural areas. The introduction of handheld computers was promoted by SDC. For a case study, see:

Using Palm Pilots to Reduce Microfinance Transactions Costs: An example from SafeSave in Bangladesh
www.intercooperation.ch/finance/download/case-studies/case%20study_2_Bangladesh.pdf

Managing Risks and Designing Products for Agricultural Microfinance: Features of an Emerging Model
www.cgap.org/gm/document-1.9.2705/OccasionalPaper_11.pdf
(See ref. CGAP, p. 13)

On increasing donor effectiveness in rural finance, see:

Financial Services for the Rural Poor
www.cgap.org/gm/document-1.9.2394/DonorBrief_15.pdf
(See ref. CGAP, p. 13)

A conducive environment for rural finance

A precondition for the development of rural financial systems is a stable political and macro-economic environment. Uncertainty about the future political situation of a country and its economic development, particularly inflation, are unfavourable conditions for investments. Moreover, policy-makers should give clear signals in favour of rural development, especially the development of inclusive financial institutions in rural areas.
Improved road infrastructure, telecommunication possibilities and security in rural areas are essential in reducing transaction costs of financial services in rural areas, but also in promoting trade linkages between rural and urban regions and in attracting other economic actors.

Economic and legal framework conditions

Rural areas generally lack legal environments enabling a sound development of the financial system and the economy. In more concrete terms, land tenure and property rights are frequently unclear, the administration is slow and inefficient, law enforcement is costly and slow, and the court system lacks transparency and efficiency. Any measures to improve these aspects will help to promote rural financial systems.

For guidelines on how to devise such regulations, please refer to:

Guiding Principles on Regulation and Supervision of Microfinance
www.cgap.org/gm/document-1.9.2787/Guideline_RegSup.pdf
(See ref. CGAP, p. 13)

Every country regulates its formal financial sector through state laws and regulations. In order to accommodate a well-functioning financial sector, a country's legal and regulatory framework should be clear and transparent, promote competition among institutions, and be favourable for the development of financial services for those persons who have been traditionally excluded from the formal banking sector.

Given the particular difficulties of financial institutions operating in rural areas, laws and regulations should be designed to foster the development of rural financial institutions. While regulations are certainly necessary, overly strict regulations can also become a disincentive for institutions interested in expanding into rural areas. For example, in many countries regulations require financial institutions serving the agricultural sector to accumulate higher regulatory liquidity reserves, both because these institutions face higher portfolio risks and because their clients have no hard collateral. This discourages financial institutions from lending to the agricultural sector. In addition, when regulations are too strict, informal microfinance providers (such as NGOs) have difficulties to obtain a formal status, and, in some cases, become illegal and have to cease operating.

An experience that has been made over and over again is that legal interest rate ceilings are not an appropriate measure to fight against high costs for clients. On the contrary, it has proven to be essential for financial institutions aiming to become financially self-sustainable to charge fees that cover their costs – and these costs are higher in rural areas. Where regulations prevent financial institutions from charging sufficient interest rates to cover their costs, these fees are collected by other means, such as administrative fees and required savings. These often remain intransparent for the clients – who end up paying a lower interest rate, but much higher fees. Alternatively, financial institutions that are not able to cover their costs refrain altogether from offering their services in rural areas.

Agricultural production and financial services

An overwhelming majority of the rural population in developing countries depends on agriculture for survival. Rural financial institutions thus often provide services for activities related to agriculture, such as input supply, production, or distribution and marketing of agricultural products. As pointed out above, providing financial services to the agricultural sector involves specific challenges related to sector-specific risks and to other specific characteristics of agricultural activities, such as seasonality and long maturation processes. Loans for agricultural production or livestock breeding usually have longer terms than those for trade or small industry. In addition, rural households need financial services that are adapted to the agricultural cycle, such as savings schemes to provide cash for the season in between harvests, or transfer schemes for remittances for migrants who leave the rural areas for seasonal work. There is also a need for **agricultural insurance** schemes among small farmers who have to protect themselves against weather-related risks. Providing affordable insurance to small farmers remains a challenge due to the pooled risks involved (natural disasters causing damage to many clients at once). Institutions providing such insurance schemes need to be reinsured by big international insurance companies in order to spread the risk beyond their geographic region. An intermediate solution for insurance schemes is to offer safe and accessible savings and deposit services.

A newly proposed insurance scheme for small farmers is the weather index insurance. Weather index insurance schemes cover the risk of determined weather events. Such a scheme pays independently of the actual losses of farmers when extreme weather events, such as flood, drought and other natural disasters occur.

Even though profitability in agriculture is generally low and interest rates are high, it is possible for rural financial institutions to operate on a cost-covering basis and offer financial services to farmers. The following examples will provide some insight into how development projects can support better collaboration between clients and institutions in order to increase access to financial services.

Credit for horticultural producers in Kosovo

Commercial banks in Kosovo have shown impressive growth rates since the 1999 conflict. Yet by 2006 only 2% of their portfolio was allocated to agriculture – even though the agricultural sector is widely considered as having the greatest potential to generate income and employment. Credit products had not been designed to meet the specific requirements of agriculture, and banks considered lending for agriculture as risky.

A project for horticultural promotion in Kosovo has supported reestablishment of the apple industry with an emphasis on promoting the development of small and medium-scale orchards. To address one of the most important problems faced by small farmers – namely lacking access to banking services – the project collaborated with a major commercial bank. The bank established a specific credit product for orchard investments which involved a loan period of five years and an 18-month grace period. The project, in turn, contributed to reducing the bank's perceived risk by providing a generic business plan based on the latest technical and market information and agreeing to carry out the first vetting of applicants based on technical criteria. The bank subsequently established a pilot credit line of 100,000 Euros on the requested terms. While many medium and

The project for Horticultural Promotion in Kosovo (HPK) is financed by the Swiss Agency for Development and Cooperation (SDC) and the Danish International Development Agency (Danida) and implemented by Intercooperation. For more information, see: www.intercooperation.ch/finance/download/inforesources/credit_horticulture_kosovo.pdf Contact: Nora Gola, HPK, Kosovo nora.gola@intercoopkos.org larger farmers seized the opportunity of accessing a loan to establish apple orchards, only five small producers applied for loans. Other small farmers reported the 14% interest rate to be too high.

The bank, however, remains committed to expanding its agriculture portfolio – including credits for planting apple orchards. The project, on its part, has continued to work on reducing the perceived risk of investing in small horticultural producers. Soon it will be able to present members of the Bankers' Association of Kosovo with software enabling credit officers and business advisers to develop tailor-made credit plans for horticultural investments for individual producers based on the latest technical and market information.

Financial services for farmers in Madagascar

SAHA (Sahan'Asa Hampandrosoana ny Ambanivohitra) is a rural development programme aiming to support civil society. The programme is financed by the Swiss Agency for Development and Cooperation (SDC) and is implemented by Intercooperation. For more information, see: www.intercooperation.ch/finance/download/inforesources/article_microfinance_SAHA.pdf Contact: Aimée Randrianarisoa, SAHA, Madagascar, saha.gdrn@iris.mg

In Madagascar, a programme called SAHA provides several forms of support for central farmers' organisations (CFOs), which are made up of several village associations, in order to improve their access to financial services. In particular, the programme facilitates the relations between CFOs and microfinance institutions. In the District of Miandrivazo a mutual microfinance institution was forced to close down after 7 years of activity due to liquidity problems. Following an analysis of the need for financial services among CFO members, SAHA launched a lobbying campaign among other microfinance institutions in Madagascar to explore possible ways of collaboration and accelerate the installation of at least one of them in Miandrivazo. SAHA also provides targeted support in institutional development to microfinance institutions that have a potential for becoming long-term financial service providers. For example, the programme assists a microfinance institution called TITEM in transforming its legal status, elaborating a business plan, and in its financial management.

What is TITEM?
TITEM is a microfinance association that applies a mutual solidarity (MUSO) methodology and aims to promote community saving and management of funds prior to granting credits.

SAHA also collaborates with farmers to improve their demands. The programme raises awareness among its partners, provides information about the conditions of access to credit and savings services, and conveys basic knowledge of the functioning of financial markets and household financial management.

Working with the livestock value chain in Mali

The Jèkasy programme is implemented by Intercooperation and funded by the SDC. For more information, see: www.intercooperation.ch/finance/download/inforesources/contrib_fin_rurale_sahel.pdf Contact: Mamadou Diarra, Intercooperation Delegation, Mali, mmdiarra@icsahel.org

In Mali, livestock production contributes 10% of the GDP. Nevertheless, the majority of livestock breeders have great difficulties accessing credit despite the existence of numerous banks and a relatively well developed microfinance sector. A study by the Jèkasy programme explored the financing problems experienced by the actors of the livestock value chain in 2007.

The study revealed that although livestock producers' cooperatives are eligible to credit from financial institutions, they have trouble accessing credits due to issues of guarantee. Indeed, financial institutions seem reluctant to accept herds as a collateral for bank loans. Following this study, Jèkasy contributed to developing services for livestock producers' organisations, such as support and consulting with regard to project and business plan elaboration, negotiating with financial institutions to access their products, and implementation of business projects.

Financial services for product processing and market access

The development of rural areas depends on access to markets, be it local, national or export markets. Different actors along the value chain, from the input provider to the producer to the consumer – cultivators, processors, traders, wholesalers, retailers – depend on access to financial services to better carry out their economic activities.
Financial institutions that target the development of a given agricultural value chain should have detailed knowledge of the actors and mechanisms in this value chain and offer well adapted services. The following example describes some instruments and financial products that can be used to improve access to financial services for several actors along a value chain.

Support of value chains: the case of quinoa in Bolivia

The cultivation of quinoa has become increasingly important in the Bolivian highlands ever since the early nineties. While the value chain of quinoa was on the rise, access to financial services adapted to the specific and characteristic demands of the different value chain actors was not granted. This is why in 2005 the Autapo and PROFIN foundations set up a programme to provide value chain actors with financial products that met their needs. Building on five existing microfinance institutions that were already linked to the quinoa sector, the portfolio disbursed to this sector could be increased from US$ 91,000 to currently US$ 3,000,000.
The microfinance institutions expanded their range of products in two ways: on the one hand, they adapted the existing traditional financial products such as individual credit to the specific demands of the quinoa value chain, and on the other hand they introduced new, innovative products such as micro-leasing (ownership of equipment remains with the microfinance institution until the last instalment is paid by the client), micro-warrant (guarantee based on product stored, in order to obtain good price for the quinoa), risk capital, and seed capital. While the programme is still running, highly interesting new products such as agricultural insurance are being developed.

The proximity of urban markets has proved an asset for a programme entitled Los arboles valen ("Trees are profitable"). The programme is carried out by Nitlapan in two Districts in the Pacific zone of Nicaragua. In connection with an agricultural reform, 700 producers received titles of property for their land, as well as training and access to credit for basic investments (water management and agroforestry activities). Located in a periurban zone, they were near to the markets where they could sell their products.
One of the results is that 85% of the families established diversified systems with agroforestry components and were then able to benefit from conventional credit from microfinance institutions to improve their means of livelihood.
For more information on Los arboles valen, see: www.intercooperation.ch/finance/download/inforesources/los_arboles_valen.pdf
Contact : Marcelo Rodriguez, Nitlapan, Nicaragua, gavino@ns.uca.edu.ni

The Programa de Apoyo al Sector Financiero (PROFIN – www.profin-bolivia.org) is financed by the SDC and Danida.
For more information, see: www.asocam.org/biblioteca/R0211_completo.pdf
Contact: Edwin Vargas, PROFIN, Bolivia, evargas@fundacion-profin.org

Perspectives

Although the importance of financial services for rural development has been recognised for several decades and the microfinance boom in recent years has once more underlined the importance of financial services, large parts of the world's rural population remain excluded from formal financial services. This mismatch of demand and offer can be explained, first of all, by the challenges faced by rural financial institutions – namely a difficult legal and economic environment, high transaction costs, and higher risks in agricultural lending. Secondly, financial products offered are not always demand-oriented, and institutions do not invest enough in careful product design. Agricultural credit has to be available over long terms, and repayment schemes should be adapted to the agricultural cycle.

Particularly the poorest parts of the rural population are excluded from access to financial services. Experience has shown that it is difficult to reach the poorest by focusing on credit only. Poor households need means to reduce their vulnerability. Therefore the emphasis should be placed more on savings and insurance services, rather than on credit only. Development of affordable and functioning insurance schemes is particularly important, and will increasingly become so.

Despite these challenges there are many positive examples of increased access to financial services in rural areas. Lessons learnt in the past should guide donors in continuing to promote rural finance: by supporting farmers and households in accessing services, by assisting institutions in offering adapted products at a reasonable price, and by promoting an improved regulatory framework. However, the promotion of access to financial services should always be seen as one piece in the larger puzzle of rural development: work towards a sustainable social and economic development of rural areas must include many other aspects, as well.

Rural finance will certainly remain on the agenda of governments and development agencies in the years to come, as large parts of the population remain excluded from the formal financial system. To tackle this issue, governments might increasingly collaborate with the private sector to find innovative solutions. Moreover, the ongoing integration of many rural areas into regional and even global markets will lead towards an improved infrastructure, which will also include financial institutions. At the same time, these changes will also expose parts of the population to the risk of becoming even more vulnerable and losing their livelihood. These are the people who should be enabled to adapt to such changes with the help of savings and affordable insurance.

Recommended reading

The following list features a documented and targeted selection of print documents and Internet sites of relevance to "Accessing Financial Services in Rural Areas". For easier reading they have been allocated to four rubrics: ***Overview, Policy, Instruments, Case studies.*** *The documents are listed by title in alphabetical order. Most of them are available online (accessed on August 2008).*

Instruments
Case studies

Quirós, Rodolfo. 2007

Agricultural Value Chain Finance: Summary of the conference, Costa Rica, May 2006

ftp://ftp.fao.org/docrep/fao/010/i0016e/i0016e00.pdf

Value chain financing was one main topic addressed by the conference. Strengthening value chains, increasing their size, and expanding participation in them requires financing from outside the chain. For example, financing can be extended to a large supplier of the chain who can offer loans or sell inputs on credit to other actors in the chain. Organised farmer groups could be financed if they can prove assured markets. Clusters that on the one hand have their own financial institutions or institutions with local information and in-depth knowledge of agricultural production, and on the other hand link up with capital from outside organisations represent another innovative way of value chain financing.

Overview
Instruments

Pearce, Douglas. 2003

Buyer and Supplier Credit to Farmers: Do Donors have a Role to Play?

www.ruralfinance.org/cds_upload/1126181060970_Buyer_and_supplier_of_credit_to_farmers_-1943486288.pdf

Any donor intervention in product and financial markets risks distorting or damaging these markets. However, there are several means to reduce market distortion: focus on farmers that are poorly integrated into product markets, but could be viable market participants; subsidies for training and technical assistance to build provider capacity, rather than for the cost of services or loans to farmers; time limits for subsidies with achievable objectives; provision of support based on transparent selection criteria.

Overview

Consultative Group to Assist the Poor (CGAP)

CGAP Advancing financial access for the world's poor

www.cgap.org

CGAP develops innovative microfinance solutions in order to expand access to financial services for poor people around the world. The CGAP website is the leading independent resource for objective information, expert opinions, industry information and research publications. The present issue of InfoResources Focus refers to several CGAP documents (see pages 3, 4, 7 and 8).

Case studies
Policy

Swiss Agency for Development and Cooperation (SDC). 2007

An Era Of Innovation: Thirty Years of SDC's Involvement with Rural Finance in India

www.sdcindia.in/ressources/resource_en_160297.pdf

Over the 30 year period covered by this report, SDC's rural finance programme has undergone three major reorientations: from supporting the farm sector only to including the non-farm sector in the mid 1980s; from supporting credit only to including non-credit activities such as promotion and development in the late 1980s; and from a programme to alleviate poverty to one that includes development of entrepreneurship and institution-building in the mid 1990s.

Policy

International Fund for Agricultural Development (IFAD). 2004

IFAD Rural Finance Policy

www.ifad.org/pub/basic/finance/ENG.pdf

IFAD supports solutions to the following challenges: participation of stakeholders, including the poor, in the development of rural finance; building an infrastructure with diverse strategies; enhancing institutional sustainability, with outreach to rural poor; promoting a conducive policy and regulatory environment.
To face these challenges, IFAD provides several recommendations, including loans and grants as the main instruments to improve food production systems and income, as well as nutrition of the rural poor. IFAD has also developed tools such as a planning framework and instruments for performance measurement and internal control of microfinance.

Case studies
Instruments

Buchenau, Juan and Meyer, Richard L. 2007

Introducing Rural Finance into an Urban Microfinance Institution: The Example of Banco Procredit, El Salvador

www.fao.org/ag/rurfinconference/docs/papers_theme_3/introducing_rural_finance.pdf

At its beginning in 1988, Banco ProCredit developed operations in urban areas. In 1992, a pilot project was initiated by granting loans to small vegetable farmers. Target areas were selected based on accessibility, proximity to a Bank's branch office, and a secure water supply to minimise the risks of crop failure due to drought. The main step of this innovation process is the definition of the lending technology for the entire range of activities carried out, determining the types of loans to be granted, the loan amounts and terms to maturity, and ways in which loans will be secured, as well as the monitoring and recovery of loans. ProCredit has been successful by adopting a flexible individual lending technology attractive to rural clients in their diversity.

Case studies

Wenner, Mark D. 2002

Lessons Learnt in Rural Finance. The Experience of the Inter-American Development Bank

www.iadb.org/IDBDocs.cfm?docnum=355579

Over the 37 years covered by this review, the IDB's rural finance activities evolved from placing a heavy emphasis on expanding the supply of rural credit to giving more attention on making sure that the financial architecture is right, i.e. on improving the regulatory framework that facilitates the development of rural financial services. One challenge in the future will be to better understand the dynamics of intra-household decision-making. Gender issues, internal distribution of power and command of productive resources complicate the loan evaluation process and can affect both willingness and ability to repay.

Case studies
Instruments

Food and Agriculture Organization of the United Nations (FAO). 2005

Microfinance and forest-based small-scale enterprises

ftp://ftp.fao.org/docrep/fao/008/a0226e/a0226e00.pdf

The indirect environmental consequences of extending microcredit to poor people generally include an increase in physical capital, as well as growth and diversification of income. There are also social effects which mostly improve the use of common forest resources. The impact of all these factors on deforestation rates and on the use of environmental resources is ambiguous, depending on borrowers' responses to the changed opportunities. Mechanisms such as government matching grants to forest-based enterprises that commit to environmentally sustainable practices may be preferable to the provision of targeted credit with subsidised interest rates, which have often proved inefficient and undermine the long-term sustainability of microfinance institutions.

Overview

Dauner Gardiol, Isabelle. 2004

Mobilizing Savings. Key Issues and Good Practices in Savings Promotion

www.deza.admin.ch/ressources/resource_en_24283.pdf

This publication provides an overview of the demands of low-income households for savings services (micro level), as well as savings mobilisation from the perspective of a financial institution (meso level) and the regulatory financial authorities in developing and transition countries (macro level). It is conceived as a tool for the SDC collaborators and partners as well as for all other concerned persons.

Overview
Instruments

Zeller, Manfred. 2003

Models of Rural Finance Institutions. Invited lead paper for the International Conference on Best Practices in Rural Finance, June 2–4, 2003

www.microfinancegateway.org/files/20074_20074.pdf

Because of the specific characteristics and the diversity of different rural areas and of agriculture, institutional and technological innovation and adaptation is crucial to reduce transaction costs for institutions and clients alike. Innovation can be enhanced through participatory processes and public-private partnerships; credit unions or village banks have comparatives advantages. All these approaches support the development of a diversity of financially sustainable institutions.

Policy

Ramm, Hans. 2007

Policy for financial sector development: Update 2007

www.deza.admin.ch/ressources/resource_en_159783.pdf

The SDC's efforts are oriented towards facilitating the outreach of institutional financial services in order to effectively alleviate poverty among target groups. On the demand side, the SDC intervenes through skilled organisations that support self-empowerment of target groups so that they can access institutional financial services. On the supply side, the SDC offers capacity development, technical assistance, and risk capital instruments to microfinance providers. Support also includes strategic alliances between self-help groups and formal financial institutions to reduce risks for both.

Overview

Portail Microfinance

www.lamicrofinance.org

From here, users can easily access the English or the Arabic Microfinance Gateway page. However, InfoResources chooses to present the French Gateway because it offers more options and relevant resources. The "Portail Microfinance" is the most comprehensive online resource for the French microfinance community. It includes research and publications, featured articles, organisation and consultant profiles, as well as tools. Users have the possibility to upload their own contributions.

Instruments

Milligan, Walter. 1994

11 Reasons for the possible failure of a Revolving Fund

www.intercooperation.ch/finance/download/divers/reasons-failure-revolving-fund-eng.pdf

This paper explains reasons why revolving funds set up for the support of small-scale farming and livestock activities have often failed to be an effective and sustainable instrument of support.

Overview

Egger, Ruth. 2005

Rural Finance – What Is So Special About It?

www.deza.admin.ch/ressources/resource_en_24697.pdf

This synthesis looks at rural finance based on 5 points, from the supply and the demand sides to what is needed, including the framework conditions and the aspects to be considered. In the 70s and 80s, the government-owned development banks and some projects offered loans. Today, agricultural credit is usually related to cash crop production. The demand of rural households for financial services includes both farm and non-farm activities. The regulatory framework as well as government supervision have to take into account the specific liquidity requirements in remote areas, the problems of communication, risks, seasonality and social links in place.

Overview

Case studies

Dellien, Hans and Lynch, Elizabeth. 2008

Rural Finance for Small Farmers: An Integrated Approach

www.swwb.org/files/pub_lang_Rural%20Finance_Focus_Note.pdf

This paper provides an introduction to the key elements of success in the expansion of micro-lending to rural areas. First, common risks in agricultural production that may impact clients' repayment capacity are analysed. Then institutions and the various steps for their expansion in a responsive and sustainable way into rural markets are considered. A case study of Women's World Banking with ADOPEM Bank in the Dominican Republic illustrates each step of the expansion process.

Overview

Rural Finance Learning Center

www.ruralfinance.org

The Rural Finance Learning Center aims to assist organisations in building their capacity to improve rural financial services. The Rural Finance website provides access to a wealth of material in the field of rural finance. Online study lessons introduce users to various topics of microfinance (all modules are available in English, some also in French and Spanish), training guides, workshop abstracts and training opportunities give an overview on ongoing learning events in the sector. A resources section contains a large database of materials relevant to rural finance. Further features of the site are a news section and a discussion room for microfinance topics.

Pearce, Douglas and Reinsch, Mika. 2005

Case studies
Instruments

Small Farmers in Mozambique Access Credit and Markets by Forming Associations with Assistance from CLUSA

www.ruralfinance.org/servlet/BinaryDownloaderServlet?filename=1127396086373_Managing_risks___case_study_5.pdf

Through its Rural Group Enterprise Development Program, the Cooperative League of USA (CLUSA) organised 26,000 isolated farmers in the Northern provinces into associations in order to establish better relationships with commodity traders and other agribusinesses. During the period of 1996–2003, a greater number of Northern Mozambican farmers contracted with agribusinesses than ever before. However, many results are not quantifiable, such as structural and long-term changes in farmers' access to finance, enhanced agricultural skills, and community lobbying power.

World Council of Credit Unions. 2003

Overview
Case studies

A Technical Guide to Rural Finance: Exploring Products

www.woccu.org/functions/view_document.php?id=rf_techguide

Rural households have various strategies for accumulating assets and minimising their vulnerability. Therefore, rural finance institutions need to assess the demand of rural clients for multiple financial services, identify and examine the income and expenses of their clients at the household level, and assess environmental credit risks associated with production. Based on case studies in Latin America, Africa and Asia, this guide gives a concise overview of rural finance products and delivery mechanisms that contribute to advancing the provision of the following financial services to rural areas: lending, savings, leasing, insurance, and remittances.

Adams, Dale W.; Graham, Douglas H.; Von Pischke, John D. 1984

Overview

Undermining Rural Development with Cheap Credit

www.microfinancegateway.org/content/article/detail/1661 (presentation only)

This book discusses reasons for the disappointing results of agricultural credit programmes in low-income countries. Five issues are emphasised: credit should be viewed as a product of financial intermediation and not as an input; commonly accepted assumptions about rural financial markets, savings behaviour and agricultural credit, to date, were weak or even wrong; cheap-credit policies were probably the most important factor causing the failure of agricultural credit programs; political considerations often block rural financial market reforms; recent research and evaluation could help improve performance.

Bugada, Kathy. 2007

Case studies
Instruments

Using Palm Pilots to Reduce Microfinance Transactions Costs: An example from SafeSave in Bangladesh

www.intercooperation.ch/finance/download/case-studies/case%20study_2_Bangladesh.pdf

This case study analyses how the palm pilot has changed the life of the staff and the clients of SafeSave in terms of transactions costs, security, and confidence. The introduction of the palm pilot and the use of this technology has increased the clients' confidence that the transactions are correct and that the staff are transparent and professional. For SafeSave, the experience generated considerable time savings which were reallocated to client's visits, resulting in higher client satisfaction and loan recovery rates.

__InfoResources Focus__ provides a general overview of pertinent and topical subjects to guide one through the information jungle. Each issue focuses on a current theme relative to forests, agriculture, natural resources and the environment, in the context of international development cooperation. Each theme is viewed from several angles:

- *Policies and strategies*
- *Implementation and practical experiences.*

The first section of InfoResources Focus proposes a brief introduction to each subject, highlights specific problems, compares theoretical approaches and opinions, and reports past experiences. The second section presents a selective and commented choice of documents, books, CD ROMs and Internet sites. The range of documents presented reaches from basic introductions, through instruments, methods and case studies, to conceptual texts. __Back issues of InfoResources Focus__ can be ordered from the address given on page 2 or downloaded from www.inforesources.ch.