

LINKING FORMAL AND INFORMAL FINANCIAL INTERMEDIARIES IN GHANA: CONDITIONS FOR SUCCESS AND IMPLICATIONS FOR RNR DEVELOPMENT

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Small-scale credit provided under appropriate conditions has long been recognised as an engine of rural development, and informal institutions have played an important role in providing this. However, their capacity is limited, but formal institutions with much greater financial capacity rarely reach rural people because of the risks and transaction costs. Describing how in Ghana the two types of institution have worked together, to their mutual advantage and to that of small-scale rural traders and borrowers, this paper draws out the preconditions that must be in place for linkages of this kind to prosper elsewhere.

Policy conclusions

- By linking with existing informal savings and credit arrangements, formal institutions can greatly increase the volume of small loans available to rural people in ways which are accessible, provide high repayment rates and are profitable.
- Important prerequisites include a wide spread network of informal savings and credit agents and groups and a recognition they have a role to play in RNR development. A second step is to reform and extend the prudential and regulatory framework to include informal financial agents will generally also be necessary.
- For linkage policies to succeed, the essential features of formal financial institutions are flexibility, innovative approaches and an openness to change. Incentives at both the institutional and individual staff level may be required.
- Policies to develop mutual understanding and build capacity are important, and should promote an understanding of each other's operations, and of their respective financial products and processes.

Background

Perceptions of high risk, high cost and low returns turn banks away from investment in small-scale renewable natural resources (NR) activities. Even where the density of formal financial institutions is high, accessibility for the rural poor, particularly poor women, remains low.

High proportions of rural credit and savings are still managed informally. To varying degrees informal financial services are characterised by easy access, flexibility in loan use, rapid processing, flexibility in interest rates and collateral requirements. However, informal agents are restricted in the size and duration of lending and in their area of operations. Moreover, they are vulnerable to co-variant risks – a particular problem of the NR sector.

Following an outline of financial service provision and financial service needs for the NR sector in Ghana¹ the paper reviews the experience of particular linkage case studies².

Financial service provision for the NR sector

The banking sector in Ghana comprises the central bank, eight commercial banks, three development banks, three merchant banks and 133 rural banks. With the exception of the rural banks, their distribution is weighted towards urban areas, and towards the south. Seven out of the thirteen districts in the Northern Region have no banks and the ratio of clients to banks in northern Ghana is much higher (100,000:1) than in the country as a whole (16,000-26,000:1).

The semi-formal financial sector in Ghana includes Credit Unions, Savings and Credit Co-operatives and a number of NGOs. Informal financial agents include: moneylenders; *susu* collectors (savings mobilisers); traders, agricultural processors and input distributors; *susu* groups/ROSCAs (Rotating Savings and Credit Associations), and friends and relatives.

Susu collectors are unusual in having an apex organisation to represent them; 850 are registered with this, though it is estimated a further 150 unregistered operate in the North. They run their businesses from kiosks located in the market place and act as mobile bankers. Deposits, often of low but regular value, are usually taken on a daily basis over the course of a

month. At the end of this period the *susu* collector returns the accumulated savings to the client but keeps one day's savings as commission. *Susu* collectors may also provide 'advances' to their clients.

As individual savings mobilisers, the banks are characterised by a large client base, large individual deposits, and high annual value of deposits. In 1997 the Rural Banks had an average of 12,000 accounts, and the ADBs (Agricultural Development Banks), an average of 4,324 accounts, against an average of 253 members for the credit unions and 300 clients for the *susu* collectors. The *susu* collectors provide savings facilities to individuals involved in a wide variety of informal income generating activities: traders, cart pushers, apprentices, mechanics, drivers, and sometimes farmers and fishermen. Of 19 ROSCAs surveyed in Northern Ghana, membership ranged from 5 to 40 persons with 63% of these groups having between 10 to 20 members, almost all women and mostly engaged in processing and marketing as throughout the informal sector.

On the credit side the banks are characterised by relatively high value and longer duration loans which require formal application and collateral. Advances made by the *susu* collectors to their regular depositors are usually low value, very short term (less than one month), provided on an interest-free basis without collateral, and disbursed immediately if the money is to hand. The moneylenders advance loans on interest (higher than the banks), but without collateral, and disbursed very quickly if the client is known.

Combining the banks' capital with the intrinsic advantages of the informal agents (small savings and loan provision, physical and social access, simple procedures, reliance on social capital and collateral, quick withdrawal and disbursement, and high proportions of women clients) is thus one argument for linking the formal and informal financial intermediaries.

Specifically, in relation to the NR sector, the banks (even the ADBs) very rarely rank agriculture as their first lending preference, and tend to limit loans to less risky and shorter duration processing and trade rather than farming or fishing.

Against a background of recent economic reform, there has been a decline in the proportion of advances (by value) for agriculture, forestry and fishing from 17% to 5% (Commercial Banks), and from 13% to 9% (Rural Banks over the period 1988 to 1995).

However, it is not the case that informal financial agents always step in where banks fear to tread: some moneylenders and *susu* collectors can be just as reluctant as the banks to advance loans for primary production and and fish catch for exactly the same kind of reasons. Thus linking the banks and the informal agents may not automatically bring about a greater flow of resources to the NR sector.

Financial service needs in the NR sector

About half the economically active population of Ghana work in NR. Excluding cocoa, the agriculture sector alone contributed some 33 per cent to the country's GDP in 1996. In 1992, non-farm self-employment accounted for 33 per cent of rural households' income, whilst many micro-entrepreneurs also own farms: a reflection of livelihood diversity in rural areas.

Amongst the most common processing and manufacturing activities related to NR are *gari* (processed cassava), shea butter production, *pito* (local beer) brewing; fish processing; boat building, charcoal making and blacksmithing. Many also work as traders of inputs or outputs. All have their own particular investment and working capital needs which are influenced by the seasonality and duration of NR activities, and the scale and lifecycle position of their enterprises. For example within the inland fishing communities the financial needs of salt sellers, fish processors, fish traders, fishermen crew, canoe/fishing net owners, fishing gear sellers, boat builders and mechanics all fall at particular and sometimes varying times within the fishing seasons.

'Linkage' between formal and informal comprises two distinct possibilities: complementarity between them among activities or among different clients in the *same* activity, or wider interaction, such as through savings or credit *across* types.

In terms of complementarity, the scale of activities and position in the enterprise life-cycle are important determinants of sources of credit preferred and to a lesser extent of deposit-making. Formal and informal sources complement each other in these dimensions. More informal sources of credit (e.g. friends and relatives in the same business) are preferred for

Table 1 Background to three Formal Financial Institutions with Links to Informal Groups/Agents

Features	CITI	M & A Bank	Ahantaman RB
Date established	1992	1995	1984
Number of branches	HO + 3 branches	HO + 3 branches	HO + 7 agencies
Location	Greater Accra	Greater Accra	Wester Region
Number of staff	54	102	104

obtaining start-up capital. Working capital is obtained in various ways from traders, moneylenders, friends, relatives including spouses, own profits and proceeds and suppliers' credit. Those clients with substantial capital assets (land, boats etc.) tend to use the widest variety of credit sources and almost always save with banks. Those groups who have formed some sort of association (tomato growers or fish processors) are more likely to have accessed donor or government funding than those who have not.

Clients' perceptions of the various financial service providers help to determine their selection, (Box 1). By themselves the individual financial service providers do not encompass all the features desired by clients but in combination, possibly through the wider linkages discussed below they may be in a better position to do so.

Wider linkages between financial intermediaries in Ghana

In terms of flow of funds, significant linkages between financial agents and institutions were found in the three research areas. Some of these are frequent and regular (e.g. traders depositing liquid funds with *susu* collectors, *susu* collectors depositing mobilised savings in banks) other linkages are more sporadic (e.g. moneylenders taking loans from banks). In addition to these 'institutional' linkages there are also important credit relations at the community level between different actors in particular economic sub-sectors e.g. between boat builders, fishing gear sellers, canoe and net owners, fishing crew, traders, processors and salt sellers.

In addition, the Association of Rural Banks (ARBs), the Credit Union Association (CUA) and the Ghana Co-operative *Susu* Collectors Association (GCSCA) influence the interface between intermediaries. Moreover, the Micro-Finance Institutions Action Research Network (MFIARN) formed in 1996, not only includes a very wide range of players in the financial services sector, but also plays an active role in policy discussion, formulation and advocacy in Ghana, including discussions on these wider linkages.

Formalising linkages between financial intermediaries

Apart from the largely spontaneous linkages described above, in recent years there have also been an increasing number of financial institutions in Ghana seeking to establish more formal, purposive linkages with informal financial agents.

Examples reported here are: (i) the links an Accra based non-bank financial institution (CITI Savings and Loans Company) had developed with *susu* collectors (ii) the links established between an Accra based Commercial Bank (The Metropolitan and Allied Bank) with ROSCAs, and (iii) the links another Rural Bank (Ahantaman Rural Bank) had established with ROSCAs and the ways in which this bank had incorporated *susu*-like operations into its own banking practices.

Box 1 Clients' perceptions of selected formal and informal financial intermediaries

Financial Intermediaries	Advantages	Disadvantages
Banks	Lower interest charges Larger amounts available Good for expanding business when timing is not so crucial and collateral available	Physical collateral required Intimidating form filling Slow disbursement of loans Untimeliness of loans Rent seeking by officials Delays in withdrawing funds Mistrust when banks fail/officials abscond Distance to travel Deposits with high inflation
Credit Unions	Relatively low interest rate Quicker than banks Cheaper than banks Facilitate loans	For members only Not so quick as friends and market women
Moneylenders	Money available Quick and easy processing Security through guarantor	High interest charges
Susu Collectors	Encourages savings habits Money can be used for personal expenditures Easy withdrawal	Some untrustworthy Need a regular source of income to use them Vulnerability of savings Credit advances very short term

Table 2 Savings mobilised through informal groups/agents						
	CITI 16 groups 4634 members	M&A Bank 7 groups 929 members	Ahantaman RB 17 groups 1260 members	Links with Susu Collectors/ Clerks	CITI 63 Susu Collectors 25,000 clients	Ahantaman RB 26 Susu Clerks 6,000 clients
Links with Susu Groups						
% women members	82%	77%	70%		>70%	60%
Savings mobilised by groups	¢262m weekly	¢26m weekly	¢24m weekly	Savings mobilised by susu collectors/ clerks	NA	¢750,000 daily ¢300m monthly
Average savings mobilised by groups	¢16m weekly	¢3.7m weekly	¢1.4m			
Savings mobilised by members	¢5,500-¢330,000 weekly	¢3,000-¢300,000 weekly	¢12,500- ¢25,000 weekly	Savings mobilised by clients of SCs/S Clerks	¢500-¢10,000 daily	NA
Interest paid on deposits	15-20%	0% or 15% depending on loan arrangements	21%	Interest paid on deposits	13-21% to SC	yes if transferred to savings account
% Deposit liability	26%	NA	2.4%	% Deposit Liability	3%	18%
N.B. In March 1998 £1=3846 cedis						

Table 1 provides background information on these three formal financial institutions. The number of accounts they hold ranges from nearly seven thousand (M&A) to just over twenty-six thousand for the ARB, with over 40% held by women CITI, M&A). Linkage to *susu* groups and *susu* collectors offers the potential for reaching even more women clients.

The right-hand side of Table 2 shows two different kinds of links. First, those that CITI has established with 63 individual *susu* collectors, 16 of whom also take loans from CITI to on-

lend to their own clients. Second, 26 *susu* clerks are employed by the ARB to operate as *susu* collectors for the bank: an interesting example of a formal financial institution incorporating an informal savings practice within its own banking operations.

The outreach potential of linkage for the formal financial institutions is very apparent (Table 3). The total numbers of indirect clients through linkage with the *susu* groups varies from 929 for the M&A bank to over 4,500 for CITI. In addition the 63 *susu* collectors linked to CITI have themselves 25,000

Table 3 Loans advanced through informal groups or agents						
Links with Susu Groups	CITI 16 groups 4634 mem.	M&A Bank 7 groups 929 mem.	Ahantaman RB 17 groups 1260 mem.	Links with susu collectors/clerks	CITI 63 (16) SCs	Ahantaman RB 26 SClerks
Loans from FI to groups	min ¢2m max ¢679m aver. ¢160m weekly	¢30m- ¢750m per cycle	¢300,000 to ¢1m		NA	NA
Loans from groups to members	min ¢0.5m max ¢30m aver. ¢2m	¢300,000 to ¢5m*	¢100,000	Loans from SCs/ SClerks to clients	RS: ¢20,000 to ¢750,000 ES: ¢90,000 to ¢1m NA	0.5m to 1m 0.5m
Interest Charges	CITI to group 38-42%** Group to member 20-25%***	65% of market rate	N/A	Average No. clients receiving loans Gender of clients Interest charges	10-30 at a time 80% female RS=0 ES CITI to SCs 3.5 a month SCs to clients 3.5-5% a month	c. 100/month 60% female 40%
Loan duration	2 year cycle	1 year cycle	FI to group: 9-12 months Group to member: 1-3 months	Loan duration	RS: 1 month ES: 3-6 months	9-12 months
Criteria for loan	Savings record Guarantors	Savings/atten. record	NA	Criteria for loan	Savings record	Savings record
Repayment rate	98%	100% better than corporate customers	95% to ARB 99% to groups 90%	Repayment rate	98%	95%
% Grad. to direct relations	Mandatory for all members to have a/cs	49%		% Grad. to direct relations with FI	Occurs but no figures available	90%
* Based on figures for three groups & depending on value of weekly contributions ** On reducing balance *** Flat rate						

clients while the 26 *susu* clerks employed by the ARB service a total of 6,000 clients. Some 60%-80% of clients are women.

These links were all established in the last 5 years. Bank requirements for linkage variously relate to prior savings, registration and governance of the group and *susu* clerks must have completed secondary education. All the groups meet weekly and interact with the banks on a weekly or fortnightly basis.

From Tables 2 and 3 the advantages of linkage for the three formal financial institutions are clear. For CITI alone the savings mobilised through groups account for over a quarter (26%) of its deposit liability. The *susu* collectors linked to CITI receive between 13 and 21 per cent on the savings they mobilise from their clients. As traditionally, the clients of the *susu* collectors receive no interest but pay one day's saving to the *susu* collector as commission. By contrast, the clients of *susu* clerks do not have to pay commission and can in fact earn interest on their savings.

The advantages of linkage for both the formal financial institutions and the informal groups are also apparent with respect to lending arrangements (Table 3): interest earnings are substantial, repayment rates high and high proportions of group members have 'graduated' to direct relations with the financial institutions. For members of groups linked to CITI and the M&A Bank a major advantage is that a greater number of members receive their loans earlier in the cycle compared with a traditional rotation system. A further advantage is the prospect of graduating to direct loan arrangements with the financial institution. However, there is a price to pay for this advantage: under CITI's arrangements, members pay a flat rate interest charge of between 20% to 25% for the loan they receive, and no members receive any loan until week ten, compared with traditional ROSCA operations where members would start to distribute rotating savings from the first week.

The advantage to CITI of links to the *susu* collectors is the access such linkage provides for cost-effective loan provision to large numbers of 'indirect' clients. In Table 3 a distinction is made between regular *susu* and extended *susu*. The former refers to *susu* collectors who operate in the traditional manner and use CITI to deposit their mobilised savings, while the latter refers to *susu* collectors (16 of the 63) who on the basis of accumulated savings deposited with CITI also take loans from CITI which they on-lend to their clients in larger amounts and on a longer term basis than regular *susu*. ARB lending is similarly channelled through *susu* clerks.

Conclusions

Different actors in the NR sector require a range of financial services. Primary producers need fixed and working capital to renew and conserve the NR on which they depend. Processors and traders need to purchase, process and market NR products, while input suppliers need to purchase their traded goods. However, urban concentrations of bank branches, and a reluctance to lend to production activities in the NR sector, means that small-scale operators in this sector largely rely upon a plethora of informal savings and credit agents even though these agents operate under capital and term constraints. If banks 'do not want to go down to the bush' as one bank official in Accra put it, then linking with informal agents may be one way of reducing the gap between needs and financial service provision in the NR sector.

Evidence suggests a complex set of relations between a wide range of players in the formal, semi-formal and informal financial sectors. However, in Ghana to date attention has concentrated on formalising linkages with individual financial agents such as *susu* collectors and traders, and with *susu* groups – agents and organisations that have the potential to channel substantial informal savings into the formal financial sector.

For the three formal financial institutions reviewed in this paper, linkage offers the range of advantages described. Linkages also offer advantages in wider rural development terms: most of the clients of *susu* collectors and members of the *susu* groups are female and are engaged in a wide range of micro-enterprise activities, some of which are directly and some indirectly linked to the NR sector. In a more rural context the potential for bank-*susu* collector linkages to improve financial service provision for farmers is much greater, and here *susu* collector-trader linkages are very evident, providing potential for indirect financial service provision for the NR sector. The large number of traders across the country also provides the opportunity for directly influencing financial service provision to small scale operators in the NR sector by linking them through the banking system.

The process of formalising linkages can be long and contentious, and there remain concerns on both sides. With official recognition of the informal financial sector and its inclusion in regulatory reform, two important preconditions for innovative policy towards the informal financial sector have been fulfilled in Ghana. Policy can now address issues relating to training and capacity building for financial intermediaries, and for apex organisations seeking to play an active role in promoting linkages between formal sector institutions and informal financial agents.

Formal linkage arrangements are recent and few in number. It is important to monitor their effects and impacts. Future comparative studies will be able to determine positive and negative impacts of different kinds of linkage arrangements on financial service provision for micro-enterprise development and for the NR sector.

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Endnotes

¹ Drawn from Winneba, Sunyani and Yeji, over 1996-8 reflecting distinct agro-ecological zones and dominant RNR activities and later supplemented by a study of financial service needs in the three northern Regions which included a survey of 19 Rotating Savings and Credit Associations (ROSCAs).

² Based on data collected during a further visit to Ghana in 1999.

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