Microfinance banks and agro-allied small and medium scale enterprises in Ogun State, Nigeria: Prospect, performance and constraints

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Abstract
Microfinance bank (MB) is currently being promoted as a key development strategy for promoting poverty eradication and economic empowerment in Nigeria. Based on this, the study examined the prospect, performance and factors affecting the financing of ASMSE by MB in Ogun State Nigeria. The entire five microfinance banks in Ijebu North Local Government Area (INLGA) of Ogun State, were used for the study. Data were collected through structured questionnaires and interview schedule. The data were analyzed using descriptive statistics such as bar chart, pie charts, frequency distribution and percentage. Results revealed that the loan schemes operated by MB differ from one bank to another. The loan schemes include micro-credit, agricultural production loan, trade and transport loan, small and medium enterprise credit, bulk purchase finance, overdraft facility, and equipment leasing. The study also revealed that MB through their various activities had affected operators' productivity positively while some ASMSE are not favoured by MB due to some factors such as long payback period and low rate of return. However, microfinance banks interest rate and loan duration period are major constraints to ASMSE operators in procuring loan. The main factor affecting MB's loan availability to agro-allied sub-sector was the type of enterprises embarked upon (fish farming, poultry production and piggery in that order) while food crops and tree crops enterprises were not favoured. The study concluded that sustained holistic government policies on microfinance would increase the ample scope for mobilizing micro savings and thus consequently increasing the productivity of ASMSE operators.

Keywords: Agro-allied, Small and medium scale enterprises, Microfinance banks

INTRODUCTION

Agriculture in Nigeria and in most developing economies still manifests most of the typical symptoms of peasant agriculture. Some of these symptoms include use of farm inputs that are mainly land and labour, small farm holdings and subsistence production and small capital investment (Famoriyo, 1984). Other variables that characterized agricultural enterprise in this region include, inadequacy of extension services, inadequate credit to meet the financial needs of farmers, inadequacy of storage facilities, seasonal fluctuation and instability of prices, over exposure of risk and natural hazards, rudimentary technology that has kept pace with the demand of the sector, inability of research effort to tackle immediate and future needs of farmers (Famoriyo and Nwegbo 1981). However, inadequate access to credit has been identified as critical factor facing the smallholders in Nigeria (Olieh, 1980, Olomola, 1990). The major challenge to the funding of agriculture in Nigeria is that farmers have relied mainly on personal finance especially from personal savings and borrowing from friends and relations in the absence of institutional finance sources. These funding sources are usually not reliable and the amount of fund available is rather limited relative to their needs. Institutional financing sources such as banks and government initiative have remained inaccessible to the farmers, for reasons of administrative encumbrances, unwillingness on the part of banks to grant agricultural loans, and lack of political will of government to ensure successful financing of agriculture through their various agencies and initiatives. The government's realization of these problems led to the creation of specific programmes such as the Agricultural Credit Guarantee Scheme (ACGS), the Nigeria Agricultural Cooperative and Rural Development Bank (NACRDB), sectoral loan allocation, rural banking scheme for commercial banks, establishment of Microfinance banks, encouraging the formation of farmers' cooperative societies. Additional to these, federal, state and local governments make annual budgetary allocations for financing various agricultural programmes basically to boost agricultural production and productivity. The failure of pervious attempts at extending financial resources (credit) to rural producers motivated the introduction of community banking system in January 1990 (Now Microfinance bank) in Nigeria.

Finance is a major input for the transformation of the agricultural sector particularly in developing countries that are dependent on agriculture and its provision determines access to essential farm and production inputs. Credit for the smallholder, especially in agriculture, is assuming increasing importance in many parts of the world in response to the needs of less privileged entrepreneur with limited capital base (IFAD, 2001). Financing of agricultural sector by microfinance banks involves the extension of credit or loan from microfinance bank to farmers/producers (both the small and large scale farmers) in order to improve greatly in their agricultural production practices. Microfinance bank is currently being promoted as a key development strategy for promoting poverty eradication and economic empowerment. It has the potential to effectively grant financial services to households who are not served by the formal banking sector. Commercial banks traditionally lend to medium and large enterprises which are judged to be creditworthy with little regard to micro enterprises because the associated cost and risks are considered to be relatively high. Microfinance banks have therefore become the main source of funding micro enterprises in Africa and in other developing regions (Iganiga 2008).

Kimotha, (2005) defined microfinance simply as the provision of very small loans (micro credit) to the poor, to help them engage in new productive business activities and/or to grow/ expand existing ones. However, overtime, microfinance has come to include a broader range of services. These include mainly credit, savings opportunities, insurance and money transfer, as practitioners came to realize that the poor, who lacked access to traditional formal financial institution, needed and required a variety of financial products to achieve meaningful improvement in their business activities. While microfinance refers to loans, savings opportunities, insurance, money transfers and other financial products targeted at the poor, micro-credit refers specially to small loans. The average loan size varies from country to country. Microfinance is acknowledged as one of the prime strategies to achieve the Millennium Development Goals (MDGs). Access to sustainable financial services enables owners of micro enterprises to finance income, build assets (Haddad et al., 1997) and reduce their vulnerability to external shocks. Access to financial services enables poor households to move from everyday for survival to planning for the future, investing in better nutrition, their children's education and health and empowering women socially (Ehigiamusoe, 2005). The use of microfinance as a major strategy for poverty reduction in developing countries, which includes Nigeria, is increasingly being perceived as an effective tool for rural poverty reduction among the farmers. Indeed, microfinance has become one of the crucial driving mechanisms towards achieving the Millennium Development Goals (MDGs), especially concerning the target of halving extreme poverty and hunger by 2015 (Fernando, 2004).

Microfinance bank are supposed to play significant role in the development of the nation's economy especially in the area of providing credits , deposits and other financial services to community members especially farmers for agricultural and economic pursuits. They are placed in a better position than other credit (financial) sources because they give soft loans on the basis of member's self recognition and credit worthiness under favourable condition and enforce repayment as scheduled. An investigation into the financing of agricultural production in the study area will lead to the knowledge of whether microfinance banks in the study area are performing their primary objectives in financing or not. It will also lead to the identification of the factors that are hindering farmers from getting enough financing resources from Microfinance banks.

The problems therefore is that, it is not known if enough credits/loans is being given out to members for agricultural production pursuits, to what degree have funding from microfinance banks been devoted to agriculture, if farmers actually use such credits/ loans collected for proposed projects, and how often do they repay such loans at the due date. It is against this backdrop that the study aims to investigate the prospect, performance and constraints of microfinance banks in relation to agro-allied small and medium scale enterprises in Ijebu-North Local Government Area of Ogun State.

METHODOLOGY

The study was conducted in Ijebu-North Local Government Area (INLGA) of Ogun State, Nigeria. The INLGA is located between latitude 6^0 55^1 and 7^0N and between longitude 3^0 45^1 and 4_0 05^1E. The study area is one of the six local government areas that form Ijebu division of Ogun State. The economic activities of the people of the division vary from farming to trading and civil service, with farming being the most dominant activity. The conductive climatic condition and physical environment have been generally supportive to farming as reflected in the variety and quantity of crops grown in the area. Common crops like maize, rice, cassava, yam, palm kernel are grown in the areas with sizable number of agro-allied industries. Operators of the entire five microfinance banks in Ijebu North Local Government Area (INLGA) of Ogun State, Nigeria were used for the study. Data were collected through structured questionnaires and interview schedule. The data were analyzed using descriptive statistics such as bar chart, pie charts, frequency distribution and percentage.

RESULTS AND DISCUSSION

Loan schemes operated by microfinance banks

From the result as revealed in table 1, microfinance banks in the study area operated different types of loan scheme. Specifically, the loan scheme covered micro credit (22.7%), overdraft (18.2%), credit to SMEs (18.2%) and customers involved in bulk purchases (9.1%). Others areas of interest od the MB included micro credit to daily contributors (9.1%), equipment leasing operators (9.1%) and civil servants (13.6%). Going by the categories of enterprises and people covered, the result is indicative of MB operations targeted at the poor. It therefore gives credence to the fact that microfinance has the capacity to reduce poverty by providing efficient, effective and sustainable financial services to poor households who are otherwise excluded from the formal banking system for lack of collateral. However, the availability of the various credit services in the banks does not mean that all categories of people, particularly the farmers have access to them. Banks' preference is an important factor that determines the usage of available facilities. Table 1 shows the banking services in percentages as preferred by the microfinance banks. The table reveals that the banks preferred microcredit service (22.7%). This may be due to the fact that the service tends to give them the highest rate of return as against bulk purchase service, daily contribution and equipment leasing facilities, each of which accounted for 9.1% that were less preferred.

Table 1: Preference of services by microfinance banks

Loan Schemes	Percentage
Micro Credit	22.7
SME Loan	18.2
Bulk purchase	9.1
Overdraft	18.2
Equipment leasing	9.1
Civil Service	13.6
Daily Contribution	9.1
Total	100

Source: field survey, 2009.

Sources of funds available to microfinance banks

Figure 1 reveals microfinance banks generate their funds from four various sources besides their owners' capital outlay. The four sources are Central Bank of Nigeria, Commercial Banks, members deposits and other sources. From the graph, members' deposit remained the main source of fund with a value of 49.1%. This may be due to the fact that members deposits perhaps remain the only source of fund that comes from efforts of employed staff members of MB who work on target for the banks. Fund from CBN and commercial banks attract interest rates, which may not favour the MB.

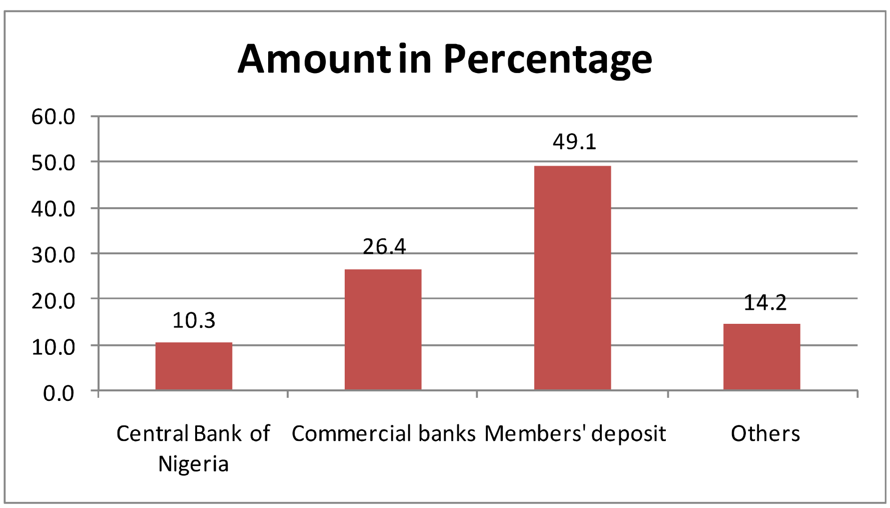

Figure 1: Sources of funds available to microfinance banks

Microfinance banks performance

The loan performance of the microfinance banks were assessed based on the level of loan application, amount granted, repaid and the amount defaulted. The study revealed improved performance from 2007 to 2008 in terms of amount repaid and amount defaulted as shown in Figure 2. The figure revealed that there was about 12% decrease in the amount defaulted from 2007 to 2008 while the amount repaid rose from about 10% within the same period. However, the amount granted reduced by about 8%. The various factors affecting the performance of microfinance banks in grating loan to investors were examined. The factors identified are interest rate, loan duration, preference to agricultural enterprise, poor working capital, protocol and bureaucracy among others. The implications of these socio-economic factors on the development of agriculture are discussed.

1. In other for the microfinance banks to meet up with their economic goal of profit making; they raise their interest rate which is so exorbitant for peasant farmers who only work on small portion of land. The loan duration given by the microfinance banks are not suitable for some agricultural enterprises that span across 12 months. Most microfinance offers between 12% - 35% interest rate on 6 months and between 22% - 30% interest rate on 12 months loan duration. With these interest rates, small and medium scale investors would not be able to afford it, and if they applied the consequence will be high loan default. In addition, the loan duration is too short for some agricultural enterprises. High interest rates may reflect high default rates or high costs associated with screening and monitoring loans. At the same time, imperfect information may give rise to imperfect competition, thereby providing lenders an opportunity to exploit borrowers.
2. The preference that microfinance banks attached to various agricultural enterprises is a factor that also affects microfinance performance in the area of agriculture. The profitability index of the agricultural enterprise coupled with their rate of return and their yield duration are some of the factors used by microfinance banks to rate these agricultural enterprises before granting loan. Fish farming is ranked as the highest profitable farming enterprise followed by poultry and piggery business (Figure 3). Microfinance banks are reluctant to give loan to farmers practicing the less preferred agricultural enterprises.
3. The internal constraints that affect microfinance banks loan availability for agricultural production are bureaucracy, collateral assessment and poor working capital. Collateral assessment and poor working capital are the major internal problems that hinder the bank from effectively giving credit facilities to the agricultural sector. Borrowers will experience unnecessary delay in obtaining loan from the financial institution because of the internal constraints and this might affect the farmers production if the loans are not released as at when due.

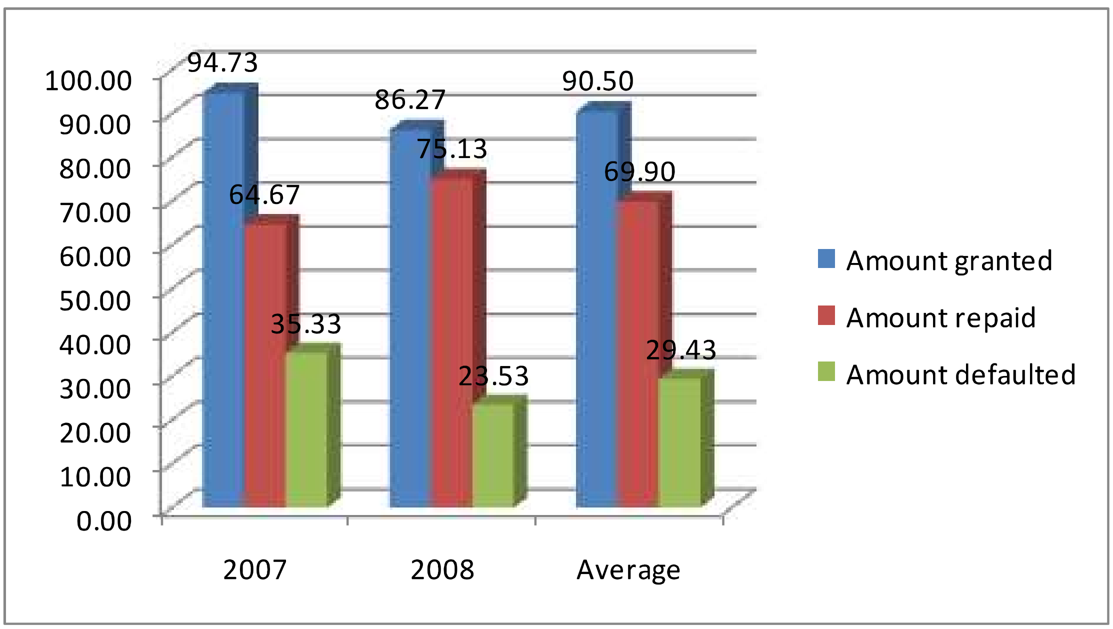

Figure 2. Performance of microfinance banks (in percentage)

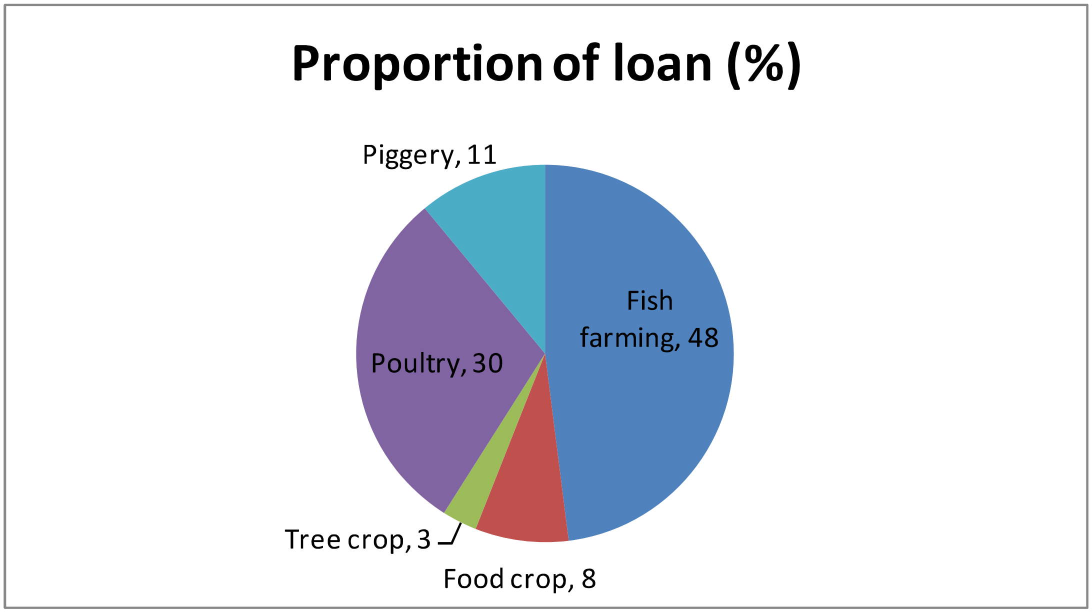

Figure 3: Proportion of agricultural loan given to farming enterprise.

Constraints to agro-allied enterprise financing by microfinance banks

To achieve sustainable microfinancing, microfinance banks must address the following constraints.

1. In adequate awareness campaigns and supports by the regulators. This suggests that there is need for continuous campaigns to all stakeholders; investors, universal banks, the banking public, the micro targeted poor and low-medium scale entrepreneurs until the micro banking ideas sink in the society and gets well accepted.
2. Lack of smallholders' trust toward microfinance banks: From the antecedents of banking industry in Nigeria, small scale investors/farmers lack trust in financial institutions. They have the perception that microfinance banks are just like the unregulated community banks and finance houses. Only effective and far-reaching campaigns and exhibited trust in the microfinance banks by the government and the regulators can achieve this desirable confidence.
3. Poor buy-ins and competitive approaches by the State Governments and Local Governments. The policy direction towards the millennium development goals is that one percent of the annual votes of the State and Local Governments should be channelled to.
4. Government involvements in microfinance banking would be counterproductive as they should concern themselves with policy formulation and control rather than implementation. Nigerian Microfinance banks have what it takes to manage micro funds for states and international bodies and should be given the chance to do so under strict supervision and controls.
5. De-marketing activities and unhealthy competition by the commercial banks: Some of these banks rather than complement the activities of microfinance banks for the general development of our country, discredit micro finance banks to the governments, donor agencies, investors and customers by painting pictures of instability, unsustainability, poor capitalization etc to the vulnerable micro-clients and potential investors.
6. Poor correspondence banking attitudes by correspondence banks: In view of the unhealthy competition rather than co-operation that should exist, correspondence banks are hardly supportive of Microfinance banks.
7. Poor structuring of some MFB's due to cheap inexperienced staff and poor operational facilities. The CBN needs to ensure that the minimum qualification and minimum experience specified for microfinance bank operators are upheld at all times. This is the only way industrial confidence and sanitization may be achieved.

Prospects and ways forward for result-oriented microfinance banks

The extent of poverty and the importance of the rural sector to the economy make it a pivotal for microfinance interventions. Poverty in Nigeria is predominantly a rural phenomenon, and it is high among self-employed households cultivating agricultural crops, this serve as an indicator for microfinance bank prospects in Nigeria. Prevalence of micro business in Nigeria is also an indicator for the survival of Microfinance bank in Nigeria. Other less important indicators are savings habit, capital base, government regulation and grassroots operation. For effective and result oriented microfinancing, the following are proposed.

1. The built up SMEEIS reserves in universal banks should be invested in or through Microfinance banks as equity, seed funds or low interest loans for on-lending to the poor and SME's. The vision behind the creation of SMEEIS must not be allowed to die until the MDG goals are actualized in Nigeria.
2. Extensive campaigns should be carried by CBN and NDIC to assure the public that MFB's are highly regulated and safe banking institutions. This should engender the investor's interest and the active poor confidence in Micro banking.
3. Strengthening and streamlining of policy that redefines operational areas for universal banks such as both to protect the young MFB industry and strengthen their operations. The idea of State and local governments dealing with mega banks on the 1% micro banking funds for poverty alleviation seems counterproductive to the microfinance industry.
4. Minimum professional qualification and banking experience already instituted by the CBN for key micro bankers and directors should be strictly and stringently adhered to and maintained by the regulators.
5. Training and development functions of the MFB's for their staff and clients should be supported by the regulators and all strata of government as well as big brothers-the correspondence banks.

CONCLUSION

Microfinance banks through various activities could affect farmers' productivity. Some agricultural enterprises are not favoured by these microfinance banks due to some factors which among others are: production period, rate of return and the profitability index. Microfinance banks interest rate and loan duration period are major constraints to these farmers in procuring loan. One of the finance policies operated by the microfinance banks is to generate profit within a very short period in order to meet their shareholders demand and keep them in existence; however, this is not suitable for some agricultural enterprises. The existence of microfinance banks in increasing agricultural productivity is perceived as an effective tool in promoting agro-allied enterprises.

Based on the findings, the following recommendations are given:

1. Microfinance banks should ensure prompt approval and timely disbursement of loans to farmers. The duration of agricultural loan should be based on the time it will take for the project to mature.
2. Farmers should be educated and enlightened on the need to seek for external funding. This can be achieved by organizing seminars for the farmers. Here they are also educated on how to ensure the productive use of the loan they provide.
3. Microfinance bank should assist farmers in procuring agricultural inputs like improved seed varieties, fertilizer, insecticides/pesticides etc. i.e. give loans in kind so as to reduce possibility of cash loan diversion.
4. Microfinance banks should intensify their methods of loan supervision to ensure prompt repayment.
5. Government should review the interest rate downward for agricultural loan. This will encourage more farmers to apply for loan.
6. Government should ensure adequate funding of microfinance banks so that they will be able to meet their financial obligations to community members.

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