

New Vista Opens in Banking for the Poor

Bola Fajemirokun

Dr. Fajemirokun, Executive Director, Development Initiatives Network (DIN), is an Ashoka Fellow. DIN is implementing in Nigeria the Financial Literacy for Micro, Small and Medium Enterprises (MSMEs) with the support of the Ford Foundation.

In common with many countries that celebrated the declaration by the United Nations of 2005 as the International Year of Microcredit, the Federal Government signalled its commitment to bringing about a more inclusive financial sector by launching in December 2005, policy and institutional reforms aimed at promoting microfinance. Briefly, microcredit is the provision of small amounts of money in the form of loans to the poor or other low-income groups. Microfinance, on the other hand, has a much broader scope, as it embraces the provision of microcredit as well as other financial services such as savings/deposits, leasing, insurance and payment (funds transfer). As explained in the National Microfinance Policy, these reforms will help to facilitate the provision of stable, reliable and affordable financial services to 65% of the economically active population that are currently not being served by formal financial institutions such as the commercial banks. With the full implementation of the Policy, the expectation is that the share of microcredit out of the total credit available to the national economy will rise from 0.9% at present to at least 20% by 2020.

The major institutional change has been the commercialization of microfinance through the establishment of corporatized, shareholder-owned bodies known as microfinance banks (MFBs). Unlike the various self-help groups and NGOs that have been meeting the needs of unbanked or unserved groups, MFBs are regulated depositary institutions. This means that they are authorized to obtain deposits from the general public under the regulation and supervision of the Central Bank of Nigeria (CBN). They are also eligible for favourable tax treatment on their income and lending activities and their deposits are covered by the deposit insurance scheme of the Nigerian Deposit Insurance Corporation. Consequently, in the event of the collapse of any MFB, depositors will receive their deposits up to the statutory maximum of N50,000 and will also be entitled to share in the proceeds realized from the disposal of the assets of the failed institution. However, although the thrust of the Microfinance Policy is to ensure that microfinance is channelled through licensed MFBs, the Policy expressly recognizes the involvement of NGOs in the microfinance sector. These types of microfinance institutions (MFIs) are classified as NGO-MFIs. They can elect to transform into MFBs or set up a MFB subsidiary, if they meet the qualifying requirements. Otherwise, they can continue with their microfinance activities provided that they remain credit-only, membership-based institutions. NGO-MFIs are required to submit periodic returns to the CBN about their activities.

Segmentation of the financial sector so as to specifically address the needs of the poor and low-income groups through microfinance not only mirrors a global trend but its effectiveness in advancing social and economic development, has been affirmed by the recent award of the 2006 Nobel Peace Prize in two parts to the Grameen Bank, a Bangladesh-based MFB and Professor Mohammed Yunus, founder of the Grameen Bank. Segmentation brings with it a number of challenges at least in the short term. On the supply side, there is the attainment of the capital requirements for MFBs. For a community-based or unit bank, that is, a MFB that is licensed to operate within a single Local Government area, the capital requirement is N20 million. For a State bank, that is, a MFB that is licensed to conduct operations across a single State or the

Federal Capital Territory (FCT) as the case may be, the capital requirement is N1 billion. By the terms of the Microfinance Policy, all existing community banks, that is, banks that have been established to serve a designated catchment area, are required at the very least to transform into unit MFBs before the end of December 2007. But this is against the background that the capital requirement for community banks stands at N5 million and out of the 600 community banks whose financial statements were approved by the CBN in 2005, only 75 had up to N20 million of shareholders' funds unimpaired by losses. It is in recognition of these constraints that the CBN has announced concessions in favour of transforming community banks. First, those that have yet to meet the capital requirements for MFBs are no longer required to deposit with the CBN the shortfall. Rather, these sums can be lodged with their correspondent banks so as not to impair business operations. Secondly, transforming community banks have been granted a 100% waiver in respect of the payment of mandatory application, licensing and change of name fees.

Nevertheless, as with the CBN-directed re-capitalization exercise for commercial banks of 2004-2005, which resulted in the emergence of 25 banks from the previous 89 and the on-going re-capitalization exercise for insurance companies, which is billed to end in February 2007, there will have to be a substantial re-organization of community banks because the injection of additional capital from existing shareholders may not be adequate or even possible in some cases. Therefore, what is likely to happen is that there will be mergers of community banks or community banks and other financial institutions or NGO-MFIs. This is in addition to the outright acquisition of community banks by new investors. With a view to boosting private capital injection from both foreign and domestic sources, the CBN has introduced a supplementary instrument to the Microfinance Policy. This is the Regulatory and Supervisory Frameworks for MFBs in Nigeria, which sets out detailed guidelines and practices for controlling the operational risks and eliminating the barriers faced by MFBs. Community banks that fail to achieve the new capital requirements by the December 2007 deadline will have to cease operations, return depositors' funds and have their operating licenses cancelled by the CBN. So far, the CBN has granted approvals to operate as MFBs to Accion MFB, Lagos; First Global MFB, Port Harcourt, Rivers State; Integrated MFB, Lagos; MIC MFB, Lagos; Mustasons MFB, Lagos; Osun State College of Technology (OSCT), Esa Oke, Osun State; Susu MFB, Lagos and Wize Trade MFB, Lagos. With the exception of OSCT and First Global, these MFBs are concentrated in Lagos. This is a reflection of the primacy of Lagos as a commercial and industrial centre as the city-state accounts for 60%-70% of the commercial and industrial activities in Nigeria. However, the successful implementation of the Microfinance Policy must lead to the accessibility to and availability of MFBs right across the country. Therefore, the reasonable expectation is that subsequent approvals by the CBN will facilitate MFB coverage nationwide.

Other operational challenges on the supply side relate to the need for MFBs to utilize advances in information and communications technology so as to achieve scale and efficiency in their operations. MFBs have to also address competition from other actors in the financial sector. By way of illustration, some commercial banks are electing not to set up separate MFB subsidiaries but they are providing microfinance products through existing branch networks and infrastructure. This is permitted under the terms of the Microfinance Policy although such banks are required to coordinate their microfinance activities through dedicated departments, comply with the Regulatory and Supervisory Frameworks for MFBs and submit quarterly returns to the CBN of their microfinance activities separate from other lending activities. It is

also important to point out that with the imminent shake-up of consumer credit through the proposed introduction in early 2007 of a new National Policy on Consumer Credit, MFBs will face competition in the provision of consumer credit from new entrants in that sector. Consequently, remaining competitive and reducing operational costs means that MFBs will need to deliver convenient, flexible and affordable products and services that are in tune with the diverse needs of their target customers. They will necessarily have to take advantage of the internet, mobile telecommunications and electronic (cashless) banking involving the use of, among others, smart cards, point of sale (POS) devices and automatic teller machines (ATMs). Already, electronic banking has witnessed tremendous growth in Nigeria and this is likely to continue. For example, with regards to the value of ATM transactions, the CBN estimates that it increased to N17.3 billion in 2005 from N1.20 billion in 2003. In terms of volume, this was an increase to 3,489,845 transactions in 2005 from 240,192 in 2003. For POS devices, the value of transactions was N41,334 billion in 2005 compared to N49,621 billion in 2003. However, this corresponded to 1,063,915 transactions in 2005, a huge increase from only 887 in 2003.

On the demand side, it is instructive that Bangladesh with a population of 140 million (the same as Nigeria) has 18 million microfinance borrowers. In contrast, formal MFIs in Nigeria serve less than one million. According to the CBN, at least 40 million may require their services. It is therefore crucial to familiarize unbanked or unserved groups with the operations and services of MFBs so that there is a high uptake based on a proper understanding of how MFBs can help to advance business, professional, household and personal goals. This can be achieved through financial literacy programmes, which also raise awareness of consumer rights. This is necessary given that many promoters or owners of micro and small enterprises in particular have little or no formal education and are more familiar with informal microfinance arrangements, which are typically group-based and lacking in formalities. Since September 2006, Development Initiatives Network (DIN), a Lagos-based NGO has been implementing nationwide with the support of the Ford Foundation, the Financial Literacy for Micro, Small and Medium Enterprises (MSMEs) Project. The aim is to widely disseminate practical information about the microfinance sector, in particular the operations and services of MFBs, so as to promote efficiencies in the running of MSMEs and in this way advance entrepreneurship development and income creation. The Project is still in its early stages but so far over 200 MSMEs in locations such as Lagos, Calabar, Ibadan and Abuja, have taken part in surveys carried out by DIN to assess awareness and understanding of microfinance practices, the emergence of MFBs and expectations on microfinance provision. Further surveys will be carried out during 2007 in the following commercial hubs: Aba, Makurdi, Kano and Ilorin. In addition, due to the emphasis on active learning, DIN has begun to facilitate meetings and discussions between MFBs and representative groups within local communities. The first of such collaborations with MIC MFB culminated in a stakeholder forum involving 70 members of the National Association of Market Traders and Leaders. This took place in December 2006 at Ikorodu, a major urban centre in Lagos State. More stakeholder meetings are planned for other locations during 2007. By project end in early 2008, DIN will also have introduced toolkits and information resources in English as well as local languages to help to improve the capacities of MSMEs to benefit from the opportunities presented by MFBs and generally improve business planning and practices. In conclusion, the implementation of the National Microfinance Policy, presents an important opportunity for social entrepreneurs to translate commitments to

poverty reduction into action. Whether working on the supply or demand side, financial literacy needs to be widely promoted. This is an issue that will become increasingly important with the anticipated growth of microfinance in Nigeria, more competition within the sector and with the introduction of new practices such as electronic banking.

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