PRACTICAL CHALLENGES OF RURAL AND MICRO FINANCE INSTITUTIONS IN GHANA IMPLICATION FOR DEVELOPMENT AND PERFORMANCE OF THE INDUSTRY THE CASE STUDY OF AVENOR RURAL BANK

Gladstone Stanley is currently Monitoring and Statistics Officer in Ghana Education Service, Ghana, PH - +233543029089. Email: gladstanley@gmail.com

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Bank of Ghana, Customers, Micro credit, Rural and Community Banks, Performance, Rural Bank and Micro Finance Institution

Abstract
This article sought to assess how microcredit is managed in Avenor Rural Bank. It also examined whether the performance of micro loan was in line with Bank of Ghana benchmark. Additionally, it examined the criteria used in identifying creditworthy clients, the effectiveness of the loan disbursement procedures, the extent to which the banks educate and supervise the customers and problems encountered in recovering bank loans granted.

1 Introduction
The allocation of resources over the past year has been concentrated in the major cities and urban centers to the neglect of most rural areas. Hence, the poverty situation in rural Ghana is serious. This has fueled the rate of rural-urban migration with its associated problems. The poverty situation in Ghana has caught the attention of successive governments in Ghana as well as non-governmental organizations (NGOs) to resource the rural folks. Ghana has over the years used rural banks as a conduit to channel aid funds to defined targets. Some of the schemes are Rural Enterprise Project (REP), Smallholder Credit Input, Supply and Marketing Project (SCIMP), Land Conservation and Rehabilitation Project (LACOSERP), Community Investment Fund (CIF), Food and Agriculture Budgetary Support (FABS) etc.

Before the establishment of the first rural bank in Ghana in 1976, the existing formal banking system—owned and managed by expatriates—was usually located in big buildings on the high streets of the major towns which essentially catered for the needs of the government, the big external trading firms, some literate wealthy Ghanaians and some senior civil servants (Asiedu-Mante, 2011). According to Asiedu-Mante majority of Ghanaian, non-literately and less affluent, feared to step foot in those building and had virtually
no access to institutional credit and other banking facilities. Most Ghanaians were at the mercy of moneylenders who charged outrageous interest rates. In the history of microfinance, Microfinance Institutions have been the first to identify the vast under-served demand for microcredit in developing countries, develop methodologies for delivering small loans, and begin credit programs for the poor and recovering (Delfiner et al. 2007).

Rural Banking in Ghana takes its origin from the early 1970s. Prior to that period, the main operators in the rural financial market comprised branches of commercial banks, credit unions, as well as other entities in informal sectors such as moneylenders, traders, and susu collectors (Asiedu-Mante 2011). The traditional commercial banks failed to betracted to the rural sector because they believed that the rural folk were mostly of the low-income group, and were scattered over wide and almost inaccessible areas. This coupled with the fact that such rural poor could not provide the required collateral to support effective commercial financial operations, served as a disincentive to the commercial banks. Since 1976, the number of registered rural banks in the country has grown to 135 (BOG, 2011).

Avenor Rural Bank was established in 1982. This was in response to the need and concern to make institutional credit and other formal financial and banking services easily available to the people of Akatsi and its environs. It has its headquarters at Akatsi South District in the Volta Region. The main purpose of its inception was to help the habit of saving into the rural folk with its catchment area so as to alleviate poverty by granting credit to the people. Today, the bank has five (5) agencies in the Volta Region of Ghana. The operations of the bank are mainly focused on income generating activities by advancing loans to its customers, especially women, to help them start businesses on their own.

In an article titled “Rural Bank in Ghana collapsing” (Ampah 2010) indicated that rural banks in Ghana are grappling with huge challenges in managing their loan loss reserves due to bad loans and poor management systems supplied by the banks. As a result, majority of these Rural and Community Banks have been rendered insolvent and could soon fold up if austerity measures were not taken to reverse the trend. The article indicated that the poor performance of these banks stemmed from both unfavorable operating environment and capacity constraints. Rural banks have unfavorable environment to mobilize scattered rural incomes at a high cost of savings, and lend to the people with virtually no collateral to support such credits. It, therefore, imperative to put in place legitimate policies and procedures that will ensure among other things that:

I. The proper authorities grant credit;
II. Credit goes to the right people;
III. Credit is granted for productive activities;
IV. The appropriate size of credit is granted;
V. Credit is used for the purpose for which it was granted;
VI. Credit granted is fully recovered;
VII. There is adequate flow of management information within the organization to monitor each credit activity.

2 Literature Review
2.1 Definition of Microcredit
Microcredit is recognized as the practice of offering small, collateral-free loans to members of cooperatives who otherwise would not have access to the capital necessary to begin small businesses (Hossain, 2002). According to Yunus (1998), credit should not be seen as a luxury for the rich, it should be an opportunity for all – “Just like food is; credit is a human right. It’s not people who aren’t credit-worthy. Its banksthose aren’t ‘people-worthy’.

2.2 Models of Microfinance
Microfinance since its inception has evolved in different parts of the world, where the poor experienced different needs, political, sanitary, and environmental concerns. Various Entities have been set up to provide support to the booming industry, considering just 1% growing at 28% to 47% from 2003 to 2007 in loan disbursements. There are two general forms of microfinance models. The first is the Indian microfinance model that was started by Prof. Muhammad Yunus, winner of Nobel Peace...
Prize 2006. The next is the Latin American Model that emerged due to the variation in demographics of the Latin American compared to Asian regions.

2.3 Source of Finance for Microfinance Institution

Microenterprises generally cover their initial capital needs with the entrepreneur's own financial means and short-term credits from banks and suppliers. As a consequence, they have high debt-equity gearing ratios and low liquidity (OECD, 2003). Equity is provided by personal means or by contributions of informal finance from friends and family. Seed and early stage Venture Capital financing is available only for innovative startups with high growth potential. In addition, many entrepreneurs do not seek such investment because it may entail dilution of their ownership.

The various forms of debt finance remain the main source of external finance for microfinance (Berger & Udell, 1998).

2.4 Credit Management

Credit Management refers to the efficient blending of the four major credit policy variables to ensure prompt collection of loans granted to customers and at the same time boost their confidence in and loyalty to the bank (Van Horne, 1995).

I. Assessment of the credit culture,
II. Portfolio objectives and risk tolerance limits,
III. Management information systems,
IV. Portfolio segmentation and risk diversification objectives,
V. Analysis of loans originated by other lenders,
VI. Aggregate policy and underwriting exception systems,
VII. Stress testing portfolios,
VIII. Independent and effective control functions,
IX. Analysis of portfolio risk/reward trade-offs

2.5 Principle of Lending

Gaurav (2010) identified general principles of good lending which every banker follows when appraising an advance proposal as follows:

I. Safety
II. Liquidity
III. Purpose
IV. Profitability
V. Security
VI. Spread
VII. National Interest, Suitability

2.6 Credit appraisal techniques

Guidelines for Commercial Banks for Pakistan Banks indicated that banks must operate within a sound and well-defined criteria for new credits as well as the expansion of existing credits. Credits should be extended within the target markets and lending strategy of the institution. Before allowing a credit facility, the bank must make an assessment of risk profile of the customer/transaction. This may include:

a) Credit assessment of the borrower's industry, and macro-economic factors.

b) The purpose of credit and source of repayment.

c) The track record / repayment history of the borrower.

d) Assess/evaluate the repayment capacity of the borrower.

e) The proposed terms and conditions and covenants.
f) Adequacy and enforceability of collaterals.

g) Approval from appropriate authority

2.7 Loan policy

Guidelines for Commercial Banks for Pakistan Banks indicated that each loan policy of the bank should develop and establish credit policies and credit administration procedures as a part of overall credit risk management framework and get those approved from board. Such policies and procedures shall provide guidance to the staff on various types of lending including corporate, SME, consumer, agriculture, etc. At minimum, the policy should include:

a) Detailed and formalized credit evaluation/appraisal process.

b) Credit approval authority at various hierarchy levels including authority for approving exceptions.

c) Risk identification, measurement, monitoring and control

d) Risk acceptance criteria

e) Credit origination and credit administration and loan documentation procedures

f) Roles and responsibilities of units/staff involved in origination and management of credit.

g) Guidelines on management of problem loans.

2.8 Credit Administration

Guidelines for Commercial Banks for Pakistan Banks (2010) indicated that ongoing administration of the credit portfolio is an essential part of the credit process. Credit administration function is basically a back office activity that supports and controls extension and maintenance of credit. A typical credit administration unit performs the following functions:

a. Documentation

b. Credit Disbursement

c. Credit monitoring.

d. Loan Repayment

e. Maintenance of Credit Files

f. Collateral and Security Documents

2.9 Loan monitoring

Credit risk monitoring refers to the continuous monitoring of individual credits inclusive of Off-Balance sheet exposures to obligors as well as overall credit portfolio of the bank. According to the Guidelines for Commercial Banks for Pakistan Banks, Banks need to enunciate a system that enables them to monitor the quality of the credit portfolio on a day-to-day basis and take remedial measures as and when necessary. Such a system would enable banks to ascertain whether loans are being serviced as per facility terms, the adequacy of provisions, the overall risk profile is within limits established by management and compliance of regulatory limits. Establishing an efficient and effective credit monitoring system would help senior management to monitor the overall quality of the total credit portfolio and its trends. Consequently, the management could fine-tune or reassess its credit strategy/policy accordingly before encountering any major setback. The bank's credit policy should explicitly provide procedural guidelines relating to credit risk monitoring. At the minimum, it should lay down procedures relating to:
Impact of Microfinance on the Rural Economy

The introduction of microfinance has in many ways impacted on the rural economy and brought about many changes in agriculture, rural housing, women empowerment and savings, reduction in vulnerability of the poor to adverse circumstances, increased household consumption and reduced income poverty. The development of the agriculture sector in many economies has been recognized as very important in attempting to reduce rural poverty. It requires the infusion of capital into the rural economy to enhance its capacity to acquire the needed technology to enhance production. In countries such as Ghana, Uganda, and Bolivia, where agricultural development is central to rural poverty reduction, there has been a renewed interest in finding the best ways to provide financial intermediation that would ensure sufficient supply of funds to the sector. Since most conventional banking institutions are traditionally very reluctant to enter the agriculture sector, microfinance institutions have emerged to fill the void.

To mitigate these problems, many Rural and Community Banks have been encouraged by successive Ghanaian governments to establish branches in the rural areas to provide financial intermediation to these poor rural dwellers that are mostly into agriculture. The availability of microfinance facilities also enables these farmers and fishermen to better negotiate business arrangements with buyers and processors as they no longer depend on these buyers for credit to do their business.

The poor are generally vulnerable to changing circumstances and microfinance helps reduce their vulnerability. Microfinance helps borrowers reduce their vulnerability against adverse circumstances by building up household assets. These can be disposed of if necessary to raise funds in times of hardships. These assets can also be used as security when they also seek credit from more conventional financial institutions.

3 Data Analysis and Discussion of Results

3.1 Source of data

The primary source of data collection was employed through the use of questionnaires. The researcher used both quantitative and qualitative methods of data collection to gather the data. With the help of the credit officers of the bank, the loan customers were interviewed through the questionnaires as they go for their normal monitoring. The researcher gave the questionnaire to the Board of Directors and the staff for their response. The purpose of these techniques was to allow discussion and probing to ascertain micro-credit management at the bank.

Secondary data was obtained from documentary sources such as books, journals, newspapers, reports, articles and other research related to this study. These sources were very useful in the literature review about micro-credit management. The literature reviewed served as both theoretical and empirical base for the analysis of the data collected.

3.2 Sample

Purposive sampling and accidental sampling techniques were used for this study. The purposive sampling allowed the picking of interview objects that fit the focus of the study (Osuala, 2001). Also, according to Kumekpor (1989) and Mensah (1997), with the purposive sampling, the sample units are selected not based on random procedure but intentionally selected for the study. This is based...
onthefactthattheyhavecertaincharacteristicsthatssuitthestudyorbecaus eofcertainqualities they possess, which are not randomly distributed in the universe but necessary for the study. The sample size was 220.

Table 4.11 Correlation matrix of Appraisal factors and policy factors and impact of the loans

<table>
<thead>
<tr>
<th></th>
<th>Pearson Correlation</th>
<th>Appraisal factors</th>
<th>Policy factors</th>
<th>Loan's boost of customer's activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appraisal factors</td>
<td>Correlation</td>
<td>1</td>
<td>.785**</td>
<td>-.322</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.001</td>
<td>.208</td>
<td>Sig. (2-tailed)</td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>17</td>
<td>14</td>
<td>17</td>
<td></td>
</tr>
<tr>
<td>Policy factors</td>
<td>Correlation</td>
<td>Correlation</td>
<td>Correlation</td>
<td>Correlation</td>
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<td>.785**</td>
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<td>Loan's boost of</td>
<td>Correlation</td>
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<td>customer's</td>
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<tr>
<td>activities</td>
<td>-.322</td>
<td>-.322</td>
<td>-.322</td>
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<tr>
<td>.149</td>
<td>.149</td>
<td>.149</td>
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</tbody>
</table>

**. Correlation is significant at the 0.01 level (2-tailed).

Source: Field survey, 2015

Table 4.12 Mean and Standard Deviation of Appraisal factors and policy factors

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Std. Deviation</th>
<th>Df</th>
<th>R</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appraisal factors</td>
<td>48.4706</td>
<td>10.79420</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Policy factors</td>
<td>29.5000</td>
<td>6.25033</td>
<td>17</td>
<td>.785**</td>
<td>.001</td>
</tr>
</tbody>
</table>

Source: Field survey, 2015

Table 4.8 Assessments of the loan policies

The results point out that there is a statistically significant difference between appraisal factors and policy factors. It is observed that appraisal factors score of M=48.4706, SD=10.79420 was found to be significantly different from policy factors score of M=29.5000, SD=6.25033, df=17, r value = .785/79, p value = p<.001. The p value falls within the accepted range of p<.05. This means the appraisal factors make a significant difference from policy factors. In other words, the respondents who had a higher score on the appraisal factors also had a higher score on the policy factors, while those who had a lower score on the appraisal factors had a lower score on the policy factors. This supports the assumption that the policy factors of the bank are in line with the appraisal factors.

Table 4.13 Mean and Standard Deviation of Appraisal factors and Loan’s boost of

Customer’s activities
Theresultspointsoutonthethe contrary that there is no significant difference between appraisal factors and loan's boost of customer's activities. It is observed that appraisal factors score $M=48.4706, SD=10.79420$ was not found to be significantly different from loan's boost of customer's activities score $M=1.0500, SD=.22361, df=14, r value=-.322, pvalue = p<.208$. The p-value falls outside of the accepted range of $p<.05$. This means the appraisal factors make no significant difference from the loan's boost of customer's activities. In other words, the appraisal activities did not have any influence on loan's boost of customer's activities. This does not support the notion that the bank's appraisal factors affect the loan's boost of customer's activities.

**4 Findings and Recommendations**
The following recommendations have been put across to make the research complete.

In rural areas where banks have high individual microcredit defaulting rate, group lending can improve repayment rate where the group is formed from areas with high degree of social connectedness. The most innovative lending methodologies that can be used by the bank are: group lending, social intermediation, and dynamic lending to joint-liable groups. These methodologies will solve the problem of inadequate appraisal, loan monitoring, and high default rate. Group members should have better access to information on reputation, creditworthiness of the group members and can put pressure on other members to repay the loan as the failure of any member to pay the loan will affect the whole group.

The loan policy of the bank must be customer-oriented. It must take into consideration the needs and the aspirations of the customers to come out with loan products that will be beneficial to the customer to enhance repayment.

To be able to solve the numerous problems of the bank, management must be proactive in credit delivery. Management must ensure that the bank works within advance to deposit ratio set by Bank of Ghana to be able to solve liquidity problems. The bank official must make sure that they get the necessary information about the loan customer before any credit is granted to the customer. In addition to physical assets as collateral, the bank can adopt group lending where social collateral and trust are sufficient for economically active poor to repay the loan. Again, it is recommended that customers receive the loan as and when needed to avoid possible loan diversion. As much as possible, the bank must avoid staff and board influence to allow institutional procedures to work.

To be able to meet at least 80% loan repayment requirement by Bank of Ghana, every staff of the bank must be responsible for every loan. The responsibility of loan monitoring and recovery should be every staff responsibility. The monitoring should be done on a daily basis to improve loan recovery.

Acknowledgement

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