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Research Application Summary

Strengthening micro financing for rural farmers: Evidence from SACCOs in Soroti district, Uganda

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Abstract

Micro financing has been hailed as an effective poverty alleviation and development tool. Despite its recognition, the expected benefits have not trickled down to all the beneficiaries due to several challenges. Indeed poverty alleviation and rural development can only be achieved if microfinance is effectively utilized by rural farmers. This study investigated possible solutions for strengthening micro financing among rural farmers drawing evidence from SACCOs in Soroti District, Uganda. Findings indicated that SACCOs carry out individual lending leading to limited participation of women in borrowing. Support and cooperation from family members as well as planning for credit contributed to effective utilization of credit. However this faced challenges such as high interest rates, limited training on credit utilization, and collateral requirement all of which contributed to limited participation of women in borrowing and unfavorable repayment schedules which also affected agricultural production. Therefore, strengthening micro financing requires MFIs to carry out group lending, train farmers on credit utilization and provide incentives that encourage farmers to save. The Uganda Government should also provide funds for monitoring farmer businesses in order to facilitate prompt repayment of loans.

Key words: Agricultural production, microcredit, Microfinance institutions, Uganda

Résumé

Le microfinancement a été apprécié comme un outil effectif d'allégement de la pauvreté et de développement. Malgré sa reconnaissance, les bénéfices espérés n'ont pas fourni de retombés aux bénéficiaires à cause de plusieurs défis. En effet, la réduction de la pauvreté et le développement rural peuvent être seulement atteints si la microfinance est effectivement utilisée par les agriculteurs ruraux. Cette étude, a investigué les solutions possibles pour la consolidation du microfinancement parmi les agriculteurs ruraux en montrant les preuves de SACCOs dans le district de Sororti, en Ouganda. Les résultats ont indiqué que SACCOs font des prêts individuels conduisant à la participation limitée des femmes dans les emprunts. Le soutien et la coopération des membres de la famille de même la planification pour le crédit ont contribué à une utilisation effective du crédit. Néanmoins, ceci a rencontré plusieurs défis tels que les taux élevés d'intérêts, la formation limitée sur l'utilisation du crédit, et les exigences collatérales toute chose qui a contribué à la participation limitée des femmes dans l'emprunt et les plans de remboursement

défavorables qui ont aussi affecté la production agricole. Par conséquent, le renforcement du microfinancement exige aux MFIs de faire des prêts de groupes, former les agriculteurs sur l'utilisation du crédit et de fournir des incitations qui vont motiver les agriculteurs à économiser. Le Gouvernement Ouganda devrait aussi fournir des fonds pour suivre les activités des agriculteurs dans le but de faciliter les remboursements prompts des prêts.

Mots clés: Production agricole, microcrédit, institutions de microfinance, Ouganda

Introduction

The provision of micro financial services to the poor in particular small loans has been hailed as an effective poverty alleviation and development tool. Despite the recognition, the expected benefits have not trickled down to all the beneficiaries due to several challenges (MOFPED, 2016). Microfinance is a powerful instrument for providing basic financial facilities to the rural poor, women, small and marginal farmers (Rao and Priyadarshini, 2013). Microfinance is provision of affordable financial services including deposits, loans, payment services, money transfers, insurance and accepting a wide variety of assets as collateral) and microcredit to urban, rural poor and low income households and their micro enterprises(Microfinance Policy, 2005). By 2013 about 128 people had received microcredit around the world (Rao and Priyadarshini, 2013). Provision of micro credit accelerates agricultural production and productivity (Obisesan, 2013). Furthermore, micro credit addresses the low growth rate of agricultural sector which is registered at 1.4 percent due to low production and productivity (MAAIF, 2013). Inadequate access to credit by smallholder farmers has been identified as one of the key contributing factors to poverty (Nathan *et al.,* 2004). To this end many developing countries including Uganda have been providing microcredit to the poor in the urban, rural and sub-urban areas through micro finance schemes (Wale *et al.,* 2013). However the contribution of microfinance in improving access to small loans by smallholder farmers remains questionable (Schreiner, 2002) posing several challenges (Ogujiuba *et al.*, 2013; Banerjee *et al.*, 2015; Namayengo *et al.,* 2016; Banerjee and Laurel, 2017).

Banerjee *et al.* (2015) viewed microfinance as a powerful institutional and political barrier to sustainable economic and social development and poverty reduction in the UK. They further argued that while microfinance model may well generate some narrow positive short run outcomes for few individuals, these positive outcomes are very limited in number and filled by much wider longer downsides and opportunity costs at community and national level. In Bangladesh, Banerjee and Laurel (2017) analysed the role of market based approaches to poverty reduction in developing countries and revealed that microfinance has led to increasing levels of indebtedness among impoverished communities and exacerbated economic, social and environmental vulnerabilities. According to Loubere (2016), although Microcredit schemes have been increasingly incorporated into development policies that aim to de-marginalize rural farmers, instead, these microcredit programmes reflect and reinforce the interlocking sets of unequal relationships that are the root cause of marginality and underdevelopment in China. In Sub-Saharan Africa, a study to examine the relationship the outreach and sustainability of microfinance institutions produced mixed evidence of trade- off between the depth of outreach and operational self- sustainability. Ogujiuba *et al.* (2013) argued that microfinance cannot be financially viable because small loans are too costly to administer and such lending does not permit profitability for small holder farmers in Nigeria. In Uganda, although the microfinance

institutions have registered good performance in controlling loan default, there success is still hampered by stressful weekly loan repayments, limited loan amounts, the diversions of loans to non-production activities, and weekly recovery programs without a grace period. This limits the contribution of micro finance loans to expanding micro enterprises and increasing in income of rural farmers (Namayengo *et al.,* 2016). This raises questions about the suitability of microfinance in improving the productivity of rural farmers, increasing agricultural production and alleviating poverty. Such findings provide evidence for the need for strengthening microfinance among rural farmers for the achievement of the Millennium Development goals in developing countries including Uganda.

Over the last two decades, the Government of Uganda has initiated, implemented and supported various rural credit schemes including SACCOs aimed at fighting poverty in the country and improving agricultural productivity. The main focus of these programmes has been the provision of revolving funds for micro credit to households at the grass root level (Peace, 2011). Notable examples include the Poverty Alleviation Project (PAP), Entandikwa Credit Scheme (ECS), Youth Entrepreneurship Fund - YEF (Mugabi, 2010; Peace, 2011; Muhumuza, 2013), Cooperative credit scheme (CCS), Progressive farmers loan scheme (PFLS) and Rural Farmers Credit Schemes - RFCS (Matovu and Luke, 2013; Muhumuza, 2013) were established. However, financing the poor through these rural credit schemes has been characterized by poor loan repayment rates, loan defaults and diversion of credit to non-productive purposes (Kalule, 2013; Muhumuza, 2013). Strengthening provision of microfinance services to reach the rural farmers has been in line with Poverty Eradication Programme (PEAP) of the Government of Uganda as early as 2005/2006 fiscal year (MOFPED, 2008) with particular emphasis on increasing outreach of SACCOs in rural areas. Proper utilization of loans by SACCO clients is expected to lead to significant impacts on the livelihood of the rural people. To the contrary, if loans are poorly utilized, it is not easy to realize significant impacts of loans (Kwai and Urassa, 2015). Better understanding of utilization of loans by rural households will inform policy on best ways to strengthen micro financing among rural farmers. The aim of this study was to investigate possible solutions for strengthening micro financing among rural farmers drawing evidence from SACCOs in Soroti District, Uganda. Specifically, the study investigates the socio economic characteristics of rural households, identifies factors facilitating effective utilization of credit among rural households and challenges faced by rural households in utilizing credit and suggests options for improving credit utilization among rural households. The findings from this study will inform policy on how best to strengthen micro financing among rural farmers.

Methodology

This study was conducted between January and April 2015 in Soroti District of Uganda. The study used a cross-sectional design whereby data were collected at a single point in time involving both qualitative and quantitative research approaches. This design was preferred because it enables the researcher to collect a lot of data in a short and limited time (Mugenda and Mugenda, 1999). The qualitative approach gave precise and testable expression to quantitative ideas. The population for the study comprised all SACCO members. A sampling frame of SACCOs in Soroti District was obtained from the District Commercial Officer. Eleven out of thirty SACCOs were purposively selected based on the active SACCOs that submitted monthly loan status reports to the District Commercial Officer and those that were operational. A sample size of two hundred fifty seven (257) out of 780 respondents was obtained using Krejcie and Morghan (1970)'s table for determining large sample sizes. The households were then selected using simple random sampling.

Primary data were collected using structured questionnaires with closed and open ended questions. The questionnaires essentially focused on generating information related to the socio economic characteristics of households, factors facilitating effective utilization of credit in the study area, challenges faced by households in utilizing credit and suggestions for improving credit utilization among farming households. A check list of key informants was also used to collect data. In-depth interviews were done with 13 Key informants (KIs) comprising one credit officer from each SACCO. According to Kwai and Urassa (2015) KIs are necessary to validate and complement information gathered through the questionnaires. Data were analyzed using Statistical Package for Social Science software (SPSS) version 16. Descriptive statistics were used to describe the socio economic characteristics of households, factors facilitating effective utilization of credit, challenges faced by households and suggestions for improving credit utilization.

Results and Discussion

Results show that an average member of a SACCO in Soroti was male (75.5%) with an average household size of nine members while only 24.5% were female borrowers. This indicates that women had limited access to credit most likely because of lack of collateral security. For example the manager Soroti Women SACCO explained that "With many Commercial institutions, women have been victims of not getting credit because many lacked securities, they doubt their capacity to repay loans, they dictate on them on what to use credit for, and most receive less than the credit requested for, like you may ask for 1,000,000Sh and you get 300,000 Sh. This situation makes it hard to comply with their terms of credit". This finding agrees with Ogato *et al.* (2017) who observed that female farmers had limited access to key productive resources such as credit in Ethiopia. Yet Sanyang and Huang (2008) argue that women play a critical role in development activities and poverty alleviation.

The average age of the respondents was 44 years most of whom had attained primary education (46.3%) and were married (87.8%).The major source of income reported by the households was farming (51.7%) with farmers having an average experience in farming of 18 years. This has implication in terms of repayment of loans since getting crop yield takes long time and is seasonal posing challenges in repayment of loans among rural households. The same issue was raised by Churk (2015) that majority of SACCO members depended on income from agriculture which is seasonal. The results also show that 31% of borrowers obtained credit from SACCOs while 29% got it from Village Savings and Loan Associations (VSLAs). This was mainly because SACCOs continue to offer favourable terms of credit especially lower interest rates that are favourable to households. For example a borrower from Stawode SACCO indicated that, "Requirements are fair to everyone however some special considerations are made to some members based on their openness. First our interest rate is a bit low compared to others at about 2.5% which is better than others of 10 – 25%; credit is given based on what you have saved." According to Tumwine (2015) SACCOs are supposed to encourage savings through extending loans to members at reasonable rates of interest. SACCOs are therefore important micro financing institutions for mobilization of financial resources for various development activities (Ikua, 2015).

The results in Table 1 also show that majority (91.1%) of rural households carried out individual borrowing while 8.9% borrowed as a group. This implies that rural households especially

women who lack the necessary collateral have challenges in accessing and utilizing credit from the SACCOs. However microfinance institutions place more emphasis on group borrowing to solve the requirement of collateral. This further reduces transaction costs and promotes collective responsibility of the borrowers to repay the loan (Garabi and Mwakaje, 2013). On the contrary Ibrahim and Zareba (2015) argues that continuous group lending is likely to reduce investment of credit into productive activities.

Table 1. Socio economic characteristics of rural farmers

Variable	Value
Mean age of household(Years)	43.99
Mean household size	8.73
Mean years of experience in with credit use	4.81
Mean years of experience in farming	18.38
Mean amount of loan applied for(Ushs)	889,000
Sex (in %)	
Male	75.5
Female	24.5
Educational level (in %)	
None	5.4
Primary	46.3
Secondary	30.6
Tertiary	17.7
Marital status (in %)	
Married	87.8
Single	7.5
Divorced	1.4
Widowed	3.4
Main source of income (in %)	
Farming	51.7
Livestock selling	6.1
Salaried employed	8.8
Trading/business	33.3
Source of credit (in %)	
SACCO	30.6
VSLA	29.2
Money lenders	1.6
MFIs	18.2
Friends and relatives	3.3
Commercial banks	17.1
Organization of households (in %)	
Individual borrowing	91.1
Group borrowing	8.9

Household factors that have facilitated effective utilization of credit. The most influencing factor in effective credit utilization at household level was planning for the credit (55.47%). This implies that respondents with well laid out plans for credit investment activities were more likely to utilize credit effectively.

From the in-depth interviews, it was revealed that households with well laid out plans for credit were able to retain their assets after repayment of credit. For example a male borrower from Katine SACCO explained that because they had a plan of how to use credit they were able to retain their assets. It is like one gets credit and buys boda boda so that he can remain with the motorcycle after repayment. This finding is however in contrast to Birech (2014) who found a negative relationship between investment plan and credit utilization. The second factor was support and cooperation from family members which accounted for 45.7%. This support was mainly important during repayment of credit. For instance, Joyce a female borrower from Ejoke Edeke SACCO, explained that she shared the credit funds with her husband and the children. Joyce allowed her husband to review her plan and make addition or subtraction. According to Joyce in some instances her husband squashed her idea to borrow credit on the ground that it was no economiucally viable. Another borrower from Kamuda SACCO also added that, "First if you get credit you have to agree with your spouse, even sometime the children at home because credit is not a simple matter and also you have to agree with your wife regarding how much to get. For me I agree with my wife and children at home since everyone at home in one way or another will participate in repayment". This sentiment agrees with Brown *et al.* (2009) who suggested that cooperation among household members especially regarding information sharing can improve allocation of credit in productive activities. Kwai and Urassa (2015) also reported that family members and other dependents within the household provide a source of cheap labour which enables them to earn more income and hence reduce poverty. Other factors that contribute to effective use of credit included skills in credit utilization which accounted for (19.53%), good record keeping (11.33%), diversification of businesses (10.55%) and timely access and issuing of credit (14.45%).

Table 2. Factors facilitating effective credit utilization among households

Factors facilitating utilization of credit	Frequency	Percentages
Family support and cooperation	117	45.70
Skills in credit utilization	50	19.53
Desire to grow the business	24	9.38
Planning for credit	142	55.47
Saving	5	1.95
Timely access and issuing of credit	2	
Good record keeping	29	11.33
Diversification of businesses	27	10.55
Timely access and issuing of credit	34	14.45
Multiple response		

Challenges facing households in utilizing credit from SACCOs. The reported challenges were high interest rates (27%), unfavorable repayment schedules (25%), need for collateral (23%) and limited trainings by SACCOs (20%). In-depth interviews with households revealed high interest rates being associated with 20% charge on loan amount. For example, a male borrower from Soroti Teachers SACCO explained that, "The interest rates are high hence discouraging people to use the credit.

For example conditions like paying 20% of the loan amount before loan is processed and short repayment periods continue to limit access to these financial services by the more financially vulnerable who are targeted more by the same financial institutions, thus they continue to lose property attached as collateral ". On the other hand repayment schedules were unfavorable because they were too short to favour agricultural production whose returns are usually long term. In this regard, a female borrower from Gweri SACCO also noted that, "The loan repayment period is too short because the moment you get it, you start paying as there is no grace period. This affects agricultural production whose returns are long term. For example long gestation period (maturity for crops) for me who is doing farming in planting oranges which the SACCO requirement may not meet". A SACCO staff from Gweri SACCO also added that, " There is no credit scheme for agricultural purpose because agricultural production takes a long period and its success mainly depends on weather conditions which is beyond our abilities yet we give loan now and we expect one to start repaying immediately because there is no grace period." Thus the credit model employed by the SACCOs does not favour agricultural investment because it locks the revenue that could otherwise be lent to another member and more profit obtained by the SACCO. This suggests that efforts towards strengthening micro financing need to focus on putting in place favourable terms of credit. This is in line with Ganesan (2009) argument that SACCOs need to extend financial products and services to the rural poor basing on non-exploitative terms.

Suggestions for improving credit utilization. The main suggestions to improve credit utilization at the household was reported to be through mainly monitoring credit utilization (55.9%). This agrees with Oluyombo (2013) that monitoring of loan use ensures that loans are utilized for intended purpose which eventually reduces loan default and encourages commitment among cooperative members. The need for conducting credit utilization trainings was raised by 51% of households with more emphasis on planning, accountability, credit management, credit repayment, business skills and record keeping. For example the Chairman of Soroti Mbale Stage said that, "Most importantly we need good training on credit utilization from the district commercial officer, we need to be trained on how to have a saving culture so as to ease loan repayment". A female borrower from Moruapesur Sacco indicated that there was need for community sensitization on credit utilization particularly planning, accountability, credit management and credit repayment. The Chairperson Awoja SACCO also explained that, "There is need to train borrowers in business skills, record keeping and business selection, how to benefit from the credit and how to use credit, when to borrow and how to repay the credit". According to Nawaz (2010) in Kwai and Urassa (2015), the effectiveness of microfinance poverty reduction requires the provision of other services such as skills training and education. For example, trainings on proper utilization of loans and business management enabled SACCO members to manage their loans and led to business profitability leading to timely repayment of loans (Absanto and Aikaruwa, 2013).

Table 3. Challenges faced by households in utilizing credit from SACCOs

Challenges	Percentages
High interest rates	27
It took long to obtain credit	3
Limited training on credit utilization	20
No incentives offered	4
Need for collateral	23
Corrupt credit officials	15
Unfavorable repayment schedules	25
Multiple response	

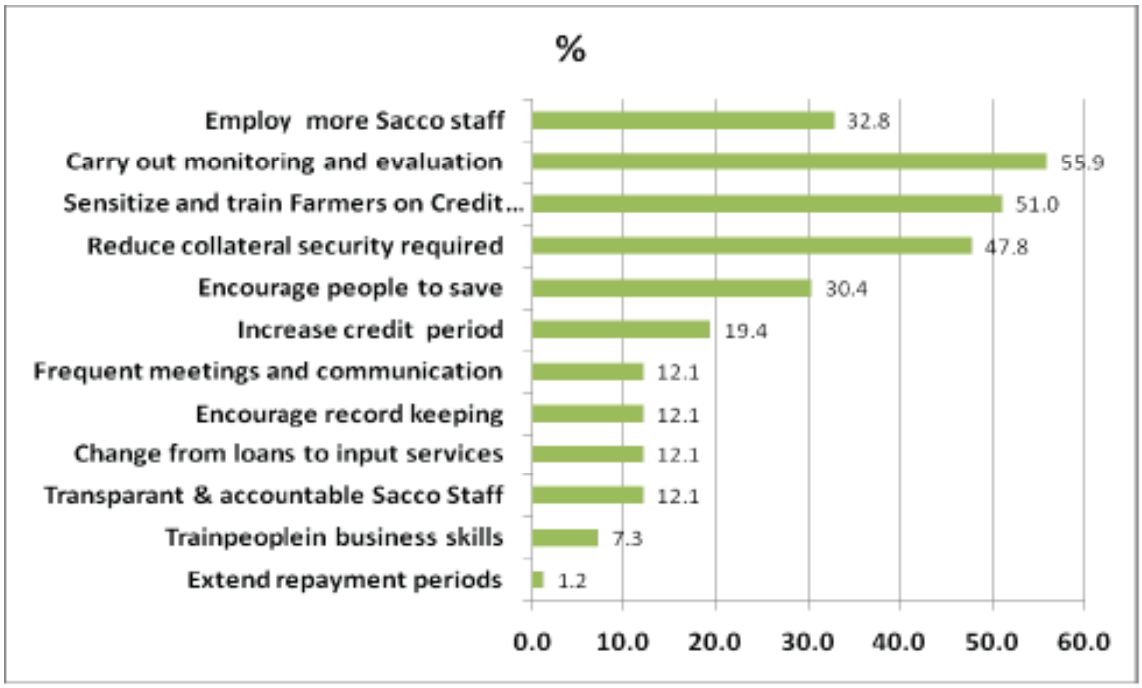

Figure1. Household suggestions for improving credit utilization

Collateral requirement still remains a major development challenge in developing countries (Tenaw and Islam, 2009). Results from this study revealed similar sentiments where 47.8% of respondents raised the need for reducing collateral as a way for improving utilization of SACCO loans. Other suggestions to improve credit utilization at household level included; employing more SACCO staff (32.8%) and encouraging people to save (30.4%). According to Ayele and Goshu (2018) savings improve access to credit and increases amounts of credit borrowed.

Conclusions and recommendations

The purpose of this study was to identify possible options for strengthening micro financing for rural farmers drawing evidence from SACCOs in Soroti District, Uganda. The findings suggest that SACCOs were mainly dominated by male borrowers, indicating a need for developing strategies and incentives that promote women inclusiveness in access and utilization of microfinance. Furthermore, majority of the households borrowed as individuals which possibly explained the low participation of women in microfinance. Major factors that facilitated effective utilization of credit included support and cooperation from family members, planning for credit utilization and repayment. Major challenges faced by households included high interest rates, limited training on credit utilization, need for collateral and unfavorable repayment schedules that mainly affected agricultural enterprises. Households also made suggestions on how to improve credit utilization and these included the need for SACCOs to carry out frequent monitoring and evaluation of businesses in which credit was provided for, training farmers on credit utilization and reducing collateral requirement. Based on the results from this study it is recommended that strategies for strengthening micro financing for rural farmers be developed in patnership with

the targeted beneficiaries. First, there is need for MFIs to carry out group lending amongst its members. This will encourage women inclusiveness in access and utilization of microfinance as well as reduce collateral requirement which is a major hindrance to women borrowers. Secondly, the Government needs to increase funding to MFIs to enable them carry out frequent monitoring and evaluation of member businesses in which credit has been invested. Thirdly, there is need to train farmers on cross cutting issues other than on only credit utilization that would include planning for credit and business skills. Fourthly, MFIs should provide incentives that encourage people to save, since saving helps farmers to access microfinance and to receive larger amounts of credit. Lastly, it is recommended that MFIs need to employ favourable repayment schedules that cater for agricultural activities whose returns take long to be obtained.

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