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Full Length Research Paper

Exploring Funding Mechanisms and Growth Challenges Facing Microfinance Institutions in Kano State, Nigeria

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This study aims to address challenges posed to Microfinance institution (MFIs) as they work to improve access to credits by poor entrepreneurs among farmers and other low resource-based individuals. This prompted this research work. A field survey, using multiphase sampling technique, was conducted to select samples for detailed analysis. Two sets of questionnaires were administered on the eleven (11) MFI decision units in Kano State, to collect information on their characteristics, financial resources and mode of operations; sources and uses of funds, resource use efficiency as well as outreach. Levels of savings of members, microloans packaged and delivered, women participation, levels of profits generated as well as returns to investments and to assets were measured. The results showed that three categories of MFIs operate in the area namely: formal finance institutions (FFIs), semi-formal finance institutions (SMFIs), and informal finance institutions (IMFI) each with its unique features and mode of operations. They share many common problems from low level of member savings, low equity levels lower than the African average in all cases and high level of borrowed funds. Though the returns indicated that average returns on assets for IMFI and SMFI ranged from 4 to 6% over the period, higher than the African average of 2% and confirms efficient use of resources, high dependence on costly borrowed funds as against savings by members may delay achievement of sustainability going by their level of dependence on subsidy. As to the main activities engaged by MFIs, petty trading ranks first followed by farming, equipment financing, livestock rearing, food and restaurant services, artisans and household wares trading respectively. With regards to problems and constraints to their growth they ranked lack of qualified staff, inadequate working capital, board decision problems, fund recovery, government policy changes, and sourcing additional funds in the fore front. Suggested solutions were made. Overall, it is evident that MFIs in Kano are profitable, efficient and could be sustainable if the identified problems and constraints are addressed by stakeholders and suggested solutions are adhered to.

Key words: Microfinance, constraints to growth, sustainability.

INTRODUCTION

Access to credit is a critical factor in development and growth of economies across the world. This is more prominent in developing nations where credit supply to a large extent, determine credit availability to the majority of entrepreneurs among farmers for procurement and adoption of improved technologies; value addition among local processors; traders, artisans, craftsmen etc.

Traditional and few formal sources together form the main sources of investible funds and identified as critical to the success of any agricultural policy goals (Gonzalez-Vega, 1997; Von Pischke, 1996; World Bank, 2007). Credit packages are meant to facilitate acquisition and use of new technologies for agricultural production, processing, and marketing for export of agro-based commodities. Credits were administered in cash or in kind through formal or informal groups. Major technological inputs acquired using such credits by farmers for instance include fertilizers, seeds/seedlings,

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irrigation equipments, mechanical services and inputs, equipment for crop or livestock production including fisheries, poultry, tree crop development as well as commodity value-added activities. The latter include processing; packaging, storage and exports. Acquisition and use of credit facilities are expected to lead to increase in production and income of beneficiaries and achievement of millennium development goals (MDGs) in view of their multiplier effect on the economy (Yunus, 2007; Laforcade et al., 2005).

The current microfinance packages designed by MFIs have in-built mechanisms to ensure broader participation among suppliers and users as well as enhance the flow of investment funds into the agricultural sector. It is claimed that commercial banks, community banks, non-governmental organizations both local and international, self-help groups, credit unions have all engaged in the provision of micro-credit in Nigeria without serious documented research on their performances and the future sustainability of their participation especially when cheap sources of subsidy fund are no longer available. This calls for an investigation into their performance. Efficiency and profitability among MFIs largely depends partly on the ability of MFIs to procure and effectively utilize cheap funds and channel them to users with minimal recovery risks, among others (Morduch, 1999; Alimi, 2000) and partly on the ability to identify and remove operational constraints. This study aims to discover the main sources of fund for MFIs and how the funds are used and finally address constraints that limit their growth in Kano State.

The main objectives of this paper is to determine the microfinance institutions involved in providing microfinance services and the constraints they face in Kano state. Specifically the objectives are to:

1) Identify the types of micro-finance institutions (MFI) and their activities in the area;
2) Identify the main sources of micro credits in the area;
3) Determine the outreach among microfinance institutions operating in the area; and
4) Identify the main constraints to the supply of micro credits in the area.

METHODOLOGY

Area of the study

Kano State was selected for this study. The choice was deliberate because all the features of the financial market are found in relative abundance in the state. Population growth rate was estimated at 2.5% per annum with population figure put at 9.6 million people as at 2006 (National Population Commission, 2010) and over 75% engaged in agricultural production or related services. Geographically, it is located within latitude 10° 35" N and 13° N and longitude 7° 40"E and 10° 35'E. It has a total land area of 43 000 km^2. Over 74% of the land is considered as arable with similar features in soil types and vegetation cover, rich and abundant rechargeable aquifers suitable for irrigated agricultural production. It has suitable and sizeable *fadama*[1] which responds well to fertilizer application.

Politically, it consists of 44 local government councils with a predominantly homogeneous population and culture (National Development Plan (NDP), 1980; Baba, 1993). It is densely populated. Kano State is richly endowed with natural resources ranging from favourable weather: good and well spread rainfall and temperature regimes, high relative humidity and suitable soil types across the state as well as substantial quantities of mineral resources in all the geopolitical zones of the state. Kano State of Nigeria is located within the northern guinea savannah with its characteristic rainfall and temperature regimes suitable for the production of a wide range of crops. As for the financial market, Kano is either a head office, zonal or branch base for almost all Commercial banks, Insurance, commodity and Stock markets institutions operating in Nigeria. It comprises of predominantly Hausa/Fulani tribe with a good presence of Yoruba, Igbo, Igala, Kanuri, Lebanese, Niger nationals and many other tribes within and outside Nigeria residing in Kano alone.

Sampling technique/data collection and analysis

The study was carried out principally in Kano financial market. To determine the size of sample a pre-survey was conducted to determine the main operators in the market. The sampling frame was made up of all financial, non financial; formal and informal microcredit institutions in the area of study. The financial market consists of Commercial Banks, Development Banks, Cooperative Societies, and Savings and Loans Associations. Self-help Groups, Credit Unions, Microfinance banks and informal lenders also exist. Each type of financial institution is represented and the actual number of operators was first determined to find those actively engaged in providing microfinance services to the clients. The following were the main category of operators in the Kano financial market:

1) Commercial banks: After the CBN consolidation exercise, 25 Banks emerged as the approved commercial banks in the country. Each of these maintains presence in Kano with most of them having at least one Branch in the metropolis. From information obtained from the Kano Branch of the Central Bank of Nigeria, all the 25 banks operate in Kano. Further inquiry on banks offering microfinance services revealed that First Bank Plc and Union Bank Plc have been identified as the two most active while most of them are yet to commence the provision of such services perhaps as wholesale providers of microfinance services. This limits our sampling frame among commercial banks to selection of only those that provide microcredit services as at the time of the study.
2) Development banks: Only two development banks operate in the Kano finance market namely Nigeria Agricultural Cooperative and Rural Development Bank (NACRBD) and Federal Mortgage Bank of Nigeria (FMBN). The latter however does not offer micro credit services both by its objectives, as well as its actual operation leaving the NACRDB as the only development bank performing this role in the market. Of course, primary mortgage institutions have taken up the challenge of engaging in providing similar services since the liberalization, consolidation and introduction of the universal banking services in the country.
3) Microfinance banks: These are recently licensed banks which pioneered the establishment of microfinance services in the country. Some were NGO based service providers while others converted from community or rural banking services MFI as required by CBN. At the time of study many were in the process of conversion; a few had just acquired the license to commence operations but only three actually started operating as MFIs.

[1] *fadama* is a Hausa word meaning area flooded during the wet season

Specifically, Madobi Community Bank converted to Freedom microfinance bank; Women Development Initiative which converted to WDI MFI; and Grassroots Health Organization of Nigeria (GHON) which was seeking registration and licensing as GHON MFI and seeking affiliation to an older MFI called Lift Above Poverty Organization (LAPO) based in Edo State. In each of these cases operations as microcredit service provider have started. In addition, some established microcredit institutions have just begun seeking to establish branches in Kano but operations have not yet started.

4) Non financial institutions: This category of microfinance service providers operate strictly to serve their members with or without profit motive. The primary purpose was to support each other and may not engage in any competitive adventure. In this category are Cooperative Societies, Self Help Groups, Savings and Loans Associations, and Rotating Savings and Credit Associations. Each of these might opt for conversion into MFIs later but at the time of the study none of them registered its intention to do so in the Kano market. This equally limit our sample selection to only operating institutions which none of these members of the group is qualified to be included.

5) Primary mortgage institutions: These are primarily financial institutions registered and licensed to provide banking services for the purpose of developing the mortgage subsector. Given the development in the nation"s financial landscape which advanced towards Universal banking, they ventured into other banking services including microcredit. Two banks were identified through surveys and searching through regulatory institutions on the functional institutions in the market. Eurobanc savings and loans and Dala Building society were already engaged in providing these services thereby qualifying them to be included in the sampling of MFI players in Kano market.

Given the aforementioned scenario, our sampling frame was made up of all the active participants in the provision of micro credit services in the financial market. After the pre-survey, the multiphase sampling technique was adopted to determine our sample. Three most active in the running of microfinance programme were selected from the 25 commercial banks that emerged after banks" restructuring and the five were found to be active in micro credit services. All informal and semi formal MFIs categories identified, totalling four each were included in the survey. The features of the participating institutions/programmes were further studied with respect to additional characteristics. In the second or main phase of the inquiry selected MFIs were categorized into three main groupings to ease collection of information. These were Formal, Semi Formal and Informal MFIs.

Data collection

Both primary and secondary data were collected from the financial institutions as well as other stakeholders involved over a three year period (2004 to 2006) as extracted from the last three years published financial statements of the institutions concerned. In addition, interviews were conducted using structured questionnaire in which detailed information on the specific aspects of the microfinance window operated by the MFIs were collected from the Chief Executives of the MFIs or their representatives.

Analytical/measurement tools used

Descriptive Statistics such as mean, range, percentage, frequency distribution, standard deviations, variance, charts and others, were used to attain objectives relating to the characteristics/behaviour of the main decision unit, the MFIs, identified their mode of operations and main sources of funding. In addition for the NGOs their purpose, mode of operations, outreach in terms of target beneficiaries, nature of supports provided, terms of repayment and as well as other peculiarities were analyzed using similar tools of analysis.

The Student „t-test" was used to determine whether SMFI and IMFI are the same with respect to level of savings and micro loans produced. The Student "t-test" was conducted using data generated from the savings records of the members of the 2 groups (SMFIs and IMFIs) over the last three years. Similarly, for the micro loans data collected was used to compare the two categories.

RESULTS/FINDINGS

Three broad categories of MFI were identified namely formal (FFI), Semi-formal(SFFI) and Informal financial institutions IFFI) each with its unique characteristics. These institutions/programs (MFI) engage in a wide range of practices across the state. Prominent operators in the area of study include Development Banks (DB), Commercial Banks (CMB), Primary Mortgage Banks (MB), Microfinance Banks (MFBs) and non-governmental organizations (NGOs). Saving and loans associations, cooperatives of whatever type, and rotating savings and credit association (ROSCA) did not participate in this survey even though records from state ministry of commerce suggest the existence of such associations. Three main categories of sources of fund for use by MFIs were identified giving rise to the financial structure. Financial structure among MFI reveal that most of them leverage on borrowed funds followed by equity funds and least on member savings as in Table 1.

Size of microloans and mode of disbursement

There is a wide gap in the size of microloans disbursed among MFIs and even within each category. FFI lend to individuals or groups from 50 000 to ₦ 250 000 per loan beneficiary. SMFI generally provide from 15,000 to ₦ 50,000 which is renewed upwards up to ₦150, 000 per active and performing client. IMFI generally start at 5,000 to ₦10, 000 but can grow to 15 to ₦ 25, 000 per beneficiary in group. The type of activity financed often dictates the size of microloan with asset acquisition attracting the highest and longest gestation period.

Outreach and depth of reach

Outreach

The combined outreach to all users by MFIs over the three year period show different levels of reach among the three categories. From Table 2 it is clear that the commercial banks extended more facilities to men than women. This skewed the results in favour of men among their micro loan beneficiaries. On the other hand both SFFI and IFI categories concentrated mainly on women,

Table 1. Proportion of equity and reserves, borrowed fund and members" savings among categories of MFIs (2004-2006).

Source of fund	Types of Microfinance Institutions (MFIs) Range in % and averages							
	FFI	Mean %	SFFI	Mean (%)	IFFI	Mean (%)	Ave.	Mean (%)
Equity and reserves	38-40	39	22-52	36	9-15	12	9-52	30
Borrowed funds	44-50	47	41-75	57	62-81	71	41-81	60
Members" savings	13-16	14	3-11	7	11-23	17	3-23	12
Total		100		100		100		100

Source: Survey Data, 2007.

Table 2. Actual numbers of men and women reached by Microfinance Institutions.

MFI	Men	Women	Total	Women(%)
FFI (NACRDB)	55,340	33,058	88,398	31
SMFI	1,230	7,120	8,350	85
IMFI	68	7,039	7,107	99
TOTAL	56,638	47,217	103,855	31

Source: Survey data, 2007.

Table 3. Total microloans disbursed by selected MFIs 2004-2006.

MFI	Naira amount in billion			Total	Disbursed to Agric sector	Percentage of Agric to total
	2004	2005	2006			
FFI	7.94	8.499	11.724	28.163	22.5304	80
SMFI	0.029	0.085	0.302	0.416	0.15808	38
IMFI	0.015	0.0483	0.0515	0.115	.0897	78
TOTAL	7.984	8.6323	12.0775	28.694	22.77818	79.38

Source: Survey data, 2007.

in fact four of the MFI deal only with women while only one MFI deals almost exclusively with men. Thus, while the average for all FFIs stands at 31%, the other two categories had over 80% women outreach. Thus, in terms of depth of reach, IFI have deeper penetration followed by SFFI and FFI is the last.

Amount disbursed

The amount of micro loans created and disbursed over the three year period showed remarkable growth from ₦ 7.984 billion in 2004 to over ₦ 22.778 billion as seen in Table 3. The agricultural sector attracted ₦ 22.77818 billion in investments through micro lending from the MFI over the period representing 79.38%. Since this is coming as a new investment there is wide scope for growth in improving access to funds by farmers.

Women participation in MFI activities

Over 80% of funds disbursed SFMFI and IMFI were made to women beneficiaries for a wide range of activities including petty trade, food and restaurant services, financing for the acquisition of capital assets among others as seen in Table 4 on activities. All the MFIs provide fund for a wide range of activities. They finance multiple enterprises simultaneously. Among the activities, petty trading tops the list followed by food vendors/restaurant services, acquisition of processing equipments for rice and groundnut; livestock rearing (including poultry), artisans, household item production, fishing etc. Out of the seven main activities, five relate directly to the agricultural sector. Specifically, farming, livestock rearing, food/restaurant services, purchase of farm produce and/or processing equipments and trading in agricultural commodities. As to the main constraints that limit the growth of MFI, the operators cited inadequate funding as the major constraints followed by lack of qualified staff, then inconsistent government policies and low working capital which together rank third. Fifth position was the board problems which led to frequent misdirection on the MFIs" policies. Loan recovery surprisingly ranked sixth which means fewer banks experience low recovery problems as shown in

Table 4. Types of activities covered by the MFIs.

Type of MFI	Farming	L/stock	Petty/ trading	Food/Rest	Artisans	Equipments	HH wares	Combination	all
NACRDB	Y	Y	Y	Y	Y	Y	Y	Y	Y
FBN	Y	Y	N	N	N	Y	N	Y	N
UBN	Y	Y	N	N	N	Y	N	Y	N
MADOBI	N	Y	Y	Y	N	Y	N	Y	N
HUDUD	Y	N	Y	Y	Y	N	N	Y	N
EURO	N	N	Y	N	N	Y	Y	Y	N
DALA	N	N	Y	N	N	Y	Y	Y	N
WOFAN	Y	Y	Y	Y	Y	N	N	Y	N
WDI	Y	Y	Y	Y	Y	Y	Y	Y	N
GHON	Y	Y	Y	N	N	N	Y	Y	N
WIA	Y	Y	Y	Y	Y	Y	N	Y	N
TOTAL	8Y,3N	8Y,3N	9Y,2N	6Y,5N	5Y,6N	8Y,3N	5Y,6N	10Y,1N	1Y

Key: Y= yes, N= No. Source: Field survey data, 2007.

Table 5. Problems encountered in administering micro finance.

Serial	Problem reported	Frequency	Percentage (%)	Ranking
01	Lack of qualified staff	8	72	2
02	Inadequate fund	7	64	3
03	Board decision and related problems	5	45	5
04	Loan recovery	3	27	6
05	Government policy changes	7	64	3
06	Sourcing additional funds	9	82	1

Source: Field survey data, 2007.

Table 6. Solutions suggested by MFI operators for identified constraints.

Serial	Problem reported	Frequency	Percentage (%)	Ranking
01	Government to provide incentives to ease implementation problems	11	100	1
02	Training of staff	10	90	2
03	Networking among practitioners	9	82	3
04	CBN to mount effective monitoring and supervision	9	82	3
05	Special Incentives and support for promising MFIs	8	72	5
06	Increase back up extension staff	7	64	6
07	Others	2	18	7

Source: Field survey, 2006.

Table 5. As to the proposed solutions, MFI operators responses are reported in Table 6 with Government active support solicited as a top priority followed by staff training, networking among practitioners etc.

CONCLUSION AND RECOMMENDATIONS

The highlights of our findings lead to the following conclusions and recommendations, among others:

1. MFIs can be effective vehicles for rural transformation and value-addition service providers, if effective support, guidance and supervision by stakeholders could be mounted. Borrowed funds which are costly seem to be the dominant sources of funding therefore cheaper sources like savings and equities and reserves could make MFIs more profitable and sustainable;
2. The commercial banks extended more facilities to men than women beneficiaries, while it is the reverse for SFFI and IFI which concentrated mainly on women with

remarkable results. Thus, future strategies to improve outreach should adopt the SFFI and IFI style of improving credit access;

3. The agricultural sector attracted ₦ 22.77818 billion in investments through micro lending from the MFIs over the period representing 79.38% of total loan issued. Since this is coming as a new investment there is wide scope for growth in improving access to funds by farmers;

4. As to the main constraints that limit the growth of MFI, the operators cited inadequate funding as the major constraint followed by lack of qualified staff, then inconsistent government policies and low working capital which together rank third. The Fifth position was the board problems which led to frequent misdirection on the MFIs‟ policies. Loan recovery surprisingly ranked sixth which means fewer banks experience low recovery problems. This reinforces the recommendation that with availability of cheaper sources of fund, more microloans could be extended to the poor entrepreneurs. Staff training and policy stability to create an enabling environment for growth are necessary support services needed by the emerging MFIs institutions to achieve sustainability.

5. Finally, it is recommended that better extension and entrepreneurial education and training be organized to sensitize farmers, processors about the potential benefits that could be achieved in setting up and operating microfinance institutions as well patronizing their services.

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