Linkages and Networking of Member-Owned Institutions (MOIs) in Remote Rural Areas

Malcolm Harper

Introduction

An in-depth study of MOIs providing financial services in remote rural areas, carried out under the direction of the Coady International Institute,[1] has identified three key drivers of successful remote outreach:

- internal governance;
- participation in networks and linkages to private suppliers, NGOs, and government; and
- regulation and supervision.

This focus note summarizes the findings on the nature and success of various linkages and networks, derived from the seven MOI cases examined within the framework of that study. The study has used the term "linkage" broadly to refer to any kind of relationship that an MOI may have with an outside institution in order to provide the services it is unable to provide on its own.

As demonstrated by the cases examined, MOIs can link or network in three ways:

- they may deal directly with market suppliers of inputs, as with a commercial bank to access liquidity or a consulting company to access technical support;
- they may create or join a second-tier structure such as a federation; and
- they may have links with bodies which support or regulate MOIs, such as NGOs or government agencies.

Linkages can be to secondary higher-tier MOIs, or to private businesses, NGOs, government bodies, or to banks which may themselves be owned by private interests, by cooperatives, or by government. The seven cases reviewed in this focus note include examples of all these linkages.

The term "network" is used in the study to describe the grouping of a number of primary-level MOIs, which can pursue a variety of purposes. For example, a network can serve as a vehicle for the exchange of information or for aggregating individual attempts to influence policy. It can also carry out financial intermediation functions and require participating MOIs to deposit part of their members' savings with it. In the latter case, a network acts like any second-tier cooperative or federation.

[1] The study, entitled "Reaching the Hard to Reach," has produced a set of publications which can be found on the Institute's website at <http://coady.stfx.ca/moi/>.

The success of any linkage is affected by the timing, nature, and origins of the inter-institutional relationship involved. Was the linkage initiated by the primary or by the secondary partner, or by some external third party, and does the secondary institution exist to serve only primary MOIs of this type or are they just one among many other types of members?

Linkages and networks also differ with regard to the services which they provide. For example, the secondary MOIs or other linkage partners may provide direct financial intermediation to its primary partners through savings and credit and access to additional external funds. They may also assist in building the capacity of member MOIs and they may provide some form of supervision to ensure the financial security of the primary groups. Furthermore, they may help "empower" the primary groups and their members.

By comparing the linkages present in the seven MOI cases from the viewpoint of their origins and the nature of the relationship and the services they provide, the study offers a comprehensive framework for examining whether these linkages are worthwhile by weighing their benefits against their costs. This analytical framework can also serve as a model for assessing the linkages and networks of other MOIs.

Guiding Questions

The study under review developed a set of questions intended to examine the costs and benefits that MOIs experience as a result of federating or using linkages to obtain needed services:

- Does it help the MOI to be financially viable, by reducing risk and/or increasing net income?
- Does it help the MOI to offer more, or better quality, services?
- Does it help the MOI to achieve broader outreach (that is, to reach more people)?
- Does it help the MOI to achieve deeper outreach (that is, to reach poorer people)?
- Does it improve the governance of the MOI?

Five of the seven primary MOIs considered in the study[2] have close links to second-tier groups or other types of institutions. Because all the secondary institutions in these five cases are also MOIs, further questions are proposed to help evaluate such "higher-level" linkages:

- Are there alternative and preferable suppliers, or could existing institutions be reformed so that they could be better sources of services for the primary MOIs than the new secondary MOIs?
- If a secondary institution serves as a "middleman" between clients and service providers, are the costs associated with this linkage justified by the additional level of services provided?
- Financial institutions should be regulated and supervised, especially when they are serving poor people with low levels of financial literacy for whom even a small loss would be very serious. Are the authorities able to supervise adequately the secondary institutions?
- The weaker members of any group typically benefit the least from membership, and enforced loyalty to a group can be a form of disempowerment and marginalization for the poor. This applies equally to federations of groups. Will the weaker members of the federation benefit as much as the larger and wealthier ones?
- In contrast to primary MOIs which can often be formed and operated by members themselves, secondary MOIs have to be promoted, their membership and staff capacity have to be built, and the cost of this process as well as the cost of continuing operation often have to be subsidized. If the case involves a secondary MOI, is this institution likely to depend on a subsidy for its start-up and continued existence?

Rather than being answered definitively within the study, these questions mainly serve to guide the readers in forming their own conclusions regarding the value of particular linkages. They can

[2] These five cases include: self-help groups in West Bengal and Andhra Pradesh in India, some village savings and loan associations in Niger, the *Mutuelles communautaires de croissances* in Cameroon, and Mixtlan savings and credit cooperative in Mexico.

also be used by members of MOIs to objectively judge the linkages they are engaged in instead of uncritically promoting or resisting them.

The Cases

Self-Help Group—Primary Agricultural Credit Society Linkage, India

This case examines the Bararanga Primary Agricultural Credit Society (PACS) in Purulia, West Bengal, linked with 85 self-help groups (SHGs) and 1,382 members, all women. The SHGs generally owe their origin to the PACS or, in some cases, to the promotional efforts of local Communist party cadres, and they use the PACS primarily as a source of loans.

Not genuine cooperatives, the PACS were originally established by the government in 1904 on a "top-down" basis, as a delivery channel for cheap credit for famine relief. This weakens their financial position and means that they have traditionally been seen as sources of "soft" money from government, rather than as community institutions for financial intermediation.

There are over 100,000 PACS in India, which is more than twice the number of commercial and regional rural bank branches. In remote areas, such as that covered by the Bararanga PACS, there is little competition either to promote SHGs or to service them once they have been formed. The PACS is therefore in a quasi-monopolistic position.

The PACS service is far from perfect. It does not allow the SHGs full use of their savings, its interest rates are higher than banks' rates, deposits are uninsured, and the PACS itself may be insufficiently liquid to provide all the SHGs with the funds they require. Yet, in other ways, its service is better than a bank would offer. The staff are accessible, locally based, and they understand the local community.

While it is most unlikely that long-established, government-backed PACS may ever be allowed to default on their obligations, the savings deposited in a PACS may not always be readily accessible. They will probably not be lost but they may be "locked in." Furthermore, in West Bengal, unlike some other Indian states, SHGs are only nominal members of the PACS, with no voting rights, and their influence on its management and governance is thus very limited.

Although the PACS are legally MOIs and are thus the obvious linkage of choice for SHGs, the actual condition of the PACS and the relative unimportance of the SHGs in business or membership terms means that the relationship with the SHGs is more like that with a private or public sector financial institution than a member-owned one.

Despite these disadvantages, the rural locations and large numbers of PACS mean that they are the best and often the only choice of service provider for SHGs in remote areas, especially in West Bengal. The Bararanga PACS is a case in point: 75% of its linked SHGs are located in the most remote border areas, and over 80% of their members belong to a tribal group, otherwise largely excluded from financial services.

SHGs Federated into the Jeevan Mutually Aided Cooperative Society, India

This case involves a federation of mutually aided cooperative societies (MACS) in Andhra Pradesh with nearly 6,000 SHGs and over 60,000 members at its base, most of whom are lower-caste women. This system grew out of a local Dalit[3] movement and trade union, and has deep roots in social activism. It is a three-tier system federated at the state and sub-district levels, with the apex serving as the system's wholesale financier and supervisor. Each sub-district MACS has an office as does the state-level MACS, and in addition there is some minimal infrastructure for the district-level teams. The infrastructure and staff are largely subsidized by the apex MACS which, through a business planning process, is attempting to wean member MACS away from subsidies. However, significant levels of grant support are still required in the system.

The case study focuses on the Jeevan MACS, a second-tier MOI, one of 108 sub-district MACS within the federation. The Jeevan MACS has 1020 members and 68 SHGs. Like other MACS, it is rooted in a

[3] Dalit is a self-designation for a group of people traditionally regarded as low caste or "untouchable."

long-standing social movement against caste and gender discrimination. It must be noted, however, that the multi-tier federations of MACS are not a product of the individual members' or SHGs' own initiative. They have been promoted by the state government and international agencies such as the UNDP, the World Bank, and CARE. That said, the social capital generated by the SHG members and their communities was another major contributing factor to their empowerment, enabling SHGs to achieve remarkable financial and non-financial results.

The MACS case is unique in having achieved something closer to genuine social change than is usual for financial interventions of this kind. The linkages between SHGs and MACS appear to have played a crucial role in this process: on their own, the SHGs could not have attained such social empowerment, with "untouchable" women holding most offices in large, highly visible institutions. This happened only with the support of the MACS.

The MACS may fail to compete with the commercial banks because their services are neither high-quality nor cheap. The MACS savings facilities are inflexible, and savings are seen as a route to loans rather than a valuable service in their own right. The banks offer lower-cost loans and more secure and flexible savings. As the SHG members become more experienced, they may come to realize that social empowerment and "ownership" of the system come at a heavy cost. Many groups already borrow from banks, taking advantage of the government-subsidized loans. Eventually, this may reduce the SHG members' willingness to give their time to the governance of their MACS and to pay its higher interest rates, and the linkages may be fatally weakened. Nevertheless, the empowerment impact may be expected to survive.

Muntigunung LPD, Indonesia

The Muntigunung LPD[4] in Bali is deeply tied to traditional community structures and government, which are themselves inextricably interlinked. It is owned by the traditional council which is nominally controlled by the assembly of all the villagers, but is effectively directed by 21 families with inherited positions in the village hierarchy.

Established by the government to reach out to smaller villages and poorer villagers (like all LPDs in Indonesia), the Muntigunung LPD is not federated or closely linked to any one institution, although it has some supervisory and financial links to local government bodies. These relationships, however, are for formal refinance and regulation rather than for membership or commercial dealings. Specifically, the LPD is regulated by the regional development bank and its sister institution, the regional LPD executive board, both of which are government agencies. They play a major role in governing the LPD, determining its staffing, interest rates, loan conditions, and the distribution of any surplus.

Despite being largely a government-controlled entity, the LPD does draw certain benefits from the traditional trust between community members, which is central to Balinese society. Securing loans is quite a simple process and almost any asset, movable or otherwise, is acceptable. Significantly, the main incentive to repay loans is the threat of being sent away from the community, which the Balinese consider to be far more serious than seizure of any property. It ensures that the LPD maintains its record of 100% on-time loan recovery. This feature is very much linked to the village and would be hardly transferable to a second-tier institution.

Somewhat surprisingly, there are about 170 borrowers yet only 88 savers in the Muntigunung LPD, and a significant proportion of its deposit balances are compulsory savings which borrowers are required to maintain. Members apparently want to borrow more than their deposits and savings will allow; accordingly, many members' requests for loans have to be rejected.

It is not entirely clear why the LPD has not been able to mobilize more members' savings, given the high degree of trust which it is said to enjoy. One plausible reason may be that the management of this LPD is in the hands of the village elite, while the rank-and-file residents may feel excluded. This explanation seems to be corroborated by a notable

[4] The acronym LPD stands for *Lembaga perkreditan desa*, which translates as "village credit board."

gender disproportion in the use of its services: 25% of the savers are women, but almost 90% of the borrowers are men. This suggests that there is some discrimination in the loan rationing process, presumably also related to the composition of the LPD management which mirrors the traditional male-dominated village hierarchy.

Likely owing to the extent and manner in which the LPD is controlled by government bodies and traditional authority, the rank-and-file members are far from being satisfied with this institution, perceiving it more as a channel for occasional largesse from government than as a genuinely local source of financial services.

Village Savings and Loans Associations (VSLAs), Niger

The VSLA model was initially designed to cope with the remote circumstances of poorer rural people, particularly women, in Niger, one of the world's poorest and most thinly populated countries. It was pioneered by CARE in 1988 in an effort to alleviate the major drawbacks that plagued the earlier forms of financial intermediation in remote rural areas (which were often known to break up because of inadequate records, dishonesty and mishandling of cash, and because minor disagreements and other issues were allowed to fester over time until they caused the groups to collapse in acrimony).

The VSLA model in Niger introduced simple but rigorous procedures which enabled even groups with no literate members to keep good records, operate a simple insurance system, and determine their own savings contributions, interest rates, loan terms, and penalties for late repayments. Most critically, Nigerian VSLAs were time-bound: they "drew a line" under their operations on a regular basis, usually every year, and "cashed out" and disbursed their accumulated fund on mutually acceptable terms.

VSLAs in Niger were originally envisaged as "stand-alone" village institutions which would be able to survive and continually serve their members without any external linkages, subsidy, or other long-term assistance from CARE or any other institution. They reportedly thrived without ongoing assistance, reaching a cumulative total of up to 200,000 women.

In recent years, however, CARE has changed its Niger model substantially. Responding to some VSLAs' requests for larger loans that their own funds allowed, it has helped VSLAs to form federations to intermediate between member VSLAs which needed more money than they had and those with temporary surpluses. Besides, VSLA federations were meant to access loans from MFIs or cooperatives and to serve as channels through which CARE could provide cereal banks for communities suffering from a shortage of basic staple foods.

The grouping of Nigerian VSLAs into federations appears to pose a number of disadvantages. The member VSLAs have to capitalize the federation with an entry fee, must deposit their members' savings with the federation, and must pay interest on loans from their federation, which reduces their own revenues and loanable funds. Federations cannot operate by way of the same simple procedures as VSLAs. They have to register, and require written records and paid staff. This not only leads to reduced transparency and higher operating costs (which are passed on to the member VSLAs), but also makes the federations "distant" from the people who nominally own them. Furthermore, the VSLAs' regular "cashing out," which served as an effective mechanism for internal control, has had to be abandoned because it is impractical for formal federations to close down every 12 months.

Overall, it appears that the funds that unlinked VSLAs in Niger can amass on their own are usually sufficient to meet their members' needs. Federations, on the other hand, require sizeable ongoing funding and management support from CARE. As such, they tend to perpetuate reliance on CARE and technical elites rather than on member control.

Mutuelles Communautaires de Croissances (MC2s), Cameroon

The MC2s were established and continue to be heavily supported by Afriland First Bank, a privately owned institution whose management appreciates the need for socially responsible initiatives (which can also, in the long term, build a rural customer base for the bank). Afriland is known for having developed new sharia-compliant savings products for its Muslim clients, which have attracted large numbers of customers who were previously unbanked, and large volumes of relatively low-cost funds. This is an unusual case of an indigenous African bank investing in the long-term development of its mass market customers.

Afriland's efforts with the MC2s are supported by ADAP, an NGO which provides ongoing subsidized technical assistance in auditing and monitoring. The linkage with these two institutions has fostered the viability and continuing empowerment of the MC2s since their establishment. For example, Afriland provides cross-subsidized funds at a lower cost than the MC2s could obtain elsewhere. The MC2s also benefit from tax concessions which have been facilitated by Afriland.

Recently, however, Afriland and ADAP have taken a joint decision to assist the MC2s in creating their own second-tier institution, the AMC2, which will take over the functions they have originally provided. The evolution of this MOI is at an early stage and it is not yet clear if it will be able to provide the linkage functions as effectively as Afriland and ADAP have done. For instance, the level of direct subsidy (which currently amounts to the rather high figure of 10% of assets) raises concerns about whether the MC2s will be able to avoid continuing dependence on subsidy after their direct relationship with Afriland is terminated. Nonetheless, this relationship is mutually beneficial and therefore likely to be continued under the new institutional arrangements.

Mixtlan Savings and Credit Cooperative, Mexico

Mixtlan is a rural MOI with nearly 3,500 members and a 90% penetration rate, which was set up in 1960 with support from the local church. In 2002, in response to the national financial crisis which weakened people's confidence in all financial institutions, Mixtlan became a member of UNISAP, a strong state-wide federation with 40 member MOIs. Mixtlan has grown rapidly since that time, partly in response to this linkage.

Mixtlan is the most remote of UNISAP's member MOIs, 80% of which are urban. The strength and volume of business contributed by its urban members have enabled UNISAP to offer a wide range of services at prices that Mixtlan would not have been able to access on its own. For example, membership in UNISAP allows Mixtlan to offer a utility bill payment facility and an extremely low-cost remittance service (at the time of field research, family members were able to remit funds to Mixtlan for the flat fee of US$1.60). UNISAP also assists Mixtlan with training and capacity building, particularly through the provision of information technology (which, in turn, provides UNISAP with routine information to monitor its members' performance).

Most importantly, Mixtlan's linkage with UNISAP gives its members confidence that their money is in safe hands. Through this linkage Mixtlan members are automatically protected and supervised by UNISAP's membership in BANSEFI. This is a government-supported third-tier institution which plays the role of a central bank for the cooperative financial sector and stands ready to assist any of its members which are in need of temporary liquidity.

Like other well-managed MOIs, UNISAP refrains from demanding "loyalty" of its members, which means that Mixtlan is free to use other suppliers of the services it seeks, if and when it can find a better deal. It seems very unlikely, however, that any competitive suppliers could match UNISAP's services and prices in the remote areas where Mixtlan operates. These are effectively cross-subsidized by the urban members of UNISAP, and Mixtlan pays an annual service fee of under US$10,000 for all the services it receives.

All these advantages notwithstanding, a serious threat looms on the horizon for Mixtlan, as UNISAP finds it costly to deal with small MOIs and has suggested that Mixtlan merge with a neighbouring institution. The proposal is strongly resisted not only by Mixtlan's management, but also by its members, who highly value the personal contacts with, and local knowledge of, the staff of "their" institution. The members fear that these benefits would be lost if Mixtlan were merged with a larger entity.

Jardín Azuayo, Ecuador

The Jardín Azuayo savings and loan cooperative is the only MOI examined in the study that has no close linkages to financial institutions aside from normal commercial transactions. It has 23 offices, 20 of which are located in remote rural areas. Unlike many second-tier MOIs (e. g., UNISAP in Mexico), it does not rely on a majority of wealthy urban groups to cross-subsidize a smaller number of rural members, having grown to a size when it can itself provide the services for which a smaller MOI might have to enter into some sort of federation.

Jardín Azuayo has devised a system which successfully combines the advantages of self-managed and independent local entities with the strengths of centralized direction of policy, treasury management, and access to a large and growing range of services. This has been achieved through delegating many functions to local offices that operate almost as if they were independent primary groups which were members and owners of the central society. For example, each office elects a board of local directors with good knowledge of their areas, who have the final authority to approve or reject all loan applications made in these areas. This clearly distinguishes Jardín Azuayo from institutions in which loan decisions are made by the head office without the benefit of local knowledge.

Apart from normal commercial linkages with its supplier of remittance services and with government for the delivery of pensions, Jardín Azuayo has no need for close links to any financial institution, since it is remarkably self-sufficient, maintaining a sound balance of loans to savings and liquidities and a healthy proportion of savers to borrowers (52,000 to 21,000). Modestly profitable, it appears to have struck the right balance between local autonomy and centralized professional management, without having to rely on other institutions.

Conclusions

The cases presented above do not provide enough evidence to accept or reject linkage in general or any particular type of linkage or secondary MOI. The variety of institutional types, the ways in which particular linkages were initiated, and the services they yield is too wide to permit valid generalizations. Some tentative lessons may, however, be drawn from these seven cases:

- One obvious issue is the ***unavoidable conflict between local, familiar management and "ownership" on the one hand and the benefits of being part of a more distant, large-scale, and professionally-run institution on the other.*** The examples of the Mixtlan cooperative in Mexico and the Muntigunung LPD in Bali clearly demonstrate the impossibility of "having the cake and eating it too." In other words, MOIs will have to sacrifice some of the benefits of local control in order to obtain a broader range of services.
- The Nigerian VSLAs demonstrate that ***secondary-level MOIs should not be imposed on small local institutions unless the members will gain real advantages.*** Very poor people who live in remote areas have the least need for the kinds of diversified services that linkages or federations can provide, and are the least able to manage such linkages. NGOs and other agencies should avoid promoting higher-level groups in order to provide themselves with convenient delivery channels for other services and a reason for their continued presence.
- Both the Indian PACS, and the Balinese LPDs were initiated by government to bring subsidized financial services to poor people in remote areas. However laudable this aim, ***state-promoted entities are usually not the best basis for a mutually-beneficial and sustainable relationship with members***. In the long term, it may be easier and less risky for MOIs which are linked to state-controlled entities to enter into arm's-length commercial relationships with banks and other service providers rather than to remain dependent on government.
- Linkages should ideally be initiated by primary-level MOIs when their members realize that they need services which their own institutions cannot provide. This rarely happens, and was only partly the case for the SHGs in Andhra Pradesh

and the Mixtlan cooperative in Mexico. In the other examples, it was a purely "top-down" process. Apparently, ***primary-level MOIs may not always be able to select or start linkage institutions and to manage their relationships with these institutions without external assistance.***

- The above case studies focused solely on "vertical" linkages between primary-level MOIs and secondary-level institutions or other providers, which can supply services that the primary level cannot supply itself. ***"Horizontal" linkages between primary MOIs—which individually lack the necessary scale or competence to supply the services they need but which may be able to do so together—may be a necessary precursor to the evolution of "higher-level" service providers.***
- VSLAs in Niger are linked to what is called a "network." This network, however, performs the same tasks as a financial intermediary which would usually be referred to as a "federation" or secondary society. While the study does not allow any substantive conclusions regarding the advantages of less formal networks, experience in India and elsewhere suggests that ***provision of non-financial services such as information, advocacy, or training may be a more suitable task for second-tier institutions.***
- All the MOIs with close linkages examined in the study are linked to other MOIs. In order to find out whether this was the best type of linkage institution, we should ask the question: Would the MOIs have been able to obtain the same services on an arm's-length basis from private providers? The answer would generally be "no." A private bank would be unlikely to cross-subsidize a very small-scale customer such as Mixtlan, and there are no effective providers of financial services in remote areas of West Bengal or Andhra Pradesh. Still, it might be more effective if Afriland First Bank did not try to off-load its responsibilities for serving its MC2s onto a new AMC2 or if CARE did not set out to build a VSLA network. ***Cooperatives are not necessarily always the best source of services for other cooperatives.***
- Finally, it may not be a coincidence that the most effective institution among the seven MOIs examined is Jardín Azuayo in Ecuador, which is largely self-sufficient and needs no close or permanent linkages other than normal commercial transactions. ***It may be fashionable for businesses to "outsource" specialized tasks rather than perform them "in-house," but MOIs in remote areas may be an exception to this trend.*** Linkages are not the solution to every problem.

This focus note is an abridged version of the thematic paper "Linkages and networking of member-owned institutions in remote rural areas" by Malcolm Harper. The original paper is available on the Coady Institute's website at <http://coady.stfx.ca/tinroom/assets/file/ford/docs/Coady_ThLink_Final.pdf>.

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COADY INTERNATIONAL INSTITUTE

St. Francis Xavier University | PO Box 5000 | Antigonish, NS | Canada B2G 2W5 | www.coady.stfx.ca

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