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FINANCIAL INCLUSION AND THE GROWTH OF MICRO FINANCE BANKS IN NIGERIA.

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Abstract
Enhancing Financial Innovation and Access (2014) report 40% of Nigeria's adult population is financially excluded. Much of this proportion includes the poor and the financially weak living in the rural areas and the urban fringes. The Micro Finance policy of the Nigerian government was intended to convert existing community banks that meet certain criteria into microfinance banks (MFBs), so as to offer services that appeal to the financially excluded adult Nigerians and bring them into the mainstream financial system. The performance of MFBs between 2007 and 2011 appears to suggest that progress is being made. The assets and liabilities of the MFBs had rose to N190.7 billion from just N55.1 billion in 2006. The loans and advances given by MFBs also increased from a mere N16.0 billion in 2006 to over N67.6 billion at end-December 2011. Moreover, the asset base of MFBs has been projected to 120 billion by the year 2010. MFBs could have done more but for a myriad of challenges that affect their operations such as poor risk management processes, dearth of infrastructure, high cost of operations, among others. It is on this premise that the paper suggest that the government should do more to create an enabling environment that will enable MFBs to thrive and grow; employment of qualified staff who are sufficiently motivated; and regular staff training to expose staff to strategies that are critical to micro financing, etc.

Keywords: Banks, Government, Microfinance and Staff training

Introduction

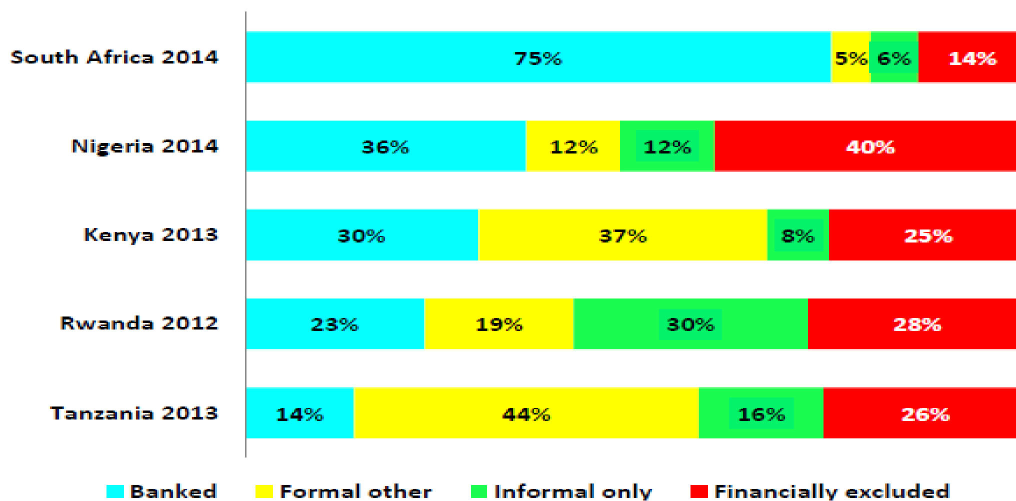
There is presently a global consensus that access to financial services can play a pivotal role in poverty alleviation and decreasing the vulnerability of poor people (Yobo and Azoroh, 2013). Consequently, some international financial institutions and development initiatives and central banks of most developing countries have committed themselves to the promotion of financial inclusion; which is geared at increasing the accessibility of the poor segments of the society to cheaper and varied tailor-made financial services.

The Nigerian financial sector comprises of commercial banks, development banks (including Bank of Agriculture, Bank of industry and Federal Mortgage Bank), credit cooperatives, primary mortgage finance institutions, insurance and capital/securities market etc. However, the deposit taking market is dominated by commercial banks. EFInA (2014) reports that 36.3% of the adult population in Nigeria have and/or use a bank account, which is equivalent to 33.9 million people; while 61.0% of the adult population has never been banked,

which is equivalent to 57.1 million people. Furthermore, 12% had access to including Insurance companies, microfinance banks, pension schemes, cooperatives etc.; while another 12% had access to informal financial institutions such as Isusu, money lenders, savings clubs, etc.

Indeed, EFInA (2014) emphasizes that about 40% of Nigeria's adult population is financially excluded. Also, figure I appears also to suggest that more Nigerians are financially excluded than South Africa (14%), Kenya (25%), Tanzania (26%) and Rwanda (28%). But figure II equally shows that progress has been made since 2010, when percentage of financially excluded adult Nigerians was 46%.

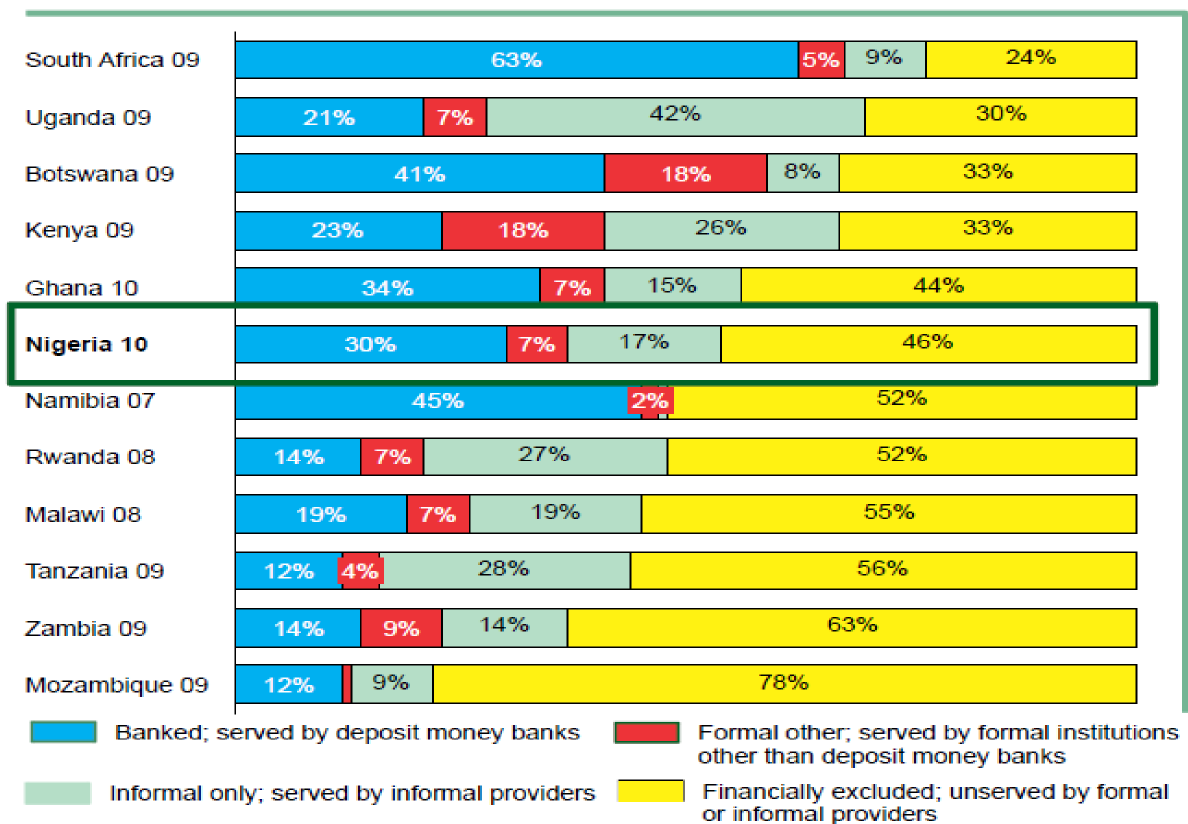
Figure I: FINANCIAL ACCESS-CROSS COUNTRY COMPARISONS, 2014.



Source: EFInA, 2014.

Kama and Adigun (2013) note that since 2005, the Nigerian financial services sector has witnessed increasing activities by both the government and the regulatory authorities aimed at deliberately promoting policies that are intended to grow financial inclusion. The CBN has been at the fore front of encouraging and supporting products that are specifically targeted at the low income and financially excluded, while the government has focused more on both interventionist financing arrangements and building institutions and frameworks that promote financial inclusion: Financial System Strategy 2020 (FSS2020) which represents a holistic and strategic road map and framework for developing the Nigerian financial sector into a growth catalyst that will enable Nigeria be one of the 20 largest economies by 2020; Introduction of a new framework for Non-Interest Financial Institutions (NIFIs) in June 2011; E-banking Products, Electronic Payment System and Cashless Policy; and Microfinance Policy, which involves the provision of financial services to the poor and low-income earners; and intended to facilitate the participation of mostly the third sector institutions, including market associations, cooperatives, non-governmental organizations, self-help groups, in the microfinance model.

Figure II: FINANCIAL ACCESS-CROSS COUNTRY COMPARISONS, 2010.



Source EFInA (2010).

The Micro Finance policy of Nigerian government was intended to convert existing community banks that meet certain criteria into microfinance banks (MFBs). But more than ten years on, operations of the MFBs are being constrained by a near absence of basic infrastructure such as good roads, water, electricity etc. and high transaction cost (Acha, 2012). All these work in concert to drive the cost of operations up and put MFBs at a very big competitive disadvantage, thereby casting doubts on their sustainability, much less on helping to improve on financial inclusion of adult Nigerians. This paper therefore examines the performance of microfinance banks as an index of their relevance and survival prospects.

Conceptual Issues

Financial Inclusion and Exclusion Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost (The Committee on Financial Inclusion cited in Manju and Mohika, 2014; see also Ibeachu, 2010). It can then be deduced from the above that the essence of financial inclusion is in trying to ensure that a range of appropriate financial services is available to every individual and enabling them to understand and access those services (Onaolapo and Odetayo, 2012). Thus, apart from the regular form of financial intermediation, financial inclusion may include a basic "no frills" banking account for making and receiving payments, a savings product suited to the pattern of cash flows of a poor household, money transfer facilities, small loans and overdrafts for productive, personal and other purposes, insurance (life and non-life), etc. While financial inclusion, in the narrow sense, may be achieved to some extent by offering any one of these

services, the objective of "Comprehensive Financial Inclusion" would be to provide a holistic set of services encompassing all of the above.

Financial exclusion on the other hand refers to a situation in which an individual or group of persons are unable to access financial services and products in the financial services market. The excluded thus has no business relationship with any financial institution and therefore cannot expand the scope of his operations beyond the level of his private saving (Nzewi, Ezeala, Nzewi, and Obi 2014)

Microfinance Microfinance refers to financial services provided to low-income people, usually to help support self-employment. Examples of microfinance products include: small loans, savings plans, insurance, payment transfers, and other services that are provided in small increments that low-income individuals can afford. These services help families to start and build "micro" enterprises, the very small businesses that are important sources of employment, income, and economic vitality in developing countries. Banking and/or financial services targeted to low-and-moderate income businesses or households, including the provision of credit.

Microfinance, according to Ehigiamusoe (2006), is the supply of loans, savings and other financial services to the poor. The Central Bank of Nigeria's Microfinance Policy, Regulatory and Supervisory Framework for Nigeria (2005), sees microfinance as a "means of providing financial services to the poor, who are traditionally not served by the conventional financial institutions. Indeed, microfinance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions such as commercial banks, who tend to concentrate on medium and large-scale enterprises, which are considered to be more profitable and viable. Banks avoid doing business with the poor and other small business because of the associated costs and risks, which they consider to be very high.

A microfinance institution (MFI), on the other hand, is an organization that arranges small loans and financial services to the poor people and small business. According to Microfinance gateway (2008) an MFI is the organization that offers financial services to the low-income people. There is a wide range of micro financial institutions. Mostly when we talk about these, financial NGO`s come into the mind. These financial NGO's provide micro credit and micro finance services but in most cases these financial NGO's are not allowed to capture saving deposits from general public. In any case, many commercial bank are also providing microfinance along with their routine financial activities, so also are some specially designed institutions like the micro finance banks which are established to focus on providing financial services to the under banked. Rehman (2007) advises that there are some other MFI´s that can be considered in the business of microfinance, such as credit unions, cooperative housing societies and some others which are owned and managed by the local entrepreneurs and municipalities. Additionally, Seibel (2004) did observe that informal indigenous savings and credit groups in Africa and elsewhere do qualify to be recognized as MFIs. However, the major focus of this paper is on MFBs.

Origin and Policy Framework for MFBs

Microfinance banks were created and licensed to begin operations in 2007 and existing community banks and NGO microfinance institutions that met the conditions spelt out by CBN for licensing were allowed to transmute into microfinance banks (CBN, 2015a). Indeed, the

microfinance policy in Nigeria is part of the global financial integration in the provision of tailor made financial services to those outside the catchments of the big banks either as a result of their income, location, literacy level or discrimination.

To qualify for a microfinance license an existing community bank was required to increase its paid-up capital from N5m to N20m. Unlike the community banking policy framework which compulsorily confined all community banks to unit banking, the microfinance banking guideline permitted the branching of microfinance banks within a state. For the microfinance banks intending to open branches within a state their paid-up capital was put at N1 billion. Another point of divergence between the community banks and their microfinance successors is in those which the regulatory guideline allows to own them. In addition to individuals, group of individuals, community development associations, private corporate entities which could own community banks, foreign investors and commercial banks, foreign investors could also own microfinance banks.

In summary, some of the notable microfinance policy strategies that was put up by the government and Central Bank of Nigeria (CBN) include (Iganiga, 2008): License and regulate establishment of Microfinance Banks (MFBs). Promote the establishment of NGO-based microfinance institutions. Promote the participation of government in microfinance industry by encouraging states and local governments to devote at least one percent of their annual budgets to micro credit initiatives administered through MFBs. Promote the establishment of institutions that support the development and growth of microfinance service providers and clients. Strengthen the regulatory and supervisory framework for MFBs. Promote sound microfinance practice by advocating professionalism, transparency and good governance in microfinance institutions. Mobilize domestic savings and promote the banking culture among low-income groups. Strengthen the capital base of the existing microfinance institutions. Broaden the scope of activities of microfinance institutions. (x) Collaborate with donors, coordinate and monitor donor assistance in microfinance in line with the provisions of microfinance policy. Increase in the capital base of community banks (now microfinance institutions) from N250, 000.00 to N20m.

The targets of the above policy measures are as follows (Iganiga, 2008): i. To cover the majority of the poor, but economically active population by 2020; thereby creating millions of job and reducing poverty. ii. To increase the share of micro-credit as a percentage of total credit to the economy from 0.9 percent in 2005 to at least 20 percent in 2020; and the share of micro-credit as a percentage of GDP from 0.2 percent in 2005 to at least 15 percent in 2020. iii. To promote the participation of at least two thirds of the states and local governments in micro-credit financing by 2015. iv. To eliminate gender disparity by improving women’s access to financial services by 5% annually; and v. To increase the number of linkages among universal banks, development banks, specialized finance institutions and microfinance banks by 10% annually.

Performance and Prospects of Nigeria’s MFBs

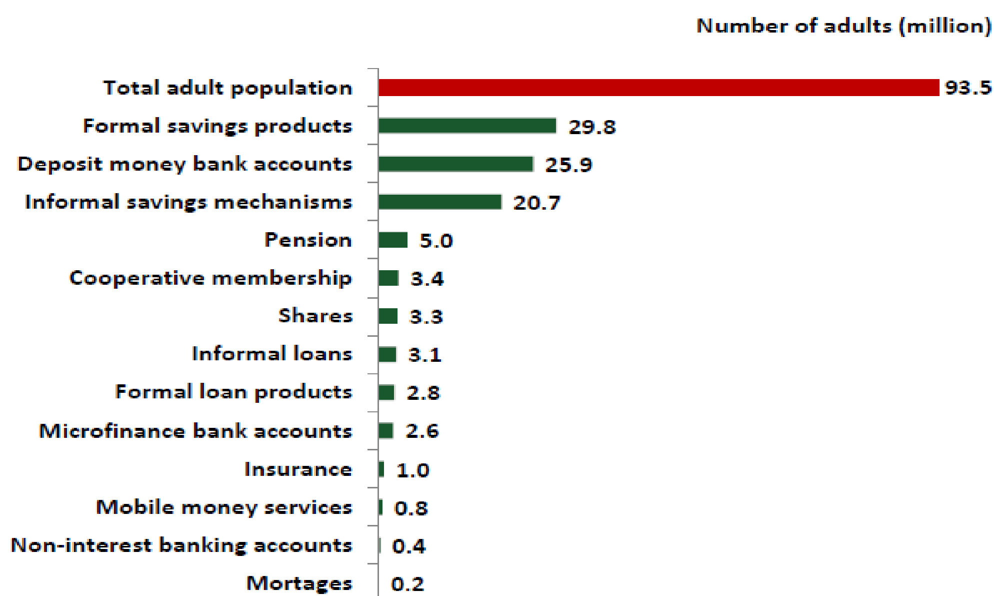
Out of 127 private investors that applied for microfinance banks licenses, the Central Bank of Nigeria, (2009), approved 840 to operate as microfinance banks. The number has since risen to 941 (CBN, 2015a). These figures are relatively small given the population of the country and the fact that majority of the people reside in rural areas. With the creation of the micro

finance policy, the question that remains is if the act can cause a transformation in those rural areas.

With the granting of the licenses, the CBN informs that the MFBs remain the major vehicle for the inclusion of the large and many users of the informal sector where the bulk of the unbanked exist. By the end-December 2011, and following the increased confidence and activities of the microfinance banks, Kama and Adigun (2013) report that the assets and liabilities of the MFBs had reached N190.7 billion from just N55.1 billion in 2006. The loans and advances given by MFBs also increased from a mere N16.0 billion in 2006 to over N67.6 billion at end-December 2011. A review of the loan portfolio structure equally showed that short-term loans, at the end December 2011, accounted for 89.7 per cent of the total. Furthermore, CBN (2015b) report that as at December 2013 assets of MFBs stood at N237,837.6 while loans and advances was 94,055.6 (CBN 2015).

In spite of the above, there is a cause for worry. The EFInA (2014) survey shows that only 2.6% of adult Nigerians patronize MFBs (Figure III). This becomes more glaring when compared to figure of those that patronize informal savings mechanisms (20.7%) and cooperatives (3.4%). But the same report does show that more than 80% of patrons of MFBs expressed satisfaction with services they received.

Figure III: PREFERENCE FOR FINANCIAL SERVICES, 2014



Source: EFInA Access to Financial Services in Nigeria 2014 survey

Though not quite the expected, the noted performance is an indication of the enormous influence the microfinance institutions can have in the process of growing the financial inclusion level of the country. The CBN/Government recently revised the microfinance policy to strengthen the institutions and reposition them for enhanced service delivery creating a more responsive sub-sector. Acha (2012) has noted that the inclusion of microfinance banks' deposits in the deposit insurance scheme and the upward review of the deposit insurance limit from one hundred thousand Naira (N100, 000.00) as stipulated by the NDIC Act of 2006 to

two hundred thousand Naira (N200, 000.00) have gone a long way to improve public confidence in the subsector.

That a lot of opportunities exist in the microfinance subsector in Nigeria is unarguable. Scholars are unanimous in their agreement that there exist a large untapped market for microfinance banks in Nigeria. We have earlier seen in figure I above that about 40% of adult Nigeria is still financially excluded and many of them are in the rural areas and urban fringes. Also a further 12% of adult Nigerians patronize the informal financial operators probably for unavailability of or lack of confidence in formal financial institutions. MFBs have not done enough to attract these groups. It is our contention here that if MFBs are able to streamline their operations and services in line with best practices and CBN policy guidelines, substantial part of this 40% could be brought into the formal financial system.

Challenges Besetting Operations of MFBs

The path to growth for Nigeria's MFBs is still beset with challenges that hamper progress. Clearly if the challenges are not addressed chances are that instead of seeing a realization of the potential of MFBs, the reverse will be the case. Some of these challenges are discussed bellow.

1. The greatest constraint to the growth and development of MFB in Nigeria is lack of risk management capacity. But this is hampered by operational risk, hence the need for effective operational risk management. Most MFIs have poor risk management processes. They fail because they do not have abilities to focus on problem detection and prevention.
2. The standard of corporate governance in many microfinance banks in Nigeria is poor. Board members are known to misuse their positions to obtain facilities way above the regulatory limit for insider related loans and worse still with no intentions of repaying such facilities. They also use their positions to unduly influence and manipulate the recruitment processes in favour of their cronies. Frauds and forgeries by both insiders and outsiders to the banks are rife and people generally obtain loans with no intention to repay.
3. Lack of basic infrastructure compounds the operational difficulties of these banks, which ordinarily are faced by high operational costs because of their nature of business. By dealing with many small clients, microfinance banks' transaction costs are usually higher than those of conventional banks. Unfortunately, these banks are also forced to incur additional costs to provide themselves with electricity and water. The absence of good roads especially in the rural areas also distorts their outreach. All these work in concert to drive cost of operations up and put them at a very big competitive disadvantage.
4. The lack of banking culture in the rural areas, among the urban poor and small business owners is another factor militating against the progress of microfinance banks. Traditionally, these people borrow money from friends and relatives and repay the same amount of money borrowed no matter the tenure of such loans. Some misconstrue banks as government institutions that should be concerned about their welfare. They therefore

find it difficult to understand the payment of interest on bank loans. An improvement in the banking culture of rural dwellers and small business owners will impact positively on the performance microfinance banks.

5. Another prevalent problem among microfinance banks is the copying, competing and mimicking the practices of commercial banks. Many microfinance bank managers and other management staff were commercial banks' staff who were either retired or sacked by their former employers. To these staff microfinance banking is just an extension of the commercial banking they know. They refuse to understand that microfinance is not micro-commercial banking but a different kind of banking requiring a different approach, philosophy and client base.

Conclusion and Recommendations.

Microfinance services are targeted at rural dwellers, the active poor and micro, small and medium sized businesses. Microfinance Banks could only achieve its stated objectives if its services are tailored to the needs of the poor and low income earners that mostly live in the rural areas and urban fringes. There is a huge untapped market for micro financing: About 40% of adult population are still financially excluded. MFBs can attract this proportion into the micro financing system with the provision of appropriate services that are tailored to the needs of the poor and the financially weak. The survival of MFB may well depend on it ability to do the needful to engender itself as partners of the poor and the financially weak.

In line with the foregoing, the following are suggested which we believe could smoothen the operations of MFBs and even propel them to higher performance. The government should encourage and create an enabling environment t enable MFBs to grow and continue to deliver financial and social services to the poor and to reduce the financial exclusion gap. Provision of efficient and effective financial services by MFBs also depends on the quality of available staff. MFBs must ensure that they recruit and retain qualified professionals. MFBs should pay attention to staff training and skills development especially in project evaluation and management. Regular and continuous training and retraining within the framework of appropriate capacity building programmes is necessary to improve the skills, knowledge and attitude of staff in the work place. Staff motivation should be given deserved attention by MFBs. Indeed, staff motivation is critical to offering services that meets the expectation of MFB clients and customers. MFBs should avoid the temptation of mimicking the operations of commercial banks in the structure and quantum of offerings. Some MFBs often lend beyond the CBN ceilings thereby exposing themselves to unnecessary risks. Operators of MFBs should understand the difference between the two. The CBN has designed a model and rules for microfinance banks in Nigeria but most operators have deviated from the rules. MFBs should seriously consider offering non-financial services (if they are not doing that already). Under this approach, The MFBs provide beneficiaries with financial services (credit, savings, insurance) along with non-financial services (primarily education, health services, practical training, insurance, technical assistance and any other service). The non-financial services are aimed at improving the borrowers' capacities to develop sustainable income generating activities.

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