THE DEVELOPMENT OF RURAL FINANCE INSTITUTIONS FOR THE POOR: THE CASE OF MALAWI MUDZI FUND

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Abstract

Due to market failures in rural credit markets in developing countries governments and donor agencies have heavily intervened in these markets by establishing rural finance institutions geared towards the poor. The performance of these institutions have varied across countries. The Malawi Mudzi Fund (MMF) was established in 1988 under the sponsorship of the International Fund for Agricultural Development (IFAD) based on the Grameen Bank model. In 1995, MMF was integrated into the Malawi Rural Finance Company (MRFC) combining MMF and Smallholder Agriculture Credit Administration (SACA) activities. This paper evaluates the operations and performance of Malawi Mudzi Fund and examine implications for the development of rural finance institutions in Malawi.

1. Introduction

In most less developed countries (LDCs) credit facilities from the formal financial institutions has tended to be extended to large scale enterprises and high income investors. In other cases, it has been argued that the formal financial system has tended to favour male borrowers and hence discriminating against women (Berger, 1989; Chen, 1989; Jiggins, 1989). Several studies in LDCs have indicated that poor farmers and small scale entrepreneurs, particularly women who are resource poor, have heavily relied on informal savings, banking and credit services to finance their economic activities. The problems of accessibility to credit facilities to the poor have been well documented (see Jiggins, 1989; Daniels and Ngwira, 1993; Steel, 1993 and Mead, 1994). However, it is also a well known fact that the informal financial system is generally exploitative and interest rates on loans are two or more than twenty times those that apply in the formal financial institutions. The argument for lack of credit extension by the formal financial institutions to the poor and small scale entrepreneurs is that this segment of the population is characterised by high risk of default. Moreover, with information problems, the cost of operation or dealing with many small borrowers does not justify the marginal benefits from investing in rural operations for the formal financial institutions.

In response to lack of accessibility to credit facilities by the poor and due to the growing poverty situation in most LDCs, other countries have deliberately created innovative rural financial institutions to help the poor, hence intervening in rural credit markets (Besley, 1994). There exist several studies on the characteristics and performance of these rural financial institutions which seem to have attracted much attention especially in Asian countries.[1] Several rural financial institutions exist in Indonesia such as Bank Rakyat Indonesia's unit desa (BRI-unit desa) and Badan Kredit Kecamatan (BKK) systems whose operations and success have been well documented (Patten and Rosengard, 1991; Yaron, 1994; Riedinger, 1994; Chaves and Gonzalez-Vega, 1996). Another successful case of rural financial institutions is the Grameen Bank in Bangladesh (Yaron, 1994; Jain, 1996; Goetz and Gupta, 1996). Egger (1986) also discusses some alternative savings and credit programmes in Bangladesh, India, Zimbabwe and Nepal. The success stories of the long established rural financial institutions in Asia have tempted other developing countries to replicate these programmes. However, such replication in other LDCs particularly in the African context may be difficult because of different socio-economic environments (Patten and Rosengard, 1991).

In Malawi a large proportion of the population, about 92 percent, live in the rural areas depending on the subsistence economy. There is a very high incidence of poverty in rural areas and most of the rural households do not have access to institutional credit. In order to help the rural poor the government and the donor agencies established the Malawi Mudzi Fund (MMF) in the late 1980s as a replica of the Grameen Bank of Bangladesh.[2] This paper, therefore, evaluates the replicability of the Grameen Bank model in Malawi and the relative performance of the Malawi Mudzi Fund in the provision of banking facilities for the rural poor in two highly populated districts in southern Malawi. It is contended in this paper, that the MMF was far from achieving the success equivalent to the famous Grameen Bank.

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1 See Yaron (1994), Egger (1986) and Patten and Rosengard (1991) for extensive discussion.

2 See Hulme (1990) on some experiments of the Grameen Bank model in Malaysia, Malawi and Sri Lanka.

2. The Malawi Mudzi Fund (MMF) [3]

The Malawi Mudzi Fund was established in 1988 as a pilot credit scheme for the poor under the Smallholder Agricultural Credit Program financed by the International Fund for Agricultural Development (IFAD). The MMF was a replica of some sort of the Grameen Bank model in Bangladesh which IFAD had funded and the project has been hailed as a success story of intervention in rural financial systems. The 1987 IFAD/World Bank mission established that a distinct group of the poor of the Grameen clientele type did exist in Malawi and that the demand for credit was very high. It was conceptualised that if credit was made accessible to the resource poor smallholder farmers without access to institutional finance, this would lead to improvement in farming technologies as well as generating interest in non-farm business activities. In turn, these could lead to generation of self-employment and paid employment in the economy. Although the MMF was established in 1988, operations and activities on the ground started in the 1990/91 fiscal year. Nonetheless, in 1995 operations of the Malawi Mudzi Fund were integrated into a new financial institution, the Malawi Rural Finance Company (MRFC), which took over the activities of the Smallholder Agricultural Credit Administration (SACA) which experienced high default rates in 1992/93 crop season.[4]

2.1 Group and Centre Formation

The objectives of the MMF were similar to those of the Grameen Bank and included: the provision of banking facilities for lending and savings to the rural poor without collateral and provision of training in business management.[5] All beneficiaries were voluntary organised in groups of five persons, and this was a condition for potential borrowers to be registered and accepted into the scheme. The MMF project officers would identify a target member to form a

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[3] The information on Malawi Mudzi Fund draws heavily on an evaluation exercise of the project by Nyanda, Chirwa and Jones (1995), in which 306 beneficiaries were interviewed.

[4] A detailed analysis of SACA and the causes of high default rates in the 1990s is contained in Msukwa et al (1994) and Chirwa (1996).

[5] Jain (1996) provides a summary of program activities, policies and strategies of the Grameen Bank while Hulme (1990) compares the Grameen Bank to the schemes that have used it as a model.

group of five persons with similar social and economic status with a deliberate differentiation by gender, but not belonging to the same family. The original criteria for eligibility to the MMF scheme was based on land holdings lower than 1 hectare and/or the equivalent asset ownership. However, operationally it became difficult for MMF to verify land holdings in assessing eligibility and hence they determined this by subjective observation of asset ownership and relied on opinion leader assessment of potential beneficiaries.

The purpose of the group was to ensure collective responsibility for loan repayment and to encourage peer review in business proposals and management. However, as Nyanda et al (1995) argue the group was not used to assume joint liability for the loans issued to group members even by the various group savings schemes.[6] Beneficiaries had a different perception about the purpose of the group. About 36 percent of the sampled beneficiaries perceived the group as being a facilitating framework for access to credit, 25 percent viewed it as a structure for mutual business assistance and 23 percent considered the group as a vehicle for collective business operations. These variations in perception imply that the officers were not able to articulate the role of the group to beneficiaries, hence the asymmetric information.

The group members met once every week to discuss business proposals, problems and management. The groups were organised into centres as an intermediate aspect of management at grassroots level. The centres comprised 2 to 3 groups in principle and were headed by elected centre 'chiefs'. Groups belonging to each centre would hold weekly meetings at which a project officer would be present to conduct banking services such as collection of savings, loan repayments and loan applications and disbursement of loans as well as monitoring of borrower's business performance and providing training. The centre unit was more administratively convenient to MMF staff because by meeting groups of beneficiaries at the centre, overheads costs were greatly reduced. However, this centre role tended to overshadow the group concept.

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[6] Similarly, Jain (1996) argues that the five member group in the case of the Grameen Bank did not guarantee loan repayment of individual members.

In essence, there has been dynamism in the organisation of beneficiaries of MMF. By the end of 1994, MMF had made major changes to its operations by focusing on centre level. Groups were allowed to comprise 3 - 7 members and centres were allowed membership ranging from 15 - 30 (maximum of six groups). The centres had a six member executives elected by and from the leaders of the groups forming the centre. Each centre was required to have a written constitution and centre executives were empowered to fine members for non-attendance and breach of the constitution. The centres, therefore, were transformed into genuinely participatory and self-regulatory units. There was discipline during centre meetings through the use of procedures to foster member commitment such as reciting the pledge at the beginning and end of the meeting.

2.2 Scheme Management Structure

The MMF was run as a non-government or non-parastatal unit with a distinct legal entity. However, as Hulme (1990) observed, the management of MMF did not enjoy the independence from government influences that characterised the Grameen Bank, since MMF was under the control of the Office of the President and Cabinet. The highest authority was the Board of Trustees appointed by the Government of Malawi with the Secretary to the President and Cabinet as chairman of the board. Policy decisions were made by the board of trustees, sometimes upon recommendations from the Scheme Administrator. At management level, the MMF had a Scheme Management Unit headed as a Scheme Administrator. The Scheme Administrator had support staff which included an accountant, a secretary, a driver and a messenger. At a lower level of management were two Branch Units headed by the Branch Manager supported by bank workers or project officers and a messenger guard. In terms of transport, one vehicle was provided at the Scheme Management Unit. Branch Managers were provided with motorcycles and project officers were also given motorcycles (although they were originally expected to use bicycles). Each branch was expected to reach 1,000 members of the target population in the villages with its project area.

3. Credit Procedures and Credit Recovery

3.1 Eligibility Conditions

Eligibility conditions for getting a loan from MMF have evolved over time. Initially, it was conceptualised that the poor could be identified with the small landholding that could not generate enough food and income for the household. However, in practice it became difficult for project officers to assess land holdings as a basic criteria for eligibility to MMF services. An elaborate questionnaire was used to solicit detailed socio-economic characteristics of potential beneficiaries covering personal characteristics, family situation and poverty indicators such as household assets, food security and nutritional status. The criteria for eligibility was broadly the poverty situation of individuals which was assessed in terms of household's land holding and assets, food security, nutritional status and income transfers from relatives. The information from the questionnaire was cross-checked by the MMF staff with the local leaders. Apart from the broad poverty criteria MMF used training and weekly meeting attendance and business experience as additional criteria for granting credit.

Business training was, therefore, an integral part of lending activities of MMF to the poor. All registered group members received a minimum basic training of eight days at their respective centres. Training was provided in the areas of business management and operation, group/centre formation, loan procedures and credit management, investment and savings. However, the training program had emphasized on general business management. About 64 percent of the sampled beneficiaries mentioned business management as the training received from the MMF compared to credit repayment (6 percent), savings (7 percent), investment management (5 percent) and market research (5 percent).

3.2 Loan Application Procedures and Repayment

Loan applications were first discussed at group level and then reviewed at centre level before they were submitted to the MMF. However, with emphasis on the role of the centre, the main discussions about loan applications take place at centre level. One advantage with this is that the applicant's proposal is subject to scrutiny by members who are not part of the group and hence the discussions are less influenced by personal considerations. Each individual borrower had to propose the type of business and the amount of loan required to support the proposed business. The business proposal was modified at the centre level before being submitted for funding by MMF. Initially, two members of the group received loans and after successful progress in repayment and attendance, two more members got loans and the group chairperson was the last one to get a loan.[7] In 1990, the average loan size was K275 but improved to K355 in 1994. Once the centre approves the business proposal and submitted to MMF, the time lag between submission and disbursement was short. Normally, successful applicants would get their loans within two weeks of their submission of the loan application. About 81 percent of the beneficiaries indicated that they got their loans within fourteen days. This shows that there was minimum bureaucratic inefficiency in the approval and disbursement of loans. This high level of efficiency was partly a result of decentralisation in the decision making process of MMF management. Most loan approvals (especially those under K1000 were made at branch level since the 1991/92 financial year. In addition, this efficiency was also facilitated by peer review within the group and/or centre framework, which meant that only refined proposals were submitted.

The setting of interest rates on MMF loans was the responsibility of MMF management subject to approval by the Board of Trustees. Interest rates were set at 15 percent per annum since 1990 but were later adjusted to 18.5 percent per annum in 1992 and remained at that level until the MMF was integrated into the MRFC. These interest rates were much lower than those which applied in the commercial banking sector especially for the latter period. For instance, the minimum and maximum lending rates for commercial banks in 1992 were 21 percent and 28 percent per annum, respectively. In 1994, there were further upward adjustment in the interest rate structure which led to the increase in the minimum lending rate for commercial banks to 40 percent per annum. With high levels of inflation real interest rates charged by MMF were actually negative.[8] Initially, loans were repaid over a period of fifty weeks along the lines of the

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[7] This procedure was similar to the operations of the Grameen Bank as documented in Jain (1996).

[8] This contrasts sharply with the interest rate structure in the Mudzi type of services in other countries (see Yaron, 1994; Patten and Rosengard, 1991).

Grameen Bank model. This meant that the scheme demanded regular small repayments which did not take into account the variability of business operations. In addition, some businesses required travelling out of the local area for more than one week and this forced borrowers to withdraw capital from the business in order to meet the loan repayment requirement. However, in 1992, the MMF shortened the repayment period to twenty-five weeks and became more flexible by allowing borrowers to pay more than the minimum weekly repayment requirement in surplus weeks.

4. Impact of MMF on the Poor

4.1 Characteristics of MMF Clientele

The MMF was established to offer credit to beneficiaries of both sexes without any conspicuous bias towards either sex. However, dynamism in the relative performance of female vis-a-vis male borrowers overshadowed the original mandate of the rural financial institution. After the first year of operation, the MMF demonstrated a clear bias towards women. It is argued that this bias was a result of the belief that women tend to be more creditworthy than men. In 1993 all lending was directed at women beneficiaries. The management of MMF contended that it had been demonstrated that the risk of lending to women was less than that associated with extending credit to men.[9] Table 1 shows the distribution of MMF clientele by gender. The table shows that even in the initial phase of the scheme female borrowers were more interested and men were only 27 percent of all scheme beneficiaries.

The average age of borrowers was thirty-eight years , ranging from eighteen years to seventy-seven years, with 83 percent of borrowers within the age range of twenty-five to fifty years. About 97 percent of borrowers owned land and 52 percent owned livestock. In addition, 56 percent of the borrowers ever attended school and were literate. About 40 percent of the borrowers had private savings outside the MMF and 53 percent indicated that the MMF scheme enabled them to increase savings.

[9] See Nyanda et al (1995) for a comprehensive discussion. In effect, nearly all the male beneficiaries had either dropped out of credit or were outright defaulters.

[Table 1 about here]

4.2 Business Characteristics

Business activities operated by MMF loan beneficiaries were concentrated in petty trading. The beneficiary survey indicated that only 30 percent of the borrowers were involved in manufacturing activities prior to obtaining a loan while 69 percent were engaged in petty trading and 1 percent were involved in restaurants and bars. The manufacturing activity was dominated by baking activity accounting for 28 percent of respondents. After obtaining loans there was a noticeable shift in types of business activities towards the trading sector at the expense of manufacturing activities. Some activities like beer brewing were completely abandoned. Beer brewing was not accepted for funding by the MMF as a matter of policy. Complete exits were also noticeable in banana, vegetable, sugar cane and firewood trading. As a result, the manufacturing activities only accounted for 14 percent. There was great interest in fish trading with 38 percent of the beneficiaries responding that they used the loan for fish trading.

[Table 2 about here]

The share of trading activities increased to 82 percent. Data on loan disbursement also confirm the relative orientation of activities towards the trading activities as reported in Table 2. Only 10.3 percent of the cumulative value of the loans were devoted to manufacturing activities while trading activities accounted for 78.2 percent of the value of loans. It is also interesting to note that petty trading was dominated by agricultural produce (65.2 percent) which is highly seasonal. The tendency for beneficiaries to concentrate in particular activities suggest that the peer review process might have had 'demonstration effects' as beneficiaries tended to propose similar operations. It was also revealed in the beneficiary survey that about 35 percent of the businesses were seasonal while 65 percent operated throughout the year.

5.3 Employment Generation

One of the objectives of the Malawi Mudzi Fund was to generate self-employment and paid employment through the provision of credit facilities. The beneficiary survey revealed that incremental self-employment was very modest although underemployment was reduced. Only 15 percent of the sample were not engaged in any business prior to obtaining a loan from MMF and only 5 percent of the sample engaged paid workers. The reason for this low level of employment is that the scheme targeted individuals who were already operating non-farm business ventures.

4.4 Savings Mobilisation

MMF had four types of savings schemes for borrowers: group fund, personal account, emergency fund and special savings account. As Table 3 indicates, the group fund was the largest savings account due to the compulsory nature of the account and the fact that this was also part of the loan from MMF. There has been steady growth in almost all the savings accounts especially for personal savings, special savings and emergency fund. Total savings grew by an average rate of 65 percent between 1990 and 1995.

[Table 3 about here]

Originally, members would utilize the group fund to get personal supplementary loans. However, there was an alteration in the system such that deposits in the group (centre) fund were used exclusively as collateral against regular MMF loans. If any member defaults at the centre, the sum of the centre's group savings was drawn to cover up the default. Furthermore, MMF did not have the incentive structure attached to savings and beneficiaries did not find it worthwhile to voluntary save with MMF. The interest on group savings was not fully passed on to savers and there was no confidentiality in the handling of savings accounts.

4.5 Enterprise Profitability

Although the activities operated by MMF clients were dominated by petty trading, most borrowers were operating profitable businesses. The beneficiary survey indicated that about 84 percent of borrowers operated businesses which were in a position to generate a surplus. About 29 percent of borrowers who were operating profitable businesses used the surplus to meet their food requirements and about 36 percent spent the profits on household durables. The use of the surplus to satisfy borrower's food requirements suggests that business activities financed by MMF had some impact on improving the nutritional status of the borrower's household.

The profitability of business activities operated by MMF clients is also reflected in the high repayment rate of loans in the scheme. In the first year of operation, the default rate was high and reached 41 percent. This is likely for such schemes due to inexperienced working staff, poor choice of target population and problems of information. However, over time the repayment rate has increased. Initially, the repayment period was fifty weeks, but was shortened to twenty-five weeks by 1992. The change in repayment period and the flexibility in repayments had a positive effect on credit performance. The repayment rate increased from 78 percent in 1991 to 99 percent and 108 percent in 1992 and 1993, respectively. The repayment rates are high and were not affected by political dispensation in 1993 as was the case in the Smallholder Agriculture Credit Project (SACP).[10] Although high repayment rates had been achieved about 70 percent of borrowers felt that the repayment period was not reasonable.

[Table 4 about here]

5. Performance of Malawi Mudzi Fund

There is no general agreement on measuring the success of rural financial institutions. Patten and Rosengard (1991) argues that the performance of a financial institution is determined by its efficiency, effectiveness, adaptability, personnel, autonomy and accountability. Yaron (1994),

10 See Msukwa et al (1994) for causes of credit repayment crisis in SACP.

however, proposes that performance should be assessed in terms of self-sustainability and the extent of outreach. It is argued that financial self-sustainability is achieved when the return on equity, net of any subsidy received, is equal to or greater than the opportunity cost of funds. On the other hand, outreach is assessed on the basis of the type of target population served and the quality of services offered including: value and number of loans, value and number of savings accounts, number of branches, real growth of assets and the participation of women. Both approaches are adopted for assessing the performance of Malawi Mudzi Fund in this study.

5.1 Efficiency and Self-Sustainability

It is argued that for a financial institution to operate efficiently the spread between savings and loan interest must cover the cost of intermediation, thus, the cost of operations and loan losses. Table 5 shows the operating income and expenses for MMF between 1990 and 1993. Although, the bottom line for the MMF appears to be mostly in surplus, the Fund did not generate income from within to cover the cost of operations. Income for MMF was dominated by grants from IFAD through the government in form of the Technical Assistance Fund and the Revolving Credit Fund (RCF) which bore interest and service charges of 2 percent and 1 percent per annum, respectively. Operating expenses since 1990 were entirely supported by grants with very little contribution from income generated from within the fund. It is arguable that the MMF relied heavily on subsidies both on rediscounting rates for its funds which in turn tended to enable the fund offer lower on-lending rates to its borrowers. It should also be noted that salaries and administration expenses are more than 50 percent of total expenditure.

[Table 5 about here]

As Yaron (1994) has noted, profit figures are of limited use as an indicator of efficiency or self-sustainability in cases where the rural finance institutions benefit from subsidies. The subsidy dependence index (SDI) which measures the percentage increase in the average on-lending rate required to compensate for eliminating subsidies is used to evaluate sustainability of rural financial institutions. An SDI of zero implies that the finance institution is self-sustainable while an SDI of 100 percent implies that doubling of the on-lending rate is required if all subsidies are to be eliminated. A negative SDI indicates that the finance institution has more than achieved self-sustainability. In the case of MMF the subsidy was mostly on its grant funds which attracted only 3 percent of interest and service charges per annum. This influenced it to on-lend the funds at below market interest rates. In calculating the SDI it was assumed that the funds from IFAD through the government attracted a market discount rate as if the cost of funds were not subsidized.

[Table 6 about here]

Activities of MMF reveal a high dependence on subsidies as reflected by the SDI in Table 6. For instance, if the scheme were to be self-sustainable in 1994, the on-lending interest rate was supposed to be adjusted upwards by four thousand percent hence leading to an effective lending rate of 752 percent which would be higher than those typically offered in the informal markets. These indices compare unfavourably with those obtained in the case of Grameen Bank in Bangladesh.[11]

Four factors have been identified as critical in the elimination of dependence on subsidies: positive on-lending interest rates, high rates of loan collection, encouragement of voluntary savings and the reduction in administrative costs.[12] Within this framework, several reasons that can be attributed to the high subsidy dependence in the case of Malawi Mudzi Fund. Firstly, the on-lending interest rate was set at low levels especially in subsequent periods. The design of the project was based on the assumption that both accessibility and cost of credit were critical in determining credit uptake in Malawi. However, with high levels of inflation the real interest rates were negative in 1992 and 1993. It should also be apparent from Table 5 that the contribution of loan interest to total income is very modest. In 1992 and 1993, loan interest income were 2.9 percent and 2.5 percent of total expenses, respectively. The loan interest income generated could not support even the cost of personnel. In essence, loan interest income

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11 In fact the Grameen Bank which was supported by IFAD had the highest SDI among the four Asian rural finance institutions reviewed by Yaron (1994). It was argued that IFAD provided low-cost funds to Grameen Bank.

12 See Yaron (1994) and Patten and Rosengard (1991).

was on average only 7.5 percent of salaries and wages paid to MMF staff.[13] The major problem in the design of the MMF was the assumption that high rates of interest on formal credit rather than access to credit facilities was the major factor in affecting the uptake of credit facilities by the poor. However, as Yaron (1994) has argued it is the converse which is true in the case of the Asian rural finance institutions. There is evidence in Malawi that the poor have actually financed their small scale enterprises through credit facilities extended by the informal financial sector (money lenders) whose lending rates ranged from 300 to 1,200 percent per annum (Chipeta and Mkandawire, 1991). The low interest rates have greatly affected the self-sustainability and the efficiency of MMF operations.

Secondly, in terms of loan recovery, default rates have not been high in MMF especially in the post-1990 periods. However, in some cases the repayment rate has been lower compared to those which were achieved in the agricultural credit facility administered by SACA. On average, between 1990 and 1994 the repayment rate was 79 percent. Such recovery rates do not justify the excessive administrative and operating expenses. Moreover, there were no transparent incentives for borrowers who manage to pay the loan within or before the loan period, apart from getting a new and slightly bigger loan.

Thirdly, perhaps one of the most critical failures of the Malawi Mudzi Fund is its lack of acumen for developing into a full financial institution providing both lending and banking (saving) services for the rural poor. Savings mobilisation did not feature prominently on MMF activities. Weekly compulsory savings rates were set at very low levels, initially at 20 tambala (US$0.07) and adjusted to K1 (US$0.29). Compulsory group (centre) savings which were in form of an additional loan from the MMF was the largest savings component of the scheme.

[Table 7 about here]

Voluntary savings were not encouraged. MMF seem to have focused so much attention on compulsory savings scheme which later became a form of collateral for loans obtained by centre

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13 These figures compare unfavourably to similar rural finance institutions in Indonesia (see Patten and Rosengard, 1991).

members. The growing interest in using savings as collateral as opposed to enforcing the group liability principle, led to the oversight in the need to mobilise voluntary savings. As indicated in Table 7, total savings as a proportion of loan portfolio were under 25 percent except for 1991 when the ratio was about 40 percent. Voluntary savings as a ratio of total savings were also modest except in 1992 and 1993. A more gloomy situation is revealed by the ratio of voluntary savings to total loan portfolio, the highest being 9 percent in 1992. In any case, the MMF situation in terms of voluntary savings is better than those observed in Asian institutions such as BKK and Grameen Bank. It should be observed that there was no transparent interest structure available to savers. Indeed, the financial accounts first indicated interest on savings in 1993 and this interest was not paid to beneficiaries unless they were dropping from the scheme and if none of the centre member had defaulted. There was, therefore, no incentive to save voluntarily within the MMF and most beneficiaries interviewed indicated that they had savings schemes outside the fund.

Finally, the cost of operating the rural finance institution in Malawi has been prohibitively high. Although the selected pilot areas for the project were densely populated and land constrained, administratively it was expensive to run the project. Personnel and administrative expenses were astronomical compared to the return in terms of loan disbursement and savings mobilisation.

[Table 8 about here]

Table 8 shows the relative operational costs of Malawi Mudzi Fund in relation to total assets, savings and loan portfolio. These figures are extremely high even compared with those of the Asian rural finance institutions (cf. Yaron, 1994). As a proportion of assets administrative and operating expenses were 53 percent in 1990 but increased to 71 percent in 1993. Higher inefficiencies are indicated by the proportion of administrative and operating expenses to the loan portfolio or savings. The figures indicate that for a unit value of the loans, MMF spent on average 327 percent on disbursing that loan in 1990 and about one and half thousand percent in 1992. Similarly, for a unit value of savings mobilised the MMF spent more than thirty times. Actually, administrative and operating expenses per beneficiary ranged from K451 per annum in 1991 to K510 per annum in 1992.

Several factors are attributed to the high expenditure pattern of the MMF. Firstly, the target areas were not as densely populated as conceptualized. This meant that a few groups could form a centre. In some cases centres could comprise of 9 - 15 members (two to three groups). Furthermore, branch offices from where project officers were operating were very far from project areas and this increased transport costs. Secondly, staff training in form of external study tours and short-term courses, which did not yield significant marginal contribution to the operational efficiency of the scheme, were very much emphasized. Almost every staff member from project officer to scheme administrator had been out of the country for study tours in Bangladesh and Indonesia. In addition, in spite of the training and the remuneration, there was a very high labour turnover with most members resigning from their posts. Thirdly, there is a tendency for donor funded projects to pay its staff more than the market wages (slack payments) even in cases of low return projects; the wage bill for staff was the largest expenditure item. Finally, since the scheme was operating on a non-profit objective basis there was no incentive for the management to devise cost containment measures or to improve their operational efficiency. For instance, there was no bonus scheme accorded to members of staff for operational efficiency.

5.2 Effectiveness and Outreach

The effectiveness of rural finance institutions can be assessed in terms of meeting the stated objectives such as clientele coverage, credit extended and savings mobilised. These ingredients constitute outreach of rural finance institutions. As stated earlier, the Malawi Mudzi Fund was established to provide loans and technical assistance to Malawians in rural areas for the purpose of generating self employment in off-farm activities of their choice and to enable the creation of a savings scheme for such activities. It is within these objectives that effectiveness and outreach will be evaluated.

In terms of the target population, MMF served the rural poor in areas where agricultural land was a constraint. Originally, the scheme targeted both men and women, but later it became a policy that credit will only be extended to women. However, as indicated in Nyanda et al (1995), due to the vagueness in the eligibility criteria used the scheme benefited some members which were relatively better economically. The number of beneficiaries to the scheme increased from 900 in 1990 to 2,443 in 1994, representing an annual average growth of 54.3 percent. This was a remarkable achievement.

Credit extended to rural poor within the MMF framework has grown at an average annual rate of 73 percent between 1990 and 1994. Loans rarely exceeded K1,000 per person. Although the International Fund for Agriculture Development provided a Revolving Credit Fund of about K500,000 in 1991, only a small proportion of the fund was utilised. Loans disbursed to borrowers averaged K137,000 per annum, ranging from K33,000 to K327,000. The value of loans per worker in 1994 was K14,843. It can be argued that although MMF received separate funds for technical assistance and enterprise development, due to high operational costs credit extension was greatly stifled by the need to support operational expenses.

Saving mobilisation has been the most difficult task for the MMF. In absolute terms, as pointed out earlier emphasis was placed on compulsory savings with very little focus on voluntary savings. In growth terms, MMF data indicates that savings have been growing at an annual average rate of 65 percent. In 1994, the value of savings per MMF worker was K2,180. Savings were affected by lack of incentives within MMF to savings accounts, and efficient and effective banking services were not therefore provided to the beneficiaries in the villages. In any case, MMF was in a better position to market its savings services as the banking facility eliminated transaction costs to its beneficiaries.

In 1994, the MMF employed 22 workers with a head office and two branch offices. The scheme administrator was head of management, and the two branches were headed by branch managers who reported directly to the scheme administrator. There was one accountant assisted by three assistants (one at each branch). Seven project officers were directly involved in daily field activities. Other support staff included three messengers, three watchmen, one driver and two secretaries. Training was adequately provided and workers expressed satisfaction at their remuneration. However, there were no performance related bonuses, which arguably contributed to inefficient operations of the scheme.

Training to beneficiaries was also provided. This is one aspect of the service that the MMF had provided apart from credit extension. Funds for training of beneficiaries were provided for in the technical assistance grant from IFAD. All beneficiaries were exposed to at least eight days training in basic business management and a selected few also attended MMF organised workshops.

6. Conclusion

This article has reviewed the activities of Malawi Mudzi Fund between 1990 and 1994 before it was integrated into Malawi Rural Finance Company. MMF was a replica of the Grameen Bank of Bangladesh with very slight modifications which essentially occurred during the adaptation of the scheme to the Malawian socio-economic environment. Nonetheless, basic tenets of the Grameen Bank governed the *modus operandi* of MMF. In any case, the replication of the successful Asian rural finance institutions in other less developed countries with different socio-economic characteristics has been less successful.

The MMF had become a women's rural finance institution by default thereby eliminating potential beneficiaries from the male target population. MMF has experienced problems of high default rates in some years and loans have tended to support petty trading off-farm activities. On the positive side, the MMF had extended credit to the rural poor based on joint liability principles (although this was not practically enforced) despite the switch to group savings as a collateral at a later stage. Savings have grown considerably in relative terms over the years although focus had been on compulsory savings vis-a-vis voluntary savings. Most beneficiaries have been exposed to business management training. The beneficiary survey indicated that none of the beneficiaries had attended training prior to becoming a member of the MMF.

Two major problems may be of particular importance in the development of rural finance institutions in Malawi, and hence the replicability of the Asian models to Malawi. Firstly, the MMF was a supply-led credit institution and ignored the importance of savings mobilisation as a sustainability factor in the development of rural finance institutions. The MMF failed to provide full banking facilities to the poor: no tangible interest was paid on savings, depositors could not make withdrawals on demand and the various savings schemes confused depositors. It is important therefore, that the development of rural finance institutions should strike a balance between credit extension and savings mobilisation to ensure self-sustainability.

Secondly, the over-reliance on donor or government low cost funds may constrain the development of rural finance institutions. This has led to the low spread between lending and savings rates and has contributed negatively to self-sustainability. Perhaps, one major constraint in the operation of the MMF was its persistent dependence on low cost funds. Like the Grameen Bank, the Malawi Mudzi Fund had been funded by IFAD and it was highly poverty-oriented drawing funds at 3 percent and on-lending at low interest rates. MMF depended heavily on subsidies from the government and donors. The subsidy dependence index has indicated the MMF was far from achieving self-sustainability. It is arguable, therefore that this continued dependence on low cost finance had encouraged misallocation of resources which led to high administrative and operating costs which were not commensurate with the output of the scheme. This raises the question of whether access to credit or cost of credit is the central issue affecting the up-take of credit facilities by the poor. This is the question governments and donors have to evaluate before implementing the MMF type of institutions.

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Table 1. MMF Beneficiaries by Gender

Year	Number of Groups			Number of Members		
	Male	Female	Total	Male	Female	Total
1990	48	132	180	240	660	900
1991	2	32	34	10	160	170
1992	-	89	89	-	337	337
1993	-	85	85	-	419	419
1994	-	123	123	-	617	617
Total	**50**	**461**	**511**	**250**	**2,193**	**2,443**

Source: Nyanda *et al*. (1995)

Table 2. Loan Disbursement by Type of Activity

Business Activity	Number of Loans	Value of Loans (Kwacha)	Value of Loans (%)
Manufacturing:	**265**	**70,745.00**	**10.30**
Baking	252	67,325.00	9.80
Weaving/Knitting	2	415.00	0.06
Tinsmith	4	1,330.00	0.19
Cane Furniture	7	1,675.00	0.24
Trading: Agriculture	**1,534**	**447,788.00**	**65.17**
Fish	754	230,417.00	33.53
Maize	213	35,583.00	5.18
Rice	182	51,335.00	7.47
Potatoes	4	1,370.00	0.20
Bananas	2	505.00	0.07
Beans	279	101,798.00	14.81
Groundnuts	63	17,855.00	2.60
Firewood	5	1,370.00	0.20
Pepper	3	900.00	0.13
Vegetables	15	2,450.00	0.36
Chickens	12	3,485.00	0.51
Sorghum/Millet	2	720.00	0.10
Trading: Non-Agriculture	**372**	**92,336.00**	**13.44**
Maize Flour	25	5,850.00	0.85
Salt	9	1,360.00	0.20
Clothes	127	53,771.00	7.83
Groceries	162	14,545.00	2.12
Sacks	1	250.00	0.04
Sugar	35	12,770.00	1.86
Plastics	2	600.00	0.09
Quarry	1	600.00	0.09
Butchery	8	2,225.00	0.32
Freezes	1	265.00	0.04
Paraffin	1	100.00	0.01
Other:	**409**	**76,268.00**	**11.10**
Restaurant	28	11,330.00	1.65
Tea Room	20	5,325.00	0.77
Agriculture	333	50,153.00	7.30
Other	28	9,460.00	1.38
TOTAL	**2,580**	**687,137.00**	**100.00**

Source: Nyanda *et al.* (1995)

Table 3. Malawi Mudzi Savings Schemes, 1990 -1995 (Malawi Kwacha)

Year	Group Fund	Personal Savings	Emergency Fund	Special Savings	Total
1990	7,455.00	1,259.00	-	-	8,714.00
1991	10,509.00	2,189.00	330.00	207.00	13,235.00
1992	4,250.00	4,379.00	1,948.00	231.00	10,808.00
1993	11,141.00	9,543.00	5,234.00	654.00	26,572.00
1994[1]	23,665.00	11,116.00	11,944.00	1,263.00	47,988.00

Note: 1. For period between April to December 1994

Source: Nyanda *et al.* (1995)

Table 4. Volume of Loans and Repayment Performance

Year	Number of Loans	Loans Disbursed (Kwacha)	Loans Repaid (Kwacha)	Loan Repayment Rate (%)
1990	478	130,765.00	77,185.00	59.0
1991	168	33,164.00	24,864.00	75.0
1992	223	49,416.00	48,820.00	98.8
1993	621	143,189.00	155,129.00	108.3
1994[1]	921	326,537.00	231,250.00	70.8
TOTAL	**2,411**	**683,071.00**	**537,248.00**	**78.7**

Note: 1. For period between April to December 1994

Source: Nyanda *et al.* (1995)

Table 5. Income and Expenditure for MMF, 1990-1993

Item	1990	1991	1992	1993
INCOME				
Grants Received	552,971.00	400,893.00	513,680.00	972,016.00
Foreign Exchange Gains	-	-	30,035.00	-
Income and Sundry Income	10,584.00	91,858.00	-	-
Loan Interest	-	-	20,933.00	24,242.00
Investment Income	-	-	92,460.00	156,921.00
Other Income	-	-	50.00	402.00
Total Income	**563,555.00**	**492,751.00**	**657,158.00**	**1,153,581.00**
EXPENSES				
Interest Paid to RCF	-	15,370.00	15,000.00	15,000.00
Interest on Savings	-	-	-	5,384.00
Salaries and Wages	134,475.00	141,302.00	247,389.00	375,631.00
Transport and Travel	58,492.00	55,799.00	112,949.00	92,694.00
Training	29,793.00	48,581.00	83,237.00	62,723.00
Administration	143,702.00	156,146.00	140,358.00	236,677.00
Provisions- Doubtful debt	-	9,189.00	-	80,288.00
Depreciation	39,455.00	44,966.00	51,396.00	50,890.00
Other Expenses	20,066.00	21,192.00	67,169.00	44,571.00
Total Expenses	**425,983.00**	**492,545.00**	**717,498.00**	**963,858.00**
Surplus /(Deficit)	**137,572.00**	**206.00**	**(60,340)**	**189,723.00**

Note: RCF = Revolving Credit Fund

Source: Nyanda *et al.* (1995)

Table 6. Subsidy Dependence Index (percent)

Indicator	1990	1991	1992	1993
Subsidy Dependence Index	4,708	2,227	3,305	3,967
Nominal Lending Rate	15	15	18.5	18.5
Real Lending Rate	3.2	2.7	-3.9	-3.4
Effective Nominal Lending Rate that eliminates all subsidies	721.3	349.1	630.0	752.0

Source: Nyanda *et al.* (1995) and Author's calculations.

Table 7. Savings Mobilisation by MMF, 1990-1994 (percent)

Year	Voluntary Savings/Total Savings	Voluntary Savings/Loan Ratio	Total Savings/Loan Ratio
1990	14.4	1.0	6.7
1991	18.1	7.2	39.9
1992	42.7	9.3	21.9
1993	38.4	7.1	18.6
1994[1]	25.8	3.7	14.7

Note: 1. For period between April to December 1994

Source: Author's calculations.

Table 8. Administrative and Operating Costs of MMF, 1990-1993 (percent)

Year	Expenses/Total Assets Ratio	Expenses/Loan Portfolio Ratio	Expenses/Savings Ratio
1990	53.3	325.8	4,888.5
1991	60.9	1,457.5	3,652.1
1992	59.4	1,452.0	6,638.6
1993	70.9	617.1	3,325.2

Note: Expenses are net of provision of doubtful debts.

Source: Author's calculations.