Micro and Rural Finance in Ghana: Evolving Industry and Approaches to Regulation

Legislation and regulations governing rural and micro finance institutions (RMFIs) in Ghana have evolved with the market, both opening up possibilities for new types of institutions and tightening up to restrain excessive entry and weak performance in the face of inadequate supervision capacity. The result — though not by conscious design — is several tiers of different types of RMFIs with a strong savings orientation and a much greater role of licensed institutions relative to Non-governmental Organizations (NGOs) than is found in many countries. Small unit Rural and Community Banks (RCBs) are accommodated in the Banking Act; savings and loan companies under the Non-Bank Financial Institutions (NBFIs) Law; and Credit Unions (CUs) under a new law being prepared to recognize their dual nature as cooperatives and financial institutions. The informal sector is dominated by a variety of savings-based methodologies, both individual and group.

Structure and performance of Ghana’s rural and micro finance industry

The financial system in Ghana falls into three main categories: formal, semi-formal, and informal. The commercial banking system, which is dominated by a few major banks (among the total of 17), reaches only about 5 percent of households, most of which are excluded by high minimum deposit requirements. With 60 percent of the money supply outside the commercial banking system, the rural banks, savings and loans companies, and the semi-formal and informal financial systems play a particularly important role in Ghana’s private sector development and poverty reduction strategies. The assets of RCBs are nearly 4 percent of those of the commercial banking systems, with S&Ls and CUs adding another 2 percent. While the term “RMFIs” is used to refer collectively to the full range of these institutions, they use different methodologies to reach different (albeit overlapping) clientele among farmers, rural households, the poor, and
microenterprises, and hence different regulatory and supervisory instruments may be appropriate.

- **Formal financial institutions** are incorporated under the Companies Code 1963, which gives them legal identities as limited liability companies, and subsequently licensed by the Bank of Ghana (BOG) under either the Banking Law 1989 or NBFI Law 1993 to provide financial services under Bank of Ghana regulation. The 115 Rural and Community Banks (RCBs) operate as commercial banks under the Banking Law, except that they cannot undertake foreign exchange operations, their clientele is drawn from their local catchment area, and their minimum capital requirement is significantly lower. They have some 1.2 million depositors and about 150,000 borrowers (some of these represent groups through collaboration with NGOs using microfinance methodologies). Only a few exceed 20,000 clients. Among the nine specified categories of NBFI, the Savings and Loans Companies (S&Ls), which are restricted to a limited range of services, are most active in micro and small-scale financial intermediation using microfinance methodologies. One leasing company has opened a micro-leasing window.

- NGOs and the CUs are considered to be the semi formal system, in that they are formally registered, but are not licensed by the Bank of Ghana. NGOs are incorporated as companies limited by guarantee (not for profit) under the Companies Code. Although some 50 NGOs have active microcredit programs, they are generally multipurpose or welfare-oriented agencies (only 4 exceed 3,000 clients and total outreach is only about 60,000 clients: GHAMFIN 2003). Their poverty focus leads them to relatively deep penetration of the poor clients base using microfinance methodologies (see Box 1), though mostly on a limited scale. They are not licensed to take deposits from the public and hence have to use external (usually donor) funds for microcredit. Credit Unions are registered by the Department of Cooperatives as cooperative thrift societies that can accept deposits from and give loans to their members only. At the end of 2002 CUA had 253 affiliates with 123,204 members, and their average loan size of US$153 is well above that for African MFIs, as well as for RCBs. Although credit unions are included in the NBFI Law, the Bank of Ghana has allowed the apex body, the Ghana Cooperative Credit Union Association to continue to regulate the societies pending the introduction of a new Credit Union Law that would explicitly recognize the dual authority of the Cooperatives Department and BOG.

- The informal financial system covers a range of activities known as susu, including individual savings collectors, rotating savings and credit associations, and savings and credit "clubs" run by an operator (see Box 2). It also includes moneylenders, trade creditors, self-

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**Box 1: Types of microfinance group and individual savings and credit programs**

**Group savings with credit:** A group of members (whether pre-existing or formed for this purpose) open a joint bank savings account and mobilize initial savings deposits to qualify for a loan. Group savings may be used as security against loans, and also are used to invest in T-bills for the group. Groups usually are made up of 3-4 sub-solidarity groups.

**Group and individual savings with credit:** Group members contribute to both a joint group account and their individual accounts. The group may be a "village bank" of 25-40 members; or as small as five members. While both individual and group savings accounts are used as collateral, the individual account includes the member's additional personal savings. Loan repayments are made by individuals but handled through the group account. Examples include Nsoatreman, Bosomtwe, and Lower Fra RBs.

**Individual savings with group credit:** Individuals lodge their savings through the group, which receives a loan for distribution to members after a qualifying period and collection of the required level of savings, and they continue to save into their individual accounts as they repay the loan. The group handles the collection of savings and repayments, acts as the interface with the loan officer, and bears group responsibility for recovery (though the loans are made to individual members). Example: Freedom from Hunger's Credit with Education program, operated through Brakwa, Lower Fra, Nsoatreman and Nandom RBs, Bulsa Community Bank, and Women's World Banking Ghana (Quainoo 1997, p. 47).

**Individual savings with credit:** Direct lending to individuals, either those who had established a credible history as a member of a group but who need larger or separate loans, or in cases where a group approach is not suitable. Examples: Lower Fra RB; Nsoatreman RB's District Assembly Poverty Alleviation Program.

_Source: Chord 2000._
help groups, and personal loans from friends and relatives.

**Flexible policy and supervision regime**

Liberalization of financial policies in the late 1980s enabled RMFIs to develop with relatively little interference, even without a clearly articulated national strategy. Nevertheless, continued high inflation and interest rates (particularly on Treasury Bills) has limited the incentive for commercial financial institutions to reach out to smaller, poorer clients (though enabling weak RCBs to improve their capital adequacy with highly restricted lending). Currently, directed, subsidized loans under special government poverty programs threaten to undermine loan performance and weaken the long-run potential for developing sound, self-sustaining RMFIs on a significant scale.

Supervision of a large number of RMFIs is costly relative to their potential impact on the financial system (about 7 percent of assets), and the Bank of Ghana has adopted a number of strategies to cope with its limited supervision capacity: raising reserve requirement for RCBs to as high as 62 percent; drastically raising the (previously low) minimum capital requirement for NBFIs; and permitting self-regulation of credit unions by their apex body. It is currently establishing an Apex Bank to serve the RCBs, link them more effectively to the commercial banking system, take the lead in building their capacity, and, eventually, in undertaking front-line supervision. Although the US$82 million minimum capital requirement makes the S&Ls less accessible for NGO transformation, it has led to some introduction of foreign capital.

While the RCBs have had limited outreach, some have effectively partnered with NGOs to introduce microfinance methodologies such as village banking, and they are now being strengthened as the backbone for the expansion of rural financial services. Linkages also occur between informal savings-based “susu” institutions and both RCBs and S&Ls. The Bank of Ghana has taken a relatively laissez-faire position vis-à-vis the informal sector.

**Box 2: Types of susu (savings collection) in Ghana**

Ghana has at least five different types of institutions known as, or offering products termed **susu**

- **Susu collectors**: Individuals who collect daily amounts set by each of their clients (e.g., traders in the market) and return the accumulated amount at the end of the month, minus one day’s amount as a commission.

- **Susu associations** or mutualist groups are of two types: (i) a rotating savings and credit association (ROSCA), whose members regularly (e.g., weekly or monthly) contribute a fixed amount that is allocated to each member in turn (according to lottery, bidding, or other system that the group establishes); (ii) accumulating, whose members make regular contributions and whose funds may be lent to members or paid out under certain circumstances (e.g., death of a family member).

- **Susu clubs** are a combination of the above systems operated by a single individual, in which members commit to saving toward a sum that each decides over a 50- or 100-week cycle, paying a 10 percent commission on each payment and an additional fee when they are advanced the targeted amount earlier in the cycle; they have existed at least since the mid-1970s, quite likely earlier.

- **Susu companies** existed only in the late 1980s as registered businesses whose employees collected daily savings using regular susu collector methodology, but promised loans (typically twice the amount saved) after a minimum period of at least six months.

- Some licensed financial institutions (commercial banks, insurance companies, RCBs, S&Ls, and credit unions) have offered a systematic savings plan termed “susu,” sometimes hiring employees to go out and gather the savings in the manner of a susu collector. The State Insurance Corporation first introduced such a “Money Back” product in the 1980s, including a life insurance benefit for clients as an additional incentive to mobilize savings, but the scheme was discontinued in 1999.

**Conclusions**

While Ghana’s approach has yielded a wide range of RMFIs and products with the potential for substantial outreach to the poor and sustainability based on savings mobilization, it has also permitted the easy entry of institutions with weak management and internal controls. Ghana’s experience demonstrates the difficulty of striking the right balance between encouraging entry and innovation on the one hand and establishing adequate supervision capacity on the other. In several segments—RCBs, credit unions, S&Ls—Ghana has gone through a cycle of easy entry, weak performance, tightening up regulations, and
some restructuring (through closing insolvent units, takeovers, or infusion of new investment). The Bank of Ghana has exercised considerable regulatory forbearance in allowing weak units time to comply with stricter regulations (or, in the case of the credit unions, to establish a self-regulating system while awaiting passage of a new law).

On the whole, this approach appears to have succeeded in giving Ghana a very diverse, reasonably robust system of RMFIs, with relatively little cost in terms of outright failed institutions (and lost deposits) and moderate drain on supervisory resources. Nevertheless, the system has failed to achieve impressive outreach, especially to the rural poor, and remains burdened by a number of weak units that the regulatory authorities are not well equipped to turn around.


References


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