

# Rural development in ghana



**ASSIGN  
BUSTER**

The problems of rural development in the Third World and in Ghana in particular, have become a major concern today. This concern notwithstanding, the problems seem as intractable as ever. There are significant disparities in income and standards of living between the rural and urban populations (GPRS, 2004). This has resulted in the continuous increase in the movement of people from the countryside to the city, creating a serious social crisis, the ramification of which is affecting the quality of life. The manifestations of this include; people sleeping on pavements and others sprawling in shanty slums, ragged beggars, crimes and other deviant behaviours such as prostitution, drug addiction and alcohol abuse. (GPRS, 2004)

About 60% of Ghana's population lives in rural areas and this can be regarded as a channel for economic growth and development in the rural areas and the country as a whole. This trend is a great potential and when adequately harnessed can lead to sustainable rural development. To achieve this, various strategies are designed to improve the economic and social life rural dwellers. Such strategies tend to include livelihood programmes aimed at the rural poor. Some of these strategies include agro-based industrialization (agricultural processing), effective decentralization and private sector development (GPRS, 2004).

The success of these strategies hinges on a well functioning financial sector. It is generally accepted that financial development is a prerequisite to economic development. Hence, Microfinance Institutions (MFIs) are indispensable to economic growth and development and thereby the reduction of poverty (Heidhues and Schrieder, 1999).

Furthermore, Heidhues and Schrieder, (1999) argued among others that financial markets are significant for economic progress, hence the inaccessibility of financial markets can be seen as a barrier to rural entrepreneurs and rural enterprise development

The Nadowli District depicts a typical rural economy dominated by the agricultural sector with the commerce and industrial sectors least developed. Agriculture alone employs about 85% of the labour force while commerce/service and industry account for 14% and 1% respectively.

The commerce/service sector is the second largest employer of the district's labor force after agriculture. It encapsulates a wide range of tertiary activities. These include retailing and petty trading, transport and financial services among other services (Nadowli District, MTDP, 2004).

There is only one financial institution in the district. This is the Sonzelle Rural Bank Agency in Nadowli and its branch in Kaleo. The main focus of rural banks is to:

Provide loans for agricultural activities

Provide loans for commerce and small scale industries

Provide security for client savings (Nadowli District, MTDP, 2004).

However, this financial institution has failed to provide the needed support for the various economic sectors in the district particularly agriculture and commerce. This state of affairs is a limitation to enterprise development and expansion.

As indicated in the district medium term developments plan, the following are the major challenges faced by rural enterprises in the district:

Poor marketing opportunities

Limited finance

Poor technology in production (Nadowli District, MTDP, 2004).

The study therefore looks at the contribution of MFIs in the development of Rural Enterprises and the rural population as a whole.

## **1.2 Problem Situation and Statement**

It is estimated that ' About 66% of Ghanaians live in settlements of less than 5, 000 people, which are defined as rural' (GPRS, 2004). Agriculture is still the main economic activity in rural areas of Ghana constituting about (67. 2%) of the labour force and the private informal sector (24. 7%). The government sector employs only 3. 9% and about 4. 2% is employed by the private formal sector (GLSS 4, 2000).

Notwithstanding the immense contribution of agricultural and the private informal sectors to national development, they are bedeviled with numerous problems, of which limited access to financial resources is the most frequently cited by entrepreneurs. Hence, any development attempts by these sectors require capital formation, of which efficient financial markets play a key role (Mckinnon, 1973)

The country has over the past decades seen the proliferation of Financial Institutions and Non-Governmental Organizations (NGOs) which provide

microfinance services and or programs. The attention these programs have drawn stems philosophically from progress in cultivating self-sufficiency among those in abject poverty, and practically from the viability and high loan repayment rates of many microfinance institutions. The programs assume that lack of or inadequate capital is the main barrier to the economic progress of the poor. The lack of entrepreneur business management experience and training, however, may create a barrier equally powerful and limit the growth potential of microenterprises. This is spurred by its popularity as a spatial development tool and a panacea to the financial needs of rural entrepreneurs, who are often unable to meet the loan acquisition requirements of conventional commercial banks, the management and control of which is vested in the people as enshrined in the Banking Law 1989 (Decree 225) (Ghana: Banking law Document).

Research shows that rural finance contributes to community economic development by lifting the poor and low-income people out of poverty by enabling them to engage in more productive farm and non-farm income-generating activities to raise their living standards (Zeller et al, 1996). The effects of these are manifested in improvement in their nutritional status, health and education, particularly in women and children (MkNelly and Dunford 1999, Khandker 1998, Wright 2000).

This brings to the fore the critical challenge facing all developing countries of the need to stimulate the development of rural enterprises, because there is growing acknowledgement that these enterprises can contribute substantially to the creation of a stable civil society and the equitable distribution of wealth and opportunities.

<https://assignbuster.com/rural-development-in-ghana/>

To overcome the financial constraints confronting rural enterprises, all developing countries, including Ghana, have developed various forms of innovative financial intermediaries over the years to provide the necessary financial and other support services required to stimulate their development. In Ghana, amongst the various forms of financial institutions initiated to promote the development of rural enterprises are the Rural Banking System, Micro-finance and Small Loans Centres (MASLOC), the establishment of National Board for Small Scale Industries (NBSSI), The Social Investment Fund (SIF), GRATIS FOUNDATION, Formal/private sector commercial firms (Lead firms), Food and Drugs Board (FDB), Ghana Standards Board (GSB), Ghana Export Promotion Council (GEPC), District Assemblies among others for the rapid development of enterprises in the country (Aggrey, 1993).

The mandate of these institutions includes the mobilisation of financial resources within the locality, inter alia, for investment principally in the development of rural enterprises, as observed by Aggrey-Mensah (1993). These institutions exist to provide financial support, training and technical knowledge among others to agro-based industries (Shea-nut and groundnut processing, cereal milling, weaving) as well as handicrafts production, trading, construction and transport services amongst others. The question that lingers on is; to what extent do MFIs contribute to the development of rural enterprises in the district?

It is in this state of affairs that necessitates the launch of this study into the operations of microfinance institutions, to assess the performance of the rural enterprises that have benefited from microfinance institutions' support and how this is reflected in the living standards of the beneficiaries.

### **1. 3 Research Questions:**

The main question addressed by this study is; to what extent do MFIs contribute to the development of rural enterprises the Nadowli District.

To achieve this, the following specific research questions are to be addressed:

What type of support or service is being provided by microfinance institutions to rural enterprise?

Do rural enterprises have access to micro financial services?

What are the conditions under which these support or services are provided?

How are the credits utilized by the beneficiaries?

What are the impacts of these on the development of rural enterprises and the livelihoods of the entrepreneurs?

What are the weaknesses and strengths of MFIs in the delivery of financial services to rural entrepreneurs?

### **1. 4 General Objectives:**

The general objective of the study is to assess the contribution of microfinance institutions to rural enterprises development in the study area.

To achieve this, the following specific objectives will pursued:

To find out the type and extent of support being provided by MFIs to rural enterprises.

To find out whether rural enterprises have access to micro financial services.

To investigate the conditions under which these supports are provided for rural enterprise development.

To analyze the utilization of the financial support given to beneficiaries and the impact on the performance of enterprises and local economic development.

To identify weaknesses and strengths in the existing management system in the delivery of financial services to rural entrepreneurs.

To make recommendations based on findings for the growth and sustainable development of rural enterprises in the study area.

### **1. 5 Scope of the Study:**

The research will be conducted in the Nadowli Districts (ND) of the Upper West Region of Ghana. The study will also focus on the credit facility provided by MFIs to rural entrepreneurs (males and females) between 2000 and 2010 who undertook non-agricultural activities for commercial purposes and how effectively these enterprises are utilizing these financial supports. The key variables to be studied include the credit quantity and transaction cost, credit targeting, delivery and support services. The rest are credit utilization, enterprise performance, change in household incomes and employment generation.

### **1. 6 Research Methodology:**

The main research design to be adopted is the Cross-Sectional Design, with Case Study as the specific method. This is an empirical enquiry that allows



the researcher to investigate and understand the dynamics of a particular system. It investigates contemporary phenomena within real life situations. Hence the case study method permits generalization of the findings (Twumasi, 2001).

The “ before” and “ after” comparison will also be adopted to assess the impact of the loans on enterprise performance in relation to changes in outputs, sales and employment. These changes observed will be analyzed in relation to the interventions of Micro Finance Institutions in the area.

### **1. 6. 1 Data Sources and Collection Methods:**

Both primary and secondary data sources will be used. The primary data intends to elicit useful information from the Micro Financial Institutions’ staff that will include savings and credit targeting, delivery and support services and loan performance, while such variables as credit utilization, enterprise performance, change in household incomes and employment generation will be elicited from entrepreneurs who are engaged in agro-processing, trading, construction, transport and other services and have had access to loans from the micro financial institutions. The secondary sources will include records and other documentations.

In view of this, a two-pronged approach will be employed in the study, focusing on both supply and demand issues in relation to the financing of rural enterprises in the study area (Twumasi, 2001).

## **1. 6. 2 Data collection tools:**

Both quantitative and qualitative research methods shall be employed to facilitate the primary data collection process. Specifically, the following methods shall be used:

Questionnaire is simply a self-administered interview. Thus, it requires particularly self-explanatory instructions and question design since there is often no interviewer or proctor present to interpret the questionnaire to the subject. (Smith, 1975: 170). This method shall be employed in generating information from staff of NGOs and complementing agencies that are into the area of rural enterprise development in the district. This will facilitate the gathering of quantitative data on the objectives. Open-ended and close-ended questions will be used to respond to the demand of the various variables in the analysis. An open-ended question is a question the leaves the respondent free to respond in a relatively unrestricted manner. By contrast, a closed-ended question restricts choice of response by forcing the respondent to respond in terms of present categories or alternatives. (Smith, 1975: 172)

Interviews shall be conducted to generate qualitative information about the trends, levels, and challenges involved in RED by the MFIs. Cannell and Kahn (1968: 530) have defined the interview as a conversation with purpose specifically the purpose of information-getting. Maccoby and Maccoby, (1954: 499) as in Smith (1975: 170), view interview as a peculiar verbal interactional exchange “ in which one person, the interviewer, attempts to elicit information or expressions of opinions or belief from another person or persons”. Structured and semi-structured interviews shall target staff of

MFIs, and other NGOs who are collaborators to the services of the studied MFIs in the district as well as beneficiary individuals, groups of individuals and communities within the area of study.

Focus Group Interviews will be employed in the study of MFIs interventions that are more of group or community benefit than individualistic.

### **1. 6. 3 Sampling technique:**

In terms of sampling technique, simple random sampling technique shall be used to select MFIs that will be covered by this research exercise, given the known list of MFIs that operate in the district. This technique gives all the MFIs that operate in the district, equal chances of being selected for the study.

### **1. 6. 4 Sampling units:**

Beneficiaries of MFIs under the study will be arrived at using stratified sampling technique which will be based on age, sex and enterprise groupings. This method allows the study population to be grouped into strata of homogeneity to ensure representative sample units for efficient and effective assessment of the contributions of the MFIs in enterprise development in the district. It will be ensured that respondents will constitute 50% of each beneficiary stratum per MFI to be studied using simple random sampling. Questionnaires and interviews will then be administered to the respondents to generate detailed information on beneficiary experiences and perceptions about the services and impacts of the MFIs enterprise development in the district (Twumasi, 2001).

### **1. 6. 5 Analysis of data:**

Qualitative and quantitative methods will be used for the analysis and interpretations of data.

Quantitative data obtained from the rural entrepreneurs and MFIs will be compiled and processed using the Statistical Package for Social Scientist (SPSS) computer software.

Cross-tabulations will be used for the analysis. These will also examine the output / growth in relation to certain characteristics of the firms (loan amounts granted, number of loan cycles and education of owners). Tables, percentages, frequencies and bar-charts will be used for the presentation of the results. Qualitative data will be analyzed by summarizing them into themes and drawing conclusions from them (Twumasi, 2001)..

### **1. 7 Scheme of Work:**

I propose a 10-Month research programme, working with three field assistants. The work will be based on the activities of micro finance programmes and rural enterprise development in Nadowli District of the Upper West Region, Ghana.

The research will be based on one-on-one interviews, focus groups, and personal observations. I anticipate approximately 30 interviewees from rural entrepreneurs, including 3-5 microfinance providers as “ case studies” who will be interviewed over time. Focus groups will complement the interviews.

Fieldwork will be conducted in English and where feasible, in the local language, to preserve people's ideas. Two field assistants that I will train in qualitative research methods will conduct some of the interviews.

### **1. 8 Significance of the Study:**

Majority of Ghana's population lives in rural areas with agriculture and small scale activities as their main economic activities. With the rural sector producing the bulk of the nation's output, their standard of living need to be improved. One way of doing this is a carefully planned and implemented rural finance programmes necessary to accelerate the pace of economic development.

Amongst the objectives of the establishment of MFIs for example Rural Banks in Ghana is to establish institutional credit to the rural dwellers in their respective areas of operation and thereby assist in increased productivity to create wealth for improved living standards. As a result of this, the provision of credit to the rural poor for the development of their enterprises has been high on the agenda of governments and multilateral aid institutions for sometime now, but success has eluded most of the Rural Financial Institutions in developing countries (Yaron, 1992). This has been blamed on high transaction cost involved in lending to small and micro-enterprises that are widely scattered, management cost, and lack of acceptable collateral amongst others. These invariably underpin the conditions under which most banks provide support to entrepreneurs. This therefore called for a study into the credit delivery support system of these MFIs, how the rural entrepreneurs utilize these supports and how it translates into improvement in the local economy in the study area.

The research therefore sought to provide an entry point for restructuring the credit schemes with the view of making them more efficient and effective for the growth and sustainable development of rural enterprises in the study area.

In view of the above, the findings of the research will be useful to the MFIs management teams since their financial viability and long-run sustainability depend on the patronage and level of commitment of their clientele, as well as the performance of their enterprises.

The findings of the research will also serve as inputs and lessons to the government and those agencies spearheading the campaign for support for rural enterprises. The significance of this study also lies in the fact that there are limited studies in MFIs activities in the development of rural enterprises and hence it will also add to the body of literature which serves as a reference material for students and researchers.

## **1.9 Organisations of Study Report**

The study report shall be presented in six main chapters. The first chapter which forms the introductory aspects of the study report shall comprise: background to the study, problem situation and statement, research questions and objectives, and significance of the study.

Chapter Two shall focus on review of relevant related literature and also look at the historical and conceptual frameworks of the study. Chapter Three shall address methodological and analytical frameworks of the study. Emphasis shall be on profile of the study area, sampling techniques, data collection and analytical methods. Chapter four shall be centered on presentation of

case descriptions from the study whilst Chapter Five shall be discussing the major findings of the study.

Chapter Six shall comprise Summary, Conclusions and Recommendations from the study.

## **2. 1 Literature Review**

### **Rural finance and rural enterprise development:**

This chapter examines the productive systems in rural economies, the MFIs and innovations in rural enterprise financing in the global perspective. In the context of Ghana, the review will be focused on the development of rural enterprises and the relationship between finance and rural enterprise development, and also examine the rural financial systems. Results and lessons learnt from various innovative MFIs in relation to financing and enterprise development will be reviewed, it will also provide an overview of what has happened in other parts of the world to help inform the analysis of the study.

### **The Nature, Characterization and Operations of Rural Financial Systems:**

Rural financial systems or markets are mechanisms within the domestic financial systems which ensure the availability, accessibility and utilization of rural finance. The nature and characteristic of each financial system is often based on the demand for and supply of rural finance. According to Pagura (2004), “ rural finance is usually demanded for;

Agriculture production – medium and long-term loans, leasing arrangements, lines of credit, crop insurance among others.

Agriculture based industry – investment and working capital loans, lines of credit

Non-farm enterprise and trade-investment loans, short-term working capital loans, and

Household consumer finance – emergency loans, health insurance, savings, remittances, housing”

As a result of these, there are a myriad of rural financial systems which tend to be fragmented (Germidis, 1990; Besley, 1994) and consist of informal, semi-formal and formal financial intermediaries (Pearce, 2004; Pagura, 2004). The role and activities of these sub-sectors are largely complementary and do overlap.

### **The Informal or Non-Institutional Rural Finance:**

Informal financial institutions tend to be non-bureaucratic and much more flexible in respect of loan purpose, interest rates, collateral requirements, maturity period and debt rescheduling (Ghate, 1992). However, Gordon (2000) observed that interest rates for rural finance are usually high and loans are taken out for short periods. Such lenders are usually based within the community – they know their clients; they know their clients’ businesses; and they can apply pressure from within the community to ensure that loans are repaid. For many rural people, borrowing from the informal sources is a last resort, but even though the cost of borrowing may be high, such lenders provide an important source of cash in rural communities where there are few, if any, alternatives. Where credit is not available, households may have



to deplete their asset base (spend savings, or sell jewels or livestock) or go without essential items, including food.

Despite these limitations, including inadequate financial resources and legal constraints (Nwanna, 1996), informal financial institutions continue to play a significant role in meeting the credit needs of rural inhabitants and rural entrepreneurs.

### **Semi-Formal Rural Finance:**

In Pagura's characterization, Village Banks, Cooperatives, Non Governmental Organizations (NGOs), Credit Unions (CUs), Input Suppliers, Agribusiness Companies and Marketing Companies are considered to be the semi formal intermediaries in the rural areas, in that they are formally registered, but are not licensed and regulated by the central bank of a country.

### **The Formal or Institutional Rural Finance:**

The formal financial intermediaries or institutions are those that are incorporated under Companies' Codes, which give them legal entities as limited liability companies, and subsequently licensed by their respective Central Banks under either the Banking Laws or the Financial Institutions (Non-Banking) Law as in the case of Ghana to provide financial services under lay down regulations.

Pagura (2004) indicated that the sources of funds in the formal part of rural finance markets are mainly: (a) co-operatives that meet the needs of short, medium and long-term credit; (b) commercial, cooperative and specialized banks; (c) micro-finance institutions (MFIs) and various government agencies including those established for agricultural development. The operations of <https://assignbuster.com/rural-development-in-ghana/>

financial institutions in formal rural financial markets are typically heavily regulated, and the nature and extent of formalities, as well as the interest rate structure, usually make access to credit from this market restricted to limited segments of the rural population.

### **Innovations in Rural Enterprise Financing in the Global Context:**

Various innovative banking systems have been developed all over the world to serve the rural population, particularly the poor, who are unable to access credit from the conventional banking institutions for investment into their enterprises and other household needs. These institutions often expand access to new segments of the rural population not traditionally served, create quality increases in terms and condition of current products already being offered and broaden the variety to offering new products and services. Amongst these innovative banking systems are the Grameen banking in Bangladesh and the Village banking in Latin America.

### **Grameen Banking:**

The Grameen Bank, started in 1976 is the brain child of Dr. Mohammed Yunus, and the first microfinance organization started in Bangladesh that provide small loans to the poor with no collateral.

The bank will give an amount to small groups and the individuals in the group utilize the money available in turns until all members benefit.

However, loan repayment is arranged to be paid weekly (Yunus, 2002). The bank's current operation covers over two million women globally and can be found in several countries worldwide.

## **Village Banking:**

Village banking, a concept developed in Latin America in the Bolivian Andes by John Hatch, Rupert Scofield and Achilles Lanao in 1980s, is now being implemented in 28 countries worldwide including El Salvador, Honduras, Mexico, Costa Rica and Haiti, in different forms. Village banking is a rural financial services model that enables poor communities to establish their own credit and savings associations, or, village banks. (Nelson, McKNelly, Stack & Yanovitch, 1996).

## **Rural Enterprise Development and Financing in Ghana:**

There are various types and sizes of rural enterprises. The nature and characteristics of these enterprises influence the extent to which they can access financial and other support services for their development. A brief on the link between finance and enterprise development is therefore necessary from which the rural financial systems in Ghana can be dovetailed.

## **Characterization of rural enterprises in Ghana**

A glance at some of the Medium Term Development Plans revealed most of the key rural economic activities in Ghana. A survey conducted by Boapeah and Poppe (1992) in the Dangme West District, Ghana also provided some of the enterprises that can be found in a typical rural environment of Ghana. These enterprises have been grouped into the following five major categories as used by Boapeah and Poppe:

Agro-based: Bakery, Cassava processing (gari), Palm oil extraction, Shea butter extraction, Dawadawa Processing, Cotton ginning, Pito brewing, Milling, Fish smoking, Distillation

Clothing: Dressmaking, Textile, Mat weaving

Wood-based: Carpentry, Charcoal burning, Boat building

Metal: Blacksmithing, Fitting

Others: Basketry, Block making, pottery

Most authors and researchers have observed that the size of an enterprise plays a significant role (amongst others) in whether or not the enterprise will obtain credit. Generally, the larger the enterprise, the greater the likelihood it has to overcome some of the structural deficiencies, and therefore the better its chances of obtaining credit. In the same vein, the smaller the enterprise the more unattractive it is most likely to be as most financial institutions will always want to recover their costs and make a reasonable profit, which always not obtainable from small lending. It is for the latter highly disadvantage group located mostly in the rural areas that the Microfinance concept was developed to make extension of credit to this group possible.

## **The Theoretical link between Finance and Enterprise Development**

The purpose of this section is to discuss the relation between finance and enterprise development.

The economic mechanism by which more investment leads to more growth and hence development can be described in terms of the Harrod-Domar growth model. The model relates the generation of total output to the stock of capital through what is described as the capital - output ratio: the amount

of output that the capital can be transformed into. This model was designed by two people; Roy Harrod (1939) and Evesey Domar (1946). These two economists worked independently but almost came to a similar conclusion. Their conclusion was that economic growth was dependent on investment which is described as the moving force behind the process of growth (Todaro, 2000).

The Harrod-Domar growth model argues that as a prime mover, investment has a dual role; the demand and capacity roles. They defined investment as a change in capital stock, and when this is taking place in an economy it creates an opportunity for increased demand; the investments create additional consumption and hence trigger off demand for real output. They also argued that net investment in an economy has the tendency to increase the economies productive capacity. Therefore for growth to be sustainable, investment must always increase to increase consumption to absorb the excess capacity that is created.

The role of finance is therefore a critical element for economic growth and invariably the development of enterprises. There is strong and growing evidence that many enterprises, particularly rural enterprises, have very high rates of return to capital that may persist overtime for some enterprises because of the highly fragmented nature of financial markets. McKenzie and Woodruff (2004) found that the rate of return is as high as 15% per month for micro enterprises in Mexico.

Enterprises are often found in both the rural and urban sectors of a country, hence it's important to examine the rural financial systems in Ghana and how they contribute to the development of rural enterprises.

## **Rural Financial Systems in Ghana**

The rural financial markets in Ghana is equally fragmented as in the case of other developing countries and consist of informal, semi-formal and formal financial intermediaries.

The informal financial institution covers a range of activities known as susu, including individual savings collectors, credit associations and savings and credit “ clubs” run by an operator. It also includes moneylenders, trade creditors, self-help groups, and personal loans from friends and relatives.

Whiles the semi-formal financial institutions includes the various NGOs and the Credit Unions (CUs) which are formally registered, but are not licensed and regulated by the Bank of Ghana. The Formal financial system in Ghana consist largely of a central bank, commercial banks, insurance companies, discount houses, finance houses, leasing companies' savings and loans associations, rural