

Ensuring financial inclusion for smallholder farmers

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Making Access Possible



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Partnering For A Common Purpose

In the framework of the [2015 Global Forum on Development](#), which focused on how “Financing sustainable development”, the [OECD Development Centre](#), the [United Nations Capital Development Fund \(UNCDF\)](#) and the [Better than Cash Alliance](#) have developed a series of articles exploring the key issues and dimensions of financial inclusion. Improving citizens’ access to financing is key to support more inclusive social and economic development. This note from Kameshnee Naidoo of UNCDF highlights the challenges of ensuring financial inclusion for smallholder farmers.



Ensuring financial inclusion for smallholder farmers

Joacquin is a subsistence farmer from Etatara in Mozambique. At 46 years, he is his family's sole breadwinner, responsible for supporting his wife and three orphaned grandchildren. He lives in a traditional house, which he is unable to use as collateral and grows maize, sorghum, cassava and beans. They consume a lot of the produce themselves, and what is not consumed is sold. Joacquin earns USD 300-500 per month depending on the season and his produce.

In the attempt to understand the real livelihoods of lower-income individuals and households in markets such as Mozambique, the lack of data and field-based insights are challenging. UNCDF's [Making Access to Financial Services Possible \(MAP\)](#) project, for instance, seeks to place demand-side analysis at the centre of the research process to focus the minds of multiple stakeholders on the end consumer. Better provision of appropriate financial services is an ancillary tool to wider development goals of enabling more sustainable livelihoods for low-income populations.

Millions of smallholder farmers like Joacquin live in or close to poverty and rely on agriculture for their livelihoods. Agriculture is fundamental to poverty reduction, driving economic transformation and ensuring growth is inclusive of the poor. Pathways out of poverty – whether through farming, employment, non-farm processing and trade or migration – are all heavily reliant on agriculture. As stressed in a [report to the G20](#) co-ordinated by OECD and FAO, improving agricultural productivity – while conserving and enhancing natural resources – is an essential requirement for farmers to increase global food supplies on a sustainable basis and enhance their livelihoods. Over the longer term, increasing agricultural productivity plays an even greater role in economic development by enabling economic transformation through a new green revolution.

For agriculture to work better and improve the livelihoods of the rural poor, however, financial services need to work better in helping the poor to diversify their source of livelihoods and reduce hunger, become more resilient to periodic shocks and prevent them from falling into poverty traps. The rural economy requires a wide range of financial services and products, and no single type of financial institution is capable of efficiently providing such a range. Microfinance, for example, can help to meet the short-term needs of farmers and other low income residents and help to finance microbusinesses but it is not so suitable for larger businesses or for the accumulation of capital and innovations to raise productivity.

The OECD's [Multi-dimensional Review of Myanmar](#) found that of all the segments of the country's economy, the rural sector is the most underserved by the formal financial system. Only about [2.5% of total loans go to the rural sector](#), even though it accounts for 30% of GDP and two-thirds of employment. The rural population has considerably less access to formal financial services than the population in urban areas and some segments, such as landless farmers, are effectively cut off from such services.

The current rural financial system is unlikely to be able to support the broader development of the rural economy in Myanmar, particularly the improvements in productivity and the creation of non-farm job opportunities that will be necessary to allow the rural population to share in rising living standards and to avoid a disruptive exodus from rural to urban areas.

Apart from the basic loan products, other financial products and services have been quite limited. For instance, remittance services are particularly important to Myanmar's rural sector, given that an estimated 2-5 million of its citizens are working in other (mainly ASEAN) countries and annually send a substantial amount of funds back to their families.

Finance is also needed for the agricultural investment that is a major catalyst for job creation, higher incomes and increased productivity across the economy as a whole. Financing agriculture and rural development more broadly, however, is complex. All of the challenges that hinder financial outreach in regular markets are larger in a rural context. Rural populations are poor, sparsely distributed, poorly literate and mostly engaged in informal activities. Data from the FinScope surveys and the MAP diagnostics indicate that agricultural activity – mostly smallholder farming – has low returns and is subject to high and covariant exogenous risks. Information failures like moral hazard, adverse selection, poor enforcement and danger of exploitation all exist on a large scale. For suppliers of financial services, the cost of operating in rural areas is often extremely high which, when combined with the low and risky returns available, leads to a large under-supply of financial services.

If financial services are to work better for rural and agricultural populations, they need to be based on an understanding of the needs of the users, which can be very different to those of urban populations. But financial service providers, governments and donors do not have a good understanding of the financial behaviour, usage and needs of rural populations and this restricts the effectiveness of rural outreach. There are also significant weaknesses in financial literacy, and an understanding of how to build financial capability of rural households and enterprises. Even though technology has helped push out the access frontier, usage remains low and there is a big problem with dormancy.

On the supply side, an increasing number of traditional and non-traditional financial service providers are innovating in the agricultural space, driven by a combination of declining profitability in more advanced markets and the huge potential offered by the unbanked millions in rural areas. Innovation is taking place: in delivery models led by technology and building alliances between those who have assets and those who have low cost outreach; in risk management enabled by big data and leveraging existing relationships within the value chain (buyers and sellers, farmers associations, co-ops); in products driven by a better understanding of what farmers need, matching tenor and interest and repayment schedules to agricultural cash flows and addressing agricultural development with finance.

If the goal is to alter the dynamics of markets so that they work more effectively for the poor and economic transformation, we need to recognise the interaction of these market systems. In this regard, understanding how agriculture shapes the demand for financial services and how the rural context in which it takes place affects the costs, risks and returns to supplying financial services is key. A key component of the MAP diagnostic is to build a target market profile based on the main income generating activities of consumers, and their financial services access, usage and needs. The analysis is informed by the context of the country and ultimately seeks to meet the policy objectives of financial inclusion as a tool to improve welfare and poverty alleviation. As a large number of the countries in which the MAP diagnostics have been undertaken are LDC's reliant on agriculture, it is able to present a more complete picture of the nature of demand and usage of financial services and potentially inform better ways of serving farmers needs.

Box 1: The Post-2015 development agenda: Sustainable Development Goals

The United Nations is in the process of defining a post-2015 development agenda. This agenda will be launched during a summit in September 2015, which is the target date for realising the Millennium Development Goals (MDGs). The SDGs are intended to build upon the MDGs and converge with the post-2015 development agenda. They were selected through a consultative process by an open working group with representative from 70 countries.

Several MDG targets have been met including poverty reduction, access to improved drinking water, gender parity in primary education and political participation of women. Some are on track to being met such as fighting malaria and tuberculosis. However, despite these achievements, large disparities remain between and within countries. This has prompted a shift in emphasis towards sustainable and equitable growth. The proposed SDGs focus on reducing poverty and inequality; improving global health; ensuring inclusive and equitable education; achieving gender equality and empowering women; ensuring access to sustainable water, sanitation and energy; promoting inclusive growth; and protecting the environment.

Source: UN Sustainable Development Knowledge Platform: <https://sustainabledevelopment.un.org/>