BMAU BRIEFING PAPER (15/13)

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Are SACCOs under the Rural Financial Services Programme sustainable?

Overview

Increasing the incomes of the rural and urban population is a key priority for the Government of Uganda (GoU) as stated in the National Development Plan. The Government aims to raise the income of poor households through interventions that seek to promote participation of the poor into the monetary economy. Provision of affordable credit is one of the important avenues through which Government is enhancing the poor's savings and living standards.

Government has spent USD 10.8 million since 2008 to support SACCO activities. In addition USD 18.5million has been spent on these activities as loans from IFAD.

In 2012, the Budget Monitoring and Accountability Unit (BMAU) conducted an evaluation of SACCOs under the rural financial services programme. This brief reviews the extent to which these SACCOs are sustainable.

Key Issues

- TAll SACCOs had some management weaknesses due to limited application of regulatory and policy practices.
- All SACCOs suffered inadequate funding
- Newly formed SACCOs had a very poor asset base and profitability level

Introduction

The Rural Financial Services Strategy (RFSS) was developed in 2005 to guide the creation and building of a nationwide network of rural financial infrastructure of SACCOs to deliver microfinance services to the population, especially, those living in the rural areas. The Rural Financial Services Programme (RFSP) was launched in 2003 following Cabinet approval of the plan for the implementation of the Rural Financial Services. The initial programme design focused on strengthening all types of Micro Finance Institutions (MFIs), including SACCOs.

In 2006, the Government reviewed its microfinance policy and decided that RFSP should be focused on SACCOs, in line with the RFSS.

The purpose of the RFSP is *"to increase access to financial services in rural areas by increasing the outreach and sustainability of selected SACCOs and the utilization of their services by poor rural households*[1]*"*. In line with the RFSS, the primary focus of the RFSP is

1 IFAD, 2007

to facilitate the establishment, strengthening and outreach of SACCOs.

The BMAU study assessed the performance of the Rural Financial Services Programme since 2003 but with special focus on the SACCO programme that had been under implementation since 2008. The study covered all districts and sub-counties where the GoU supported SACCOs existed in 2008.

Sustainability of SACCOs was assessed in terms of institutional procedures/practices, sources and adequacy of funding, trends in net income and savings, and loan portfolios at risk.

The SACCOs were classified into 4 categories namely:

i. Formation[2] SACCOs (FORM)
ii. Start-up[3] SACCOs (STUP)
iii. Strong/Outreach/Advanced[4] SACCOs—(OUTR)
iv. Flexible[5] SACCOs (FLEX)

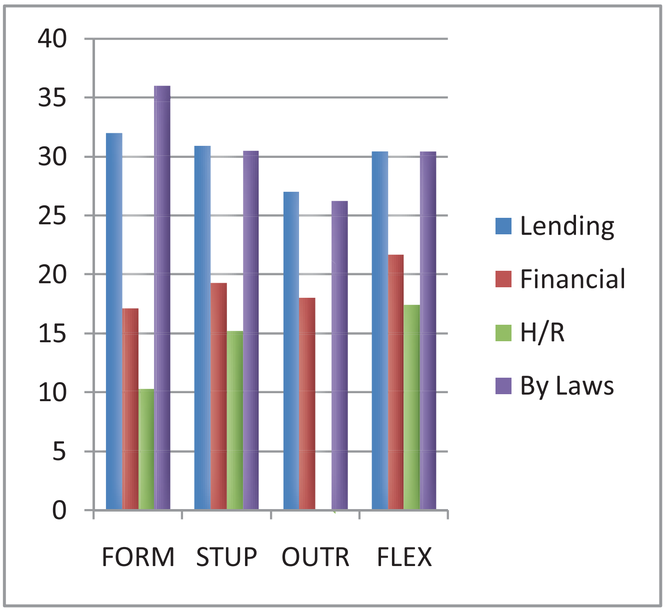
Key Findings

1. Ownership of Business Development Plans, Regulatory and Policy documents

Eighty seven percent of the SACCOs had a Business Development plan which is a good practice that ensures focused implementation of activities. However, ownership of Regulatory and Policy documents is still on the low side. Only 30 percent of the SACCOs had By Laws, Constitutions and Lending/Credit policies.

Further still, less than 20 percent had Financial and Human Resource policies. Absence of these policies negatively impacts on operational practices among most SACCOs and raises questions on sustainability.

Figure 1: Ownership of Policy documents by category of SACCO



Source: *Field findings*

2. Management practices

The study examined some management practices as a pointer to possible sustainability of SACCOs. The practices included: role of management boards and staff, quality of staffing, banking operations, accounting systems, type of collateral accepted as well as loan recovery methodology.

Eighty two percent of the Managers were shareholders within the SACCOs across all categories. There was perceived commitment of managers and objectivity in making management decisions since they had a stake in the SACCOs.

Most of the SACCOs have the day to day operations managed by managers However, in a few cases cashiers, and Loans officers were found managing the daily operations of the SACCOs.

[2] New SACCOs under the RFSP that the Uganda Cooperative Savings and Credit Union limited (UCSCU) assisted to form
[3] SACCOs that had limited operational self sufficiency, but with potential for growth
[4] These were existing strong community based SACCOs with business plans that set forth credible plans for mobilizing additional rural members in previously un-served communities.
[5] These are SACCOs which are selectively supported according to their need

Ninety one percent of the SACCO staff were contract paid employees, while about 9% were volunteers.

Eighty six percent of SACCOs were using manual accounting systems. Among the Formation and Start up SACCOs, it was above 90%. Manual accounting systems have problems of tracking and reconciliation among others which is critical for SACCO operations.

In terms of safety of financial operations, at least 4 percent of the SACCOs had no bank accounts.

These were all either Formation (18%) or Start up (2%) SACCOs. On the other hand among those that had bank accounts, 42 percent did not carry out monthly bank reconciliations.

Majority were Formation (57%) followed by Start-up (44%) and Strong (26%) and Flexible (21%) SACCOs respectively.

Thirty five percent and 26 percent of the SACCOs prepared monthly and annual financial statements respectively.

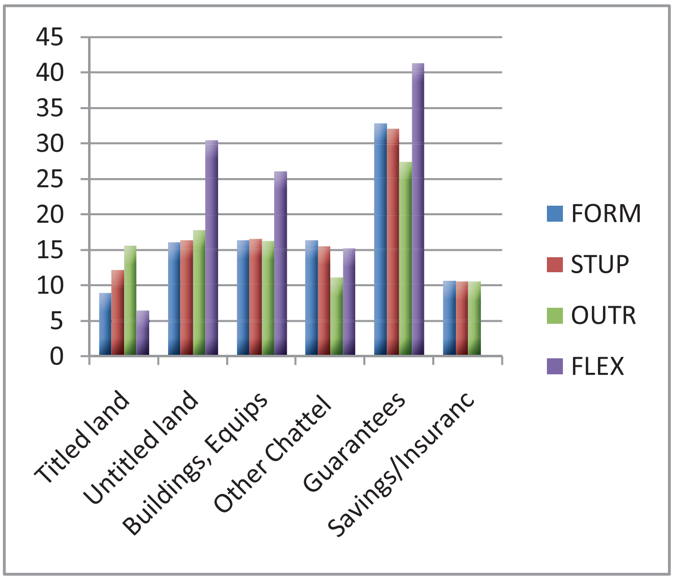
The problem was rampant among Formation, Start –up and Flexible SACCOs where 32%, 42% and 48% respectively prepared monthly financial reports. This implies poor financial reporting practices among most of the SACCOs.

Type of collateral accepted has implications for recovery of funds from bad loans. Where collateral can easily be converted into cash, then a SACCO reduces on risky loans.

It was noted that risky collateral (untitled land, guarantees and no collateral at all) amounted to 43 percent (Figure 2).

Loan default was a major challenge across SACCOs, due to failure to use tougher loan recovery methods such as Courts of law. Only 21% used Courts of law and attachment of collateral (20%) as methods for loan recovery. These practices were poor across all SACCOs.

Figure 2: Type of collateral accepted by SACCOs



Source: Field findings

3. Sources and adequacy of funding

Close to 69 percent of SACCOs had savings and share capital as the major source of funding followed by loans from the Micro Finance Support Centre Limited. Generally, all SACCOs are increasingly being funded through loans.

Use of own saving and share capital would be sign of SACCO sustainability but the funding is grossly inadequate. About 91 percent of SACCOs reported inadequate funding as a key challenge. This was an issue across all categories of SACCOs.

4. Asset base and SACCO profitability

The asset base and profitability of a SACCO are indicators of future sustainability. A SACCO with a solid asset base and or consistent profitable operations has good chances of continued existence. Four measures were assessed namely:

a) Operational Self Sustainability showing the extent to which SACCO incomes could cover operational costs. The net income should be positive.

b) Financial Self Sustainability showing the SACCO's ability to cover cost of funds and other forms of subsidies when valued at market price. The assets should be more than the liabilities.

c) Return on Assets showing the extent of profitability per unit of asset.

d) Portfolio at Risk showing the total loan portfolio that is due for payment but has not been paid. The ratio compares the actual amount in arrears to the total portfolio. The higher the ratio the bigger the risk. It was established that:

- Formation SACCOs were doing poorly on all fronts and are therefore not sustainable without additional external support.
- Start-up SACCOs were on track and had high chances of sustainable operations.
- The Strong SACCOs had a mixed picture but were still profitable and their sustainability was guaranteed.
- Flexible SACCOs had a fluctuating performance, but they were generally sustainable.

Conclusions

All SACCOs had some management weaknesses, especially the Formation and Start-up categories. This was due to the limited application of regulatory and policy practices. However, most SACCOs had Business Development plans indicating some focused mode of operation.

Most SACCOs had savings and share capital as the major source of funding although this was grossly inadequate. To that effect many were increasingly soliciting loans.

In terms of asset base and profitability, SACCOs except the Formation category, are performing fairly well and are sustainable.

Recommendations

- Government should continue supporting the programme especially the Formation SACCOs. The other SACCOs may need backstopping support through intensified supervision and monitoring. To this effect the department of Microfinance, in the Ministry of Finance, Planning and Economic Development should play a more active role with the technical supervision of the Uganda Cooperative Savings and Credit Union Limited.
- The programme should stop the formation of new SACCOs for support but strengthen existing ones for sustainability.
- The Government should invest more in effective sensitization about SACCOs, particularly to sensitize the public on how to save, benefits of saving, activities of SACCOs and their ownership. This would foster more savings and share capital to finance SACCO operations as opposed to loans.

Reference:

Ministry of Finance (2012): *Evaluation Study of the Rural Financial Services Programme and the Uganda Cooperative Savings and Credit Union – Formation and Strengthening of SACCOs*

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