GOVERNANCE AND REGULATORY ISSUES: MICROFINANCE AND DEVELOPMENT OF RURAL COMMUNITIES IN NEPAL

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Abstract

Microfinance Institutions (MFIs) that have a mission to provide credit to the poorest of the poor appear to be the panacea for rural poverty and hardship and bring forward a promise of better tomorrows. However, MFIs as a means of expanding financial inclusion and competing with the informal financial sector are not such a success story in rural Nepal. The increasing demand for cash to meet social and religious obligations in largely subsistent village economies is increasingly supported by short-term seasonal migration. The removal of working-age males from communities produces a range of unanticipated and not necessarily desirable outcomes. MFIs, it is suggested, could ameliorate the problem and positively contribute to improved sustainable development outcomes.

Keywords: MFI, Seasonal Labour Migration, Nepal, Cash Need, Policy Implication

1. INTRODUCTION

In this article the financial and social benefits of expanded Microfinance Institution (MFI) outreach[9] in rural Nepal are examined. Central government policy makers and research funders emphasize the necessity to develop MFIs to uplift the social and economic situation of the poor in developing nations. Potentially, significant gains in outreach are realistically achievable in the context of remote village settings where there is currently little access to cash. The cash requirements among the rural poor are increasing as more and more activities, such as the purchase of chattels and livestock plus other transactions such as religious festivals and weddings, now require money.

The barter economy has operated well but is gradually waning in importance as urban habits gain more traction in remote communities. MFI services, in particular credit and savings extension, can be achieved by removing the access barriers in rural areas (McIntosh et al., 2011& (Bos & Millone, 2015). Acceptance of small amounts as deposits may encourage a saving practice and contribute to building confidence in saving for the future among poorer communities. Access to finance can contribute to a long-lasting increase in income by raising investment in income-generating activities (Agbaeze, 2014) and to a possible diversification of income sources. An accumulation of assets may be achieved and importantly a smoothing consumption, which may reduce vulnerability to illness. Drought and crop failures are ongoing issues in rural communities but slow and steady improvements in education, health and housing through the deliberate choices of borrowers who are in improving economic spaces will make for better lives. In addition, access to finance can contribute to an improvement of the social and economic situation of women who have very, very limited opportunities at present. Finally, microfinance may have positive spillover effects in addition to the direct economic and social improvements obtained by the borrower (Zhou and Takeuchi, 2010). The positive contribution microfinance can make to reducing poverty has convinced many governments, non-government organizations (NGOs) and individuals to put effort into supporting MFIs and their activities.

MFIs have also received criticism, including their failure to reach the ultra-poor (Scully, 2004 & (Lønborg & Rasmussen, 2014), and not adequately providing benefits through financial services and programs (Aghion and Bolton, 1997). The tension between financial performance and outreach is manifest in the lack of confidence from the MFI sector and seeing the risk that the ultra-poor present as borrowers. Hulme and Mosley (1996) suggested that the poorest of the poor, the so-called core poor, are generally too risk averse to borrow for investment purposes. Therefore, they benefit only to a very limited extent from microfinance schemes (Newman et al., 2014, & (Lønborg & Rasmussen, 2014). Staff of microfinance institutions may prefer low-risk exposure, if bad debts are unfavorable in terms of bonuses or advancement, then seeing ultra-poor as extremely credit risky promotes a desire to avoid them (Hulme and Mosley, 1996). MFI practices may also lead to the exclusion of the core poor, such as a requirement to save before a loan can be granted (Kirkpatrick and Maimbo, 2002; Mosley, 2001; (Lønborg & Rasmussen, 2014).

In an economy where rural workers receive payment in kind, there is little money in circulation. The opportunity to acquire additional poultry or grow a roof garden to supplement in-kind receipts with cash sales requires an initial investment. If

[9] Outreach relates to the number of customer served by an MFI and the benefit the borrower achieves from the credit (Lafourcade et al., 2005).

there are no MFIs operating in the area, then the moneylender, a traditional source of money, who some now consider high-country loan sharks, is one option. Migration has long been an important livelihood strategy for the people of rural Nepal. Whenever the population has risen to such an extent that people can no longer secure a livelihood, they have migrated elsewhere. Even today, poor people pursue short-term seasonal[10] migration as a livelihood strategy in Nepal. The migratory worker culture is becoming a staple pattern for survival rather than a process of generating surplus cash to invest in money-producing agriculture or trade. Often this form of work is necessary even where moneylenders operate. This is now a common situation for rural people, particularly those in more remote villages

The poorest rural people in Nepal own no land, have no regular income sources, collateral or financial literacy. The tyranny of remoteness is an obstacle too large to address through an immediate policy change. Small incremental steps are more likely to be successful. Development of investment lending in rural communities will stimulate a trickle-down effect through paid day-labor having cash in hand.. Aghion and Bolton (1997) find that the trickle-down mechanism can lead to a unique steady-state redistribution, improving the production efficiency of the economy. Applying this trickle-down mechanism in Nepal may enhance economic growth and in turn further contribute to the expansion of lending and saving activities. In Nepal, those who have more wealth and are more capable of a managing resources will be creating jobs through investment and therefore producing more business or businesses. This would encourage people to work more to earn more. This process leads to local economic growth and wealth creation that benefits everyone, not just those who invest.

2. NEPAL BACKGROUND

Nepal is one of the world's least developed countries located in the north of South Asia. According to the World Bank (2014) the annual per capita income of USD750 ranks at 157th of 187 countries in world in the Human Development Index. More than 80% of the total population lives in rural areas and their livelihood depends on agriculture and related activities (World Bank, 2014).

A landlocked republic surrounded to the north by China and to the south, east, and west by India, Nepal has potential to grow its economy capitalizing on its location, sandwiched between the two emerging giants of India and China. Geographically, it is divided in three zones: a) high mountains and the Himalayas in north, b) small mountains and hills in middle, and c) the plain (Terai) in the south.

Nepal and India share a 1,778 km border that is very porous, making it difficult to capture accurately data on cross-border movement and undocumented migration. There is an 'open' border as per the agreements of a bilateral treaty signed in 1950. According to the Treaty, Nepalese and Indians can travel and work across the border and are treated on a par with local citizens. Rural Nepalese, who have long been suffering poverty, unemployment and more recently a civil war, migrate to India in their thousands every year.

The Central Bureau of Statistics (2011a) estimated that nearly 30% of the population of 28 million live on less than USD14 per person per month. Some of the causes for the poverty are disparities of caste, gender, and geography. Stimulation of migration, according to Bhattarai (2007) is a main source of income to ameliorate poverty, unemployment, declining natural resources, and more recently the Maoist insurgency.

Bhattarai (2006) argues that there are reasons to migrate from Nepal such as limited employment opportunities, deteriorating agricultural productivity and armed conflict. Further, he observes that many villagers go abroad to work for a while, returning with some money and the experience of living in a different geographical location. However, what is clear is that most would be worse off if they were depending solely on local employment (Walsh and Jha, 2012).

3. PROFILE OF A VILLAGE

Dekaha is a village where people engage in short-term seasonal labour migration. Dekaha is a village in the Village Development Committee (VDC) of Ekarahiya located in the Mahottari district in the Janakpur Dham zone, southeastern Nepal. It is 25km from the district headquarters, Mahottari and 7km from Janakpur. The VDC Ekarahiya consists 1441 households of approximately 12,000 people with Dhekaha consisting of 400-500 households with a total population of 3,000 (Central Bureau of Statistics, 2014).

The village has access to a primary school and post office but does not have infrastructure such as transport and communication, nor are there services such as health and other basic facilities. The village economy mainly depends on agriculture laboring and animal rearing. Most inhabitants do not own land and are dependent on day labor for subsistence. The landowners and farmers of a neighboring village normally hire workers for agricultural or domestic work each morning on a daily basis.

Agriculture in the area depends on rainfall for cultivation. Some landowners in the neighboring village have pumps to access underground water for irrigation and this is just enough to make it worthwhile for Dekaha's day laborers. Dekaha, however, faces frequent drought and irrigation sources are very limited. The entire village would otherwise be completely dependent on rainfall without some small ponds. These supply water for bathing, cleaning clothes and livestock drinking water. There are also a few wells and bores in this area. An international non-government organization (INGO) donated hand pumps for the village to obtain drinking water. Farmers grow traditional crops such as rice, wheat, maize, paddy and jowar. The agricultural wage per day is NRs. 100 (USD0.98)[11] for males and NRs.70 (USD0.68) for female labor.

In Dekaha, the main credit supplying sources are commercial banks, MFIs and cooperative banks, which all require collateral for loans. These

[10]Seasonal migration comprises a period of a few weeks or months and implies a regular return of migrants to the original place (Shrestha 2009; Department for International Development, 2007)

[11] NRB foreign exchange rate at the date of 03 Aug 2015, USD1= NRs102.3

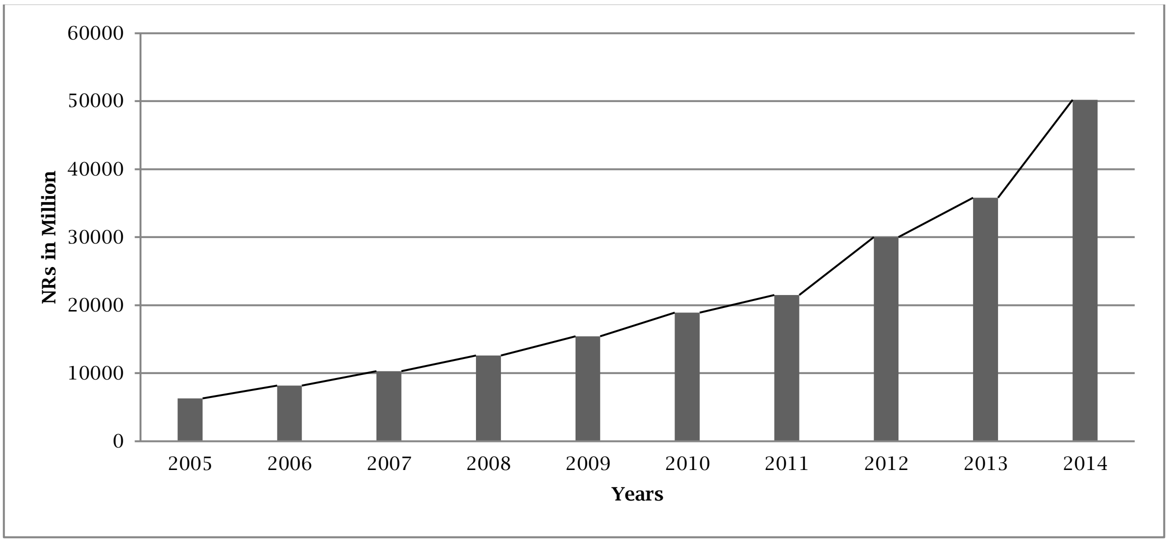
institutions do not have branches in this village. People have to travel at least 7 km to Janakpur or 25 km to Jaleswor for credit purposes. However, recently, the Grameen Bank opened a center 3km away from the village to ease access to the credit process. There are also informal sources of credit, including moneylenders, traders, relatives and friends. One of the peculiar features of the village is that work is only available for a few months in the agricultural fields – it is seasonal work and after the monsoon, in order to generate cash, men in particular migrate from the village to various destinations in India.

4. EVOLUTION OF INSTITUTIONAL MICRO CREDIT ACTIVITIES

The formal banking system started in 1937 by establishing the Nepal Bank Limited with credit and deposit financial services to the commercial sector in Kathmandu and some urban areas in Nepal. In 1956, the Nepal Rastra Bank (NRB) was established as the central bank of Nepal to monitor and administer the banking system to control the money with a view to improving the lives of people.

The Nepal Rastra - Central Bank established the Agricultural Development Bank (ADB) in 1968 to support farmers by providing credits and marketing support for agriculture and its products. It was the beginning of the rural financial services the first microfinance in Nepal. In the process of developing the standard of living for the deprived sector and rural regions, the NRB directed that all commercial banks should invest a portion of their resources for these needy groups. Furthermore, NRB mandated for all the commercial banks to invest 5% of their sources in rural development projects with 80% to be in agriculture. There is a steady upward trend in MFIs lending as reflected in Figure 1.

Figure 1. Asset/ Liabilities of Microfinance Development Bank (MFDB) and Rural Development Bank (RDB) for 2005-2014



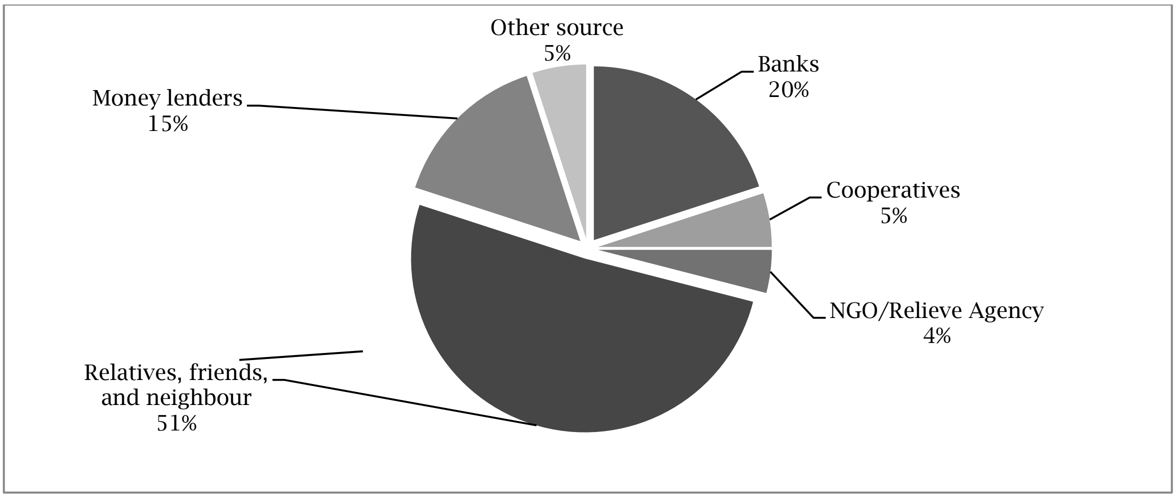
Data source: (Nepal Rastra Bank, 2014a)

Regional disparity is a consideration for the NRB, which encourages the private sector to participate by providing financial services in the rural areas of Nepal. In the process of facilitating the financial service to the rural region, the NRB opens its doors to participating with the private sector, to continuous development and to modifying its Acts to regulate banking and financial services (Shrestha, 2009). The NRB should be playing a positive role in forming and executing the policies for the financial sector to enrich rural people through access to financial services as a minimum. The financial sector is still in its infancy and needs more nourishing in order for it to provide services to all corners of the country. Financial services are still limited and focused more on urban rather than rural areas. The rural poor, in the interior regions, consequently have no financial services and depend traditional methods of dealing with their financial needs.

The formal sector's loan fund supplies, as shown in Figure 2, is 29% of total funds and is constituted by 20% from banks, 5% from cooperatives, and 4% from NGO/relief agencies. The informal financial sector in rural Nepal is widespread, supplying 71% of funds with relatives, friends and neighbors being the largest component with 51%, moneylender provide 15%, and a further 5% comes from other sources. The informal financial services come from property owners, merchants, farmer-lenders, goldsmiths, pawnbrokers, friends and relatives or informal group institutions such as dhikuti, dharambhakari, and guthi (United Nations Capital Development Fund, 2011).

The easy approach to personal credit, a short-term loan with quick access, and flexibility with or without collateral, is a popular informal financial service in rural Nepal. In most cases, the informal sector provides loans on the same day or within a week as a maximum. Most importantly, from the borrowers' perspective, lenders are flexible with the repayments. Borrowers in rural view them more favorably than MFIs. The forms of collateral preferred by lenders include gold or silver ornaments, bonding land or property, in some cases livestock, and even in the form of labor services.

Figure 2. Fund suppliers



Data source: (Central Bureau of Statistics, 2011b)

The interest rates charged by the informal fund providers range from 25% to 60% and in some cases 100% compounded annually. Informal fund providers receive the labor services and small gifts, in addition to the repayments, given by the borrowers as a way of keeping warm relations with the fund providers.

The availability of widespread informal financial services in rural areas suggests outreach would occur if MFIs were present and offering suitable terms. Efforts to date by the NRB to encourage formal financial institutions to establish themselves in rural areas have met with limited success.

5. MFIS OPERATIONS IN RURAL NEPAL

Banking services allow people to develop savings, which in turn will help them to improve their livelihoods and meet unexpected expenses. Importantly, savings will increase the likelihood of obtaining a loan for investment purposes. Local investment activities will help local economies grow and stimulate job opportunities. This will be an improvement upon the current situation where many cannot access financial services provided by the larger financial institutions, which effectively increases the income inequality gap. The poor remain trapped with debts for medical expenses, social obligation and sometimes consumption from which there is no escape and no way forward to earn money.

Statistics reported by the NRB 2013/14 reveal that approximately 40% of the Nepalese population now have a bank account, which is far greater than the 26% in 2006. However, it is unknown whether there have been multiple accounts opened by the same person, which might cause distortions in the per person calculation. Opening a bank account requires holding identification documents, which many rural people do not have, and distance to a bank, time involved, and the opportunity cost of lost laboring pay all suggest there are significant costs to accessing a bank (Demirguc-Kunt and Klapper, 2012).

The Central Bureau of Statistics (2011b) shows there are 40% and 44% of households that have access to financial services in less than or equal to half an hour and more than an hour's distance respectively. Rural households' access to financial services comes to 27%, compared to 89% of urban households. Furthermore, the percentage of households able to access banking services within an hour is highest in the plain (Terai) region at 75%, while the hilly region is 45% and the mountainous region is 17%. Even though the plains have the highest number of households with access to banking services, the interior parts of the plains region do not have ready access to banking services. In 2014, India made it compulsory for all people to have a bank account in order to be eligible to get loans and government benefit payments (Lakshami, 2014).

The Central Bureau of Statistics (2011b) indicates that during the last two decades there has been little change in the number of people taking out loans. The number of households receiving loans increased but proportionally the non-included households remained constant. Any progress is not good enough to tackle rural people's financial needs.

Table 1. Statistics of household loans, 1995/96 - 2010/11

Description	*Nepal Living Standards Survey*		
	1995/96	2003/04	2010/11
Number households receiving loans	1,924	2,538	3,715
Percent of households receiving loans	61.3	68.8	65
Average number of loans received	1.6	1.6	1.6
Number households having outstanding loans	1,830	2,468	3,566
Percent of households having outstanding loans	58.4	66.7	62.6
Average number of outstanding loans	1.5	1.6	1.5

Data source: (Central Bureau of Statistics, 2011b)

Central Bureau of Statistics' (2011b) data in Table 1 show the percentage of households receiving loans decreased in 2011 to 65 from 68.8 in 2004. However, the average number of loans remains constant at 1.6. The percentage of outstanding loans declined from 66.7 in 2004 to 62.6 in 2011, while average outstanding loans in 2011 are the same as in 1996. The financial institutions have not promoted a scheme to reach poor households or increased their outreach and service to those people who are still unattended.

The majority of the rural households have a low chance of getting financial institution support because: (i) they lack of physical collateral; (ii) the lengthy process of banking services discourages financially illiterate folk; and (iii) financial institutions are more focused on urban than rural areas in credit allocation.

Cumbersome processes for completing loan application documentation is a step too far for many financially illiterate poor. The supporting documents, recommendations, and guarantors heighten this disparity of access between services rural and urban. This significantly increases the likelihood that rural poor will only have the informal sector of relatives/friends/neighbors or moneylenders for credit purposes.

Table 2 presents demographic and MFI information for the Janakpur region. Four of the six districts show an improvement in the number of people per branch, i.e. a lower number, while one is unchanged and one has a very significant decline. When a branch closed in Ramechhap there was a big increase in people per branch. When the transport difficulties are included, the low level of service provided in rural areas is compounded. There is no internet or mobile banking in these areas.

Table 2.MFIs in Janakpur

Zone	*Districts*	*MFIs Branches*		*Population*	*Population per branch*	
Janakpur Dham		2013	2014		2013	2014
	Sarlahi	21	21	769729	36654	36654
	Dhanusha	19	23	754777	39725	32816
	Mahottari	15	20	627580	41839	31379
	Dolakha	4	5	186557	46639	37311
	Ramechhap	3	2	202646	67549	101323
	Sindhuli	7	11	296192	42313	26927

Data source: (Nepal Rastra Bank (NRB), 2014a)

A consequence of obtaining a loan from an MFI or the informal sector is the struggle to generate cash to service such loans, which may lead to short-term migration. Success stories are few, but occasionally working overseas does pay off. Pragas[12] and his three brothers spent their childhood as domestic help at Dekaha neighboring villages. Their teen years were bonded labor and rickshaw pulling. They tried hard to pay back the debt their parents assumed on different occasions from moneylenders, normally from the same landlord where Pragas and his siblings were working as domestic help and later as bonded labor. Their parents took credit for consumption, medication for elders and themselves, and a daughter's marriage and were barely able to provide food for the family.

Pragas got married, after his sister, and was unable to manage on his earnings consumption expenses and servicing the debt burden. They started a group for workers to short-term migrate to India. Their earnings from migrating work were enough for consumption but not debt repayment. Migration to foreign lands, such as Qatar and Malaysia, became popular among group members. Pragas decided to go to Qatar after meeting with an agent from a labor consultancy in Kathmandu. He took a loan of NRs 100,000 from a neighboring village's moneylender. He worked for three years at Qatar and then returned home. He manages to repays the credit but does not save money for investment.

He borrowed again to return to Qatar and this time took his two other brothers. In Qatar, he knew where to go and what to do and did not need other people's assistance. He returned to Nepal after three years with his brothers. This time they paid back the credit and bought a small piece of land where he built his own bamboo house. He spent all his earnings on building house and the buying land. He did not have savings but he was reluctant to go abroad again.

He started investigating local credit options, visiting banks that operated in the nearest towns; Janakpur and Jaleswor, the district headquarters. His time in Qatar had given him greater confidence, especially relating to financial matters. He was unable to get any help from banks, so he borrowed from a moneylender and started a business; a tea stall at his village. This time he is confident he will be able to pay back the moneylender from his local earnings. His wife and mother help him to run the tea stall and he makes regular debt repayment instalments to extinguish his debt. He is able to send his kids to school. MFIs can assist people like Pragas, making their life easier by providing credit facilities at the local level instead of through urban-based financial institutions. Credit facilities in rural communities save time and ease the access to credit for simple people. They can motivate rural people to get involved in financial activities to accumulate cash for their family's wellbeing.

Labor migration and remittances have their own role to play in household economic development. However, migration also has a role to play in human capital accumulation. The longer-term migrant worker, using their caste based vocation with which they grew up, may receive an injection of new competencies through working in a foreign land. Sunam (2014), in a Nepalese village case, discusses how one man developed his tailoring skills and established a tailoring business after returning home with their savings from Qatar.

Those who do not have skills can accumulate benefits by acquiring new skills working overseas

[12]Personal friend of researcher

and the exposure they gain puts them to the fore of the crowd to do things differently. These people are asset to their country from what they accumulate during their stay abroad. The foreign sojourn promotes entrepreneurship, and transferrable knowledge and skill (Dahal, 2014; Aghion and Bolton, 1997). The new working culture, habits, behavior, norms and ideas (Levitt and Lamba-Nieves, 2010) may help them to be able to start their own small businesses with the little savings accrued. Their engagement in economic activities contributes to the country's economic development. As the local economy improves, new opportunities for self-employment arise and there are job opportunities for others. The success of these new businesses will provoke others to do the same. MFIs' initiations are also potentially capable of promoting significant economic success for the poor. MFIs are essential in a situation where there is minimal employment creation (Nepal Remittance Association (NRA), 2014) while government and private sectors sleep (Karobar, 2015). The MFIs' role is vital to help poor escape the poverty trap and have a better life.

Short-term migration has arisen as the way of self-help. The wages earned through migration are a vital source of cash but it a cycle of poverty with little likelihood of escape. Money earned through short-term migration, in most cases, dissipates through repayment, partially or fully, to moneylenders, friends or others who supplied loans. When the purpose of the credit is for consumption, weddings, medical expenses, or travel expenses to find work it becomes a vicious circle. There are no surplus funds available for investment in productive use. MFIs may be able break the poverty cycle. A lack of education and financial literacy contributes to the repetitious cycle. Without mentoring and financial planning assistance, there are limited prospects for creating wealth from the meagre funds available.

6. CASH GENERATION

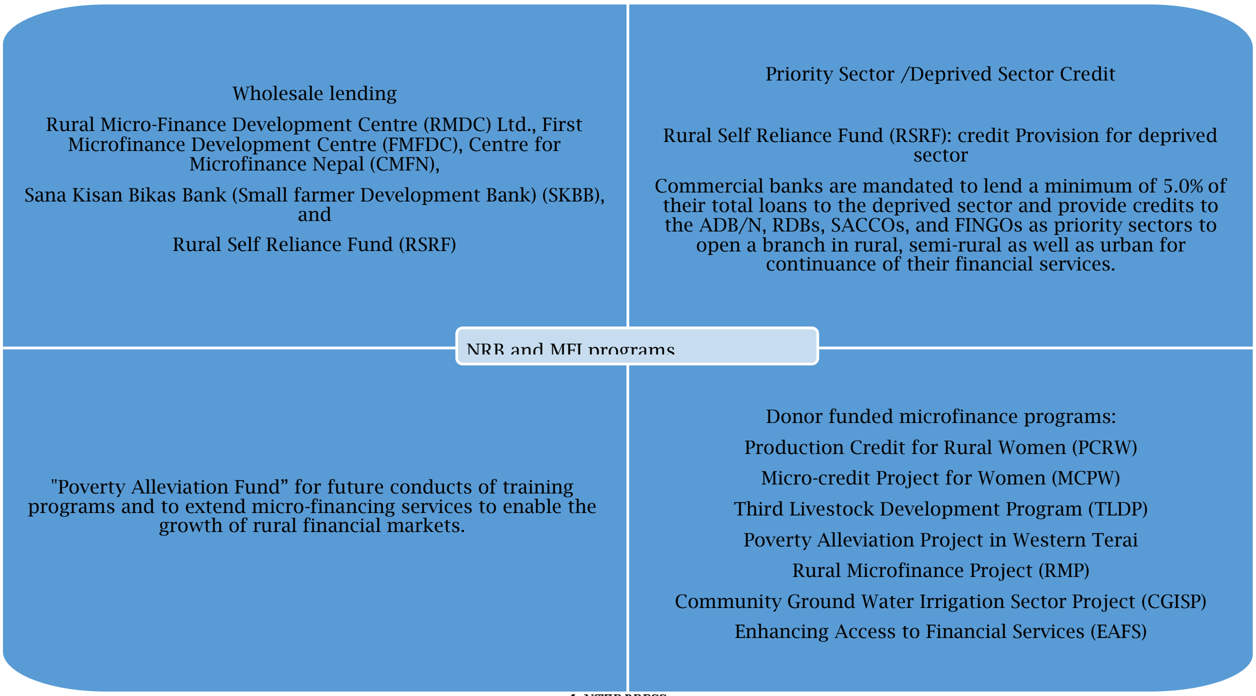
Credit supplier continue to meet the increasing demand for cash. As demand increases so does the cost of credit. The lack of financial inclusiveness in Nepal, as reflected in Figure 1, reflects a low-level of penetration by the formal sector. The informal sector operating in a largely unregulated setting means there are good arbitrage opportunities in lending money. Seasonal migration (also known as labor circulation) has also long been a major feature of livelihoods in rural Nepal (Rose and Scholz, 1980). In rural settings, the majority of family members engage in migratory work. Almost without exception, at least one member of each family leaves the village in search of a job in a nearby town or city and often in the Indian border area.

Cheaper transportation costs and readily available transport facilities from the Indian boarder to cities in India encourage short-term migration. The major border crossing points from Nepal into India are serviced by railway and road transport to major Indian cities. Costs associated with short-term migration principally consist of transportation, food for the journey and funding a couple of days at the destination while finding employment. These expenses consume the majority of money provided by friends, relatives, and local moneylenders.

7. POSITIVE ACTIONS TOWARD MICROFINANCE IN NEPAL

There is a range of initiatives, established by successive administrations, to promote financial services and improve rural production and the quality of life for village people. In Figure 3 below, major programs are noted. There is potential to rationalize the various schemes but no consolidation has occurred. Overlapping programs, present a moral hazard problem and some exploit these to their advantages while others fall through the gaps.

Figure 3. NRB and MFIs programs



The Central Bureau of Statistics (2011b) reports an 80% use of no collateral loans. The figure is 5% higher than the second survey of 2004 and 6% higher than first survey in 1996. This shows that the presence of MFIs and their services has produced an improvement upon the previous decade. This performance has reduced pressure on land and housing as well as other categories: ruminant collateral loans, which have reduced to 12% and 3% in 2011 from 14% and 9% in 2004 (Central Bureau of Statistics, 2011b). MFI financial services in Nepal have made it compulsory to an open account for their clients for their savings, credits and repayments and a savings account for saving purposes.

8. CAPITAL BUILDING

The need for cash for consumption and other purchases creates opportunities for the informal money suppliers to capitalize their investments. Informal sector operators who supply cash to needy poor to fulfil their consumption and other needs are accumulating plenty of cash and growing their incomes. Capital is being limited to the money suppliers. The borrowers are unable to get rid of the debt. The moneylenders are in most cases landowners. In the case study region, landowners are selling land for prices five to eight times higher than the price a decade ago. This gives moneylenders even more cash for their credit supply business and those landowners in the credit business find money lending less risk than sole dependence on agriculture and agricultural products. The gap between wealthy and poor is increasing. MFIs can intervene, bringing their financial services to the poor people in rural, as well as urban, areas for investment and creation of job opportunities at local level (Newman et al., 2014).

9.SUSTAINABILITY

The improvement of agricultural production through self-sufficiency to capital accumulation is essential for the rural poor of Nepal. The traditional way of agriculture forces people to be unemployed where they live or, through economic necessity, to look for employment opportunities elsewhere (Department for International Development, 2007; Walsh and Jha, 2012). From Table 3 it is apparent that the majority of households depend on non-agricultural activities more than agricultural for most of their income. Table 3 also indicates that among for those who do not own land that non-agricultural activities are very significant. There is a reversal for the land-owning portion of the population. The sufficiency of the agricultural products for the landless households is too low at approximately 5%, implying that 95% are not self-sufficient. However, the situation is completely different for landholders.

Table 3. Households and their dependence on agricultural and non-agricultural activities

	Total				Main source of income in the household		Sufficiency of agriculture produce	
	Number of holdings	Area (ha)	Farm population	Average household size	Agriculture	Non-agriculture	Sufficient for household consumption	Insufficient for household consumption
Holding without land	9,327	172.7	52,538	5.6	2,484	6,842	489	8,838
Holding with land	71,517	64,804.5	433,462	6.1	53,597	17,920	35,474	36,044

Data source: (Central Bureau of Statistics, 2013)

Encouraging the development of efficient markets for agricultural products, in the sense of transparency regarding prices and a regulatory framework to minimize corruption and cartel practices, is an essential component for encouraging agricultural investment. A greater confidence in fair prices for agricultural products will, coupled with access to capital through MFIs, will expand the quantity and range of produce available to consumers. There does need to be a market and transport for crops produced.

A recent problem relating to ginger production in Nepal serves as a salutary lesson. Nepal is the third largest producer of ginger after India and China (Prasain, 2014, February 12). The Nepalese farmers having limited training and no access to technical advice on pre- and post-production of ginger to reduce spoiling of this perishable crop by rhizome rot (Nepal Trade, 2014). The lack of a processing plant at local level means export is essential and more than 60% of Nepali ginger goes to India (Gurung, 2013). Indian importers process the ginger adding value (Gurung, 2013) and re-export it internationally.

The farmer while benefiting from the sale is not benefiting from the added value of processing. A producers' cooperative to store, dry and process ginger may be viable but requires investment.

Without access to capital, farmers have no option but to sell ginger to the intermediaries at the offered price or face the ginger rotting (Gurung, 2013).

A market, supported with soft interventions to ensure there is no monopsony present and ginger can reduce the trend of migration or foster reverse migratory trends (Mercy Crops, 2014). The intervention of the financial institutions to facilitate the proper market for the ginger, collecting ginger and establishing processing centers in production regions will benefit growers and the economy. MFI support for individual growers and smaller entrepreneurs will promote a vibrant industry context. MFIs inclusion of rural area has significant and positive impact on people lives in Nepal (Rajbanshi, Huang, & Wydick, 2015) which may support the local and country economy in long term. Furthermore, Lønborg and Rasmussen (2014) find MFIs supported people living is better even though they are poor.

The flow-on effect in terms of better diet, improved health and less reliance on imported perishables will be considerable (Walsh and Jha, 2012 & (Mazumder & Lu, 2015). Government intervention in supporting a more open market is a necessary component of a sustainable solution for the cash poor families to ‘ginger up’ their local economies. This will have direct impact on the agricultural jobs in the region. An increase in agricultural activity will affect employment opportunities and may translate to downstream processing activities (Walsh and Jha, 2012).

Investment in lifestyle changes is not a one-off capital injection. A loan to buy a female kid (goat) can be a start. Support for good nutrition, access to good semen for breeding, basic equipment for milk collection and distribution/sale and care for kids will require ongoing investment. A small enterprise that is successful will repay the capital and interest. If it grows larger, then there is likely to be ongoing leverage required and this is good business for the MFI.

Poultry farming – duck, chicken or geese – can provide a source of protein to the family and produce for sale. When planned and managed at the local level it is obvious that not every poultry owner needs a drake, rooster or gander. The possibility of borrowing with payment in kind for the service can lead to further spin-off business.

Cash crops offer potential and do not necessarily require much land to get started. Roof gardens are common and there is potential to improve with a small injection of capital for quality seedlings and nutrients. The conversion of livestock manure through composting or liquefying is a basic source of nutrients. There is the potential for commonalities. If peas are grown, then pea-hay provides a good source of feed for livestock during the winter months.

MFI credit and on the ground agricultural extension advice is important. In communities where literacy is low schooling is unlikely to provide the necessary knowledge and skills to bolster production, manage risks and improve productivity. MFIs individually or jointly supporting extension services can assist in remedying the knowledge/skill gaps.

Progress is happening in some matters as shown in Table 4, which presents several performance metrics. There additional MFI activities, including both more staffing and lending but there is no evidence indicating an inclusion of the rural poorest of the poor. Delays are costly in terms of quality of life –morbidity rates, health, education and social structures and national cohesion

The number of staff in MFIs has increased due to the number of registered MFIs increasing from 18 in 2010 to 37 in 2014. The Table 4 progress report shows that total staff involvement in MFIs increased from 3296 to 5715, which is 31% and 32% for 2013 and 2014 respectively. There is a significant jump of 78% in MFI branch establishment from 2012 to 2014. The number of centers increased by 42% for 2013 and reduced by 29% in 2014. The sharp downfall in members, number of borrowers and number of passive members points to a potential ineffectiveness in MFIs’ programs. The closing of centers and staff inefficiency in promoting outreach to the neediest people remains a concern. MFIs’ distribution of the microfinance loan improved 41% and then dropped 36% in 2014. This is indicative of the MFI focus towards a profit objective in making loans rather than prioritizing an outreach perspective.

Microfinance loans repaid dropped in 2014 to 30% from 42% in 2013 and outstanding MFI loans increased to 84% in 2014 from 30% in the previous year. Loan loss provision in 2014 reached 31%, up from 15% in 2013. These figures do raise some concerns about MFIs’ staff efficiency and program effectiveness in urban as well as rural areas. The number of depositors declined to 27% in 2014 from 31% in 2013, which would be concerning if it becomes a trend. The total saving-to-total-loan ratio reduced in 2014 to 28% from 31% in 2012. This is only a small reduction and when combined with the share of compulsory savings in total savings the decline does start to raise concerns. The proportion of compulsory savings to total saving assumed to be MFIs borrowers, reduced to 35% in 2014 from 38 % in 2013 and 41% in 2012.

10. WHY DOES MICROCREDIT NOT REACH MANY OF THE POOR?

Rural poor in Janakpur, indicated they did not join the programs because they lacked the skills in the particular specified program or they lacked labor resources as family members were already fully committed and sometimes out of Nepal. Some mentioned that they are afraid of the consequences if they failed to meet a loan repayment. Most people did not want to join the program because they thought MFIs charged high interest rates. Prospective borrowers can readily compare the cost related to a loan with of the charges made by local moneylenders but the knowledge to do this is not available. Rules and regulations that borrowers must accept when taking the loan from an institution appear too demanding compared with the flexibility of moneylenders. An MFI loan is formal and does not give a grace period to commence making loan instalments, and this gives a bad impression of the MFI program vis a vis moneylenders. People preferred not to deal with an MFI even when one became available.

Another perspective respondents gave was that the staff of these institutions were picky and did not reach out to the households of the rural poor. It is because of the pressure placed on field staff from their senior officers to collect loan repayments and to make sure people do not default. If Field staff performance measured by the percentage of repayment of the loan and no defaults, then an adverse selection failure arises. Prospective borrowers who appear most likely to repay the loan and exhibit low default risk get the money. The poor and unskilled rural people who are the target clients are excluded.

Partnering arrangements with the local communities for MFIs that have a policy to encourage local people to take responsibility to ensure payment of loans are difficult. When requested to be local representatives there is general reluctance, on the part of villagers, to take on the task. The possibility of default discourages village members from wanting to be responsible for uncomfortable action. The confidence level of repayment on a group loan diminishes with individual member's poverty level. MFI field staff play a significant role in choosing groups and their respective members. If non-performing loans have a bearing on the field staff's performance record there is low risk taking. Typically, there is no confidence that the poorest people will make their loan repayments on time, which effectively excludes them from consideration for taking out loans. Barriers within the MFI and doubts in the community combine to ensure a maintenance of the moneylender hold on the poor and social pressures from short-term migratory labor continuing.

Table 4. MFIs in Nepal

Indicator	***2014***	***2013***	***2012***	***2011***	***2010***
No. of MFIs	37	31	24	21	18
				Changes	
				2013	2014
Total no. of Staff	5715	4319	3296	0.31	0.32
No. of Branches	1062	813	598	0.36	0.31
No. of Centers	73076	56503	39895	0.42	0.29
No. of Groups	290368.2	280871.2	215128	0.31	0.03
No. of Passive Groups	11020	9959	8844.4	0.13	0.11
No. of Members	1476636.85	1542345	1163712	0.33	-0.04
No. of Passive Members	52846	68543	61811	0.11	-0.23
No. of Borrowers	1030914	1060315	848974	0.25	-0.03
Total loans disbursed	249169122	181155300.9	129519366.8	0.40	0.38
Microfinance Loan	201572927.3	147887362.6	104856050.1	0.41	0.36
Micro Enterprise Loan	16610437.93	11301362.11	7900618.787		
Other Loan	30985756.73	22789231.14	16762697.91		
Loans Recovered	199152117.7	149228936.1	108504536.3		
Microfinance Loan Repaid	164999794.1	127082834.6	89545338.64	0.42	0.30
Micro Enterprise Loan Repaid	11323438.36	7865274.145	5786789.956		
Other Loan Repaid	22828885.25	14280881.88	13172407.66		
Total Loans Outstanding	50302718.17	31926362.24	21014830.54		
Microfinance Loan Outstanding	36753899.68	19984277.54	15317580.39	0.31	0.84
Micro Enterprise Loan Outstanding	5394309.343	3436076.441	2109430.783		
Other Loan Outstanding	8154509.148	8506008.42	3597397.82		
Overdue Loan	470825.3157	527067.1495	668542.7994		
No. of Overdue Borrowers	32742	30044	52585		
Total Interest Recovered	12258424.1	8552126.779	5595176.416		
Total Due Interest	474816.965	450136.9224	468863.9296		
Loan Loss Provision	1058900.39	807060.935	702705.4045	0.15	0.31
No. of Depositors	1451453.5	1142160	866222	0.32	0.27
Total Savings	14200338.24	9917091.892	6409471.449		
Compulsory Saving	5019172.834	3793767.201	2600161.822		
Optional Saving	4659335.561	3253525.832	2200609.475		
Other Savings	3731066.188	2338395.547	1265497.466		
Saving from People	790763.6595	531403.3114	343202.6858		
Total Saving/Total Loan %	28%	31%	30%		
Total Microenterprises Loan/Total Loan %	11%	11%	10%		
Microfinance Loan / Total Loan Outstanding	73%	63%	73%		
Compulsory Saving in Total Savings Ratio	35%	38%	41%		
Loan Recovered Ratio	83%	85%	83%		
Loan Recovered to loan disbursed ratio	82%	86%	85%		

Data source: (Nepal Rastra Bank, 2014b; Nepal Rastra Bank, 2014c; Nepal Rastra Bank, 2014d)

11. SUMMARY

Nepal through recognizing short-term migratory labor, as an economic and social cohesion issue can promote the alternative model of an enhanced quality of life for rural poor through the provision of connecting sources of cash, viz. microfinance. This requires no additional organization or large-scale bureaucratic injection of resources. Rather it requires MFIs to say collectively that they will move to address the problem of rural poor in selected regions. There are establishment costs as there are no offices or personnel in the remote regions.

MFIs, in the modern sense, emerged with a mission of providing low interest loans to the poorest of the poor. They were, and are, a key component of financial inclusion. However, when financial performance becomes the key consideration above outreach, then managing risk gains greater sway. There tends to be a safety first goal in lending and this almost inevitably results in an urban drift. Also if MFI staff receive bonuses for achieving lending targets, then this sends a clear signal, encouraging staff to maximize safe lending rather than promoting outreach to the poor.

There is a lack of goal congruence for Nepalese Government, Central Bank, and MFI boards and management. Regulation and directives generate adverse selection outcomes and the way forward requires an incentivizing of MFI activities in rural communities, which is largely fiscally neutral and has minimal monitoring costs. A trickle-down effect could be helpful and may start to build some confidence among Nepal's poor population that MFIs can be trusted and they can be working partners, because they encourage increased employment through the MFIs' financial services activities and income generation opportunities.

The village committee team, which is the hallmark of rural lending by sub-Sahara African MFIs, has potential at the village level. Where there is an informal financial sector operating, e.g. a moneylender, then it may be possible to license them to be an MFI representative. It would be a first step toward more financial formality and, more importantly, open a low cost channel to the village poor. Structuring the remuneration to achieve goal congruence between loan shark and MFI may prove interesting but it is unlikely to be insurmountable. For the moneylender, a move to cooperation rather than regulatory interference is preferable.

An adaption of the adage "that money makes the world go round" for rural Nepal could be "a lack of money makes the people go around".

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