# Report on the Boulder-Bergamo Forum on access to financial services in rural areas, Italy 18-20 September 2008.

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The forum on financial services in rural areas and for agriculture held recently in Italy brought together researchers, people who work in the sector and political decision makers, following the example of the FAO conference of March 2007 or the FARM foundation's conference last December in Paris[1]. One of this forum's major partners was the Bill and Melinda Gates Foundation. The Gates Foundation's goal in providing this support was to encourage dialogue and make progress in implementing a strategy to be agreed upon by the different groups involved (researchers, decision makers and people from the field) to collect important data systematically in order to assist research work in the field of rural finance and agricultural financing.

The speakers were selected by personal invitation rather than by a call for proposals. There was a poster session to provide information in addition to the speeches. The major names in the English-speaking rural finance field were present; researchers from Ohio State University (Rural Finance Program) were particularly well-represented. There were few important figures from the South, which was under-represented.

All the contributions, notes taken during discussions and questions asked by the audience are available on the conference's wiki site (in English):

http://www.bouldermicrofinance.org/bergamowiki/index.php?title=Main_Page

The point of this update is not to summarise the complete contents of every discussion but rather to note the major thoughts and questions raised. In comparison with the FARM conference held eight months earlier (December 2007), we can see that some ideas were not broached at all (farming community organisations, fair trade), while others were touched upon as background ideas (particularly the question of public policies). However, three themes came up regularly: the problem of climate change, research methods and lastly new information technologies.

**A new paradigm?**

One of the forum's objective announced consisted of considering the emergence of a new paradigm for rural financing. Dale Adams, professor emeritus of Ohio State University and founder of the OSU Rural Finance Program, who was publicly recognised for his life-long devotion to rural finance in a reception organised in his honour, attempted to answer this question. He first proposed a brief historical review to mark two periods, the first being the period from 1950 to 1980, which he calls "Agricultural Credit I" typified by bank contracted, agriculture-focused credit combined with a push for modernisation of the agricultural systems (green revolution). The many well-known failures of this approach (short-term handout solutions, loan defaults, corruption, etc.) led to a complete denial not only of public intervention, but also of agriculture itself. The paradigm that has been in place from 1980 to the present, what Adams calls "Agricultural credit zero" was born out of this; development financing in this system is limited to microfinancing, a useful but limited instrument that focuses on "urban areas, women, short term loans, regular repayments, consumption smoothing and high interest

[1]The documents from these conferences are available at the following addresses: http://www.ruralfinance.org/servlet/CDSServlet?status=ND00NjY0MCY2PWZyJjMzPSomMzc9a29z http://www.fondation-farm.org/spip.php?article222

rates, all "light" guarantees. All these specifics are hardly compatible with agricultural financing. In the face of an emerging food crisis, which may turn out to be major, he calls for a new paradigm ("Agricultural credit II") which would restore financing dedicated specifically to agriculture and would focus more on savings, with the point being to avoid repeating the mistakes of the past. He did not venture to make further proposals and expressed a certain pessimism given the lack of agricultural experience, both in the academic sector and within international aid organisations. None of the other speakers or discussions at the forum directly addressed this question of a new paradigm, leaving participants to judge for themselves what might it might entail.

**Developing agricultural financing: managing climate change**

Many of the discussions were focussed on the question of risk management and climate risks in particular, which are considered an essential condition for developing agricultural financial services.

The solutions are therefore to be found in climate insurance and loans coupled with insurance. Faced with the risks that affect agricultural production, J. Skees considers that while integrating distribution channels can provide some answers to climate risks (and a session was dedicated specifically to the idea of "supply chain finance" a topic that was already heavily covered during the FARM conference) he noted first that the distribution channels (input access/product disposal) are underdeveloped in Southern countries and secondly that where the insurance and credit markets work jointly there is a stronger positive impact on growth than in places where the insurance market is not very strong. Savings makes it possible for people to face some risks but insurance protects populations from greater risks.

For that matter, it seems important to broaden scientific knowledge on the perception of risk and in particular its psychological dimension for the populations concerned. This would no doubt help to explain the limited success of insurance products (see Morduch's and Copestake's contributions).

**How can interest rates be reduced?**

a) Subsidise interest rates?

The academic participants attempted mainly to show the problems of subsidising interest rates, with a conclusion-cum-caricature by Jacob Yaron. According to his analysis, the choice facing governments is this: either we change interest rates and affect only a minority of farmers or we don't touch interest rates and we increase access to financial services. After that partisan and un-scientific view, Mr Thorat, former chairman of the National Bank for Agriculture and Rural Development (NABARD) in India stressed that the Indian and Chinese governments thought of these arguments but were led to act differently by practical considerations: they subsidised interest rates! The current approach in India is guided by the desire to find a proper balance between the "cost-plus" approach (real cost + a profit margin for the financial institution), which he believes to be politically unfeasible and the low level that the State is seeking in order to end annual interest rates of the order of 9%. He feels that research must play a part in balancing different approaches while keeping in mind the political dimension of agricultural financing.

b) Other possibilities

For some speakers, "Credit bureaus" appear to be the most promising option for reducing interest rates. Sharing information on borrowers makes it possible to reduce transaction costs. However, they do not reduce the risks that weigh on these loans (particularly those linked to climate risks). The difficulties of setting them up (in particular coaxing the IMF to share their information) which have not yet been resolved should also be mentioned. New technologies have also been mentioned as so many tools that could considerably facilitate their set up (e.g. use of cell phones to access information in real time), with the important thing being to find a balance between consumer protection, personal privacy and financial inclusion.

**What role should research play? Better understanding of the diversity of people and financial needs**

The lack of information (in particular as to the question of risks) was brought up time and again. As for research, understanding the diversity of people and their financial needs was stressed, as this will make it possible to match the supply to the demand, to better understand who is financially excluded and why and also how to reach them.

Two innovative research projects in this field were dealt with:

a) Financial diaries

The research programme on financial diaries (the result of previous work by Stuart Rutherford) proposes an astute analysis of demand using an exceedingly qualitative approach, i.e. very specific data collected regularly (every two weeks) on cash-flows within households from a small sample (between 40 and 100 households, with studies being led in Bangladesh, South Africa and India). The following principal results were obtained:

- there is a an intense borrowing/lending practice independent from micro-financing, a sort of "personal financial intermediation" which aims to create large sums from small sums,

- the impacts of microfinance are limited in terms of business creation (e.g. the Grameen Bank) or collective dynamic (e.g. SHGs in India) but are most widely seen in an intensification/acceleration of this practice of personal financial intermediation

However, despite the great number of these debt/credit practices, the analyses stemming from these financial flows show that not all households are over-indebted.

b) Randomised Evaluations

On the other hand, randomised evaluations (presented by Dean Karlan in a plenary session and then by Annie Duflo in a workshop) offers an analysis of the impact and the demand (with a very operational viewpoint) using clinical trial type methods, i.e. two identical populations are compared, one which has a service and one which does not (the exercise can also consist of comparing two populations that have services A and B, respectively). Several examples of results were provided: the effectiveness of restricted savings accounts (with a preference for illiquid accounts), greater sensitivity to the amount of payments than to the interest rates, effectiveness of training, clients' preference for individual loans and the effectiveness of individual loans compared to collective loans, the effectiveness of weekly compared to monthly payments, etc.

James Copestake (Bath University, founding member of the ImpAct programme) made some interesting comments and raised some criticism[2], which are both helpful in understanding the impacts and the limits of such methods of evaluation. According to his comments:

- randomised evaluations are a "neat" and "elegant" method that offers real answers to the constant problems of impact studies – in particular the questions of attribution (like isolating the effects of microfinance) and bias in selection (how to compare two similar populations); it also has the advantage of providing clear results;
- while this method resolves certain problems, we may wonder if it doesn't worsen others:

[2] http://bouldermicrofinance.org/bergamowiki/resources/CopestakeRandomizedTrials1.pdf

- lack of contextualisation and consequently, difficulties in generalising information ;
- does this technique attempt to take the place of certain research questions?
- this method doesn't remove some of the biases concerning the control groups (information is circulated among the population targeted by the study);
- what about ethical questions regarding control groups? "Financial services are not chemicals and people are not plants";
- what about the costs? This method is both time consuming and costly; aren't less rigid methods (focus groups, satisfaction surveys of clients) more appropriate in some cases? (Are we "hitting a fly with a hammer?");

- and lastly, Copestake considers that we must invest in research and that lenders' enthusiasm for randomised evaluations is, for that reason, welcome, but this enthusiasm must not allow this method to supersede all others employed by researchers and people who work in the field, thereby reducing the range of impact studies used.

c) "Mental Models"

Echoing the impact studies based on randomised evaluations, James Copestake presented what may have been one of the most interesting and innovative points of the forum, the concept of the "mental model" [3], i.e. the way in which people view themselves and understand their environment (in this case, the financial environment). Mental models are similar to social standards, but they also draw upon psychological and cognitive variations, habits, and routines that result from the socialisation process. These models vary from person to person and have a strong influence on their monetary and financial practices as well as they way in which they use (or don't use) microfinancing services; taking these factors into account is essential to understanding the diversity of client profiles.

**New information technologies**

During the forum, numerous speakers brought up the role of Information and Communications Technologies (ICT). As a potential source of technological innovation, ICTs encourage the development of tools that help to encourage financial inclusion. In no particular order, we can cite the experiences in Brazil with digitised agent banks (Kumar, Nair, Parsons, Urdapilleta, 2006) or in Columbia where mobile banking agencies are connected to banks' information systems via satellite.

The most innovative contribution concerned the theme of "Technologies and the financial access frontier". The founder and director of Bankable Frontier Associates, David Porteous led the topic of discussion to "transformational branchless banking" which can be defined as "the use of information and communication technologies (ICTs) and nonbank retail channels to reduce costs of delivering financial services to clients beyond the reach of traditional banking." To clarify the concept, Lyman, Pickens and Porteous (2008) [4] differentiate between "additive branchless banking" and "branchless transformational banking services", additive branchless banking indicating services that "merely add to the range of choices or enhance the convenience of existing customers of mainstream financial institutions" while transformational services "extend to customers who would not be reached profitably with traditional branch-based financial services."

[3] http://www.welldev.org.uk/news/news-pdfs/Briefing-CGAP1.pdf

[4] http://www.microfinancegateway.org/files/46734_file_FocusNote_43.pdf

To the question “how do mobile phone users’ literacy or illiteracy affect the service?” the answer “this doesn’t seem to be a major problem because the important part is typing in numbers and most people know how to deal with numbers” brought some remarks on illiteracy as a limiting factor in the development of rural financing. We would remind everyone of Amaeshi’s work (2006), for example, showing that one of the major factors determining financial exclusion in developing countries is none other than an inability to read and write. Against the enthusiasm raised by ICTs, which should transform clients’ lives, modify their perceptions of things, their relationships, etc., other comments pointed to the effects of these dematerialised exchanges in building confidence[5] and even social capital through what remains simply communication concerning debt.

## Bibliography

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[5] For more about this subject, see Donner and Tellez, 2008.