RURAL FINANCIAL DEVELOPMENT IN ZIMBABWE: PAST, PRESENT AND FUTURE OPTIONS.

By

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INTRODUCTION AND BACKGROUND

1. Historically, output in the smallholder agricultural sector has been relatively low, as reflected by the low level of contribution to the market. In 1979, less than 5,000 commercial farmers produced Z$362 million of agricultural output, while 9,000 Purchase Area farmers produced about Z$10 million and 640,000 communal area farmers Z$15,4 million of agricultural output. It is generally argued that the smallholder sector was not very productive because of lack of essential support services such as relevant technical research, extension, price support, marketing and financial services.

2 In development literature, it has been argued that economic growth is to a very large extent a function of the rate of investment. In agriculture, in order to shift production functions upward, farmers must be able to invest in new improved technologies such as high yielding varieties and fertilisers. The rate of investment has been seen to be heavily influenced by the availability of financial services whose key functions include mobilization and allocation of savings. If financial markets fail to mobilise and allocate savings, profits become lower than would otherwise have been and performance of the entire economic system may be impaired. In Zimbabwe, failure of the financial system to address people's needs has been seen to impair growth in the smallholder agricultural sector.

3. The development of rural finance has been characterized by the channelling of cheap credit to a small proportion of farming households and the very limited provision of markets that mobilise savings. This direction of development supports the belief that rural households do not have the propensity to save and therefore they can not invest. Because the formal sector does not provide adequate financial services to the rural sector, the informal sector has risen to fill in the gap. In the process of Zimbabwe's economic development, the two financial sectors formal and informal, have grown side by side. Their main aim has been to increase productivity in the various economic sub-sectors.

4. Since 1980, Zimbabwe's agricultural policy statements have been dominated by the need to increase productivity and improve the standard of living in the smallholder sector. Between 1980 and 1985, there was a dramatic increase in output recorded in the smallholder sector. This was due to farmers returning to their land after the end of the war of liberation and the provision of a whole package of support services which included technical research, extension, price support, marketing infrastructure and finance. Growth in output could not be attributed to one factor, but to a combination of all the above. Although credit was important even, non borrowers experienced this growth in productivity, confirming the fact that credit alone is not the key determinant.

5. Because supply of land is inelastic, increased agricultural productivity is to a very large extent a function of the rate of investment in improved technologies. As indicated above, the rate of investment itself is dependent upon availability of finance either through loans or savings. Most households in the smallholder sector are believed to have a low marginal propensity to save, and therefore are not able to invest from savings. This has

partly explained why government of Zimbabwe (in common with many other governments in developing countries) has focused on the provision of credit, as a strategy for smallholder development. Such credit is often subsidized - which places a heavy drain on scarce national capital resources. And, as a corollary, little attention is paid to savings mobilisation. But experience has shown that most smallholder farmers are high risk borrowers so that their capacity to use credit efficiently and repay their loans is questionable.

HISTORICAL DEVELOPMENT OF FINANCE IN THE AGRICULTURALSECTOR

6. Until Zimbabwe's independence in 1980, financial development was geared towards the more commercially oriented sectors. Smallholder producers requiring financial intermediation had to travel to urban centres and carry out their transactions at these urban - based institutions. The types of financial services they could access were very limited and information on various forms of financial investments such as securities and stocks did not easily reach rural areas. Of more significance, loans to invest in various forms of productive enterprises were not available.

7. The large - scale commercial farming sector has historically enjoyed a great deal of financial support from successive colonial governments, through both public and private institutions. As far back as 1924, the Land Bank was established to assist large-scale commercial farmers to acquire farm land. It facilitated acquisition of farm land by a significant number of white commercial farmers who would have otherwise been unable to afford the land. Another scheme that assisted large-scale commercial farmers (whites) in acquiring land was one introduced at the recommendation of the Danziger Commission. The Commission recommended the abolition of interest on loans for capital development such as purchase of farms and loan repayments were deferred for three years. In 1935, a subsidy programme was launched to allow farmers to build dams. After the World war, a scheme to facilitate ex-service men's entry into commercial farming was launched. Under this scheme, government purchased farms and allocated them to ex-servicemen. In addition to financial grants these emergent farmers were given free intensive training, resident on a farm, under supervision of an established farmer with the cost of living and allowances met by government.

8. In 1930, the Southern Rhodesian government for the first time extended credit to peasant farmers who were on Trust Land Irrigation Schemes. The credit was made available on a very small scale and was provided in the form of physical inputs and services. Costs of these inputs and services were deducted from revenue received from sales of products. This type of repayment is referred to as stop-order system. It was not until 1956 that credit to dry-land farmers was introduced, through the African Development Fund, and through the African Co-operative Societies between 1956 and 1958 (Whitsun Foundation 1981). The use of co-operatives to make credit available to Trust Land and Purchase Area farmers continued until 1979 when the AFC started making advances to Trust Land Farmers.

9. Until 8th February 1979, the Agricultural Finance Corporation was precluded from making loan advances to farmers in communal areas. Although the AFC's Small Farm Credit Scheme was introduced in 1978, it was initially designed to service Purchase Area farmers, particularly for seasonal finance.

10. The shift towards the inclusion of communal area farmers in 1979 was due to the changing political environment. The provision in the AFC Act, Chapter 109, which precluded AFC from lending to communal area farmers could no longer be accepted in an independent Zimbabwe. The relevant provision, (subsection 3 of section 22) read as follows:

> "The Corporation shall not make advances to a tribesman as defined in section 37 of the Land Tenure Act (Chapter 148) in relation to any operations carried on by that person on Tribal Trust Land".

This provision was repealed on February 9th 1979.

THE ROLE OF INFORMAL FINANCE

11. It is often argued that the size of the informal financial sector is a reflection of lack of development of the formal financial sector. In rural Zimbabwe, informal finance is predominant particularly in the area of savings mobilization by mainly women's groups. Savings clubs constitute the single largest movement mobilizing rural finance. These clubs come under a number of umbrella organizations such as the Self-Help Development Foundation (SDF), the Association of Women's Clubs (AWC), Input Suppliers such as Agricura, Windmill, and various churches.

12. Membership of savings clubs has been increasing steadily since the sixties. Data for those clubs affiliated to the SDF, which until the late eighties was known as the Savings Development Movement, are more readily available. Table 1 shows the growth in membership between 1970 and 1991. The current total membership is estimated to be standing around half a million. (SDF,1994). Over 75% of savings club members are women. A study carried out by IFAD in 1985 estimated that over 30% of rural households had members belonging to informal financial groups. Of these, close to 19% were members of SDF savings clubs (see Table II). According to current statistics provided by SDF, this percentage has since gone up.

13. Savings clubs have mobilized millions of dollars in rural areas which they have deposited in urban-based financial institutions. In 1994, SDF estimated total deposits by savings clubs to be over $5million. These deposits are invested mainly in urban centres because financial institutions which collect the deposits do not advance loans to savings club members for investment in rural areas. These informal groups mobilize savings for formal financial institutions and bear the bulk of transaction costs. Clubs collect small deposits

from individual members, record the amounts and take them to financial institutions where they deposit them. All these transaction costs are borne by savings club members who only get an interest rate that is frequently below the rate of inflation. A number of studies in different regions have shown low interest rate elasticities suggesting that other factors such as convenience and safety may far outweigh interest rates in determining the desire to save. (Wai 1977, Chimedza, 1993)

14. With respect to informal lending this activity is not as widespread as savings mobilization. Pure money lending is not as common in rural areas as it is in urban areas. A large part of the informal lending in rural areas takes place between relatives or friends and it is often interest-free. A significant proportion of credit facility may be operated by local retailers. This includes loans for things ranging from household items to agricultural inputs and equipment. Here, the arrangement is informal. Some of the more widespread informal lending initiatives tend to have a savings and credit element. Rotating Savings and Credit Associations (ROSCAs) are a case in point. Members of ROSCAs deposit an agreed sum at regular periods and pay out the pooled savings to individual members on a rotational basis. The whole concept involves making a number of deposits which one withdraws at some date in the future. In many cases the use of this money is targeted. Whatever the use is, these savings alleviate cash flow problems of those involved.

15. One of the major objectives of savings clubs has been to mobilise savings for the purpose of purchasing inputs. In using their savings they run the risk of losing their past income when there are crop failures. The future income from investment in inputs is not guaranteed. This is the same risk that credit institutions take. Where loans are subsidised and administrative costs are high, the risk taken by lending istitution is even greater.

16. In many cases, these informal groups provide training, supervisory and advisory services for the sustenance of the enterprise. Informal finance is designed by the people to meet their special needs. It has flexibility, ease of transactions and rapidity in implementation. These important features make informal finance suited to the needs of low income people. It is however very clear from the operations of savings clubs that informal finance does not always stand on its own. It links up with formal finance at some point. Through holding savings club deposits in formal financial institutions, informally mobilized savings link with formal services. It may be that in order to develop financial systems that service rural areas effectively, one needs to look to both formal and informal systems and draw the best elements from each of them.

AFC's LENDING TO THE SMALLHOLDER SECTOR

17 During the first year of lending to smallholder producers, a group of 2,846 loans amounting to $478,000 were granted to communal area farmers with the assistance of the Department of Agricultural Development (Devag) on a pilot project basis. The manager of the Small Farm Credit Scheme was authorised to grant loans of up to $10,000.00 per

individual, including existing indebtedness. Most seasonal loans were made available in the form of inputs except for limited cash disbursements for payment of labour. The programme was extended in the 1980/81 season with the disbursement of 18,000 loans valued at Z$4,8 million.

18. In 1985, numbers of small farmers loans reached their peak at 77,526 with a total value of $38.9 million. Thereafter, the number of loans started to decline while the value increased in real terms Table III (AFC 1994).

19. Right from the beginning, it was recognized that lending to smallholder farmers was more risky and that operational costs per dollar would be higher than they were in large-scale commercial lending, and therefore government accepted the responsibility of indemnifying the AFC for the difference between the return on lending and lending costs. In addition, government also acts as guarantor of small farm lending.

AVAILABLE SPECIAL SCHEMES

20. The Agricultural Assistance Scheme was established, along side with the Small Farm Credit Scheme. It advanced loans for more than normal business risks. The establishment of the Agricultural Assistance Scheme was a recognition of special circumstances that may arise, requiring particular kinds of financial innovations. This is an area that has not been well developed in Zimbabwe and yet it provides potential for growth in agricultural support industries. The Tenant Farming Scheme was another innovation that was meant to respond to special needs. Tenant farmers could benefit from this scheme after satisfying AFC that they had the necessary experience and ability and could contribute not less than 10% of advances. Loans under this scheme were not underwritten by government and therefore the AFC was highly selective because it carried the full risk of loss.

21. While credit facilities to communal area farmers were being introduced on a limited scale, large-scale commercial farmers continued to benefit disproportionately more than any group. In addition to finance for land acquisition and improvement, large amounts of seasonal loans were advanced by AFC (see Table III). This was not their only source of formal agricultural credit. Commercial banks and input suppliers also provided a significant proportion of credit requirements. By 1980, AFC accounted for 38% of the large-scale commercial farmers' short-term credit requirements, while commercial banks supplied 34% and co-operatives and companies, 28%. (Slangen, 1989). Table IV clearly shows that large-scale commercial farmers have had alternative sources of formal finance, while communal area farmers have been totally dependent on public lending institutions such as the African Loan Fund and subsequently the AFC.

22. The land resettlement programme which was launched after independence, was designed with its special loan fund. The three resettlement models, A B and C had credit schemes that were designed to help farmers achieve the objective of producing surplus for

the market. Model B schemes which are collective co-operatives were initially provided with settlement grants and then loan funds. In 1981/82 , the first loans valued at Z$10,6 million were advanced to farmers on resettlement schemes (AFC 1982, and 1984).

23. It was soon realized that loan funds under the resettlement programme were not adequate. This was particularly true for the model B collective co-operative schemes which were trying to operate large-scale farms along the same lines as the privately owned ones. Some members of Model B collective cooperatives, who recognized inadequacy of finance as a serious impediment in their efforts to operate their enterprises along profit making lines decided to take an initiative and identify or help develop alternative sources of finance. They believed that for them to succeed in the absence of such specialised financial institutions as cooperative or Rural Development Banks, they had to break into existing formal financial markets and borrow at commercial interest rates. To facilitate this process, a group of co-operators came together in 1988 and started a specialist scheme called the Collecting Self-Financing Scheme, (CSFS). This is a guarantee scheme formulated and controlled by collective co-operatives. It seeks to utilise bank finance for their development. To date, it has relied on donors for guarantee funds. The scheme has broken the reluctance of banks to lend to co-operatives.

24. In addition to supporting existing mainstream activities commercial banks have also supported diversification activities such as game ranching, export horticulture etc. In most cases, banks are reluctant to provide long-term finance for diversification because the risk is higher. AFC has made substantial funds available for farming operations which are starting up. Again, the risk in these new operations is high.

25. A number of financial innovations have been developed to meet special needs of large-scale commercial farmers. From 1980 to 1989, there was a decline in AFC's large-scale commercial farm lending despite the Corporation's relatively more favourable lending rates. A major factor in their decline was the breakdown of AFC's computer system in 1986 and 1987. This created problems whereby a lot of data was lost and never recovered. Some farmers were seriously inconvenienced and lost confidence in the Corporation while others benefited. However, some of the clients lost through this mishap were regained when AFC established a special scheme to provide its clients special access to foreign exchange for equipment. The World Bank supported Agricultural Credit and Export Promotion Project contributed significantly to AFC's recovery of the large-scale commercial farm market. It became quite clear that for this group of farmers, availability of finance was not a constraint. What was of concern to them was their lack of access to foreign exchange for purchase of equipment. With the recent liberalization of the financial sector and in general the opening up of the economy, there do not seem to be any serious deficiencies in financial markets serving the large-scale commercial farming sector.

26. On the contrary, formal financial services in the smallholder sector face serious deficiencies. This is to a large extent reflected in the persistence and expansion of informal finance in this sector. At its lending peak, the AFC, the only formal financial institution

providing agricultural loans to smallholder producers, advanced loans to only 10% of communal area farmers. This is way below real demand. The remaining 90% had to resort to self-financing and informal sources. It is estimated that the major source of production finance is crop sales. Remittances from household members in wage employment, off-farm income from such activities as brickmaking, beer brewing and sale of labour and savings (which often times are major part of income from crop sales) are also important sources of finance.

27. Until 1980, the few formal financial institutions which were available in rural areas confined themselves to accepting deposits and did not engage in lending activities at all. Due to the deliberate policy to promote faster growth in the smallholder sector in general and the communal areas in particular, government encouraged the decentralization of formal financial institutions into rural areas. In addition, because the favourable policy environment led to increases in agricultural output resulting in improved incomes, there was increased demand for financial services, to which formal institutions responded in a limited way. By 1991, the Post Office Savings Bank, all Building Societies and most commercial banks had branches, sub-branches and agencies in rural areas. Table V shows the distribution of formal financial institutions countrywide in 1992. However, these institutions continue to confine themselves to savings mobilisation without advancing loans.

SUPPLY OF CREDIT TO THE SMALLHOLDER SECTOR

28. The AFC continues to be the single largest source of institutional agricultural credit for communal and resettlement areas. In the Zimbabwean context, the perception is that AFC has both social, moral and economic obligations to farmers. Social or moral obligations have dictated the fixing of lending rates at lower than the market interest rates, about 13% between 1981 and 1991. These obligations have also dictated that government underwrites loans to smallholder producers, allowing AFC to continue with development activities as opposed to having commercial ones only. This provides an explanation as to why AFC continues to lend to a sector where it is losing $0.16 on every dollar lent to communal area farmers and $0.26 on each dollar lent through the resettlement credit scheme, while lending to large-scale commercial farmers yields $0.07 profit on each dollar (AFC, 1990).

29. Short-term credit constitutes AFC's largest lending category for all groups of farmers including the large-scale commercial farmers. In 1988/89, short-term lending accounted for 90% share of loans granted, whose value was 82% of total funds. During the following year, 1989/90 shares of short-term loan numbers remained at 90% but their value dropped to 70% (AFC, 1990). In the category of communal area farmers alone, 91% of loans granted or 92% of funds went to short-term lending in 1989/90, while proportions for large-scale commercial farmers were 61% share of loans, taking up 75% of total disbursements. Although the number of short-term loans granted to large-scale commercial farmers was

very small, 590 compared to 39,911 for communal areas, their value was disproportionately high at $102,35 million compared to $30.85 million granted to communal area farmers (AFC, 1990). This meant that communal area farmers accounted for 98% share of loans whose value was only 23% of total funds disbursed as short-term loans, while the reverse was true for commercial farmers.

30. Large scale commercial farmers, whose loan share in numbers constituted 3% of the total, accounted for 85% of financial resources granted during the 1990/91 season (AFC, 1991). This has been the pattern of credit distribution since the establishment of the AFC Small Farm Credit Scheme in 1979.

31. Disparities in resource distribution do not only occur among various farmer categories but also along regional lines. The most productive provinces tend to get a larger share of loan funds. Out of the eight provinces, two accounted for 57% of loan funds granted (AFC, 1991). Mashonaland West and Mashonaland Central which have some of the most productive cropping land get the largest share of AFC loans. This is in line with AFC's deliberate policy of targeting loans to farmers with the greatest potential for repayment.

32. The AFC witnessed rapid rise in the number of loans granted from a grand total of 23,859 in 1980/81 to a peak of 95,269 in 1985/86, thereafter declining to a low of 36,742 in 1990/91 (AFC, 1991). The number of loans continued to decline reaching a low of 22,319 in 1993 (AFC, 1994). Much of the decline was experienced in the Communal farming areas. From 1990 to 1992, there was a steady increase in the commercial farmers loan share.

33. The recent growth in loan demand by large scale farmers has been attributed to the diversification of AFC's lending operations. Such expanding operations as horticultural production and game ranching are placing increased demand for credit. Diversification is not only confined to large-scale commercial farming operations. The smallholder sector has also benefited from it. However, demand for loans in this sector has not increased despite the fact that lack of finance continues to be cited as one of the major constraints in the expansion of agricultural output in this sub-sector. Lack of growth in demand for loans by smallholder producers is an indication that the system is not working efficiently.

FACTORS HINDERING DEMAND FOR LOANS BY SMALLHOLDER PRODUCERS

34. AFC's lending activities in the smallholder sector have not produced the desired results. In addition to the continued decline in the demand since 1986, rates of repayment have not been pleasing for most of the time. In January 1990, 80%, 68% and 77% of communal area, small-scale commercial and resettlement loan recipients respectively were in arrears (World Bank, 1991). At the same time, AFC was making a loss on every dollar it lent to and recovered from these farmers. Transaction costs were high while interest rates remained fixed below commercial rates. It may not be wrong to assume that there was a

problem, particularly with the supply side of the scheme. Why were farmers not willing to take advantage of cheap loans?

35. In much of financial development literature, interest rates have been identified as key determinants in demand for loans. In Zimbabwe, however, it can be argued that demand for loans is interest rate inelastic. (Chimedza's (1993) study found that interest rates were not a significant factor in the farmers decision to use credit. This then attributes farmers' unwillingness to take advantage of cheap loans to other factors.

36. Some studies have identified the stop-order repayment system as one of the major factors responsible for farmers' reluctance to borrow. The system has been unpopular with many farmers because:

a) the stop-order system forces all loan recipients to market through the Grain Marketing board even where it is not the most convenient way.

b) confining credit to recommended input packages erroneously assumes homogeneity in the conditions, knowledge and experiences of farmers. Obviously such rigidity results in some farmers losing out. For example, some farmers have greater access to manure from their livestock and other organic materials. Through experience they have come to realise that their soils are more responsive to a certain mixture of organic manure and fertiliser. Such farmers may find that what they need is less of the fertiliser and more of herbicides and insecticides. On the other hand those farmers who do not have access to organic manure would be totally dependent on fertilisers for their soil fertility. Their fertiliser needs may turn out to be a lot higher than of the other group. Such diversity in requirements has not been taken into account in advancing credit to smallholders.

c) administration of the stop-order system delays payments to farmers. Sometimes it can take up to six months before farmers are paid for their produce. This creates serious cash-flow problems for many farmers.

d) when loan deductions are made by GMB after sales, they are not staggered even where deliveries are staggered. This means that the full loan may be deducted from the first payment, leaving the farmer with very little or nothing at all, at a time when they need their money the most.

37. In the current economic reform programme the stop-order system is becoming irrelevant. The AFC has responded to the new economic order and is in the process of phasing out this repayment system.

38. AFC's size of loans to smallholder farmers is another explanation for farmers' reluctance to borrow. In most cases, loans granted are considerably smaller than those requested and are too small to be productive. In 1990 the average loan granted to a

communal area borrower was valued at $761.76. This was enough to purchase inputs recommended for 2.6 hectares of maize in Natural Region III. Considering that the average size of land under cultivation per household in communal areas is estimated to be 5 hectares, this means that AFC loans account for less than 50% of input requirements. A study conducted in Zvimba (1986) found that AFC loans accounted for only 21% of total input costs for sample households. Most of these households felt that the loans were not adequate and they had to supplement them with own savings.

39. The cost of loans to the borrower has been a lot higher than is often assumed. Loan application procedures require that farmers meet the loan officers at designated points on days and times that suit the loans officers. For some farmers, this entails travelling long distances and spending whole days away from their homes and work. In cases where input deliveries are delayed, this may lead to late planting which results in reduced yields. This situation is now being addressed by AFC and the incidence has been reduced. The delay in processing payments is partly due to the fact that marketing boards have to collect loan repayments for AFC by deducting them from proceeds from marketed produce. Processing these stop-orders appears to be time consuming. Waiting for five months before receiving payment for produce delivered is quite costly. Assuming one would have deposited the money in a bank account, it would mean a loss of five months' interest. If one had alternative investment options with higher returns, the loss would even be greater. All these costs plus the interest rates paid by farmers make borrowing not viable for many. Although there does not seem to be any research done to quantify all these losses, it is a very useful exercise particularly at this point when there is concern about developing more efficient financial institutions that are responsive to the heterogeneous needs of the rural population.

40. Well known constraints - chronic cash shortages, poor performance of improved technology, severe manpower shortages at critical peak labour times - mean that a large proportion of the population in communal areas is not able to use commercial credit (as offered by institutions such as the AFC) efficiently. However, this does not mean that such cannot benefit from the provision of financial services. What it means is that the type of service that AFC has offered them has not been the most appropriate because it has not effectively addressed their needs.

41. Patrick (1966) identified two phenomena in financial development which he termed "Demand Following" and "Supply Leading". The "Demand Following" approach takes the view that lack of financial institutions in underdeveloped countries is simply an indication of the lack of demand for the services. According to this approach, the more rapid the growth rate of real national output the greater will be the demand by investors for financial intermediation. The "Supply Leading" approach takes the view that financial institutions are created and they supply their assets, liabilities and related financial services in advance of demand for them. "Supply Leading" thus facilitates transfers of resources from low productivity, to high productivity sectors, and promote and stimulate an entrepreneurial response in the high productivity sectors. "Supply Leading" is thus seen as representing an opportunity to induce growth by financial means.

42. This paper argues that there is no reason for making the strategies exclusive of each other. Due to the heterogenous nature of Zimbabwe's rural population, a mixture of both strategies might be found to be more responsive to the diverse needs. As demonstrated by the Zvimba study, there is heterogeneity in financial needs. Some farmers initiate their own savings mobilization schemes while others respond to the supply of credit. There are various other forms of financial intermediation that different groups opt for and at the same time, many people go for more than one option. Some even combine formal and informal forms of financial intermediation in order to balance savings mobilization and loan portfolios.

43. Patrick (1966) argued that in most cases there is likely to be an interaction of "Supply-Leading" and "Demand Following" phenomena. He suggested a sequence where the "Supply Leading" strategy is adopted first to induce investment and then as growth takes place, the impetus of "Supply Leading" gradually becomes less important and "Demand Following" response more dominant.

44. Although a similar strategy may be recommended for Zimbabwe, the importance of adapting it to the local situation should always be borne in mind. The strategy should be taken as a broad framework to be modified to accommodate local conditions. It is also important to take note of what is available, and then build upon it to ensure sustainability.

45. Until about three years ago, AFC loans to smallholder producers were not flexible enough to respond to the heterogenous needs of communal area farmers. With the exception of credit for labour payment, loans were given in kind and not in cash. They were limited to controlled crops which could be marketed through the Grain marketing board to allow for the implementation of the stop-order system of repayment. They were also restricted to the recommended crop packs. Until AFC introduced diversification in its lending operations the Small Farm Credit Scheme restricted borrowers to the above. It was only during the 1989/90 season that AFC for the first time granted loans for such crops as tobacco, coffee tea and sugar to smallholder producers. Credit facilities were further extended to cattle schemes such as fattening, breeding and stocking.

46. Delivery systems have not been efficient and flexible enough to accommodate the diverse group of recipients. Other than confining its lending to the production of a limited number of agricultural commodities, loan processing procedures have been lengthy, so that in some cases, deliveries have been made after the need of particular inputs has passed. For instance, seasonal loans, comprising seed and fertilizer, have been delivered after the planting seasons is over. Since the loans are made in kind, it then leaves it to the farmer to either sell or hold the inputs for the following year. Meanwhile, the farmer is still expected to pay interest on the loan which she/he cannot use productively. Some of the problems in loan processing are due to the poor quality of field workers who in many cases have been difficult to access because of their small numbers. Applications are often sent in late and are further held up at head office where final approval is given. The centralized nature of AFC's organization contributes towards inefficient delivery of financial services.

47. Well developed financial systems introduce borrowers' incentives in order to capture and retain good quality clientele. Where there is timely loan repayment, institutions increase the amount of credit available to a client in subsequent loans, and for prompt repayment, interest rate rebates are offered. AFC does not appear to have a clear cut policy on the former. Although past performance is taken into account in loan approval, it is not clearly stated that prompt repayment enables one to access larger amounts of credit in succeeding periods.

48. In general, effective demand for AFC loans among smallholder producers has been very low and has continued to decline because the institution has not structured itself for lending to smallholder producers. A lot of potential borrowers have viewed AFC lending as very high risk and this has to a large extent been linked to the repayment system and to the "once off" action of seizing assets following failure to repay. This action has given AFC the reputation of being an unfair and high risk lender. This has resulted in the reluctance to borrow by a lot of farmers, including those who have never borrowed, or plan to borrow from AFC. Despite the fact that demand has been low, AFC is still not able to meet all of the expressed demand. It is constrained by lack of resources in this credit scheme which does not generate returns but losses.

SOME MEASURES TAKEN TO OVERCOME PROBLEMS OF DECLINING DEMAND

49. In an effort to reach more farmers in communal and resettlement areas at lower transaction costs, the AFC launched the Group Lending Pilot Project in 1989/90. This is essentially an on-lending scheme whereby AFC lends to groups at a slightly lower interest rate and then the group lends to individuals at a rate paid by AFC's individual borrowers. During the first two years of the Pilot phase AFC was lending to the groups at 10% and the groups would lend to their members at 13%. Under this scheme, a large portion of the transactions costs are passed onto groups, which have to screen their borrowers and ensure loan recovery.

50. The Group Lending Scheme was not only addressing the problem of supply of credit to larger numbers of smallholder farmers but was also addressing the gender issue. Although it is generally accepted that women carry out over 60% of the agricultural work, financial institutions have been slow in accepting them as "farmers". When AFC's Small Farm Credit Scheme was established in 1979 it did not advance loans to married women. In 1983 a major development took place. For the first time the Corporation started giving credit to married women in their own right provided AFC was satisfied that they were farmers. Even after this proclamation, the proportion of women loan recipients remained insignificant. Very few were applying for loans. Some of the explanations given for the low demand for loans by women were that they did not hold grain marketing cards or that their husbands barred them from obtaining credit in their individual capacity. The Group Lending Scheme addressed these two problems. Since the loan was advanced to the group, individuals did not need to hold marketing cards which, in majority of households, were held by male heads.

On the latter, most husbands did not seem to mind their wives borrowing through groups. This increased the number of women loan recipients significantly. At any one time of the pilot scheme women made up more than 50% of the group borrowers.

51. The initial response to the pilot phase of the Group Lending Project was positive because it introduced some element of flexibility in lending. The sizes of loans were relatively larger and lending activities became more diversified. Some loans even included a consumption element. In addition the stop-order system was no longer the single method of repayment since some of the enterprises financed by loans were not for controlled products nor linked to the central marketing system. Borrowers could make their repayments in cash by instalment over an agreed period. This method improved the cash flow situation for many borrowers.

52. The Group Lending Scheme has made use of existing informal groups to channel credit. A study carried out in Mashonaland East found that the use of existing and fuctional multipurpose groups as on-lending channels produced better results than initiating new ones specific to group lending. The latter performed poorly with high default rates. (Chimedza, 1992). AFC has recognized some benefits in linking up formal and informal finance. Informal finance possesses certain features which are more effective in dealing with people at the individual level, while formal finance may find it too costly to do so because of the sizes of the transactions involved. The point to be noted is the importance of recognizing the different capacities the various parties have, and taking advantage of them.

53. AFC has recognized these capacities and has taken advantage of them through the Group Lending Scheme. It has gone further and linked up with NGOs working in the area of finance, through its Linkage Programme. This Programme which has been newly introduced to ensure sustainability of lending activities, links the AFC with NGOs through the establishment of a credit guarantee scheme, to guarantee loan recipients from its affiliate groups. The initiative has reduced the risk borne by AFC. Other than spreading the risk, the scheme has established a link between AFC and informal financial institutions. It has taken a step towards linking savings mobilisation with credit.

54. It is too soon to assess the impact of the Linkage Programme on efforts to improve financial services to smallholder producers. It is also still premature to proclaim its success. One can however, note some of the positive points. One of the difficulties in the provision of financial services to the rural poor is to design a scheme that can be sustained. The interaction of the linkage programme and the Group Lending Scheme begins to address that. The Group Lending scheme gives individuals greater responsibility over their financial actions. Through peer pressure, the individual is forced to identify financial needs which they believe they have the potential to make use of in a productive manner, so that they are able to service their loans.

55. The linkage programme on the other hand links informal savings mobilisation schemes with a formal institution that directly benefits them by making loans for investment

available to them. As AFC moves towards becoming a Bank, this linkage becomes more meaningful because savings clubs involved in the scheme are likely to choose to place their deposits with AFC which invests in rural areas. This is different from depositing with Building Societies and Commercial Banks whose reinvestment is almost all in urban areas or in the commercial agricultural sector.

OTHER EXISTING SOURCES OF RURAL FINANCE

56. A number of commercial banks have recently established sections that advance loans to the rural sector for a variety of investments. For example, ZIMBANK's Small Business Services Division has a co-operatives section that deals with loan applications from co-operatives, groups (clubs) and associations. These loans are not specifically for agriculture but for working capital or acquisition of tools mainly for rural or village industries. In addition to giving loans, the Small Business Services Division also provides guidance, advice and supervision on the spot to its clients. It is believed that these services are essential for the survival of the enterprises.

57. The Small Enterprise Development Corporation (SEDCO) is an institution which provides finance to support development of small industrial and commercial ventures with a particular emphasis on those in rural areas. It does not fund agricultural and mining ventures. To promote development, it lends to rural projects at concessional interest rates, about 2% below its going rate.

58. There is a potential role for Venture Capital in rural areas. In Venture Capital Financing, the financial institution injects seed capital into a new company or existing one by purchasing a minority shareholding. This is called "equity financing". It means that the new entrepreneur has the capital base needed to purchase equipment, pay for raw materials and meet overheads without the burden of interest and loan repayment. Once the company is well-established, Venture Capital Companies earn a return on their investment by selling their shareholdings to the owner or other interested parties. This is a high risk financial innovation which will only give returns to the source of finance if the enterprise is successful. This means that Venture Capital Companies have to be highly selective to avoid excessive losses. Venture Capital is relatively new in Zimbabwe and to date it has funded a diversity of enterprises including Horticultural projects. Venture Capital Companies normally shun away from purely agricultural production projects, but they help establish agro-based industries. This is an area in which there is a greater deal of potential for rural areas.

59. The Credit Guarantee Company is also promoting investment in rural areas. By helping entrepreneurs who would not normally qualify for loans from commercial banks because of lack of collateral, the company facilitates investment in rural enterprises as well as urban ones. Such facilities could be expanded to further benefit emerging entrepreneurs in rural areas.

60. The above initiatives are very critical in the growth of the rural economy. For a long time the provision of credit facilities in smallholder sector has focused on agricultural production loans with very little, if any, going to agricultural support industries. The whole aim has been to increase agricultural productivity. Manufacturing and repairing of simple farm implements have not been viewed as part of the rural industry which indirectly contribute to agricultural productivity. Development of such industries has thus. not been seen as an integral part of the rural development process. This has therefore resulted in a very narrow perception of investment, in the context of rural development. The narrow view of investment has impeded financial development in rural areas. Demand for agricultural loans is closely tied in with available technologies. Farmers borrow to acquire improved technologies. As new technologies are introduced, demand for loans increases. Since the largest proportion of loan funds goes to seasonal inputs, which are basically biological technologies, the rate at which they are generated has a positive relationship with the demand for financial services. Unfortunately. biological technologies take time before they are developed, tested, marketed and then accepted by farmers after observing their success. Such a process means slow development in financial services, if their growth is a response to demand for them.

61. If the perception of investment for rural development were broad enough to include support industries, there would always be a demand for investment capital for a wider range of enterprises. This would facilitate the creation of integral financial institutions that, according to Desai and Mellor, (1993)

> ".....are necessary and desirable to accomplish financial intermediation between surplus and deficit units, seasons, years, regions and economic sub-systems for agriculture"

The "Demand - Following" phenomenon in financial development would mean creation of more financial institutions in response to the demand for services.

CAN COMMERCIAL BANKS PLAY A ROLE?

62. Commercial banks have a role to play in this situation. In the group of smallholder producers, there are farmers who are able to use credit productively. It has been argued that credit can play an important role in development, but only if savings exist so that they can be mobilised and loaned to producers (Miller, 1977). Commercial banks provide the link between savers and borrowers. However, in many cases, e.g. Zimbabwe, there is a tendency for commercial banks to divert rural savings away from agriculture to other sectors of the economy. It is thus, desirable for policies that direct banks to reduce drain of rural savings to be put into place.

63. Stiglitz (1993) has argued that integrated financial markets emerge as a result of

deliberate policy. Development of some of the most successful financial sectors, such as Japan, USA, Korea and Taiwan has been through public sector support. Government intervention in the operations of commercial banks is often necessary for the banks to be more responsive to the needs and circumstances of smallholder producers. In Indonesia for instance, the government owned Commercial Bank Rakyat Indonesia has been able to reach out to farmers in poor areas and has been successful in the sense that revenues have exceeded expenditure and the programmes have been self - sustaining. The bank was decentralized to be in physical reach of a large proportion of the rural population by establishing units similar to sub-branches and agencies located in simple offices where clients could deposit savings, apply for loans and make loan repayments. Loans were made for both working and investment capital.

64. Replicating such an initiative in Zimbabwe is more likely to yield positive results. This should however, be modified to suit local conditions. Since commercial banks have been reluctant to move into rural areas as true banks, the government of Zimbabwe could use AFC to introduce such financial innovations. It is important to note that even though most parastatals are being encouraged to privatise, there are some that will need to continue to operate as development agents. In the financial sector the AFC is the institution which should commercialise but still continue to play its development role. It should take the lead in rural financial development particularly in bringing commercial finance to the smallholder agricultural sector where the potential for using commercial financial services is still unexploited.

65 For AFC to spearhead the above initiative it will need to be decentralised to rural areas through sub-branches and agencies. In cases where office space is not easily available and where it may not be that viable to maintain an office, mobile banking units could present a viable alternative. The main idea would be for the bank to be physically accessible by the majority of the population. Such a move by AFC can only be taken with a great deal of push and support from government because in the short and perhaps medium - term, returns are often negative. The initiative can be quite costly. Subsidies will be necessary between the different categories of clients until such a point when the institution will have better established its clientele for the various types of financial services i.e. for genuine borrowers who are able to utilise loans productively and those with surplus funds they wish to deposit. Even after this point AFC will have to continue playing its development role in support of the smallholder agricultural sector. However, it is also expected that in the long-term, those genuine borrowers who will have used loans to invest and pushed their production functions upward will expand their use of financial services and generate higher returns for the financial institution.

66. Decentralization of banks should not only be interpreted as establishing units in outlying locations in rural areas. It should also be understood to mean decentralization of decision making processes particularly in the approval and disbursement of loans. It is widely accepted that rapidity, flexibility and ease of transactions are key to the effectiveness of financial markets serving the rural low income population. As long as decision making

in the bank is highly centralized, the above elements cannot be found in the system, and even if borrowing interest rates are low, demand for loans will be negatively affected.

67. Subsidized credit schemes have not had much success in many developing countries particularly because they allocate resources to people who do not make optimal use of them and are thus, not able to sustain themselves. It is not the intention here to suggest low interest rates for the rural people because it is not the belief that every poor farmer needs credit in order to invest in productive agricultural technologies which allow them to shift their production functions upward. The idea is to facilitate access to loans by those farmers who can use credit productively. It is important to bear in mind that credit never stimulates innovation and greater output if farmers are unwilling to adopt better methods or have poor incentives to do so. Furthermore, credit is unlikely to be used productively unless it is combined with other services and prerequisites. The impact of credit depends on technology, markets, infra-structure, information and attitudes. Charging low interest rates is therefore, not sufficient to make credit productive. Correct market rates are in fact useful rationing mechanism which facilitate more efficient allocation of financial resources for investment.

68. Absence of banks in rural Zimbabwe has limited resources available for investment by farmers who can use credit productively. One of the factors limiting commercial bank lending in rural areas, other than lack of collateral, is that they do not effectively mobilise savings to allocate to loans. In fact, most of the savings mobilisation is done for them by informal groups or farmers who are forced to use banks because payment for their marketed produce is done by checks which they can only cash at banks. There appears to be very little other incentive for rural people to use banks.

69. Subsidized credit has been found to reduce the incentive to mobilise rural savings and prolong the dependence on foreign aid for financing credit projects. The net effect has been to benefit larger or better off farmers who normally use up the greater proportion of available credit facilities (Eicher,and Doyle, 1982). Chimedza (1993) found that in Zvimba Communal area, AFC loan recipients tended not to get involved in savings mobilisation initiatives. Savings club membership was made up of people who did not use credit either out of choice or because they could not qualify. The study did not examine in detail because this was beyond its scope. (This will be an area that is worth pursuing for future research). However, the logical conclusion was that since AFC loan recipients had access to cheap money, they did not have any incentive to mobilise additional surpluses.

70. The inability of commercial banks to effectively mobilise savings in rural areas cannot only be attributed to the common belief that rural households do not have any propensity to save. As indicated earlier, a number of studies have shown that rural households have a lower saving thresholds than urban ones. It is becoming increasingly clear that a large portion of the problem lies with financial institutions themselves. There are hardly any commercial banks launching aggressive campaigns to mobilise rural savings. Most bank employees servicing the rural sector have not received any special training or exposure to

effectively deal with the rural population. There are hardly any special advertisements of available financial services and their benefits, that are designed for rural areas where televisions and newspapers are not easily accessible. Rural financial institutions do not treat their services as products to be marketed mainly because they do not have a full appreciation of the business potential. They do not possess adequate knowledge of their market and thus not able to service it effectively. This paper argues for appropriate human capital development in order to realise the desired financial institutional set up.

HAS CREDIT FROM AFC MADE THE DESIRED IMPACT?

71. To date, there have been very few studies that have attempted to alienate the impact of credit on levels of productivity. This is a very difficult exercise. In fact, it is almost impossible, because productivity levels are a function of a combination of factors. In most cases the assumptions on the response to input use have been wrong. The reponse has often been overrated and does not reflect the variability in either farming circumstances or farmer's management abilities. There have however, been attempts to carry out a comparative analysis of productivity levels between borrowers and non-borrowers. A study carried out in Zvimba Communal area, under similar farming conditions found that output levels of borrowers and non borrowers were not significantly different (Chimedza, 1993). In fact, the study found that AFC loan recipients registered lower earnings from maize output than members of savings clubs. (Table VI) During the same period, expenditure on agricultural inputs was not significantly different for borrowers and non-borrowers. In general, the group of AFC loan recipients although having been selected from the relatively better-off farmers, were not performing any better than those who did not enjoy access to credit. This was also true for the rate of investment in productive assets, mainly farm implements. Their rate of saving (cash deposits) was not significantly different from that of non-borrowers.

72. Results from this study were cause for concern, particularly when at the policy making level, the assumption has been that availability of credit leads to increased productivity. The link between availability of credit and productivity levels has been assumed but not tested. The absence of this link in a situation such as Zvimba raises a number of questions, both on the demand and supply side of credit. On the demand size, and important question is whether the loan recipients in Zvimba had reached a level where they had the capacity to utilise credit productively. Credit can only be productive when a farmer has reached a certain level in acceptance, adoption and understanding of the improved technologies. Furthermore, a farmer should have reached a level of wanting to commercialise because without wanting to make a profit one cannot guarantee repayment and sustainability. On the supply side the question is whether the product was right. Did the institution provide the required types of loans and were the delivery systems appropriate?

73. A large proportion of the population in communal areas has not reached a level of utilising credit efficiently, particularly the AFC type credit. However, this does not mean

that this category of farmers cannot benefit from the provision of financial services. What it means is that the type of service that AFC has offered them has not been the most appropriate because it has not effectively addressed their needs. Results from the comparative analysis of the behaviour of borrowers and non-borrowers suggest that maybe a different type of financial service might work better for the various groups of farmers.

HOW AFC CAN BE MORE RESPONSIVE TO SMALLHOLDER BORROWERS

74. It is generally accepted that fragmentation of financial markets in most developing countries, which resulted in a bias in favour of credit advancement with little focus on savings mobilisation, has created inefficiencies in the delivery of financial services. The argument being that the design of the institutions is such that they would be able to offer both loan granting and savings mobilisation services using the same infrastructure. Focusing on one area of financial services only means that there is underutilisation of resources in a situation of scarcity. The AFC falls in this category of financial institutions. As the only formal lending institution advancing loans to smallholder producers, there is no good reason why it has not been involved in the mobilisation of deposits. Yet it would reduce transaction costs for both the institutions and borrowers if the two functions were carried out under one roof. For example, when a client already operates a deposit account, the manager of the institution gets to know her and when she applies for a loan the manager already has most of the information she needs about the client. The fact that the manager does not have to look for information about a client reduces the amount of work involved in loan approval. Furthermore, if an institution is involved in both savings mobilisation and provision of credit, it cuts on transaction costs by reallocating the savings that it has already mobilised to credit. It does not go out to borrow all its loan funds as is the current situation with AFC.

75. AFC's recent proposal to operate as a commercial bank is an attempt to improve efficiencies and become more profitable. However, for this to be effective, AFC needs to undergo some structural changes. One of the major criticisms levelled at formal financial institutions in their dealings with small borrowers is lack of flexibility. Small farmers have heterogeneous needs. Their financial needs are often urgent and therefore need speedy responses. In most cases small farmers have relatively low levels of education and therefore require loan procedures that are simple to follow. All these are features that would be essential to have in a financial institution that serves the needs of people. Absence of these features from most formal institutions has created barriers for borrowers. For example, in the case of AFC, loan approvals may take up to four months. Some needs, particularly consumption needs, cannot wait for four months. Completion of application forms has been a barrier for those who have had no formal education. Some application forms are very long and use language that borrowers may not be familiar with. There is need to simplify application procedures. One of the ways to get around the problems of delays in loan approval and complications in application procedures would be to decentralize the institutions so that some of these facilities are as locality specific as is possible.

76. Because flexibility, rapidity and ease of transactions are essential elements in the provision of loans to smallholders, decentralization of financial institutions, which allows for the development of intimate knowledge between the client and the institutions, can allow for special arrangements to be made. For example, a facility similar to an overdraft can be made to some special clients. The decision to extend such a facility would be based on the institution's relationship with the client over time. Such facilities can make it possible for clients to take greater risks and have a more diversified portfolio of investments.

77. In order to play its new role effectively, AFC would need to retrain its employees and give them more exposure to rural banking. They could benefit from experiences of such institutions as the Grameen Bank of Bangladesh and the Commercial Bank Rakyat Indonesia. While most of AFC's employees have had some experience with loan advancement, very few have had exposure to savings mobilisation. Different approaches may be required and the challenges will be different. It may be that on the one hand there is need for closer links with informal groups while a direct approach to individuals may work for the other. Making active use of such agencies as church groups, grassroots NGOs and extension agencies with a wealth of local knowledge and experience can facilitate efficient lending. It would benefit AFC to establish a formal and effective liason with such groups. All this needs to be explored and staff will be required to gear themselves towards adapting and being relevant. The processes of developing this relevant human resource are manifold. Short-term training, interaction with other formal and informal institutions and study visits are some of the options. These processes entail costs which the new AFC should be prepared to bear in its efforts to be both more responsive and profitable.

78. The need for management skills in the process of transforming the AFC cannot be overemphasised. A lot of the credit schemes and development banks have collapsed mainly because of poor management. In some cases institutional overheads have tended to absorb more funds than the actual lending activities. Since overheads do not directly yield returns, this has resulted in negative rates of return to institutions which are only able to continue operating because of donor support. In the case of AFC, it will have to reorient its staff towards viable lending. Currently AFC has been guided by rigid lending criteria and by a narrow focus on agricultural production loans. In many cases the viability of the enterprise has not been closely scrutinised. In the last couple of years AFC has made efforts to move towards viable lending. More needs to be done in this area. The new institution, which will have a more diversified loan portfolio will need to develop a more competent team of loans officers who should manage loans more efficiently and cut down on costs to the institution. Sound selection of loan recipients, which is dependent on availability of information about the clients results in higher repayment rates strengthening the financial management.

79. The move towards operating as a commercial bank is, among other things an acknowledgement by AFC that smallholder producers' financial needs are not confined to borrowing but also depositing. It is an acceptance that there are some rural households with financial surpluses but no investment options and others with deficits for their viable investment opportunities. However, although desirable, it does not follow that the investor

must be the source of savings. The key role of the AFC as a bank would be to intermediate between these two groups of households and ensure that each one is able to access the service it requires. The ultimate objective for all involved should be to generate growth in the economy. For this growth to occur, capital formation is crucial. Capital is not formed until savings are transformed into productive goods. Savings must therefore precede capital formation.

80. Rural areas have had low investment rates partly because of lack of financial development but also because of lack of investment opportunities. Focusing efforts on developing rural financial systems alone without creating investment opportunities will not necessarily result in economic growth. There is need to link the relevant institutions so that an appropriate investment environment is created. In rural Zimbabwe agriculture is the main economic activity and most investment is directed towards this sector. It is imperative for financial development to link up with sources of agricultural growth. Agricultural research and extension are very crucial because they produce and communicate the new technologies that increase productivity. The link between finance, research and extension needs to be strengthened to allow capital formation in the agricultural sector.

81. For AFC to be effective and more responsive, it has to fully appreciate the importance of mobilising savings and at the same time recognise the fact that smallholder producers have a greater than zero propensity to save. A study by Mauri (1984) which showed that rural people have a lower saving threshold than urban people came to the conclusion that the saving threshold in rural areas was lower partly because of the absence of many consumer goods. In his study of rural households in Sri Lanka , Bouman (1984) concluded that thrift came naturally for households with irregular income flows. He found the majority of his sample households saving about 26% of their income. Chimedza's (1993) study of households in one rural are in Zimbabwe concurred with Bouman's findings. It estimated that households saved about 32% of their income during a particularly good season.

82. Although for a long time the assumption was that rural households had a zero marginal propensity to save, there is now a wealth of evidence to the contrary. The fact that the potential for mobilising all the surpluses in rural areas is there does not mean that establishing a bank and locating it in rural areas will do the job. The bank will have to reach out to people and provide incentives for them to deposit all their surpluses which would otherwise be hoarded. Other than providing attractive rates of returns which relate to the inflation rates positively, banks will need to be as easily accessible both physically and non-physically. This implies decentralisation and use of mobile units which is necessitated by sparse settlement patterns that are a feature of many parts of rural Zimbabwe. Application procedures need to be simplified. Clients should be able to access bank officials (including managers) for any queries they may have. In general, there should be no barriers keeping clients from obtaining vital information directly from responsible sources.

83. An important incentive would be giving preferential treatment to savers in loan applications. This means that there should be a direct relationship between a client's

deposits and loan portfolio. This encourages potential borrowers to mobilise savings.

CONCLUSION AND RECOMMENDATIONS

84. Zimbabwe's rural financial sector clearly needs to be restructured in order to be more responsive to the needs and conditions of smallholder producers. This paper argues that the new AFC should take the lead in this process.It contends that government has a central role to play in giving direction to financial development. As an arm of government, which is in the process of being transformed to be in line with the new economic order, AFC is the right entry point for a new strategy in the rural financial sector. While it is pushing commercial finance to the smallholder sector, it should also continue with its development role in order to meet the heterogeneous needs of the rural population.

85. A number of problem areas which need to be addressed have been noted. The fragmentation of financial services, which has resulted in institutions not being able to take advantage of scale and scope economies has been responsible for some of the higher than necessary transaction costs. The suggestion here is to integrate financial services and make use of the infrastructure to provide support services that enable financial institutions to sustain themselves. A proposal such as is made by Desai and Mellor, (1993) for a multifunction rural financial system may be worth looking into. Multifunction institutions directly and indirectly undertake operation of farm level loans, extension, input sales, produce marketing, consumer goods sales, collection of deposits or share capital, borrowing and loan recovery. Such an institution would be ideal for many areas where both physical and socio-economic infra-structure are not well developed. At the moment there are some institutions offering some of these services e.g. marketing co-operatives. They however need strengthening for more efficiency and broader coverage in terms of people and areas of operation. Designing appropriate multifunction institutions is an area that is worth investing in because it allows for scale and scope economies.

86. Mobilisation of rural savings has not been given its due attention by many formal financial institutions . AFC will need to put more effort into developing incentives for potential savers. In the process of integrating financial services, it is important to also integrate the client i.e. potential borrowers should be motivated to save so that the borrower and the saver are one and the same. In pursuing this objective, it is worth investigating into why borrowers tend to have a lower marginal propensity to save than non-borrowers. Seeking answers to such questions will help in designing institutions that can mobilise and allocate financial resources more efficiently.

87. It has been accepted that smallholders are riskier borrowers. Lack of collateral has been found to be one of their major impediments to borrowing. With respect to collateral, there has been a tendency for formal lending institutions to treat borrowers as a homogenous group, and therefore seek the same forms of collateral. This is one area which requires rigorous studies which can come with recommendations for different forms of

collateral that will be more suited to the heterogenous group of smallholder borrowers. Not enough attention has been paid to possible existing options and it is strongly recommended that work in this area should be supported. Such studies need to focus most of their energies on the demand side of credit.

88. The development of rural financial systems should be closely accompanied by technology innovations and a conducive investment environment. These elements need to come as a package for productivity to occur. This calls for closer links between financial development, technical research, extension and other delivery and receiving systems. The macro-economic policy environment should be supportive of the initiatives. Government has an important role to play. It has to intervene and stir things in the right direction through policy instruments and other forms of support. Government's role is also critical in supporting technology development and transfer. Without the generation of technology, financial development becomes meaningless, because there is no productive capital that can make economic growth possible through expanded productivity. It is thus recommended that stronger links be established between agricultural research, extension and financial development.

FUTURE RESEARCH AREAS

89. This study has demonstrated a need for a new approach and different strategies for rural financial development. It has highlighted the need to for the design of new financial institutions that are more responsive to rural people's needs and conditions. Relevant future research should thus focus on designing these new financial institutions. Research is required to investigate both the demand and supply sides of finance to contribute to the proposed initiative. It is particularly important to understand the demand side so that the institution designed suits the conditions of rural people. In this regard, it is imperative to establish the productivity of inputs and relate that to the cost of borrowing including the risk involved. The assumption has been that returns on inputs are high enough to cover the cost of borrowing and leave some profit for the borrower. With interest rates of up to 35%, this assumption needs to be tested so that appropriate recommendations can be made.

90. The need to link savers and borrowers through financial intermediation has been highlighted. The paper has stressed the importance of savings mobilisation preceding lending. One of the important recommendations made in the study is that institutions providing deposit services and loans, should, as an incentive for savings mobilisation, relate one's loan portfolio to their savings deposits. This means that there should be a positive correlation between the sizes of savings and loans.

91. This paper has also noted studies that have shown that borrowers tend to save less than non-borrowers. Reasons for this low saving rate by borrowers have not been explored rigorously in the Zimbabwean situation. This a very important research area because of the central role of savings in financial development. This study proposes a rigorous analysis of

saving behaviour of borrowers. It is anticipated that such a study will contribute towards the design of appropriate saving incentives.

92. The importance of strengthening linkages between complimentary institutions that contribute to capital formation in the agricultural sector was noted. It was also observed that there is currently not much interaction between these institutions that are key players in the rural development process. This area of strengthening institutional linkages requires investigation which will come up with policy recommendations.

93 The proposed research areas should all contribute towards the design of financial institutions that will make a difference to Zimbabwe's agricultural sector.

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Table I Savings Club Membership Between 1970 and 1991

Year	No. of clubs (approximate)	Membership (approximate)
1970	30	200
1971	202	7.000
1972	501	20.000
1973	200	4.000
1974	1.500	30.000
1975	3.000	60.000
1983	5.000	125.000
1984	5.500	140.000
1986	6.500	162.000
1988	7.800	195.000
1989	9.800	250.000
1990	10.500	280.000
1991	12.000	315.000

Some clubs have registered as co-operatives mainly because they needed bank loans

Table II Informal groups involved in Financial Intermediation in Rural Areas in Zimbabwe in 1985

Types of groups	Primary purpose	No. of groups	Members	% of rural households
Savings Development Movement	Savings mobilisation	6.000	150.000	18.8
Silveira House	Credit	567	59.535	7.4
Windmill	Inputs for cash/credit	2.000	60.000	7.5
Agricura	Inputs for cash/credit	n/a	n/a	n/a

Source: IFAD, General Identification Mission in Zimbabwe : May 1985

Table III: AFC Number and Value of Loans granted by Sector From 1981/82 to 1993.94

Year ended March	Large Scale Commercial		Small Scale Commercial		Resettlement		Communal		Coops and Coop Unions		Grand Total	
	Number granted	Value ($m)	Number granted	Value ($m)	Number granted	Value ($m)	Number granted	Value ($m)	Number granted	Value ($m)	Number granted	Value ($m)
1982	2103	88.80	3649	4.60	911	0.50	30150	10.10			36813	104.00
1983	1645	88.70	2953	4.50	4154	1.50	38912	13.20			47664	107.90
1984	1400	110.20	3052	8.10	19874	10.60	50036	23.40			74362	152.30
1985	1484	110.30	2744	8.70	19926	10.70	65793	32.00			89947	161.70
1986	1308	113.00	2569	11.50	13866	8.50	77526	38.90			95269	171.90
1987	1007	94.90	1910	9.60	11800	8.60	77384	60.00			92101	173.10
1988	990	111.20	1542	6.80	11217	9.00	69885	49.40			83634	176.40
1989	900	117.40	140	5.30	7022	5090	57679	41.30			66741	169.90
1990	969	136.30	844	4.50	5193	5.90	43846	33.40			50852	180.10
1991	1133	195.10	761	3.60	4658	4.70	30190	26.40			36742	229.80
1992	1499	358.24	727	6.78	6307	10.52	27344	29.73			25877	405.27
1993	1340	248.59	376	7.59	4624	13.73	15973	34.04			22319	305.13
*1994	550	237.92	172	5.29	1931	9.83	8024	26.65			10680	280.43

* Figures are from April to 30 September, 1993.

Table IV Distribution of short-term credit to Agriculture 1980-85 (in percentages)

Year End	AFC %	Commercial Banks %	Co-ops Companies %	Total	
				%	Z$000
1980	38	34	28	100	164.075
1981	34	30	36	100	179.871
1982	37	35	28	100	228.711
1983	41	32	27	100	304.236
1984	43	32	25	100	333.161
1985 (March 31st)	42	35	23	100	412.567

Source: Taken from Anthony Slange, 1989 (ed) Mario Masini for the FAO-FINAFRICA Working Group "Rural Finance Profiles in African Countries, Volume 2.

Table V Distribution of Financial Institutions - 1992

NAME	Total No. of outlets in the country	No. of rural outlets	% of total (rural institute)
CABS	72	11	15
Founders Building Society	29	1	3
Barclays Bank	52	14	30
Standard Chartered	69	14	20
Zimbank	71	28	39
Beverly	14	5	36
Bank of Credit and Commerce	46	8	17
POSB	195	128	66
Total	548	209	38

Source: Data was obtained by author from interviews with Manager in the institutions

Table VI: Income From Crop Sales by Group/Year

	AFC	LWF	SC	NP	Total Sample
1985					
Maize	809.85 (34)	1193.82 (14)	603.70 (28)	641.95 (21)	812.33 (97)
Groundnuts	195.45 (5)	227.33 (7)	101.40 (21)	145.00 (11)	167.30 (44)
Millet	70.00 (4)	0.0	21.00 (5)	144.0 (2)	78.00 (11)
Cotton	817.4 (4)	467.75 (6)	0.0	0.0	642.58 (10)
Total	890 (36)	1162.1 (21)	590.06 (32)	548.05 (28)	797.6 (117)
1986					
Maize	690.00 (34)	1155.96 (16)	743.57 (30)	712,23 (25)	825.44 (105)
Groundnuts	270.25 (18)	0.0 (0)	128.67 (20)	260.00 (10)	220.64 (28)
Millet	105.50 (9)	0.0 (0)	280.50 (7)	24.00 (3)	136.70 (12)
Cotton	545.75 (9)	321.17 (7)	0.0	250.00 (2)	372.31 (18)
Total	954.00	1170.00	839.00	750.00	865.00
1987					
Maize	181.55 (16)	325.20 (18)	232.00 (31)	401.06 (24)	285.00 (41)
Groundnuts	50.00 (4)	0.0	16.67 (25)	0.0	33.36 (41)
Millet	40.00 (4)	44.85 (4)	0.0	0.0	42.43 (8)
Cotton	285.00 (10)	284.91 (10)	0.0	0.0	284.95 (20)
Total	257.00	493.00	238.00	344.00	314.00

APPENDIX 2
A.F.C. NUMBER AND VALUE OF LOANS GRANTED BY SECTOR 1981/82 TO 1994/95

YEAR ENDED MARCH	LARGE SCALE COMMERCIAL		SMALL SCALE COMMERCIAL		RESETTLEMENT		COMMUNAL		COOP & COOP UNIONS		GRAND TOTALS	
	Number Granted	Value ($m)	Number Granted	Value ($m)	Number Granted	Value ($m)	Number Granted	Value ($m)	Number Granted	Value ($m)	Number Granted	Valu ($m
1982	2 103	88.80	3 649	4.60	911	0.50	30 150	10.10	-	-	36 813	104.0
1983	1 645	88.70	2 953	4.50	4 154	1.50	38 912	13.20	-	-	47 664	107.9
1984	1 400	110.20	3 052	8.10	19 874	10.60	50 036	23.40	-	-	74 362	152.3
1985	1 484	110.30	2 744	8.70	19 926	10.70	65 793	32.00	-	-	89 947	161.7
1986	1 308	113.00	2 569	11.50	13 866	8.50	77 526	38.90	-	-	95 269	171.9
1987	1 007	94.90	1 910	9.60	11 800	8.60	77 384	60.00	-	-	92 101	173.1
1988	990	111.20	1 542	6.80	11 217	9.00	69 885	49.40	-	-	83 634	176.4
1989	900	117.40	1 140	5.30	7 022	5.90	57 679	41.30	-	-	66 741	169.9
1990	969	136.30	844	4.50	5 193	5.90	43 846	33.40	-	-	50 852	180.1
1991	1 133	195.10	761	3.60	4 658	4.70	30 190	26.40	-	-	36 742	229.8
1992	1 499	358.24	727	6.78	6 307	10.52	27 344	29.73	-	-	35 877	405.27
1993	1 340	248.59	376	7.59	4 624	13.73	15 973	34.04	6	1.17	22 319	305.13
1994	808	308.63	379	9.65	3 706	18.39	13 755	54.95	4	0.80	18 652	392.42
1995*	665	311.28	216	12.02	2 036	14.10	5 463	43.37	2	0.79	8 382	381.56

* Figures as at September 1994.