COURSE GUIDE

CRD 303
RURAL FINANCE

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Published by:
National Open University of Nigeria

ISBN:

Printed: 2017

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INTRODUCTION

CRD 303 is an undergraduate course meant to equip students with knowledge of financial practices and options available for rural dwellers. This course guide will help students to understand financial characteristics of rural dwellers as well as their needs and financial mechanism available for them. The course consists of 22 units categorized into 4 modules. This course guide tell you what the expectations of the students should be, knowledge required to manage financial services for rural dwellers as well as requisite skills needed to design and implement financial services. It suggests guideline about how to get the best out of the course.

This course is also an introduction to rural finance, meant for beginners. It runs through definition of terminologies in rural finance, savings mobilization mechanisms to cooperative financial practices. Topics covered include Cooperative rural finances, Rural finances approaches and paradigm, Savings mobilization in rural areas, Rural financial system, Cooperative banking and financing, techniques for investment appraisal and different rural financial institutions both in Nigeria and abroad such as microfinance banks, credit cooperatives and rural development programmes in Nigeria.

COURSE AIMS

This course is meant to provide indepth understanding of financial practices and systems especially in the areas of:

- Familiarize basic terminologies in cooperative rural financing
- Expose approaches and paradigms to rural financing
- Stimulate savings mobilization mechanism in the rural area
- Explain rural financial system
- Discuss rural financial institutions
- Define cooperative financing system and cooperative banking

COURSE OBJECTIVES

The overall objective of this course could be achieved when the unit objective stated at each unit is achieved. They serve as study guide to enable students know if she or he understand each unit. At the end of the course period, the students are expected to be able to:

- define the concepts of cooperative and rural financing and other terminologies
- understand the overview, benefits, paradigm and approaches to rural finance

- explain Nigerian rural finance system, savings mechanism and objectives of rural finance
- distinguish different investment appraisal techniques and time value of money
- understand cooperative banking, structure and problems of loan repayment
- explain rural financial institutions and rural development programmes in Nigeria.

WHAT YOU WILL LEARN IN THIS COURSE

The course CRD 303 consists of 22 units specifically; the course is an introduction to rural finance studies. Before graduation you are likely to specialise in areas like financial savings, promoting rural finance, financing of cooperatives, cooperative management, micro finance banking, nature of Nigerian rural financial system and problems of loan repayment in cooperative banks.

The course gives you a general background of who a rural finance is and looks at your own characteristics to see if you have what it takes to be an entrepreneur. You will also learn about some business concepts and other objectives of an entrepreneur and business environment.

WORKING THROUGH THIS COURSE

For you to complete this course successfully, you are required to read the study units, reference books and other resources that are related to the unit. Each unit of the course contains Tutor-Marked Assignments, practical activities and self-assessments.

COURSE MATERIALS

Major component of the course are:

1. Course Guide.
2. Study Units.
3. Assignment File.
4. Presentation Schedule.

The time to submit the TMA will be specified. This course is a two-credit course. This means that you are to spend a minimum of two hours every week studying the course. You are expected to complete the entire course outline within a period of 18 – 25 weeks.

STUDY UNITS

In this course, we have discussed the topic of the course content titled Principles and practice of co-operation under different topics. Based on this, the following units have been designed for the course.

MODULE 1

MODULE 2

MODULE 3

MODULE 4

The units follow sequentially and as such must be studied in that order. A maximum period of one week is required for every unit.

TEXT BOOKS AND REFERENCES

The materials and books relevant to this course are listed below. However, you can use other ones that are not listed here.

Baumback, C.M. (1992). *Basic Small Business Management.* London: Prentice Hall.

Central Bank of Nigeria (1993) "Small and medium Scale Enterprise Development in Nigeria". *Annual Report and Statement of Accounts.*Lagos Central bank of Nigeria. Vol. 30 (4) P.246.

Green, G. C. (1975), *-How to Start and Manage your Own Business.* New York: McGraw Hill.

Ikpe, K.I. (1989). "Financing Small Business in Nigeria under the Structural Adjustment Program". *The Executive:*An International Business and Economic annual Journal, Vol. 2, April, pp 13-19.

INSTRAW (1991), *Analysis of Women's Participation in the informal Sector.* (Report of the Consultative Meeting of Experts on Macroeconomic Policy), Rome: United Nations PP 6-10.

Ho, M.S. and Urata (1994). Small and Medium Size Entreprises Support Policy in Japan Washington D.C.: World Bank policy Research Department.

Ijere, M.a. (1992). *Prospects of Nigerian Cooperatives.* Nigeria: A Johnson Publishers Ltd.

Nweze, N.J. (1997). *Essentials of Cooperative Economic* Nigeria: A Johnson publishers Ltd.

Okonkwo, J.N. (2001). Introduction to Cooperatives Nigeria: Dulacs Press Ltd.

Iwuafor, E.N. (1986). "Business organization, in Ezeaku, L. C. et al, (eds) *Principles and practices of Management and Business Studies.* Nigeria Educational publication Nig. Ltd.

Siropolis, N. (1994), *Small Business Management:* A Guide *to Entrepreneurship.* USA: Boston Houghton, Mifflin Company 5th Edition.

ASSIGNMENT

The assignment file will be made available to you. You will find all the details of the work you must submit to your tutor for marks. The marks you obtain for this assignment will count towards the final mark you will obtain for this course. Any further information on the assignment will be found in the assignment file.

ASSESSMENT

Your performance in this course will be based on two major approaches. First, are the tutor-marked assignments (TMAs), and the final examination

TUTOR-MARKED ASSIGNMENT

With respect to TMA, you are expected to apply the information, knowledge and techniques gathered during the course or studying this material. The assignment must be submitted to your tutor for formal assessment in accordance with the laid down rules. The total score obtain in the TMAs will account for 30 per cent of your overall course mark. There are many TMAs in the course you should submit any four to your tutor for assessment the highest three of the four assignments will be counted and this credited to your overall course mark.

FINAL EXAMINATION AND GRADING

At the end of the course, you will need to sit for a final written examination of two hours duration. This examination will count for 70 per cent of your overall course mark. The examination will consist of questions which reflect the type of self-testing, practice exercises and TMA Questions you have previously encountered. You are advice to prepare adequately for this examination. Since the general broad area will be assessed.

COURSE MARKING SCHEME

The following table lay out how the actual course marking is broken down.

Presentation Schedule

Assessment submitted	**Marks**
Assignments 1-12	Ten assignments, best five of the ten counts 8% each (8 X 5 = 40%) of course marks
Final examination	60% of overall course marks
Total	**100% of overall course marks.**

FACILITATORS/TUTORS AND TUTORIALS

Detailed information about the number of tutorial contact hours provided in support of this course will be communicated to you. You will also be notified about the dates, time and location of these tutorials, together with the names and telephone number of your tutor, as soon as you are allocated to a tutorial group. Your tutor will make and comment on your assignments, keep a close watch on your progress and on any difficulties you might encounter, and provide assistance to you during your course. Please do not hesitate to contact your tutor by telephone or email if you need help. The following might be circumstances in which you would find help necessary.

- You do not understand any part of the course units.
- You have difficulties with self-test or exercises.
- You have a question or problem with an assignment or with the grading of assignment.

You should endeavour to attend tutorial classes, since this is the only opportunity at your disposal to experience a physical and personal contact with your tutor, and to ask questions, which are promptly answered. Before attending tutorial classes you are advised to thoroughly go through the study units and then prepare a question list. This will afford you the opportunity of participating very actively in the discussion.

SUMMARY

Rural Finance is a course you would have had some background knowledge of. It will expose you to basic knowledge of rural finance. It discusses issues in rural financing, cooperative financing, benefits and paradigm, rural financial systems, rural financial institutions, investment appraisal technique and cooperative banking. It also provides overview of rural savings mobilization, rural development programmes and member financing. It is meant to enlighten students on the peculiarities of rural financing.

COURSE GUIDE

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MODULE 1

UNIT 1 RURAL FINANCING

CONTENTS

1.0 INTRODUCTION

The concept of rural finance maybe new to many people who are used to finance. Some people who thought that it is an abstract concept has seen that it is a reality that they experience daily. In this piece, you would be exposed to definition and basic terminologies in rural finance. People who see rural finance as esoteric language will relate that it is simply about the raising and usage of money by rural dwellers. You will surely see rural finance as largely the financial practices of rural populace.

2.0 OBJECTIVES

At the end, students shall be able to:

- understand the concept of finance
- understand the importance of finance in business
- understand the definition of rural area and extension

- understand the concept of rural finance
- understand the definition of rural financial services
- understand the objectives of promoting rural finance
- understand the challenges in rural service provision

3.0 MAIN CONTENT

3.1 The Concept of Finance

Finance is the raising and using of funds by individual, cooperative enterprises, firms and governmental organizations for the day to day running and management of their business undertaking.

As a discipline, finance is merely a body of facts, principle and theories which deal with raising and using of money individuals, governmental organizations, firms and cooperatives.
Finance is the raising and using of funds by individual, enterprises, firms and governmental organizations for the day to day running and management of their business undertakings.

3.2 Importance of Finance in Business

Finance is important to businesses due to the following:

- It is always regarded as the life blood of any organization.
- Provides basis for business planning, investment, diversification and cash flow statements.
- It provides the basis for control and employee maintenance.
- It provides basis for business growth and expansion, through ploughing back profits.
- Adequate finance ensures continuity of the enterprises, helps enterprise to plan ahead in investing in shares, stock and in human element and other viable business undertaking.

3.3 Definition of Rural area

Some organizations use population density as the main distinguishing factor, e.g., the Organization of Economic Co-operation and Development (OECD) classifies a community as "rural" when it has less than 150 inhabitants per square kilometer.

- International Fund for Agricultural Development (IFAD), defines "rural" in terms of two main characteristics, firstly, rural people generally live on farmsteads or in groups of houses containing perhaps 5000 - 10000 persons, separated by farmland, pastures, trees or scrublands. Secondly, the majority of rural people spend most of their time on farms.

- According to the Small Enterprises Education and Promotion (SEEP network), a rural area is defined as "an area in which the primary economic activities are small scale agriculture and live stock rearing, although it also includes small-scale trade, service and manufacturing activities. It is also characterized, in relative terms, by geographical isolation, low population densities, poorly developed infrastructure, underdeveloped markets for goods and services, and high poverty concentration".
- A rural area can be described as a non-urban area that is an area that is not urbanized or that does not have the types of infrastructural, social and other services associated with urban centres.

3.4 The Concept of Rural Finance

Rural finance encompasses the financial side of almost all economic processes in rural areas. These include: everything which .involves savings, financing and insurance of financial risks. Rural financial infrastructure or the rural financial system includes all savings and financing opportunities and thus the financial institutions which provide saving and financing opportunities as well as valid norms and models of behaviours related to the financial system.

Rural financial services is about providing financial services - secure savings, credit, money transfer services for remittance and insurance in rural area. The ability of rural households to make long term investments to ensure time-patterned income flow is shaped by an economy's financial services. The efficient provision of loans, deposits, payments and insurance services encourages rural entrepreneurship, helps the rural economy to grow and reduce poverty. Today's financial system approach to rural finance recognizes that sustainable institutions offering a menu of financial servicespriced to cover cost reach the greatest number of rural producers and enterprises.

3.5 Definition of Rural Financial Services (RFS)

In order to investigate rural financial services, It IS important to define what is included when considering "rural financial services". How to define a, "rural population" or "rural area"? it remains problematic to identify a clear definition of what constitutes a rural area that can be used uniformly across countries.

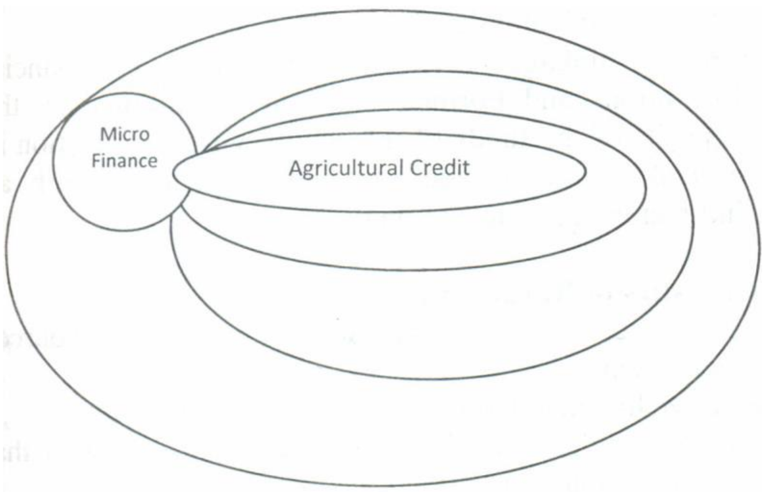
3.6 Definition of Rural Finance (RF)

Another important issue when discussing rural financial services is which financial services are included. The definition by Nagarajan and Meyer (2005) provides a useful guideline. Rural Finance: "The provision of financial services to a heterogeneous, rural, farm and non-farm population at all income levels through a variety of formal, informal, and semiformal institutional arrangements and diverse types of products and services, such as savings, loans, insurance, leasing and remittances.

Rural finance includes agriculture finance, micro finance and is a subsector of the larger financial sector.

Furthermore, rural finance encompasses the financial side of almost all economic processes in rural areas. They include: everything which involves savings, financing and insurance of financial risks. Rural financial system includes all savings and financing opportunities and the financial institutions which provide savings and financing opportunitiesas well as valid norms and models of behaviours related to the financial system.

Figure 1: Rural in Perspective



Experts: Rural Finance Group of MicroNeeds.

3.7 Characteristics of Rural Area

1. Dependence on sustainable natural resources management
2. Relative low profitability of on-farm investments.
3. Limited availability of conventional bank collateral that farm households can offer.
4. Low population density
5. Inadequate availability of skill personnel.

6. Dispersed economic activity.
7. Supply of credit services is limited by lack of collateral and lack of risk management mechanism.

3.8 Objective of Promoting Rural Finance

There are primary objectives for promotion of rural finance both by donors, agencies, banks, NGOs, producers organizations, buyers of produce, agro-processing firms, micro finance institutions, input suppliers, co-operatives, informal savings and lending groups, for finance is the key to enhancing economic development and reducing poverty in rural area. These objectives are summarized below:

1. Development of accessible financial institution.
2. Maximizing outreachbuilding up existing institutions.
3. Achieving sustainability in order to make the greatest possible impacts on the lives of the rural people,through increase in local income and creation of more savings.
4. Improvement in the supply of financial services to the target group.
5. Financial infrastructure in rural areas can help to the advantage of rural development.
6. Creates linkage between the Informal Financial Institutions and Formal Financial Institutions i.e. the deposits of the funds of informal savings association in a bank could provide association members with an indirect interest income on savings.

3.9 Challenges in Rural Financial Service Provision

Generally, it is recognized that supplying rural finance is more difficult than supplying urban microfinance. Difficulties relating to the development of the financial sector in the rural are listed by Milter (2005), in (Gabrielle, Having and Moi, 2008). They are 12 constraints which are classified into four groups - vulnerability constraints, operational constraints, capacity constraints, and regulatory constraints.

These are summarized:

3.2 Vulnerability Constraint

1. Systematic or covariant risk - same risk at the same time.
2. Market risk - fluctuation of prices
3. Credit risk – lack of collateral.

3.3 Operational Constraints

1. Investment returns - seasonality gives non-constant cash flow.
2. Low investment and assets - weak safety net.
3. Geographical dispersion-high dispersion and low population densities.

3.4 Capacity Constraint

1. Infrastructural capacity
2. Technical capacity and training rural population is less skilled.
3. Social exclusion - cultural, linguistics, etc., affects market and financial integration.
4. Institutional capacity.

3.5 Political and Regulator Constraint

1. Political and social interference - subsidized and/or directed credit from state-owned banks.
2. Regulator constraints - Regulations and/or lack of enforcement in rural environments.

4.0 CONCLUSION

In this unit you have studied basic terminologies and concepts. You should remember that rural finance is about providing financial services such as savings, credit, insurance and money transfer in rural areas. You have also learnt that since rural finance is a subsector of larger financial sector. It is critical to promote and develop it in order to achieve sustainable growth, financial inclusion and meeting financial needs of target groups.

5.0 SUMMARY

Rural financial service has become a critical tool in poverty alleviation and in achieving financial inclusion. Their benefits top rural dwellers and the vulnerable groups cannot be emphasized. It is expected that policy makers and rural financial services experts should continuously evolve products and policies that will make rural financial services cheap, convenient and flexible.

6.0 TUTOR-MARKED ASSIGNMENTS

1. Define rural finance
2. List and discuss the various challenges facing rural financial service provision

7.0 REFERENCES/FURTHER READINGS

Baumback, C.M. (1992). *Basic Small Business Management.* London: Prentice Hall.

Central Bank of Nigeria (1993) "Small and medium Scale Enterprise Development in Nigeria". *Annual Report and Statement of Accounts.*Lagos Central bank of Nigeria. Vol. 30 (4) P.246.

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Ikpe, K.I. (1989). "Financing Small Business in Nigeria under the Structural Adjustment Program". *The Executive:*An International Business and Economic annual Journal, Vol. 2, April, pp 13-19.

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Siropolis, N. (1994), *Small Business Management:* A Guide *to Entrepreneurship.* USA: Boston Houghton, Mifflin Company 5th Edition.

UNIT 2 RURAL FINANCE EVOLVING PARADIGMS

CONTENTS

1.0 INTRODUCTION

In the preceding unit, definitions of basic terminologies in rural finance were discussed. In this unit, you shall be focusing on the different paradigms of rural finance. You will learn the difference between the old and new paradigm as well as reasons why new paradigm is more sustainable and popular.

The old paradigm was supply-led because of the belief that there is high risk and special cost in rural finance which made financial institutions to be reluctant in moving into the rural areas. This approach focused on using governments and donor agencies to deliver financial interventions. As you would learn on this unit, the old approach lack sustainability and depth outreach. As a result, the new paradigm has taken over.

In this section, you will learn the assumptions of the old paradigm, reasons for its failure and operations of the new paradigm.

2.0 OBJECTIVES

At the end of this unit, you should be able:

- enumerate the objectives of rural finance programs in both old and new paradigms.
- examine the lessons learnt from the old paradigm.
- understand the new rural finance paradigms.

3.0 MAIN CONTENT

Several paradigms and policies have been used in developing countries to address the especially difficult and costly problem of providing financial services in rural areas. The old Rural Finance (RF) paradigm dates back to 1960s and 1970s. This ushered in a plethora of rural credit projects around the world. These projects were premised on the recognition of the special costs and risk assumed to be involved in rural finance - that made formal financial institutions reluctant to expand into rural areas. A rationale was developed, therefore, that urged governments and donors to intervene in rural financial markets.

These rural finance programs were expected to promote agricultural developments. The interventions were intended:

1. to increase rural lending by reducing the costs and risks to lenders that made loans to preferred rural clients and sectors.
2. subsidized interest rates. Loan waivers and forgiveness programs were also used to reduce the debt burden of priority - sector borrowers, especially following floods, droughts and periods of floods, droughts and periods of low farm prices.
3. credit was considered an important means to speed agricultural development, expand exports, promote small farmers, reduce poverty, and ensure cheap food supplies to urban areas.
4. multilateral and bilateral donor invariably supported the approach taken by many governments and funded many of the targeted supply led projects.

3.1 Lessons from the Old Paradigm

1. Helped developing countries to improve agricultural yields in the short term. But it was costly and unsustainable over the long term.
2. It failed to reach the majority of rural households.
3. The few positive benefits were unable to achieve the intended objectives of increasing rural incomes, stimulating asset formation, and reducing rural poverty.
4. The focus on lending only for agricultural purposes ignored the potential benefits of supporting growth- intensive investments more appropriate for the rural poor or small, off farm rural enterprises.
5. In many cases, costly bailouts of state-owned agricultural credit institutions undermined the development of private, for profit, rural financial institutions.
6. Most governments invariably use rural finance for political objectives and underestimated the difficulties, costs, and risks of supplying sustainable rural financial services.

Note: The majority of RF programs that followed the old paradigm failed, based on these:

a. Subsidized interest rates did not cover costs, so rural financial institutions (RFI) were unviable and they lost the confidence of depositors.
b. There was a huge build-up of non-performing loans since cheap credit encouraged unprofitable investments and led to concentration of loan portfolios in the hands of the rich and powerful.
c. Subsidized agricultural credit often resulted in production inefficiencies by targeting the wrong products and creating artificial preference for capital intensive investments that "crowded out" abundant labour in rural areas.
d. In some cases borrowers intentionally defaulted because they believed that governments would waive or forgive their loans or not take action against defaulters in priority sectors.
e. Financial discipline was damaged and intermediaries weakened.
f. Several development finance institutions became insolvent and were closed or had to be recapitalized.
g. In some cases, Refinance schemes discourage savings mobilization and financial intermediation.
h. Deposit mobilization was largely ignored, since donors and governments provide most of the funds used by RFls to channel subsidized services.
i. It made rural people not to be bankable.

3.2 The New Rural Finance Paradigm

This began to emerge in the late 1980s and gained momentum in the mid-1990s. It is based on lessons from the old paradigm, though being fine-tuned as new information becomes available. The new paradigm reflects a financial system approach:

Since market principles to deliver financial services aimed at facilitating rural development that in turn promotes asset creation and poverty reduction.

1. The new paradigm treats finance as a valuable way to expand and integrate markets, rather than as a policy tool targeted for specific market segments.
2. Efficient financial markets are expected to increase the productivity of the available factors of production.
3. That finance should not be controlled or redirected to 'pursue non-financial goals but needs to be promoted to achieve desired development (Gonzale-Vega, 2003a).
4. The new rural finance paradigm is based on the principle that a commercial, market-based approach is most likely to reach large numbers of clients on a sustained basis.

5. It recognizes that financial services are part of an interactive system of financial institutions, financial infrastructure, legal and regulatory frame works, and social and cultural norms.

4.0 CONCLUSION

In this unit, you have been educated on paradigms evolving in rural finance. We discussed both the old paradigm rural finance programmes and the new rural finance paradigm. You were also educated on the objectives these paradigms set to achieve as well as reasons why majority of the rural finance programs that followed the old paradigm failed. Furthermore, we have come to understand the concept of the new paradigm and that it reflects a financial paradigm and that it reflects a financial system approach.

5.0 SUMMARY

In this unit, you have learnt the reasons for the old and new paradigm in the rural financial. You have also learnt the difference between the old and new paradigm. Lastly, you have learnt about the strength of the new paradigm and why it is sustainable and attractive to private sector operators. And roles of cooperative in credit mobilization.

At the end of the course, students would have developed understanding of rural financing terminologies, systems, institutions, mechanism and programme. They will be able to design rural financial services, interact with experts, understand rural financial practices and help rural client to handle financial difficulties. It is expected that students should relate what they would learn here with practical life experiences in order to assimilate their importance. We hope you will find the course interesting.

6.0 TUTOR-MARKED ASSIGNMENT

1. State 3 reasons why the rural finance program that followed the old paradigm failed.
2. How does the new paradigm see rural finance?

7.0 REFERENCES/FURTHER READINGS

Baumback, C.M. (1992). *Basic Small Business Management* London: Prentice Hall.

Central Bank of Nigeria (1993) "Small and medium Scale Enterprise Development in Nigeria".*Annual Report and Statement of Accounts.*Lagos Central bank of Nigeria.Vol. 30 (4) P.246.

Green, G. C. (1975), *How to Start and Manage your Own Business*New York: McGraw Hill.

Ikpe, K.I. (1989). "Financing Small Business in Nigeria under the Structural Adjustment Program".*The Executive:* An International Business and Economic annual Journal, Vol. 2, April, pp 13-19.

INSTRAW (1991), *Analysis of Women's Participation in the informal Sector.*(Report of the Consultative Meeting of Experts on Macroeconomic Policy), Rome: United Nations PP 6-10.

Ho, M.S. and Urata (1994). Small and Medium Size Entreprises Support Policy in Japan Washington D.C.: World Bank policy Research Department.

Ijere, M. A. (1992). *Prospects of Nigerian Cooperatives.*Nigeria: A Johnson Publishers Ltd.

Nweze, N.J. (1997). *Essentials of Cooperative Economic* Nigeria: A Johnson publishers Ltd.

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Iwuafor, E.N. (1986). "Business organization, in Ezeaku, L. C. et al, (eds) *Principles and practices of Management and Business Studies.* Nigeria Educational publication Nig. Ltd.

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UNIT 3 RURAL FINANCE APPROACHES

CONTENTS

1.0 INTRODUCTION

In unit 2, we learnt about rural finance paradigms and exposed to both the old and new rural finance paradigms. In this unit, we focus on rural finance approaches used in assessing the remote rural poor so that financial services can be easily accessed by them. We identify various methods used, the focus and the partner organizations. Also, financial products that are essential to the rural poor would be identified.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- discuss approaches supporting the provision of rural financial services, focus and challenges.
- identify the rural financial products.

3.0 MAIN CONTENT

Currently, there is considerable interest in using innovative models to reach the remote rural poor and to provide financial services required by farmers and rural households in general. These models arises from the observations that integrated operations are emerging between real and financial sectors to facilitate the smooth flow of commodities and services from producers to consumers within the activity sectors.

Three main methods can be distinguished as deployed by Co-financing organization (CFOs). The first-and most common approach focuses on building financially sustainable microfinance institutions, (MFIs). Support focuses on MFIs' financial and operational sustainability. This approach targets credit led MFTs that receive external funds for their loan funds and introduce deposit services when they have matured and acquired the appropriate legal status. The challenge of this approach, though, in a rural context is to adapt products and delivery mechanism to meet the need of rural population and to keep costs low while serving clients in low-density population areas.

The second approach being applied to practice, entails support to Member-Owned Microfinance Institutions, (MOMFI), like the co-operatives, self-help groups, credit unions etc. Members of these institutions are both users and owners of the institution; members are involved in decision making. CFO supports these MOMFls both directly and through NGOs that promote and assist member-owned institutions.
The NGOs provide training and technical assistance. Cost recovery is not the main bottle neck. The key challenge relates to governance and management capacities for those MOMFI have grown too large to be monitored by their peers. Most times focus is on the MOMFls' institutional sustainability.

The third approach involves financing actors in the value chain, based on rural economic development perspective. A value chain can be defined as "the full range of activities that are required to bring a product from its conception to its end use".

The value chain consists of enterprises that collaborate in various degrees, the chain is defined by its raw material and market segment. The enterprises, or actors in the chain can provide (financial) services to other actors outside the chain, such as a bank or MFI. The lenders rely on the strength of the value chain to reduce risks. CFOs are increasingly interested in value chain development. This means that CFOs actively promote sustainable – inclusion target groups into value chains to improve participation and benefits (Gabrielle, et al 2008).

Table1: CFOs' Three Main Approaches to support the Provision of Rural Financial Services

APPROACH	Support to credit led microfinance institution	Support to member owned microfinance institutions	Support for the provision of financial services to actors in the value
FOCUS	Building financially and operational sustainable microfinance institutions that provide financial services tailored to their clients	Building institutional sustainability directly or through an NGOor MOMFIs to provide financial services tailored to their members	Include or strengthen the position of CFO target groups III value chains.
Partner Organizations	MFIs, MFI networks microfinance services providers	Co-operatives, credit unions, SHOo	xoos, MFIs, trading companies fanners organizations.

Source:

3.2 Rural Financial Products

The historical focus of rural finance has centered on the extension of credit, often subsidized and directed, to rural areas. Infact, rural people demand a diverse array of financial services including savings, money transfers, insurance and credit. These financial services support wider real goods sector production, contributing to employment, economic growth and income generation.

Given that rural households have diverse strategies for accumulating assets and minimizing their vulnerability, rural finance institutions need to:

1. Assess the demand of rural clients for multiple financial services.
2. Identify and examine all income sources and expenses of their clients at the household level and;
3. Assess environmental credit risks associated with production and market cycles.

Sparse and geographically dispersed populations characterize the rural operating environment, making it difficult for financial institutions to achieve economies of scale. Financial products and services need to suit the rural agricultural environment where production and market cycles affect client income and expenses.

The following financial services to rural areas are:

- Savings mobilization Credit (lending) Leasing
- Savings mobilizatioon
- Credit (lending)
- Leasing
- Remittances.

4.0 CONCLUSION

This unit discussed three main approaches to support the provision of rural financial services. The first approach focused on building financially sustainable Microfinance Institutions (MFIs) that targeted MFIs that receive external funds for loans and introduce deposit services when they mature and acquire appropriate legal status but it had the challenge of adapting products and delivery mechanism to meet the need if rural population and to keep costs low while serving clients in low density population areas.

The second approach supports ember owned Micro-Finance Institutions, (MOMFI) like cooperatives, self-help groups and credit unions. Its key challenge lies with the governance and management capacities due to large size of those MOMFIs.

The third approach involves financing actors in the value chain, based on rural economic development perspective. In this unit also, financial services to rural areas were identified as: savings mobilisation, credit (lending) leasing, credit, leasing and remittances.

5.0 SUMMARY

You have been presented with practical approaches in providing rural financial services. Also, you have learnt about basic financial services provided to rural areas.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the CFO’s main approaches to support the provision of rural financial services.
2. List 4 financial services that can be rendered to a rural area

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UNIT 4 RURAL FINANCING HISTORICAL OVERVIEW

CONTENTS

1.0 INTRODUCTION

The introduction of cooperative credit movement started in Germany in the 19^{th} Century- by Fredrick Wilhelm Raiffeisen who was born between (30^{th} March 1818 - l l" March, 1888). He was fondly referred to as the founder of credit cooperative society in Germany. His order profile include:

- a German mayor of several communities in Germany
- he was inspired by observing the suffering of the farmers who were often in grip of loan sharks
- It was reported that almost every house and farmland was encumbered with debt
- He established a cooperative bakery known as (society for bread and gain supply) cooperative
- noticed thrift lessness among farmers credit society, started Heddsdorf benevolent society based on principle of benevolent assistance
- general central bank at Neuwied, called (Rhenish Agricultural Cooperative Bank) created also a printing house in Neuwied, which still exists today, though merged with the German cooperative publishing house in 1975

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- explain the history of cooperative credit movement and the founders.
- analyze Schulze Delitzch's urban bank model
- provide a description of its large area of cooperation.

3.0 MAIN CONTENT

Philosophy: Raiffeisen stated that there is a connection between poverty and dependency. In order to fight poverty, one should fight dependency first. Based on this idea, he came up with the three "s" formular: SELF-HELP, SELF GOVERNANCE AND SELF RESPONSIBILITY.

- It was from this credit outfit that the cooperative maxim of each for all and all for each emanated.
- He initiated community bank. Raiffeisen Rural Bank Model
- Membership was limited to the rural masses especially farmers
- Unlimited liability of the member
- Small area of operation
- Small loans were given to the members which were recovered over a long period. Loans were given on the basis of personal security of the members and only for productive purpose.
- Emphasis is on personal character of the borrower. .
- There is no share capital and profit earning was not the motive.
- The management was paid honorary.

3.1 Schulze DeIitzsch (1808 - 1883) A Lawyer by Profession

- Just like Raiffeisen, he witnessed the harsh economic situation brought about by economic liberation,
- Familiar with the problem of small scale industries
- concerned himself with urban credits
- founded the first friendly society of shoemakers
- founded his first credit society in his native town in 1950 and its major function were to raise funds to be lent to its members in 1861 called on congress of his banks where General Union of German Industry Societies was formed Initiated 1926 Peoples Banks.

Philosophy: Schulze believed that societies should be run on economic lines, no wonder, his cooperative societies were viable units and withstood competition.

3.2 Schulze Urban Bank Model

- Membership was limited to artisan, industrial workers and middle class people living in cities and towns
- Limited liability of the members.

3.3 Large Area of Operation

- The amount of loan advanced was big and the period of the repayment was short.
- Loans were given on the basis of tangible assets, for productive purposes and under supervision.
- A strong capital profit earning was main motive and the rate of dividend quite high.
- The management was paid salary.

4.0 CONCLUSION

You have learnt in this unit about the history of cooperative credit movement. We were exposed to founders such as Raiffeisen and Schulze Delitsch together with their achievements each to cooperative credit. We also looked at the philosophy upon which their operatives were based. We further identified the similarities and differences between these founders.

5.0 SUMMARY

In this unit, we explained how the cooperative credit movement started and also presented an overview of the similarities and differences between Raiffesen's philosophy and Schulze Delitsch's philosophy. Lastly, the large area of operation as well was viewed.

6.0 TUTOR-MARKED ASSIGNMENT

1) Explain the history of cooperative credit movement
2) Analyze Schulze Delitsch's urban bank model

7.0 REFERENCES/FURTHER READINGS

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MODULE 2

UNIT 1 SAVINGS MOBILIZATION

CONTENTS

1.0 INTRODUCTION

There is nothing as important as meeting the financial needs of the rural population. The poor need very little compulsion to save but require safe and convenient saving mechanisms.

Savings can be seen as that part of disposable income which is not spent on consumption. Savings is normally considered in economics as disposable income minus personal consumption expenditure.

Savings is regarded as income that is not consumed by immediately buying goods and services. Savings and savings mobilization in any economy is undertaken by formal, semiformal and informal institutions.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- ascertain the importance of savings mobilization
- discuss the mechanisms used in mobilizing savings.
- know the concept of credit (lending)

- know the concept of leasing.

3.0 MAIN CONTENT

3.1 Importance of Savings Mobilization

1. Savings mobilization increases supply of internally generated funds that can be invested in rural micro enterprise, off - farm small business loans and shelter improvement.
2. It helps to achieve sustained economic growth and development, but also to strengthen domestic financial intermediaries (Sebhatu, 2012)
3. It helps to overcome liquidity constraints in individual household.

Note: Savings among rural people is a function of income. Arguably, the larger the income, the greater the propensity to save. However, among rural depositors, proximity and convenience are crucial factors to savings.

3.2 Savings Mobilization Mechanism in Rural Area

1. Daily deposit scheme in savings are collected daily at the doorsteps of rural depositors by mobile deposit collectors (called micro-savings agents) e.g. Peru, Nigeria.
2. Post office savings banks - (POSBs) are emerging as significant providers of deposit services in rural areas. E.g. POSBs in China, Indonesia, etc.
3. Use of lockboxes for clients to deposit their savings and collect or accept the contents of the box at periodic intervals. An example is the "ganansya box" provided by Rural Banks in the Philippines (Campion and Owuns, 2003).
4. In places with good access to commercial banks or with MFI branches close to rural areas, it is useful to train group members and self-help group to collect and manage savings accounts at the bank.
5. Small offices with part-time staff and/or small offices that operate within the existing infrastructure, such as community based organizations.
6. In technologically advanced countries, the use of electronic banking technologies such as hand-help personal digital assistants, smart cards, phone and internet banking can be effective in reducing transaction costs.

3.3 Credit (Lending)

"Rural lending requires greater effort to assess loans than in urban lending due to greater complexity of rural 'households' economies which arises from seasonality and diversified incomes" (Joan Buchenau, 2003). Families in rural areas seek to diversify their sources of income beyond agriculture. Households often have a number of income sources that include agricultural production, non- agricultural production and both on and off-farm labour income. Lending to rural households requires tailoring products to meet client demand and assessing client repayment capacity based on multiple income streams.

The assessment of a client's repayment capacity should include an:

1. Analysis of projected cash incomes and expenditure for households different economic activities.
2. Once repayment. capacity has been determined, a payment schedule can be agreed upon and from
3. This information, a tailored loan repayment schedule is drawn up.

Rural households with multiple income sources have restricted (if any) access to formal financial services and rely on informal providers such as traders, money lenders, friends, families and agricultural processors for financing. Other times from co-operative societies.

Discussions on rural lending involves the following nature of lending:

a. **Long-term Agriculture Investment Loans:** This type of lending finances production, processing and marketing of agriculture related businesses. However, insufficient forms of collateral and uncertainty about long term agricultural output restrict the availability of agricultural investment loans.

b. **Short-term Rural Enterprise and Farm Loans:** A working capital loan for rural family enterprises is geared to households with diversified income sources from agriculture and or other rural enterprise. This is comparable to an individual urban micro lending product yet differs due to flexible/tailored loan repayment plans subject to a clients repayment capacity. A loan officer defines a repayment schedule based on a household's projected cash income from andexpenditures on economic and non-economic activities.

c. **Lending Against Warehouse Receipts:** A grain-specific form of rural lending is offered through warehouse receipts. In order to access this type of credit, a farmer delivers a minimum grain quantity to a grain warehousing facility that then produces a receipt to document the quantity of grain delivered. The farmer pays a monthly storage fee. The farmer can then sell grain during favourable market conditions or as is needed to meet expenditures. Warehouses often have minimum grain requirements for storage. Small farmer may affiliate with cooperative or other type of farm association to overcome obstacle of meeting minimum grain storage quantities. In addition to providing storage mechanism for grains, the warehouse receipt may be used as collateral by the producer to obtain loan from a financial institution.

d. **Group-based lending:** This is wherein group liability replaces fixed asset collateral requirements for borrowing, provides a credit product to clients which would not be considered credit worthy on individual basis. Group-based lending (loans approved generally for 16 week terms) is useful to finance rural productive activities such as supplying inventory for food vendors. Group-based lending in the rural context needs to offer an advantage over individual lending due to its higher delivery costs.

e. **Buyer and Supplier Credit Product:** Market credit extended to farmers by input supplies, retail traders, wholesalers, processors and exporters addresses an unmerit demand for formal financial services in the rural areas. Product market credit enables farmers to access short-term advances, seasonal credit for the purchase of product inputs, and technical advice (Pearce, 2003). This enables the supplier/traders to secure certain quantity and quality of produce from the farmer.

f. **Contract Farming:** Is one type of financial arrangement in which a wholesaler extends financial credit and may also offer technical assistance to the producer. The farmer obtains credit upon contract signature. The contract specifies the production calendar, required volume and produce quality. While interest rate is explicitly stated, there is usually a discount on the selling price for the producer built into contract.

g. **Trader Credit:** Provides farmers with in-kind advances or cash advances, contingent upon repayment at harvest or as agreed upon selling price of goods at harvests. Trader credit is not intended for financing long-term investments, such as purchasing equipment or property, expanding operations, improving quality standards or starting new activities. However, it secures a local supply of produce and generates income from the related interest gained from loan transaction. Trader credit may help farmers with building relationships and obtaining credit.

3.4 Leasing

Leasing is now recognized as an alternative financial mechanism for reaching poor rural clients with limited access to term loans. Leasing can be a means to acquire equipment and machinery needed to expand and diversify micro-business and farm businesses and to acquire capital assets through pay- as-you-go leasing contracts.

Leasing can allow new businesses with limited capital and credit history or small businesses without a history of financial statements to quickly boost their operations as long asthe cash flow from operations is sufficient to cover the lease service payments.

When leasing equipment instead of lending funds to a client to purchase equipment until its purchase costs are completely repaid with interest. **In** the legal frameworks of some country, if the lessor maintains the title to the equipment, then seizure and repossession of the piece of equipment in the case of repayment default by the lessee will be facilitated. The lessor insures the equipment and the lessee is responsible for equipment maintenance.

Emerging lessons from leasing experiments III rural areas show that:

a. Leasing contracts are suitable for individual rather than group, transactions,
b. Leasing contracts require a significant down payment or pledge collateral to reduce the risks for the lessor.
c. Provides the lessee with the opportunity to buy the equipment at the end of the lease term for a nominal fee.
d. Leasing provides a viable financial option for a large proportion of the poor, rural residents who are engaged in agriculture based enterprises.

4.0 CONCLUSION

In this unit, the importance of savings mobilization was enunciated as well as mechanisms that can be effectively applied in rural areas in mobilizing savings. Some identified mechanisms were: daily deposit scheme, post office savings banks, use of lockboxes, training group members and self-help group to collect and manage savings accounts at the bank, small offices like community based organisation technologies. We also discussed what rural lending's and different nature of lending such as long term agriculture investment loans, short term rural enterprise and farm loans, lending against warehouses receipts, group based lending, buyer and supplier credit product, contract farming and trader credit. We have also learnt what leasing entails.

5.0 SUMMARY

This unit provided an understanding on the importance of savings mobilisation, discussed the concept of leasing and lending.

6.0 TUTOR-MARKED ASSIGNMENT

1. What is the importance of savings mobilization?
2. Discuss the nature of lending

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UNIT 2 OBJECTIVES OF PROMOTING RURAL FINANCE

CONTENTS

1.0 INTRODUCTION

The improvement of the living, condition of the target population through a strengthen of rural finance can be broken down into more concrete immediate or secondary objectives.

Specific promotion measures can be directed towards these intermediary objectives, and their success can be guarded by them. One criterion for classification is whether the target group profit directly or only indirectly from attainment of the objectives.

The first intermediate objective with direct effect on the target groups is the development of accessible financial

7.0 OBJECTIVES

At the end of this unit, the students will be able to

i) explain rural financial activities operating outside the formal financial system (non institutional saving).
ii) Enumerate the basic principles for cooperative financing
iii) Ascertain the importance of finance in rural cooperative business.

3.0 MAIN CONTENT

3.1 Rural Financing Activities

Cooperative financial activities in villages include all types of credit savings associations operating outside the formal financial systems.

These associations are regarded as non-institutional saving methods and they include Isusu institutions, money lenders, daily savings club, merchant or trader's- credit etc. They exist as an unregistered association and operate outside the banking system not regulated and they are being monitored than formal sources.

3.2 Isusu Credit Association

Isusu is an association of people for the purpose contributing fixed sums of money at regular intervals to meet the members various needs. It is a kind of club organized among people with trust and confidence in themselves and us al y in the same geographical location. Isusu club may be organized on the basis of dance groups, age grade, religious *and social*organizations. Organizationally, the coordinator collects the agreed amount of money each month and the total will b given to a member of the group in an arranged order.This goes on until all the members must have collected theirs. There is no interest attached.

3.3 Characteristics of Isusu Credit Association

They include:

i. Grouping of few savers who trust each other.
ii. Lack of legal protection.
iii. Existence of some link between members of same group of farmer or religious organization the same area.
iv. Need for savings and credit facilities felt by members.
v. No formal procedures
vi. Enhancing the viability and liquidity position of the rural banks through deposit accumulation.
vii. Reduction in default rate as saving mobilized could be used to offer outstanding loans when the need arises.
viii. The transformation of informal to formal rural financial system with all the benefit derivable there from.

3.4 Principles for Cooperative Financing

Certain principles have evoked over turn, which are considered basic to cooperative financing. These include:

1. Control of cooperatives should be invested on the common stock or membership fee either on one man vote basis or in proportion to patronage.
2. Capital should be subscribed in relation to patronage.
3. If capital is subscribed in proportion to patronage, there will be less need to pay interest on capital, patronage refunds will be

larger in such cases.

4. Additions to original capital should be on a pro rata basis of patronage.
5. Ownership and control should always be vested with active patrons, this necessitates; a kind of revolving fund plan whereby the oldest equities are retired and replaced by current ones.
6. Entry investment cost should not be too small and not too large to be prohibitive.
7. Patrons who are inactive from one year to three year should have their voting equity converted into a non-voting equity or retire in cash.
8. There will be sufficient working capital to operate newly acquires facilities.
9. Equity capital contribution should be evaluated yearly on the basis of patronage volume of each member.
10. Its term browning for fixed assets or liabilities should not exceed 60% of the value of such assets.

3.5 Importance of Finance in Rural Cooperative Business

The quintessence of any organization is finance, and finance being very sensitive in the light of its closeness to the people and coupled with the fact that it symbolizes the yearnings of the masses requires adequate attention. Indeed without the requisite muscle and effective financial Management, the policies adopted by cooperative business organization in a great variety of areas may not be capable of being 'successfully implemented, hence the importance of finance. Finance provides the basis for business planning, investment diversification and (ash flow statements etc. Without finance/in business, no meaningful and viable ideas, articulation thoughts or any other thing can come to reality.

Finance in business provides the basis of control and employee maintenance of any commercial undertaking from what is invested comes forth the output which is converted intocash with which further investment are made and also for employee welfare.

Finance provides the basis for business growth and expansion no business grows without adequate financing and investment plans. Profits are made from margins added to the pricing of business articles of trade. From this result profits are ploughed back into the business for further business growth and expansion.

Finance helps business in planning and control. No meaningful and effective business plan can be done without other organization, in human element and some viable deference to the financial plan of the cooperative business undertaking. How effective the financial plan is, determine how well the business plan will be.

Adequate financing of a cooperative business ensures and guarantees the continuity of the enterprise, help the enterprise to plan ahead in investing in shares, in stock of otherorganization, in human element and some viable business undertaking.

4.0 CONCLUSION

You have studied what rural financial activities entail. You have also discovered that there are rural financial activities done outside the formal Banking system some of which we identified as ISUSU institutions, money lenders, daily savings club, merchant or trader's-credit. They are unregistered associations. Characteristics of Isusu credit Association were also tested. We further looked at the principles guiding cooperative financing and the significance of finance in rural cooperative businesses.

5.0 SUMMARY

In this unit, certain unregistered rural financial systems were taught. You were exposed to core principles guiding cooperative financing and understood the importance of finance in rural cooperative business.

6.0 TUTOR-MARKED ASSIGNMENT

1. What are the basic principles for cooperative financing?
2. What is the importance of finance in rural cooperative business?

7.0 REFERENCES/FURTHER READINGS

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UNIT 3 NATURE OF NIGERIAN RURAL FINANCIAL SYSTEM

CONTENTS

1.0 INTRODUCTION

Nigeria rural sector can be said to consist of all economic activities outside the urban community. Akinbide stated that rural settlement can be regarded as those whose population engaged primarily in economic activities involving the direct and indirect exploitation of the land by under-taking crop production, animal husbandry, fishery, food processing and cottage industries including rural crafts, mining, trading and transportation services. Mbagwu (1978) says that many people believe that rural community as in Nigeria are characterized by traditional agriculture gathering, hunting and fishing practice. As a result of this, he claimed that many people give thought to the existence of primary sectors in the occupational mix of the rural population of the country. He recognized the existence of traditional industries which exist side by side with agriculture in the rural sector.

Olashore (1979) in his contributions said that economic indicators showed that about 70 percent of the population of Nigerians live in the rural areas and most of them have been denied access to banking facilities. The significance of this lack of access to banking facilities is better appreciated when one realizes that the bulk of the rural population is engaged in agriculture, handicraft and other basic small-scale industries long finances. The urban development bank opened for business with an authorized equity capital of N800 million subscribed by the three tiers of government (federal, state and local), the Nigeria Labour Congress and individual Nigerians .Another N800 million for on lending to customers for project development. The bank is expected to operate strictly as an independent institution and to provide financial assistance to both public and private sectors of the economy for the development of dwellings, mass transportation and public utilities.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- understand the cooperative financial structure
- know the structure of cooperative financial system
- discuss ways to access finance using cooperative financial institutions, banks and insurance
- determine the capital need of a cooperative enterprise.

3.0 MAIN CONTENT

3.1 Financial Structure of Cooperatives

This structure reveals what makes a cooperative distinct from other types of businesses. A review of some of the key operating principles of cooperatives will illustrate how these differences are related to cooperative financing.

1. **User-owner principle:** This principle suggests that the cooperative members those who use the cooperative-should provide equity (ownership financing) in proportion to their use of the cooperative.
2. **User-benefit principle:** Financial benefits of cooperative membership are distributed to members in proportion to their use of the cooperative, unlike other types of businesses, where benefits are distributed according to the amount of investment.
3. **User- control principle:** The one member-one vote rule by which cooperatives operate serves to distribute power equally among all the current member owners.
4. **Limited return on equity:** Investors' return is limited by law. By limiting the return available on investment, cooperatives limit the accumulation of wealth by a few owners.

3.2 The Structure of Cooperative Financial System

a. At the primary society level) every member must subscribe a minimum amount as share capital. A non-refundable entry fee is charged which each co- operator decides how much he/she will save regularly at stated intervals. Additional funds may be collected through fines imposed for infringement of cooperative by-laws, or fees charged for specific services. The by-laws spell out the details, which may vary from society to society.

b. At the union level, every affiliated society subscribes a democratically determined amount while additional funds are generated through business transactions. The affiliated societies are expected to pass their businesses through the union so that the union makes profits, which accrue to the societies and partly to the union. This happens whether it is a product marketing or savings/credit operation.

c. At the apex or Federation level, every union subscribes to the funds that are used for managing the body. It is important that the apex helps the unions to achieve their business objectives. Funds gathered through the three tiers of cooperatives are accumulated to form a substantial base for cooperative financing.

3.3 Access to Finance through Cooperative Financial Institutions, Banks and Insurance

a. **Special Cooperatives** are set up to cater for the provision of financial intermediation. These include finance houses such as Cooperative Finance Association (CFAs) and Banks which receive savings from cooperative societies and extend credit to the needy individuals and societies charging moderate interest rates. Some banks have been established using the savings of the cooperative society members plus grants or subventions from government or other donor agents. The key to success is financial probity and good management.

b. **Cooperative Insurance** is another good means of mobilizing funds for cooperative development. As millions of co-operators pay small premiums across the country, the amount of money accumulated will be very large. Such capital will form the basis of financing payments to those who incur losses and for loan operation in the Movement.

3.4 Determining Capital Need of a Cooperative Enterprise

No business organization can survive without adequate flow of finance which can either be short or long term capital.

LONG-TERM CAPITAL: Long term capital is made up of funds to, acquire long term assets such as land, building equipment, vehicles, in addition it include stock investment made in other cooperative or cooperation such as membership in a federated buying or selling cooperative societies.

SHORT-TERM CAPITAL: These are funds used for making crop and livestock advances, inventories, supplies, wages and other current expenditure. If cooperative extends credit, financing of accounts receivable is also included as short-term capital.

ORGANISATIONAL FUNDS: These are funds used for legal and recording fees, business permit, incorporation fees, promotional supplies and expenses incurred in forming the cooperatives.
The exact amount of capital necessary for cooperative organization depends on:

1. The type and size of cooperative anticipated
2. The extent of ownership or rental of fixed facilities
3. The pledges of business volume
4. The availability of borrowed funds and the ability of members to subside for capital.
5. The type and extent of services to be provided such as whether credit will be extended.

4.0 CONCLUSION

The cooperative financial structure reveals thee distinctiveness of cooperatives compared to other business types using: its core principle of user-owner principle, user-benefit-principle, user control principle and limited return on equity. Also, we discussed the structure of cooperative financial system at the primary union, and apex or federation level. In accessing finance using cooperatives, we considered special cooperative and cooperative insurance. We further explained the capital need of cooperatives enterprise.

5.0 SUMMARY

Cooperative financial structure and cooperative financial system have been explained in this unit. You were also exposed to ways of obtaining finance through cooperatives and lastly we saw the essential importance of capital to cooperatives

5.0 TUTOR-MARKED ASSIGNMENT

1. Discuss ways to access finance using cooperative financial institutions, banks and insurance.
2. Discuss the structure of financial system at the primary society level.

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UNIT 4 FINANCING OF COOPERATIVES

CONTENTS

1.0 INTRODUCTION

Cooperatives are businesses and they need finance to function. Capital is the blood of every business. Cooperatives obtain such capital either through, internal funds or source for external finding. But, nonetheless, cooperatives have some identified constraints in obtaining such funds as discussed in this unit.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- discuss the sources of finance to cooperatives.
- enumerate limitation of cooperatives in obtaining funds.

3.0 MAIN CONTENT

Sources for the financing of the cooperatives can be grouped into internal financing and external financing.

3.1 Internal Financing

a. **Share Capital-** Share capital is one of the equal parts into which the ownership of a cooperative is divided. This is the main source of capital at the beginning of the life of the cooperative society. The members fix the minimum share capital to be contributed by each member. This fund enables the cooperative to operate its business enterprises.

b. **Thrift savings -** This refers to the wise and careful use of money, so that none is wasted. That little surplus of money accruing to a member is brought to the cooperative society and it is recorded as savings for the member, who also has a savings passbook for this purpose. The cooperative society can utilize the accumulation of the thrift savings to run its enterprises, make profits (margins) and still reimburse members accordingly. It is important to note that thrift and credit cooperative societies develop from this setting.

c. **Entrance fee -** Cooperative societies make the payment of entrance fee a requirement or qualification or condition for membership. The entrance fee is used to buy such items as books of accounts, passbooks, byelaws, stamps, etc.

d. Members' Deposit - This is a lump sum of money paid into an account as special savings. It is from these savings or deposit that the society is able to give out loans. Credit cooperative societies accept members deposit/saving as their main source of income.

e. **Levies-** This is an additional amount of money which members of the cooperatives impose oil themselves in order to raise money to execute a programme or project.

f. **Fines-** This refers to the fee or payment required from a member as a penalty or punishment for breaking a cooperative rule or law or legal agreement. Examples are noisemaking, disturbances during functions, unruly behaviours and failure to pay agreed sums of money.

g. **Donations-** Donations can trickle in from members of the cooperative society for the purpose of improving the financial strength of the cooperative or to off-set a particular item or project. With this strategy, a lot of money can be generated from good spirited and philanthropic members of the cooperative.

3.2 External Financing

a. Loans and Overdrafts - These amounts of money can be sourced from the banks and other financial institution. Loans are monies borrowed from the banks(86) participation of members in the management of cooperatives.

b. Small income earners can make meaningful savings and investment.

c. It is the most appropriate way for rural mobilization and organization. Agricultural cooperatives serve as the most suitable channel for delivery of inputs and services to rural farmers (Ijere, 1992).

3.3 Disadvantages of Cooperative

- Required expertise in business may not be exhibited especially where members have low level of education.
- Capital contributed may not be enough to stock the consumer

shop. This results in low patronage by members and may result in lack of commitment by members.

- Where assistance from government or other non-governmental bodies is not forth, coming (especially where formation is premised on that) it will lead to the cooperative going moribund.
- Where assistance from government or other non governmental bodies is not forthcoming (especially where formation is premised on that) it will lead to the cooperative going moribund.

4.0 CONCLUSION

Cooperatives can obtain funds internally or externally. Internally includes: share capital, thrift savings, entrance fee, members' deposit, levies, fines, donations. Externally includes: loans and overdrafts, small income earners can make meaningful savings and investment, it is the most appropriate way for rural mobilisation and organisation. However, compared to various other types of business, cooperatives are faced with some disadvantages limiting their capacity to obtain funds.

5.0 SUMMARY

In this unit, we looked at the various internal and external sources of finance available to cooperatives. Also, we looked at disadvantages cooperative faces in funding.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the sources of finance to cooperatives.
2. Enumerate limitation of cooperatives in obtaining funds.

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UNIT 5 TIME VALUE OF MONEY

CONTENTS

1.0 INTRODUCTION

In most of our financial discussions, money is an absolute terms. Time is not considered when computing the value of money. If a firm borrows ₦5,000,000 (five million naira only) from a bank in January 2007 to finance the acquisition of plant and machinery and repays the money in December 2007, a lot of people may not see the difference between the ₦5,000,000 in January 2007 and the other ₦5,000,000 in December 2007. But in real terms, the two sums of money do not have the same value because of what is known as the time value of money. In this Unit, we shall discuss the concept of the time value of money which is very important. The applications of the time value of money will feature repeatedly throughout this be course. Understanding the concept will be useful to you as you go along in your study.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- discuss the concept of the time value of money
- explain the methods used to adjust the impact of time on money

3.0 MAIN CONTENT

3.1 Time Value of Money

In practical terms, time usually separates the firm's receipt of cash and its disbursement of cash in its day to day operations.

Expenditures and other movements of cash out of the firm are usually termed outflows of cash while revenues and other movements of cash into the firm are termed inflows. Outflows and inflows are separated usually by time. But it is important to recognize the fact that the inflows that a firm expects to receive and the outflows should be logically comparable especially if they are separated by time. To explain the time value of money, we shall proceed by discussing the time preference for money.

3.1.1 Time Preference for Money

A rational person who is offered to collect the sum of ₦1,000,000 in January 2007 or December 2007 would prefer to collect the money in January 2007 instead of December 2007. There are many reasons for this namely:

The future is uncertain and anything can happen to cancel the opportunity of receiving the money later. The desire to spend now instead of later. The money could be invested immediately to earn interest. Most people know profitable avenues to invest money. This attitude of preferring money now instead of in the future is referred to as an individual's time preference for money.

So we shall define "time preference for money" as an individual's preference for possession of a given sum of money now rather than at a future date.

The concept of the time preference for money does not apply only to individuals. It also applies to the firm. Firms are usually supposed to be rational investors and therefore properly recognize time preference for money. Ordinarily, a firm recognizes the fact that a future cashflow involves a lot of risks which arise from the market place.

3.1.2 The Time Preference Rate

We have recognized the fact that the same sum of money separated by time may not have the same value for a rational investor. If the time value of money exists, is there any way that it can be expressed? Yes. The time preference for money is usually expressed by an interest rate. This interest rate is usually known as the time preference or discount rate. This discount rate is very important in investment analysis and evaluation. Different individuals or firms will have different discount rates. But in all, the discount rate is expressing the same thing.

For example, if an individual has a time preference rate of 20%, it means that he can forgo the opportunity of collecting ₦1,000,000 now if he is offered ₦1,200,000 a year later. It means he is going to be satisfied by earning 20% interest on his investment. Also firms have their own time preference rates which assist them in taking their investment decisions. As we shall see in subsequent units, the discount rate is a very crucial rate which cannot be glossed over in financial evaluations.

SELF-ASSESSMENT EXERCISE

How is the time preference for money expressed?

3.2 Compound Value

Consider an individual called Peter Panwhoon 1st January, 2007 deposits the sum of ₦1,000,000 in a savings account in Diamond bank at an interest rate of 10% per annum. By31st December, 2007 the savings deposited with the bank would have earned an interest of ₦100,000 (one hundred thousand naira only). You will recall that in financial analysis, interest 1 = P x T x R

Where

P = Principal
T = Time
R = Interest rate

By the end of December 2007, the value of Peter Pan's money in his savings account will be ₦1,000,000 + ₦100,000 = ₦1,100,000. On 1stJanuary2008, Peter Pan may decide to reinvest his money (₦1,100,000) in the same savings account in his bank. This sum will grow at the interest rate of 10% per annum. By 31st December 2008, the money would have grown to ₦1,210,000 (one million two hundred and ten thousand naira only).

So generally if the investor (in this case Peter Pan) insists on earnings interest on his original sum ₦1,000,000 and also further interest on his interest of ₦100,000 earned for the year 2007, the concept is known as compound interest. Having understood the concept of compound interest, we will go a step further to examine the various forms that compound interest may take.

3.2.1 Compound Value of a Lump Sum of Money

Let P = Lump sum placed in a savings account
r = Interest rate in decimal points e.g. 0.100
n = no of years the sum is placed then I (interest) = P x r x n

At the end of one year, the total sum of the previous lump sum can now be called A1.

A1 = P + 1 (principal + Interest)
= P + Pr n, where n = 1
A1 = P (1 + r)

In year 2, Interest 1 = A1. x r = A1 . r

The Sum at the end of year 2 now called A2 is

A2 = A1 + A1 .r (the Interest Component)
A2 = A1 + A1. r = A1 (1 + r)

If we continue the process to n years,

We can now write generally that:

An= P (1 + r) n. So generally, the equation for calculating the future value of a lump sum may be written as follows:

An = P(1 +r) n

Worked Example

A sum of ₦1000 is placed in a savings account that promises10% interest annually.

What will be the compound value at the end of 2years.

Note that 10% interest rate is also 0.10

Solution

Interest in year 1 can be derived as follows: 1 = P x r x n

= ₦1000 x 0.10 x 1

= ₦100

A1 (amount at the end of year 1) = N1000 + N100 = N1,100

The principal sum at the beginning of year 2 is N1,100

Interest in year 2 = A1 .r

= ₦1,100 x .10

= ₦110

A2 (amount at end of year 2) = A1 + A1. r = ₦1,100 + ₦110 = ₦1,210

Using the formula, the compound value of the same amount can be computed by

A2 = P (1 + r) 2

= ₦1,000 (1 + 0.10) 2

= ₦1,000 (1.21) = N1,210 If you have followed this discussion very closely you will realize that if the number of years that a sum is invested is very long, the computation becomes rather difficult.

The solution can be obtained by the use of compound value tables. Generally, to compute compound value, the principal sum (Lump Sum) is multiplied by the appropriate compounding factor.

Worked Example

A man deposits N50, 000 in a bank deposit paying 10% per annum for a period of 5 years. What is the compound value of the sum of the end of 5 years?

Solution

The first step is to determine the compounding factor from the table. Since the interest rate is 10%, open to the page for 10% under compound factor.

In the year column, the appropriate year is 5.The corresponding compound value factor is 1.610510.

Multiply the principal sum by the compound value factor i.e. ₦50,000 x 1.610510

= ₦80,525.50

3.2.2 Compound Value of an Annuity

We have discussed the compound value of a lump sum of money. We will now discuss the compound value of an annuity.

An annuity is a sequence of periodic equal payments. Ordinarily an annuity may be paid at the end of say each year. In investments, interests are also paid on the annuities.

The difference between a lump sum and an annuity is that while a lump sum is one sum that increases with interest and time, and annuity is paid at the end of a period possibly a year.

Example

On 31st December of each year, International Manufacturing Company Limited pays in the sum of ₦5,000 into an Investment fund yielding 10% interest annually for a period of 5 years. How much is the worth of the annuity?

Solution

You will need to use the compound value of an annuity table to get the answer. From the compound value of an annuity table, you get the compounding factor to be 6.105100.

The sum of the annuity will be ₦5,000 x 6.105100
= ₦30,525.50
The interpretation of this is that if you invest ₦5000 annually for 5 years at an interest rate of 10%, the sum of money will grow to ₦30,525.50 at the end of five years.

3.3 Present Value

When we treated compound value, we arrived at a technique for estimating any amount of cash into its future value. In the present value technique it is the opposite. The central question to be asked is "What is the present value of a future sum of money given an investors time preference rate?

The present value of a future cash inflow or outflow is defined as the amount of current cash that is of equivalent desirability, to the decision maker, to a specified amount of cash to be received or paid at a future date.

3.3.1 Present Value of a Lump Sum

We have seen so far in our discussions that cash inflows and outflows that are separated by time can be logically comparable.

They are comparable only if there is a time preference rate or interest rate being used by the decision maker or investor.

By implication, if a person is promised a sum of money in the future, it must also have a present value for the person today.

We shall define present value of any future cash inflow or outflow as the amount of present cash that has an equivalent value with a sum to be received at a future date or spent in the future.

You will recall that when treating compound value, we said that the compound value of a lump sum of money is usually expressed by the equation: An = P (1 + r) n

Substituting for P becomes

P = An
(1 + r) n

P is the present value of an amount An to be received in n period.

Generally we can state thus:

To get the present value of any future amount, all that you need to do is to multiply the future amount by the discount factor.

You will need to refer to a discount factor table to be able to do this.

Example

A sum of ₦1000 is to be received by Mr. Bola in 5years time. The interest rate or discount rate is 10%.

What is the present value of the ₦1000 that will be received in 5years time?

Solution

The first step is to get the correct discount factor. The correct discount factor can be got from the discount table. Open the section on 10% in the table. You will notice that the appropriate discount factor is .620921 (from the year 5 column).

Present value = ₦1,000 x . 620921

= N620.921.

The Interpretation given to this result is that N620.921 today is the same as ₦1000 to be received in 5years time if the interest rate is 10% per annum.

Generally thus, to estimate present value of a lump sum, the basic technique is to multiple the future sums by the discount factor.

You can now write thus:

PV (present value) = future sum x discount factor.

3.3.2 Present Value of an Annuity

We have just discussed the present value of a lump sum of money.

In that same way, we could equally discuss the present value of an annuity.

You will recall that we have earlier defined an annuity to be a sequence of periodic equal payments. Since the payments are made at the end of each period, it is possible to compute the present value of an annuity.

Consider an investor who receives a series of annuities A1 indifferent years.

In year 1, he receives an annuity. In year 2, he receives an annuity. We can write that the present value of all the annuities can be estimated thus:

Year1. Present value of annuity = A

1+ r

Year2. Present value of annuity = A

(1+ r) 2

Year 3. Present value of annuity = A

(1+ r) 3

If we add up all the present values, we will get the total present value of all the annuities.

However you will realize that if the number of years involved is very large, then the calculation of the present value of an annuity becomes rather difficult and cumbersome.

The computation of the present value of an annuity can be made easier with the use of an appropriate table known as the present worth ofan annuity factor table.

Example

At the end of 31st December of each year Alhaji Bashir deposits ₦500 into his bank savings account for a period to cover 15 years. The interest rate is 8% per annum. What is the present value of the annuity?

Solution

The first step is to get the correct present worth of an annuity factor.

From the table, the factor is 8.559479.

Present Value of annuity = ₦500 x 8.559479
= ₦4,279.7395

SELF-ASSESSMENT EXERCISE

Laraba is 25 years old. How much should she invest each year so that by the age of 40, she would have the sum of ₦100,000 in her savings account in the bank. The interest rate is 10% per annum.

3.3.3 Present Value of a Perpetual Annuity

When we discussed the present value of an annuity, we did attach a time frame. However, there are situations where annuities are expected to run for ever.

When a series of constant periodic sum (annuities) is expected to be go on perpetually (forever), the perpetual constant periodic sum is called a perpetuity.

Let A = Perpetual Sum of money

r = Interest rate

Then P (Present value of a perpetuity) = A r

Example

Harry expects to receive a perpetual sum of ₦500 annually from his investment in shares. What is the present value of this perpetuity if his time preference or discount rate is 10%.

Solution

The present value of the perpetuity can be determined thus ₦500

P = r or 0.10

P = ₦5000

The present value of the perpetuity is ₦5000.

3.3.4 Sinking Funds

Most often, it is very difficult to raise money at very short notice. And so, most forward looking firms plan their investments so that acquisition of much needed equipment will not be problematic. Such firms keep money aside periodically to purchase or replace equipment.

When such a fund is created, it is called a sinking fund. Also when a country borrows money from other countries, it is fair to create a sinking fund to accumulate the value of the principal loan amount and interest as at the target date of repayment.

Example of Sinking Fund

Master Ebo is 8 years old. In the next 10 years, he will enroll at the University of Ibadan to read medicine. His father intends to save ₦250,000 for his University education by Investing in an industrial stock yielding 10% interest.

How much should Ebo's father invest annually so that he will be able to get ₦250,000 for his son's education in the next 10 years.

Solution

The most important step is to determine the sinking fund factor from the table. From the sinking factor table, the appropriate sinking fund factor is 0.062745.

₦250,000 x 0.062745 = ₦15,686.25

Sum required for Sinking fund money to be invested master Ebo's factor for 10 annually by Ebo's father education years at 10%

ANSWER TO SELF-ASSESSMENT EXERCISE

1. The time preference for money is usually expressed by an interest rate. This interest rate is usually known as the time preference or discount rate. The discount rate varies between Individuals.

2. The difference between 40 years and 25 years is 15 years. The future sum Laraba expects is ₦100,000. Let the amount she will invest annually be A

₦100,000 = A x Compound value of annuity at 10% for 15 yrs
₦100,000 = A x 31.772

A = N 100,000 31.772

A = N3147.43.
So Laraba will need to invest ₦3147.43annually for 15 years so as to get N100, 000 by the time her age will be 40 years.

4.0 CONCLUSION

In this first unit, we have discussed fully the concept of time value of money which is very crucial in our study. We also looked at time preference for money. We treated compound values and also annuities. Finally, we discussed sinking funds.

5.0 SUMMARY

This unit treats the time value of money, time preference for money, compound value of a lump sum of money, compound value of an annuity, present values of an annuity and perpetuities.

All these provide us with the necessary background for further discussions. Now that the background has been built, in the next unit, we shall discuss Basic Valuation Models

6.0 TUTOR-MARKED ASSIGNMENT

1. Why is the consideration of time important in financial decision making?
2. How can time be adjusted?

7.0 REFERENCES/FURTHER READINGS

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MODULE 3

UNIT 1 DISCOUNTED CASH FLOW CRITERIA

CONTENTS

1.0 INTRODUCTION

In previous units the two approaches for investment appraisal were discussed. We also examined their advantages and of course their deficiencies. In this unit we shall discuss Discounted Cash Flow Criteria.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- understand discounted cash flow criteria in investment decision making
- discuss their practical applications

3.0 MAIN CONTENT

3.1 Discounted Cash Flow Criteria

Our task in this unit is to discuss investment criteria that recognize the time value of money in evaluating investment proposals. The two methods are the net presentvalue(NPV) method and the internal rate of return (IRR) method. As a group they are known as the discounted cash flow methods. We shall now devote more time discussing them.

3.1.1 The Net Present Value (NPV) Method

The net present value method is the most admired amongst thediscounted cash flow methods of evaluation. This is so because it recognizes the time value of money. At the background,it correctly postulates that cash flows which arise at different periods have different values. And that they can only be comparable when their present values have been computed.

In the analysis, there are three basic steps to be taken to compute the net present value (NPV).

First, an appropriate rate of interest is selected which will be used to discount cash flows. Technically, the appropriate rate of interest to be used is the firm's cost of capital which as we said is theminimum rate of return expected by the investors to be earned by the firm on any of its investment proposal.

Secondly, the present values of investment proceeds (inflows)are computed and the present values of investment outlays (outflows)are computed also using the cost of capital as the discount rate.

Thirdly, the netpresentvalue (NPV) iscomputed by subtracting thepresent value of cash outflows from the present value of cash inflows. If the present value of cash inflows is greater than that of outflows, then the project has a positive net present value. However if the present value of cash inflows is lesser than the present value of cash outflows, then the net present value of the investment proposal will be negative. We shall now proceed to define the net present value NPV method.

The net present value method is a process of calculating the present value of cash flows (inflows and outflows) of an investment proposal using the cost of capital as an appropriate discount rate.

And like we said, the net present value is found out by deducting the present value of cash outflows from the present value of cash inflows.

Assuming that all cash outflows of an investment are made in year to, then the equation for the net present value is given by:

NPV = A1 + A2 + … + An - C (1+ k) (1+ k) 2 (1+ k) n

Where A1, A2 … + + An = Cash inflows

K = the firm's cost of capital C = cost of the investment proposal n = expected life of the investment proposal

Under the net present value method, the acceptance rule is to accept the investment proposal if the net present value (NPV) is positive and to reject it if the net present value is negative.

Worked Example

A bakery project costs ₦2,000, 000 to set up and generates yearend cashinflows of ₦800,000, ₦900,000, ₦1,000,000 and ₦800,000 over a four year period .The required rate of return is 10%. Calculate the Net present value of the bakery project.

Solution

Year Cash Inflow Discount Factor Present Value at 10% of Cash Inflow (₦) 1. ₦800, 000 .909 727,200 2.₦900, 000 .826 743,400 3.₦1,000,000 .751 751,000 4. ₦800, 000 .683 546,400 2,768,000

Less Project Cost 2,000,000

Net Present Value = 768,000

3.1.2 Interpretation of Net Present Value (NPV)

We have used the example of the bakery project to compute net present value (NPV). But we need to understand what NPV is and be able to interpret it.

The positive net present value may be interpreted as the immediate increase in the firm's wealth if the investment proposal is accepted. It is equivalent to an unrealized capital gain. The unrealized capital gain will be when the expected cash inflows materialize.

3.1.3 Evaluation of Net Present Value Method

We have discussed the net present value concept and used an example to compute the NPV of a project. We shall go ahead to evaluate NPV method.

The most important merit of the NPV method is that it recognizes the time value of money. Also it considers all the cash flows that arise throughout the duration of the investment project. The NPV method is consistent with the objective of maximizing the objective of the firm.

However the Net present value method suffers from some limitations. Firstly, it is difficult to use. It involves the use of discount tables and also computers.

Secondly, in calculating NPV, it is assumed that the appropriate discount rate is known. The discount rate to be used is the firm's cost of capital. The cost of capital is not very easy to compute. The NPV method may not give satisfactory answers when the projects in question have different initial outlays.

NPV result may be misleading when we are dealing with alternative projects – under capital rationing situations.

3.2 The Internal Rate of Return (IRR) Method

We have discussed the net present value method and did a computation of NPV. We shall now discuss the internal rate of return (IRR) method.

The internal rate of return is another discounted cash flow technique which recognizes the time value of money and apparently the magnitude and timing of cash flows.

The internal rate of return (IRR) can be defined as that rate which equates the present value of cash inflows with the present value of cash outflows of an investment. At that rate (IRR), the net present value of the investment is zero (0).

It is called an internal rate because it depends entirely on the outlays and inflows of the investment and not any other rate outside the investment. If we write the equation;

$$C = A1 + A2 + \ldots An$$

(1+ r) (1 + r) 2 (1 +r) n
Where C = the Investment outlay

A1, A2 + + … An = Cash inflows

Then 0 = A1 + A2 + …. An __ C
(1+r) (1+ r) 2 (1 +r) n

The value of r in the equation where the cash inflows and the investment outlay is zero is known as the internal rate of return.

Under the internal rate of return (IRR) method, a project is accepted if the internal rate of return is higher than or equal to the minimum required rate of return. This minimum required rate of return is known as the firm's cost of capital.

3.2.1 Interpretation of IRR

The interpretation of IRR is that it is the highest rate of interest that a firm will be ready to pay on the funds borrowed to finance a project without being financially worse off after repaying the principal and interest. In a technical sense, the IRR is the break – even rate of borrowing from a bank.

Obviously if a firm is able to borrow at a rate lower than the internal rate of return, the investment project will be profitable.

3.2.2 Measurement of Cash Flows

In the earlier section of this unit, we discussed two of the discounted cash flow methods – the Net present value (NPV) and the internal rate of return (IRR) methods. And we saw that the two methods used information on cash flows for the investment analysis.

In discussing both methods, we discussed cash inflows and cash outflows. But at this point in time, we are going to take a technical look at cash flows and make sure we understand how they are used in the investment analysis.

A lot of students do confuse profit and cash flows. And so we must first draw a line between the two. Changes in profits may not lead to changes in cash flows.

Increase in profit may be tied up in credit sales with no increase in cash flow. So a firm may be very profitable but at the same time will be experiencing severe cash flow problems.

So it is to be stated that in the Investment Analysis, it is the inflows and outflows of cash that is important. In an ideal situation, the receipt of cash is a clearly defined corporate objective.

3.2.3 Depreciation and Cash Flows

In computing cash flows, the net cash flow is usually on an after – tax – basis. That is to say that taxation should be deducted before arriving at the net cash flow. In the computation of after-tax net cash flows, the treatment of non-cash items deserve special treatment. One of those non-cash items is depreciation. Depreciation is a way of allocating cost of fixed assets. In accounting, depreciation is usually charged to the profit and loss account as a way of matching cost of fixed assets with their benefits. Depreciation however does not involve any outflow of cash. And so depreciation is usually ignored in cash flow computation. And in a situation where depreciation has been deducted before arriving at profit after tax, the practice is to add back depreciation to arrive at after tax net cash flow.

Worked Example

Below is the projected income statement of Fellowship Aluminum Limited. Compute the net cash flow after taxation.

Note: The Company has an outstanding loan for which it pays ₦10, 600,000 per annum.

PROJECTED INCOME STATEMENT FELLOWSHIP ALUMINIUM LIMITED

YEAR ENDING 31/12/ 2007	N REVENUE
Sales revenue	839,280,000
Direct Cost of Production Production raw materials	567,927,360
Electricity and gas	6,880,000
Repairs and maintenance	500,000
Depreciation of machinery	3,346,000
TOTAL DIRECT COSTS	578,653,360
INDIRECT COSTS Management and Labour	2,508,000
Interest and bank charges	3,000,000
Selling expenses	7,250,000
Insurance of assets	50,000
TOTAL INDIRECT COSTS	12,808,000
TOTAL DIRECT + INDIRECT COSTS	591,461,360
PROFIT before taxation	247,818,640

Taxation	74,000,000
Profit after taxation	173,818,640

PROJECTED CASH FLOW STATEMENT FELLOWSHIP ALUMINIUM LIMITED

CASH INFLOWS	**N**
Profit before taxation	247,818,640
Add back depreciation	3,346,000
Total cash inflows	251,164,640

CASH OUTFLOWS	**Loan**
repayment	10,600,000
Taxation	74,000,000
TOTAL OUTFLOWS	84,600,000
Cash inflows less cash outflows	166,564,640
Opening cash balance	-----
Closing cash balance	166,564,640

3.2.4 Fixed Assets and Cash Flows

After treating depreciation, another item which we need to understand properly is fixed assets. What we are really interested in is the treatment of the purchase of fixed assets. In the cash flow analysis, when an asset is purchased, the purchase cost is treated as an outflow. The entire purchase price is an outgoing.

3.2.5 Salvage Value and Cash Flows

When we talk of salvage value, we are talking of the estimated value of an asset at the completion of its useful life for the firm. Normally, salvage value is of two types namely:

- Book salvage value is the cost of the asset at the end of its useful life.
- Cash salvage value is the market value of the asset at the end of its useful life.

SELF-ASSESSMENT EXERCISE

List four expense items that you consider as cash outflows in a firm's profit and loss account.

ANSWER TO SELF-ASSESSMENT EXERCISE

Four expense items I consider as cash outflows in a firm's profit and loss account are:

1. Salary and wages 2. Raw material expenses 3. Advertising expenses 4.Telephone expenses.

4.0 CONCLUSION

In this unit, we have discussed discounted cash flow criteria. We discussed the net present value (NPV) and the internal rate of return (IRR).

5.0 SUMMARY

In this unit, we have treated discounted cash flow criteria which are more sophisticated than the traditional criteria. We also discussed cash flows.

In the next unit, we shall discuss net present value (NPV) Vs internal rate of return (IRR).

6.0 TUTOR-MARKED ASSIGNMENT

A hospital costs ₦5,000,000 to set up and generates year end cash flows of ₦1,000,000, ₦1,500,000, ₦2,000,000, ₦3,000,000. The cost of capital is 10%. Calculate the Net present value of the hospital investment.

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UNIT 2 NET PRESENT VALUE (NPV) VS INTERNAL RATE OF RETURN (IRR)

CONTENTS

1.0 INTRODUCTION

In this unit, we shall discuss Net present value (NPV) Vs the Internal rate of return. The relevance as well as peculiarities of these important methods of appraising investment shall also be discussed.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- compare the Net present value (NPV) with the Internal rate of return (IRR)
- identify the source of their differences.

3.0 MAIN CONTENT

3.1 Net Present Value (NPV) Vs the Internal rate of return (IRR)

In our earlier studies we discussed the net present value (NPV) method of investment evaluation. The net present value method is a process of calculating the present value of cash flows (Inflows and outflows) of an investment proposal using the cost of capital as an appropriate discount rate. We also discussed the internal rate of return (IRR).

We defined the internal rate of return (IRR) as the rate which equates the present value of cash inflows with the present value of outflows. At that rate, the net present value of an investment is zero (0).

We note that the net present value and the internal rate of return are closely related as discounted cash flow methods.

Firstly, both are time-adjusted methods for measuring the worth of an investment.

But the two methods do not invariably lead to the same decisions – accept or reject. It is the source of the differences that we now want to examine as evaluators.

3.1.1 Equivalence: Independent Projects

As a starting point, we shall first distinguish between what is known as conventional and non-conventional investments. In the analysis a conventional investment is defined as one whose cash flow take the pattern of an initial cash outlay (Outgoing) followed by cash inflows. Therefore the conventional investment will have only one change in sign.

For example a conventional investment may be stated thus: - + + + + …

Where – represents the initial cash outlay and + represents the cash inflows.

Truly when the investment is undertaken, it is followed by spending of financial resources called outlays. After the investment has been undertaken, what follows is the return in the form of cash inflows.

Now let us look at a non-conventional investment. A non-conventional investment is one whose cash outflows are not restricted to the initial period. For example a non-conventional investment can be expressed thus: - + + + - - + +

Where – represents cash outflows and + represents cash inflows.

If you examine the cash flow pattern of the non-conventional investment, you will note that a cash outflow can occur at any time and not only at the commencement of the investment.

Generally, we can state that in the case of conventional investments which are economically independent of each other, the net present value (NPV) and internal rate of return (IRR) methods result in same accept or reject rules if the firm is not constrained in any way in accepting all the profitable projects.

Put in a simpler way, what we are saying is that if the firm has all the funds it requires for investment, and has an array of conventional investments facing it, both NPV and IRR methods will arrive at consistent accept or reject decisions.

If a project is indicated to be profitable by the NPV method, then the IRR method will also indicate it to be profitable. In that case, we say that both methods are showing consistency. The reason is not farfetched.

You will recall that we stated earlier that if the NPV method is used, all projects having NPV greater than zero (NPV > 0) would be accepted.

Similarly, we also stated that all projects for which the internal rate of return is greater than the required rate of return (r > k) will be accepted if the IRR method is used. The last or marginal project to be accepted under the NPV method is that which has zero (0).

NPV i.e. (NPV = 0). Also if we are using the IRR method, the last or marginal project to be accepted will have internal rate of return equal to the required rate of return (r = k).

Therefore it is easy to picture that any project which has a positive net present value (NPV) will have the internal rate of return greater than the required rate of return.

3.1.2 Difference: Ranking of Dependent Projects

We have seen that the NPV and IRR methods arrive at the same accept or reject decisions when conventional independent projects are being evaluated. However, they tend to yield differences when ranking dependent projects or investments. Practically the firm does not always have the resources to undertake all of the investment proposals brought before it.

So that when faced with a variety of projects, accepting a project will mean not accepting the other projects. That leads us to the concept of mutual exclusiveness.

Investment projects are said to be mutually exclusive if acceptance of one investment completely eliminates the expected proceeds of other investments. For example a car manufacturer has to choose between making and buying tyres. Also a distributor of baby food has to choose between selling through distributors or through direct sales to the consumers.

Also there is what we refer to as financial exclusiveness. If a firm has a financial constraint, it will not be able to accept all investment projects. It will either accept Project A or Project B. In such a situation, we say that there is financial exclusiveness or capital rationing.

Under a situation of mutually exclusive projects, the NPV and IRR can give conflicting ranking to projects submitted for evaluation.

Worked Example

There are two investment proposals A and B facing a firm. Project A involves a capital cash outlay of ₦20, 000 and year end cash inflow of ₦24, 000. Project B involves a capital outlay of ₦30, 000 and year end cash flow of ₦35, 400. If the firm's cost of capital is 12%, which of the investment proposals should the firm accept if it uses NPV and IRR methods of project evaluation?

Solution

Project A

Cash Inflow Discount Factor At 12%
Present Value (N) N 24,000 0.893 21,432
Less initial cash outlay 20,000
Net Present Value = 1,432

Project B

Cash Inflow Discount Factor At 12%
Present Value (N) N 35,400 0.893 31,612.20
Less initial cash outlay 30,000.00
Net Present Value = 1612.20

SUMMARY OF RESULTS Project Cash outlay (N) Inflow (N) NPV at 12% IRR (%)
A. 20,000 24,000 N 1432 20%
B. 30,000 35,400 N 1612.20 18%

You will note that if Project A and Project B are independent projects, both of them will be acceptable by both NPV and IRR methods.

However if they are mutually exclusive projects then NPV and IRR can give us conflicting results. It is important to note this fact.

It is seen from the result that under the NPV method, Project B has a higher net present value and is ranked higher than Project A.

However, if the IRR method is used to evaluate the two projects, Project A will be ranked higher than Project B.

3.1.3 Sources of Conflicting Results -NPV Vs IRR

We have just seen through the last example that under exclusiveness, the NPV and IRR will give conflicting results when ranking projects.

The conflicting results arise under the following conditions:
Projects have different expected lives.

The life span of a project goes a long way to determine the nature of the cash flows and how they affect both NPV and IRR computations.

Different capital outlays

Another condition under which NPV and IRR will yield conflicting ranking of projects is when the outlays of projects are of different sizes. Differences in capital outlay for projects usually lead to conflicting ranking of the projects using the NPV and IRR methods.

Differences in cash flow pattern

Another condition under which the NPV and IRR will yield contradicting results is where the cash flow patterns are different. In some projects, the cash inflows may arrive earlier than in other projects. Some projects are like that.

3.1.4 Incremental Approach

The apparent conflict between the NPV and IRR methods of evaluation can be resolved through using the incremental approach.
Consider for example two projects with the following cash flows
Cash Flows (N).

t0 t1 t2 NPV at 8%

IRR Project A - 20,000 20,000 4,800 2,633 20%

B - 30,00020,000 16,680 2,818 15%

It is to be observed that the incremental project is called Project B – A, and the incremental cash flow is expected thus:

Incremental Cash Flow (N)

t0 t1 t2

IRR Project (A- B) -10,000 0 11,880 9%

We need to perfectly understand what we are trying to reach at. You will note that Project A has a lower NPV (N 2633) but a higher IRR at 20%. Project B has a higher NPV (N 2818) but a lower IRR.

Under the incremental approach, we can define a project called B - A. Project B- A is an algebraic deduction of Project A from Project B.

Ordinarily one would be tempted to prefer Project A under the IRR method because it has an IRR of 20%. But if you take a critical look at the incremental project, Project B-A, you will realize that the incremental project offers an extra 9% IRR over and above the 20% offered by project A. So one would be inclined to prefer or select Project B-A.

As far as the NPV and IRR conflict exists, the most satisfactory solution is to use the incremental approach. A good financial manager should be interested in evaluating the impact of incremental cash flows on the investment proposal.

SELF-ASSESSMENT EXERCISE

Project A has outlay of ₦30,000 and cash inflow of N50, 000. Project B has an outlay of ₦50, 000 and cash inflow of ₦90,000. What is the incremental project?

3.1.5 NPV AND IRR: Choice of Method

We have discussed the NPV and IRR methods. Although both methods are discounted cash flow methods, they give conflicting answers under conditions of capital rationing or financial exclusiveness. So the key problem facing financial decision makers is that of choosing between the two.

The NPV gives a consistent solution to investment analysis problems. This is because it gives a figure known as NPV which can be easily comparable. It is also easier to compute and so many analysts prefer to use the NPV method in their analysis.

On the other hand, some other analysts prefer to use the IRR method. First, IRR appeals a lot to businessmen because it is a rate that can be used to compare with a required rate of return. It is therefore according to them, easier to understand IRR than Net Present Value. Also in the IRR method, the analyst is saved the problem of calculating the cost of capital which is the starting point of the NPV analysis.

ANSWER TO SELF-ASSESSMENT EXERCISE

The incremental project is Project B-A. It can be expressed thus:

t0 t1 Project (B-A) - ₦20,000 ₦40,000

4.0 CONCLUSION

In this unit, we have discussed the Net Present Value (NPV) Vs the Internal Rate of Return (IRR).We tried to look at the sources of conflict between the two methods. There unique roles in investment appraisal were also discussed.

5.0 SUMMARY

The NPV method and the IRR method are both discounted cash flow methods used in the investment analysis and evaluation. This unit treated comparison between the methods, bringing out their differences. It also traced the sources of their apparent conflicting solutions to the investment decisions. In the next unit, we shall discuss Risk Analysis in Capital Budgeting.

6.0 TUTOR-MARKED ASSIGNMENT

In the cases of financial exclusiveness, the IRR and NPV do not yield consistent answers in evaluating projects. What are the reasons for the inconsistencies?

7.0 REFERENCES/FURTHER READING

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UNIT 3 COOPERATIVE BANKS

CONTENTS

1.0 INTRODUCTION

A cooperative bank is a financial institution specially set up to offer greater access to savings and borrowing facilities for cooperative societies and their members at relatively cheaper costs. A cooperative bank can be defined as a cooperative society carrying on the business as other banks but in such a manner that they fill the financial gaps created by the conservative financing practices of other commercial banks:

2.0 OBJECTIVES

At the end of this unit, you should be able:

- explain the characteristics of cooperative banks.
- discuss the objectives of cooperative banks.

3.0 MAIN CONTENT

3.1 Characteristics of Cooperative Banks

i. Being service-oriented and not profit-oriented, they can operate at minimal profit and cheap credit to the farmers. Moreover their funds cannot be channeled into projects other than those set up by their members and hence the opportunity cost of agricultural finance is nil.
ii. Being rural-based their administrative charge will not be as high as those of commercial banks since their staff do not need additional training In rural banking.
iii. Being intimate with the borrowers, their procedures need not to be as intricate as those of commercial banks. Infact their procedures readily explained by their staff to the illiterate farmer borrowers.

iv. Being acquainted with the borrowers business and his character, they can easily evaluate the viability of his proposal and need not insist on adequate security.
v. The incidence of bad debts among the borrowers of cooperative banks are less because a defaulter is likely to face loss in the circle of his friends and relations who are all members of bank. Hence recovery cooperative bank advances is achieved through extra-legal means.
vi. Being rural-based, cooperative banks can monitor the advance more easily thereby reducing the possibility of banking frauds like diversion of funds.
vii. Although they initially receive a helping hand from the state, the rural cooperative bank can gradually generate their funds so that in the long run they will not suffer the burden of subsidizing credit to agriculture. Thus rural cooperative bank are ideal financial institution of poor, by the poor, and for the poor.

3.2 Objective of Cooperative Bank

Cooperative bank has among other things the following objectives:

i. To operate as a secondary financing agency for securing finance from available resources to cater for the needs of the registered cooperative societies within its operational area.
ii. To promote thrift among its members by offering them an opportunity to accumulate their savings.
iii. To develop, assist and co-ordinate the financial aspect of registered societies within the area of operation.
iv. To have power to accept savings and/or deposits from members.
v. To have the power to contract financially with the approval of the Registrar on behalf of cooperative societies and to pledge assets of the societies.
vi. To have the power to invest or dispose of the surplus funds of the societies in the overall interest of the cooperative movement.
vii. To have the power to borrow for the purpose of its business from sources whatsoever with the approval of the Registrar.
viii. To have the power to acquire assets of any nature in the interest of the bank considered necessary, and conducive to the nature of their business.
ix. To harness all available resources within the cooperative movements for the overall benefits of all the members and to undertake other work that will promote the cause of cooperation.

4.0 CONCLUSION

In this unit, cooperative banks are seen as financial institutions carrying on the business as other banks but in such a manner that they fill the financial gaps created by the conservative financing practices of other commercial banks. The peculiar characteristics of cooperative banks as well as their objectives were explained.

5.0 SUMMARY

Students can appreciate the role of cooperative bank more when they situate the operations of these banks in rural areas. They play significant role and exhibit flexibility, balancing economic motives with social and friendly services. Cooperative banks have emerged into a potent tool in financial inclusion and poverty reduction in many developing economies.

7.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the concept of the time value of money.
2. Explain the methods used to adjust the impact of time on money.

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UNIT 4 PROBLEMS OF LOAN REPAYMENT IN COOPERATIVE BANKS

CONTENTS

1.0 INTRODUCTION

Previously, we discussed cooperative banks, its characteristics and its objectives. In this unit, we focused on the problems encountered during loan repayment in cooperative banks.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- ascertain the problems of loan repayment in cooperative banks.
- help to proffer advice both to the bank and clients on how to minimize default

3.0 MAIN CONTENT

3.1 Absence of Non Factual Project Feasibility Studies

Feasibility studies are very necessary in establishing projects and in obtaining loan from any financial institutions.

Basically, feasibility studies shows all the expenses to be made and mote to determining the viability of the project through economic indicators such as net present value (NPV) internal rate of return (IRR), benefit cost ratio (B/C). In the absence of non-factual project feasibility studies, it will be difficult to determine the viability of the project. If it happens that loan is obtained for such a project, there will be a high probability of the project not yielding a good result and the resources committed will not be recovered. Invariably, the society that owns such a project will stand to default.

3.2 Giving Loan to Societies when not required

It is not uncommon to observe that some societies obtain loan when they do not need them or the loan are received when the operational periods have elapsed. They may divert such loan to non-profit projects, which may be difficult to recover for repayment.

3.3 Attitude of Societies to Loan

Some cooperative regards loans especially loans from the government as 'national cake'. They have the misconception that securely getting the loan is their own share of the national cake, they therefore share the money and deliberately refuse to repay when such loans are due.

3.4 Illiteracy of Co-Operators

Many of the co-operators are illiterates and most of them are poorly educated. Hence they are not in a position to organize their business activities. Even with a good feasibility report, they find it extremely difficult to adhere to the specification made in the report. Again accurate records of the business are not kept and hence loans are managed and repayment becomes difficult.

3.5 Improper Loan Disbursement and Poor Supervision

Improper loan disbursement and poor supervision could lead to loan default. For instance if the loan is disbursed at a stretch (bulk), it is likely to be mismanaged. Lack of adequatesupervision of the loan by the Agency could result in diversion of the loan and may face repayment problem.

3.6 Lack of Securities for Loans

Submission of securities for securing loans will inspire societies to work harder and make surplus for easy repayment. Loans granted without adequate securities may face repayment problems because the co-operators may not be inspired to work in order to recover the loan and repay as and when due.

i. Poor leadership of the society: Poor leadership may result in poor management of the loanand it may be difficult for the society to repay the loan.
ii. Natural Disaster and Weather vagaries: Natural disaster such as fire outbreak, flooding erosion, oil spoilage pollution etc. and weather vagaries such as draught, too much rain will adversely affect projects carried out by the societies especially the agricultural projects, it may be difficult to recover loan and invariably its payment becomes difficult.
iii. Poor facilities for project performance: Poor facilities in areas where the societies operate especially the rural areas will adversely affect the performance of the project. For instance, unavailability of processing and storage .facilities will result in farm produce losses especially during bumper harvest, which may reduce income. Again lack of spare parts could delay production. All these will affect repayment of loan as and when due.

3.7 Economic Problem

Inflation results in high cost of production and if there is significant fall in prices of farm produce the society stand to less and recovering the capital will be difficult which will affect repayment.

4.0 CONCLUSION

Cooperative banks have been identified with some obstacles which it faces during its period of loan repayment. Some of these obstacles amongst others have been ascertained to be absence of nonfactual project feasibility studies, giving loan to societies when not required, attitude of societies to loan, illiteracy of cooperators, improper loan disbursement and poor supervision, lack of securities for loans and economic problem. Improved understanding of these problems will assist the bank to improve operation and loan administration.

5.0 SUMMARY

In this chapter, we have been able to study and understood some problems faced by cooperative banks during loan repayment. It has been made clear that due diligence and effective monitoring is needed in order to minimize default.

8.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the problems of loan repayment in cooperative banks.
2. Provide solution on how bank and clients can minimize default

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UNIT 5 COOPERATIVE ORGANISATIONAL STRUCTURE

CONTENTS

1.0 INTRODUCTION

Every organizational setup has a structure to which it organizes its activities. Cooperatives likewise have an organizational structure that enables it to manage its activities and comply with statutory provisions. Cooperatives are usually organized in a four tier structure.

2.0 OBJECTIVES

At the end of this unit, you should be able to discuss the cooperative organizational structure.

3.0 MAIN CONTENT

Cooperatives are usually organised in a four tier structure. There are primary (societies), secondary (unions), state and national apexes. In Nigeria each state has a Federation while a Federation of Federations forms the culminating apex. It is called Cooperative Federation of Nigeria (CFN).

3.1 Societies

a. The organization of primary cooperatives into societies at village (rural) level and ward level (urban) is ideal as it permits people who live close to each other to participate in and patronize the society's business. In future, efforts must be made to ensure optimal membership sizes based on the types and functions of Cooperative Societies. This is important to ensure viability and sustainability.

b. One important approach to establishing optimal membership size is to encourage voluntary coalescing of small sized societies doing the same types of businesses within an area. This should be encouraged whenever and wherever feasible.

c. Horizontal linkages between primary societies within and between Local governments and States should be encouraged for mutual benefits, for example, a grain producer cooperative in a northern state should be in touch with a garri processing/consuming society in a southern state. Both will gain from information exchange and price negotiations.

3.2 Unions

The advantages of having primary Societies coming together to form unions are well known. However, future union formations should be voluntary among societies which carry out the same or similar businesses. They should come together voluntarily, not by force. It is hoped that cooperative development will proceed rapidly in all parts of the country so that several unions of similar societies can replace the single union in each Local government area. This will reduce friction and encourage cooperation among cooperatives.

Cooperative unions should henceforth strive to be relevant and to fulfil the felt needs of the societies that make up such unions. The societies will then be encouraged to pay their subscriptions and stop agitation for direct affiliation to an apex (or Federation).

In addition to revenues accruing to them from subscriptions by affiliated societies, Cooperative Unions must have profitable ventures to reduce dependency on the subscriptions.
The unions must act firmly as mouth-piece for the societies that they represent. This will boost their relevance and ensure success.

3.3 Apexes

In the context of the democratic space subsisting in the country, all apexes must be seen to be the outcome of the needs and wishes of members of cooperative societies and unions that form the apex.

The CFN must operate in a way to earn the recognition and respect of all Cooperative apexes nation-wide so that they can make the prescribed subscriptions to it annually.

All unions and other state "apexes" must be affiliated to the State Cooperative Federation. They must make prescribed subscriptions to the Federation and be represented on its Board. Where many unions are involved, a method of proportional (or rotational) representation must be worked out. State apexes must stay relevant to the grassroots societies which form them.

The plethora of apexes at the national and state levels must be critically reviewed to remove the confusion and streamline them for effective administration. Only the relevant apexes which are likely to contribute positively to the overall cooperative development efforts should be retained. The CFN must set in motion the process of this review.

Placement of Cooperative Matters at Federal and State Levels:

Cooperative matters at National and State Levels should be upgraded and placed in full-fledged. Ministry of Cooperatives and Rural Development to facilitate proper coordination and relationship among cooperatives at all levels.

4.0 CONCLUSION

In this unit, we explained the various tiers to which cooperative functions. These tiers were identified as societies at the primary level, unions at the secondary level, the state and then the National apexes. Nevertheless, we clarified that each state in Nigeria consists of a federation while a federation of federations forms the culminating apex called the cooperative Federation of Nigeria (CFN).

5.0 SUMMARY

In this unit, you have been made to understand that cooperatives exist within a four tier organizational structure of primary societies (primary), unions (secondary), state and Apexes. This arrangement enables it to discharge its function and achieve its mandate

6.0 TUTOR-MARKED ASSIGNMENT

Discuss the organizational structure

a) Union
b) Apexes
c) Primary

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MODULE 4

UNIT 1 COOPERATIVE INSTITUTIONS

CONTENT

1.0 INTRODUCTION

Many institutions were established to play important roles among members and in local economies, serving both economic and social purposes. They come in all shapes and sizes and all sectors of the economy performing such functions as providing access to market and building members socioeconomic capacities, providing access to credit and building required skills.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Understand the history and operations of formal financial institutions
- Roles of these institutions in rural credit economy

3.0 MAIN CONTENT

3.1 Formal Financial Institutions

Bank of Agriculture (BOA) formerly called or known as Nigeria Agricultural, Co-operative and Rural Development Bank (NACRDB).

History

- Was established on 6th March, 1973
- Was informed by the experience of frustration and dissatisfaction with the system of Agricultural credit in Nigeria over the years.
- It was established for the provision of medium and long term credit for the creation or expansion of mostly agricultural activities
- This was established by the government to fill the financial gap in the agricultural sector, specifically, low savings, inadequate investment and lack of entrepreneurial skill are among the various factors that necessitated the establishment of BOA

Objectives

As a development finance institution, it was established:

- To deliver credit to the agricultural sector, to the co- operative societies
- To provide agriculture and rural development with finance.
- To improve the income and welfare of Nigerians in the rural areas.
- To contribute to the overall growth and development of the economy
- To mobilize savings from low-income earners and advance it to small scale enterprises
- To provide microcredit
- To provide funds for processing and marketing of agricultural products.

3.2 Lending Operations of Bank of Agriculture

The BOA's major banking function is granting loans. It is also engage in the provision of some non-banking services such as project identification and articulation and the search for the appropriate technical and managerial know-how which will benefit clients. The banks operate three major categories of loan schemes for farmers, though, now greatly improved in its services, and namely:

- The small holder loan scheme
- The on-lending scheme and;
- The investment loan scheme.

The small holder scheme is meant for farmers whose loan requirements are too small, mostly initiated and repayment of both principal and interest completed within two years and this type goes without collateral demand by the bank. The On-lending scheme involves channeling of loans through state government or state apex financial institutions or organization for on-lending to farmers, farmers group or co-.operative or corporate bodies, subject to the state government accepting to guarantee such loans. The loan is granted at a lower rate of interest to the state or its apex organization which in turn on-lends to the ultimate beneficiaries at a mark of rate. Also the investment loan scheme takes care of those farmers whose loan request is bigger in size, this is associated with a lot of requirement from the applicant (Onyemenam, 2013).

3.3 National Cooperative Development Fund

a. A National Cooperative Development Fund (NCDF) shall be set up to provide a major source of cooperative financing. All co-operators shall subscribe to the fund, which will accumulate to form the basis for guaranteeing all cooperative credit transactions. With the fund in place, any society or union will be able to approach a bank or finance house for a loan using the fund as guarantor. In addition to co-operators subscription, the fund's assets shall be increased through government grants, donor funds etc.

b. Private organizations which appreciate the contributions of cooperatives to the democratic governance, the peaceful coexistence and the improvements in the income, the welfare and living standards of large numbers of Nigerians should also be willing to make grants and donations towards the movement's activities. There could also be international assistance in various forms, for example, such united Nations' Institutions like the UNDP, ILO, WHO, FAO could provide assistance to the movement in specific areas of need from time to time. In the past, they have provided specialists to find solution to specific problems or to plan a new venture for the Movement.

3.4 Role of Microfinance Institutions in Rural Economy Credit

This is perhaps one of the most important roles of microfinance banks, as the loans extended are used to expand existing businesses and in some cases to start new ones. According to CBN (2008) microfinance loans granted to clients is increasing from 2007 to date and most of it goes to financing microenterprises in rural areas. Thus improving the entrepreneurial capacity of the farmers.

3.5 Microenterprise Development

It is believed that about 60% of poor people live in the rural areas and 80% of them are farmers and artisans (NBS, 2005). Microfinance banks have been the main sources of funding to these less disadvantaged groups. Rural people are empowered through micro finance loans and services and hence small scale agricultural practice and micro enterprise is development.

3.6 Employment Generation

Agriculture and microenterprise contributes immensely to job creation, and are of particular interest to a microfinance institution in rural areas. Microfinance banks have so far engaged in extending credits and other services to many rural enterprises and hence generating employment and promoting entrepreneurship. The employment generated in the rural areas, "- covers the following areas; barbing, food selling, carpentry, bricklaying, drumming etc.

3.7 Improvement in Skill Acquisition

Improvement of the condition of women through the provision of, skills acquisition and adult literacy is another role played by microfinance banks. This is done through building capacities for wealth creation among enterprising poor people and promoting sustainable livelihood by strengthening rural responsive banking methodology and the introduction of simple cost-benefit analysis in the conduct of businesses.

3.8 Facilitates Poverty Alleviation

Employment and income generation are important aspects of poverty alleviation efforts. Microfinance banks have accelerated the operation of government poverty alleviation programmes and in doing that promising entrepreneurs are supported and new ones emerged. When the entrepreneur organizes production process, they are engaged in wealth creation and subsequent reduction in the level of poverty (Muktar, 2009).

4.0 CONCLUSION

Despite well documented and positive impacts of the rural finance institutions on the livelihood of the rural poor, rural finance should not be considered as a panacea for poverty reduction. It is but one of several important areas for investment in poverty reduction, and its impact is fully felt only when conducive policies are in place, markets are functioning and non-financial services are available. The poorest of the poor and destitute may be more effectively reached through income transfers, safety nets and improved social infrastructure.

5.0 SUMMARY

These financial institutions were established by successive government administration as means of achieving their goals for rural areas. They play important role in mobilizing credit and in building capacities of rural dwellers to enable them pull out of poverty.

5.0 TUTOR-MARKED ASSIGNMENT

1. What are the 3 major challenges of loan scheme for farmers?
2. Discuss each loan scheme

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UNIT 2 RURAL DEVELOPMENT PROGRAMMES IN NIGERIA

CONTENT

1.0 INTRODUCTION

Several efforts have been made towards rural development in Nigeria through the establishment of various programmes like NAPEP, NEEDS and DFRRI. They play critical role in different sectors of the economy, assisting the poor to build capacity and helping government to achieve its rural development goals.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Reasons for establishing these initiatives,
- Their modes of operation and
- Challenges they faced by these initiatives

3.0 MAIN CONTENT

3.1 National Poverty Eradication Programme (NAPEP)

National Poverty Eradication Programme (NAPEP) was established in 2001 as a central coordination point for all anti- poverty efforts from the local government level to the national level by which schemes would be executed with the sole purpose of eradicating absolute poverty. The government arranged NAPEP into four schemes. These are Youth Empowerment Scheme (YES), Rural Infrastructure Development (RIDS), Social Welfare Schemes (SOWESS) and the National Resource Development and Conservation Scheme (NRDCS).

The Youth Empowerment Schemes (YES) is concerned with providing unemployed youth opportunities in skills acquisition, employment and wealth generation. To achieve this, the scheme was further subdivided into Capacity Acquisition Programme, Mandatory Attachment Programme and Credit Deli very Programme.

The second is the Rural Infrastructure Development Scheme (RIDS). The objective of this scheme is to ensure that the provision and development of infrastructure needs in the areas of transport, energy water and communication especially in rural areas. The scheme was broken into four parts: the Rural Transport Programme, the Rural Energy Programme, the Rural Water Programme and the Rural Communication Programme.

The Social Welfare Services Scheme (SOWESS) aims at ensuring the provision of basic social services including quality primary and special education, strengthening the economic power of farmers, providing primary health care, and so on. This third scheme consists of four broad sub-categories, which are, the Qualitative Education Programme, Primary Health Care Programme, Farmers Empowerment Programme and Social Services Programme. The last is the Natural Resources Development and Conservation Scheme (NRDCS). The vision of this scheme is to bring about a participatory and sustainable development of agricultural, mineral and water resources through the following sub-divisions: Agricultural Resources Programme, Water Resources Programme, Solid Minerals Resources Programme and Environment Protection Programme.

So far, about 140,000 youths have been trained in more than 190 practical hand-on trades over a period of three months. Every trainee in this intervention project was paid N3, 000 ($21) per month while N3, 500 ($25) was paid to each of the trainer. The training programme was packaged with the understanding that beneficiaries would subsequently set up their own businesses in line with the skills.

They have acquisition. To actualize this, 5,000 beneficiaries were resettled with assorted tailoring and fashion designing equipment. Also under the Mandatory Attachment Programme for unemployment graduates, 40,000 beneficiaries were attached in 2001, each of whom was paid a monthly stipend of ₦10,000 ($71). The installation of equipment under the Rural Telephone Project is currently in progress, while the KEKE NAPEP project is currently being vigorously implemented (Elumilade, Asaolu and Adereti, 2006).

3.2 National Economic Empowerment and Development Strategy (NEEDS)

NEEDS is a federal government plan, which also expected the states and local governments to have their counterpart plans- the State Economic Empowerment and Development Strategy (SEEDS) and the Local Government Economic Empowerment and Development Strategy (LEEDS) respectively.

The objective of NEEDS is to enable Nigeria achieve a turn around and grow a broad based market oriented economy that is private sector - led and in which people can be empowered so that they can, as a minimum, afford the basic needs of life. It is therefore a pro-poor development strategy with sources of economic empowerment being gainful employment and provision of social safety nets for vulnerable groups.
NEEDS is not only a macro-economic plan document, but also a comprehensive vision, goals and principles of a new Nigeria that would be made possible through re-enacting core Nigerian values like respect for the elders, honesty and accountability, cooperation, industry, discipline, self-confidence and moral courage.

NEEDS strategy of wealth creation and by implication, employment generation and poverty reduction, is through the empowerment of the people and promotion of private enterprise. The NEEDS document asserts:

By allowing the private sector to thrive, NEEDS creates opportunities for employment and wealth creation. It empowers people to take advantage of these opportunities by creating a system of incentive that reward hard work and punish corruption, by investing in education and by providing special programmes for the most vulnerable members of the society (National Planning Commission and Central Bank of Nigeria, 2005).

The achievements of NEEDS have centered on macroeconomic stabilization of the Nigerian economy by improving budgetary planning and execution, and provided a platform for sustained economic diversification and non-oil growth (Okonjo-Iweala and Osafo-Kwaako, 2007). The reform fiscal policy had enabled accumulation of government savings for back-up purposes. Government expenditure estimates were based on a prudent oil price benchmark.

4.0 CONCLUSION

Experience showed that Millennium Development Goals, specifically the first two goals, which focus on reducing hunger and poverty' by half and ensuring universal primary education by 2015 were not achieved. There is the need to change the traditional working modalities of international aid agencies and address the needs of the world's biggest neglected majority - rural people. This can be achieved through new multi-sectoral and interdisciplinary alliances and partnerships among aid specialists working in education and those working in agriculture and rural development.

5.0 SUMMARY

In this unit, you learnt the objects for establishing these initiatives, their modes of operation and challenges they faced. It is important to note why they did not achieve their targets as expected in order to incorporate the lessons in new programmes that will be initiated.

6.0 TUTOR-MARKED ASSIGNMENT

1. What are the objectives of NAPEP?
2. What are the objectives of NEEDS?

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UNIT 3 RURAL FINANCIAL INSTITUTIONS

CONTENT

1.0 INTRODUCTION

Rural finance institutions are institutions involved with the provision of financial services in the rural areas. They could be formal or informal in nature. Some of these associations operating outside the formal financial systems like the traditional rotating savings and credit association (ROSCA).

Formal financial providers are "those that are subject not only to general laws but also to specific banking regulation and supervision (development banks, savings and postal banks, commercial banks and non-financial intermediaries).

Semi-formal providers are registered entities that are subject to commercial laws but are not necessarily regulated or supervised by banks, including financial NGOs, credit unions and co-operatives, although these may also fall into the category of informal groups.

Informal financial providers, on the other hand, refers largely to traditional methods of trading and financial exchanges that emerge organically and are shaped by cultural values and norms. They are outside the purview of government regulations.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- understand formal, semi-formal and informal financial providers
- examine the rotating savings and credit association (rosca)
- list the role of rural financing

3.0 MAIN CONTENT

3.1 Rotating Savings and Credit Association

A Rotating Savings and Credit Association or ROSCA is a group of individuals who agree to meet for a de 1 in order to save and borrow together. "ROSCAs are the man's bank, where money is not idle for long but changes hands, rapidly, satisfying both consumption and production need".

3.2 Structure

Meetings can be regular or tied to seasonal cash flow cycles in rural communities. Each member contributes the same amount at each meeting, and one member takes the whole sum once. As a result, each is able to access a large sum of money during the life of the ROSCA and use it for whatever purpose she or he wishes. This method of saving is a popular alternative to the risks of saving at home, where family and relatives may demand access to savings.

Every transaction is seen by every member during the meetings. Since no money has to be retained inside the group, no records have to be kept. These characteristics make the system a model of transparency and simplicity that is well adapted to communities with low levels of literacy. The system further reduces the risk to members because it is time limited - typically lasting no more than 6 months. Each member receives at least once the amount collected. This reduces the size of the loss, should someone take funds early and not pay back.

3.3 Diversity and Distribution

ROSCAs are informal microfinance groups that have been developing world.

ROSCAs are "intermediate" within peasant social structure, economic patterns with commercial ones, to act as a bridge between peasant and trader attitudes toward money and its uses. The individuals in the ROSCA select each other, which ensure that participation is based on trust and social forces.

Variously called "committee" in India and Pakistan "Ekub" in Ethopia, "Susus' in Southern African and the Caribbean, "Seettuva" in Srilanka, "Tontines" in West Africa "Gye" in Korea, "Arisan" in Indonesia, "Likelembas" in the Democratic Republic of the Congo, "Xitique" in Mozambiqu: and "Djanggis" in Cameroon.

Most often, they exist as unregistered association an: operate outside the banking system not regulated. It is the preferred mechanism for many micro entrepreneurs. Example of this informal micro finance (institutions or associations) sometimes are tagged. Non-institutional savings methods are Isusu or Esusu or Adashi Clubs Money Lenders, Daily Saving Clubs, Trader's Credit.

Advantages

1. It offers an opportunity for members to save.
2. Social capital getting to know contacts or information within the ROSCAs.
3. ROSCAs offer a personal source of income for members.
4. Protect an individual savings against immediate consumption.
5. The savings of many are transformed into a lump sum for one person. This is often used to improve household’s livelihoods to invest in a new business or to pay school fees.
6. Transparency due to group regulation.
7. Offers a protection against theft as savings are not lei within houses.
8. Reducing pressures on free cash, i.e. cash on hand i subject to the pressure of family members and friends Savings allows members to shed the pressure placed on their free cash by husbands, neighbours, and friends. Ultimately, this enables people to commit their surplus cash towards future purchases with the potential to improve their quality of life.
9. Enabling access to funds for unexpected life events or large purchases. Participating in a group creates additional flexibility and builds a social structure that creates discipline.
10. Increasing the strength of social networks -Working together towards the same financial goal as part of a group that meets each month creates strong bonds. Individuals are able to leverage other members of the group to further create opportunities for themselves.

Disadvantages

1. Relatively ineffective as a means of capitalizing productive investment.
2. The amount of money is fixed and may be inadequately matched to person's investment plans.
3. There is no return on people's investment in a ROSCA, except a marginal time - value of money benefit of receiving a lump sum at no interest cost before reimbursement.
4. No legal status, in that, they are not registered scheme.
5. No regulation and supervision of activities and records.

6. Activities limited only to the economically weak of the society.

Ways to Stimulate Rural Savings and Capital Formation

1. Opening of rural financial institution like MFIs.
2. Developing a savings - borrower relationship.
3. Adoption of simple but convenient system of servicing deposits.
4. Education to rural people on the need to be bankable.
5. Creating an atmosphere of mutual confidence and trust between the bank and community, an assurance of safety of deposits.
6. Insurance of deposit up to a certain level of promote public confidence.

3.4 Role of Rural Financing

i. Ensures transformation of informal to formal rural financial system with all the benefit derivable there from.
ii. Inculcates the habit of contributing, saving among rural people and depositing same with formal financial institutions.
iii. Accumulated deposits with banks could serve as collaterals to loans granted to people.
iv. Enhances the viability and liquidity of the rural areas for savings mobilized can be used for investment purpose.

4.0 CONCLUSION

In this unit, we have studied the Rotating Savings and credit Association. The structure which is basically how they operate or function has been discussed as well as the advantages it provides and also the disadvantages it faces. Furthermore, the importance of rural finance was also brought to light.

5.0 SUMMARY

The Rotating Savings and Credit Association are informal groups that save ad borrow together. In this unit, we analyzed its structure, diversity and distribution, advantages and disadvantages. Also, we learnt ways used in stimulating Rural Savings and capital formation together with the role of rural financing.

6.0 TUTOR-MARKED ASSIGNMENT

1. Examine the Rotating Savings and Credit Association (ROSCA)
2. List the role of rural financing.

7.0 REFERENCES/FURTHER READINGS

Abdul J.B. (2011), National Economic Empowerment Development Strategy&Poverty Reduction in Nigeria: A Critique, Economics and Finance Review 1(1), Www.Efr.Businessjournalz.Org.

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UNIT 4 MICRO FINANCE BANKS (MFB)

CONTENTS

1.0 INTRODUCTION

The significance of Microfinance Banks especially to the growth and development of the rural areas cannot be overemphasized. It specifically issues micro loans, micro savings, micro insurance and micro credit products that are easily accessible to the people or organizations. There have been profound improvements in its activities over the years and it has greatly impacted the economy thereby contributing to its advancement through empowering those in the rural areas.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- explain the concept of microfinance
- ascertain the reasons for the growth of microfinance
- know the principles of microfinance
- describe the evolution of microfinance in Nigeria

3.0 MAIN CONTENT

3.1 Definition of 'Microfinance'

A microfinance bank is a financial institution that extends small loans to people, business and unemployed or low-income individuals. Ultimately, the goal of microfinance is to give low income people an opportunity to become self- sufficient by providing a means of saving money, borrowing money and insurance.

3.2 Background

- Microfinance arose in response to doubt about state delivery of subsidized credit to poor farmers.
- Most programs accumulated large loan losses and required frequent recapitalization.
- More market based solutions required.

3.3 Microfinance: A Development Tools

Typical microfinance activities involves

- Small loans, usually for working capital.
- Informal appraisals of borrowers and investment Collateral substitute, such as group guarantees or compulsory savings.
- Access to repeat and long loans, based on repayment performance.
- Streamlined loan disbursement and monitoring
- Secure savings products.

Effect of Government Programmes

- Often perceived as a social welfare.
- Forgive existing debts of the poor.
- Tremendous effect on private sector MFIs.

Facts about Microfinance

- Subsidized credit undermines sustain ability and development of microfinance.
- Poor people can pay interest rates high enough to cover MFIs' transaction costs and the consequences of imperfect information markets.

Meaning: Imperfect Market (Market inefficiencies) A market where information is not quickly disclosed to all participants in it and where the matching of buyers and sellers isn't immediate. Generally speaking, it is any market that does not adhere rigidly to perfect information flow and provide instantly available buyers and sellers.

3.4 Understanding the Country Context (Supply Side) of MFIs

1. Formal financial institutions; public/private banks,

insurance firms, finance companies.
2. Semi formal: credit unions, co-operative banks.
3. Informal: NOOs, self-help groups individuals.

3.5 Microfinance Target Market (Demand Side)

- Allocation of funds to a particular sector of the economy or population.
- Concentrates on production and income generation.
- "Incentive compatibility" unwanted clients will not be interested.
- MFIs need to consider debt capacity (Debt Capacity: amount of addition debt a client can take without running the risk of inadequate cash flow) as opposed to a "credit need" approach.

3.6 Growth of Microfinance

Microfinance has been growing for several reasons:

- The premise of reaching the poor. Microfinance activities can support income activities generation for enterprises operated by low-income households.
- The promise of financial sustainability. Microfinance activities can help to build financially self-sufficient, subsidy-free, often locally managed institution.
- The potential to build on traditional systems. Microfinance activities sometimes emulates traditional systems (such as rotating savings and credit associations).
- The contribution of microfinance to strengthening and expanding existing formal financial system. Microfinance activities can strength existing formal financial institutions, such as savings and loan co- operatives.

3.7 Principles of Microfinance

- The poor needs a variety of financial services
- Micro credit is a powerful instrument for poverty alleviation.
- Microfinance must be able to build financial systems that serve micro enterprises.
- Financial sustainability is necessary to reach a significant number of poor people.
- Microfinance is about building permanent local financial institutions.
- In addition to credit, it provides;
- Financial services
- Social services

- Health services
- Microcredit is not always the answer
- Institutional and human capacity building is imperative.
- There is need for transparency and good corporate governance; herein lies the key issue in Board responsibility.
- Interest rate ceiling hurt poor people by making it harder for them to access credit.
- The role of government is to enable financial services, not to provide them directly.
- Microfinance works best when it measures and discloses its performance.

3.8 Evolution of Microfinance in Nigeria

Nigeria is rated as one of the 20 poorest countries in the world with a worsening poverty incidence of over 70 among its population, (CBN, 2001). The situation contradicts the nations abundant resources in terms of enormous agricultural, oil, gas and several untapped solid mineral resource endowments. Key to any poverty reduction strategy in Nigeria is the provision of .specially tailored financial services to enable the poor engage in economic activities such as trading, tailoring, farming, processing, vulcanizing, restaurant business, etc. By enabling the poor to engage in such economic activities employment would be generated, earnings will be increased and standard of living improved. This will lead to economic growth and development.

4.0 CONCLUSION

The ultimate goal of microfinance is to give low income people opportunities of becoming self-sufficient by providing a means of saving money, borrowing money and also access to insurance. It arose in response to doubt about state delivery of subsidized credit to poor farmers. There are peculiar activities which it is involved in and operates on both the supply and demand side. The principles guiding microfinance activities were also discussed.

5.0 SUMMARY

This unit focused on evolution and operations of microfinance in Nigeria. Understanding the demand and supply side of microfinance will enable students to develop a holistic approach to microfinance philosophy as well as appreciate its principles.

6.0 TUTOR-MARKED ASSIGNMENT

1. Explain the concept of microfinance

2. What are the principles of microfinance?
3. Describe the evolution of microfinance in Nigeria

7.0 REFERENCES/FURTHER READINGS

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UNIT 5 CREDIT UNIONS IN CANADA

CONTENTS

1.0 INTRODUCTION

Throughout its history, the Canadian credit union system has maintained a record of sound, prudent financial management, solid growth and unparalleled service to members.

Credit unions are financial cooperatives. Their products, services and operations-and even their physical appearance-may resemble those of banks, but there are some major differences. The biggest ones are that they're locally owned and invest their profits in the communities where they operate; where their members live and work.

Unlike banks, credit unions are autonomous. Each one has its own brand identity, management and Board of Directors, but they're united through provincial centrals. These provide financial, technology and trade services to their member credit unions.

The Canadian Credit Union Association (CCUA) is the national trade association for the Canadian credit union system. It's also a cooperative, owned and governed by Canada's credit unions and caisses populaires (outside Quebec). This unit focus on understanding why they stand out among all cooperatives that are involved in credit mobilization.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

1. Give account for the credit union in British Columbia and Ontario
2. Explain the Deposit Insurance Corporation
3. Discuss the credit union legislation, regulation and stabilization authority.

3.0 MAIN CONTENT

3.1 In British Columbia

- There are 42 independent credit unions with 374 branch locations
- The province's first credit union, Powell River Credit Union, was established in 1939. In 2007, it became First Credit Union
- Credit unions serve more than 1.9 million members (approximately 42 per cent of the provincial population)
- They hold $72.1 billion in assets (as of September 30, 2016)
- They employ 9,082 British Columbians

3.2 In Ontario

- In total, there are 70 independent credit unions (affiliated and non-affiliated), with 525 branch locations
- The province’s first credit union, Civil Service Co-operative Credit Society, was established in 1908. Today, it's part of Alterna Savings and Credit Union Ltd.
- Credit unions serve more than 1.3 million members (approximately 11 per cent of the provincial population)
- They hold $43.6 billion in assets (as of September 30, 2016)
- They employ 5,888 Ontario residents

3.3 Deposit Insurance Guarantees your Money

In B.C., the Credit Union Deposit Insurance Corporation (CUDIC), a statutory corporation, fully guarantees all money on deposit and money invested in non-equity shares, including foreign currencies and accrued interest, accepted by a credit union in British Columbia. CUDIC is administered by the Financial Institutions Commission, an agency of the provincial government of B.C.

In Ontario, the Deposit Insurance Corporation of Ontario (DICO), a provincial agency, covers eligible deposits in Canadian dollars up to $100,000 in each of the prescribed categories. Additionally, DICO provides unlimited insurance for each registered savings plan or contract, including registered retirement savings plans (RRSPs), registered retirement income funds (RRIFs), registered education savings plans (RESPs), registered disability savings plans (RDSPs) and Tax-Free Savings Accounts (TFSAs).

In both provinces, deposit insurance applies automatically.

3.4 Legislation

Credit unions in B.C. and Ontario are incorporated under provincial legislation.

In B.C., they're authorized to conduct deposit business or both deposit and trust business under the *Financial Institutions Act* of British Columbia. The Act confers powers on credit unions to lend, borrow and invest. It also specifies the amount and types of reserves they must maintain.

Provisions relating to credit union membership and shares are set out in the *Credit Union Incorporation Act* of British Columbia.
In Ontario, credit unions operate under the provincial *Credit Unions and Caisses Populaires Act 1994*, which includes provisions related to credit union membership and shares.

3.5 Regulation

The *Financial Institutions Act* requires that each credit union have an audit committee and be audited by independent auditors. Credit unions are also subject to inspection by the Superintendent of Financial Institutions, an official (or an appointee) of the Financial Institutions Commission. In B.C., financial institutions, including credit unions, are regulated by the Financial Institutions Commission. The Commission is responsible to the provincial Minister of Finance.

In Ontario, credit unions are regulated through a comprehensive framework that involves the provincial Ministry of Finance, the Financial Services Commission of Ontario (FSCO) and the DICO. FSCO regulates registration of credit unions and caissespopulaires under the *Credit Unions and CaissesPopulaires Act 1994*. FSCO is responsible for ensuring that credit unions operate in accordance with the requirements of that Act.

DICO is responsible for overseeing compliance with solvency rules and for insuring eligible deposits. As part of this responsibility, DICO has the authority to issue bylaws to ensure that insured institutions operate in accordance with sound business and financial practices.

3.6 Stabilization Authority

Stabilization Central Credit Union of British Columbia is a self-regulatory organization (SRO) that monitors and assists credit unions with governance, risk management, operational and financial challenges. It strengthens the provincial system through supervision of credit unions that are assigned to it by the Financial Institutions Commission. It also provides services including financial analysis, Enterprise Risk Management (ERM) and IT Governance.

Every local credit union in B.C. must be a member of Stabilization Central as a condition of holding a business authorization. These same credit unions fund the stabilization authority, which is directed by a Board elected by, or appointed from, these members. The transport cooperative can only indulge in a motor fabrication and building. The management of this type of cooperative is same with other of cooperative is same with other types of cooperative societies.

1) Benefits to members

A member will drive the following benefits Patronage dividend;- This is also called patronage refund and has been working out at a substantial sum of money, depending on the amount of purchase made by the members.

The money paid to the member as dividend can be regarded as a wind fall, for the member could not have gotten it, if they did not buy from the cooperative consumer shop.

2) Best quality commodities at reasonable prices

The member will be able to purchase best quality commodities of everyday consumption at moderate prices.

There is no adulteration of, goods or giving of short weight. This factor helps to attract customers to the consumer shop. This will result in a Hugh turnover, and eventually to a higher profitability.

3) Dividend on Shares

This is also another benefit for member of a consumer cooperative society. After the preparation of the society's annual account, there will be division of surplus. From this surplus 'every member is paid the dividend on his shares.

4.0 CONCLUSION

Credit unions are financial cooperatives. In Canada, credit unions trace their roots to the early 1900s with the first caissepopulaire formed by Alphonse Desjardins, in Levis, Quebec. Unlike banks, credit unions are seen to be autonomous with its own brand identity, management and Board of Directors and are accountable to its members. In British Columbia there are 42 independent credit unions with 374 branch locations, serving more than 1.9 million members, holding $72.1 billion in assets and employing 9,082 British Columbians. In Ontario, there are 70 independent credit unions with 525 branch locations, serving more than 1.3 million members, holding $43.6 billion in assets and employing 5,888 Ontario residents.

5.0 SUMMARY

In this unit, you have learnt what credit union in British Columbia and in Ontario entails. Also, we looked at the Deposit Insurance Corporation of British Columbia and of Ontario, the legislation, regulation and stabilization Authority which monitors and assists credit unions.

7.0 TUTOR-MARKED ASSIGNMENT

1. Give account for the credit union in British Columbia and Ontario
2. Explain the Deposit Insurance Corporation
3. Discuss the credit union legislation, regulation and stabilization authority

7.0 REFERENCES/FURTHER READINGS

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UNIT 6 ADMINISTRATIONS AND MANAGEMENT OF COOPERATIVE BUSINESSES IN RURAL SETTING

CONTENTS

1.0 INTRODUCTION

Cooperative business function both in the urban and rural areas. As opposed to urban areas, cooperatives in the rural areas are constrained to perform below its required standard especially due to the financial constraints and lack of adequate managerial capabilities amongst others. Therefore, there is need to employ special care and attention to its administration to ensure its smooth operation.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Ascertain ways for effective cooperative business management
- Enumerate areas for technical support services and capacity building among cooperatives.

3.0 MAIN CONTENT

3.1 Cooperative Business Management

a. Due partly to the financial limitations discussed above and partly to the smallness of societies, it has been difficult for cooperative societies to employ competent managers for the proper management of their businesses. Hence the new cooperative policy is aimed at ensuring viable societies and unions through proper funding. The societies to be registered in future must demonstrate capacity to carry out profitable and sustainable businesses.

b. Each society must have adequate number of members and present feasibility reports of viable business enterprises before being registered. The decision to liquidate a society must be based, in part, on its persistent unprofitability in spite of efforts by the management committee to improve its performances.

c. Where necessary assistance should be sought from higher levels such as union in the case of a society or the relevant apex in the case of a union. Problems militating against profitability and viability must be diagnosed and appropriate solutions proffered.

d. For the enforcement of an arbitration award, well- informed cooperative and legal practitioners should constitute the membership of any arbitration panel at all levels.

3.2 Cooperative Business Extension and Advisory Services

The CFN in collaboration with the State Federations should employ the services of consultants to provide extension and advisory services wherever and whenever the need should arise. Where such services are extended to small societies to strengthen their businesses, they will appreciate the relevance of the apex body and subscribe to its upkeep. Future cooperative education should embrace relevant business management subjects.

3.3 Management Systems Development

The CFN and State Federations as well as all the societies, unions and special apexes that could afford it should hire competent professional managers to manage their affairs. Those societies and unions that cannot afford to hire professional managers should use the facilities of CFN and State Federations to train their members/managers, giving them the rudiments of the techniques of modem management. Cooperative Societies carrying out similar businesses could share the time of a joint expert with each society paying only' a fraction of the charges.

3.4 External Audit

It is mandatory for all Cooperative apexes and Federations to appoint qualified External Auditors, while unions and societies that can afford it should also do so. Those unions and societies which cannot afford External Auditors should retain the services of the State Cooperative Development or the State Federation Auditors. Appropriate audit fees should be paid as and when due by every audited society or union. This will help maintain the audit unit. In order to ensure accountability and transparency, audit reports should be made available to members and where feasible, published in National Newspapers.

3.5 Technical Support Services and Capacity Building

Education and Training Services:

a. Formal education

i. Formal educational preparation for cooperative career is now being provided by the three National and several State Cooperative Colleges and Polytechnics. A degree programme in cooperative studies exists in both Enugu State University of Technology (ESUT) and Nnamdi Azikiwe University (NAU). The government shall continue the current efforts underway to harmonize the curriculum and ensure its accreditation by the National Board for Technical Education (NBTE). This will enable the graduands to fit in with the nation's educational **mainstream and facilitate the recognition of their** certificates by employers outside Government and the Cooperative Movement. It will also help them get admission to the universities at home and abroad. In order to make this a reality, Government would provide better funding to its colleges to facilitate the upgrading of their infrastructural facilities, libraries, teaching equipment, workshops and computer services, and call on states with similar institutions to do so.

ii. Government would, within available resources sponsor students for training in cooperative affairs by awarding scholarships and bursaries tenable at home and abroad.

iii. At the state level, co-operators should be trained by their respective states through awarding scholarships and bursaries to students and staff to attend courses in cooperative colleges. Cooperative education should be included in the secondary school curriculum throughout the country.

b. Non-Formal Education and Short-Term Training

i. Government shall undertake, as part of its Universal Basic Education Programme (UBE) a literary drive in conjunction with the Local Government, State Governments and the Cooperative Movement. This will ensure that all co-operators in Nigeria are literate within the shortest possible period of time.

ii. The Cooperative Movement shall be supported by government to conduct regular training of cooperative management cadres to enable them refresh their knowledge of cooperative principles and acquire new management skills and techniques.

iii. Government shall also support and fully equip the Cooperative Research Institute of Nigeria (CORIN) at Sheda, Abuja in order to enable it provide effective management training for cooperative leaders, management and members.
iv. Federal and State Governments shall ensure that the staff of their Departments of cooperatives are given opportunities to improve themselves by attending refresher courses and conferences locally and internationally. The governments shall explore bilateral and multilateral assistance from foreign governments, agencies and institutions for such purposes.
v. At the state levels, respective State Government should assist the Cooperative Movement in training co-operators on basic literacy, book-keeping, secretarial work and simple management techniques.
vi. In order to inculcate the Cooperative spirit in our Youths, the Federal and State Governments should direct their Ministries of Education to promote the formation of Cooperative Clubs throughout the nation's secondary school system and the active assistance and support of the Cooperative Movement.

3.6 Training Fund

The mandatory reserve of 10% of the surplus funds for education shall be strictly adhered to and the fund regularly utilized for induction courses for officials and newly appointed cooperative workers in the States and Local Government.

Management Systems Development:

a. The CFN and State Cooperative Federations as well as those societies, unions and apexes that can afford it, should hire competent professional managers to effectively manage their affairs.
b. Those societies and unions that cannot afford to hire professional managers should utilize the opportunities provided by CFN and the Federations to train their members and managers giving them the rudiments of the techniques of modem management.

4.0 CONCLUSION

Cooperatives in rural settings should employ effective strategies in operating their businesses so as to achieve the aims for which it was established. It would be useful to provide extension and advisory services especially to start ups and ailing cooperatives. There should be hiring of competent professional managers to manage their affairs, external audit should be conducted, technical support and capacity building provided and adequate amount (10%) of reserve should be allocated for education especially for officials and workers.

5.0 SUMMARY

This unit explored issues relating to Cooperative business management, Cooperative business extension and advisory services, Management System Development. External Audit, Technical support services and Capacity building for cooperatives are critical for cooperative effectiveness.

9.0 TUTOR-MARKED ASSIGNMENT

1. Ascertain ways for effective cooperative business management
2. Enumerate areas for technical support services and capacity building among cooperatives

7.0 REFERENCES/FURTHER READINGS

Abdu J.B. (2011), National Economic Empowerment Development Strategy&Poverty Reduction in Nigeria: A Critique, Economics and Finance Review 1(1), Www.Efr.Businessjournalz.Org.

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UNIT 7 CREDIT COOPERATIVE SOCIETIES

CONTENTS

1.0 INTRODUCTION

A credit society is cooperative society which provide its members with a means of saving money and of obtaining credit at reasonable rate of interest. The credit society is organized with a group that has something in common e.g. Workers in an establishment. Members of the same club, organization or community, it operates under cooperative law just like other cooperatives and renders some services to its member which include.

1.) It serves as system for accumulating savings; members make regular deposits of small amount depending on the circumstances surrounding them. This means that it encourages thriftiness.
2.) It is a source of credit members borrow from the credit society when they are in need for money and pay back with little interest install mentally.
3.) It serves as a means of training to the members. This means that members are exposed to financial investment and best use of funds that would have been lying idle. This unit exposes the needs and operations of credit cooperatives especially in rural Nigerian context.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- understand the need for a credit society
- discuss the problems encountered by credit cooperative

- state the functions of cooperative credit societies

3.0 MAIN CONTENT

3.1 Need for a Credit Society

There are several reasons why credit society is needed especially in this part of the world these include:-

These societies were in two categories.

1. Those catering for town dwellers,
2. Those catering for the villagers

In the western states, the early attempt by the credit cooperative union to undertake to trade in consumer goods was a failure. But they are doing better today in this state. Here in Nigeria, generally, this kind of cooperative society is not widespread even though credit cooperation started in Nigeria as far back as 1940's it is unfortunate that many of them collapsed.

3.2 Problems of Credit Cooperative

The problems of consumer cooperative can be grouped into two (a) internal and external problems Internal problems are those problems emanating from within the cooperative society itself and they are;

1.) Lack of patronage by members

Where the members of the cooperative society fail to patronize their cooperative credit shop that is to buy goods from the shop, the business of their shop will decline, because there will be fierce competition among so many other shops around that vicinity. If all the members of a credit cooperative decide to buy their requirements and those of families from the credit shop, then their will enjoy a distinct advantage over the other shops around the result will be a large turnover followed by large surplus in trading business.

2.) Credit sale

Many credit cooperatives have collapsed as a result of heavy debts incurred by members as a result of credit purchases they made from their credit shop. The society's capital is tied down in the hands of those debtor members so that there are no funds to stock the credit shop. As a result of this, business will begin to dwindle and the credit shop will eventually fold up.

3.) Dishonesty of the employees of credit cooperative societies one of the worst problem confronting the credit cooperative societies is the dishonesty of its employees. Shop attendants, shop supervisors shop managers etc. They perpetrate various acts of dishonesty, ranging from embezzlement, misapplication and misappropriations of funds, to forgery, pilfer of goods etc.

4.) Dishonesty of officers of the credit cooperative society

3.3 External Problems

The main external problem IS unhealthy competition and rivalry from the capitalist shops and supermarkets. They adopt all imaginable forms of unhealthy competition to stifle the cooperative consumer shop. Such methods adopted include under-selling of cooperative consumer shops, blocking the channels through which consumer cooperative societies buy their commodities, under-rating and discrediting the goods marketed by consumer cooperative societies and several other unhealthy methods of competition adopted.

3.4 Functions of Cooperative Credit Societies

a.) Agricultural credit societies: Is an important approach to development and progress in the agrarian sector of the economy its success depends on the ways in which the farmer can gain access to credit facilities and the degree of supervision of his utilization of the credit. There are various sources by which agricultural credit can be made available to farmers. These include government institution, commercial banking institutions, rural cooperative credit societies and private sources.

b.) Workers productive societies: This- type organized on the basis of co-partnership and profit sharing with workers. These societies operates mainly in the inlands and specialize largely in the manufacturing of clothing, textiles, footwear and in printing

c.) Marketing of farmers produce through cooperatives is a very important aspect of agriculture. There are what you may call sizecilised marketing cooperatives and they are regarded as the main agents

3.5 Information and Extension

For the farmer to adjust his production to the demand of the market he must be sufficiently informed of development on the domestic and world market. Information about trends in demand regarding quality and varieties the prices of agricultural produce at wholesale and retail level the estimation of production in other areas and similar factors help the farmer to assess his own position in the market and plan ahead.

Many societies do not confirm themselves to the supply of market new but they also try to keep members informed of the development of new farming techniques and new methods of handling storing and processing aimed at improving the quality and yield of agricultural production.

3.6 Selling

In selling agricultural produce cooperative societies can adopt either an agency system or a fixed price system.

1. Under the agency system the society sells the produce on behalf of and on account of each .member. Although the individual member does not necessarily appear as the seller, the Society only assumes the role of an intermediary agent negating the sale.
2. At no stage of the marketing process does the society assure ownership of the commodity handled. This procedure leaves the society free from some marketing risks.
3. Under the fixed system, the society acts as an independent trader. By purchasing the produce from the member on delivery it assumes ownership until resale. The society thus has to carry the full extent of the marketing risk although ultimately it is transferred back to the member in form of lower prices or refund.

4.0 CONCLUSION

Credit cooperative societies enable members save money and obtain credit at a reasonable rate of interest. Nevertheless, they encounter problems such as lack of patronage by members, credit sale, dishonesty of the employees and dishonesty of officers of credit cooperative societies likewise external problems of competition and rivalry from capitalist shops and supermarkets. They are also seen to perform functions in the agricultural, workers, and marketing societies.

5.0 SUMMARY

This unit explored the need for credit society. We discussed problems faced by credit cooperative and looked at some functions performed by credit cooperative societies in different types of cooperative societies. Despite that challenges facing credit cooperatives are universal in scope, some of them are peculiar to rural cooperatives.

6.0 TUTOR-MARKED ASSIGNMENT

1. Understand the need for a credit society
2. Discuss the problems encountered by credit cooperative
3. State the functions of cooperative credit societies

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