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Microfinance Support Centre's provision of Institutional loans: Why is uptake declining?

Overview

The Microfinance Support Centre (MSC) is a government owned company established in 2001 to manage all Government of Uganda (GoU) micro-credit programs. The MSC seeks to act as a lynchpin of government for delivery of Rural Financial Services (RFS). It also; facilitates access to affordable, sustainable and convenient financial and business development services to active and productive Ugandans.

The MSC is currently implementing the flagship project Rural Income and Employment Enhancement Project (RIEEP). The project started on 3rd September 2010 and ends on 31st July 2015. The total project cost is USD 27million over a period of 5 years.

The RIEEP is funded by the Government of Uganda, African Development Bank (ADB), the Islamic Development Bank (IDB) and Interest income from loans. These funds are mainly meant for loan provision to the eligible institutions for on-lending.

The MSC Annual reports of FYs 2011/12, 2012/13, and Q3 FY 2013/14 reflect a declining trend in the uptake of loans by the institutions. The actual number of loans disbursed in FY 2012/13 reduced by 30%. By the end of Quarter 3 (Q3), FY 2013/14; 33% of the annual planned number of loans had been disbursed.

This policy brief therefore analyses; the trend in loan provision by the MSC, explores reasons for the declining trend, and provides recommendations for reversing the trend.

Key Issues

- Poor governance and management practices due to the incompetence and fraudulent practices of the Board members of some borrowing institutions. They cannot effectively supervise the financial flows of their institutions.
- Security requirement; as a delinquency control measure for all loans above 100 million has limited some potential clients from accessing credit from the Centre.
- Low outreach to potential clients for the credit services and products offered by MSC.
- Poor repayment culture especially in regions previously affected by the war. These communities are used to free handouts from Government.
- Political interference where some politicians have misinformed communities that MSC funds are free and should not be paid back.

Introduction

Provision of loans to institutions is the key role for the Microfinance Support Centre (MSC). Financial services are extended to the rural poor through wholesale and retail loans to microfinance institutions (MFIs) and other partner organizations for the purpose of on-lending to their clients.

The loans are to support legal entities engaged in trade and service, agricultural related activities along the value chain i.e. production, productivity enhancement, agro processing, asset acquisition, marketing and construction of farm and warehousing.

The institutions specifically targeted for the loans are; Savings and Credit Co-operative Organizations (SACCOs), Area Co-operative Enterprises (ACEs), Microfinance Institutions (MFIs), Co-operative Unions, Producer and Marketing Co-operatives and Small and Medium Enterprises (SMEs).

The MSC created twelve (12) zonal offices in order to provide a fair distribution of services, throughout the country. These provide number of loan products to institutions.These include but are not limited to:

a) **Agricultural Loan:** This is extended to support productivity enhancement, asset acquisition, bulk purchasing and construction of farms.

b) **Environmental Loan:** This is extended to support environmental and clean energy products i.e. Production of solar, biogas and energy savings stoves, and agro-forestry.

c) **Special Interest Group Loan:** This is extended to Women, Youth, and Persons with Disabilities, Elderly Persons and weak SACCOs.

d) **Commercial Loan:** Funding is extended to institutions for onward lending to their members engaged in trade and service activities.

e) **Small and Medium Enterprise (SME) Loan:** This product targets businesses with minimum annual sales turnover of Ug shs 50 million for agricultural related SMEs and Ug shs 70 million for non-agricultural related SMEs.

Table 1.1 shows the trend in the loans disbursements to institutions for FYs; 2011/12, and 2012/13 and by end of Q3 FY 2013/14

Table 1.1: Loans Disbursements to Institutions for the FYs 2011/12, 2012/13 and by end of Q3FY 2013/14

Financial Year	Item	Planned Target	Achieve-ment
FY 2011/12	Number of loans disbursed	400	381 95% of the planned target
	Amount disbursed Ug Shs (Billions)	40.75	31.8 78% of the planned target
FY 2012/13	Number of loans disbursed	300	194 65% of the planned target
	Amount disbursed Ug Shs (Billions)	35	23.4 66% of the planned target
FY 2013/14 (End of Q3)	Number of loans disbursed	400	133 33% of the planned target
	Amount disbursed Ug Shs (Billions)	40.75	18.9 46% of the planned target

Source: MSC Annual Reports FY 2011/12; 2012/13; and Q3 MSC Report FY 2013/14

A trends analysis shows a significant decline in the number of loans and amounts disbursed to the institutions for on-lending. In the FY 2011/12, 95% of the planned number of loans and 78% of the amount was disbursed to the Institutions. This was a good performance.

In FY 2012/13, 65% of the planned number of loans and 66% of the amounts were disbursed. This indicated a decline of 30% in the uptake of loans and 12% in the amounts disbursed to the institutions.

By the end of Q3, FY 2013/14; only 33% of the planned number of loans and 46% of the amounts had been disbursed. This showed a further drop in uptake of loans from MSC by the targeted institutions.

Reasons for the declining trend

- **Poor governance and management practices.** This arises from the fraudulent tendencies and the incompetence of the Boards of some institutions like SACCOs. The Board members take loans and hardly monitor and supervise the managers who in turn do not produce reports to reflect the financial status.

- **Security requirement.** The requirement to provide security for all loans above Ug shs 100 million was instituted by the MSC. This policy measure led to the failure by most clients to meet the eligibility criteria for loans, hence leading to low credit disbursements.

- **Low Centre outreach.** The outreach to the potential clients for the services and products offered by MSC is still low. For example; it was reported in the BMAU FY 2012/13 report that small enterprises within districts like Gulu and Lira hardly had any knowledge about the services or products offered by the MSC.

- **Poor repayment culture and attitude.** The poor repayment culture was common with clients in the regions previously affected by the LRA insurgency. The communities were used to free handouts from Government and NGOs. This crippled their repayment culture and attitude towards loans taken from the MFIs and SACCOs as there are considered free money from Government.

  Most politicians like Councilors are part of the SACCO Boards and protect loan defaulters. In addition, some politicians have also borrowed money and failed to pay back. For example in Sembabule district, in Lugusulu SACCO and Taala Lya Mawogola SACCO, the politicians were part of the defaulters and also protected other defaulters.

- **High staff turnover at institutions after training.** As part of capacity building, the MSC has trained staff members like managers and accountants of their client SACCOs in book keeping and governance. However there is high staff turnover.

- **Multiple borrowing by MFIs and SACCOs.** Some MFIs borrow from different institutions other than MSC after acquiring the latter's loans. This leads to a high portfolio at risk at the MSC due to higher default rate by the clients. For example the BMAU Report FY 2012/13 reported that; Malawoli SACCO in Iganga district and the Uganda Co-operative Society (USC) accessed loans from MSC However, it took the intervention of court bailiffs for the MSC to recover its funds.

Conclusion:

The ultimate goal of the Government and other development partners in the MSC was to help the rural poor access sustainable and convenient financial services from the MFIs. This was to be achieved through provision of loans to Institutions like SACCOs, SMEs and MFIs.

This however has met a lot of challenges like; poor governance and management practices, poor repayment culture and attitude, and low outreach among others. This has crippled on-lending prospects from the Centre.

Policy Recommendations

- The Micro finance department in the Ministry of Finance, Planning and Economic Development should ensure that the SACCO regulatory framework is concluded expeditiously to protect member savings and also reduce on multiple borrowing.
- The MSC should design tailor made training for SACCO Board members and management in; SACCO Management, Business planning and Controls. In the same breath the SACCO members should be trained on their rights and aspects of good management.
- The MSC should relax the new policy on security for the threshold of Ug shs 100million.
- The Micro finance department through Uganda Cooperative Savings and Credit Unit (UCSCU) should motivate trained staff of borrowing institutions by increasing salaries to reduce on staff turnover.

References:

- Micro Finance Support Centre Annual Reports for FYs 2011/12; 2012/13
- Micro Finance Support Centre Quarter 3 Report for FY 2013/14
- Annual Budget Monitoring Report for FY 2012/13

Budget Monitoring and Accountability Unity
Ministry of Finance, Planning and
Economic Development,
Plot 2-12 Apollo Kaggwa Road,
P.O.Box 8147 Kampala,
www.finance.go.ug