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THE BASES OF THE VIABILITY OF AGRIBUSINESS MICROFINANCE INSTITUTION (AMFI): FINDINGS OF A SURVEY OF SUCCESSFUL GOVERNMENT-SPONSORED AMFIs IN WEST SUMATERA, INDONESIA

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ABSTRACT

Government involvement in developing microfinance institutions highlights the rise of welfare state approach to sustainable rural-agricultural development. In West Sumatra province, government initiated the development of 1037 units Agribusiness Micro Finance Institution (AMFI) since 2008. By 2016, however, more than 30 percent of these AMFIs were reported inactive, most of those considered active were actually stagnant in terms of assets accumulation, and only a small number were able to double, or more, their assets. This research aims at disclosing some key characteristics of this successful AMFIs based on a survey of 30 successful AMFIs in three districts in West Sumatra. Based on the methods these AMFIs used to mobilize funds, their policies in the ways credit being delivered and the methods they used to ensure credit repayment it is concluded that these AMFIs are developing closer toward institutionalist, rather than welfarist, perspective on microfinance institutional development. Inevitably, serving particularly the better-off segments of the rural population is likely to be the basis of their viability. The poorer segments of rural agricultural population are unlikely to be able to access credit from these AMFIs.

Keywords: *microfinance, rural agribusiness, social collateral*

INTRODUCTION

Government involvement in initiating the development of microfinance institutions in rural areas marks important changes in the government approach to solving various problems arising from lack of capital faced by small farmers and villagers in general. Firstly, it is clear a move of 'get the government back in' instead 'let the market solves the problem.' Secondly, it is a move from relying mainly on credit program, that helps only those involved in certain programs and only during the program implementation, toward developing established microfinance institutions available for small farmers and villagers at any time and for any purpose (productive and consumptive, agricultural and non-agricultural) (see among others Ellis 1992). As such, it is also an appreciation for the long neglected fact that small farmers are in constant need of credit, productive as well as consumptive, since most of their small farm income is consumed leaving almost nothing to fund, for example, the next farming seasons. Developing an established microfinance institution is expected to increase access of villagers, especially the poor, to the much needed credit as microfinance institutions should be able, so it is expected, to be more flexible than the rigid formal bank and, at the same time, at least as flexible as the informal credit institutions that usually supply credit to the poor at very high interest rates.

In Indonesia, these changes manifest in various programs, sponsored not only by the central government but also by provincial governments as well as district governments, aiming at developing one or other kinds of microfinance institutions (MFI) in rural areas. The approach in general is in the form of providing money as a start-up capital to groups of villagers, usually farmers groups, or village governments to start microcredit institutions. The money is expected to be delivered to those in need of credit employing schemes like small group lending or revolving funds within small groups of villagers. It is expected that the villagers will develop their management capacity and to expand the MFIs service outreach beyond the initial groups members. Overtime, so it is expected, the MFI will be able to sustainably serve the needs of those villagers excluded from the formal banking system and at the same time will also be able to take over the role of informal money lenders.

One prominent Indonesia's central government programs involving the development of MFI is the Program of Developing Rural Agribusiness (PDRA). Started being implemented about ten years ago, in this nationwide program, the government provides support to a large number of federations of adjacent Farmers Groups (FFGs) all over Indonesia to form their own Agribusiness Microfinance Institutions (AMFIs). Each FFG is granted start-up capital Rp100.000.000,- to start establishing an AMFI particularly meant to serve the needs of the FFG members for credit for various rural agribusiness purposes. The government also provides a number of university graduates trained to be supervisors for the FFGs in this program.

In the province of West Sumatra alone, this program develops in total 1037 units of Agribusiness Micro Finance Institution (AMFI). By 2016, however, more than 30 percent of these AMFIs were reported inactive, most of those considered active were actually stagnant in terms of assets accumulation, and only a small number of the AMFIs were able to double, or more, their assets. This assessment based on data provided by the Provincial Secretariat of PDRA (STP PUAP, 2016) is a bit discouraging, although may not be unanticipated in the literature of MFI (see Lapenu, 2000, Murdoch, 2000, Moon, 2007). Obviously, it may not an easy endeavour to develop established MFIs in large number, especially if the MFIs were expected to particularly serve the rural poor sustainably.

This research was done in order to shed some light on the issues by focusing on the successful AMFIs. What makes them different from the not so successful AMFIs? Are they able to be viable while maintaining their initial missions as credit providers of the rural poor? To answer these questions, a survey was conducted aiming at disclosing some key characteristics of these successful AMFIs. The survey was done in three districts of West Sumatra Province, i.e. Dharmasraya, Limapuluh Kota, and Pasaman Barat. The districts were purposively chosen based on consideration that the district contains a larger number of successful AMFI than other districts and municipalities within the province. All of successful AMFIs defined in this research as AMFIs which are able to at least double their initial start-up capital, in the chosen districts were selected as samples. Questionnaire were used in interviewing the management of the AMFIs. Secondary data in the form of annual reports of the AMFIs was also used. Then, with the help of descriptive statistic, the data is presented around two main themes: the methods used by these successful AMFIs in mobilizing funds, and their policies in the ways credit being delivered and the methods they used to ensure credit repayment.

This paper will progress in the following order. The above introduction will be proceeded by a brief discussion on the debate between welfarist perspective vs institutionalist perspective on MFI development as well as trends found in some empirical literature. The findings and discussion of this research then followed before some conclusions as well as policy and research implications are presented.

THE DEBATE

Should the MFI be supported by government all the way from the beginning or should the MFIs be developed to be independent from government or other outsiders support, or is it possible for the MFIs to be financially viable without outsider support when they are expected to provide credit for a large number of poor villagers are questions that has been plagued the microfinance movement for a long time (see Moon, 2009). In other words, since microfinance movement is meant to alleviate poverty, can an MFI maintain it viability by relying on the poor as its credit market?

Morduch (1999) argues that it is difficult for MFIs to be profitable and at the same time successful in poverty alleviation. Theoretically, the transaction costs of serving a large number of small credits to the poor would be significantly higher than serving small number of large credit to wealthy clients (Morduch 2000, see also Moon 2009). Empirically, Morduch (1999) implies that even the renowned Grameen Bank would have been collapsed had it not for various supports and subsidies, from the Bangladesh government. Left on their own, the MFIs would likely, therefore, go to wealthy clients for their own survival, leaving the poor and poverty alleviation from their mission.

In the other line of thinking, the proponents argue that relying on government or outsider support and subsidies would be unsustainable for the MFIs. To be sustainable, the MFIs must justify themselves financially on their own. Moreover, it is actually possible for the MFIs to be viable relying on the poor as their market base since the poor, so the argument goes, can save, no matter how small it may be, implying the credit worthiness of the poor (see Ellis, 1992). The MFIs can also rely on their low overhead costs to make higher transaction costs justifiable. It is important, however, for the MFIs to set interest rate at the level of market rates both for saving and lending. Lower interest rates will only discourage local saving mobilization and threaten the MFIs long terms prospect to expand their outreach and to accumulate capital. Market rates are also justified based on fact that they are usually lower than rates charged by informal money lenders (see Ellis, 1992, and Moon, 2009).

These two opposing lines of argument have come to be known as the welfarist perspective and the institutionalist perspective, two polars of thinking in microfinance movement (Moon, 2009). While the formers emphasis the importance for the MFIs to perform well in their welfare function of poverty alleviation, the later emphasis the importance of MFIs to be institutionally and financially sound. Empirically, both lines of thinking would have real world cases supporting them. Large scale government initiated programs of developing MFIs could be the case for the welfarist perspective, while small scale program of developing MFIs particularly those done by non-government organizations (NGOs) would support the institutionalist perspective—if they were able to maintain their mission in poverty alleviation. However, forcing the MFIs to survive out of their own business profits may lead the MFIs to also leave the poor and serve the better off in order to economize on transaction costs and get greater profit.

Moon (2009), however, suggests that it could be not an either-or position. It is possible to follow the welfarist perspective, providing support and subsidies for the MFIs, at least at the formation stage of MFIs and then let the MFIs go on their own, as institutionalist perspective would suggest, when they are ready.

It is not clear as to where the position of the government of Indonesia is in this debate. In case of AMFIs, the government seems to have let the AMFIs to develop on their own after being granted start-up capital although the government continues to provide government paid supervisors years afterward. However, in the district of Limapuluh Kota, one of three locations of this survey, the district government has been supplying good performing AMFIs with revolving funds of around Rp100 millions at subsidized rate to strengthen the AMFIs liquidity.

RESULT AND DISCUSSIONS

The Sample AMFIs

The 30 successful AMFIs taken as samples in this survey are located in three districts, 12 in Dharmasraya, 10 in Limapuluh Kota, and 8 in Pasaman Barat. These three districts are known for their large commercial as well as small scale plantation (palm oil, rubber and gambir) and transmigration settlements, particularly Dharmasraya and Pasaman Barat. Sawah cultivation is also an important economic mainstay in the three districts, particularly Limapuluh Kota.

As mentioned earlier, these AMFIs are considered successful because they are able to at least double their initial assets, the start-up capital of Rp100 million granted by the government to each AMFIs. As can be seen in Table 1, eight AMFIs (26,7 percent) have developed their total assets up to more than Rp1 billion while most of them (56,6 percent) have assets worth between Rp200 million and Rp500 million. The rest (17,7 percent) is between Rp500 million and Rp1 billion. Interestingly, most of these AMFIs (60 percent), and all the eight most successful AMFIs, are located in transmigration settlements. Local economic mainstay of villages where the AMFIs are located are predominantly land cultivation and plantation.

Tabel 1. Some salient features of the AMFIs according to class of assets

		AMFIs acc to class of asset*)			Total	
		Class 1	Class 2	Class 3	No	Percent
1	Number of sample AMFIs	17	5	8	30	100,0
2	Legal certificate					
	Have legal certificate	4	5	4	13	43,4
	Have no legal certificate	13	0	4	17	56,6
3	Forms of Legal Entity					
	Cooperative	0	4	2	6	20,0
	BMT (Shar'e)	2	1	4	7	23,3
	Ordinary microfinance	2	0	0	2	6,7
	Unclear	13	0	2	15	50,0
4	Communities					
	Transmigration	8	2	8	18	60,0
	Non-transmigration	9	3	0	12	40,0
5	Local Economic mainstay					
	Sawah	14	1	2	17	56,7
	Plantation	2	4	3	9	30,0
	Plantation and sawah	1	0	3	4	13,3
6	The Manager					
	Professional managers	14	4	8	26	86,7
	Non-professional managers	3	1	0	4	13,3
7	Reward to management					
	Salary or honorarium	8	1	4	13	43,4
	Percentage of yearly net income	9	4	4	17	56,6

*) Class 1 = less than Rp500 million; Class 2 = Rp500 million to Rp1 billion;
Class 3 = More than 1 billion

All of the AMFIs have been operating without any legal permit as required by Law No. 1/2013 on microfinance institution, although 43,4 percent of them have acquired certificates as legal entity from the government. Some of the AMFIs are said cooperatives or BMT (Baitul Maal wa Tamwil) or share AMFIs but not all of them are officially certified so. Some others are said ordinary microfinance, but most of the AMFIs have no clear legal entity at all. Nonetheless, as will be clear later on, all of them are actually functioning as cooperatives.

As to the management, 86,7 percent of the AMFIs are run by professional managers. The professional managers in this case are persons elected by the officials of the FFG (Federation of Farmers Groups), the FG (Farmers Groups), and their members based on consideration of their perceived potential ability in managing the AMFIs. In some case, the head of village or sub-village involved in the process of selection. All the managers are local community members, although not necessarily the member of the FFG, usually known as local prominent figures as youth activists or successful traders. In four other AMFIs, the managers were selected not based on consideration of their potential ability but because of their prominent social position in FG or in local community. Most of the managers has not been replaced since being appointed, implying stability and that the FGs' officials and members had not chosen the wrong persons.

The management of the AMFIs are typically consisted of 4 to 5 officials, only the biggest one has 19 officials. All the officials are rewarded for their works in AMFIs. In about 60 percent of the AMFIs, the officials received certain percentage of yearly net income of the AMFIs. In 40 percent of the AMFIs, the officials are given salary or honorarium but also received part of AMFIs yearly net income. The percentage paid for the officials ranging from two percent to 18 percent of total yearly net income. The average me

Members of the AMFIs is 257, ranging from the lowest 50 to the highest 700 with the highest also coincident with the biggest AMFI. All of the members are required to pay monthly principal contribution to their respective AMFI ranging from Rp1.000 to Rp100.000, with most required to pay around Rp5.000 to Rp10.000. The highest contribution is also required by the biggest AMFI. As in cooperative institution, the member are also required to pay obligatory deposit mostly ranging also from Rp5.000 to Rp10.000. In some AMFIs, they only serve their original members who are the members of the FFGs initially received the start-up capital granted by the government. In some other AMFIs, the non-original FFG members are allowed to get credit provided that they pay obligatory deposit and monthly contribution, and thus become members of the AMFIs. As already mentioned, the AMFIs are practically functioning as cooperative institutions.

Policies in Funds Mobilization

While there is hardly any debate on the roles of MFIs in general in helping the poor to live a better life, literature are debating on where should the funds used by MFIs to help the poor come from. Should the funds be raised by the MFIs themselves, that is from accumulating profit out of serving the poor, or should the funds come from grants or subsidized funds from government or other outsiders individuals or institutions? As shown above, welfarist and institutionalist perspectives are in the opposite positions on this questions. With regard to AMFIs surveyed in this research, the AMFIs have shown a remarkable growth rates in their assets, ranging from more than 100 percent up to more than 1000 percent, in less than 10 years. How has this been possible?

With regards to the source of funds, the AMFIs in fact have many. Aside from start-up capital granted by the government, obligatory deposit and monthly principal contribution from their members, the AMFIs accumulate capital from profits out of various services they provide. A couple of AMFIs are also selling stocks priced at Rp500.000 and Rp1 million each to the wealthy villagers. There are also six AMFIs that have used loan from commercial banks to increase their liquidity. Moreover, performed AMFIs in Limapuluh Kota district are also rewarded by the district government with revolving funds with subsidized interest rates. This fund, Rp35 million-Rp100 million, can be used by the AMFIs for three years and contribute much to improve the AMFIs liquidity. An AMFIs may also increase its liquidity by saving the funds of government projects such as for certain crop development and the construction of a market place. One AMFIs also receive grant from a legislative member's aspiration funds.

Various kinds of saving are also significant sources of fresh money for the AMFIs. These savings, offered to the villagers at large (not limited to the AMFIs members), and the number of AMFIs offering them are presented in Table 2.

Table 2. AMFIs according to saving they offered

No.	Name of Saving	Number of AMFI
1	Ordinary saving	30
2	Education saving	2
3	Student saving	2
4	Pregnant mother saving	1
5	Eid al-Adha saving	17
6	Eid al-Fitri saving	16
7	Saving for Ramadhan	1
8	Wedding anniversary saving	1
9	Umroh haj saving	2

AMFIs set various interest rates for these various savings ranging from one percent per annum to three percent per annum. The biggest AMFI, however, sets quite high interest rate, that is eight percent per annum. In general, the rates for the savings are about the same with the market rates. As shown in Figure 1, however, the average yearly saving trend is declining after peaking at more than Rp500 million in 2014.

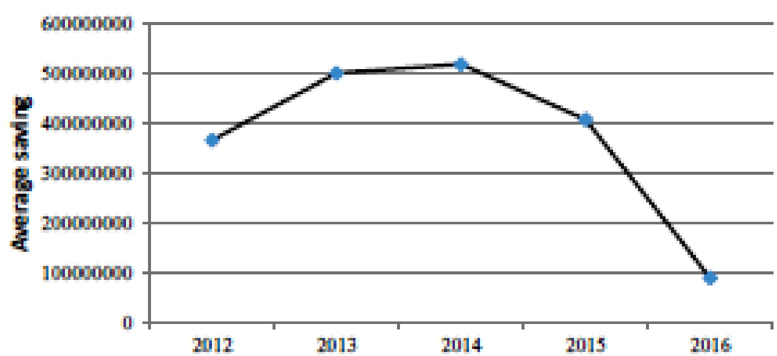

Figure 1. Trend of average saving in the sample AMFIs.

AMFIs also earn profit from interest rates or profit sharing (in the case of BMT) after providing various kinds of credits to the clients. Interest rates charged depend on duration of credit, the shorter the duration of the credit, the higher the interest rates, and vice versa.

Different AMFIs charge different interest rate but in general the interest rates are between at minimum 12 percent per annum and at maximum 18 percent per annum. Non-members clients are usually have to pay higher interest rates than the lending members. Some AMFIs also provide weekly credit with interest rate 2,5 percent per week. Duration of credit ranges from a week to four years. The amount of money lent by the clients also varies, mostly at around Rp 1 million to Rp5 millions with the lowest found at Rp200.000 and the highest at Rp50 millions.

Figure 2 shows the trend in average lending of the sample AMFIs in the last five years. The trends, as in the case of saving, is declining after reaching the maximum at more than Rp700 millions per year per AMFI in 2015.

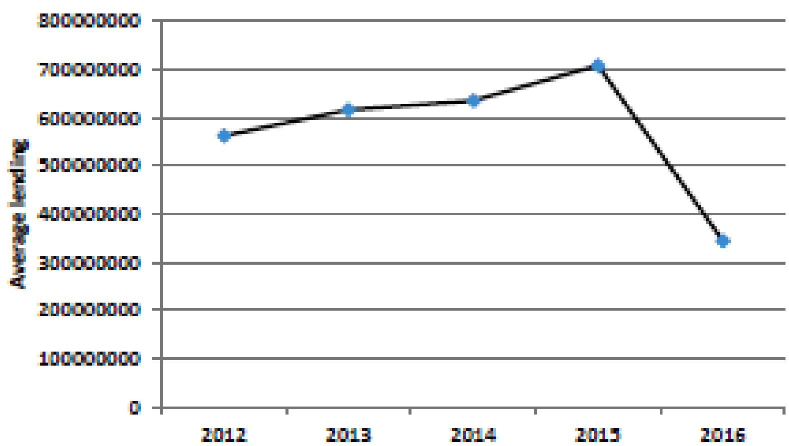

Figure 2. Trend of average lending in the sample AMFIs

Both declining average saving and lending trends may be signalling problems below the surface of these successful AMFIs. However, based on their policies in interest rate and seeking any source of funds it is clear that the AMFIs are trying hard to mobilize funds for their continuous operation.

Policies in Credit Delivery and Repayment

The single most crucial factor determining the viability of an MFI, as any commercial bank, is credit repayment. Policies in ensuring repayment are closely related to policies in credit delivery, both policies will affect the survivability of the MFIs. In commercial banks, they can choose their clients and require them to provide collateral as credit provision in order to ensure that risk of default are not detrimental to the viability of the banks. In MFIs, unlike in the formal banks, they are expected to help the poor segment of population (it is even explicitly stated in the definition of MFI in Indonesia's Law No. 1/2013 on MFI). As such, the MFIs may not be able to impose the requirement for their poor clients to provide collateral as commercial banks usually do to their wealthy clients. Most of the poor are so low in assets ownership that they would choose to not using credit rather than risking the only assets they have.

How the AMFIs, as any MFIs, deal with this issue may determine their identity as finance institution of the poor. Literature on this, fortunately, is abounding. But, unfortunately, the recommendation on this is limited, mostly refers to the Grameen Bank approach of group lending. If the clients are too poor to provide meaningful real collateral, use social collateral. Let the clients supervise each other so that credit repayment is ensured or else everyone in the group will have to pay or not getting any chance of using credit at all in the future until the credit repaid. In West Sumatra, the concept of social collateral has been widen to include community pressure by involving adat (customary) leaders or even shaming those who do not repay their credit by announcing their debt in the mosques. How have the successful AMFIs deal with this issue?

In this research, however, it is found that, except one single AMFI, none of the successful AMFIs have chosen group lending as their method of credit delivery. All AMFIs require real collateral like land certificate or certificate of ownership of vehicles (usually cars or motorcycles) or even television sets. However, in some AMFIs, treatment may be different if the clients are villagers known to AMFIs' officials which is most of the case when the clients are also the members of AMFIs and involving amount of money not more than certain minimum limit. Some AMFIs impose the minimum limit at Rp500.000, while other at Rp1 million. Moreover, in some AMFIs, the projects to be funded are checked to ensure that they are in fact true. To further ensure the proper use of the credit, 60 percent of the AMFIs provide assistance about how to do good businesses, including for example how to farm maize appropriately. Forty percent other AMFIs have not doing anything like this.

As to the outreach, most AMFIs prioritize the member clients. Non-member clients are only served when internal needs are fulfilled, with higher interest rate, and if they have real collateral. Since there are a number of rural poor, mostly are also farmers who are not the members of any FG or FFG, do AMFIs serve these people? Ten AMFIs said they did not, nine AMFIs said they would if the repayment seemed guaranteed and only 11 AMFIs have actually done this. Moreover, these AMFIs seem to concentrate on productive credit, leaving consumptive credit beyond their duties.

Given precaution on to whom and for what purposes and on what requirement the credit to be delivered, how have the AMFIs really performed in credit repayment? Data on non-performing loan for the last five years is mixed. About 25 percent (eight AMFIs) report no NPL at all. The remaining 75 percent report the existence of the problem of NPL. Some AMFIs report NPL in only one year or more in insignificant amount, but quite a number of them (four AMFIs) are actually overwhelmed by the problem of NPL. Some AMFIs have NPL amounting to tens of millions every year.

When asked about their main problems in managing AMFIs, the management of the AMFIs, however, confirmed the threat of NPL. About 75 percent of the management said NPL as their main problem. Other found problems in finding funds to operate, competing with other government sponsored program of Small Business Credit, and lack in management capacity.

Concluding Remarks

Previous narration shows that despite their remarkable performance, the successful AMFIs are actually struggling for their existence. Firstly, there is a tendency that the trends in saving and lending are declining in the latter years. The findings on NPLs and problems faced by the AMFIs management in finding funds to operate must be closely related to this negative trend. NPLs makes funds unavailable for paying both due saving and new loans. This may build distrust of the clients toward the AMFIs and then withdraw from saving their money in the AMFIs. Secondly, it is likely that the AMFIs in their operations have left the need of the poor unattended. The AMFIs policies in providing loan to non-members and the requirement of real collateral instead of some forms of social collateral must have deprived the poor segments of the villagers, members or non-members of the AMFIs, from fulfilling their need for credit. Research by Elhakim (2017) in Limapuluh Kota district reveals that, on average, the AMFIs fulfil only 66 percent of the capital needed by rice farmers.

Although this struggling feature of the successful AMFIs may have been due to the unclear government policy implementation, for example in having let the AMFIs use real collateral instead of social collateral based on group lending, and instead of developing capacity by concentrating their service on internal FGs members, the AMFIs may have let themselves to expand earlier than it should be, but with shaky bases. It is as if the AMFIs have advanced toward institutionalist perspective on MFI development, as if they are already able to survive on their own, and the government therefore can leave them as such. But it might be too early for most of them. Some who force their way toward that direction may find they actually have market but, at the same time, they also have to leave their mission in helping the poor farmers.

Based on these findings, it may be good to have more research on this involving more AMFIs to have a more solid conclusion. In the mean time, it is worth suggesting that the government pay attention to persuading the AMFIs to first build their capacity to help their poor farmers members before starting to expand and get bigger.

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