Village Banking in Upland Communities

The role and relevance of village banking

Attempts to increase income are often related to an investment. Labour, money, know-how and other inputs have to first be supplied in order to obtain a return, which is expected to be higher than the value of the invested goods. An initial accumulation of assets is thus a necessary precondition. Increased economic security, too, is obtained by accumulation of assets, which, in times of need, will cover indispensable expenses like food or medical treatment.

Assets can be accumulated either by forgone consumption (saving) or by repayment of borrowed assets (loaning). Poor people tend to focus on buffering their fragile livelihoods by saving or borrowing small amounts. The better-off can afford to make bigger investments, or deposit bigger amounts.

The formal bank system in Laos so far has little outreach into poor rural areas. Where there is no project intervention, villagers depend on relatives and moneylenders for credit. Relatives can lend only limited amounts, while moneylenders are very expensive, at monthly interest rates of 10% or more. For savings, people have to rely on in-kind savings (e.g. jewellery or livestock) and cash stocks kept in the house, which is both unproductive and insecure.

The Lao-German Programme for Integrated Rural Development of Mountain Areas in Northern Laos (RDMA) aims to stabilise and possibly increase household income in target villages by creating opportunities for micro-savings and credit that are accessible at village level. In its search for a financially and organisationally sustainable solution, the Village Bank model has been chosen and adapted to local conditions.

Village Banking is not a remedy for poverty and its various symptoms, but is rather a facility to be used in alliance with other business and infrastructure services. Carefully implemented, it can have a considerable stabilising and increasing effect on the income of both poorer and better-off households.

Village banks: A specific type of micro-finance

A Village Bank is a tiny cooperative bank normally run by the community of a village. Its customers, who are at the same time its members and owners, can deposit money in their savings accounts, or borrow small and medium funds for various purposes. The income obtained through interest on credit is, after deduction of costs, redistributed to savers as a yearly dividend. There is no common fund, only savings privately owned by its member-customers. Thus these banks mobilise internal resources and responsibility and optimise the feeling of ownership.

Because of the low level of development in the target villages selected, the RDMA project offers a grant facility to increase the impact of Village Banks.

Generally, the establishment of a sustainable and socially compatible financial system is the main priority, rather than the stimulation of particular activities (like agricultural production) or the pursuit of particular group interests (such as 'credit to the poorest'). The philosophy is that a well-designed and well-developed system will be able to support the needs of the broadest possible range of people.

The Genesis of a Village Bank

RDMA aims at a minimum of regulating, and a maximum level of self-management and self-determination among its Village Banks. From the very beginning, and with a few exceptions concerning the payment of project grants, decision-making is left to the villagers, and the role of outside support is limited to facilitation, counselling and provision of a project grant. The preparatory process leading to the foundation of a Village Bank needs time – three to seven months - and consists of a partially formalised but highly flexible process. This includes '10 Steps' of continuous village meetings, a study tour to a village with a well-run Village Bank, and finally training in management, organisation and accounting for future committee members.

Just as crucial to success is the careful follow-up of newly-founded Village Banks. Coached by the project team, the community, the committee and the single members learn by doing. All the actors gain experience in their new options and responsibilities, seeing that problems are to be solved before they become big. It takes from six months up to several years, before a Village Bank is mature and does not rely on regular outside support anymore.

Striving for sustainability, RDMA hopes that the Village Banks will become independent from both project and government. The plan is to initiate a Village Bank Association that will be responsible for future servicing of the Village Banks, helping mainly with accounting, supervision, problem solving and lobbying. It is envisioned that this association may grow to be a type of cooperative bank, replacing the VBs themselves.

So far the RDMA has set up 36 village banks in Sing and Nalae Districts, Luangnamtha Province. Table 1 highlights a number of relevant figures.

Key elements of Village Banking

- Village Banks are owned and managed by village members through a members' assembly, which is the highest decision-making body.
- An elected Village Bank Committee conducts day-to-day management.
- Except in emergencies, members pay in or withdraw on monthly service days.
- Initial 'outside' start-up advice and periodic methodological support is required. This responsibility is ultimately to be transferred to an independent Village Bank association.
- Interest earned on credits by the bank must, in the long term, cover all costs including future servicing, remuneration for Village Bank Committee Members (VCMs), and yearly dividends.
- Members agree on a minimum compulsory savings amount, which must be small enough not to exclude the poorest groups. In most instances, this is 2,000-5,000 Kip per month. Besides that, members can save additional, voluntary amounts.
- Villagers agree on criteria and activities suitable for loans.
- Interest on credits must be paid monthly. Delay of payment without notice attracts a penalty - normally double payment next month! Interest rates normally depend on the activity related to the loan, these range from 0.5 to 5% per month. Loans for emergency cases are normally interest-free for a two to three months' period.
- Priority is given to saving withdrawals over new credits (if funds are limiting).
- Provision of credit for long-term and low return investments, e.g. large animal raising and plantations, has to wait until the demand for short-term, high interest rate loans is saturated, and money is no longer scarce
- Credit ceilings are put in place to diminish the risk in case of loan default, and ensure that more members can get loans during the start-up phase. Loans are commonly limited to a duration of five or six months. As the bank's capital grows, ceilings are extended, with additional collateral demanded for bigger loans.
- Credit is protected through various social and economic mechanisms such as social pressure and guarantees given by relatives, as well as physical collateral like livestock and the loan-taker's saving deposit.

Table 1: Village Banks in Luangnamtha (part of RDMA project area) as of April 2005	
Item	**Total**
Number of Village Banks:	16
Percentage of family members to total amount of families (range):	86.2% (69- 100)
Total equity:	187,977,500 Kip
Percentage of internally created capital to total capital:	32% (18 - 59)
Project grant (5 times the amount of money initially saved by each family): up to max. amount per family, paid in two instalments	max. 300.000 Kip
Repayment Rate	100%

Case study: two Village Banks in mountainous areas

The two neighbouring villages of Ban Longmounechomgaeo and Ban Longmounexingxai, both Khamu Youane villages, started out with similar economic situations after resettlement in 1999. Both villages set up Village Banks in 2004. Today however, the way these villages, their village banks and the villagers that support them have developed is markedly different.

Reasons cited for the success of the Village Bank in Ban Longmounechomgaeo are that leadership is strong and many villagers engage in more profitable and diverse activities other than shifting cultivation. Money seems not to be a serious bottleneck, as there are many savers but few loans. A considerable amount

Table 2: Village Banks in Longemounechomgaeo and Longmounexingxai		
Item	**B. Longmounechomgaeo**	**B. Longmounexingxai**
Number of families	78	6974
Number of VB members	78+5 individual memberships	69
Equity (at 25/9-04)	38,700,000 Kip	11,600,000 Kip
Internally created capital	70%	38%
Current number of credits	14	40
Average credit amount	2,360,000 Kip	342,000 Kip

Ban Longemounechomgaeo

Ban Longmounexingxai

has been paid in credit to outsiders. The much poorer Ban Longmounexingxai is described as having weak leadership and villagers continue to rely on traditional slash-and-burn upland rice production. They take many small loans, mostly for emergency cases.

Lessons from the field

Experience to date shows that sustainable financial services are an essential and viable supplement for upland villages in their progression towards a market economy. Villagers can access saved money and take credit as an insuring safety net for emergency situations, and for investments which need an accumulation of initial capital such as agricultural or off-farm activities, or for private investments like weddings and house construction.

Cohesive communities with strong leaders and committed, educated committee members will quickly conceptualise and manage the Village Bank with minimal outside help. Weak village communities with low-skilled and inexperienced committee members need longer term support before being able to work independently. The relative success of banks is directly related to the type and character of leadership involved.

Poor people save small amounts and take small loans, which they mainly use in emergencies such as during periods of sickness or rice insufficiency, or for income-generating activities like small animal raising. Better-off people deposit bigger amounts and take bigger loans, which may be used for large animal raising, trade or for private purposes. Poor people are

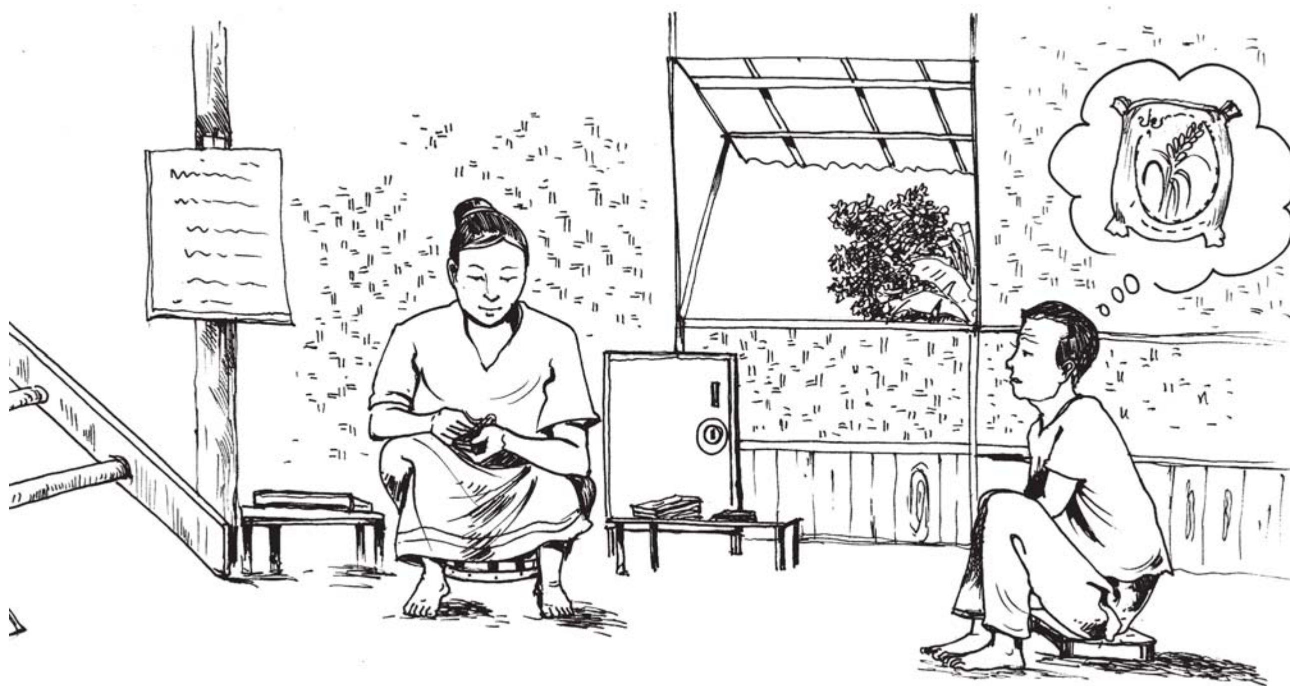
often more reluctant to borrow money for production purposes, as it increases risk.

Scope and conditions for village banking differ from village to village. Poor villages and villages with poor market access will deal with smaller amounts of money than better-off villages close to a major market. At the same time, this fact makes them relatively more expensive to service.

In some village banks there is a cash surplus. In others, immediate demand for credit exceeds the available funds. As long as money is scarce, and there is a continuously unsaturated demand for short-term, high-turnover loans (emergency, trade, small-animal raising), bank capital is too little and the interest rate normally too high to serve bigger, long-term loans e.g. for large animal raising or perennial crops.

The majority of farmers will not use loans to invest in 'new' alternative productions, because credit increases risk and hence vulnerability. They prefer to stick to their indigenous investment practices: new technologies are tested at a micro-scale and with minimal financial investment, and are gradually adapted to the conditions. If successful, the profit is re-invested, and thus production increases slowly.

Micro-finance is about attitudes and social skills as well as economic issues. A successful Village Bank will strengthen the whole community and its members in their capacity to find local solutions to a range of problems. The investment attitude of villagers towards concepts such as loans, savings, risk assessment and re-investment, is stimulated. Thus, skills development occurs alongside savings, and credit increases.



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