The Status of Agricultural and Rural Financial Services in Southern Africa 2011

March 2013

Zambia country report

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Abbreviations

AMIZ	Association of Microfinance Institutions of Zambia
ASCA	Accumulated Savings and Credit Association
ATM	Automated Teller Machine
BETUZ	Basic Education Teachers' Union of Zambia
BOZ	Bank of Zambia
CAZ	Cotton Growers' Association
CRB	Credit Reference Bureau
CSO	Central Statistics Office
CUSA	Credit Union and Savings Association of Zambia
DBZ	Development Bank of Zambia
DFA	District Farmers' Association
DFID	UK Department for International Development
FAO	(United Nations) Food and Agriculture Organisation
FEF	Financial Education Fund
FMT	FinMark Trust
FSDP	Financial sector development framework
FSDP II	Financial Sector Development Plan Phase II
GDP	Gross Domestic Product
GNI	Gross National Income
GRZ	Government of the Republic of Zambia
GTAZ	Grain Traders' Association of Zambia
IFAD	(United Nations) International Fund for Agricultural Development
ILO	(United Nations) International Labour Organisation
JSE	Johannesburg Stock Exchange
LCMS	Living Conditions Monitoring Survey
LUSE	Lusaka Stock Exchange
M4P	Making Markets Work for the Poor
MBT	Micro Bankers Trust
MCDSS	Ministry of Community Development and Social Services
MFI	Microfinance Institution
MoFNP	Ministry of Finance and National Planning
MoH	Ministry of Health
NAPSA	National Pension Scheme Authority
NSCB	National Savings and Credit Bank
PIA	Pensions and Insurance Authority
PMU	Programme Management Unit
POS	Points of sale
PROFIT	Productivity Finance Technology / USAID
REES	Rural Economic Expansion Services
ROSCA	Revolving Savings and Credit Association
SACCO	Savings and Credit Cooperatives
SADC	Southern African Development Community
SEC	Securities and Exchange Commission
SIDA	Swedish International Development Agency
SNDP	Sixth National Development Plan
TAZ	Tobacco Association of Zambia
UNCDF	United Nations Capital Development Fund
USAID	United States Aid and International Development
VSLA	Village Savings and Loans Association
WFP	(United Nations) World Food Programme
ZAMACE	Zambia Agricultural Commodities Exchange
ZBS	Zambia Business Survey
ZIPSS	Zambia Interbank Payment and Settlement System
ZNFU	Zambia National Farmers' Union
ZSIC	Zambia State Insurance Corporation

Acknowledgements

This study relied on secondary data in the form of various reports and documents reviewed, together with FinScope data for Zambia, and input from the various industry players and stakeholders. The authors are grateful to all industry players and stakeholders that participated in this study.

The authors wish to convey special thanks to Juliet Munro, FinMark Trust Zambia Coordinator and Mike de Klerk who reviewed the first draft of the paper, and provided valuable insights and useful comments.

Limitations and disclaimer

This report is based on information from various reports reviewed, as well as information from interviews with relevant industry players and stakeholders. The analysis is only as reliable as the data and information upon which it is based. While reasonable steps have been taken to ensure the validity of the data and information, the consultants can accept no liability for errors in the investigation arising from incorrect data or information. This report must be read as a whole and considered in its entirety, as parts taken in isolation could be misleading.

1 Executive summary

Background

FinMark Trust (FMT), an independent trust based in Johannesburg, South Africa, was established in 2002, and is funded primarily by UKaid from the Department for International Development (DFID) through its Southern Africa office. FinMark Trust's purpose is 'making financial markets work for the poor, by promoting financial inclusion and regional financial integration'. FMT does this by commissioning research to identify the systemic constraints that prevent financial markets from effectively reaching out to the poor. It advocates for change on the basis of analytic research, and uses research findings to help shape the types of policies, frameworks and market conditions that ultimately lead to the development of inclusive financial systems.

In Sub-Saharan Africa most people still live in rural areas where agriculture is the mainstay of the rural economy. According to the FinScope Zambia 2009 survey, 62 percent of Zambia's adult population lives in rural areas[1]. Moreover, almost 90 percent of Zambians who live below the extreme poverty line are concentrated in rural areas, and the poverty gap ratio (a measure of how far average incomes fall below the poverty line) is far higher for the rural population than their urban counterparts (20 percent and 3.7 percent, respectively). Overall, 30 percent of adults (rural and urban) say that they rely mostly on agriculture as a source of income, and over half the rural population (53 percent) report agriculture as being the only source of household income[2]. The overall level of population in rural areas, combined with household dependency on agriculture in rural areas especially, point clearly to the need for policies, strategies and operational actions that stimulate and reinforce agricultural and rural development.

Increasing access to, and improving the quality of agricultural and rural financial services across target agricultural and rural businesses, and other target market segments is highly relevant to national strategies for economic and agricultural sector growth, poverty reduction, and food security. At household level, well-designed and well-targeted inclusive financial support will be a catalyst for economic strengthening and for accelerating the transition of the poorest and low-income families out of poverty. Moreover, increasing women's equitable participation in agricultural and rural markets through the adoption of 'gender-smart' policies and intervention strategies will contribute to poverty reduction, and to achieving national development and Millennium Development Goals.

1 In this survey, the definition of 'rural' and 'urban' follows that of the CSO, where rural and urban is defined according to enumerator areas in its master sample frame based on population density.
2 This includes the sale of crops, livestock, or poultry and/or the sale of agricultural by-products.

Objectives, ambit and methodology

Sponsored by FinMark Trust, this country study examines the status of agricultural and rural finance in Zambia in order to better understand the context and progress-to-date in financial sector development, and the nature, extent, and causes of the problems and challenges that are hindering growth and realization of financial sector development goals. Based on these findings and the implications for sector growth, the study derives a set of practical recommendations for effectively addressing cross-sectoral problems and challenges.

The study for Zambia is one of six Southern African Development Community (SADC) country studies[3] and represents the first phase of a three-phase programme envisaged by FMT. The findings of the first phase are intended to contextualise and provide the basis for the second and third phases of the programme. The essence of the second phase is to identify best current practices and innovations from across the African and international spectrum that are amenable to adaptation and application in the SADC region. The objectives of the third and final phase will be to use the research findings of the first and second phases in order to work with policymaking and strategy-formulating bodies in the public and private sectors of the six countries to develop or enhance policy frameworks and strategic approaches, to assist countries toward operational action, and to provide a benchmark and structures for monitoring progress in deepening financial inclusion in agricultural and rural finance in the region.

In addition, the study provides a practical point of reference for those seeking to understand the financial services marketplace and the stakeholders involved. It elaborates on existing sector support frameworks, contextual factors, promising new developments and, in contrast, the persistent obstacles and challenges to financial inclusion, which ensue from demand-side and supply-side constraints; all of which impact on rural economic growth and prosperity.

The study, which covers developments up until December 2012, used desk-based research and analysis of existing financial sector studies[4] and data information coupled with select meetings and interviews for updates, status reports and verification purposes. It was conducted amidst contextual variables and new developments not least of which include: –

- legal and regulatory reforms in the banking and non-banking sectors;
- extension of the national financial sector development programme through 2014;
- Government of Zambia's (GRZ) decision to establish a rural finance unit within the Ministry of Finance and National Planning (MoFNP);
- commencement of DFID's Access to Finance programme in early 2013;
- design of a new GRZ / IFAD rural finance programme (starting 2014); and
- roll out of national strategies on microinsurance and financial education.

3 The other SADC countries where studies were undertaken are Botswana, Malawi, Mozambique, South Africa and Zimbabwe.

4 The reference section provides a list of key documents analysed.

The report echoes government's recently developed rural finance policy and strategy document, which endorses the principles and practices of 'making markets work for the poor (M4P)' as a framework for designing, implementing and evaluating financial sector development. 'M4P' is a practical approach to reducing poverty, grounded in best practice and guided by four underlying principles: systemic action, sustainable change, large-scale impact, and facilitative role.

The study seeks to understand the nature and extent of financial sector problems and challenges by analyzing and comparing the demand for, and uptake of, financial services with supply across the various levels of Zambia's agricultural and rural economy. Where appropriate, the study adopts a structured analysis of the contextual factors at the macro, meso and micro levels of the financial sector, which are either enabling or disabling progress in the provision of financial services to farmers, other businesses and households. The analysis at macro, meso and micro levels includes an examination of:

- Macro-level: macro-economic policy and financial sector legislation, regulation and supervision.
- Meso-level: industry-wide infrastructure and systems (e.g. for market trading, financial transactions or assessing creditworthiness), as well as auxiliary organizations, and financial sector representation.
- Micro-level: individual financial service providers' products, services and delivery channels with respect to credit, savings, insurance and transactions services.

Though the study offers a deep examination of demand-and supply-side constraints, as well as the enabling environment, infrastructure, key players and products, services and delivery approaches, it does not go as far as evaluation of policies, programmes or initiatives nor does the report specifically address impact. However, on the basis of thorough situational analysis, the report findings point to key implications and practical recommendations for strengthening sector support.

Demand-side analysis - Top-line findings

1. The demand-side research reveals that rural households and enterprises have a need for various types of financial services. In a number of cases, the study shows that supply of rural financial services is also a strong demand factor; the lack of supply of financial services to rural areas has also accounted for the nature and level of demand. For instance, looking at existing financial services, for credit, the lack of access for rural enterprises, especially small-scale farmers, and the concentration of credit supplied to large commercial farmers reinforces the big gap between the value of loans received respectively by small-scale and by commercial farmers. This contributes to the belief among small-scale farmers that rural credit is not designed for them.

2. The study also shows that the uptake of financial services in rural areas is influenced by various demand factors that can be broadly categorised as: (1) need, (2) knowledge and (3) access.

3. Under need, the study revealed that there is a thin line between household and enterprise need particularly because most rural households rely on farming as a major source of enterprise and household income; this is actually the case of most low-income households in Zambia be it in rural or urban areas. Consequently when thinking about rural areas, it is imperative to take into consideration both household and enterprise needs.

4. The income from agriculture is erratic and lumpy. Income seasonality analysis revealed that income for most rural households depends heavily on the performance of agricultural activities during the rainy season. Any disruptions in the rainfall pattern and performance negatively impacts on income. Unfortunately rural households usually do not have/use any formal risk management financial services.

5. Rural households can benefit from accessing and using several financial services including credit, savings, insurance and transactional services. Usage of these services, in part or whole, can enhance their financial security and economic resilience.

6. Under knowledge, the rural markets are characterised with a low understanding of most financial services and this, in part, is influenced by the lack of exposure to, and experience with financial services. The study revealed that a lack of knowledge of financial services partially accounts for the negative perceptions and/or by misconceptions around financial products.

7. Under access, again, both demand and supply factors come become relevant The 2009 FinScope survey revealed that 66% of adults living in rural areas do not use any formal financial service; this is higher than the proportion of adults in urban areas, which stood at 58%. In terms of usage of formal financial services, only 8.6% of adults in rural areas use formal financial services compared to 22.6% for urban areas.

8. As 70% of MSMEs are located in the agricultural sector, their challenges include limited physical access to financial services. Furthermore, the high costs of maintaining access also mean that MSMEs cannot afford to use financial services. There is also a very limited range of products on offer, and a dearth of appropriate services for agricultural MSMEs.

9. FinScope data also shows that physical access is not necessarily a prerequisite for uptake. To address uptake issues, it is imperative to understand the demand constraints including affordability, product appropriateness and issues of perception and trust. The design and supply of rural finance should ideally encompass the needs of both rural households and enterprises. The sustainable flow and uptake of rural finance also has to take into account issues around cost of services and sustainability of operations of financial service providers.

Supply-side analysis – Top-line findings

1. Under the IFAD-funded RFP and work of the FSDP, policymakers, regulators, and support institutions have formulated a policy framework for rural financial sector development. However there is scope to provide a more comprehensive policy and intervention framework and set of guidelines that focus on stimulating micro-level investments by financial service

providers in rural finance and guide the implementation of holistic approaches required to embrace both demand and supply constraints.

2. The bulk of finance flowing to the agricultural sector is targeting commercial level producers and agricultural processors. Only a handful of financial service suppliers are actively engaged in rural and agricultural finance. The overall consensus is that agricultural business finance is expensive and difficult to obtain with the exception of the largest lead firms.

3. Up-to-date and collated information on actual numbers served, and the value of portfolios for savings, credit and insurance at the emergent and small-scale farmer levels is not readily available, but it is known from existing demand-side data (e.g. the FinScope Survey, Zambia Business Survey, Agclir Zambia Report, and ZNFU/PROFIT Agricultural Finance Report) that outreach remains extremely shallow and there is a lack of appropriate products and services, particularly at the lower end of the market.

4. Agricultural credit is insufficient and unevenly distributed on the basis of three factors:

   - Credit flows are highly unevenly distributed across the sector, with the bulk of finance going to commercial level agriculture.
   - Agricultural businesses, particularly those involved in the production of field crops, are intensive users of credit. Seasonality and cash flows associated with agricultural production means that farmers are very reliant on credit.
   - Levels of credit overall in Zambia are low compared to neighbouring countries.

5. On the supply-side key constraining factors include viability challenges and high cost structures of operating in rural areas and lack of affordability and appropriateness of products and services. The current costs of maintaining a physical presence in rural areas, as well as the real and perceived risks related to lending in agriculture have resulted in cost structures and prices, which are unaffordable for many rural businesses and individuals. Product appropriateness also remains a challenge as suppliers apply layered risk management strategies to products and service delivery resulting in products that are unsuited to borrowers' needs.

6. Despite the growing proliferation of market-led financing models, aside from Zanaco's Lima programme, it is notable that there are very few examples of supplier models working at scale. Key factors constraining the replication and scaling of promising financial models include a lack of means and support available, and a lack of information on overall market potential in many agricultural subsectors.

7. Suppliers lack understanding of agricultural and rural financial needs, particularly small-scale farmer and household needs. Another information gap lies in the better understanding of growth potential in agricultural markets - financial service suppliers do not have detailed information on the growth potential of agricultural/agribusiness subsectors and value chains and on specific target groups (e.g. the number of potential borrowers for tractors and farm machinery is currently unknown).

8. The microfinance sector remains under-developed and there is a fundamental question over whether formal MFIs really have the capacity to be cost-effective suppliers of rural credit. Only five out of a total 26 microfinance institutions are deposit-taking developmental credit providers (microenterprise focused), and only four of these are actively reaching out to low-income rural and agricultural communities. MFIs have been very slow to initiate deposit-taking services in rural areas.

9. With respect to savings, the mismatch between supply and demand is compounded by key disabling factors based around accessibility, affordability and cost, and product appropriateness. Furthermore, the realities of income seasonality means that rural households only have cash at certain times of the year – and there are business and household pressures on usage of this income. Consequently well-targeted savings products will need to align to these needs and interests, and ensure that the mobilization of cash has tangible benefits and helps drive growth and improve household economic security.

10. Low market penetration of insurance products has a direct bearing on low levels of exposure to insurance. However, insurance companies investments in market research, product development and marketing will only go so far – with the current low levels of understanding of insurance, as well as misconceptions around the concept of insurance, and distrust[5] of insurance companies, it is imperative that strategic investment in consumer education takes place.

11. Agricultural leasing is not well developed, and current leasing tax laws are a disincentive to lease financing. However, there are a number of small-scale partnerships involving commercial banks and market development programmes, which focus on opening up leasing finance for agricultural equipment for emergent farmers.

12. There is a notable absence of informal, community-based savings and credit institutions. Ultimately, the reasons for this are not clear and there is justification for research to explore and identify preferences, levels of demand, and potential for scale with respect to future potential for community-based finance models in rural areas. There are significant information gaps regarding the distribution, scale and functionality of Accumulated Savings and Credit Associations (ASCAs) and Savings and Credit Associations (SACCOs) in rural areas.

13. Whilst banks and MFIs grapple with the challenges of bringing sustainable access to formal services to rural communities, with the right support structures, approaches and technical resources, community-based finance, e.g. Village Savings and Loan Associations (VSLAs), could play a vital role in offering rural Zambian populations access to productive credit and financial safety nets.

14. There is a lack of appropriate financing for MSMEs in rural areas. However, MSME performance has to improve for MSMEs to be attractive to financial suppliers. As it stands, access to finance alone will not drive growth in MSME productivity. For this to happen, a

[5] FinScope 2009 data.

combination of measures is needed including: improved access to infrastructure (roads, electricity, communications, etc.); increased education levels and business management skills; and increased business facilitation support to strengthen the platforms on which businesses grow.

15. There is strong justification for designing and increasing access to well-structured market-led incentives or subsidies, which, if done well, can effectively stimulate financial service innovation and scale-up by bringing down risk in the short term. However, more research is needed into what those incentives should look like and where they could best be targeted.

16. Opportunities exist for ‘fast-tracking’ financial access and inclusion through effective and scalable mobile banking and payment systems models. The relatively hands-off approach of the government and BOZ, and their deliberate policies to not overly control market developments, has resulted in increased cross-sector collaboration and experimentation. However, there is work to be done to complete regulations and guidelines for usage. Though developments are on the right track, widespread confidence in, and usage of accessible and affordable mobile banking and payment systems, in rural areas especially, is still a long way off.

The Access-inclusion gap

1. Financial inclusion initiatives are unlikely to succeed unless people have the knowledge, skills and confidence to make effective use of financial products. The tripartite and simultaneous approach of financial education, financial inclusion initiatives and financial consumer protection has a vital role to play, as none is likely to be sufficient on its own to achieve the goal of greater, more sustainable financial inclusion.

2. Macro, meso and micro level players can all play a role in implementing parallel, complementary initiatives to build inclusion, improve consumer protection, and stimulate the development of innovative, appropriate financial services for rural businesses and households.

3. Constraints to pro-poor sector growth in rural areas extend well beyond access to finance – financial service development therefore has to be coupled with production and market development support (infrastructure, market linkages, skills and knowledge development, etc.). Moreover the need for more complete and effective retail infrastructure encompasses market place infrastructure, and as such the need for sound policy and regulation in areas such as branchless banking and payment systems, consumer protection, and legal recourse.

4. Human resource and systems capacity weaknesses, and the risks associated with them span all levels of the financial sector, from top level leadership down to community-based leaders and treasurers tasked with recording and protecting a village savings group's finances. These weaknesses are constraining factors that if left unabated will have a significant negative impact on progress towards financial inclusion, but they also represent an opportunity for timely, constructive investment in human capital development.

Based on the findings, the following serve as key recommendations:

Macro-level

1. Incorporation of a research and development component within one or more national level programmes to identify new developments and innovations in rural and agricultural finance.

2. Introduce and support a framework for knowledge management. Some appropriate ways of bringing learning to Zambia and expanding in-country learning could be through the sponsorship of industry-wide learning events or hosting of events such as a high-level annual financial sector conference, the publication of financial sector bulletins, sponsoring and publishing research studies and papers, as well as integrating formal appraisal and feedback mechanisms, case study development and documenting of best practices into contract agreements, MOUs, etc.

Meso-level

3. Support to sector associations and support agencies (e.g. PIA, BAZ, AMIZ, CRBAL) to strengthen their business models and capabilities for supporting their membership.

4. Representative organisations need to equip themselves with the tools, resources and management capacities to effectively respond to needs and ensure efficient and appropriate targeting of resources.

Micro-level

5. Sector support will need to be demand-driven, but it should also be packaged in such a way as to promote and significantly contribute to industry strengthening.

6. Increased market information and feasibility studies (commissioned by or for suppliers) on growth opportunities need to be conducted for specific rural and agricultural market segments, including more concrete data on potential demand (potential scale and outreach numbers, potential portfolio sizes, and costs and timelines for achieving break-even levels).

7. Increased investment in research and development, piloting and testing of innovative product design and delivery, and support for scale-up of successful pilots.

8. Product feasibility assessments on business and financial service models that propel growth in agriculture in rural areas and that enhance financial management skills among rural households, leading to household economic strengthening.

9. Financial suppliers, and those supporting sector development, need to maintain a flexible approach, continually monitoring market developments, reading market signals, and anticipating unintended outcomes as best possible, with a view to re-prioritizing, and adjusting strategies and interventions in a timely manner. First and foremost, however, is the need to sharpen focus and quantify market opportunities in agricultural and rural finance.

10. Increase focus and support to grow informal community-based financial services, including sound market research and contextual analysis to determine appropriate support, and analysis of best practice and regional experience in developing good models of structure, governance and operational procedures, as well as approaches for ensuring sustainability, transition to semi-formal associations and preparedness for formal financial inclusion.

11. Support product and service development that is tailored to the needs of households and businesses, which are at different economic levels.

12. Leverage recent developments in the use of mobile phone and other technologies (e.g. smart cards, e-vouchers, etc) and further engaging technology service providers to develop cost effective solutions to financial access and inclusion challenges.

Cross-cutting

13. Encourage and support the design and roll-out of risk reduction mechanisms that are market-led and incentivize private sector involvement, e.g. the use of a part-guarantee fund, which then allows a financial institution to extend loans or leases for agricultural equipment; or part contribution (or time-bound support) to cover the salary of a technical field expert who works on behalf of a lead buyer to help small-scale farmers improve production yields - the technical expert eventually being recruited on a full-time basis by the lead buyer (or by a collaborating financial institution).

14. Encourage the use of smart subsidies (assisting with research and development if need be).

15. Short-term strategies for strengthening the sector should involve industry representative institutions such as IAZ, BAZ and AMIZ. Support efforts should build the capacity of these institutions to identify institutional needs, and determine client-centred approaches for packaging technical training and learning forums that impart latest approaches in product development, outreach and delivery, and best practices and lessons learned from around the region.

16. Efforts to build industry level knowledge must extend to leadership and management at branch level, and to relationship managers and credit officers who are on the frontline of portfolio growth and management.

17. Over the long term, there is a need to build the pool of available expertise for commercial banks, MFIs and community-based financing partners, and to integrate curricula development and roll out through primary, secondary, and tertiary learning institutions. It remains the role of policy makers to determine which institutions are best positioned to do this.

2 Introduction

2.1 Country Context

Zambia is a landlocked Southern Africa country bordered by Tanzania, Malawi, Mozambique, Zimbabwe, Botswana, Namibia, Angola and the Democratic Republic of Congo. The country has a landmass of 752,614 square kilometres. Zambia enjoys a reputation for peace and stability and is endowed with abundant water and mineral resources as well as favorable climatic conditions for agriculture. In terms of potential, of Zambia's total landmass, 58 percent is classified as medium to high potential for agriculture production. Unfortunately only 14 percent of this land is cultivated. Water resources are equally unexploited with only 11.8 percent of Zambia's irrigation potential being utilized[6]. The population of Zambia, estimated at 13.1 million as of the 2010 census[7], is largely rural (61 percent of the total population resides in rural areas)[8]. The population is relatively young (54 percent of the population are aged under 18 years; and 48 percent of adults are aged under 30) and fairly evenly divided along gender lines (49 percent are male and 51 percent are female).

2.1.1 Economic and political overview

Zambia's economy is mixed in nature, with liberal policies towards private and foreign investments. The economy is largely based on mining of copper and agriculture, with potential in tourism, energy and industry. The international price of copper, Zambia's main export, remains high and provides the country with vital financial resources for growth and investment and for tackling its infrastructure deficit. In 2011, almost half of Zambia's Gross Domestic Product (GDP) came from the services sector (43.4 percent), followed by the industrial sector (35.2 percent). Agriculture accounted for 21.5 percent of GDP[9]. However, agriculture sector contribution to GDP growth has stagnated over the past three years (0.9 percent in 2009, 0.8 percent in 2010, and 1.0 percent in 2011).

Zambia has enjoyed a sustained period of rapid economic growth from 2008 through to 2011 in spite of the global financial crisis. Averaging five percent annually since 2000, growth picked up pace and grew in excess of six percent annually during the period 2008 to 2010, with real economic growth rates of 6.4 percent in 2009 and 6.6 percent in 2010. Revised estimates indicated that the economy grew by as much as 7.6 percent in 2010, driven by high international copper prices, a bumper maize harvest, and a boom in the construction sector. Growth in real

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[6] Zambia National Rice Strategy, August 2011.
[7] Based on Finscope data 2009, some estimates show that the population is currently around 14 million.
[8] CSO (Central Statistical Office) 2010 Census of Population and Housing Preliminary Report, http://www.zamstats.gov.zm.
[9] Central Intelligence Agency, World Fact Book.

terms was 6.6 percent in 2011[10]. However, further slowdown is not foreseen, and on the contrary, stronger agricultural growth, continued investments in mining and power supply, increased public spending, and continued high copper prices are likely to push growth to a forecasted 6.3 percent in 2012, and an average 6.9 percent for 2013 – 2016[11].

Inflation has been on a downward trend over the past five years. After a peak level of about 16.6 percent at the end of 2008, due to high food and fuel prices, inflation fell to 9.9 percent in 2009, and further to 7.9 percent in December 2010. This was due in part to rapid reductions in food prices, following the bumper crop harvests in 2009 and 2010 (food price inflation fell to 4.4 percent in December 2010, from 8 percent in 2009 and 20.5 percent in 2008), and to the appreciation of the Zambian Kwacha. Inflation remained moderate in the 12-month period ending in August 2011 at 8.3 percent.

The election victory of Mr. Sata and his party, the Patriotic Front (PF), in September 2011 ended two decades of rule by the Movement for Multiparty Democracy (MMD). In contrast to the perception that economic growth under the MMD largely benefited the political elite and foreign investors, the current government's focus is on re-distributing wealth, cutting unemployment and tackling corruption. The government's campaign to tackle corruption certainly continues. However, a series of actions appearing to target senior figures of the MMD party have led to speculation in some camps that anti-corruption efforts are little more than a political witch-hunt. Zambia remains politically stable, although Mr. Sata's pro-labour rhetoric in the first half of 2012 boosted demands for wage increases and sparked bouts of unrest and a series of strikes across the private sector. Despite these frictions, Zambia's continued positive growth trends and its strong credentials as a multi-party democracy bid well for the future. The government is expected to strike a balance between re-distributing wealth and sustaining investment and growth. Macroeconomic stability is likely to be maintained and, whilst policies in the mining sector are likely to tighten, drastic change is not anticipated[12].

Zambia's Sixth National Development Plan (SNDP) is organized around the theme of 'broad based wealth and job creation through citizenry participation and technological advancement.' Specific development goals include fostering a competitive and outward-oriented economy, significantly reducing hunger and poverty, and reaching middle-income status. A step toward achieving this came in September 2011 as Zambia joined the ranks of lower middle-income economies, moving from a 'low income' country category to a 'lower middle income' country category.

[10] Bank of Zambia, Annual Report for 2011.
[11] The Economist Intelligence Unit, Country Report, February 2012.
[12] Central Intelligence Agency, World Fact Book.

According to the World Bank Group's 'Doing Business' economic ranking, Zambia was recognized as being among the top ten reformers globally in 2011, as its ranking improved from 116 in 2008 to 76 in 2011. In the first quarter of 2011, Zambia obtained an international credit rating of B+ by Fitch and by Standard and Poor on its long-term public external debt. This is four notches below investment-grade and is similar to the ratings for Ghana, Kenya and Angola. This development should facilitate access to relatively low cost international finance.

In the past 12 months (2011 – 2012), various significant developments have taken place in the financial sector. As an overall trend, the banking sector has continued rapid growth, and, at the same time, financial sector performance has clearly improved. In 2011, the total assets of the 19 commercial banks grew by 20.5 percent to ZMK 27.8 trillion. The profitability of the banks increased sharply by 80.9 per cent from the 2010 level, and there was also a significant increase in credit to private sector, which rose by 30.8 percent in 2011. The share of non-performing loans had declined to 10.4 percent by the end of 2011 (from 14.8 percent the year before). The number of bank branches increased by 20 to 286, which further reduced the number of Zambian districts without any commercial bank branch[13]. At the same time, financial intermediation is on the rise, regulatory and supervisory frameworks are being strengthened, and there are on-going efforts to strengthen financial sector infrastructure.

2.1.2 The rural economy

Poverty and unemployment remain the biggest detriment to Zambia's economic profile. Despite the acceleration in the rate of growth and the improvements in the macroeconomic environment described above, there has not been a notable decline in poverty levels. According the World Bank, 60 percent of Zambia's population lives below the poverty line and 42 percent are considered to be in extreme poverty[14]. The absolute number of poor has actually increased from approximately 6.0 million in 1991 to 7.9 million in 2010, primarily due to population growth. The urban/rural divide is significant: in the Copperbelt and Lusaka provinces, poverty incidence is fairly low (22 percent and 34 percent respectively), whereas in the rest of the country, which is dominated by agriculture, poverty rates are greater than 70 percent. Moreover, almost 90 percent of Zambians who live below the extreme poverty line are concentrated in rural areas, and the poverty gap ratio (a measure of how far average incomes fall below the poverty line) is far higher for the rural population than their urban counterparts (20 percent and 3.7 percent, respectively).

[13] Bank of Zambia (BOZ), Annual Report, 2011.
[14] According to the World Bank, anyone living on less than US$2.00 per day is below the poverty line, and those on less than US$1.25 per day are considered to be in extreme poverty.

In Sub-Saharan Africa most people still live in rural areas where agriculture is the mainstay of the rural economy. The population of Zambia, as captured during the 2010 Census of Population and Housing, was 13,092,666[15]. According to the CSO 2010 Census, 61 percent of the adult population lives in rural areas[16]. Overall, 30 percent of adults (rural and urban) say that they rely mostly on agriculture as a source of income and over half the rural population (53 percent) report agriculture as being the only source of household income[17]. The overall level of population in rural areas, combined with household dependency on agriculture in rural areas especially, point clearly to the need for policies, strategies and operational actions that stimulate and reinforce agricultural and rural development. Further, accelerating growth and reducing poverty in rural areas will necessitate increasing the competitiveness of the Zambian economy by reducing the cost of doing business and ensuring that the rural economy, upon which much of the population depends for its livelihood, contributes meaningfully to overall growth.

Access to appropriate and sustainable financial services is a key contributor to business productivity and growth globally. In Zambia, increasing access to, and improving the quality of agricultural and rural financial services across agricultural and rural businesses, and other target market segments, is highly relevant to national strategies for economic and agricultural growth, poverty reduction, and food security. At household level, well-designed and well-targeted inclusive financial support will be a catalyst for strengthening the rural economy and for accelerating the transition of the poorest and low-income families out of poverty. Increasing financial access can also contribute to addressing the urgent need to raise women's participation in agriculture. According to a report compiled by the Food and Agricultural Organization (FAO) together with the International Fund for Agricultural Development (IFAD) and the International Labour Organization (ILO)[18], women face discrimination that limits both their economic productivity and their personal development. Increasing women's equitable participation in agricultural and rural markets through the adoption of 'gender-smart' policies and intervention strategies will contribute to poverty reduction, and to achieving national development and Millennium Development Goals.

Access to formal financial services in Zambia is still extremely low. At the same time, not enough is known about the demand for, supply of, and effective level of access to agricultural and rural finance or about the impact that existing policies, institutions and other contextual factors are having on growth. Rural and urban agricultural businesses are intrinsically linked through the flow of agricultural goods and services at all levels of business. There are existing and potential rural off-farm businesses (primarily informal MSMEs), which rely on urban suppliers. Rural households are also highly dependent on agriculture for employment, self-employment and household income. There is currently unmet demand for products and services across these various market segments, but also significant barriers to financial inclusion. Whilst there is increasing supplier interest in meeting agricultural and rural demand, the demand- and supply-side factors that

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15 Central Statistics Office, Zambia.
16 The FinScope survey uses the Central Statistical Office's (CSO's) definition of 'rural' and 'urban', where rural and urban is defined according to enumerator areas in its master sample frame based on population density.
17 This includes the sale of crops, livestock, or poultry and/or the sale of agricultural by-products.
18 Gender Dimensions of Agricultural and Rural Employment: Differentiate pathways out of poverty, FAO Rome, 2010.

characterize the current access-inclusion gap represent a major barrier to productivity and performance improvement, which are needed for household economic resilience and broader rural prosperity.

2.2 Objectives, ambit and methodology of the report

Sponsored by FMT to further its objective of 'making financial markets work for the poor', this country study examines the status of agricultural and rural finance in Zambia in order to better understand the nature, extent, and causes of the problems and challenges that are hindering growth and realization of financial sector development goals. Based on these findings, the study examines the implications for sector strengthening and derives a set of practical recommendations for effectively addressing cross-sectoral problems and challenges.

In addition, the study provides a practical point of reference for those seeking to understand the financial services marketplace and the stakeholders involved. It elaborates on existing sector support frameworks, contextual factors, promising new developments and, in contrast, the persistent obstacles and challenges to financial inclusion, which ensue from demand-side and supply-side constraints; all of which impact on rural economic growth and prosperity.

The study, which covers developments up until December 2012, used desk-based research and analysis of existing financial sector studies[19] and data information coupled with select meetings and interviews for updates, status reports and verification purposes. It was conducted amidst contextual variables and new developments not least of which include –

- legal and regulatory reforms in the banking and non-banking sectors;
- extension of the national financial sector development programme through 2014;
- Government of Zambia's (GRZ) decision to establish a rural finance unit within the Ministry of Finance and National Planning (MoFNP);
- commencement of DFID's Access to Finance programme in early 2013;
- design of a new GRZ / IFAD rural finance programme (starting 2014); and
- roll out of national strategies on microinsurance and financial education.

Existing and new developments for sector strengthening are covered in detail in Section 4.1 of the report.

The report echoes government's recently developed rural finance policy and strategy document, which endorses the principles and practices of 'making markets work for the poor (M4P)' as a framework for designing, implementing and evaluating financial sector development. 'M4P' is a practical approach to reducing poverty, grounded in best practice and guided by four underlying principles: systemic action, sustainable change, large-scale impact and facilitative role. Applying

[19] The reference section provides a list of key documents analyzed.

the 'M4P' approach prescribes that the role of macro and meso players is primarily a facilitative one. Their intervention support should be enabling and, in the context of financial services development, be based on a sound analysis of both consumers' and financial service providers' needs at the micro level. Support activities and processes should be market-led and should lead to positive systemic change in the way that the suppliers and consumers of financial services interact.

Whilst there are clear linkages and overlap in rural and agricultural finance, there are also distinctions between the two, particularly in relation to demand and supply, and responding to consumer needs. Rural financial services encompass both businesses and households located in rural areas. In Zambia, whilst the vast majority of those living rurally are engaged in agricultural production and marketing, there are household, and off-farm, financial needs to be met, which may not be directly related to agriculture. A good example would be financing school fees or physical improvements to the home. As this study shows, very different factors influence rural-based businesses and households with respect to their financial needs, and decision-making around the use of, often scarce, financial resources. It follows that developmental support focused on the rural and agricultural financial sector requires good understanding of these factors as well as demand-driven solutions for both rural agricultural and non-agricultural financial needs.

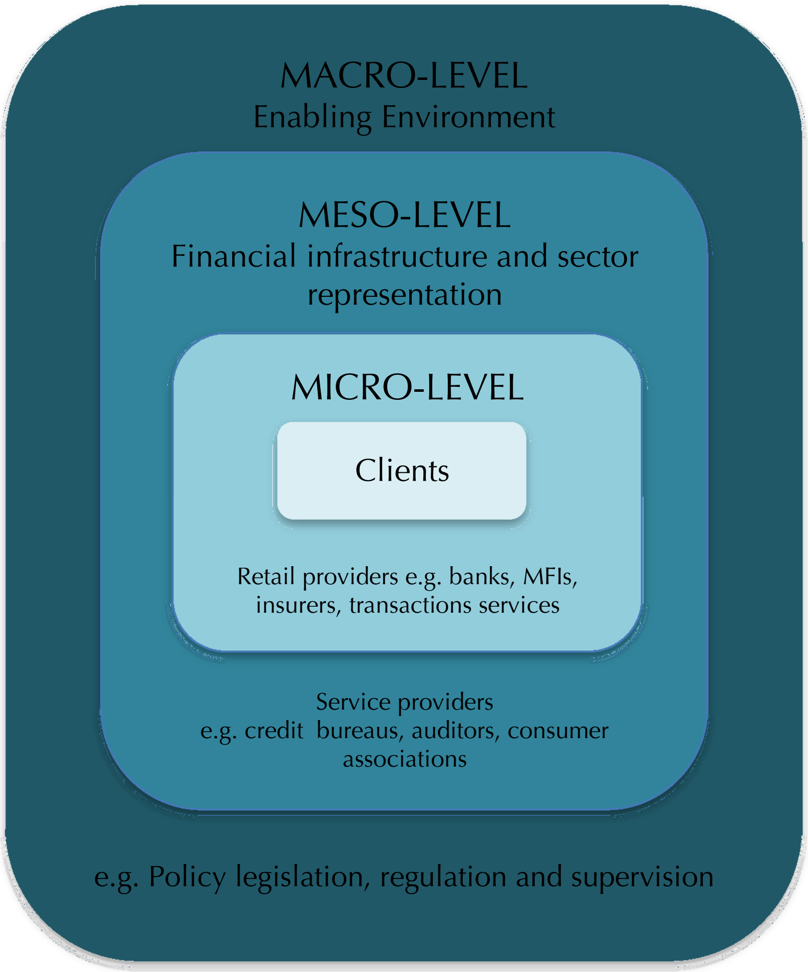
Where appropriate, the study adopts a structured analysis of key factors at the macro, meso and micro levels of the financial sector (see figure 1 below), which are either enabling or disabling progress in the provision of financial services to farmers, other businesses and households. The analysis at macro, meso and micro levels includes an examination of:

Macro-level: macro-economic policy and financial sector legislation, regulation and supervision.

Meso-level: industry-wide infrastructure and systems (e.g. for market trading, financial transactions or assessing creditworthiness), as well as auxiliary organizations, and financial sector representation.

Micro-level: individual financial service providers' products, services and delivery channels with respect to credit, savings, insurance and transactions services.

Figure 1: Financial sector analysis framework



The study seeks to understand the nature and extent of financial sector problems and challenges, by analysing and comparing the demand for, and uptake of, financial services with supply across the various levels of Zambia's agricultural and rural economy.

On the demand-side, the report bases its analysis on client-level demand studies and FinScope data that seek to measure and understand financial access and financial inclusion. The primary sources of reference have been the FinScope 2009 data and the Zambia Business Survey 2010. The approach taken in the report has been to examine data from these two studies and to use the findings to build the case for sector strengthening and demand-led investments in rural and agricultural finance based on need, knowledge and access levels. The analysis of demand from these three broad perspectives helps unveil the enabling and disabling factors around demand, which have implications for policy and strategy development, and inform the report's final recommendations.

On the supply-side, the analysis presents the existing financial sector development framework, and profiles key market segments and players, and their products and services, in order to fully understand the current status of financial supply at the micro level, as well as the environment and context at the macro- and meso-levels, which are impacting on demand and supply in a positive (enabling) or negative (disabling) way. Key financial credit delivery models are also presented as many of these demonstrate emerging use of innovation and partnership to overcome barriers to access and point to the types of concepts and opportunities that are most likely to succeed in achieving growth and expansion in financial services. The current status of savings, insurance and transaction services is examined, including new developments in the use of branchless banking technologies. Developments in the informal sector are also brought into perspective, as again, emerging opportunities exist to strengthen support to this relatively untouched market.

2.2.1 How to use the report

The introductory sections of the report provide an overview of the country context, in particular, the economic and political background and the rural economic context in which financial sector development is taking place. In addition, the overall objectives, ambit and methodology of the study are explained. The body of the report focuses on demand- and supply-side analyses that help clarify and gauge the nature of Zambia's access-inclusion gap, whilst concluding sections examine demand- and supply-related enabling and disabling factors, as well as key findings, implications and recommendations emanating from the study.

The study begins with an in-depth analysis of the demand (Section 3 through to Section 3.3). The analysis is based on the FinScope understanding and measurement of financial access and financial inclusion. FinScope differentiates between financial access: 'a measurement of financial inclusion across the formal-informal institutional provider continuum', and financial inclusion: 'giving people access to appropriate financial products and services such as savings, transaction banking, credit and insurance, whether formal or informal' and applies different lenses to better understand usage. With respect to financial access, FinScope uses 'access strands' to examine and segment the population. Ultimately all adults in a country will fall into one of the following categories of financial access:

Banked – individuals using one or more bank product provided by a formal banking institution. This is not exclusive usage – these individuals could also be using financial products from other formal financial institutions or informal products.

Formal other – individuals using one or more financial product from a formal financial institution other than a bank such as a microfinance institution or insurance company. This excludes bank usage, but is not exclusive in terms of informal usage - these individuals could also be using informal products.

Informal – individuals using one or more informal financial products only. This category is defined as exclusive informal usage and does not count those within the banked or formal other categories that also use informal services.

Excluded – individuals using no financial products to manage their financial lives – neither formal nor informal.

Demand is explored through the lens of the consumer. An analytical framework is introduced in Section 3, which unlocks issues relating to demand for financial services based around three broad, key demand factors namely, need, access, and knowledge. The subsequent sections examine each of these areas in detail, including household needs and enterprise needs (Sections 3.1.1 and 3.1.2). Knowledge is examined via a set of demand determinants – concepts, products, perceptions and practices in Section 3.2. In Section 3.3, access and usage are examined through the application of FinScope financial access strands as explained above. The final demand section (Section 3.4) examines current levels of consumption of financial services.

The study then moves on to unpack and examine the supply-side. The analysis flows from macro-level through meso-level down to micro-level. The opening section 4.1 examines the current financial sector development framework, including key regulatory and supervisory bodies (Section 4.1.1.1), and existing and future national plans/programmes and strategies (Sections 4.1.1.2 through 4.1.1.6). The scope and effectiveness of meso-level infrastructure is covered in detail in Section 4.2, including an overview of the main supplier representation associations and auxiliary organization. Meso-level market place infrastructure is also analyzed. Micro-level analysis begins in section 4.3, including an overview of supply (section 4.3.1) that captures formal and informal supplier networks, as well as the main market segments and types of financial suppliers. Key financial credit delivery models are also presented in Section 4.3.3 as many of these demonstrate emerging use of innovation and partnership to overcome barriers to access and point to the types of concepts and opportunities that are most likely to succeed in achieving growth and expansion in financial services. An overview of the savings, insurance, and branchless banking and payment systems subsectors is provided in Sections 4.3.4 to 4.3.6 The role of social protection grants is touched upon separately in Section 4.3.7 and whilst they are not considered as a driver of financial inclusion, and are still on a relatively small-scale, they are still an important social safety net for extremely vulnerable individuals and households.

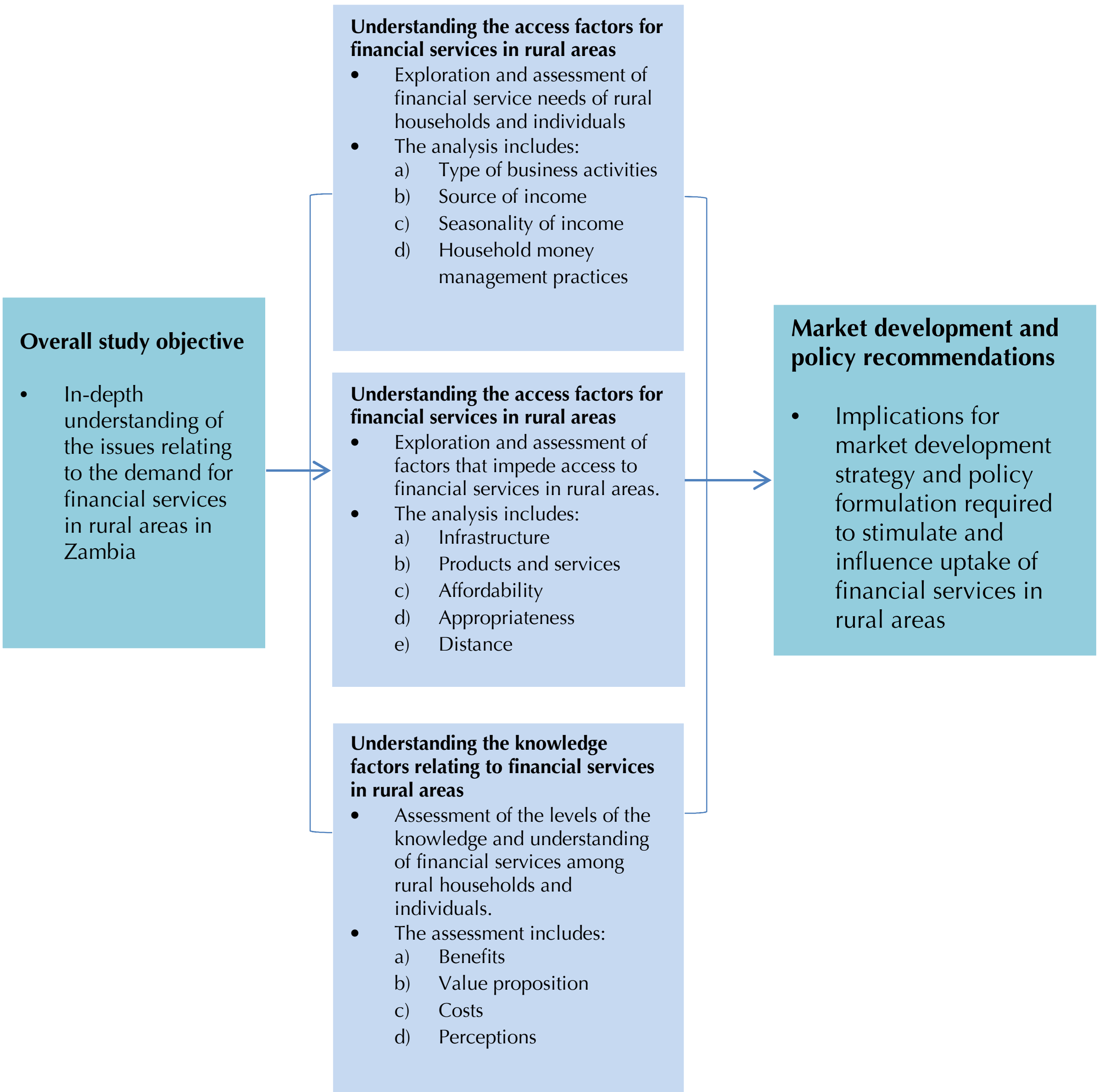
Section 5 explains in more detail the contextual factors, which contribute to the mismatch between the current demand for and supply of agricultural and rural financial services. These contextual factors, including those related to the microfinance sector (section 5.3), human resource capacities (section 5.4), and MSME financing (Section 5.5), help us understand the nature of the access-inclusion gap and they hold implications for policy and strategy formulation, refinement and implementation. The study goes on to identify and discuss the enabling and disabling factors with respect to demand and supply (Section 6), as these are powerful factors, which potentially strengthen or undermine growth efforts across all levels of the sector.

The concluding sections of the report capture key findings, implications and recommendations emanating from the study (Section 7), as well as a summary of consultants' own conclusions (Section 8).

3 Agricultural and rural financial services: The consumer's perspective

This section discusses the demand for financial services in rural areas. An analytical framework is used to unlock the issues relating to demand for financial services based around three broad key demand factors, namely, need, access and knowledge. The report uses demographic and financial access data on agricultural and rural finance to highlight the current status of demand, and in doing so makes a strong case for increased focus on understanding and meeting the needs for agricultural and rural finance. The demand-side analysis also demonstrates how the gaps in the demand for agricultural and rural finance in Zambia result from both demand and supply factors. Figure 2 summarizes the analytical framework for demand.

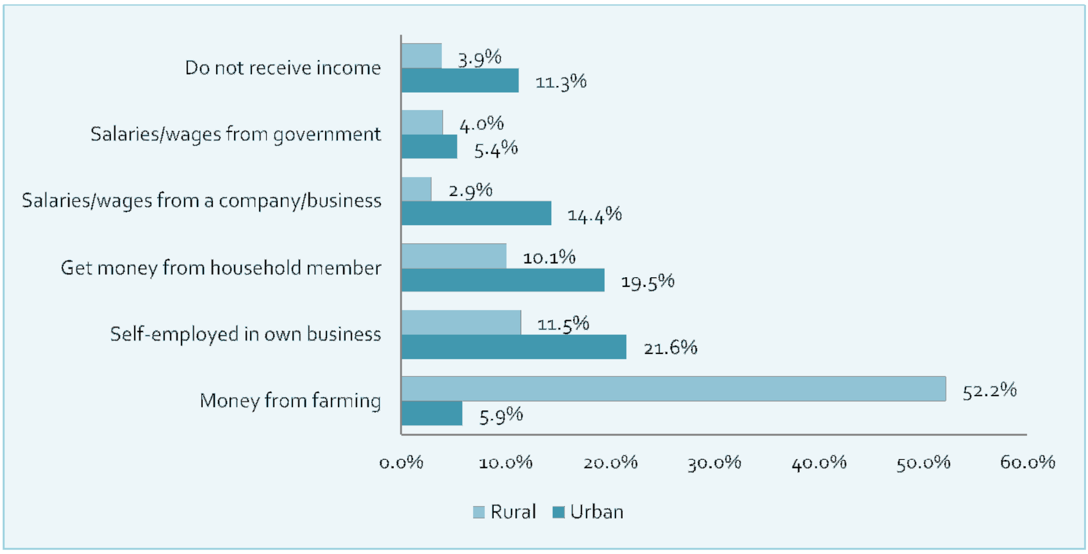
Figure 2: Analytical framework for demand



3.1 The need for financial services

The Finscope 2009 survey shows clearly that agriculture is the main source of income for rural households. Figure 3 shows the various sources of income in rural areas. 52 percent of households rely entirely on farming, whilst only 6.9 percent earn a relatively stable income from salaries, and wages from public service or private companies.

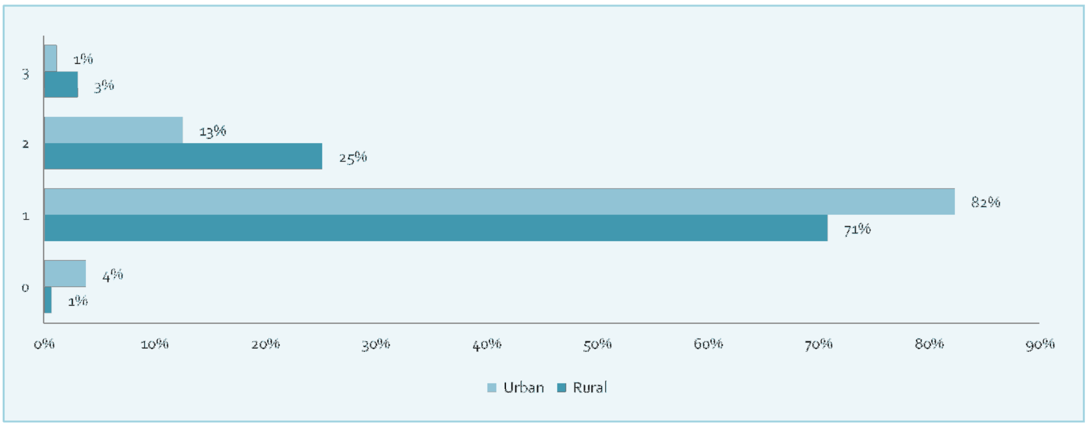
Figure 3: Main sources of income of rural households in Zambia, 2009



Source: FinScope, 2009

The FinScope data also shows that 56 percent of rural households regard agriculture as their regular source of income, whilst Figure 3 indicates that 72 percent of rural households have just one source of regular income. It can be inferred that for most this is agriculture.

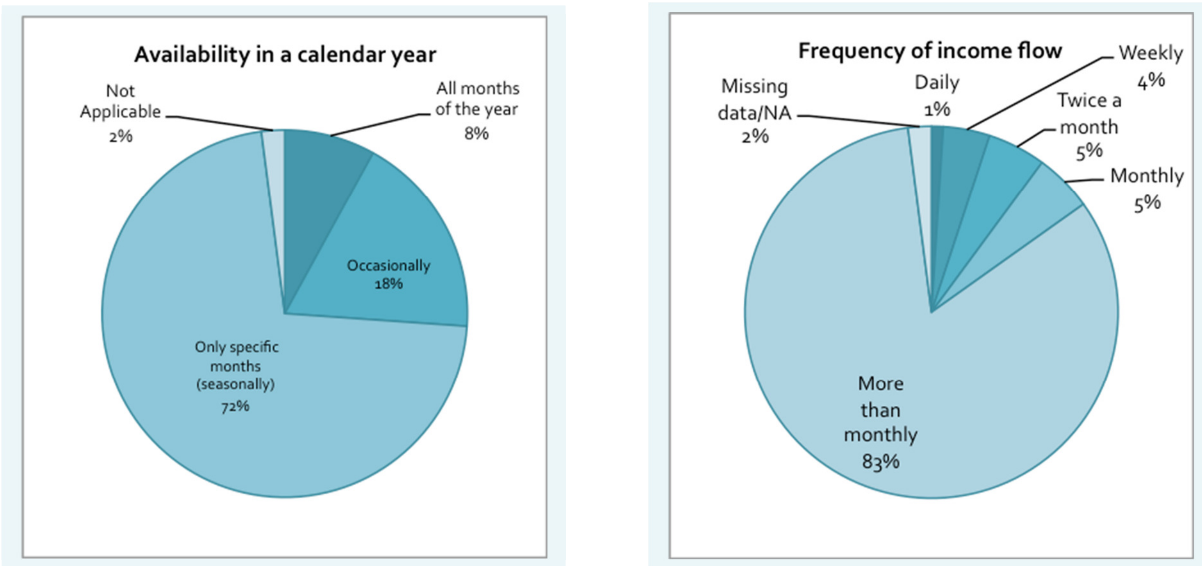
Figure 4: Number of regular sources of income of households in Zambia, 2009



Source: FinScope, 2009

For those adults in rural areas whose main source of income is agriculture, this income is erratic and lumpy (see Figure 5). Household income is variable and fluctuates with the farming season and main agricultural activities. In fact, only 8 percent of rural households reported having income throughout the year. For the majority of rural households (72 percent), income is only received in specific months of the year, which for most are likely to be those months in which they receive payments for farming produce from rain-fed agriculture. For example, the majority of small-scale farmers usually receive money in the dry season (June - September) after harvesting and supplying their cash crops such as maize and cotton, to agribusinesses and public sector entities such as the Food Reserve Agency. Figure 5 shows that the majority of rural households (83 percent) actually receive income more frequently than monthly during peak periods. However, although income is received more often than monthly, it is nonetheless irregular and generally unreliable. Very few farmers receive income on a regular daily or monthly basis (dairy and poultry farmers perhaps being an exception). In particular, small-scale farming, which is wholly dependent on the rainy season, does not bring cash in on a regular basis. With obvious risks relating to climatic changes, rural households lack a consistent source of income - hence their even greater need for effective risk management strategies and supportive financial services.

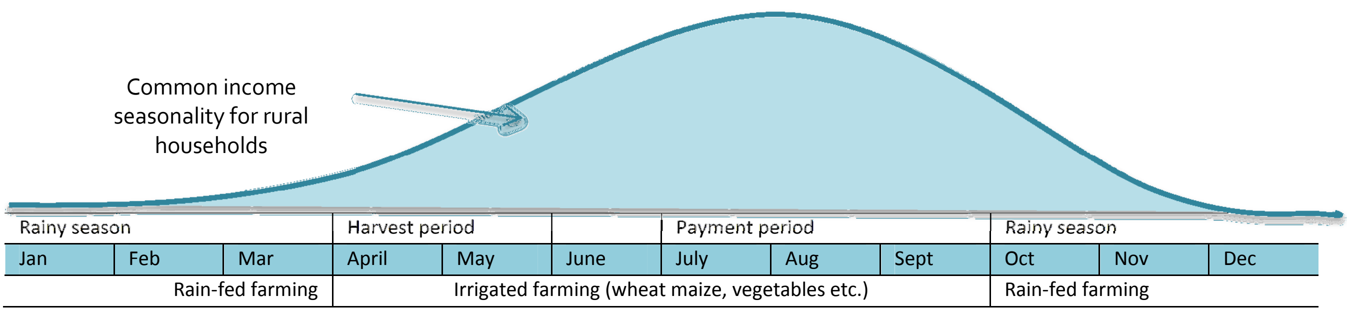
Figure 5: Availability of income of rural households



Source FinScope, 2009

Some farming households engage in various activities, including irrigated farming activities to smooth income and cash flow. Figure 6 illustrates the different income patterns or seasonality for a typical calendar year for the majority of Zambian rural households.

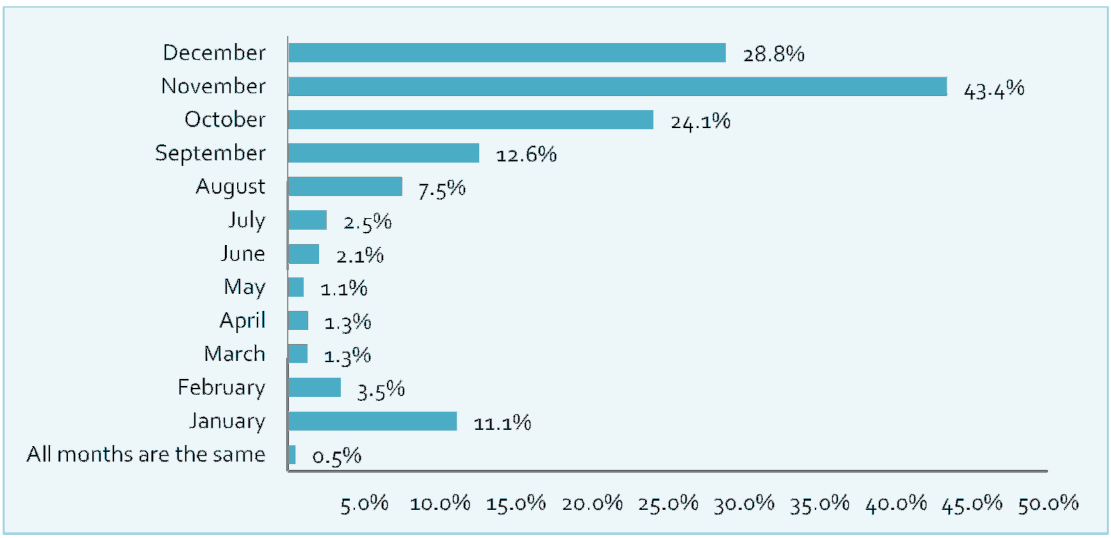
Figure 6: Typical income seasonality, rural households in Zambia



Appropriate financial services for rural households and enterprises need to be well aligned with types of income, income levels and seasonality in rural areas. Financial services accessed by farmers should help in smoothing cashflow, in aiding effective management of expenses and in enhancing timely farming investments. There is also a strong case for ensuring that rural financial services address both household and farming enterprise needs.

For example, expenditure patterns for rural households show that expenditure is highest in the fourth quarter of the year (see figure 7). There are a number of reasons for this. Firstly, most rural households receive income during the fourth quarter from the sale of agricultural produce and receipt of payments, which are usually made in August through September. Secondly, the fourth quarter is also the commencement of the new farming season for annual crop farmers, who incur expenses related to land preparation, the purchase of inputs and hire of labour. Thirdly, January is the beginning of the school calendar year and most households incur back-to-school expenses in the run up to school re-starting. The typical pattern of rural household expenditure described here strengthens the case for providing financial services that assist rural households to save and/or to borrow to cover outflow seasonal peaks.

Figure 7: Typical rural household expenditure patterns over a calendar year, Zambia, 2009



Source: FinScope data 2009

Another dimension to the need for financial services in rural areas is linked with household risk management practices. Statistics show that low-income households dominate rural areas. For instance in 2006, the poverty rate was 77 percent in rural areas, compared to 27 percent for urban areas[20]. Low-income rural households are more vulnerable to, and have to face, financial shocks and risks that require effective coping strategies. These financial shocks and risks account for the persistence of chronic poverty[21] for some rural households as they reduce chances of sustaining income gains. Coping mechanisms used by rural households include savings, social capital[22] and harsh measures such as the sale of household assets. In fact, owing to non-abating poverty levels, for many, social capital is no longer an option as a coping mechanism. Currently in Zambia, most rural households have little or no access to any type of formal, risk-managing financial services and there is a strong case for building inclusive access to services such as insurance and emergency loans, which help cushion rural households and enterprises against economic shocks as well as prevent them from falling further into the poverty trap.

Another financial services need for rural households is transactional services, particularly money transfers. Rural households often receive remittances from relatives in urban areas, or they have to send money to urban-based connections for the purchase of agricultural input supplies or household assets, which are not within reasonable reach in rural areas. The last five years in Zambia have seen the emergence of a number of mobile phone-based money transactional facilities, which enable rural households to send or receive cash. Celpay, Mobile Transactions Zambia and Bayport Financial Services are among the new entrants in the money transfer business space. These service providers, who are also increasingly competing with the likes of the commercial banks and the post office in swift cash services, are also contributing to changing the financial landscape by providing an alternative to higher risk manual transfer mechanisms such as via public buses, friends and relatives. More on emerging types of innovative transaction services and partnerships is presented in section 4.3 (supply) below.

Financial inclusion refers to the access to and the uptake of appropriate and affordable formal and informal financial products and services by society in general, and by vulnerable and low-income groups in particular. For rural areas in Zambia, financial inclusion entails increasing access to and usage of financial services that address both individual, household and enterprise needs effectively, that is, in the main, appropriate and sustainable savings, credit, insurance and transactions services. In Zambia, financial services can and should play a critical role in rural development. Understanding the profiles and the needs, interests and priorities of rural households and enterprises is essential for determining and designing appropriate financial services that are well tailored to their needs.

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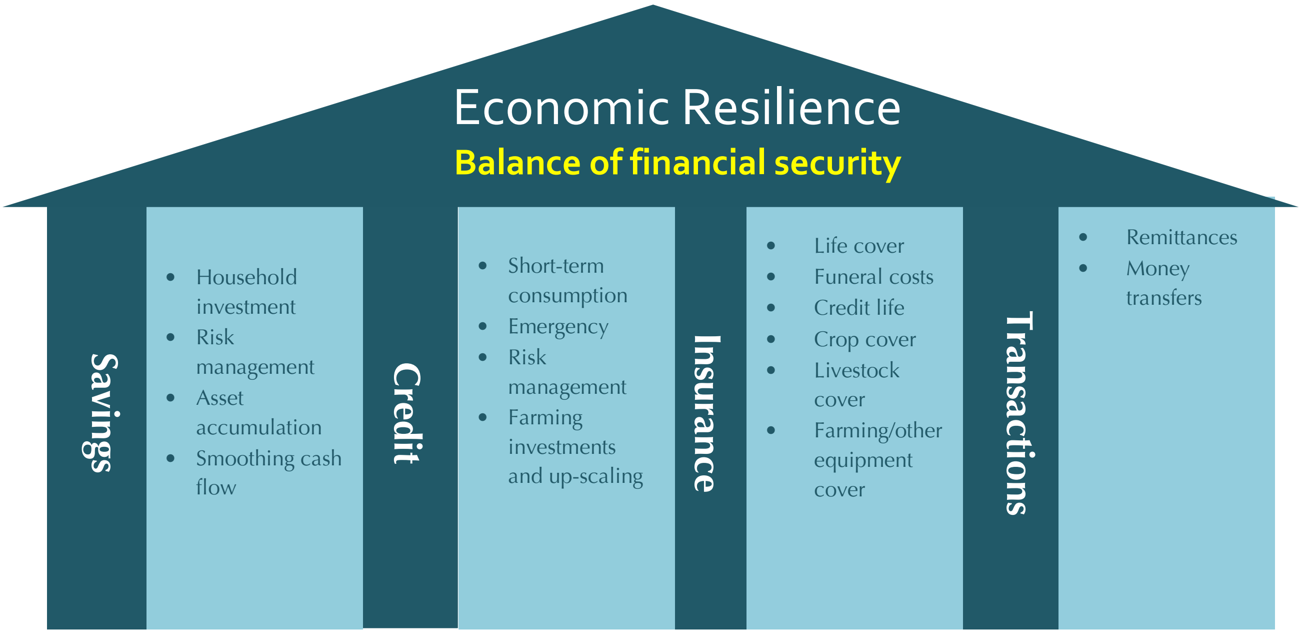
[20] Zambia Institute for Policy Analysis and Research, www.zipar.org.zm.
[21] Poverty trap or long-lasting poverty.
[22] A definition of social capital (according to Collins English Dictionary, 10th edition, 2009) is ‘the network of social connections that exist between people, and their shared values and norms of behavior, which enable and encourage mutually advantageous social cooperation’.

3.1.1 Household needs

Providing a variety of financial services to rural households can enhance their financial security or economic resilience. There is a thin line between household and enterprise income in most households in Zambia, be it in rural areas or urban areas. Given that rural areas mainly rely on farming as a source of income, in thinking about rural finance, it is important that both household and enterprise needs are also taken into account. Figure 8 summarises the 'pillars' of financial security and how their effective use can contribute to building financial security or economic resilience at household level in rural areas in Zambia.

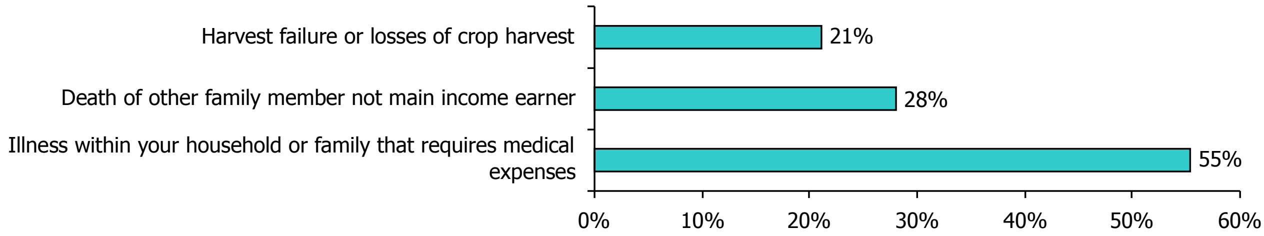
Figure 8 Pillars of financial security



Source: Authors' summary

Savings and insurance products can assist rural households and businesses in reducing vulnerability to risks, in planning more effectively for the future and in investing in assets, as well as in smoothing irregular income flows and covering unexpected expenses. Insurance such as livestock and weather index insurance can serve as effective risk management tools for small-scale farmers. To influence uptake of most of these financial services, consumer education is required. Notably insurance is harder to sell to low-income people given low levels of understanding and experience. The Zambia Business Survey revealed that, regardless of location, insurance penetration in Zambia is very low. In terms of demand, no doubt, there is a need for insurance that can cover both household and enterprise needs. Figure 9 shows the three risks that rural households are most concerned about. FinScope 2009 also revealed that coping strategies used by most households for risks such as death and illness lean more on social capital. However social capital has been eroding in both rural and urban areas due to factors such as poverty levels. Therefore, rural households struggle to meet all of the 'before' and 'after' financial requirements of responding to these risks and eventualities.

Figure 9 Risk factors that affect rural households



FinScope data 2009

Potential credit products for rural households include short-term consumption or emergency loans that help households cope with financial shocks and prevent them resorting to measures such as the sale of assets. Money transfer services assist rural households to send or receive money from urban areas and pay accounts. With mobile phone ownership among rural based entrepreneurs being around 71 percent[23], mobile phone transactions are spreading to rural areas and gaining acceptance by rural communities as a more efficient means for moving cash and managing supplier payments.

3.1.2 Enterprise needs

Financial services promoted and facilitated by NGOs and agribusinesses mainly focus on credit towards inputs; this enables rural farming households to purchase their desired agricultural inputs. For some years now, agribusinesses (lead firms and processors) have provided credit (mainly in the form of inputs) to small-scale farmers through outgrower contractual arrangements. For instance in the dairy subsector, tripartite lending arrangements involving buyers, small-scale dairy producers and banks, and based on contract farming agreements, have enabled small-scale dairy farmers to acquire more dairy animals[24]. In the cotton subsector, lead firms provide small-scale cotton farmers with input supply packages on credit. The credit is liquidated when the small-scale farmer sells his/her raw cotton to the lead firm. Successes such as these can be explored for potential replication or scale- up. Section 4.3.3 in the report looks in more detail at credit delivery models.

In summary, needs for financial services at household and enterprise level are only being met to a limited degree. Consequently financial services are not driving agricultural growth or enhancing financial management among rural households and enterprises to the extent that they should. While investments in financial literacy can potentially influence uptake, complementary initiatives to remove other barriers to access are required on the supply side.

[23] FinScope 2009.
[24] USAID PROFIT success story publication.

3.2 Knowledge of financial services

The lack of supply of formal financial services in rural areas has impacted on the knowledge of financial services. In Zambia, a significantly high proportion of rural households have poor orientation and understanding of financial services. Figure 10 captures the demand factors attributable to the lack of knowledge of financial services, which is characterized by negative perceptions and/or by misconceptions around financial products, particularly insurance. The Zambia Business Survey 2010 reported that 52 percent of uninsured MSMEs did not understand what insurance is, 27 percent were not aware of the benefits of insurance, whilst 20 percent did not know what types of insurance products might be applicable to them. Consequently only 0.2 percent of rural MSMEs surveyed had insurance (ZBS 2010).

With respect to credit, some rural households (e.g. those in small-scale farming in the cotton and tobacco subsectors) have exposure to credit through outgrower schemes, whereby credit repayment mechanisms are usually in-kind. Overall, however, small-scale farmers' perceptions of credit are that it is in scarce supply, expensive and heavily skewed towards the larger, corporate sector[25].

Informal savings mechanisms are common and in some areas, NGOs promote community-based banking through the use of village savings and credit groups.[26] Rural households rarely use formal savings products for two major reasons: firstly, lack of formal savings facilities within reach and secondly, they consider bank charges for existing savings products as excessive, making net returns low if not negative. MFIs that operate in rural areas offer mandatory savings products[27] as a condition to accessing the loans; this is in the form of a percentage of the loan - usually around 20 percent. MFI clients do not perceive this as a savings product, but as a precondition or administrative requirement for accessing loans.

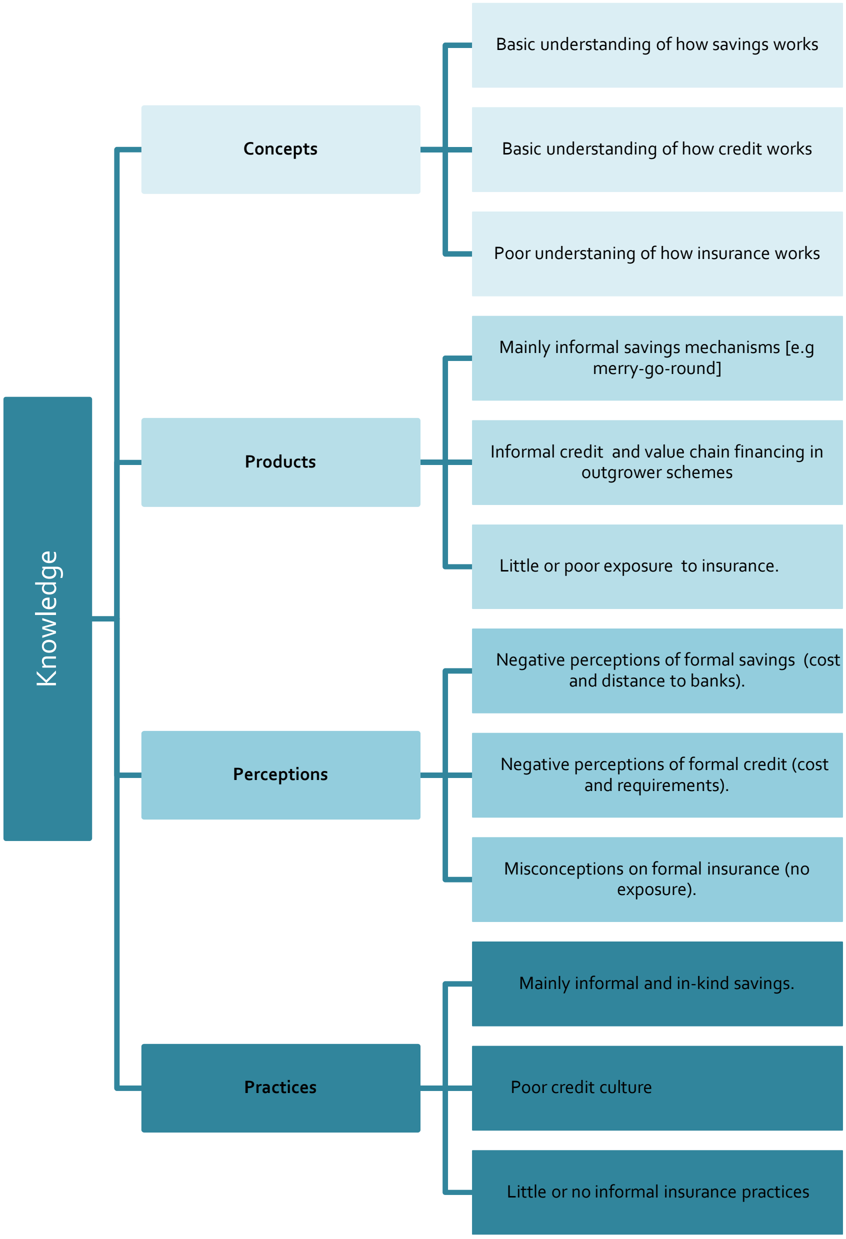
Figure 10 below summarizes consumers' knowledge-related demand determinants. The four categories, concepts, products, perceptions and practices, are interrelated. Low levels of exposure and access to products influence current practices. Perceptions are influenced by lack of understanding and knowledge of financial services and of the terms and conditions of existing products, which most rural households find unattractive, especially in view of high bank charges.

[25] USAID PROFIT, Zambia's Agricultural Finance Market challenges and opportunities, study by PROFIT and ZNFU, December 2009.

[26] Some of these programmes are supported by grants from the Rural Finance Programme, Ministry of Finance and National Planning.

[27] Mandatory Savings is a pre-requisite to access micro loans; all borrowers are required by the MFI to deposit a stimulated amount as conditional savings before getting a loan. This amount cannot be withdrawn until the loan is repaid.

Figure 10: Knowledge-related demand determinants



Source: deduced from USAID 2009,[28] FinScope data 2009, ZBS 2010[29]

Rural data shows that aside from lack of knowledge of financial services, there is also a lack of capacity in financial management for most rural households. Figure 11 shows how consumer profiles can be linked to potential financial products and the need for financial education as a key intervention strategy. However, the findings show that not only do rural households have low knowledge levels in financial management they also do not look to financial institutions for financial advice. These circumstances are partially as a result of the lack of interaction between

[28] USAID PROFIT, Zambia's Agricultural Finance Market Challenges and Opportunities. A Study by PROFIT and ZNFU, December 2009.
[29] Zambia Business Survey, FinMark Trust, Zambia Business Forum, Private Sector Development Forum Programme, World Bank, June 2010.

financial institutions and rural households. Where contract farming, outgrower schemes and value chain finance are reaching out with credit to rural households, the interactions are between small-scale farmers and agribusinesses, processors or large commercial farmers. Typically, there is no formal financial advice or financial education component linked with agricultural finance arrangements. Whilst we are seeing the emergence of financial education for small-scale farmers through commercial banks like Zanaco Bank and other agri-support organization including ZNFU (Zambia National Farmers Union) and NGOs such as CARE and Plan International, these initiatives are too recent and too small a scale as yet to be impacting on financial inclusion generally.

Figure 11: Profiling rural consumers' financial education and alignment of appropriate response interventions and products.

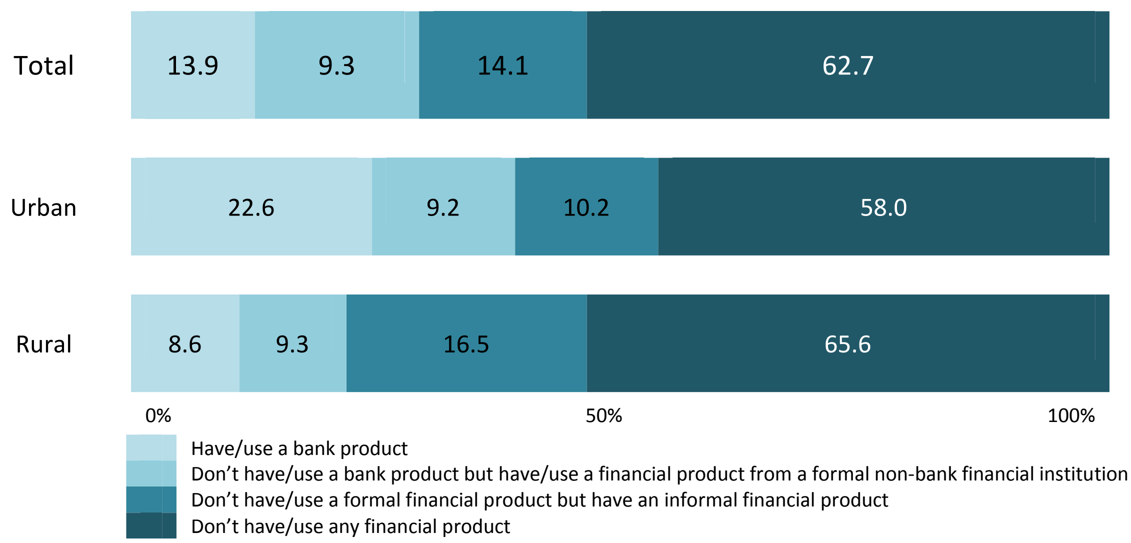
Keeping track of money		**Potential interventions/ Products**
Heard of and understand budget.	65%	Income smoothing loans Financial education
Keep track of expenses on a monthly basis.	24%	
Maintain a monthly or weekly budget.	28%	
Spend within the budget.	85%	
MAKING ENDS MEET		
Borrowed money from a person/institution in the last 12 months.	27%	Emergency loans Financial education
Missed a payment in the last 12 months.	24%	
PLANNING AHEAD		
Save for a specific purpose.	65%	Savings products Insurance products Financial education
Saving money for emergency.	19%	
KNOWLEDGE AND USAGE		
Heard of and understand 'interest'.	38%	Current and savings accounts targeted at low income clients Financial education
Heard of and understand 'insurance'.	18%	
Do not know any advantages of a bank account.	22%	
Ask family member or friend for financial advice.	45%	
Ask financial institution for financial advice.	5%	

Source: FinScope data 2009

3.3 Access to financial services

The FinScope Zambia 2009 survey indicates a decrease in the total percentage of adults that are financially excluded (i.e. using no financial products, either formal or informal to manage their financial lives); from 66.3 percent in 2005 to 62.7 percent in 2009. However, the overall picture of financial access and the differences between urban and rural usage are significant and compelling. In total, 23 percent of the overall adult population use formal financial services (both bank and formal non-bank products) and only 14 percent use informal financial services, with formal financial services usage significantly higher in urban areas compared to rural areas. The FinScope survey summarizes financial service usage through the application of access strands, which present segments that reflect financial product usage patterns and distinguish between those who are banked and those who are not banked, but who are at the same time making use of other products provided by formal financial service providers. Figure 12 analyzes financial service usage according to FinScope access strands, together with a rural/urban breakdown. The analysis shows that 22.6 percent of adults in urban areas use a bank product, compared to only 8.6 percent of adults in rural areas, whilst 32 percent of adults in urban areas use formal financial products, versus 18 percent in rural areas[30]

Figure 12: Financial access strands for Zambian adults in 2009

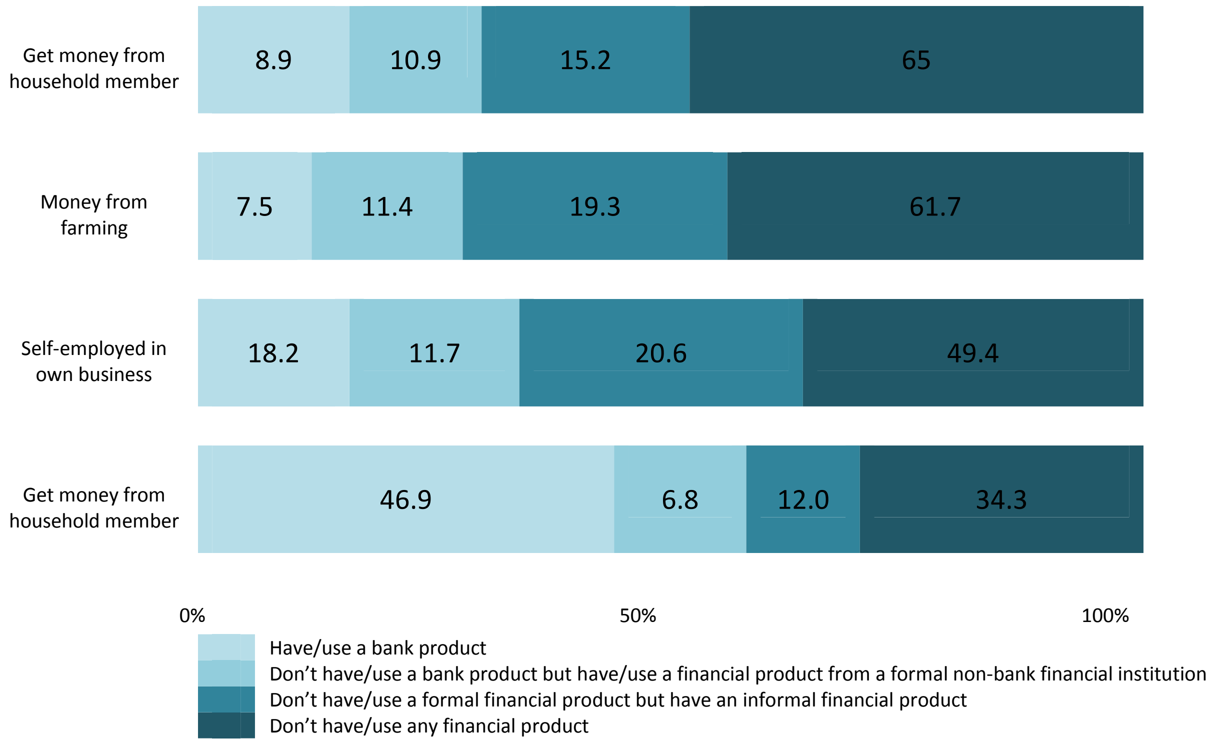


Source: FinScope Zambia 2009

Further analysis of the access strands by type of income generating activity (see Figure 13) shows that very few adults (7.5 percent) who rely on farming as an income generating activity use bank products. In fact, 62 percent of adults who earn money from farming alone do not actually use any formal financial product.

[30] FinScope 2009.

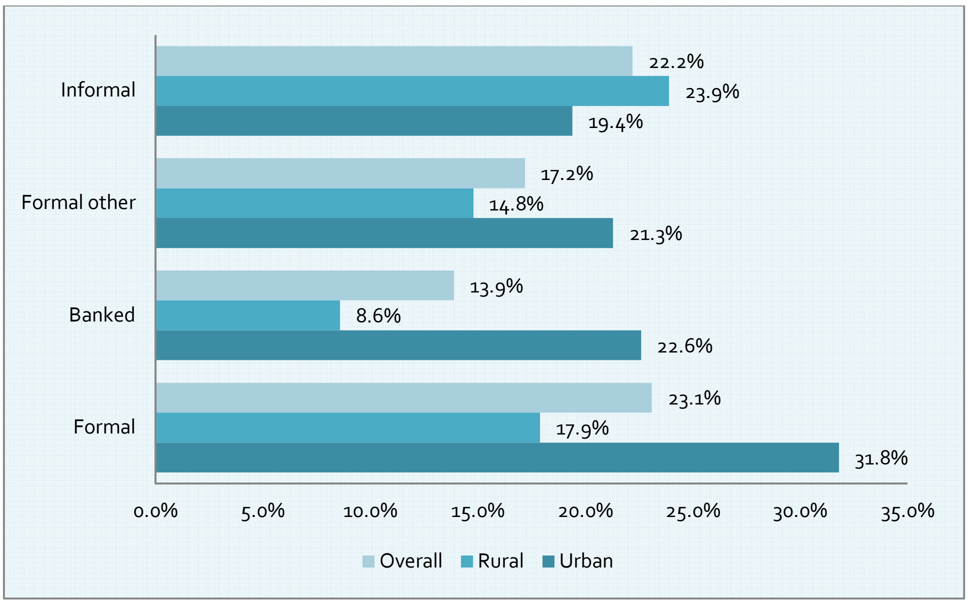
Figure 13: Breakdown of the Zambian access strand, different income-generating activities, 2009



Source: FinScope Zambia 2009

Figure 14 compares the consumption of financial services between rural and urban areas. Not surprisingly, there are more adults in urban areas that are banked and use formal financial services than in rural areas. The picture is more telling for Zambian MSMEs. The ZBS 2010 revealed that 85 percent of rural based MSMEs are financially excluded while only 5 percent are banked.

Figure 14: Percentage of adults using formal and informal financial services in rural and urban areas



Source FinScope data 2009

Physical availability of financial services as well as product affordability and appropriateness are among the key factors that influence access to, and uptake of, financial services, in addition to need and knowledge issues described earlier. Other key constraints (which are indicative of the access-inclusion gap) include:

- poor infrastructure - absence of bank branches, ATMs and agent networks alongside poor physical infrastructure such roads to some remote rural areas;
- low returns on savings deposits - taking into account inflation, interest earned on savings is not an incentive;
- high bank charges;
- real and perceived high costs of borrowing - interest rates deemed too high by most small-scale farmers and rural households;
- collateral requirements - deemed out of reach for small-scale farmers and most rural households.

Looking more closely at existing financial services, for credit, the lack of access for rural enterprises, especially small-scale farmers, and the concentration of credit supplied to large commercial farmers reinforces the big gap between the value of loans received respectively by small-scale and by commercial farmers. This contributes to the belief among small-scale farmers that rural credit is not designed for them[31], and a general acknowledgement of the reality that some credit, which is not specifically intended for agricultural production, ends up indirectly being used for it. Box 1 summarizes small-scale farmers' perspectives on current available credit and agricultural financial services.

Box 1: Access to credit: small-scale farmers' perspective
In 2009, USAID/PROFIT in collaboration with the Zambia National Farmers Union (ZNFU) conducted a study that provides useful insights into small-scale farmers' perspectives of agricultural financial services. Major findings included: • Not enough credit available to farmers - Smallholder farmers believe that the financial sector does not provide sufficient financing opportunities to meet their financing needs; • Agricultural finance is not inclusive – Small-scale farmers feel credit is only available to large-scale commercial farmers; • The cost of credit is very high – Small-scale farmers feel that the high interest rates applied to agriculture credit make farming less viable; • Collateral requirements are very high - Banks ask for excessive collateral which makes it difficult for small-scale farmers to secure credit; • Loans are usually limited to short-term with inappropriate payment terms - Farmers expressed concern that current loan facilities do not permit them to acquire medium/long-term credit for capital development; • The approval process is too long - Farmers asserted that banks normally take too long to approve agricultural loans; • Bankers do not really understand agriculture - Farmers feel that bankers rarely invest time to understand how farming works in order to design appropriate products. Source: USAID PROFIT 2009

[31] ZBS 2010, USAID PROFIT 2009.

3.4 Current levels of consumption of agricultural and rural financial services

Aside from the demand factors impacting access and inclusion described above, the poor or limited supply of agricultural and rural financial services also account for the current low access levels. The 2010 ZBS shows that banking penetration for rural MSMEs that have at least one paid employee is only 16 percent for rural areas while it is nearly 50 percent in urban areas, and only 0.2 percent of rural MSMEs use insurance services. Service delivery by Zambian financial institutions to the rural areas in general, and the small-scale farmer sector in particular, is presently very limited. Commercial banks that had operations in rural areas, including those with a physical presence, such as Lima Bank and Barclays Bank, have now closed their operations.

Over the past three years there have been significant and promising developments in the supply of agricultural and rural finance. Agricultural market facilitators such as Musika, Conservation Farming Unit (CFU), and International Development Enterprises (iDE) Zambia are facilitating access to finance, but initiatives are on a relatively small scale. An important lesson learned from these efforts is that the appropriateness of financial services for smallholder farmers is a critical demand factor. Rural households and individuals are more likely to take on savings, credit and insurance that tangibly improve the farming enterprise and ultimately the household income.

A further lesson learned is that physical access is not necessarily a prerequisite for uptake. Improving uptake of financial services in rural areas seems to be influenced by a number of factors including affordability, product appropriateness and issues of perception and trust. It is worth noting that the design and supply of rural finance should ideally encompass the needs of both businesses and households, and should be addressed in a structured way. The sustainable flow of rural finance also has to take into account issues around cost of services and sustainability of operations of financial service providers; these supply-side factors will be discussed in the next section.

4 The supply of agricultural and rural finance

The following sections examine in detail the supply-side of Zambia's rural and agricultural financial sector, and more specifically, introduces and analyses the institutions, sector initiatives, and support partners with respect to their roles and functions in overseeing and/or participating in financial sector strategy development, programme management and implementation. The analysis flows from macro-level through meso-level down to micro- level. In addition to providing up-to-date information on the status of financial sector development initiatives, the analysis also highlights strategic focus with respect to where supply-side support has been, and is currently, targeted. Sections 4.3.1 to 4.3.6 examine in more detail the key players and emerging financing models that are already, or, with appropriate support, could be drivers of growth in the market place. It should be noted that, for the most part, the review focuses on those aspects of sector support that hold more direct relevance to agricultural and rural finance development.

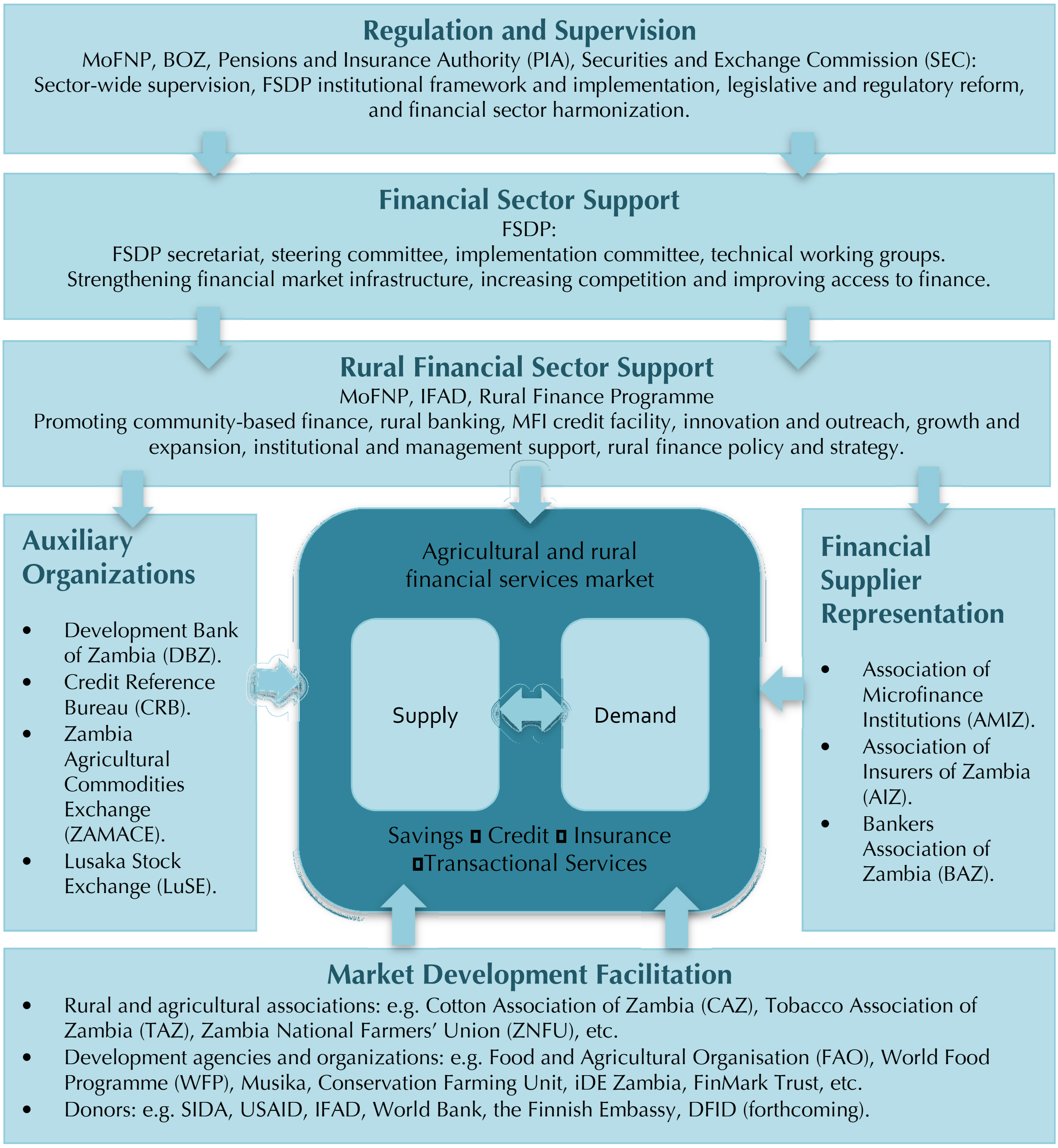
4.1 Macro-level: frameworks and focus for sector development

Sections 4.1.1 to 4.1.1.6 provide a comprehensive description of the core macro-level framework, which focuses, and has direct bearing, on rural and agricultural financial sector strengthening, including the current Financial Sector Development Plan (FSDP), (in section 4.1.1.2), the on-going Rural Finance Program (RFP), (in section 4.1.1.3), and the Zambia Rural Finance Policy and Strategy (in section 4.1.1.3). These sections also capture planned extensions to existing programmes, and provide briefs on upcoming initiatives for 2013 – 2014.

4.1.1 The financial sector development framework

In Zambia, there is an existing, relatively coherent framework for financial sector development, which aims to strengthen and expand regulation and policies, rural financial access, piloting and innovation, technology uptake, product and service delivery mechanisms, financial education and awareness, as well as knowledge transfer and learning dissemination both in Zambia and across the region. Figure 15 summarizes the current and planned financial sector development initiatives and the main support partners.

Figure 15: Financial sector development framework



4.1.1.1 Key regulatory and supervisory bodies

The three main regulatory and supervisory bodies providing oversight to Zambia's financial sector development under the framework of the FSDP are the Bank of Zambia (BOZ), the Pensions and Insurance Authority (PIA), and the Securities and Exchange Commission (SEC). As part of the FSDP, technical support has also been directed at strengthening the autonomy and capacities of these core supervisory agencies. An overview of their main roles and responsibilities is provided below.

1. BOZ

   BOZ is the supervisory authority responsible for overseeing banks and non-bank financial institutions. As the central bank, it is responsible for formulating and executing monetary and supervisory policies, acting as banker, fiscal agent and advisor for government, and as the central banker for commercial banks. A core function of BOZ is to contribute to an enabling environment for the evolution of the financial sector to stimulate economic growth and social and financial stability. As such, BOZ is primarily responsible for overseeing the implementation of comprehensive reforms and strategies, which are taking place under the FSDP (see Section 4.1.1.2).

2. PIA

   PIA is the agency responsible for regulating and supervising the pensions and insurance industries under the Pension Scheme Regulations Act (1996) and Insurance Companies Act (1997) respectively. Core to PIA's work under the FSDP has been to implement a comprehensive review of these two Acts. This exercise was completed in late 2012, with proposed revisions submitted for Government approval. The FSDP has also contributed to strengthening PIA itself with support to strengthen internal resources, staffing levels, and capacity in order that the agency can operate as a stand-alone entity reporting to Government.

3. SEC

   The SEC is responsible for regulating, supervising and developing the securities industry in Zambia. Core functions of SEC include overseeing the licensing, registration, and authorization of financial intermediaries, issuers of debt and equity instruments, and collective investment schemes. Zambia's capital markets are underdeveloped. Under the current FSDP, and in line with its own strategic plan for 2012 - 2015, the SEC has been overseeing the development, and strengthening of stable capital markets, including strengthening its internal institutional capacities, which includes building a cadre of professionals in capital markets, strengthening the commission's financial base, and building confidence in Zambia's capital markets through effective legal and regulatory oversight, and supporting product development and marketing to stimulate capital market activities, which includes bringing existing and emerging companies to the market place.

4.1.1.2 The Financial Sector Development Plan

The Financial Sector Development Plan (FSDP) lies at the core of GRZ's financial sector reform agenda and as such offers a comprehensive strategy designed to address fundamental weaknesses in Zambia's financial system, including weaknesses and inconsistencies in sector policies and regulations, and lack of focus, and direction, for agriculture and rural financial sector development. BOZ is mandated to coordinate the implementation of the FSDP on behalf of GRZ.

The first phase of the FSDP (FSDP I), which was implemented from 2004 – 2009, focused on legal harmonization, as well as on filling key knowledge gaps through research studies such as FinScope supply-side and demand-side studies, which helped to strengthen the framework conditions for future sector reform and growth. Under FSDP I the priority areas that were addressed included: a review of key financial sector legislation, including the Banking and Financial Services Act (BFSA); developing transitional legislation for the three main state-owned institutions - Development Bank of Zambia (DBZ), Zambia National Building Society (ZNBS) and National Savings and Credit Bank (NSCB)[32]; drafting new legislation in the critical areas of rural finance, housing finance and development finance; and a review and harmonization of laws governing financial institutions. Other areas of focus included resolving the future of insolvent state-owned financial institutions (for which resolutions have yet to be found); the production and dissemination of market information on the demand for and supply of financial services (primarily through the FinScope studies); and supporting the development of an effective credit reference bureau[33].

The second phase of FSDP (FSDP II) aims to improve the business environment by reducing the impediments of limited and costly access to finance. The programme design was completed by BOZ, with technical support from the World Bank. The Finnish Embassy funds the programme, which is being implemented from January 2010 until December 2012. Discussions were underway in late 2012 to extend the programme, with a formal decision expected on the same by the end of 2012 or early 2013. FSDP II envisions a financial system which is 'stable, sound, and market-based' and which can 'support efficient resource mobilization necessary for economic diversification and sustainable growth'. FSDP II focuses on three main pillars: enhancing market infrastructure, increasing competition, and increasing access to finance. Two key sub components under 'Access to Finance' are the Rural Finance Programme and Financial Education, both of which are targeting significant resources to the rural finance sector. More detail on the activities and impact of these two sub-components is provided in sections 4.1.1.2 and 4.1.1.3.

The structure of FSDP II comprises: the FSDP Secretariat (the overall coordinating body housed within the BOZ) with a four person team, which includes full-time seconded officers from the BOZ,

[32] The Zambia National Building Society is not a key player in rural finance and does not receive attention in this report. The NSCB has received support through the RFP and details of support efforts and current status is covered in more detail in section 4.1.1.3 and 4.3.4 on Savings.

[33] There is currently only one privately operated credit reference bureau in Zambia, Credit Reference Bureau Africa Ltd (CRBAL). Section 4.2 provides a description of CRBAL role, services, performance and business development challenges.

PIA, and SEC; the FSDP Steering Committee (providing overall direction and advice and chaired by the MoFNP); and the FSDP Implementation Committee (responsible for implementation and performance monitoring, and chaired by BOZ). A cadre of six technical working groups support research and development, implementation and coordination across the sector components of:

- Legal reforms and corporate governance;
- Payment systems;
- Market efficiency and contractual savings;
- Financial education;
- Access to finance;
- Financial markets.

Under FSDP phase II, longer term issues have been prioritized including: broadening harmonization of legislation; strengthening the capacities of the main regulatory authorities; sector wide initiatives to improve corporate governance and build capacity; enhancing payment systems; National Pension Scheme Authority (NAPSA) supervisory and investment reforms; developing professional 'competence banks'; and prioritizing and costing remaining FSDP recommendations in acknowledgement of the fact that these may not be completed by December 2012, when phase II is due to end.

The MoFNP and the FSDP II working groups, with the technical oversight of BOZ, PIA and SEC, and together with key stakeholders and sector development experts, have been systematically working on reviewing, revising and filling gaps in Zambia's financial legal and regulatory framework. These reforms have encouraged, and continue to foster, market experimentation and new market entrants.

Key reforms and restructuring that impact directly on rural and agricultural financial sector development, and on rural-based, low income businesses and households especially, include:

- development of the Zambia Rural Finance Policy and Strategy - the final strategy document is awaiting cabinet approval and a copy of the same is available to the public. Section 4.1.1.3 provides an overview of the strategy document;
- amendment of the Agricultural Act to include a regulatory framework to support and increase the usage of warehouse receipting systems and commodity trading – functions which will need to be adequately captured under the Agricultural Credit Act, Marketing Act, and Commodities Exchange Act;
- a comprehensive review of and substantive amendments to the Insurance Act, including specific provision for microinsurance;

- amendment of the Banking and Financial Services Act (BFSA), a principal piece of financial sector legislation under which various Acts fall[34], including those providing for branchless banking. Branchless banking regulations have been drafted and underwent review in July 2012. A draft bill with proposed amendments to the BFSA was presented mid-2012. Work continued during the remainder of 2012 to conclude amendments to the Act;

- development of appropriate legislation for the leasing sector, including review of laws relating to VAT charges on finance leases, which includes agricultural equipment leases;

- repeal of the Money Lenders Act (pushed back to 2013) with appropriate provisions incorporated into the BFSA;

- establishing the Zambia Enterprise Development Fund;

- reviewing risk-based Know Your Customer (KYC) principles and drafting a practice note to be issued to guide bank and non-bank entities working in rural areas;

- development and launch of the national microinsurance strategy. Section 4.1.1.4 provides an overview of the microinsurance strategy, including an update on progress to-date;

- providing for and increasing access to lower cost funding to support lower cost retail microfinance;

- facilitating the growth of remote access delivery channels: the BOZ has not yet developed regulations around agent banking and mobile-phone based transactions and payments, but is creating regulatory space for piloting and development and is working on a draft directive on e-money and draft regulations for payment system operators;

- development and launch of the national strategy on financial education under the FSDP II Access to Finance component. Section 4.1.1.5 provides an overview of the National Strategy, including an update on progress to-date;

- undertaking a series of initiatives to develop human capital in the finance sector, including: HIV/AIDS guidelines for financial institutions; a comprehensive database on professional expertise in the financial sector; and consolidated gender policies for financial sector places of work; and

- developing and implementing a Unified Collateral Agency.

Other achievements related to financial sector reform, which have less direct bearing on the agricultural and rural financial sector, but which are nonetheless key for strengthening Zambia's overall financial sector framework include:

[34] The BFSA captures key legislation for the formal financial sector, including banking and non-banking regulation and licensing requirements, establishment of physical premises, institutional governance structures, financial accountability, and privatization and structuring, among others.

- a study to review the tax regime in the financial sector, including identifying its implications for sector development and examining the role that taxation and regulatory measures can play in promoting financial inclusion;

- drafting a bill to amend the legal chapter for the Central Securities Depository;

- conducting a comprehensive follow-up review of the Pension Scheme Regulation Act (PSRA);

- amendments to the Building Societies Act, and the development of housing finance regulations; and

- harmonisation of the Companies Act and Accountants' Act (which underwent comprehensive review during 2012).

In many cases legislative reform has fallen behind the original planned timelines. Layman's draft bills have been developed in most cases, and a series of stakeholder consultations took place from May through to July 2012. However, there are still activities planned under the current FSDP, many of which have a direct impact on agricultural and rural financial sector strengthening, which have yet to be completed or initiated. A follow-up harmonization exercise is also required to ensure adequate consultations, and the removal of inconsistencies. This will again push out the final timelines for completion in many cases.

Work in progress and/or to be undertaken includes:

- the expansion, refinement or re-visiting of regulations and/or BOZ directives that affect the cost of providing financial services in rural areas (e.g. physical branch requirements, client verification requirements);

- under the framework of the FSDP, the BOZ plans to introduce a more diverse and appropriate framework for collateral coverage for agricultural and rural loans within the context of Basel II guidelines. The process will include an analysis of current regulatory gaps and weaknesses, the development of a proposal with appropriate options for broadening collateralization approaches and models, including the formulation of legal changes if required, and finally adoption and awareness raising across sector once appropriate solutions have been legalised;

- BOZ also plans to establish a sound regulatory and supervisory framework for tier III microfinance institutions (MFIs), which includes the need to identify one or more appropriate supervisory bodies for tier III financial entities;

- reviewing and strengthening microfinance regulations, including developing separate regulations on consumer lending so that there is a clear distinction between developmental microfinance institutions and consumer lending companies (often referred to as salary-based lenders) and appropriate monitoring and supervision of tier III MFIs[35] in order to address the proliferation of unregulated MFIs - the draft of the development finance regulations are still under BOZ management consideration;

- the acquisition of an appropriate national switch 'model' to ensure sharing of infrastructure for retail payment systems - revised timelines have yet to be agreed;
- the implementation of a corporate governance status audit across the financial sector;
- the subsequent development of a set of corporate governance and ethics codes and the holding of seminars on corporate governance, targeted at executives in financial institutions;
- the drafting of technical proposals for developing a new financial identification system, including the use of biometrics - this requires the undertaking of a broader stakeholder consultation process and appropriate oversight by the Ministry of Home Affairs; and
- the development and implementation of training course curricula targeted at financial actuaries.

4.1.1.3 The Rural Finance Programme: focus and progress to-date

The Rural Finance Programme (RFP) is a key sub-component under the FSDP II Access to Finance component. With a total budget of USD 17.4 million, the RFP comprises a highly concessional loan from IFAD of USD 13.8 million, and co-financing from GRZ, as well as from participating financial institutions and beneficiaries. The loan, declared effective on 7 September 2007 is scheduled to close on 31 March 2014, with programme completion by 30 September 2013. The programme is managed and coordinated by the Programme Management Unit (PMU) placed under the MoFNP. The overall development goal of the RFP is to improve the livelihoods of the target group, which includes some 150,000 rural households that can benefit from improved access to financial services.

Plans are already underway for a follow-up programme. IFAD and GRZ hope to avoid a total close down by ensuring a new financing agreement is out and ready for implementation by September 2013. In the meantime, the evaluation of the current programme, together with stakeholder consultation will contribute to the design of a new rural finance programme, which is being undertaken by IFAD and GRZ, and is due for completion by mid-2013. The design process includes a review of current RFP areas of activity, which should continue under a new programme, as well as identification of new activities and resource gaps.

The current RFP components are summarised below together with possible plans under the new rural finance programme.

[35] Tier III MFIs includes all non-deposit taking MFIs with paid up capital less than ZMK 25 million (approximately US$5,000).

1. Rural finance policy and strategy: The RFP has overseen initiatives for developing a conducive and supportive enabling environment particularly for providing financial services to the MSME sector. A vital output under this facility has been the development of the Zambia Rural Finance Policy and Strategy document. The policy and strategy fills a critical gap in financial sector development planning, and provides a well-structured development blueprint and an investment framework for cooperating development partners to buy into over the next five years. The policy and strategy framework offers a contemporary roadmap for addressing systemic weaknesses at macro-, meso- and micro-levels, which should also lead to better coordination of both public, and donor funds that will be available in the future for the development of Zambia's rural finance markets. The Policy and Strategy document includes:

    - a diagnosis and situational analysis of the (demand-side and supply-side) challenges currently facing the rural finance system;
    - preferred strategic options for developing it (encompassing market opportunities, capacity building, targeting and delivery mechanisms, as well as guiding principles and priorities for implementation);
    - recommendations to strengthen policy, legal, regulatory and supervisory functions related to rural microfinance;
    - recommendations for improving sector coordination;
    - institutional arrangements for developing and overseeing monitoring and evaluation mechanisms;
    - recommendations for information and learning dissemination; and
    - a draft of a rural finance policy, together with a critical action plan, which are currently contained within a main report[36], and which, at the time of finalizing this study, were under cabinet review. Based on GRZ decisions, the draft policy will eventually emerge as a short policy document of the government.

2. Strengthening community-based savings and credit: it is highly likely that this component will figure again in a new IFAD/GRZ rural finance programme. Needs already identified in this area include documenting successful community-based finance models, including village savings and loans models (VSLAs) developed under the current RFP, and support for strengthening and scaling-up appropriate models. An increased emphasis on capacity building (sector training and technical assistance) at the informal level and across the sector as a whole is likely to figure prominently in the new programme design. Section 4.3.4 provides further insight into emerging lessons and the impact of VSLAs' development under the current RFP.

[36] Zambia Rural Finance Policy and Strategy, Oxford Policy Management, Final Report, 18th June 2012.

3. The DBZ wholesale credit line: This facility for accelerating MFI expansion in rural areas has led to growth and provided valuable lessons. Although there were initial delays around appropriate targeting of funds[37] and disbursement, the fund has been effective in supporting the buying down of risk for key MFIs, enabling them to enter new markets and expand in those in which they were already operating, with the aim of directly benefiting low-income rural households in their agricultural and non-farm enterprises. DBZ's apex lending is described in more detail in section 4.3.3 of the report, including insight into lessons learnt. A future rural finance programme is unlikely to offer a credit line to DBZ since developments in the second half of 2012 meant the bank received significant capital from GRZ for wholesale lending to MFIs and potentially SME lending. Plans for support are likely to focus on building internal capacity in product design and roll out, and in managing multiple refinancing products, which would ideally include agricultural term finance.

4. Innovation and outreach: Under the current RFP, this facility provided small grants and matching grants that supported innovation and expansion in rural agricultural finance. Funding for piloting financial models flowed through a selection of local NGO partners, known as 'promoters'. A key success has been the establishment of revolving savings and loan schemes that provide small-scale production loans as well as community-based savings mechanisms. Under the same facility, grants for branch start-ups or expansion in rural agricultural lending were awarded to MFI partners[38] committed to growing and strengthening their rural and agricultural loan portfolios. Celpay Zambia also received grant support to invest in new software and expand its point of sale (POS) network. The intention is that Celpay will have a POS presence in every district in Zambia as a result of the investment. Supporting innovation and outreach will be a key window of opportunity under a new rural finance programme, with greater emphasis on outreach to mutiple partners, on encouraging and scaling successful, and innovative, agricultural and rural financing models (including, for example, value chain finance and cellphone-based financial service delivery channels), as well as on results-based monitoring and evaluation.

There has yet to be a formal evaluation of the RFP particularly with respect to the impact, and effectiveness of the programme's components. However, programme reports[39] point to satisfactory results in terms of outputs and outcomes under the RFP key components, and progress in achieving the programme goal - 'to increase the use of sustainable financial services in rural areas'. Key achievements as of the end of June 2012 include:

- 808 savings and credit groups (CBFIs) formed or strengthened, with 12 689 members (8,983 women and 3,706 men), with USD 283,462 in voluntary savings, and USD 381,261 in

[37] Originally the credit line was to facilitate commercial bank lending for contract outgrower schemes or production companies supporting or willing to support small-scale producers. However, uptake by the banks at the time was so sluggish that the decision was taken to re-target the fund to MFIs that were committed to transformation and rural and agricultural expansion.
[38] CETZAM Financial Services Ltd (based out of Lusaka), Empowerment Microfinance (based in Siavonga) and Microcredit Foundation (expansion into Zambia's eastern province from across the Malawi border).
[39] The Mid-Term Review, Cardno Emerging Markets (East Africa) Ltd, January 2011, and more recently the IFAD Supervision and Implementation Support Mission Report, August 2012.

gross loan portfolio;

- 1,059 clients are accessing micro-loans (with the portfolio value of USD 252,525) from the NSCB through its five branches where microfinance services have been launched with RFP support;

- 892 loans with the value of USD 3.2 million disbursed through four participating financial institutions using the credit line extended by the DBZ; and

- the development of the Rural Finance Policy and Strategy, submitted for Cabinet approval.

However, overall RFP achievements against the original target of reaching 150, 000 rural households is still limited. The number of households benefiting from RFP support was estimated at about 28,000 in IFAD's supervision report of June 2012. There are several reasons for the RFP being behind in terms of outreach targets. Firstly, there were lengthy delays around procurement of services, but only some 18 months after the inception of the programme, were appropriate and streamlined procedures for procurement put in in place. Latterly, the procurement process has been much smoother and faster. The RFP encountered major challenges and setbacks with regard to NSCB branch expansion, and the procurement and installation of an appropriate management information system, which as joint activities, were intended to reach 100,000 rural households. The RFP mid-term review report also highlighted the weak capacities of implementing partners responsible for mobilizing and strengthening VSLAs, which slowed growth in this area. Aside from on-going challenges in supporting NSCB, the RFP has been able to make up ground, and there is good scope for further progress before the end of the programme.

4.1.1.4 National microinsurance strategy

Since 2009, a multi-stakeholder Technical Advisory Group (TAG), in partnership with FMT and the International Labour Organisation (ILO), has been implementing a sector development approach aimed at stimulating interest in, and accelerating the development of, a viable microinsurance market in Zambia. This approach is based on the assumption that working with the private sector and engaging all relevant industry stakeholders is the most effective way of developing a sustainable market. An action plan that outlines the sector development framework and activities was formulated in January 2010 and has been the main guide in shaping the on-going process. Annual work plans have been developed alongside this action plan to guide the sequencing and resource allocation for specific activities within a given year.

With the financial support from FMT, ILO and United Nations Capital Development Fund (UNCDF), a number of market development interventions have been implemented, including capacity building of the insurance industry through microinsurance innovation seminars and training workshops. In 2010, a Microinsurance Acceleration Facility jointly funded by FMT, ILO and UNCDF was launched with the overall objective of supporting insurers and potential distributors in testing various strategies for increasing microinsurance penetration in Zambia. There have been some recent promising outcomes. For instance in 2012, four insurers (Professional Life, African Life, Zambia State Insurance Corporation (ZSIC) Life and Madison Life) launched new life insurance products, and a number of other life and non-life products are in the pipeline. Of these new microinsurance products, it is worth mentioning that ZSIC Life's products were developed and launched specifically for rural households.

4.1.1.5 FSDP II National strategy on financial education

An important sub-component of the FSDP II's Access to Finance component is the national, five-year strategy (2012-2017) for financial education[40]. The strategy, developed by a specially appointed working group, and spearheaded by BOZ, PIA and SEC, is guided and monitored by the Financial Education Steering Committee (FESC). Implementation is carried out through the Financial Education Coordination Unit (FECU) housed within the BOZ. The strategy provides a comprehensive framework for improving the financial education of the Zambian population, and for reaching out to poorly educated and rural populations in particular.

The strategy document itself refers to the fact that existing programmes at national level are fragmented, lack coordination, and, as a result, have had limited overall outreach, contributing in this respect to the high financial exclusion rate in Zambia. Many people lack the skills, knowledge and confidence to be able to manage their finances well in Zambia. FinScope 2009 reports that zero percent of small-scale farmers were saving for retirement or old age. Low and very low income-earners are not familiar with basic terminology. Moreover, they lack the confidence to approach financial service providers, and do not have a positive attitude towards them. These barriers to access are particularly acute in rural areas. Over indebtedness is also an increasing concern. According to FinScope 2009, 16 percent of adults accessing credit report using more than half of their incomes to service their debt.

The primary objective of the National Strategy on Financial Education is to empower Zambians with knowledge, understanding, skills, motivation and confidence to help them to secure positive financial outcomes for themselves and their families. At a practical level, this translates into better money-management, savings, accessing information, and choosing and using financial products and services, which will contribute to increasing financial inclusion. The strategy, commissioned by the BOZ, and co-funded by BOZ, the UK's Department for International Development's (DFID's) Financial Education Fund (FEF), and FMT, prescribes priority financial education programmes for Zambia, together with the principles, which will be employed in programme implementation.

Under the strategy, financial education programmes will target children, youth and adults with a particular focus on workplaces, small-scale farmers and MSMEs. Multiple partners from across a broad range of sectors are being recruited to support implementation of the strategy. The strategy is highly contextualized and focuses on 'teachable moments' – times in people's lives and contexts where they are more likely to be receptive to financial education, e.g. starting or completing school, starting work or a small business. Leveraging activities will also play a key role in formulating partnerships, pooling financial resources and scaling outreach through existing community-based structures, organisations and groupings, including, for example, piggy-backing on social cash transfer schemes, which target most vulnerable populations.

There are existing and meaningful financial education programmes being implemented, and a key approach of the nationwide financial education strategy is finding practical means for

[40] Extracts from the National Strategy on Financial Education are the main source for this section of the report.

collaborating with existing initiatives. Some of these programmes are highlighted below[41].

1. Programmes sponsored by commercial banks

A number of commercial banks have introduced financial education programmes to drive either their own business needs to establish a more educated client-base, or as part of their corporate social responsibility activities. Some of the most extensive initiatives fall under Zanaco's Financial Fitness programmes, which include financial education for schoolchildren (reaching 150 schools, in 33 districts), youth, adults, SMEs, and a series of workplace programmes, including one for Zanaco's own staff. Zanaco is also working in collaboration with ZNFU, reaching out to small-scale farmers, many of which are clients under Zanaco's Lima Credit Scheme[42]. Other banks supporting programmes include Access Bank, Barclays Bank, and First National Bank (FNB). Aside from Access bank, which has provided over ZMK100 million in support to community schools in Lusaka, these programmes are very small-scale[43]. Other formal sector institutions involved in financial education, but which do not have dedicated programmes, include BAZ, BOZ, and PIA. These programmes target the general public through roadshows, information dissemination at trade fairs, and other similar type awareness raising events.

2. Programmes implemented by NGOs

A number of NGOs are also using the Zanaco curricula materials in their own programmes, e.g. Camfed (targeting financial education at young women in rural areas, with over 10,000 young women trained) and Restless Development (targeting school children and student teachers through education colleges). The NGO 'Children International', whose program began in 2011, has helped train some 15,000 under-privileged children through a network of community-based centres and schools. Savings mobilization is a key part of the programme's approach. Lastly, 'Junior Achievement', an American-based organization with funding from Barclays Bank, Stanbic Bank and Citi Group, focuses on financial education and entrepreneurship materials for youth. Training is through the Basic Education Teachers' Union of Zambia (BETUZ).

Benefits from implementation of the nationwide financial education strategy will include improved financial knowledge and understanding for household consumers, businesses, financial service providers, government and civil society. Effectively reaching these targets will help pave the way to increasing financial interaction between the various parties, and to making interaction more beneficial. Better financial education is also one of the key ways for influencing the uptake of financial products, services and related technologies.

However, financial inclusion initiatives are unlikely to succeed unless people have the knowledge, skills and confidence to make effective use of financial products. While the increased availability of financial products and services, which has occurred in recent years for some sections of the

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[41] A stock-take study commissioned by FMT on behalf of BOZ and entitled 'Stock-take of Financial Education in Zambia: A Review of Financial Education Initiatives, M&N Associates, 2012' provides a detailed description of existing financial education initiatives and is available from the FSDP Secretariat on request.

[42] Section 4.3.3 and Box 3 provides a summary of Zanaco's Lima Credit Scheme, as well as plans for expansion.

[43] The National Strategy on Financial Education for Zambia, 2012 – 2017, FSDP, Financial Education Working Group, FMT.

population, has opened up opportunities for people to manage their finances more flexibly and more effectively, it has also given rise to new risks to consumers and financial service providers, e.g. from over indebtedness and high levels of default.

Therefore, the tripartite and simultaneous approach of financial education, financial inclusion initiatives and financial consumer protection has a vital role to play in achieving the goals of the FSDP, as none is likely to be sufficient on its own to achieve the goal of greater, more sustainable financial inclusion. Macro, meso and micro-level players can all play a role in implementing parallel, complementary initiatives to build inclusion, improve consumer protection, and stimulate the development of innovative, appropriate financial services for rural businesses and households.

4.1.1.6 Future sector development support

1. Establishment of a Rural Finance Unit within the MoFNP

An appropriate institutional home for rural finance was explored as part of the Zambia Rural Finance Policy and Strategy development process. Various government ministries, including those that oversee areas of economics, finance, agriculture, cooperatives, community development, commerce, trade, and industrial development, are important stakeholders in agricultural, and rural financial sector development. Of key importance is to ensure adequate human and financial resources as well as sufficient supervisory influence to champion and drive the rural finance agenda across both the public and private sectors. Since rural finance has direct relevance to national priorities and requires close linkages with BOZ, and key sector regulators and associations, the overall consensus has been that the MoFNP is the appropriate institutional base for a rural finance unit. The government plans to establish a rural finance unit within the ministry, which will coordinate, and provide oversight of, nationwide initiatives such as those under the Zambia Rural Finance Policy and Strategy (current), DFID Access to Finance programme (see below) and the new GRZ/IFAD rural finance programme (follow-up to the current FSP, with planned start-up in early 2014).

2. DFID Access to Finance Programme

In addition to the planned continuation of the FSDP after December 2012, and the prospect of a new GRZ/IFAD rural finance programme to come on line in January 2014, DFID is expected to support a five-year ‘access to finance’ programme. The purpose of the programme will be for the financial sector to deliver a wider range of financial services to more people, and businesses in rural Zambia. Based on DFID’s TOR for the design and implementation of the programme, the goal of the programme will be to make sustainable improvements in the livelihoods of poor people in rural areas. The programme will take direct attribution for giving 300,000 additional people and businesses access to financial services (of which 195,000 will be women), providing 50,000 smallholders with access to agricultural credit (of which 25,000 women), and 12,000 SMEs access to credit from banks or microfinance institutions. By 2017, the programme aims to have contributed to an increase in the percentage of people financially included in Zambia to 50 percent of the population, and to a 25 percent average mean increase in the income levels of

200,000 rural households. DFID states that its programme will take a market development approach to support increasing access to savings, loans, payment mechanisms, insurance and pension services. The programme will address sector constraints at macro, meso and micro-levels, with an emphasis on supporting retail suppliers (commercial banks, microfinance institutions and community-based finance initiatives) whose financial services lead to increased incomes, and greater financial inclusion. The programme is expected to become operational in early 2013. There appears to be considerable potential for synergy with national strategies and priorities.

4.2 Meso-level: scope and effectiveness of financial sector infrastructure

This section of the report describes the main entities and initiatives at meso-level that are contributing to developing financial infrastructure. These meso-level entities are at different stages in their maturity, and in most cases there is still work to be done to refine the regulatory environment in which they operate, and also their business models. Zambia's Rural Finance Policy and Strategy presents a set of draft policies and strategies for strengthening meso-level infrastructure. In addition to institutional strengthening, it captures policy and strategy requirements to enhance payment systems, credit reference bureau(s), warehouse receipting, collateral management, microinsurance (including weather-based index insurance), as well as increasing access to demand-side and supply-side market information, and well-structured, demand-driven skills development, aimed at financial institutions and support organisations.

1. Credit Reference Bureau Africa Limited (CRBAL)

As of June 2011, less than 5 percent of individuals and firms in Zambia had a credit record.[44] CRBAL is currently the only registered, operating credit reference bureau in Zambia, and whilst the number of credit reports searched increased by almost 60 percent in 2011[45], its coverage and usage remains limited. The bureau, initiated in 2007, and with its head offices in Nairobi, is supposed to collect and maintain positive and negative borrower information. In most cases, those banks and non-bank financial institutions that are using the service are only submitting negative information (i.e. information on poor or non-performing clients) and they are not using the bureau to obtain credit reports as part of their credit analysis process. This neither enables, nor takes advantage of the positive dimension of credit referencing. If working effectively, this should support and encourage both increased lending and good repayment performance, as financial institutions are better able to identify good clients, and borrowers have an incentive to build a history of on-time payment to lower the cost of credit. At present, financial service providers still have to expend significant resources on assessing creditworthiness, which pushes up the cost of borrowing. There are also concerns around CRBAL's current fee structure in that it is a disincentive to users who work primarily with low-value credit obligations, for whom the costs of using the agency frequently would prove unsustainable. It is felt that support should be given to reviewing CRBAL's current business model in consultation with financial services supplier associations (and other key industry stakeholders) to ensure that the model serves the best interests of the industry by bringing value-add to financial service suppliers' internal control and

44 See www.doingbusiness.org/data/exploreeconomies/zambia/getting-credit.
45 BOZ Annual Report, 2011.

risk management functions, thereby contributing to increasing access to credit and reducing the costs of borrowing. A review should also help ensure that appropriate consumer protection is being applied and that consumers are being accurately represented. Such a review process should also consider consumer interests from the perspective of there being just one privately run bureau, and whether or not pricing, service delivery and client orientation would best be improved by encouraging healthy competition, and multiple, competent service providers, including, for example, a separate bureau to cater for developmental microfinance sector requirements.

2. Lusaka Stock Exchange (LuSE)

LuSE opened in 1994 in line with GRZ's broad economic reform and private sector development goals. There are still relatively few companies trading on the exchange, and it remains dominated by foreign companies. Though under-utilized as a means for raising capital, and despite the need to build confidence in it so more Zambian companies engage with the exchange, market capitalization reached an all time high in 2011, growing by 58.3 percent from ZMK 30,911.6 billion as at December 2010 to ZMK 48,929.2 billion as at December 2011. The All-Share index was 22.3 percent higher by December 2011 in relation to the previous year[46]. This was despite reduced participation of non-resident investors, and a decline in net capital inflows (from US$100.5 million in 2010 to US$13.5million end of 2011[47]). According to its strategic plan, the SEC plans to build LuSE functions as an effective contributor to economic development by increasing confidence in capital markets by stimulating growth and expansion of trading, developing an appropriate legal and regulatory framework, introducing and growing new trading exchanges, promoting new products and securities, and increasingly engaging professional bodies that can help strengthen, and ensure best practice approaches in licensing, transparent transactions and trading, and monitoring and supervision.

[46] BOZ Annual Report, 2011
[47] Idem

3. Zambia Agricultural Commodities Exchange (ZAMACE)

Whilst LuSE offers a platform for raising investment capital through the sale of bonds and shares, ZAMACE is Zambia's platform for formalized and transparent commodity trading. Since its inception in May 2007 as a private corporate entity, ZAMACE has developed and tested a model for commodity trading. It has traded close to US$ 80 million in commodities between last quarter 2007 and first quarter 2011. ZAMACE official website[48] provides a good overview of efforts to develop a robust commodity trading framework. For several years the SEC has been supporting the development of a regulatory framework for exchange trading of commodities, including the Commodity Exchange Bill, which underwent stakeholder review in February 2012, and will likely be enacted in 2013. The Bill provides for licensing of commodity exchanges and various parties on the exchange. Focused on agricultural commodities, the exchange offers a formal and transparent platform for commodities trading. The Exchange has developed industry accepted quality standards for maize, wheat, soy and sunflower.

In July 2011, the Board approved the re-structuring of the Exchange in order to make it more responsive to market needs, to broaden ownership, and to attract fresh capital. As at the end of 2012, ZAMACE had converted to a public corporation, with its fully subscripted membership dropping from 15 to four[49]. Several new shareholders joined at the end of 2012 including ZNFU and the Grain Traders' Association of Zambia (GTAZ). At the same time, shareholding and brokerage membership were separated, meaning that brokers are now required to meet specific requirements, pay an annual membership fee, and collect trade commissions. Brokerage has also been tiered, allowing smaller players such as farmers' association and small-scale individual traders to become members.

Other than trading services, ZAMACE's mandate is to support database and documentation management, offer training and certification of warehouse operators, and provide warehouse inspection and certification, which provide the foundation for warehouse receipting. When backed by a suitable legal framework, warehouse receipts can act as collateral for inventory financing. Collateral management agreements oversee stored commodities and lenders secure their loans against the stored value. From 2013 onwards, trading at the Exchange will be based on warehouse receipts. In addition to traditional spot trading and trade information distribution, the restructured ZAMACE will offer US dollar denominated Zambian grain futures to be listed and traded on the Johannesburg Stock Exchange (JSE). More on the latest developments around warehouse receipting and community trading are covered in section 4.3.3 which explores emerging financial credit delivery models.

[48] www.zamace.org.

[49] The remaining initial shareholders - Afgri Corporation, Cargill Zambia, CHC Commodities and Quality Commodities.

4. Financial Sector Associations

There are a number of associations linked with the financial sector. However, the most notable associations, and those most proactive in sector reform, include the Association of Microfinance Institutions of Zambia (AMIZ), the Bankers' Association of Zambia (BAZ), the Insurance Association of Zambia (IAZ), Credit Union and Savings Association of Zambia (CUSA), and the recently established Payment Systems Association (PSA). The core functions, capacities, and future plans of these facilitating institutions with respect to their support to sector development are examined below.

AMIZ - AMIZ was established by microfinance practitioners and was officially registered under section 7 (1) of the Societies Act in 1998. Its role is to facilitate, support and upgrade the activities undertaken by its members. AMIZ is dependent on revenue grants (donations) and member subscriptions, but also raises income through the provision of services such as training (participation fees) and action research for its members and broader microfinance industry stakeholders. As of October 2012, AMIZ had 23 members of which five are deposit-taking institutions. The remaining membership is non-deposit-taking financial institutions, which includes salary-based lenders, and small faith-based institutional lenders.

It is some years since AMIZ has been able to play a transformational role in the microfinance sector. Donor funding for AMIZ has declined in the past five years as donors turned their attention away from direct support to the microfinance institutions, and framework support bodies like AMIZ. Membership fees are on the decline as the Association lacks resources to attract and sustain members by providing demanded services. At the close of 2012, the financial position of AMIZ remained fragile. Continued operation of the Association is dependent on negotiations of significant amounts payable and sourcing funds to settle the same, and to sustain day-to-day operations. Despite its willingness to respond to industry challenges, its current weak financial position and lack of resources mean AMIZ is unable to address members', and broader industry needs effectively. There is no other meaningful platform for microfinance learning or knowledge dissemination in Zambia. AMIZ needs to invest in and upgrade its product and service offerings.

Though progress is reportedly slow, AMIZ is actively involved in re-formulating microfinance regulations to distinguish between developmental MFIs and salary-based lender MFIs. Whilst initially involved in the formulation of CRBAL and the more recent Consumer Lenders Association[50] (CLA), AMIZ working relations with these other associations is more at arms length; a factor linked with AMIZ's weak financial position.

Despite the above challenges, AMIZ is taking critical steps to re-invigorate its role, services and membership base. In September 2012, the Board of AMIZ was reconstituted. The CEOs of four member institutions form the executive committee, whilst three sub-committees have been established to oversee key functions – finance and audit, governance, and strategic and business planning. As at the end of 2012, AMIZ's business plan and strategy was in the early stages of

[50] The equivalent of AMIZ, but established to service membership needs of the consumer-based / salary-based lenders

development. However, plans comprise four main pillars for development – 1) advocacy, 2) information dissemination (including research and development), 3) marketing and positioning and 4) industry capacity building.

Any increased focus on financing, capacity building and regulation of the microfinance sector should involve AMIZ, although this may necessitate re-visiting the association's role and the scope of its services. For example, it could guide the development of a more appropriate business model for the sole existing - or any new - credit reference bureau (and/or take a lead role by housing and overseeing the activities of a new bureau for the microfinance sector). AMIZ is also well positioned to commission and manage capacity building efforts, though support is needed to identify what types of training and capacity building are priority at this stage in the sector's growth. AMIZ could also take on responsibility for conducting operational audits (on behalf of DBZ or other potential investors) by either building internal capacity or hiring expertise. Cost recovery for operational audits, training and technical assistance should come through MFIs themselves, as donor support is not sustainable. MFIs should be encouraged to seek and pay for capacity building that enhances their profiles and accountability to investors, shareholders and clients.

BAZ - BAZ is proactive in its representation of the banking sector, and in both formal and ad hoc dialogue with BOZ and associations such as the newly established PSA (see below). The Chief Executive of BAZ also sits on the current Rural Finance Programme (RFP) Programme Reference Group (PRG), which oversaw the development of the Rural Finance Policy and Strategy. The Association is also playing an active role in contributing to developing an appropriate regulatory framework around mobile and electronic payment systems. BAZ is also interested in building its own capacity to service members' needs. During the GRZ/IFAD programme design mission (December 2012), BAZ agreed on the rudiments of a support framework under the new IFAD/GRZ rural finance programme, which proposes a structured approach to developing the Association's institutional capacities and resources, aiming to strengthen its participation in implementing sector development initiatives such as industry training, research and development exercises, and joint collaboration with associations such as AMIZ and PSA in industry information dissemination.

PSA - Three founding members, namely, Mobile Payment Solutions, Mobile Transactions, and Celpay, established PSA in 2011. The Association welcomes bank and non-bank membership and charges a minimal membership fee. The formation of the PSA is both timely, and relevant for financial sector development in Zambia. The Association has done well in establishing itself as a credible industry representation and knowledge resource in its first year. Having achieved recognition by BOZ, PSA is an active participant in the FSDP Payment Systems Working Group. It is also closely monitoring new developments for a national switch. According to its by-laws, the PSA will support the growth of a strong mobile and electronic payments industry, which could potentially contribute to lower costs, and increased financial inclusion. On the supply-side, the PSA strives to be a focal point for industry representation, dialogue and advocacy, and to contribute to developing the enabling environment by promoting interoperability and integration of systems, and to expanding the types of users (e.g. financial companies, institutions and associations). On the demand-side, PSA is planning to increase the scope and usage of services by educating consumers, and by increasing their access to the financial sector and financial products.

The Insurers Association of Zambia (IAZ) is the industry body with mandatory membership of all licensed insurance companies in Zambia. The main mandate of IAZ is industry representation of all issues pertaining to the creation of an enabling environment that can foster industry growth and smooth operations of insurance companies. IAZ participates in various forums including lobbying and advocacy of issues that can impede the growth of the industry growth. Since August 2009, IAZ has been a member of the Technical Advisory Group on Microinsurance. As noted in section 4.1.1.4, this Technical Advisory Group has been spearheading the implementation of the national strategy on microinsurance. Among future plans, IAZ, in partnership with other key industry stakeholders would like to invest in insurance education, with a view to increase knowledge and awareness of the benefits of insurance even among low-income people.

CUSA – CUSA has a long-standing history in Zambia[51]. It considers its mandate as being to represent the interests of member savings and credit unions and cooperatives in Zambia, which reportedly includes the provision of taxation advice, and technical assistance programmes in financial management, the creation of nationwide credit union networks, and the promotion and uptake of technologies to broaden and upgrade services. The official website for CUSA reports that the Association represents over 500 credit unions with some 700,000 members. Membership is very much focused on public sector / civil service employees (e.g. airport, teachers, army, air force and national service). In 2011, CUSA unveiled ambitious plans to roll out a management information system that supports a network of automated teller machines (ATMs) and points of sale (POS) terminals accessible to all member unions and cooperatives. More detail on this project is provided in section 4.3.6.

CUSA's plans to invest in and upgrade savings and transaction platforms for its union and cooperative membership could have relevance for rural financial sector deepening. However, CUSA's role in supporting the growth and stability of rural-based savings and credit cooperatives (SACCOs) is not well developed. Core issues with respect to strengthening SACCOs include the need to establish an appropriate regulatory and supervisory framework for SACCOs (as third tier financial service providers), and to establish if, and how, SACCOs (and informal financial institutions in general) can enhance their contribution to financial product and service delivery in rural areas. A detailed situational analysis for rural and agricultural SACCOs is covered in section 4.3.1.

[51] See CUSA's website for more information, www.cusa.co.zm

Based on identified constraints, the Rural Finance Policy and Strategy proposes a package of macro-, meso-, and micro-level policies and strategies, which will contribute to strengthening financial cooperatives, including SACCOs. These include:

a) a review of the financial landscape (including the legal and regulatory framework) to assess the need to introduce new tiers and/or types of regulated financial institutions in rural areas;

b) undertaking a review of the sector to gather market information to be used in developing an appropriate regulatory framework and a well-designed capacity building programme;

c) building capacity for direct or delegated regulation and supervision of SACCOs; and

d) expanding and strengthening the supply of capacity building support for FSPs and their representative associations.

5. National Switch

BOZ took over spearheading the introduction of a national switch in 2012. The aim of a national switch is to establish a platform for interoperability in order to maximize on efficiencies and use of retail payment infrastructure. Banks remain reluctant to share payment infrastructure, and non-banks, such as electronic payment and mobile money providers, are also reluctant to increase interoperability of their services. The risk of companies developing and operating their own systems, which do not talk to each other, is that this leads to duplication, fragmentation and inefficiencies in what is a relatively small marketplace. Lack of shared switch also results in expensive and slow interbank transactions. Protectionism of this kind may also lead to disjointed efforts in resolving challenges in rural and agricultural financial service development. Progress remains slow, however, and options such as enhancing the existing Zamlink[52] platform are evidently not being explored. Moreover, some of the largest banks have not joined Zamlink, and BOZ is not imposing compulsory membership. BOZ anticipates that a national switch can be fully implemented by 2014. However, unless stakeholders can identify common ground through a structured approach to resolving issues, it is likely to take longer.

6. Branchless banking and electronic payment systems

There has been a significant increase in the use of electronic payment systems in Zambia over the past three years. Table 1 below provides comparative figures for 2009 and 2011 for key types of transactions in the electronic payments sector[53]. For the period 2010 to 2011, the overall volume and value of transactions on the Zambia Interbank Payment and Settlement System (ZIPSS) increased by 16.0 percent, and 22.0 percent respectively. The volume and value in POS alone has more than doubled in the last three years.

[52] Zamlink is a privately owned and operated switch in Zambia, which is currently used to support ATM withdrawals, electronic airtime vending, and VISA gateway for member banks offering VISA cards.
[53] Source: BOZ Annual Report, 2011.

Table 1: Use of electronic payment systems, comparative figures for 2009 and 2011

Type of transaction	Volume increase 2009 - 2011	% increase 2009-2011	Value increase 2009-2011	% increase 2009-2011
Direct Debit and Account Credit Clearing (DDACC)	1,510,645 - 3,024,080	100.1%	4,503 – 8,751 billion	94.3%
Automated Teller Machines	18,919,304 – 27,506,714	45.3%	7,567– 13,209 billion	74.5%
Points of Sales (POS)	542,623 – 1,210,436	123.0%	240 – 507 billion	111.2%

The relatively hands-off approach of the government and BOZ, and their deliberate policies to not over-control market developments have resulted in increased cross-sector collaboration and experimentation in the use of branchless banking and electronic payment systems.

The potential for application in the financial sector has huge implications for increasing financial access in rural areas and for reaching out to most remote communities at reduced cost, and with more diverse and user-friendly products and services. High levels of enthusiasm and the testing (and in some cases the scale-up) of models are already evident as, for example, lead electronic transaction providers enter into partnership with MFIs to establish electronic platforms for credit disbursements and collections, or work with lead commodity buyers or agricultural suppliers to offer pre-paid cards and vouchers for products and services targeting small-scale farmer clients. The use of mobile and electronic payment platforms has also extended to food security voucher programmes, and cash transfer programmes for extremely vulnerable households. For the most part initiatives have lacked, or are slow, to achieve scale, and whilst some of these activities are gaining traction, in other cases, pilots have encountered problems directly linked with issues around limited understanding, low knowledge, low buy-in and uptake, and weak trust (across consumers) and weak management capacity (across providers and agents). A summary appraisal of current practices and emerging mobile and electronic payment initiatives and partnerships is provided in section 4.3.6, whilst section 7 of the report captures the implications and recommendations for increasing financial inclusion using branchless banking and electronic payment system technologies.

A study commissioned by FMT, and completed during 2012, explores the retail payments landscape in Zambia, and contributes to an increase in the understanding of retail payment systems development[54]. According to the study, there are no significant policies or regulatory constraints holding back progress. However, there is work to be done to complete legislation and guidelines for usage, and though developments are on the right track, widespread confidence in, and usage of accessible and affordable payment systems, in rural areas especially, is still a long way off.

Current gaps in the regulatory framework for payment systems include:

[54] Mapping the Retail Payment Services Landscape, Bankable Frontier Associates LLC, October 2012.

- e-money regulations that provide minimum standards for compliance, and clear guidelines for new entrants in the market;

- rules and guidelines, which enable and inform banks' use of service delivery agents, help expand banks' outreach to rural areas, and support increased efficiencies and customer convenience, as well as helping create a level playing field for banks and non-banks;

- establishing effective supervisory practices, including risk management functions; and

- puttingadequate measures in place for fraud prevention, and for tracking and penalizing fraud.

The study on payment systems reveals that whilst gaps and weaknesses in infrastructure constrain payment systems development, other real obstacles to the development and expansion of retail payment systems emanate from constraints in the market place, and market dynamics and organization in particular. Findings from the study indicate that the formal financial sector still lacks interest in low-income markets, and that without meaningful incentives (and meaningful market opportunities) targeted at lower-end rural market entry, they are likely to remain focused on high-end market segments, where it is easier to reach target markets, and exploit opportunities rather than attempt to address the real and perceived high costs, extra administration, and challenges of product development and low education levels associated with low-income, rural market segments. At the same time, the reluctance by formal banks and non-banks to share infrastructure and to move toward interoperability, as well as overly stringent account opening requirements, implies that advanced payment systems services remain out of reach for most low-income individuals and micro enterprises. In the same study, the demand-side analysis showed that, as may be expected; urban-based populations and those with regular, consistent incomes have greater access to a range of options than those living in rural areas with irregular incomes and/or employment and/or informal employment. Across all sectors, however, there is a need for increased levels of payment services that are timely, efficient and reliable.

7. Market information

Financial sector development stakeholders and financial services suppliers need regular access to credible market information for strategizing and decision-making. There are a wide variety of sector studies and assessments in the public domain in Zambia to guide the improvement of industry development planning and intervention support. The pace of sector change warrants that such studies should be conducted on a regular basis to assist industry development efforts. Currently, financial service providers tend to rely on internal market intelligence and experience when it comes to product and service development and there is a gap in suppliers' understanding of agricultural and rural financial needs, particularly small-scale farmer and household needs. This gap is being partly filled by NGOs and market development facilitators, such as FMT. Increased spending on research and development (focused on increasing financial inclusion) could help private sector businesses and financial service providers to develop new financing models and partnerships, or to take existing models to scale.

Another current gap in market information lies in better understanding of the growth potential in agricultural markets. Financial service suppliers (and for that matter market development facilitators) usually lack detailed information on the growth potential of agricultural/agribusiness subsectors and value chains and on specific target groups (e.g. the number of potential borrowers for tractors and farm machinery is currently unknown).

Increasing access to quality market information, which facilitates market segmentation and market analysis, would help suppliers in decision-making around market entry strategies and private sector partnership opportunities, and potentially increase scope for innovation and 'fast tracking' in financial services provision. Whilst not sustainable in the long-term, models such as the FMT model, work well in a market like Zambia, where public funding is used to finance well designed and credible market research and analysis that is available to all. Sector stakeholders, including private sector firms, are then at liberty to make use of data for policy-making, business development, or programmatic design. A potential role for existing or new rural finance programmes could be to finance market research or analysis to help fill identified market information gaps and to find market-led solutions, leading to new developments and innovations in rural and agricultural financing, including viable models for replication and scaling up. Principles underlying such research initiatives include the need for public forums (similar to those conducted by FMT), which position information as public goods. Another caveat is to ensure that information is packaged in such a way that it is easy to digest, and user friendly for decision-making by policy-makers, businesses, and sector development specialists.

4.3 Micro-level

At the micro-level, there are promising market developments in the supply of rural and agricultural finance when comparing the current status, even with three years ago. However, while the face of financial sector supply at large has changed rapidly over the past three years, scale and outreach with respect to the numbers of people served and the diversity of products and services remains strikingly low for agricultural and rural businesses and rural households.

4.3.1 Overview of the supply of rural and agricultural finance in Zambia

Loans and advances by commercial banks to the agricultural, forestry fisheries and hunting sector accounted for almost 18 percent of total loans and advances by commercial banks in 2011 at ZMK 2,124.40 billion[55]. This makes the sector the second largest recipient of commercial bank credit (after personal loans, which represent 29 percent of total commercial credit). Whilst there was strong expansion in credit to the agricultural sector, up 30.8 percent in 2011 compared to an 18.3 percent increase in 2010, the overall share of commercial credit to the agricultural sector has declined - 19.9 percent in 2009, 17.6 percent in 2010 and 17.7 percent in 2011[56]. The agricultural sector accounts for a relatively high percentage of total non-performing loans at 15.7 percent (agriculture, forestry, fishing and hunting combined) - on a par with construction at 15.8 percent, and ahead of personal loans at 15.1 percent.

It could be construed from the figures in the previous paragraph that the agricultural sector is attracting relatively large amounts of capital investment. However, reportedly there is a critical lack of supply and uneven distribution of credit. The Fintrac report[57] on legal and institutional reform in the agricultural sector refers to two distinct agricultural economies with 'vastly different constraints and opportunities'. The first economy is made up of small-scale farmers that are undercapitalized, technically weak, usually far from market channels and main transport routes, and making very limited use of appropriate equipment, irrigation, improved seeds and fertilizers. We know that these farmers represent at least 75 percent of Zambians involved in the agricultural sector, but they have limited or no access to finance. The second economy is made up of medium-sized and large commercial farmers that are capital intensive, and have relatively easier access to credit and other financial services.

In 2009, the ZNFU commissioned the USAID PROFIT programme to research into the challenges and opportunities in agricultural finance[58]. This study supports the premise that agricultural credit is insufficient and unevenly distributed on the basis of three factors, which are as relevant today as they were in 2009.

1. Credit flows are highly unevenly distributed across the sector, with the bulk of finance going to commercial level agriculture. Moreover, the percent and volume of agricultural credit reported by BOZ includes support to the forestry, fishing and hunting sub sectors. It also includes the broader range of secondary enterprises – agri-processors, commodity traders, milling houses, etc. The Fintrac report does not indicate figures for levels of credit or actual distribution across the main agricultural economies. In fact, there does not appear to be up-to-date data on the breakdown of credit for the farming sector. The ZNFU / PROFIT agricultural finance study appears to offer the best available breakdown using (consultant's own) estimates. According to the study, of the portfolio of approximately

[55] BOZ Annual Report, 2011.
[56] Idem.
[57] AgCLIR Zambia, Legal and Institutional Reform in Zambia's Agricultural Sector, Fintrac, February 2011, funded by USAID/Zambia.
[58] ZNFU / PROFIT, Zambia's Agricultural Finance Market: Challenges and Opportunities, December 2009.

US$463million in September 2009, including loans to all forms of agribusinesses (agro-processors, supplier companies, grain traders, etc.), the amount in the hands of primary producers is estimated at only around US$230million (less than 50 percent) and this is almost entirely with large-scale commercial producers.

2. Agricultural businesses, particularly those involved in the production of field crops, are generally intensive users of credit. The seasonality and cashflows associated with agricultural production mean that farmers are very reliant on credit; it is as critical an input as fertilizer, seeds or chemicals. They require substantial levels of credit relative to production output, and for relatively longer terms compared with, for example, businesses that operate on daily turnover of goods and services. Typically, a freehold commercial farmer's annual inputs will exceed the value of the farm's land and fixed improvements. Many Zambian commercial farmers rely 100 percent on bank financing to cover in-field production costs. Yet, according to the ZNFU / PROFIT study on agricultural finance, only half of all the loan finance that banks supplied in 2009 was used for primary production.

3. A third, broader factor to consider is that the levels of credit overall in Zambia are low compared to neighbouring countries. In 2011, credit to the private sector was 12.3 percent of GDP in Zambia compared with 17.8 percent in Tanzania, 24.3 percent in Botswana, and 19.8% in Malawi[59].

The picture for emergent and small-scale farmers is better now than it was in 2009. Two key players, CETZAM Financial Services Ltd and Zanaco Bank, have continued to pilot and refine suitable lending models for these sectors, with portfolios growing significantly over the past three to four years. At the end of 2011, CETZAM Financial services Ltd had reached over 2,600 small-scale farmers (with total disbursements of ZMK 8.2 billion, approximately US$1.5 million), the bulk of the loans having been disbursed in the previous 15 months. As of the 2011/2012 agricultural season, the Zanaco Bank and ZNFU Lima Credit Scheme was working with over 5,000 small-scale farmers through 25 District Farmers' Associations (DFAs), with a total credit exposure of ZMK 20 billion (up from just two DFAs and a portfolio of ZMK 600 million in 2008). Growth of Zanaco's emergent farmer portfolio has been slower. As of the 2011/2012 agricultural season, Zanaco had serviced 124 farmers, with a credit exposure of US$ 4,545,000.

The overall consensus is that agricultural business finance is expensive and difficult to obtain with the exception of the largest lead firms. In 2011, the annual average interest rate in real terms of commercial banks was 16.8 percent.[60] Table 2 below captures data on interest rates for NBFI in 2011. For medium sized firms, the most common formal loan product cited is the overdraft which is also considered difficult to come by and expensive. Box 2 in section 3.3 of the report gives an interesting summary of small-scale farmers' perceptions of agricultural credit.

[59] Source: World Bank data indicators, domestic credit to private sector (% of GDP), 2011
[60] BOZ Annual Report, 2011

Table 2: Non-bank financial institutions 2011 interest rate levels

Description	Second half 2011	First half 2011
Microfinance Institutions	131.5	138.1
Leasing Finance Institutions	69.5	88.1
Building Societies	24.7.	37.6
DBZ	29.6	29.6
NSCB	33.0	22.3
Overall for the sector	57.7	63.1

The BOZ has taken decisive steps to reduce the cost of borrowing. In November 2011, the Bank of Zambia reduced both the statutory and core liquid asset ratios by three percentage points to 5 percent and 6 percent respectively in an effort to ease the cost of credit to productive sectors. As this report underwent final review, the BOZ in a very controversial move, introduced a cap on the effective annual lending interest rates for NBFIs of 42 percent. BOZ will designate which NBFIs are required to comply with this measure. All remaining NBFIs are not to exceed 30 percent interest rate[61].

Another important contextual factor is that apart from large-scale commercial farming, rural household and agricultural business finances are inextricably intertwined, making it extremely difficult to verify how much formal credit flows into agricultural production. It is likely that some credit through both developmental and consumer lending MFIs that is intended for agricultural activities is diverted for household use, and vice versa.

Whilst there is still a great deal of work that can be done to bridge the financial inclusion gap, the commercial banking sector is as proactive as the microfinance sector, if not more so, in acquiring agricultural finance expertise for product and service development. There is a notable trend in the past two to three years of banks introducing agricultural finance departments, and bolstering local employee agricultural and banking expertise by reaching out for regional expertise to support product, systems and staff development. For example, FNB, Stanbic, Zanaco have well-established departments and strategic plans for increasing their respective agricultural finance portfolios (see section 4.3.3). Athough supply is still insufficient, the trend is moving in the right direction.

Whilst it is evident that agricultural leasing in Zambia through both banks and NBFIs is under-developed, there is a distinct absence of available data on the portfolio spreads of commercial banks and NBFIs, making it difficult to verify the size of the agricultural leasing sector. According to BOZ, there were a total of nine NBFI leasing companies registered with the central bank in 2011 (a drop from 12 in 2009). As of 2011, the leasing sub-sector as a whole had a total asset base of ZMK 250.9 billion – up from ZMK 174.2 billion in 2010 (a 44 percent increase). No data is available on what percent of this asset base represents agricultural financing. The ZNFU / PROFIT study done in 2009, provides consultant's own estimates of Zambia's agricultural leasing sector, estimating approximately US$ 34 million with the commercial banks and US$ 14 million on the books of

[61] BOZ Official Press Release, January 2013

NBFIs. Non-bank financial institutions (NBFIs), such as leasing companies, usually play a more important role in providing agricultural leasing finance for farming production and processing. This has not been the case in Zambia. However, there are number of partnerships involving commercial banks and market development programmes, which focus on opening up leasing finance for agricultural equipment for emergent farmers. These various initiatives are covered in section 4.3.3.

The total Zambian microfinance industry is still relatively small. There are a total of 26 MFIs licensed with the Bank of Zambia (BOZ). These MFIs include both developmental credit providers and payroll-based consumer lenders. Just five out of the 26 are deposit-taking developmental credit providers (microenterprise focused). According to BOZ data, across the five lead developmental MFIs - CETZAM Financial Services Ltd (CETZAM), VisionFund Zambia (VisionFund), Entrepreneurs Financial Centre (EFC), MicroBankers Trust (MBT) and Finca - the cumulative gross loan portfolio stood at US$7 million in 2009, with deposits at US$1.5 million. These five institutions were servicing 33,793 active borrowers, with an average loan balance of US$207. As at the end of June 2011, the total assets of licensed MFIs accounted for less than 37 percent of the total assets of non-bank financial institutions, and less than 2.2 percent of the assets of the total financial sector. Four of the five deposit-taking institutions are profitable, with the fifth, MicroBankers Trust (MBT), consistently making losses. According to AMIZ, most micro-lenders, including deposit-takers, are struggling to achieve 30-day Portfolios At Risk (PAR) of 5 percent or lower. Most MFIs operate in a range of between 5-10 percent, making profitability problematic.

Whilst CETZAM, VisionFund, EFC and MBT are relatively proactive in reaching out to rural and agricultural communities, the reality is that their footprint outside of main urban towns is very small. There is no credible information available on the size of the agricultural and rural portfolio across these four MFIs. None of Zambia's registered MFIs currently report to the MIX Market[62] and there have been no published results through DBZ on MFI performance since they received loans for rural and agricultural expansion under the bank's apex credit line facility. Another issue is that the MFIs classify rural as being anything between 10km-30km from a main urban centre and many of the MFIs are not able to segregate out rural and/or agricultural loans through their loan tracking software.

Of the five lead developmental MFIs in Zambia, all except one have been licensed by BOZ, and have made the transition to deposit-taking institutions over the past two years. Latest data from the Bank of Zambia records that deposits taken by these institutions, as at the end of March 2011, had grown to US$8.4 million. The bulk of this is mandatory saving which is tied to accessing credit facilities (and acting as collateral against loans) and it is not clear what portion, if any, is from agricultural and rural depositors. However, demand-side data point to the conclusion that very few adults in rural and agricultural sectors are proactively saving with MFIs.

There are also a considerable number of smaller unregulated credit-only institutions, as well as a

[62] CGAP Microfinance Information Exchange.

number of savings cooperatives. Data is not currently available regarding the number of such institutions or the size of either industry. What is known for Zambia is that there is a notable absence of informal, community-based savings and credit institutions at work. The culture of informal grassroots revolving savings and credit associations is not a traditional aspect of rural community life in Zambia, nor has the practice taken root with NGO support. Some analysts have pointed to a lack of cash and high incidence of deferred payments (i.e. borrowing and then paying later for goods and services) to explain the lack of informal savings and credit in rural communities. Lack of trust, low education levels (low financial literacy especially), and a lack of structured and sustained support to develop appropriate models for this country could be contributing factors. Ultimately, the reasons for the absence of Revolving Savings and Credit Associations (ROSCAs) and Village Savings and Loan Associations (VSLAs), and other similar models of community-based finance, are not clear and there is good justification for research to explore and identify preferences, levels of demand, and potential for scale with respect to future potential for community-based finance models in rural areas. The RFP's community-based finance component is one of very few structured and documented initiatives, which focuses on expanding savings and credit in rural areas (see section 4.1.1.3). A formal evaluation of this component should capture promoters' experiences in VSLA development – the challenges and lessons learnt - but also give valuable insight into users' preferences, what has worked and why, as well as contextual factors required for taking desired models to scale.

Savings and Credit Cooperatives (SACCOs) and Accumulated Savings and Credit Associations (ASCAs)[63] have received sporadic focus with respect to their potential role in the financial sector in recent years. According to the Ministry of Agriculture and Livestock (MAL), Department of Cooperatives, there were over 20,000 registered cooperatives as of December 2010[64]. The three main categories include multi-purpose, agricultural and savings and credit cooperatives. Table 3 shows the concentration of registered cooperatives by geographic location and for these three main categories, according to the Department of Cooperatives 2010 statistical report. With respect to SACCOS, there is very little current information to draw on regarding their distribution, scale and functionality in rural areas. Formal SACCOs can be registered and operate according to sector or industry, or according to main activities. There is a proliferation of urban-based SACCOs across the country linked with teachers, miners, and other key industries and professions. In rural areas, SACCOs have been formed around the main agricultural production sub-sectors (such as dairy, livestock, fishing and bee-keeping), marketing functions (such as the bulking and sale of soya beans or groundnuts) and agro-forestry activities. With respect to ASCAs, this study came across no current, reliable data on the number of ASCAs currently registered in Zambia, or on their functionality, performance, or support frameworks.

[63] ASCAs are often considered a stepping-stone toward the creation of a formal SACCO. As an ASCA group, members formulate constitutional elements, leadership and governance frameworks and practical day-to-day operations. These are usually aligned to SACCO requirements with the aim that the ASCA will transform into a formal SACCO.
[64] Ministry of Agriculture and Livestock, Department of Cooperatives, Cooperative Statistics in Zambia, 2010.

Table 3: Type and geographic distribution of registered cooperatives, Zambia, 2010

Type	Multi-Purpose	Agricultural	SACCOs
Total Registered	10,044	7,903	783
Geographic Concentration	Copperbelt, 2395 Eastern, 1173 Central, 1269 Southern, 1150	Southern, 2218 Copperbelt, 1747 Northern, 1136 Eastern, 761	Northern, 195 Eastern, 193 Southern, 133 Copperbelt, 119

Source: Department of Cooperatives, statistical report on cooperatives in Zambia, 2010

Under the Agricultural Support Programme (ASP), which ran from 2003 until 2007[65], efforts were made to support the growth and development of ASCAs. Reportedly some 550 groups with some 12,800 members were formed over a four-year period: these were a mix of ASCAs, investment groups and revolving savings and credit groups (ROSCAs)[66]. By the end of the ASP, some 45 percent of groups had portfolios in arrears, 40 percent had no savings books and 50 percent had no financial records. This poor track record points to fundamental weaknesses around a combination of factors such as approach, motivations, demand, contextualization, technical support capacities and viable exit strategies. However, despite such a false start there remains huge potential for community-led financial models in Zambia. Informal savings and credit groups are generally the entry point into financial services for most low-income people, especially in rural areas. There is also growing consensus that, whilst the likes of banks and MFIs grapple with the challenges of bringing sustainable access to formal services to such communities, with the right support structures, approaches and technical resources, community-based finance could play a vital role in offering rural Zambian populations access to productive credit and financial safety nets. Gathering and collating learning from previous initiatives such as the ASP and the current RFP will be critical for development and scale, and for positioning this financial sub-sector as a viable contribution to financial sector deepening.

As of today, the VSLAs conceived under the RFP need further technical support to strengthen and sustain group cohesion. At the same time, rural and agricultural ASCAs and SACCOs remain weak with respect to leadership, governance and financial management capacity. Many ASCAs and SACCOs lack direction and purpose and as a result are not playing a viable role in financial sector growth and outreach. The opportunity is unquestionably there for VSLAs, ASCAs and SACCOs to be a flourishing part of the agricultural and financial sectors, as providers of productive credit[67]. This, combined with access to technical know-how and markets - and as a first step, instilling a much needed savings culture - requires significant investment. There also remains a high risk of failure

[65] Under the Ministry of Agriculture and Cooperatives and funded by Swedish Sida, the Agricultural Support programme focused on increased food security and income generation for small-scale farmers by promoting the concept of 'farming as a business'. The programme ran from 2003-2005 with an extension through until 2007.

[66] ASP Process Document, Savings and Credit Cooperative Society (SACCOs) Development, Romboli, date of publication unknown.

[67] VSLAs and ASCA's, which distribute their accumulated savings and the interest earned on internal loans on a pro rata basis annually, are excellent vehicles for enabling members to build up the savings that they need to finance their own high risk annual outlays on agricultural inputs – a better option than seeking what are often expensive loans.

if models are supply rather than demand driven. The role and potential of community-based finance vehicles and the requirements for them to operate successfully (including the required skills sets and capacities of promoters) in Zambia do need to be thoroughly explored as do strategies for wide dissemination and organic growth of preferred models.

The success of the current RFP community-based finance component has helped raise the attention of policy and strategy decision-makers to the extent that the new GRZ / IFAD rural finance programme will have a scaled-up component dedicated to community finance development. At the same time, GRZ is also exploring options for the launch of community banks. Establishing an overall framework for community-based financial sector development is therefore a priority area in terms of further investigation and intervention strategies. Research in this area should include a review of how things have worked in other countries in the region. The current RFP has already shown how capable NGOs, with the right skills sets, can be an effective form of intervention support, and, though different contextually, lessons can be learnt, for example, from CARE International's groups in Malawi and SaveAct's experiences in South Africa.

In view of the timeline for the new GRZ / IFAD rural finance programme, there is good justification for informative research taking place prior to the planned 2014 programme start-up. In this respect, this may be an area that FMT or the new DFID Access to Finance programme can take up.

4.3.2 Market segments and key rural and agricultural finance suppliers

As described earlier, the bulk of finance flowing to the agricultural sector is targeting commercial level producers and agricultural processors. There is only a handful of financial service suppliers actively engaged in emergent and small-scale rural and agricultural finance in Zambia. Up-to-date and collated information on actual numbers served, and the value of portfolios for savings, credit and insurance at the emergent and small-scale farmer levels is not readily available, but it is known from existing demand-side data (e.g. the FinScope Survey, Zambia Business Survey, Agclir Zambia Report, and ZNFU/PROFIT Agricultural Finance Report) that outreach remains extremely shallow and there is a lack of appropriate products and services, particularly at the lower end of the market. The key rural and agricultural finance suppliers are summarized in Figure 16. In this context, the report is able to provide most detail on formal sector suppliers. More detailed profiles of the key emergent suppliers, including an overview of their products and services, is provided in Appendix One. An analysis of supply chain and value chain finance is included in Section 4.3.3 which explores current financial credit delivery models being applied in Zambia.

Figure 16: Rural and agricultural finance suppliers active in Zambia

Developmental Banks	Global and national level infrastructure, developmental financiers. ▫ Key players: World Bank, African Development Bank (ADB).
State-Owned/Parastatal Finance Institutions	Nationwide, accessible, government or part government owned. ▫ Key players: Development Bank of Zambia (DBZ), National Savings and Credit Bank (NSCB).
Formal Private Sector Finance Institutions	Commercial banks. ▫ Key players: First National Bank (FNB), Stanbic Bank, Zanaco, Standard Chartered Bank. Deposit-taking and developmental microfinance institutions. ▫ Key players: Cetzam Financial Services Ltd (CFSL), Entrepreneurs Financial Centre (EFC), VisionFund Zambia Ltd, MicroBankers Trust (MBT).
Formal Non-Bank Finance Institutions	Insurance companies. ▫ Key players: Diamond General Insurance Ltd, Madison General Insurance Ltd, NICO Insurance, Zambia State Insurance Corporation Ltd. Leasing companies. ▫ Key players: Afgri Leasing Services Ltd. Non-banking microfinance service providers. ▫ Key players: Empowerment MFI, Microcredit Foundation.
Social, Semi-Formal and Informal Financing Entities	SACCOs. ▫ Key promoters: Zambia Cooperative Federation (ZCF). ASCAs and VSLAs. ▫ Key promoters: Plan International, MBT, REES, Keepers Foundation, Africare. Supply Chain and Value Chain Businesses. ▫ Key players: large-and small-scale agri-input suppliers, agri-processors, traders.

4.3.3 Financial credit delivery models

Whilst Figure 16 above highlights the key rural and agricultural finance suppliers operating across the financial sector, the contents of this next section describes emergent credit delivery models currently being used to facilitate access to finance in rural areas.

1. Apex Credit Line through DBZ

With the support of IFAD and the RFP, DBZ received a tranche of funding for apex lending to the microfinance sector. The total available fund was US$4 million. Four out of the five lead developmental MFIs (namely CETZAM Financial Services Ltd (CETZAM), VisionFund Zambia, Entrepreneurs Financial Centre (EFC), and MicroBankers Trust (MBT)) received soft loans between late 2010 and the first half of 2011 of up to US$1 million each. The MFIs were chosen because they were already licensed or were close to receiving a license for deposit-taking and because they demonstrated commitment to transforming to deposit-taking institutions and to expanding their rural and agricultural lending operations. Aside from regular reporting to the BOZ, the four MFIs are required to send DBZ regular financial statements. DBZ monitors the apex loan repayments. However, there has been little in the way of performance monitoring or of tracking target-effectiveness by DBZ and it is not clear what the impact has been on overall outreach as a result of the soft loans. Box 2 below provides more detail on CETZAM's use of the DBZ credit facility. Whilst the MFI was able to disburse the total loan fund, progress was slower than anticipated. On the other hand, CETZAM has been able to report an extremely good repayment rate of above 97 percent overall.

Box 2: CETZAM use of DBZ credit line to expand lending to small-scale farmers

In early 2011, CETZAM received a loan from DBZ of US$1million. The loan was used to refine and replicate the MFI's existing small-scale farmer group lending model, which provides small-scale vegetable farmers with access to micro irrigation and agricultural input loans. CETZAM works with selected agricultural input suppliers (and NGO partners such as iDE Zambia) to provide irrigation and recurrent inputs on credit to groups of farmers. CETZAM has continued to replicate the model since the original pilot in 2009 and is now offering agricultural credit in partnership with iDE Zambia in Kafue, Mumbwa, Kalomo, Choma, Mazabuka, Kabwe and Kapiri. CETZAM has also recently expanded the model into the dairy sector. In June 2012, CETZAM had approximately 2200 clients (in groups), with loan sizes ranging from ZMK 1.5million (US$ 300) to ZMK 2.5 million (US$ 500). However, portfolio growth has been slower than expected. Reasons for this include limited human resource capacity within the MFI to assess and manage agricultural credit, a lack of creditworthy farmers, lack of sound market information on potential growth areas, and stretched institutional resources. At the same time as developing its agricultural lending, the MFI was transitioning to a deposit-taking institution. As of mid-2012, CETZAM had not yet launched deposit-taking for small-scale farmers though it collects and uses mandatory savings as group collateral against loans.

2. Down-streaming by commercial retail banks

There is an emerging group of commercial banks (see Figure 16 above and emergent supplier profiles contained in Appendix One) that are assuming a role as rural enterprise development bankers and financers and, as such, are achieving success in developing products and services directly targeted at lead firm agri-processors, emergent and small-scale farmers. Whilst some are relatively new market entrants, there are several key players that have been operating in the sector for five years or more. Aware of the key role agriculture plays in Zambia's economy, these banks continually monitor and manage exposure according to sector performance and risk appetite. Examples of current partnerships and product delivery models are highlighted below.

Zanaco Bank emergent farmer finance and small-scale farmer finance models

In 2007 the Rabobank group bought a 49% share in Zanaco Bank. Since then divisions of Rabobank such as Rabo Development and Rabobank Foundation have been supporting Zanaco Bank to develop and extend credit and technical support facilities to emergent and small-scale farmers (See Box 3 below). The emergent farmer model focuses on medium sized producers whose farms are currently too small to earn structured business income by, for example, investing in farming equipment or securing buyer contracts. Historically, limited access to finance has prevented these farmers from increasing productivity and improving farm performance and efficiency. Zanaco Bank provides finance, linked with technical support and based on stringent business principles, to farmers who have been unable to access appropriate finance and support services. The bank focuses on farmers who possess proven entrepreneurial skills, positive track records, minimum farm sizes and assets, aiming to transform these farms into larger, independent commercial farms, and ultimately to grow the commercial farming sector in the country. The credit facility is linked with technical support from input suppliers servicing the value chain to address challenges in respect of the quality and consistency of produce, which are critical for emergent farmers wanting to enter into buyer contracts.

Box 3: Zanaco Bank's Lima model

- District Farmers' Associations (DFA) made up of Zambia National Farmer Union (ZNFU) members borrow from Zanaco (up to 50 in a group).
- Based on pre-defined criteria, ZNFU selects the groups Zanaco should target.
- The DFAs aggregate the loan needed and screen eligible farmers.
- 50 percent upfront deposit is raised by the DFAs (farmers), plus personal guarantees.
- Zanaco pays the input supplier and the input supplier provides inputs to the DFAs.
- The input loans are timed for on-time planting (Oct-Nov).
- The DFAs (farmers) harvest and sell their maize to the Food Reserve Agency (FRA) (Jun– Sept).
- Revenues from the sale of maize are used to pay back the input loan; the upfront deposit of 50 percent sitting with the bank is drawn down to make up the balance due to Zanaco Bank.
- Support in organizing the marketing and sale of the crop maize[68] is provided by the local ZNFU Representative and District Level Officer.
- Interest rate is 20 percent flat rate.
- The average loan size is approximately US$600.
- Outreach to over 5,000 active clients by 2012.

3. Outgrower Schemes

Characteristically, outgrower schemes in Zambia have focused around key commodities for export (e.g. cotton, sugar cane, tobacco, and, on a smaller scale, coffee, paprika, groundnuts, and soyabeans). With perhaps small variations, the main form of outgrower schemes is contract-farming arrangements between large commercial agricultural firms and small-scale farmers. Written or verbal agreements enable small-scale farmers to access inputs on credit, which is then paid back to the commercial firm when the farmer sells his production yield to that buyer at an agreed price (often a pre-set price). The credit facility (in cash or in-kind) is normally linked with a degree of control over the production process.

This study was unable to find current data on the actual number of outgrower schemes across the various sub-sectors. However, table 5 below presents estimates for the number of small-scale farmers involved in outgrower schemes, and the main sub-sectors in which schemes are operated as of 2010.

The key features around Zambia's most promising outgrower schemes are: transparent pricing on the part of lead firm buyers, adherence to pre-agreed prices and sales terms, finance combined with technical production support and, in some cases, farm operation support[69]. Input credits are 'packaged' and based on smallholder production levels. The cost of credit is embedded in the input and deducted when the farmer sells his produce to the lead firm. These relatively sophisticated mechanisms for financing are also being taken up by the commercial farming, trading and processing sectors. Some schemes began as donor-funded pilot initiatives (as was the

[68] To-date the model has focused on maize production. However, plans are to extend the loan facility to other cash crops

[69] USAID/PROFIT: Presentation 'Exploring Supply Chain Finance in Zambia', August 2010

case in the cotton and dairy sub-sectors). However, several outgrower schemes are operating at scale and have attracted the attention of commercial banks. Though still in their early stages, partnerships are emerging whereby the banks provide financing to agri-processors in targeted sub-sectors. The bank uses these lead firms as aggregators for extending input credit to small-scale farmers. Unfortunately, the risk of side-selling (selling to a buyer that did not provide inputs and is outside of the contractual agreement made) remains a challenge across all sub-sectors, except sugar cane where there are rigorous controls on output selling.

Table 4: Number of small-scale farmers engaged in formal outgrower scheme, Zambia (2010)[70]

Sub-sector	Scale – Number / % of SMEs	Average loan size
Cotton	150,000 / 77 percent	< US$50
Tobacco	40,000 / 20 percent	> US$200
Other	5,000 / 3 percent	Unknown

Key to each of these successes is that the financial product and service has been launched in collaboration with one or more partners, including NGOs, the farmers' union, farmers' associations, and private sector enterprises, that collectively support by developing intervention models for testing in the market. Facilitating partners bring together private sector players, propose approaches and incentives for buying down the risk of the financing partners' market entry. However, in all cases gaps exist around deeper knowledge and understanding of the potential market for existing products and services, as well as new products and services.

Outgrower / Production loans in the tobacco sub-sector

The Tobacco Association of Zambia (TAZ) has in the region of 2200 members[71], 2100 of which are small-scale farmers and the remainder large-scale commercial farmers. TAZ's mandate is to provide advocacy, technical assistance and credit to its membership. However, by far the biggest credit providers in the tobacco sub-sector are the buyers themselves with as much as 60 percent of small-scale production credit flowing through them. Lead buyers include Chinese, Japanese, British and German lead firms. Loans are based around an outgrower contractual arrangement, and are a combination of input supply credit and cash for labour and other production costs. Loans are liquidated when the farmers sells his crop to the buyer. TAZ acts as an intermediary, using a ticketing system to record sales volumes, issuing statements of sales and calculating monies owed.

[70] Source: USAID/PROFIT: Presentation 'Exploring Supply Chain Finance in Zambia', August 2010.
[71] Interview with Mr. K. Mbazima, TAZ General Manager, June 2012.

TAZ itself offers very limited credit to its members. During the 2011 - 2012 production season, around 60 members received credit directly from TAZ. A network of councils provides field-based support in the major tobacco growing areas. Special interest counselors (SIs) have been appointed in three key areas to oversee small-scale production (Choma, Kaoma and Kabwe). In the case of TAZ, production loans for inputs, labour and firewood are disbursed through the SIs with a 12.5 percent flat interest rate. The SIs monitor loan repayments, production and selling processes. Repayment performance is mixed. TAZ's recovery rate was about 80 percent in 2011, though expectations are for a much higher recovery rate in the 2011 - 2012 production season. There are instances of TAZ carrying over loans from one season to the next when the season is bad and production yields fall away.

Lead tobacco buyers provide short-term seasonal credit only. Repayment rates are generally good as the credit for input costs is deducted at the time of sale. Credit for fixed assets or equipment is provided on a very selective basis. The banks are not prevalent players in the tobacco sub-sector. They are wary of how buyers' contracts are issued, and of the lack of collateral small-scale producers can offer. A second gap in financing is lack of appropriate capital for upgrading or expanding tobacco curing systems. The lack of investment capital makes it difficult for small-scale farmers to expand production.

Another challenge is the lack of capital for re-forestation. Harvesting and using local wood in the curing process is an increasing environmental concern. Zambian buyers are just beginning to address planned planting and re-forestation. GIZ (formerly GTZ) was behind a project two years ago that focused on upgrading small-scale tobacco production through the introduction of technologies and training, but the programme appears to have had little overall impact in upgrading the sub-sector.

Outgrower / Production loans in the cotton sub-sector

The cotton sub-sector, where the majority of outgrowers are engaged, has had schemes in place for several years. According to the Cotton Association of Zambia (CAZ)[72], there are over 450,000 small-scale cotton producers in Zambia (168,000 of which are members of CAZ). The main form of financing of these producers is through formal outgrower contract schemes. All nine of Zambia's main ginneries offer similar type schemes, but Dunavant, Zambia's largest cotton ginning company, is the largest provider of credit and is estimated to serve between 150,000 and 200,000 small-scale cotton growers. Dunavant provides farmers with 'packaged' input supply credits in accordance with production levels and capacities (i.e. starter, intermediary and top level packs). Dunavant supplies the credits through distributors to farmers. Farmers receiving credits are contracted to sell to Dunavant and loans are paid off when farmers come to sell their cotton.

Dunavant has extended its support to various business development 'add-ons' for willing small-scale farmers. There are examples of farmers becoming suppliers of cotton inputs on credit

[72] (CAZ) is an affiliate of the Zambia National Farmers' Union) ZNFU and operates within the established structures of the Union through District Farmers Associations (DFAs) and information centres (ICs) in all of the key cotton producing areas of the eastern, central and southern provinces of Zambia. CAZ's mandate is to serve the interests of the cotton farmers and to provide a platform for effectively addressing sub-sector challenges.

(receiving a sales commission from Dunavant), with other crop inputs also being increasingly supplied through the same channels. Other business development initiatives include farmers' being encouraged to recruit other farmers and a financial leasing scheme being offered in partnership with Afgri Leasing Services Ltd. Farmers are using the facility to purchase tractors, which they then hire out to other farmers locally. Initially supported by USAID / PROFIT, the leasing facility has achieved notable success in improving small-scale farmers' production capacity and in supporting the growth of emergent farmers in the cotton sub-sector.

4. Supply chain and value chain finance

The scarcity of domestic credit in Zambia, which is the equivalent of 19 percent of GDP, compared to 51.8 percent in Namibia and 166.9 percent in South Africa[73], means that the large processing, manufacturing and exporting businesses that are the main users of agricultural commodities need their own liquidity to provide input supplier and/or buyer credit. Currently of the more than 900,000 SMEs (24 percent) that either provide or access credit from input suppliers or buyers, the majority (58 percent) are in the agricultural sector[74].

Though innovative, 'structured' models in agricultural supply chain financing are beginning to appear in Zambia, these are restricted to a few key sub-sectors (e.g. cotton, tobacco, dairy, horticulture, groundnuts and honey, the last three of which are still on a very small-scale). In all cases, there has been intensive business development and market linkage support to get marketing systems and business partnerships to the levels that they are at today.

Characteristically, informal supply chain and value chain finance between suppliers, farmers and buyers is short-term and cannot readily be used to invest in the capital assets needed to grow a business. Providing credit actually ties up cash. Small-scale input suppliers complain that, if they give products on credit, they then lack money to be able to re-stock when needed. For many farmers, their cashflows are simply not sufficient to extend credit to buyers. The farmer needs cash for sales so he can use it to re-plant, buy chemicals or for household use.

The USAID/PROFIT study on supply chain finance also revealed that finance is often flowing the 'wrong way'. Smaller firms, which often cannot afford to, are providing product on credit to large-scale buyers because the large-scale buyer demands it. Competition is high, and if the small-scale supplier refuses, the large-scale buyer will go elsewhere. In Zambia, most supply chain financiers offer credit reluctantly or because they have no choice. Zambia's poor credit repayment culture also affects the willingness to lend even for relatively short terms. Clients are slow to repay and in some cases do not repay at all, and this includes some of the largest commercial firms.

[73] www.data.worldbank.org, 2011.
[74] Source: USAID/PROFIT Presentation 'Exploring Supply Chain Finance in Zambia', August 2010.

There is also an active informal agricultural input finance market, which operates through local lead farmers, traders and shopkeepers. However, while the risks of side-selling and default on such lines of credit are relatively low, the cost of finance can be extremely high[75].

5. Warehouse receipting systems

Several leading commercial banks are working with farmers, traders and millers in extending inventory and commodity trade financing against warehouse receipts and certificates. Nevertheless, warehouse receipting systems are still only serving a small percentage of the market. With the right oversight and management, and continued efforts to strengthen infrastructure and smallholder usage, warehouse receipting can play an increased part in Zambia's rural and agricultural market development.

Increased usage and benefits depend on several factors, including the need for behavior change on the part of small-scale farmers and cessation of government interference in commodity markets. The banks cite a lack of physically adequate and secure warehouse storage facilities as a constraint on scaling up warehouse receipting finance mechanisms. The storage industry as a whole is still fragmented and weak. Moreover, government has yet to establish a regulatory framework for warehouse receipting and commodity trading (which includes amendments to the Agricultural Credit Act, Marketing Act, and Commodities Exchange Act).

7. Leasing finance

Early and adequate land preparation hinders productivity and farm efficiency at the small-scale farmer level. In terms of a USAID/PROFIT initiative, attempts were made to develop a business platform whereby tractor owners contract out their services for land preparation. At the time, a major issue was the shortage of available tractors at the small-scale farming level as well as a shortage of appropriate credit with which to buy tractors for use by contractors. Farmers have been unable to access finance due to perceptions of risk, the lack of adequate collateral and in many cases weak financial literacy and weak farm management capacity. On the supply-side, there was also a lack of appropriate financial suppliers and leasing products.

Musika has picked up where USAID/PROFIT left off, and is playing a facilitating role in refining a business and finance model for small-scale farmer mechanization focused on increasing access to tractors and ripping technologies at the lower end of the market. Several pilot initiatives involving leading machinery supply firms, leasing firms, commercial banks, emergent and small-scale farmers are currently being implemented. An important aspect of the business model is the emphasis on farmers as contractors. Income revenue streams from the contracting out of the tractor or ripper are important for paying off the lease, and for supporting the business expansion of the contractor / farmer. Therefore, the business management capacities of the contractor / farmer are a critical contextual factor. In at least one pilot, risk reduction mechanisms includes a partial credit guarantee, which is being put up by the facilitating NGO partner to incentivize the

[75] Source: USAID/PROFIT, Value Chain Finance in Zambia: Supply Chain Solutions to Financial Constraints, Cardno EM USA Ltd, March 2010.

leasing company to enter into lease agreements with farmers. A strong technical support component is also included to help the contractor / farmer to develop their business models. Achievements in the past two years (2010-2012) include:

- over 30 tractor units purchased and leased out by Dunavant Cotton. Musika supports this initiative by identifying equipment suppliers willing and able to provide solid after sales service. The model also provides training and mentoring for lessees to support them in developing and implementing their contractor service business model. At least two commercial banks have shown an interest in purchasing Dunavant's lease portfolio.
- Afgri Leasing Services Ltd has leased out 26 tractors to emergent farmers/contractors with Musika support. These farmers are, on average, working with 10 – 28 hectares of land. With respect to scope, there is no particular geographic focus, and the tractors and tillers are being used for various types of crop production.
- The UN Food and Agricultural Organisation (FAO), ZNFU and the Ministry of Agriculture and Livestock leased out 10 tractors during 2011. In this case, subsidies to the lessees for land preparation mean that the model is not fully commercial, which makes it difficult to evaluate its long term sustainability.

However, there are key market information gaps that need to be addressed to verify overall market potential and scalability of lease financing models in the small-scale and emergent farmer sectors. For example, the market for the purchase or lease of tractors and rippers across the small-scale and emergent farmer sector is unknown, as is the level of demand for contractor services using locally hired tractors or rippers. The banks offering leasing agreements, or the leasing companies themselves, need to do more in-depth market research into the overall market potential for such products. They also need to understand what, if any, market incentives or market stimulants would be appropriate and effective for engaging more equipment suppliers and/or leasing companies on the supply-side, and for attracting increased numbers of small-scale and emergent farmers on the demand-side. Depending on the view of FSDP and sector support partners such as FMT and DFID, it may be feasible for partners to support a research study that provides market information on the potential of the small-scale and emergent farmer leasing finance, which is made available to the industry.

At least one known, important, disincentive to small-scale and emergent farmers with respect to lease financing is the current laws regarding the application of VAT on lease purchases. In 2007, the tax coding applied to financial leasing was changed, which meant that finance lease payments went from being tax deductible to being almost entirely non-deductible - all but the finance charge element is considered tax deductible under the new tax coding[76]. Since the change, the value of the leasing finance sector (banks and NBFIs combined) has shrunk by some 60 percent.

4.3.4 Savings

Several leading banks have introduced savings products specifically targeted at the lower income bracket and youth, but, at present, these products are reaching urban populations only. They are

[76] Fintrac, AgCLIR: ZAMBIA, Legal and Institutional Reform in Zambia's Agricultural Sector, Michigan State University, 2011

not being marketed to rural populations and, as highlighted in the demand side analysis, users and non-users consider formal bank savings products expensive and not good value for money. Accessibility is also a key factor because, while banks are increasingly engaging customers through online and mobile transaction technologies, many account options require customers to visit branches, which is an additional cost and time factor for rural consumers. To date, banks have not seriously turned their attention to securing rural and agricultural communities as customers and this is reflected in their current product offerings.

For suppliers, there are also major cost implications in servicing large numbers of accounts with relatively small balances. Using standard models, this is not profitable for banks. Traditionally, MFIs have required savings as a precondition for accessing credit, a mandatory condition for urban and rural borrowers. For some two years now, four of the five leading developmental MFIs have been fully registered for deposit-taking, but this has not resulted in much growth of outreach into rural areas, as they have still to integrate deposit-taking fully into their systems. It requires time to do this successfully and there appears to be little or no external support from the Bank of Zambia or from existing financial development programmes to achieve this.

Savings mobilization under RFP has focused on community-based financial service development through three main intervention areas. These are explored in more detail below.

1. Support for informal, social group savings development through grant-funded NGOs that promoted the introduction and strengthening of village savings and credit associations (VSLAs). Under the RFP programme, a cadre of local NGOs, including Africare, Rural Economic Expansion Services Ltd (REES), Keepers Foundation Zambia and one MFI (MBT) have been supportive in mobilizing and establishing VSLAs. The specific model (based on Care International's highly successful VSL model) is new to Zambia and reportedly has had promising results. This is notable as there are very few examples of community-based savings and credit working well in Zambia. To date, the initiative has helped mobilize and train 12, 689 members, 8983 of which are women.

   Earlier, in Section 4.3.1 the report explored the landscape of community-led informal savings and credit with respect to the current RFP, past endeavors, and emerging lessons learned. However, there are other initiatives and sources of learning, which policy and decision-makers can tap into in reviewing progress-to-date, and in consolidating future strategies for community-led savings and credit. Two of these initiatives are highlighted below.

   Firstly, aside from RFP-supported VSLA development, Plan International, since 2009, has been working on mobilizing and strengthening VSLAs under the 'Banking for Change' programme partnership[77]. In Zambia, in its first two years, the programme, which is particularly targeted

[77] Launched in 2009, in partnership with Barclays Bank, CARE International UK and Plan UK, the programme comprised a three-year, GBP 10 million commitment to support financial inclusion through the development of savings-led community finance; the programme has provided basic financial services to over 513,000 people, supporting 25,000 groups across 11 countries in the period 2009-2012. Most of the 11 country programmes run until October 2012. See www.plan-international.org, and the following link: www. group.barclays.com/about-barclays/citizenship/our-programmes/community-programmes/banking-on-change.

at women, established more than 1,000 VSLAs, with over 9,000 individuals in Chibombo and Mazabuka districts. Though not specific to Zambia, the 'Banking for Change' programme has produced a comprehensive report on the challenges and barriers to financial inclusion, as well as the opportunities for systemic change at national and international levels.

Secondly, in late 2012, the RFP VSLA promoters as well as other NGOs with expertise in community-led banking, took the initiative to form a network. Members of the network include World Vision, Catholic Relief Services (CRS), Churches Health Association of Zambia (CHAZ), Plan International, Africare, and others. The set-up of the network is in its very early stage, and its members have yet to formulate intentions and strategies, though they are in the process of doing so. As this report was being finalized, CRS had agreed to house the network, and provide technical support to its members. The set-up of the network offers opportunities for consolidating learning from the field, and for addressing research and development issues around the contextual factors for success and sustainability of community-led savings and credit groups such as understanding and addressing the needs of support providers, understanding the interests and motivations of target groups, and formulating intervention rationale, strategies, and implementation approaches based on target group interests and motivations.

The RFP engaged in partnership with the National Savings and Credit Bank (NSCB) in an attempt to expand the bank's footprint in rural areas. Box 4 below captures the inherent challenges, and the achievements, that came out of the initiative, and highlights unanswered questions regarding overall scope for profitability in rural areas.

Box 4: The National Savings and Credit Bank's capacity to contribute to increasing financial inclusion in rural areas

Under the RFP programme, the National Savings and Credit Bank (NSCB) received support to set up branches in two particularly remote areas with no previous access to financial services. Lukulu branch was opened in 2009 and broke even within nine months. The second branch on Chilubi Island opened in September 2011 and is already financially sustainable. However, this story of success is in contrast to the inherent challenges with respect to the bank's overall institutional role and capacity. Referring to NSCB, the recently formulated rural finance policy pointed to the importance of more appropriate governance, management and operational structures to be introduced throughout the institution. Support to NSCB through the RFP support has included significant investment for new management information software, together with IT technical expertise, management capacity building and product development support. However, these interventions appear not to have resulted in marked institutional strengthening. NSCB outreach is still relatively limited (currently only 27 branches, located in rural and urban areas). Decisions around further investment in the institution would need to be preceded by a candid appraisal of stakeholders' commitment to a re-engineering process that includes changes to ownership, governance, operations, and product and services, as these appear to be prerequisites for NSCB to be able to establish itself as a key player in the rural and agricultural financial sector. In addition, however, decision-makers must also have understanding of why it is that two deep rural branches opened under RFP were able to become profitable in such a short time, and whether or not it is possible to replicate these successes, and what would it take to do so. It will be important, either under the current RFP, or in the framework of future support, to ensure these questions are asked and that answers provide guidance for the future of the bank.

2. Over the past two years the RFP has provided grant funding to eleven community-based projects to support the upgrading of community-based small-scale production, which is also linked with establishing revolving savings and credit associations (RoSCAs) within the producer groups. RFP's small-scale producer support focused on different sub-sectors, including honey and rice. Small grants were channelled through one MFI and several NGO partners[78] that provide training and technical support to the producer groups to introduce improved business and market linkage models, and to develop management capacity in the ROSCAs. The projects are all rural based, with NGO partners working in Northern, Eastern and Western and North Western Provinces. Box 5 describes Keepers Foundation Zambia's work with a small group of honey producers in North Western Province.

Box 5: Strengthening community-based honey production

With support from Keepers Foundation Zambia, a group of small-scale farmers involved in bee keeping and honey production in Kasempa District in North Western Province have introduced a consolidated storage and marketing business model and set up their own revolving savings and credit association. Traditionally, the farmers' approach has been to produce small quantities of honey and sell individually on an ad hoc basis. With funding from RFP, the group received training and technical support through Keepers Zambia to introduce a new business model as well as a small grant to purchase a storage container for the honey. The project has supported 123 honey producer groups with over 1,230 members (609 female). Reports indicate over 100% increase in sales value since introducing the consolidated marketing model.

78 Keepers Foundation Zambia, Rural Economic Expansion Services (REES), Africare, MBT.

4.3.5 Insurance

As highlighted in the demand section, there is limited understanding in low-income communities of insurance products and very limited voluntary uptake of insurance. However, on the part of suppliers, there is very little in the way of marketing outreach or, for that matter, appropriate products and service offerings for low-income communities.

To catalyse the development of a pro-poor insurance market, a microinsurance development strategy was formulated in 2010 by a multi-stakeholder technical advisory group and is in the process of being implemented, with financial and technical support from FMT and the International Labour Organisation (ILO). The overall goal of the strategy is to stimulate and accelerate the provision of microinsurance products and services in the country. The strategy outlines various demand stimulation and supply-side strengthening interventions, which have been implemented over the past three years with the objective of improving access to insurance for low-income people.

Through this process, insurers have received market information, capacity building training and exposure to microinsurance innovations as well as access to grants to pilot product development and service delivery. As a result, insurers are starting to develop insurance products tailored specifically to meet the needs of low-income consumers. Developments include the launch of three new life insurance products in 2012. For example, Bantubonse Life Plan, a product of Professional Life Assurance Limited, is a simple and affordable life plan with a minimum once off annual premium of ZMK 30,000 for a sum assured of ZMK 1,000,000. Life-after-Life is the first insurance product ever to be offered in Zambia using a mobile phone platform. African Life Assurance Zambia (ALAZ) has partnered with MTN Zambia (MTN) to enable MTN customers to buy affordable and convenient life cover for as little as ZMK 1500 per month for a payout of ZMK 1,000,000. Product simplicity and innovative delivery mechanisms characterize the new offerings and cross-sector partnerships are emerging as a means for improved accessibility and enhanced affordability.

In terms of the rural penetration of microinsurance products, not much has been achieved as yet, although there are attempts by life assurers to partner with agribusinesses and rural based aggregators. For example, in partnership with Musika and Dunavant, Professional Life Assurance is selling its Bantubonse life cover through rural agent networks. ZSIC Life is also using rural based community agents to sell its new microinsurance product, Munditule life plan in Southern province. At the same time, some non-life insurers (such as NICO Insurance, Madison General Insurance and Diamond General Insurance) are interested in looking into livestock, weather index and other products applicable to rural communities. However, these are complex products requiring further feasibility and viability assessments. In the case of weather index insurance, gaps in historical data on weather patterns also pose challenges for product development and roll-out.

4.3.6 Branchless banking and payment systems

There has been impressive organic growth in the range of branchless banking and payment system partnerships and market testing in Zambia in recent years. For example, Zoona (formerly Mobile Transactions Zambia Ltd), a leading electronic financial transactions provider, which started out as a pilot initiative linked to Dunavant in the cotton sub-sector, has launched various innovative financing models, and is supporting initiatives specifically focused on rural and agricultural financial inclusion. Aside from its in-country money transfer product and service, Zoona is currently involved in providing:

- electronic MFI loan disbursements and repayments with VisionFund Zambia; now nationwide for loan disbursements, the partners have still to commence piloting repayments; start-up challenges that need to be addressed in order to achieve scale include lack of financial education and lack of confidence in using the model, on the part of consumers, and lack of liquidity at agent disbursement points;
- a 'pre-paid debit card' through which small-scale cotton farmers are receiving part payment from the leading cotton buyer, Dunavant; the model covers six districts, with potential outreach to about 50,000 smallholder farmers, but according to Zoona the service has not been gaining traction over the past two years;
- a pre-paid voucher card redeemable for seeds and inputs with MRI Seed Zambia, which attracts up to a 9 percent discount if small-scale farmers 'pay' into the card upfront; the service currently covers three districts, with about 15,000 sales to smallholder farmers to-date;
- mobile phone-based purchasing services, through which buyers can order and purchase from lists of suppliers and goods and pay by mobile phone; the service, which began in 2011, is just beginning to look at potential application in the agricultural sector; more work is required to market the service, as, according to Zoona, sales volumes to date through retailers currently using the system (which includes Zambia Breweries) are low;
- a farmer input support programme (FISP): the programme is envisaged to provide small-scale farmers with agricultural input vouchers redeemable at selected suppliers; the service is being explored by the Ministry of Agriculture, FAO and CFU as an alternative approach to the current government-subsidized fertilizer scheme; the plan is understood to be for 40,000 such vouchers to be distributed over 30 districts; the programme got off to a slow start due to problems with the design of the management information system and poor field coordination, as well as a lack of fertilizer distribution warehouses;
- Kiva loans through branchless agents: piggy-backing on the Kiva model[79], MTZ is working with Kiva to facilitate electronic disbursement of Kiva loans through 'champion agents' and selected retail outlets;

[79] Kiva is non-profit organization, which facilitates access to credit via the internet. Would be lenders can browse the Kiva website to select and lend to a micro entrepreneur of their choice. Kiva works closely with select field partners (including microfinance institutions, social businesses, schools and non-profit organisations) to manage a system that supports the aggregation and flow through of lenders' funds to field partners, who use the money to replenish the loan made to the entrepreneur. Loans are managed by field partners, which are also

- Partnership with the World Food Programme (WFP) Zambia to implement a mobile delivery and tracking system that delivered and tracked 275,000 e-vouchers to beneficiaries across five districts as part of the Sustainable Programme for Livelihoods and Solutions for Hunger (SPLASH), which operated from 2009 to 2011.

Other firms that are leading in electronic payment systems include: Celpay Zambia, which is a major provider of domestic remittances and provides a variety of mobile transaction services. It received a grant under the RFP outreach and innovation programme to invest in software and to broaden its points of sale (POS) network in order to expand its payment system services into rural areas with the aim of providing affordable electronic money transfer services for all districts. After initial problems with software, the system is now reportedly fully operational with agents operating in almost all districts. As a next step, the RFP is supporting Celpay to establish a mobile phone based savings service. Design work for the service and staff training has taken place during 2012 with expected launch in the last year of the RFP. Zanaco's 'XAPIT' mobile banking service, which is linked to a Zanaco bank account, offers traditional card services, such as access to ATMs, as well as a range of mobile phone based banking services, including payment of utility bills and subscriptions, mobile phone top-up, and money transfers. The Credit Union and Savings Association of Zambia (CUSA) signed a partnership with Calltrol Zambia[80] in 2011 to establish ATMs and POS terminals for all its members. The management information system will allow members remote access to savings and transfer services. Initial plans were to work with a pilot number of credit unions and cooperatives, before eventual scale-up.

4.3.7 The role of social protection grants for most vulnerable households

67 percent of rural Zambian households live in conditions of extreme poverty[81]. Prevailing challenges of HIV and AIDS, unemployment and recurrent drought exacerbate vulnerability at this level. Moreover, households at this level cannot lift themselves out of destitution. Without appropriate support, livelihood failure is likely to worsen for this sector of the population. Historically, social protection has not figured highly in the priorities and budget of the government. In addition, uncertainties related to the impact and cost effectiveness of cash transfer programmes have slowed efforts to scale up from earlier pilots and model testing. In 2009, however, the Ministry of Community Development, Mother and Child Health (MCDMCH) decided to roll out a national social cash transfer scheme that would attain national cover by 2015. The decision to move forward on a national scheme comes as a result of a series of pilots that took place between 2004 and 2010 and growing acceptance that social cash transfers can play a valuable role in assisting extremely poor households.

Whilst, social protection grants cannot be positioned as a financial inclusion driver, there is some evidence that these grants are helping to lift people out of poverty. The social grant programmes

responsible for loan performance and collecting repayments. When loans are re-paid, lenders have the option to re-lend, donate to Kiva or to reclaim their loan via paypal.

[80] Calltrol Zambia is a BOZ accredited and licensed independent switch operator, which specializes in developing infrastructure for electronic payment solutions.

[81] Source: UNDP Human Development Report, Zambia 2011.

piloted over a number of years in Zambia have proven effective in building basic household resilience in numerous respects, including: increasing food consumption and improving the range of food consumed, increasing ownership of small-scale farm assets such as goats and chickens and increasing levels of self-esteem and confidence.

Pilots to-date have captured urban and rural / agricultural populations. Community welfare assistance committees oversee outreach and targeting. Key challenges encountered in implementing manageable schemes include low literacy levels, which negatively affect means testing. Complex, weak, and in some instances corrupt, selection and approval processes, as well as weaknesses in institutional and organizational capacities, have also slowed roll out in some pilot areas. Accessibility was also a challenge until a system of localized 'pay points'[82] was introduced in 2010.

DFID has committed to support the further scale up of the current programme and, together with MCDMCH, has set an outreach target of 99,000 individuals, 47,600 of whom should be women, by 2015. In late 2012, MCDMCH initiated plans to procure an electronic payment system provider to support the scale-up of the programme. The programme will eventually cover 17 districts in Zambia, of which several are very remote. The new payment system, once procured, should increase the chances of offering additional financial services (e.g. store of value, financial education, etc.) both to grant beneficiaries, and hopefully also to others within these remote communities. Social grant programmes will not drive economic growth, but merely offer a security net for the extremely vulnerable. In the case of Zambia, the target of 99,000 beneficiaries represents a further scale up in numbers reached, but it is still a drop in the ocean in the whole scheme of things and there are some that would maintain that the evidence base is still not yet strong enough to build a strong argument for massive up-scaling of support.

Financial inclusion intervention strategies will focus on the need to identify and service those individuals and businesses that have greater potential for growing into more productive, commercial enterprises because of their potential to act as drivers of growth, whilst government and collaborating partners step in to support as far as possible those that cannot get themselves out of extreme poverty on their own. The means and delivery channels of paying social cash transfer beneficiaries, may well end up having a positive spin off in terms of facilitating delivery of other financial services in target areas, but this will be more an incidental benefit than a driver.

The introduction of broad scale social grants can have implications in shaping the marketplace at the lower end of the spectrum. In South Africa, lending based on regular social grant income has become widespread. In contrast to urban areas, social grant payments are far more common than regular wage income and are used as a collateral substitute in rural areas. Whilst this is potentially a good form of unsecured lending, it is an area open to potential abuse by financial institutions. In extreme cases, the over-extension of credit by financial institutions has led to agents arriving at social grant pay points to take possession of grants, thereby completely defeating the object of

[82] Civil servants, most typically teachers, are recruited and act as Pay Point Managers (PPMs). The current payment process involves the physical movement of the PPM to collect cheques from the MCDMCH and disburse funds at his/her pay point.

the social support payments. Steps such as encouraging grant payments through a bank account (which has certainly increased the level of formal financial inclusion in South Africa, although many people seem to make no use of the account other than to receive the payments), and/or the receipt of grants in themselves may encourage people to join informal savings and credit groups (which also seems to have happened in South Africa). It will be important for policy makers and those involved in social grant programmes to not only monitor the benefits and impact of programmes, but to be watchful of, and ready to take action against, abuse of such systems and unintended consequences.

5 Understanding the gap between supply and demand

Based on demand-side and supply-side analyses, this section of the report explains in more detail key contextual factors, which contribute to the mismatch between the current demand for and supply of agricultural and rural financial services. These contextual factors clarify the nature of the access-inclusion gap. They are also hold implications for policy and strategy formulation, refinement and implementation.

5.1 Demand related contextual factors

On the demand side, limited access to financial services has contributed to a lack of understanding of many such services, as well as a lack of appreciation of their benefits. Achieving meaningful inclusion will require strong elements of consumer education to help activate the market and stimulate the uptake of financial services by rural households. The recent launch of the strategy on financial education for Zambia is one of the initiatives by the government aimed at contributing to financial inclusion.

All recent demand-side assessments for Zambia - the FinScope studies in particular - point to the importance of increased usage of appropriate savings, credit, insurance and transactions services as a means for protecting and growing agricultural and rural enterprises and household economic resilience. What is also clear is that meeting unmet demands is as much about providing appropriate and sustainable savings, insurance and transactions services as it is about increasing access to credit.

In the case of insurance, low market penetration of insurance products has a direct bearing on low levels of exposure to insurance. Insurance risks for people in rural areas encompass household and business risks. The distribution strategies of some insurance companies, such as Professional Life Assurance Limited, include partnerships with rural-based aggregators[83] as a means to increase the uptake of microinsurance products by rural households and individuals. The biggest gap is still in agricultural insurance. Aside from product development, increasing the uptake of insurance products will require investment in consumer education. Given the current low levels of understanding of insurance, as well as misconceptions around the concept of insurance, and distrust of insurance companies[84], it is imperative that strategic investment in consumer education takes place. However, insurance companies' investments in market research, product development and marketing will only go so far. Other key stakeholders such as ZNFU, ZAMACE as well as those commercial banks looking to offer finance based on forward contracts, can also play an active role in breaking down barriers to financial inclusion, including the use of appropriate tools and approaches to build small-scale farmers' and other rural entrepreneurs' capacities for informed decision-making.

[83] Potential rural based aggregators for insurance include membership-based, NGO-led and large agri-business-outgrower groupings of small-scale farmers. Examples of such groupings are farmers associations under the Zambia National Farmers Union, farmers under large outgrower schemes like Dunavant and farmers formed by NGOs like Musika.

[84] See FinScope 2009 data.

With respect to savings, the mismatch between supply and demand is compounded by key disabling factors based around accessibility, affordability and cost, and product appropriateness. Furthermore, the realities of income seasonality means that rural households only have cash at certain times of the year – and there are business and household pressures on usage of this income. Consequently well-targeted savings products will need to align to these needs and interests, and ensure that cash, which is mobilised has tangible benefits and helps drive growth and improve household economic security.

With regard to bank accounts, the FinScope data suggests that the high level of self-exclusion is not because people prefer to receive their income in cash, but because at current fee levels, bank accounts appear unaffordable for as much as 90 percent of the rural adult population (although they are likely to be affordable for a higher proportion of the urban adults - up to 50 percent). This knowledge has clear implications for addressing the viability and operational cost structures of existing and new providers, as well as the need for deeper exploration of the potential for demand-driven and cost effective solutions for the long-term.

In the case of transaction services, the frameworks for expansion exist, though there is need for improvement. There are still regulatory gaps with respect to e-money regulations, which need to be put in place for consumer protection, including rules surrounding use of delivery agents, enhancement of fraud prevention measures and legal recourse in the event of fraud[85].

A critical list of demand-side measures - other than a firm understanding of customer interests and needs - are also required to close the gap. Better financial education, improved business management capacity, and appropriate marketing and communication are needed for sure, but other critical non-financial contextual factors such as poor marketing infrastructure (e.g. lack of, and poor quality, feeder roads, storage options and market information) are inherently linked with access and uptake of financial services and, of course, broader rural prosperity. Better roads, wellfunctioning producer groups, and effective linkages to markets, in which there is price transparency, offer farmers increased income-generating opportunities. As a result, they are more likely to need, and want to use, financial products and services, as well as wanting a stronger voice in shaping those products and services.

5.2 Supply related contextual factors

Financial service providers often have products and systems that inhibit people in rural areas from gaining access to the financial system. Weak physical and technological infrastructure and the sparseness of the rural population are among the supply-side barriers that worsen the situation in Zambia. Financial service providers have to mitigate these factors by investing in more innovative products and delivery mechanisms that are demand-led and user-friendly in order to drive access to and the uptake of financial services by poor people in rural areas.

[85] FinMark Trust, Mapping the Retail Payment Services Landscape: Zambia, Bankable Frontier Associates, Second Revised Draft October 2012.

However, increasing supply on its own may simply open the access-inclusion gap further, unless the new supply initiatives are inherently customer-oriented. A good example is understanding the extent to which those that are currently unbanked in rural areas are willing to embrace mobile phone based banking and transaction services, or, will they reject this in preference for a physical rural bank facility, which may be further away, but provides the levels of credibility rural Zambians require from their financial service provider; they may be interested to embrace both on the proviso that they have sufficient understanding of mobile banking and conventional banking services, and their financial needs and interests warrant the use of both types of services.

A key contributor to low access has been and remains the challenge of slow growth and limited outreach across all levels of financial services supply, and is attributable to a combination of key disabling factors on the supply-side.

- Viability challenges and high cost structures of operating in rural areas: For some years, banks and MFIs have remained within their comfort zones, achieving sufficient and manageable business growth by taking advantage of unmet demand for financial services across urban populations. Increasing competition in urban markets and a slow emerging awareness of opportunities in agricultural and rural finance (often facilitated by NGOs) is pushing the formal sector to explore new market opportunities. However, gaps with respect to understanding what those opportunities are combined with unanswered questions around viability and cost structures of operating in rural areas continue to impede formal suppliers' decision-making.

- Lack of affordability and appropriateness of products and services. The current costs of maintaining a physical presence in rural areas, e.g. the start-up costs of conventional branch structures, maintaining mobile teams of credit officers, maintaining online systems, etc, as well as the real and perceived risks related to lending in agriculture have resulted in prices which are unaffordable for many rural businesses and individuals. Product appropriateness also remains a challenge as suppliers' apply layered risk management strategies to products and service delivery resulting in products that are unsuited to borrower's needs. Small-scale farmers in particular complain that product attributes (e.g. loan amounts, loan repayment frequency), the costs of borrowing (e.g. upfront fees, time needed to attend meetings, transport costs to payment points) as well as methodologies (such as group guarantees) are not what they want or need.

5.3 The microfinance sector

The Zambian microfinance sector is underdeveloped by African standards and has market peculiarities and weaknesses that mean it is not as well positioned as it should be with respect to increasing access to sustainable financial services at the lower end of rural and agricultural markets. Revision of the Microfinance Act in 2006 was intended to stimulate sector growth. However, it resulted in a proliferation of consumer lenders entering into the market, and did little to stimulate growth of developmental MFIs. Of the 33 BOZ registered MFIs as of December 2012, less than ten focus on microenterprise development, and only four of these have become more proactive in their efforts to develop rural financial services in recent years. In stark contrast to countries such as India or Ethiopia where microfinance was engineered to meet rural financial needs first, with expansion occurring in urban areas afterwards, the microfinance sector in Zambia grew out of lending almost entirely focused on urban-based microenterprise development.

A combination of factors has led to delays in microfinance development and slow, unsteady growth across the sector, with institutional contraction and failure in some cases. In the early 2000s, microfinance growth was predominantly donor-driven. Various donors injected large amounts of capital into leading MFIs. Weak governance and accountability coupled with weak capacity to manage growth contributed to leading institutions growing rapidly, then spiralling into decline, which resulted in significant contraction of the sector, and the collapse or near-collapse of several leading MFIs in the ensuing years. Box 3 highlights how the misalignment of products and services also contributed to decline of services in rural areas.

Slower than anticipated growth in the microfinance sector, and in rural microfinance in particular, has also been attributed to poor credit culture, a lack of appropriate technical support, and the high expense of service provision due to weak transport and communications infrastructure[86]. This rings true given the size of MFI loan books relative to the overall size of the market, and given that even successful MFIs seldom seem to reach more than ten thousand clients, while the overall number of potential agricultural borrowers (excluding subsistence producers) runs into hundreds of thousands.

[86] MF Transparency, June 2011.

Box 6: Learning from the past; how lack of client responsiveness impacted sector growth in Zambia

In 2004, Zambia's microfinance sector had an estimated 40,000 active clients and total outstanding portfolio of ZMK 8.94 billion. High delinquency rates and default typified the sector. Portfolio at risk ranged between 7-50 percent across the five lead MFIs and key NGO-led programmes at the time. Weak performance led to significant market contraction in prior and subsequent years the most significant of which included the collapse of one lead MFI, and contraction of another to one quarter its former size. MFIs were experiencing client drop-out rates of above 30 percent during the same period. In the period 1995-2004 two lead banks cut their rural branches by half. A study, conducted in 2004, identified the top reasons for the extremely poor repayment rates in the microfinance sector. These included:

On the demand-side:-

- misuse of the loan due to overriding family needs;
- dissatisfaction with loan amounts, repayment terms, as well as effective interest rates, and the lending methodology (focused on solidarity group lending); and
- multiple borrowing illness and death of clients, and loss of client productivity due to HIV/AIDS.

On the supply-side:-

- inability of MFIs to offer a broader range of products and services;
- lack of monitoring; and
- lack of staff training and staff incentives.

As far back as 2004, study participants voiced a need for general-purpose loans (e.g. emergencies, medical, and education), pro-poor insurance products delivered as an insurance product and not an attribute of a loan product, and voluntary savings products. The study also picked up on the key issue of gender and how control of financial resources lay firmly in the hands of men. So whilst the bulk of loans were in the women's name and women were held accountable for loans outstanding, they had little or no control over loan proceeds. Whilst default rates were also attributed to a very poor credit culture ('willful default'), the majority of client feedback pointed to the lack of affordability and inappropriateness of the credit products, and the need for microfinance providers to learn more about actual needs and interests in their target markets.

Source: AMIZ, Study on the Causes of High Delinquency and Default among MFIs in Zambia, M&N Associates Ltd, 2004

The developmental MFIs have experienced a marked turnaround in performance over the past four years. Successes include being approved for (or working toward) deposit-taking licenses, significantly improved portfolio quality, increasingly innovative product and service developments and piloting of mobile banking technologies. They also have institutional strengths, which provide a good foundation for growth in rural areas, including capable leadership and a willingness to overcome constraints and engage the rural agricultural market. However, they are not operating as significant drivers of growth in rural areas. On the one hand, the MFIs require less formality with respect to information and loan guarantee requirements, and they are willing and able to handling small transactions. On the other hand, the MFIs' cost structures are high, branch outreach remains relatively limited in rural areas, and capacity, at management and field levels, for managing extensive portfolio and geographies is limited.

There are a number of critical areas that need closer examination in order to understand the role that MFIs can play in expanding financial inclusion in rural areas, and to determine support needs in order to ensure that gains made in the microfinance sector are viable and are a good fit for the overall vision for financial sector deepening in rural areas. Aside from MFIs internal capacity issues related to product development (savings, credit, insurance and transaction services), portfolio management and field-based client servicing, other overarching concerns relate to operational efficiency and pricing strategies. A recent survey conducted by BOZ to investigate interest rates charged, revealed that the majority of MFIs in Zambia charge interest rates ranging from 5-10 percent per month, while a few charged interest rates greater than 15 percent per month. On the whole, annual effective interest rates ranged from 13 percent-400 percent.

5.4 Human resource capacity: A cross-sector challenge

Human resource and systems capacity weaknesses and the risks associated with them span all levels of the financial sector from top level leadership - required to lead, command and sustain sector growth through key institutional and corporate structures - down to community-based leaders and treasurers tasked with recording and protecting a village savings group’s finances. These weaknesses are constraining factors that if left unabated will have a significant negative impact on progress toward financial inclusion, but they also represent an opportunity for timely, constructive investment in human capital development.

Efforts to build industry level knowledge must extend to leadership and management at branch level, and to relationship managers and credit officers who are on the frontline of portfolio growth and management. Strategies for strengthening the sector should involve industry representative institutions such as IAZ, BAZ and AMIZ. However, it is necessary to build the capacity of these institutions so they are able to identify institutional needs, and determine client-centred approaches for packaging technical training and learning forums that impart latest approaches in product development, outreach and delivery, and best practices and lessons learned from around the region. It may be possible for industry representative organisations to partner in offering generic training in areas such as M4P and value chain finance to strengthen linkages between financial service provision and market-based economic growth. Many of the commercial banks have the backing of international expertise, which they tap into or bring in-house to help establish agricultural credit departments. This includes developing appropriate human resource and operational capacities. However, there is scope for using BAZ as a conduit to broaden and accelerate learning across the banking sector. Some MFIs are better equipped than others to provide in-house technical training, but there is nothing at industry level through AMIZ for several years, and there has been very little, if any, external support for newly transitioned deposit-taking MFIs. RFP and Plan International have been the leading technical support for community-based finance.

5.5 The MSME sector

Another key set of contextual factors linked to driving financial inclusion in Zambia is based around MSME financing for both agricultural and non-agricultural MSMEs. MSMEs can be vital contributors to economic growth, offering increased employment opportunities, and backward and forward supply chain finance. The Zambia Business Survey (ZBS) highlighted very low levels of access to finance across Zambian MSMEs, with 80 percent of MSMEs overall, and 85 percent of MSMEs in rural areas financially excluded. Moreover, according to ZBS, only two percent of MSMEs have access to credit, and whilst 96.7 percent of large businesses have access to insurance, a mere 0.9 percent of MSMEs have access. As 70 percent of MSMEs are located in the agricultural sector, their challenges include limited physical access to financial services, but also the high costs of maintaining access means MSMEs cannot afford to use financial services. There is also a very limited range of products on offer, and a dearth of appropriate services for agricultural MSMEs. On the supply-side, increasing access to MSME finance will require reducing costs of delivery, and investment in innovative product and service delivery channels. To become drivers of growth, MSMEs need access to a range of business development financial services, including short-term credit for working capital, but also credit available on longer terms for asset growth. Savings and insurance options are just as vital to protect the business, and to reduce risk and offer protection to financial suppliers servicing the businesses.

However, MSME performance also has to improve. According to ZBS, 40 percent of MSMEs earn less than US$2.00 per day, and only 15 percent of MSMEs have a turnover of US$200 a month or more. Even if products were cheaper and more widely available, the reality is that the majority of MSMEs would be impossible to serve. As it stands, access to finance alone will not drive growth in MSME productivity. For this to happen, a combination of measures is needed including: improved access to infrastructure (roads, electricity, communications, etc); increased education levels and business management skills; and increased business facilitation support to strengthen the platforms on which businesses grow.

6 Enabling and disabling factors

The following section outlines and discusses the key enabling and disabling factors that form part of the considerations in addressing the supply-demand gap for rural financial services.

6.1 Supply-side enabling factors

Level	Enabling	Key observations
Micro	• Contract buyers (in the cotton sub-sector particularly) have improved on-time payments to small-scale farmers: there is also better matching of input and cash loans to production needs, and increased levels of embedded extension support (dairy, cotton and tobacco sub-sectors). • Market-led facilitators are bringing players together and supporting innovation and market testing in agricultural financing. • Emergence of financial suppliers and supply chain products that support emergent farmers, and mechanisation. • Transition of leading MFIs to deposit-taking institutions, increased regulation and supervision, increased scope for rural savings. • DBZ overseeing MFI apex credit line. • Accessibility of grants for piloting microinsurance product and service delivery in the market. • Emergence of products for low income needs.	• Identifying opportunities and support mechanisms for replicating good and working rural financing models can potentially stimulate increased supply of financial services in rural areas particularly to farmers in productive sub-sectors such as dairy, cotton and tobacco. • Further support may be required particularly in identifying the market potential and assist in scaling up successful partnerships. Identification and replication of good practices must be encouraged. • Support may be needed to established value chain players to assist organization of small-scale farmers into commodity groups and integration into value chains. • Intensify performance-based financial and non-financial support to lead deposit-taking MFIs, including bespoke in-house support to strengthen systems and human resource capacity for retailing microfinance savings and deposits. • Innovation grants are providing opportunities for financial service providers to test new approaches of expanding their product portfolio and reaching new markets particularly the low-income markets. • Product simplicity and innovative delivery mechanisms characterize new products; cross sector partnerships are slowly emerging as a means for improved accessibility and enhanced affordability.
Level	Enabling	Key observations

Meso	• Increased use of technologies as retail tool. • Supply of credit information. • Presence of sector representative associations.	• Continued support to strategy implementation; funding and resources for on-going pilots and appropriate scale-ups. • Although still in its early stages, establishment of the first credit bureau in Zambia is an important development. However, there is scope to scale up coverage and usage. • Although there are number of functioning private sector led associations such as BAZ and IAZ, there seems to be scope for their increased role in effectively contributing to addressing issues that are currently impeding the supply and uptake of financial services in both rural and urban areas.
Macro	• BOZ distribution of new guidelines for 'Know Your Customer' (KYC) requirements**.** • FSDP tax review study on the impact of and distortions in taxation on the financial sector with the aim of minimizing tax distortions and enhancing tax neutrality. • Revision to the Banking and Financial Services Act (BFSA): a draft bill with proposed amendments to the BFSA. • Facilitating the growth of remote access delivery channels: BOZ has not	• Aims to contribute to creating a more conducive and appropriate environment for improving financial inclusion, allowing banks and non-bank financial institutions to apply flexibility in their KYC requirements. However, the initiative does not seem to be having the intended impact. Why this is the case may be worth exploring more deeply. • Development of appropriate legislation for the leasing sector - Includes a review of laws relating to VAT charges on finance leases, which includes agricultural equipment leases. • Regulatory reforms well underway/completed: 1. Amendment of the Agricultural Act to include a regulatory framework for warehouse receipting systems and commodity trading under the Agricultural Credit Act; 2. Comprehensive review of and substantive amendments to the Insurance Act, Includes specific provision for microinsurance; 3. Amendment of the Banking and Financial Services Act (BFSA), including those providing for branchless banking. Draft branchless banking regulations underwent review in July 2012. A draft bill with proposed amendments to the BFSA was presented mid 2012; includes a repeal of the Money Lenders Act, with appropriate provisions being incorporated into the BFSA; work continued during the remainder of 2012 to conclude amendments to the BFSA • Leverage opportunities to further engaging technology service providers and to use

	yet developed regulations around agent banking and mobile phone based transactions and payments. However, it is creating regulatory space for piloting and development. Development of a regulatory framework for electronic money is work in progress; as at October 2012, BOZ had drafted e-money regulations, which have yet to be finalized. • As at October 2012, BOZ was also working on regulations for banks use of agents, which will frame and set minimum standards for payment service providers, retail networks, deposit collection, etc.	technologies to develop cost effective solutions to financial access and inclusion challenges.
	• Development of a rural finance policy strategy for Zambia: the final strategy document is awaiting cabinet approval and a copy of the same is available to the public. Section 4.1.1.3 provides an overview of the strategy document.	• Development of intervention strategies and operational actions that complement and enhance national level priorities.
	• Review and strengthening of microfinance regulations, including separate regulations on consumer lending and appropriate monitoring and supervision of Tier III MFIs.	• Aims to create a clear distinction between developmental microfinance and consumer lending companies (often referred to as salary-based lenders); addresses the proliferation of unregulated MFIs. • Needs parallel initiatives that lead to increased product development, microfinance performance efficiencies and cost effectiveness.
	• Development of a microinsurance national strategy; launch of microinsurance promotions due for launch in 2013	• Overall goal of the strategy is to stimulate and accelerate the provision of microinsurance products and services in Zambia. • Increase penetration of microinsurance products in agricultural and rural areas and support feasibility and viability studies for development of livestock and weather index insurance.
	• Development of a national financial education strategy under FSDP II, expected to become operational during 2012 through the establishment of a Financial Education Coordination Unit (FECU) housed within BOZ.	• Financial education and awareness approaches should focus on ‘points of access’ that maximize outreach (e.g. MFI clients, outgrower schemes, rural and agricultural associations, VSLA members, church groups, etc).

6.2 Supply-side disabling factors

Level	Disabling	Key observations
Micro	• Poor condition of storage facilities and lack of availability of facilities is limiting potential for growing and integrating warehouse receipting and other financing products at small-scale farmer and emergent farmer levels.	• There is need to support and incentivize public private partnerships (PPPs) that improve warehousing and distribution networks. Further support is required for increased access and usage of commodity-backed financing schemes.
	• At small-scale farmer level, lack of access to water and lack of irrigation, as well as poor access to quality inputs, result in limited crop cycles and under-productivity, which means farmers are not a strong value proposition for financial suppliers.	• There is scope to explore options for scaling up finance for inputs and irrigation, including supply chain finance, working through lead firms.
	• For many small to medium scale farmers, the high costs and capital requirements related to investing and scaling up in agriculture are prohibitive: for example, the costs and challenges of mechanisation are a barrier for emergent producers that would like to invest and scale-up.	• Low levels of mechanisation and technology uptake at small-scale and emergent farmer levels, linked with weak production and post-harvest management capacity, mean that many farmers are not considered creditworthy by financial suppliers. • Expand successful working models that combine finance and business development support to emergent farmers in promising agricultural sub-sectors.
	• Lingering culture of credit default and lack of recourse in situations of non-payment of credit.	• Whilst Zambia's credit culture has improved in recent years, there are still a number of compounding factors around delayed repayments, credit default, lack of trust, and lack of effective legal recourse in situations of non-payment that contribute to a prevailing reluctance on the part of financial service providers and supply chain actors to extend credit.
	• Lack of collateral, including land title. The land tenure system, which limits individual title to land, constrains the ability of small farmers to access finance and adversely impacts their willingness to invest in the sector.	• This constraint is particularly acute for women, who comprise 65 percent of the rural population and 85 percent of the total small-scale farmer labor force for agriculture production. There is also limited ability to develop or expand production using the bank's capital when there is absence of land title.
	• Linked with this constraint, on the supply-side, is the reluctance of financial suppliers to look beyond traditional forms of collateral.	• Support the development of financial products and financing mechanisms that are not reliant on land as security against borrowing (e.g. buyers' contracts, equipment leasing, etc.). • Accelerate plans to establish a central collateral agency.
	• Side-selling: small-scale farmers opting for side-selling and reneging on	• Among banks' biggest complaints is that their farmer clients over-estimate projected yields and revenues. They fail to follow up with lender requirements

	buyers' contracts is still a common complaint.	and are slow to provide documents as required. These factors combined with unpredictable prices, currency fluctuations and changing weather patterns make the Zambian small-scale farmer a high risk option for the banks.
	• Prevailing high levels of perceived and real risk on the part of financial suppliers.	• Closer collaboration needed between farming associations, law courts, lawyers and legal advisors; develop contracts and dispute resolution mechanisms that build confidence on the supply side.
	• Low understanding of financial supplier credit risk management needs.	• The limited pool of expertise results in regular poaching of staff across the banks and MFIs. It is very difficult to find people with combined knowledge in agronomy, business and finance.
	• Lack of human resource expertise across all levels of the financial sector: there has also been little or no structured, external support in recent years for building and expanding expertise for financial services industry growth.	• Industry-wide training and technical support based on market needs required: develop and integrate professional training into educational institutions; facilitate access to learning opportunities.
	• Limited market information.	• Financial suppliers lack initiative in going out and gathering information on market potential for specific agricultural production sectors, as well as value chain finance opportunities. • Opportunity to support in filling market information gaps and disseminate through industry-wide forums.
Meso	• Unclear role, lack of future direction and lack of proactive sector support on the part of AMIZ, the main MFI representation body. • Weak client service delivery model and resulting weak uptake of services on the part of the existing credit reference bureau. • Weak client service delivery model and resulting weak uptake of services on the part of the main agricultural commodities exchange platform.	• Support needed to strengthen capacities, strategic planning and business delivery models of key industry service organisations.
Macro	• Relatively low levels of public sector expenditure on the agricultural sector.	• On-going technical support for policy development and reforms, including stronger alignment of government-led interventions and subsidies with markets.

	• Government interference and subsidies are contributing to market distortions and crowding out of private sector. On-going government intervention in maize commodity trading, in particular, is a disincentive to private sector players. • Current tax implications are a disincentive to farm equipment leasing: currently farmers opting for lease financing to acquire or upgrade equipment are liable to pay VAT on capital and interest amounts, whereas buying direct from an agri supplier qualifies the farmer for VAT free purchase. • There are no specific policies or an enabling framework that encourage leading firms to extend financial support to small businesses. • Linked with this are the high on-going operational costs of overseeing client portfolios in rural areas (e.g. costs of online banking, mobile communications, transport). • Weak and inadequate physical and technology infrastructure hinder efforts to reach out to rural and agricultural communities. • Costly branch set-up requirements for financial suppliers. Current branching regulations are out-of-date and out-of-touch with the reality of doing business in rural areas since high start-up and fixed costs make conventional rural branch networking unprofitable. • Absence of legal framework for delivering insurance to low-income people; law that can potentially stimulate provision of insurance services to rural areas.	• On-going support needed to review and improve tax regulations; explore new and innovative tax breaks and incentives that promote agricultural sector growth. • Innovative policies, PPPs and incentives called for, that stimulate markets and partnerships that engage lead firms. • Develop and refine cost effective branchless banking models that help overcome physical access challenges; support scale-up of successful and viable mobile transaction models. • The Pensions and Insurance Authority is currently in the process of formulating specific regulations for microinsurance. Although there is currently policy statement that allows and encourages insurers to develop and deliver microinsurance and accounts for current traction, specific regulations on microinsurance business, once in place, can create further momentum.

6.3 Demand-side enabling factors

Level	Enabling	Key observations
Micro	• Participation of rural households in productive agricultural sectors.	• There seems to be great scope of innovation in financial product design and supply to rural areas, particularly in introducing value chain financing in sub-sectors with greater participation of small-scale farmers.
Meso	• Presence of productive farmer clusters and groupings: farmer groupings, organized and supported by agricultural market development facilitators and umbrella organizations such as ZNFU, can be leveraged for aggregation, cost-effective financial education and product awareness, especially for group based financial services • High mobile phone usage and acceptability: growing electronic money platforms through mobile phones, and increasing orientation and usage of mobile phone based transactions services.	• Where there is emerging good practice, scale-up and replication could potentially yield greater results. • Increasing orientation, usage of mobile phone based transactional service, coupled with financial education could potentially drive expansion of innovative e-solutions for rural financial services.
Macro	• Launch of the financial education strategy: financial education to rural based small-scale farmers is a key element of financial education programmes for adults.	• Leveraging existing farmer groupings and clusters can potentially enhance flow of financial education.

6.4 Demand-side disabling factors

Level	Enabling	Key observations
Micro	• Insufficient collateral and lack of credit history: insufficient information on prior repayment performance (if any) and a lack of trust in clients' own information result in collateral requirement levels that MSMEs cannot meet. • Poor exposure to and experience of financial services and service providers: the majority of rural households have little or no experience with formal financial services. • High levels of financial illiteracy partly account for the low uptake of financial services in rural areas: financial education would empower people with knowledge, skills and information that would enable them to make better financial management choices. • Poor financial service infrastructure: lack of physical presence of financial service providers in some areas worsened by non-availability of appropriate financial services. • Nature and level of income: the majority of rural households have low, seasonal and irregular income.	• Farmers see collateral requirements as excessive and a barrier to accessing credit (see Box 1, Section 3.1). • Besides the need to introduce more financial services in rural areas, financial service providers need to invest in trust building. • Financial education alone cannot lead to increased uptake of financial services. There is need for complementary initiatives, including supply of appropriate financial services. • Accelerate development of branchless banking services.; encourage KYC campaigns as foundation for development of more appropriate products. • Advocate undertaking of non-financial initiatives to strengthen household income, e.g. expenditure on transport and water supply infrastructure.
Meso	• Lack of consumer protection mechanisms: currently small-scale farmers and poor households are at the mercy of financial service providers or agri-businesses that provide credit. In particular, current financing arrangements through outgrowers and other forms of contract farming are not closely monitored. In many cases, small firms are often dictated to by larger firms that offer inequitable pricing contracts and arrangements based on hard cash.	Consumer protection mechanisms to enforce transparency are needed, as well as sound, transparent business practices that encourage the uptake of financial services.
Macro	• Absence of coherent rural finance policies: there are still gaps with respect to policies that provide incentives to financial services providers to develop appropriate financial services. For instance, there is no policy framework that provides guidelines on the development of insurance products for low-income people in rural areas.	• Ideally the policy framework and strategies for developing rural finance need to be comprehensive and provide guidelines for all forms of financial service arrangement.

7 Summary of findings, implications and recommendations

Findings	Implications	Recommendations
Macro Level		
• The importance of an inclusive financial system is widely recognized by policy makers, though not all market players. • Many areas for policy and strategy development affect, and are best addressed by, a combination of players. • The main issue for stakeholders is recognizing the broad reach of policy and strategy development, and the current opportunities for building on the efforts of multi-sectoral institutions and businesses to-date, to significantly deepen and expand financial inclusion. • Currently subsidies in some agricultural subsectors and in maize production in particular are crowding out opportunities for increased private sector business. • There is a need for structured approaches toward knowledge management across the financial sector.	• Ultimately markets drive growth. Therefore, policy-makers' efforts to strengthen the regulatory framework must result in an enabling environment, which brings market players to the table. Reforms need to be timely and keep the interests of rural businesses and households at their core. • The need for coordination and coherence across existing and new programmes, partnerships and market developments. • Ensure understanding of, and partnering in, tackling the root causes of high costs that persist on the demand- and supply-side, rather than applying short-term or punitive measures that may hinder rather than promote sector growth. • There is scope to develop and introduce simple and manageable tools and practices that identify, catalogue and make practical use of successes and at the same time acknowledge and extract learning from mistakes. • Sector development facilitators can provide support in developing and integrating mechanisms for 'knowledge management' into current and future programmes.	• Incorporation of a research and development component within one or more national level programmes to identify new developments and innovations in rural and agricultural finance • Continue to identify new sources of funding for research, development and scale-up support needs. • The importance of knowledge management should be at the fore as one of the most efficient and effective means for accessing and gaining from latest thinking, innovations and best practices. • Introduce and support a framework for knowledge management. Some appropriate ways of bringing learning to Zambia and expanding learning in-country could be through the sponsorship of industry-wide learning events or hosting of events such as a high-level annual financial sector conference, the publication of financial sector bulletins, sponsoring and publishing research studies and papers, as well as integrating formal appraisal and feedback mechanisms, case study development and documenting of best practices into contract agreements, MOUs, etc. • Practical approaches and feedback mechanisms within national level working groups to disseminate latest developments and successes in the marketplace so these can inform policy-makers' decision-making.
Meso-level		

• There is a need for focused efforts to strengthen financial institution representative and support agencies.	• Strengthening the supply and use of credit information through support to develop a central collateral agency, and to promote increased usage of the current credit reference bureau. • Representative organisations need to equip themselves with the tools, resources and management capacities to effectively respond to needs and ensure efficient and appropriate targeting of resources.	• Support to sector associations and support agencies (e.g. PIA, BAZ, AMIZ, CRBAL) to strengthen their business models and capabilities for supporting their membership.
Micro-level		
• The majority of poor men and women live in rural areas and the main source (and in many cases only source) of income is from agriculture. • To alleviate poverty and positively change the lives of the poor, financial services need to promote asset growth and protection, and economic resilience. • There is a need for deeper understanding of target market financial needs and priorities on the part of financial suppliers to enhance market knowledge and to ensure demand-led growth. • It will be important for supply-side support efforts to support access to practical tools, approaches and emerging best practice for addressing the costs, risks, product development challenges of agricultural and rural finance. • Well-designed initiatives for financial service delivery have stimulated the interest, and risk appetite of financial	• Efforts to integrate vulnerable and low-income groups into financial systems will require a strong focus on effective product and service development linked with driving agricultural productivity and growth – this includes appropriate and diverse products and terms and conditions for different farming levels. • Meeting unmet demand in rural areas is as much about providing appropriate and sustainable savings, insurance and transactions services as it is about increasing access to credit. Strategies to facilitate the development of agricultural and rural financial services will need to encompass the broad spectrum of Zambian financial service providers in order to ensure that the comprehensive range of financial products required by rural communities is provided. • Suppliers have to deepen their understanding of small-scale farmers' interests and priorities with respect to access to finance. However, weak consumer financial literacy can distort market research exercises (if, for example, respondents do not have a full grasp of financial terms being used). Interviewers, tools and approaches need to take into account consumers' education and financial literacy levels.	• Sector support will need to be demand-driven, but it should also be packaged in such a way as to promote and significantly contribute to industry strengthening. • Increased market information and feasibility studies (commissioned by or for suppliers) on growth opportunities need to be conducted for specific rural and agricultural market segments, including more concrete data on potential demand (potential scale and outreach numbers, potential portfolio sizes, and costs and timelines for achieving break-even levels). • Increased investment in research and development, piloting and testing of innovative product design and delivery, and support for scale-up of successful pilots. • Product feasibility assessments on business and financial service models that propel growth in agriculture in rural areas and that enhance financial management skills among rural, leading to household economic strengthening. • Starting small and piloting products and delivery

suppliers, e.g. Afgri Leasing's partnership with Dunavant to lease tractors to emergent cotton farmers / contractors; VisionFund Zambia's collaboration with Zoona to establish a network of local agents to support the disbursement and collection of loans via mobile phones; RFP's collaboration with NGO partners to establish rural VSLAs. • Zambia's relatively untouched market represents a huge opportunity for financial suppliers. However, history has shown that mistakes can be costly in terms of financial loss and loss of credibility at institutional level, and more broadly at industry level. • Achieving scale and outreach for low income men and women in rural communities will require multi-dimensional approaches. • The opportunity is there for VSLAs, ASCAs and possibly SACCOs to be a catalyst for of flourishing financial and agricultural sectors as providers of productive credit and as a first step in instilling a much needed savings culture. • Models are likely to fail, however, if supply driven.	• Increasing access to, and uptake of, financial products and services will require similar on-going innovations and partnership approaches to further stimulate existing supplier / promoter interests and to bring new suppliers to the table. It will require increased levels of know-how, and investment targeted at product and service development. • Suppliers need to be able to develop and apply tools and approaches for appropriate cost-benefit analyses, and for effectively analyzing cost efficiencies - for the client as well as the financial institution. • Market testing (through structured piloting and appraisal) needs to be time-bound so lead times and costs for developing new products and delivery options are kept to a minimum. • More information is needed to explore how best to support the expansion and sustainability of VSLAs and how they receive long-term supervision and support. Experience has shown that developing such an apex entity presents many challenges (particularly around leadership, governance, roles and responsibilities, and financial sustainability) and takes several years. • Decision-making around future investment in and growth of ASCAs and SACCOs needs to begin with looking at capacities, motives and intent, rationale for support, and their future role in expanding rural and agricultural financial access as well as broader rural agricultural development.	models should be encouraged and supported to ensure sufficient time for products to be refined to meet users' needs, and to ensure that feasibility and cost implications of scale-up are clearly understood. • Financial suppliers, and those supporting sector development, need to maintain a flexible approach, continually monitoring market developments, reading market signals, and anticipating unintended outcomes as far as possible, with a view to re-prioritizing, and adjusting strategies and interventions in a timely manner. First and foremost, however, is the need to sharpen focus and quantify market opportunities in agricultural and rural finance. • Increase focus and support to grow informal community-based financial services, including sound market research and contextual analysis to determine appropriate support, and analysis of best practice and regional experience in developing good models of structure, governance and operational procedures, as well as approaches for ensuring sustainability, transition to semi-formal associations and preparedness for formal financial inclusion. • Support to design and conduct research to identify what support is needed to expand current VSLA development initiatives, including examining the need for, and recommendations on, appropriate models for umbrella/parent entities. • Sector support activities should consider commissioning research on status of SACCOs and ASCAs in Zambia. The study would help determine the potential for re-positioning SACCOs and ASCAs based first and foremost on demand-side needs and

		interests. • Increased business development support for small-scale farmers in practical application areas such as farm planning, raising return on investment, breaking the cycle of low productivity-low returns, and how markets work (e.g. understanding market requirements, accessing and using market information, and organisational development skills). • Apply the lens of the financial service provider when devising frameworks and strategies to strengthen the functionality of farmer commodity groups, clusters and associations. • Timely implementation of the financial education strategy is important, since increased levels of financial literacy are intrinsically linked to increased financial access. Strategy implementers should remain open and flexible to adding new 'points of access' that can accelerate and scale up access to financial education. Linked with this is the need to identify and mobilize 'agents of change'[87] that can work effectively in rural areas to promote financial education and awareness. • Support product and service development that is tailored to the needs of households and businesses, which are at different economic levels. • Leverage recent developments in the use of mobile phone and other technologies (e.g. smart cards, e-vouchers) and further engaging technology service providers to develop cost effective solutions to financial access and inclusion challenges.

[87] 'Agents of change' in this context are local men or women that work or live close to target groups and can through their work or through voluntary participation act as conduits for improving financial education. They may be trained to provide training or support mobilization of locals to attend training sessions.

Cross-cutting all levels		
• There is a need to broaden and intensify market stimulation initiatives. Moreover, financial sector development is likely to move faster and be more sustainable if driven mainly by the private sector. • Promoting and institutionalizing learning: A holistic approach needs to be developed to growing human resource capital across the sector which will result in an increased pool of rural and agricultural finance expertise capable of supporting growth of the industry at all levels. • There is a need for capacity building strategies, which encompass both short- and long-term needs and which access to evidence-based learning, innovations and best practices in financial sector development regionally and internationally.	• Market scans by government or facilitating NGOs can help identify existing initiatives that are suitable for replication or scale-up, as well as what additional support would help (e.g. technical assistance, market information, smart subsidies or other incentives for growth). • Market scans can be expensive and there is, therefore, merit in doing them for the benefit of industry as a whole rather than individual institutions doing them in isolation. • It is important to recognize that there is still very limited available expertise in rural and agricultural finance, both within institutions and across the sector generally. Suppliers need to be able to effectively voice their needs through BAZ, AMIZ, and the other key sector representative organisations to ensure demand-driven use of resources. • Approach would include broader and more diverse access to learning (in Zambia and regionally), mainstreaming of curricula and material through existing institutions, access to recognized qualifications, needs based and market-led training and technical assistance, and ensuring up-to-date, relevant courses and curricula. • However, financial sector capacity strengthening will only show dividends in the medium to longer term. Therefore plans to address weaknesses have to be identified and implemented early on. • At the same time, resources should be channelled to where there is the highest potential for success with respect to systemic action, sustainable change and large-scale impact, rather than to where there is the temptation (or political pressure) to plug gaps or to try to	• Encourage and support the design and roll-out of risk reduction mechanisms that are market-led and incentivize private sector involvement, e.g. the use of a part-guarantee fund, which then allows a financial institution to extend loans or leases for agricultural equipment; or part contribution (or time-bound support) to cover the salary of a technical field expert who works on behalf of a lead buyer to help small-scale farmers improve production yields - the technical expert eventually being taken on full-time by the lead buyer (or by a collaborating financial institution). • Encourage the use of smart subsidies (assisting with research and development if need be). • Short-term strategies for strengthening the sector should involve industry representative institutions such as IAZ, BAZ and AMIZ. Support efforts should build the capacity of these institutions to identify institutional needs, and determine client-centred approaches for packaging technical training and learning forums that impart latest approaches in product development, outreach and delivery, and best practices and lessons learned from around the region. • Efforts to build industry level knowledge must extend to leadership and management at branch level, and to relationship managers and credit officers who are on the frontline of portfolio growth and management.

	rescue what is not viable.	• Over the long term, there is a need to build the pool of available expertise for commercial banks, MFIs and community-based financing partners, and to integrate curricula development and roll out through primary, secondary, and tertiary learning institutions. It remains the role of policy makers to determine which institutions are best positioned to do this.

8 Consultants' conclusions

1. There have been promising developments in recent years in Zambia with respect to the supply of financial services and, for the most part, the trends and future outlook are positive. Notable new developments in the past three to four years include commercial banks moving downstream, more aggressive tactics to capture market share, targeting of select subsectors and value chains, and strategic partnering to gain traction in agricultural markets. There are an increased number of players in the market – though still not enough.
2. The rapid pace of change, and an almost continuous flow of emerging opportunities on the demand and supply sides, imply that sector policy, strategy and intervention support at the macro, meso and micro-levels need to remain open and responsive to market developments, and to re-aligning priorities and resources as needs and opportunities arise.
3. The shift from a stagnant, poorly performing / non-performing rural agricultural finance sector to one in which there will be increasing competition in the future, make it more important than ever to ensure this increased competition works in favour of the end users – i.e. demand-driven products, services, and delivery mechanisms that are a catalyst for growth.
4. It will be important for the decision-makers and implementers of policy and interventions to take into consideration the unique social and demographic factors in Zambia that will shape and determine the demand for and uptake of financial services in the next five to ten years. The following social, economic and demographic determinants represent just a handful of the factors that currently impact on household decision-making with respect to financial needs and priorities.
    - Zambia has a young adult population. 54 percent of the population is younger than 18 and 48 percent of adults are under 30 years of age.
    - Education levels remain low, particularly in rural areas and for women. Almost 40 percent of Zambians have not completed primary education and there is a marked gender gap with respect to education levels in rural areas: 51 percent of males in this segment have at least a primary school education whilst the proportion for women is just 34 percent.
    - There are still significant numbers of households and businesses without access to electricity grids. According to Zambia's forth demographic and health survey (ZDHS)[88], almost half of Zambia's urban population has access to electricity, compared to only 3 percent in rural areas.
    - Many Zambian households take on the financial responsibility of additional family members, with 36 percent of Zambian households supporting orphans or foster children under the age of 18 years old.

88 Zambia Demographic and Health Survey ZDHS, 2007 (CSO and MoH).

- The high rates of HIV/AIDS infection and mortality continue to place a huge burden on household resources, which are diverted to care for the sick and mourn the dead, and valuable human resources are being lost.
- Most small-scale farmers rely on one crop, maize, which is harvested once a year and is susceptible to increasingly unpredictable climatic changes. Moreover, a season that is characterized by low yields and/or low prices can mean that many rural households become more economically vulnerable as they fall prey to food production shortfalls and price increases in staple foods.

5. Under the IFAD-funded RFP and work of the FSDP, policy-makers, regulators, and support institutions have formulated a policy framework for rural financial sector development. However there is scope to provide a much more comprehensive policy and intervention framework and set of guidelines that focus on stimulating micro-level investments by financial service providers in rural finance, and guide the implementation of holistic approaches required to embrace both demand and supply constraints.
6. There is a growing proliferation of market-led financing models that are working well, such as: the small-scale farmer input credit model operated by Dunavant, a leading cotton buyer; CETZAM's outreach to small-scale horticultural farmers using a 'cashless' loan model; and Zanaco's Lima credit programme for small-scale and emerging farmers (See section 4.3for a detailed description of emerging agricultural finance models). However, aside from Zanaco's Lima programme, which has grown from two pilot districts and a credit portfolio of ZMK 600 million (approximately US$120,000) in 2008 to 25 districts and a credit portfolio of ZMK 20 billion (approximately US$ 4 million) in 2011, it is notable that there are very few examples of supply working at scale. Key factors that currently constrain the replication and scaling of promising financial models such as those described above include a lack of means and support available to suppliers for replicating and scaling successful models, and a lack of information on overall market potential in many agricultural sub-sectors. Financial suppliers (banks and developmental MFIs especially) need access to credible and up-to-date market information for prudent growth and risk management decision-making.
7. There is strong justification for designing and increasing access to well-structured market-led incentives or subsidies, which, if done well, can effectively stimulate financial service innovation and scale-up by bringing down risk in the short term. However, more research is needed into what those incentives should look like and where they could best be targeted.

   Sector support providers should consider a market scan of current rural finance and agricultural subsidies in Zambia, including Government subsidies, to look at how subsidies in the market place are being applied, including the costs, targeting and overall levels of effectiveness. At the same time as looking at current subsidies, the research can explore the potential role of market-led subsidies for stimulating growth and outreach in the supply of agricultural and rural financial services in Zambia, and propose alternative incentive models (smart subsidies), which will effectively align to market needs on both the demand and supply side, and contribute to narrowing the access-inclusion gap. This type of research and an ensuing implementation framework for incentivizing growth could fall under the remit of a future rural finance programme.

8. There is a fundamental question over whether formal MFIs really have the capacity to be cost-effective suppliers of rural credit. If they suffer from the same information asymmetry and collateral problems that larger financial institutions have and with loan books that are small relative to their operating costs, then it is difficult to see them being able to 'make it', especially if they don't offer deposit-taking facilities, using conventional approaches. In urban areas, where the costs of outreach are lower and there are far more people earning regular wages and salaries, it is a different story. However, there are other more promising alternatives for MFIs in rural areas – such as agency models, value chain financing for more commercial smallholders, and supporting 'semi-formal' VSLAs/ASCAs.

   Sector support should consider feasibility research that examines more closely the role MFIs can play in rural areas, current and potential operational structures and pricing strategies for MFIs committed to rural and agricultural market expansion. The research should also look at best practices adopted elsewhere to address similar problems. As the costs of doing business in rural areas undoubtedly pushes up the costs of borrowing, to the extent we see today, interest rate caps are clearly not an appropriate measure. At the same time, incentives such as access to lower cost funding may not be the answer if it then leads to laxity in credit appraisal processes or unfair competition in the market. More appropriate action would be to incentivize MFIs to increase cost effectiveness, learning from best practice as to what are appropriate incentive options for enhancing cost effectiveness without distorting markets. Options may include tax incentives, subsidized investment capital linked to performance monitoring, access to training and capacity building, or other direct or indirect subsidies that stimulate growth such as support through AMIZ to access expertise in conducting operational audits, and implementing cost-reducing operational enhancements.

   Other avenues that can be explored include building capacity for innovative market research to facilitate MFI entry into new markets. Research should go beyond conventional microfinance product development approaches to explore areas such as behavioral economics, more complete analysis of value chains (to identify growing end markets, the businesses in the value chain and where financing will best stimulate growth), as well as management capacities and cashflows of existing and potential agency networks. As with any financial supplier entering into rural areas, MFIs need to be able to efficiently deliver products and services that act as accelerators of agricultural production through supporting access to technologies that can improve production efficiencies, yields and income levels, and equally importantly, protect investments and gains made by clients through access to appropriate savings and insurance products and services.

9. Other questions that are fundamental to developing sustainable service provision in rural areas and which require answering include:

a. **Where should financial suppliers focus and what products and services are most needed?**

   A current gap lies in the lack of information on the market potential for agricultural and rural finance. The need for sound market analysis is fundamental to financial suppliers for business planning and to inform product and service development. Currently, financial services suppliers (and for that matter market development facilitators) lack more detailed information on market growth potential in different geographic areas and at the sub-sector and value chain level, and for specific target groups. As examples, credible data on the numbers and locations of potential borrowers for tractors, other farm machinery and dairy livestock are currently not available.

b. **What is the effective demand for rural financial services?**

   Deficiencies in supply, as well as limited exposure and orientation to formal financial services across the target groups and the poor knowledge of financial services in rural communities make it more difficult to assess the nature and extent of effective demand for financial services. Using FinScope data and other studies, it is possible to deduce what types of agricultural and rural products and services households and enterprises need. More pilots are required to expose agricultural and rural sectors to existing and new products and services and to build experience and usage, which helps inform product refinement on the part of suppliers. The evidence of growing levels of credit tied to contract farming shows that this category of farmer is more than willing to accept credit that boosts their production and increases income. However, we do not know how many of this type of farmers would sign up for credit tied into a buyer contract, even if, in principle, it is intended to raise production and incomes. Moreover, many sources of credit are not private sector driven. They may be implemented with funding and support from agricultural market development facilitators and involve subsidies, which may actually mask the demand for unsubsidized credit. Lastly, such schemes rarely provide credit that supports the scale-up of production, so again demand for credit specifically for scale-up is masked.

c. **How are financial services subsidies currently being applied? What are the costs?**

   Are they well targeted and what are overall levels of effectiveness in achieving defined policy goals? Sector support providers should carry out an evaluation of current rural finance and agricultural production subsidies, particularly public subsidies, to determine their overall impact. At the same time the research should propose alternative incentivizing models for effectively stimulating financial service innovation and scale-up, by buying down risk. More research is needed into what those incentives could look like and where they could best be targeted in order to bring about long-term lasting industry benefits.

d. **Auxiliary organisations: An opportunity for increased focus and investment?**

There are 20 or so auxiliary organizations in the form of agricultural associations, which represent a broad range of agricultural subsectors. Depending on their capacities and functionality, is there potential to increase their role as aggregators for capacity building, financial education, and business strengthening, which when combined would contribute to growing the numbers of 'investment ready' small-scale farmers? Where is there greatest potential to work with such associations? Ideally, priority should be given to associations representing growing sub-sectors. This could be poultry, dairy, livestock, cotton, or others to be identified. In this way, there is a strong link between promising agricultural markets (which are attractive to financial suppliers) and 'investment ready' small-scale producers who stand a better potential of accessing finance.

10. Opportunities exist for 'fast-tracking' financial access and inclusion through effective and scalable mobile banking and payment systems models. This study has provided insight into current contextual factors (e.g. high levels of mobile phone usage in rural areas) and highlights current models and their effectiveness. Whilst such models offer solutions to bridging the access-inclusion gap, there is also the need for caution: products and services need to be developed around evidence-based demand; adequate support frameworks for technologies as well as market testing (including analysis of unintended outcomes and supply partner due diligence) are crucial before broader launch; and business cases should include cost-benefit analysis and clearly identify the potential for achieving economies of scale.
11. Constraints to pro-poor sector growth in rural areas extend well beyond access to finance – financial service development therefore has to be coupled with production and market development support (infrastructure, market linkages, skills and knowledge development, etc). Moreover the need for more complete and effective retail infrastructure encompasses market place infrastructure, and as such the need for sound policy and regulation in areas such as branchless banking and payment systems, consumer protection, and legal recourse.

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Appendix I: Emergent suppliers' profiles - products and services

Stanbic bank	

Organisation
 	
• Part of the Standard Bank Group.
• 16 branches nationwide (June 2012).
• Originally focused on big corporate business.
• Renewed focus in the agricultural sector began 2009.
• Agriculture falls under commercial banking.
• Currently 12 relationship managers in the agricultural section.
 	
Focus
• Sector focus: sugarcane, livestock, wheat, maize production, soya beans and coffee.
• Main portfolio clusters are in Makushi, Lusaka (East and West), and Mazabuka. Expanded in to Eastern province in 2011.
• Strategic budget allocation, based on sector growth and performance.
• Gradually broadening its sphere of interest, exploring downstreaming opportunities and most viable market 'entry points'.
	Financial products and services
	
	• Corporate and investment banking, largescale corporate finance.
	• Retail banking, personal and business finance including commercial farmers and SMEs in various sectors.
	• Savings and current accounts.
	• Overdraft facilities and seasonal short term finance.
	• Medium term (three to five years) and long term (five to eight years) capital, odd exceptional case of ten year financing (e.g. for land procurement or dam construction).
	• Guarantee discounting facilities, bank guarantees provided mainly for inputs, discounting fee as a percentage of total.
	• Vehicle and asset financing, including lease financing of up to five years.
	• Collateral management agreements, certificate issued against stored commodity (maize, wheat, soya beans), bank finances up to 60-70% of current price.
	• Global markets, foreign exchange services, market information and advisory services.
	• Non-banking Products and Services
	    • Insurance is not done directly, but handled through the bank assurance section, acts as an intermediary to insurance companies.
	    • Very limited weather-based index insurance.
	    • Fire insurance, available for properties and crops.
	    • Farm property, assets and equipment insurance, offered through a comprehensive 'farm pack' insurance product.
	    • Personal and life insurance.

Standard Chartered Bank	
Organisation • Presence in Zambia since 1906. • Part of the Standard Chartered Group, UK-based, Group is registered on the UK stock exchange. • Present in 18 countries across Africa. • Global presence includes Europe, USA, South America. • Portfolios managed by experienced relationship managers. Focus • Working with top end global corporates, Zambian corporates. • Also working with large and medium scale agribusinesses, includes farming portfolio. • Input financing through 'anchor' clients, working with small-scale farmers primarily through contract buyers. • Financing through FRA, purchase of small-scale farmer maize, self-liquidating loans, release of stock against payment by millers. • Financing Government sponsored input supply firms (up to 80% of business is through SC).	Financial products and services Personal banking. • Deposits: Savings accounts, current accounts, foreign currency accounts. • Cards: Visa credit and debit cards. • Personal loans. SME banking. • Trade and working capital loans. • SME treasury services. Wholesale banking • Transaction banking. • Global markets. • Financial institutions. • Commodity traders and agribusiness. Warehouse Receipting and Storage • Traders (180 days) and millers (270 days). • Main commodities are maize, soya, wheat. Other • Corporate affairs. • Preferred banking. • Priority banking. Non-banking • Insurance: • BancAssurance: Educare plan, hospital plan, funeral plan. • Credit life and travel insurance.

Stanbic Bank and Standard Chartered Bank receive significant strategic guidance and technical assistance from the parent group. For example, Stanbic Bank applies a contextualised version of its South African agricultural finance model to guide its structured market growth in Zambia.

Zanaco Bank	
Organisation • Partnered with Rabobank in 2007 (49% ownership. • 57 branches and agencies nationwide. Focus • Emergent Farmers Finance Support Program (Emergent farmers production and asset financing for scale up). • Zanaco has had the support of Rabo Foundation and IFC specifically to build capacity of the bank's in-house team. Technical expertise is provided 'on the job'. • Intensive support to the emerging farmers being targeted for loans is being provided by private sector agricultural suppliers, farmers' associations and consultancy firms. • Munda credit facility for small-scale farmers. • Lima product for small-scale farmers. Loan paid off through the sale of maize to the FRA; loan groups are handpicked by Zambia National Farmers Union (ZNFU) and farmers have to be a member of the local District Farmers' Association (DFA). The DFAs aggregate the loan need and act to screen eligible farmers. • Zanaco pays the input supplier and the input supplier provides inputs to the DFAs; • Loans are timed for on-time planting (Oct-Nov); DFAs (farmers) harvest and sell their maize to the FRA (Jun– Sept). • Revenues from the sale of maize are used to pay back the loan; the upfront deposit of 50% sitting with the bank is drawn down to make up the balance due to Zanaco Bank. • 'Xapit' mobile telephone banking and transactional services	Financial products and services Retail Banking. • Savings Accounts, current accounts, debit card, personal loans, SMS banking, internet banking, e-timer and bill muster. Agricultural Finance. Zambia Emergent Farmer Credit. • Seasonal overdrafts to finance crop inputs, 5-10 months; Medium term loans to finance agricultural equipment and infrastructure, 3-6 years. Loan size $10,000 - $150,000 or kwacha equivalent. Facility arrangement fee, available in both dollar and kwacha. Interest rates are floating and are subject to change. • Criteria used on issuance of loans: farms are subject to valuation, proven entrepreneurial skills, title to land, minimum farming sizes and assets 10-50 ha arable land, record of farm performance no less than three years, good business proposal concept, minimum equity contribution. Munda credit facility. • Farmer coops and associations (members of NAPSSFZ); members of coops and associations required to put up 50% deposit of total loan sought. • Seasonal loans (12 month loan term) for purchase of seeds or fertilizer; linked with select suppliers. • 20% per annum, fixed rate. Lima small-scale credits focused on maize production. • Upfront deposit of 50% as well as personal guarantees required. • Interest rate is 20% fixed. • The average loan size is approximately US$600. • Support in organizing the marketing and sale of the maize is provided by the local ZNFU and District Level Officer. Xapit • Balance enquiries, Cash withdrawals, Utility bill payments, Money transfers, Mobile phone credit.

FNB	
Organisation • Began operations in Zambia three years ago. • High level of training and technical support from FNB in South Africa for building FNB Zambia agricultural portfolio management capacities. • A team of dedicated mobile agricultural managers (in depth credit analysis expertise), supported by branch-based relationship managers. Focus • Initial focus on deposit-taking only to establish a footprint in-country. • Potential in rural finance extends beyond agricultural finance to creating 'multi-facility' economic zones. • Value chain finance, strategic partnering to reach downstream rather than direct financing. • Broadening value chain finance portfolio (e.g. suppliers, processors, etc) in dairy, livestock, cotton). • Emergent farmer financing for scale up. • Set up an agricultural asset financing unit in January 2012.	Financial products and services • Commercial business finance, including agriculture. • Overdraft facilities. • Business term loans for capital expenditure. Asset financing, including agricultural asset financing. Non-banking products and services • FNB current does not offer insurance, clients have to source for themselves, a requirement for leasing credits (currently support through facilitating partner).

CETZAM Financial Services Ltd	
Organisation • Began agricultural lending in 2009. • Received a loan from DBZ for US$1million for rural agriclutural scale-up. • Approximately 2200 small-scale farmer group credits as of June 2012, representing a portfolio of approximately ZMK4,4billion (US$90,000). • Working in partnership with iDE Zambia and DAPP (and more recently Heifer International and DAZ, still very smallscale). • Rural agricultural loans offered in 13 areas (Lusaka peri urban, Kabwe, Chibombo, Kapiri Mposhi, Serenje, Mkushi, Chirundu, Kafue, Mumbwa, Mpongwe, Masaiti, Choma, Kalomo). • PAR over 30 days 4% though some areas have high instances of non-performing loans (e.g. Chibombo). Focus • Trialing and launching deposit-taking in select branches. • Small-scale irrigation and input supply loans (credit, and part cash). • Exploring replication of model for dairy livestock development credits. • Exploring partnership with Celpay Zambia on electronic payment system for loan replayments (early stages).	Financial products and services • Trust bank loans, solidarity group loans, individual and SME loans. • Small-scale farmer group loans. • Tusunge savings account, attracts 6% pa, unrestricted withdrawals per month, no withdrawal charges, no fees for deposits, minimum opening balance ZMK 20,000, ZMK 10,000 monthly service charged Non-banking products and services • Insurance, credit life and funeral benefits insurance (mandatory, embedded in credit offering). No voluntary insurance as such.

Entrepreneurs Financial Centre (PFSL Zambia)	
Organisation • A deposit-taking MFI licensed and supervised by the Bank of Zambia with a share capital of over ZMK 16 Billion offering specialized financial services to MSMEs. • Has attracted a number of key investors and partners including AfricInvest, Triple Jump, Blue Orchard and Desjardins. • DesJardins has been working with the MFI since 2008 to transform it into a financially sustainable entity and to build its internal capacity in agricultural finance. Focus • Received a loan from DBZ for on lending to small-scale farmers and value chain service providers. • Micro-savings, growing financial base, improving business, enabling access to other product offering.	Financial products and services Credit • Business loans, Market Women Trader, Commercial MSME (individual, working capital and fixed assets). • Business loans extend to agriculture enterprises. • Home improvement loans Savings • Naine micro savers account. No ZMK 10,000.00 fixed monthly fee. Applicable service fees include admission and closing fees. Minimum amount of ZMK 20 000. Unlimited deposits/withdrawals. For savings clients only without loan, account will be converted into a Regular Savings Account if a loan is authorized. • Regular savings account. • Premium savings account. • Term deposit account. Non-banking products and services • ID SMARTCARD, which enhances client information security, promotes business efficiency and offers future potential for use at ATMs and through debit card system providers. • Client share ownership program

Empowerment MFI	
Organisation • Began operations in 2008. • As of 2010, it had two branches and less than 2,000 clients. Focus • The MFI lends predominantly to women • Has a strong track record with respect to repayments.	Financial products and services • Agricultural input loans, Solidarity group loans. • School fee loans. • Salary-based loans.

VisionFund Zambia	
Organisation • Microfinance subsidiary of WorldVision. • Rural operations in: Choma, Chongwe, Kasama and Mbala and Chipata, Monze, Sinazongwe, Solwezi and Lufunyama. Focus • On the rural poor; piggybacks on the work of World Vision in its program development areas (though not exclusive to these areas). • 70% women clientbase.	Financial products and services Asset, household and business (working capital) loans. Providing financial education and consumer protection. Branchless banking through a mobile payment platform. Home improvement and education loans. Value chain financing.

MicroBankers Trust	
Organisation • Re-orientated from wholesale to retail lending in 2001. • Regulated by the BoZ since 2008. • MBT has a provisional license to transform into a deposit-taking institution. • As a Trust MBT falls under the MoCDSS, the MoCDSS is the 'settler'; historically MBT has been a quasi-Government institution; future structure will be as a company limited by shares; legal requirements of this transition are being examined; issues such as retention of the Trust, transition of the Trust and/or new company start-up are under debate. • Consistently loss making as an institution. • Works in urban, rural and peri-urban areas where MBT has its presence: Lusaka, Kafue, Monze, Kabwe, Masaiti-Luanshya, Chingola, Chongwe, Petauke, Chipata, Lundazi and Mongu-Senanga. Focus • Twende group loans focus on women.	Financial products and services • TWENDE loans; interest charged is 60% p.a., reducing balance; loan term is 4 – 12 months; target is women in rural and peri-urban areas. • Individual loan products include the following: - a) Business loans for SMEs; interest is 72% p.a, reducing balance; loan term is up to 12 months. b) Dairy loans (for small-scale dairy farmers); interest is 30% p.a., reducing balance; loan term is up to 24 months c) Small Livestock Loans; targets small-scale farmers that are keeping small livestock i.e. pigs, goats and chickens; interest is 30% p.a., reducing balance; loan is up to 24 months. d) Agricultural equipment loans i.e. (i) Irrigation loans, targeting small-scale farmers that are interested in irrigation farming and have their own land with water (bore hole/dam/stream); interest is 25% p.a., reducing balance); loan term is up to 36 months (ii) Mechanization/Power tiller loans with same conditions as irrigation loans.