

Agricultural Analyses and Design *Analyses Agricoles et Conception*

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RWANDA FINANCIAL SECTOR PROFILE: IMPACT ON AGRIBUSINESS INVESTMENT

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PREFACE

The Agricultural Analyses and Design (AAD) activity is an eight-month design activity undertaken by the Chemonics International RAISE Consortium through funding supplied by USAID/Rwanda. USAID/Rwanda is using this study and design effort to support its Strategic Objective Number Three (SO3) *to increase the ability of rural families in targeted communities to improve household food security*. Specifically, USAID seeks to obtain information and proposed intervention strategies, approaches and activities suitable for USAID/Rwanda's support in achieving the second Intermediate Results under SO3 (IR3.2) *of creating and enhancing internal production / marketing chains that promote broad-based economic growth*. The purpose of AAD, therefore, is to provide USAID/Rwanda directions and information for their use in future development and eventual funding of a project that seeks to revitalize agribusiness in Rwanda and recreate links between the rural sector and private sector traders and processors. This USAID project will achieve its objective by addressing identified constraints and opportunities within the commodity chain for increasing economic growth via agricultural production and agribusiness. The principal task of AAD is to identify these constraints and opportunities.

The Agricultural Analyses and Design activity is divided into three phases. The first phase (two months) is to identify and recommend for in-depth study to USAID/Rwanda those *commodity chains and interventions* that have the most potential for creating increased economic growth, internal and external trade, opportunities for employment and increased income. The second phase (four months) will consist of a number of in-depth studies. Some studies will look at crosscutting issues such as transportation, finance and human capital development. An additional study will look at the creation of Agribusiness Support Centers. The remaining studies will be in-depth analysis of interventions related to commodity chains identified in phase one and selected for study by USAID/Rwanda. The results of these studies will provide the basis for phase three of the activity, the synthesis of the studies done in phase two and development of a technical proposal and supportive design components for USAID/Rwanda's use in developing a request for proposal (RFP) for a project to support IR3.2.

This crosscutting study on finance was completed by Mr. Harry Shutt, financial specialist, during a visit to Rwanda from 16 to 30 November 1999.

EXECUTIVE SUMMARY

This study provides a brief profile of key financial institutions in Rwanda and the extent they impact on investment in the agricultural and rural sectors. Its aim is to provide background information on and analysis of the role of the financial sector in relation to the development of agricultural and related activities in Rwanda.

PROFILES OF LENDING INSTITUTIONS

1) Banques Populaires

The Union des Banques Populaires de Rwanda was founded in 1975. It is organized on the basis of autonomous entities which are cooperatively owned and managed by their members / depositors. Because of its nationwide presence in rural areas the impact of the 1994 war was particularly catastrophic for the Union. The Union was able to resume operations from the end of 1995, permitting it to increase the number of member banks to 135 by end-1998, with a total of just over 162,000 individual members. The Union's national management is currently pursuing an extremely conservative lending strategy. This translates into a portfolio of assets of which no less than 45 per cent comprises of: a) deposits with the National Bank and other commercial banks, and b) treasury bills, with loans to members accounting for only 42 per cent of the total.

The Union's funds consist predominantly of members' deposits, which totaled Rwf 7.3 bn. Despite the fact that farmers account for 43 per cent of all deposits their share of total credits outstanding at end-1998 - including emergency pre-harvest loans (credits de soudure) - was only 8 percent. The policy of the national management of BP is to discourage advancing credits without the provision of sufficient collateral by the borrowers - equal in value to most of the sum borrowed. How this policy is followed naturally varies from one member bank to another, bearing in mind the autonomy of each unit in approving loans. Each member bank is responsible for appraising loan applications made to it. Because of this, there is felt to be a danger of significant abuse or mislending by local managements.

2) Banque Commerciale de Rwanda (BCR)

The BCR, founded in 1963, is the largest of the five commercial banks in Rwanda. As of end-1998 it had total assets of Rwf 40.2 bn (\$ 121.6 mn). BCR was previously wholly state-owned, its shares are now split between the government (45 per cent), Bank Bruxelles Lambert of Belgium (42 per cent) and private Rwandan shareholders (13 per cent) Aside from capital and reserves the bank's resources are derived from individual deposits and those made by other banks and financial institutions. There is concern that the growth of deposits has started to level off since 1998, as real personal disposable incomes have been squeezed. Lending to agricultural and related enterprises presently accounts for less than 5 per cent of all outstanding loans. Nearly all of these are for livestock enterprises in the vicinity of Kigali. One of the reasons for this low level of lending is the lack of capacity for appraising and supervising loans in more remote areas. Non-livestock projects are generally perceived as unable to offer adequate security relative to the risks involved. There appear to be no rigid requirements for collateral, mainly because the difficulty of foreclosing on or disposing of many of the assets against which loans are nominally secured often means that collateral is

somewhat theoretical. Although seemingly quite well equipped at head office, in terms of both human and other resources, to appraise and supervise loans, the BCR is seriously handicapped in relation to the management of loans away from the capital. Management lays particular emphasis on the need to a) access new sources of funds, b) increase its capacity to service the rural economy. In this connection it has sought (so far unsuccessfully) to develop collaboration with the Banques Populaires, with a view to combining the latter's extensive national network and proximity to rural communities with its own greater banking expertise, c) diversify further into profitable financial services other than lending, such as international money transfer (Western Union) and insurance.

3) **Banque de Commerce, de Développement et d'Industrie (BCDI)**

The BCDI is the third largest of the five commercial banks in Rwanda. As of end-1998 it had total assets of Rwf 16.2 bn (\$ 49.2 mn) and its loan portfolio accounted for some 15 per cent of all commercial lending in the country. However, the fact that around half of outstanding loans were in the form of overdrafts to depositors reflects a very weak demand for commercial borrowing and a general deterioration in the economy. Because of the weak demand for credit the bank actually felt obliged to turn away deposits from institutional investors in 1998.

Lending to agricultural and related enterprises presently accounts for less than 1 per cent of all outstanding loans (excluding seasonal credit for coffee marketing). BCDI management indicated that they normally require collateral equal to as much as 130 per cent of the value of any loan. The main emphasis for management of BCDI appears to be on the need to develop profitable financial services other than lending, notably automatic cash dispensing and money transfer (ATM and POS machines).

4) **Banque Rwandaise de Développement (BRD)**

Founded in 1967, the BRD is Rwanda's only development bank. As such it differs from commercial banks in being able not only to adopt less rigidly commercial criteria in its lending policy but also to take minority equity stakes in enterprises it is supporting with loans. The difficult market conditions still confronting the bank were reflected in a more than halving of its earnings compared with 1997 due to an increase in the level of provisions made against bad and doubtful investments. In addition to its share capital and reserves, the bank has undertaken long-term borrowing predominantly from foreign development finance institutions. Of total new investments approved in 1998 only 15 per cent by value were in the agricultural and related sectors, compared with an average of 34 per cent in the preceding four years. Within these sectors the main sub-sectors in which resources have been concentrated are livestock and dairy production and flower cultivation for export. The BRD no longer gives loans for small projects. Normally a minimum security of 30-40 per cent of the total investment amount is preferred.

With a view to expanding its participation in the agro-industrial sector, the BRD is examining the possibility of investing in: agro-processing projects, including grain milling for the brewery sector and rehabilitation of existing sugar and tomato paste enterprises, and a leasing company which could make equipment available to small and medium rural and other enterprises at minimal capital cost to the latter (e.g. tractors, dairy equipment).

5) World Vision / Amizero (NGO)

Amizero has been created by World Vision as an entity to distribute micro loans to individuals organized in groups on the basis of a revolving fund. Amizero is entirely dependent for funds on sums contributed by the various overseas branches of its parent organization. Since the Amizero is not a bank, it is unable to accept deposits from private individuals, although it can accept funds from other development agencies.

All loans are within the range \$200-400 and are for 6-8 months. The reason for these limitations, which are subject to review, is the small amount of funds available. Currently Amizero has outstanding loans equivalent to \$71,000, loaned to 600 beneficiaries. Agriculture-related lending has thus far been avoided both because it is considered too risky and because those operations which seem potentially most viable – notably dairy production – require larger sums for longer periods than the entity is able to consider within its present limitations. Not collateral is required for loans. The main priority at present is to expand the total number of loan beneficiaries to 2000 by September 2000.

6) Banque Nationale du Rwanda (BNR)

As the central bank, the BNR is responsible not only for bank regulation but, unusually among the countries of sub-Saharan Africa, for the conduct of monetary policy. To date the BNR has shown little sign of treating rural sector finance as a matter of priority concern. This stance, however, may be about to change. There are indications that the BNR may be intending to adopt a more proactive role towards investment promotion in the economy generally.

THE POTENTIAL FOR INCREASED PRIVATE INVESTMENT IN THE AGRICULTURAL AND RELATED SECTORS

The principal constraints identified are (not necessarily in order of importance):

- 1) Low level of farm / rural household incomes, partly related to the small size of most agricultural holdings and the consequent difficulty of producing a marketable surplus;
- 2) Limited cultural awareness among the rural population of the obligations involved in borrowing money, not least because of the widespread tendency of NGOs and other donors to distribute funds on a non-reimbursable basis (particularly in the aftermath of the 1994 genocide);
- 3) Inadequate banking infrastructure in rural areas, leading to difficulties in processing and supervising loans and associated high transaction costs;
- 4) Deficiencies in, or even total absence of, other key links in the production / marketing chain, e.g. input supply, extension, storage, transport;
- 5) Low, and in some cases declining, real prices for marketed commodities;
- 6) Strong risk aversion because of past losses (not only resulting from war) and persistently unfavorable or uncertain market conditions in different sectors (e.g. road haulage).

More broadly, it seems clear that the most essential requirement for facilitating the mobilization of funds for productive investment (agricultural or otherwise) in Rwanda is to take steps to improve the overall investment climate, whether at sartorial or macro-economic level. It is clearly beyond the scope of the present exercise to determine the type or scale of policies or interventions that might be necessary to achieve this. However, there can be no doubt that, in order to promote appropriate investment in agro-related activities detailed and up-to-date information on the cost and revenue structures (from crop planting to the final markets of processed products) must be assembled. In the absence of such information measures to support individual product chains are likely to be wasteful and ineffective and any enterprise investment largely speculative.

LE SOMMAIRE EXECUTIF

La présente étude offre un aperçu des principales institutions financières au Rwanda et de la façon dont elles influent sur l'investissement dans les secteurs agricole et rural. Elle se propose d'analyser et de donner des informations générales sur le rôle du secteur financier dans le développement des activités agricoles au Rwanda.

PRESENTATION DES INSTITUTIONS DE PRET

1) Banques populaires

L'Union des Banques populaires du Rwanda a été créée en 1975. Elle est composée d'entités autonomes gérées en coopérative par les membres ou les déposants. Représentée dans toutes les zones rurales du pays, les conséquences de la guerre de 1994 ont été particulièrement catastrophiques pour l'Union. Elle a repris ses activités à la fin de 1995, s'agrandissant au point de se retrouver avec 135 banques affiliées à la fin de 1998, comptabilisant un total d'un peu plus de 162 000 membres. La direction nationale de l'Union applique actuellement une politique de prêt extrêmement conservatrice ; ce qui se traduit par un portefeuille d'actifs dont au moins 45 % sont constitués de :

- a) dépôts à la Banque nationale et dans les autres banques commerciales ;
- b) bons du trésor, avec des prêts accordés aux membres équivalents à seulement 42 % du total.

Les fonds de l'Union sont principalement constitués des dépôts des membres, équivalents à 7,3 milliards de FRW. Les dépôts des paysans représentent 43 % de la totalité des dépôts, et pourtant les crédits qui leur étaient accordés n'étaient, à la fin de 1998, que de 8 %, y compris les crédits de soudure. La direction de la BP a comme politique de ne pas accorder de crédits si les garanties sont insuffisantes, en effet elles doivent correspondre à la majorité de la somme empruntée. Evidemment, cette politique diffère d'une banque à l'autre, car chaque entité est autonome en matière de prêts. Chaque banque doit évaluer elle-même ses demandes de prêts. C'est pour cette raison que des abus sont à craindre ainsi que le risque d'accorder des prêts aventureux.

2) Banque commerciale du Rwanda (BCR)

Créée en 1963, la BCR est la plus importante des cinq banques commerciales du Rwanda. A la fin de 1998, elle comptait 40,2 milliards de FRW en actifs (soit 121,6 millions de dollars US). Auparavant, la BCR était une banque d'Etat. Aujourd'hui, l'Etat détient 45 % d'actions, la Banque Bruxelles Lambert de Belgique, 42 % et les actionnaires privés rwandais, 13 %. En dehors des capitaux et des réserves, la banque tire ses ressources des dépôts des particuliers et des banques et autres institutions financières. La situation est préoccupante car, depuis 1998, le niveau des dépôts tend à se stabiliser, les revenus réels des personnes ayant baissé. Actuellement, les prêts aux sociétés agricoles ou dont les activités sont liées à l'agriculture représentent moins de 5 % de la totalité des prêts accordés. Ces prêts ont été pratiquement tous accordés à des entreprises de bétail aux environs de Kigali. L'une des raisons de cette faiblesse des prêts est l'absence des moyens d'évaluation et de contrôle des prêts dans les

zones éloignées. On considère, en général, que les projets non liés au bétail n'offrent pas suffisamment de garantie par rapport aux risques encourus. Il semble ne pas y avoir de conditions de garantie rigides, ceci surtout parce qu'il est difficile de saisir ou de disposer de la plupart des biens servant de caution nominale aux prêts ; ce qui signifie souvent que la garantie est plutôt théorique. Même si au siège, la BCR semble disposer des ressources humaines et autres nécessaires à l'évaluation et au contrôle des prêts, elle rencontre de grandes difficultés pour ce qui est des prêts accordés en dehors de la capitale. Les préoccupations majeures de la direction sont :

- a) d'accéder à de nouvelles sources de financement ;
- b) d'augmenter ses capacités de services en direction de l'économie rurale. A cet égard, elle a cherché, jusque-là sans succès, à établir une collaboration avec les Banques populaires, en vue d'allier leur réseau national étendu et leurs relations avec les collectivités rurales à sa plus grande expertise bancaire ;
- c) de diversifier davantage les services financiers rentables autres que le prêt, tels que les transferts internationaux d'argent (Western Union) et les assurances.

3) Banque du Commerce, du développement et de l'industrie (BCDI)

La BCDI est la troisième banque commerciale du Rwanda. A la fin de 1998, elle totalisait 16.2 milliards de FRW d'actifs (soit 49,2 millions de dollars US) et son portefeuille de prêts représentait environ 15 % de la totalité des prêts commerciaux du pays. Cependant, environ la moitié de ces prêts était sous forme de découverts des déposants, ce qui reflète une très faible demande pour l'emprunt commercial et une détérioration générale de l'économie. En raison de la faible demande de crédits, la banque a été obligée, en 1998, de refuser les dépôts d'investisseurs institutionnels.

Les prêts aux entreprises agricoles ou dont les activités sont liées à l'agriculture représentent moins de 1 % de la totalité des prêts accordés (excepté le crédit saisonnier pour la vente du café). La BCDI demande en général des garanties équivalentes à au moins 130 % de la valeur d'un prêt. La préoccupation majeure de la BCDI semble être de créer des services financiers rentables autres que les prêts, notamment le retrait automatique d'argent et les transferts d'argent (ATM et machines PDV).

4) Banque rwandaise de développement (BRD)

Créée en 1967, la BRD est la seule banque de développement. En tant que telle, elle est différente des autres banques commerciales car elle peut non seulement adopter des critères commerciaux moins rigides dans sa politique de prêts, mais également prendre des capital actions minoritaires dans les entreprises auxquelles elle accorde des prêts. En raison de la difficile situation que connaissent les banques, elle a perdu plus de la moitié de ses profits par rapport à 1997, car les dépôts de garantie contre les mauvais investissements et les investissements à risques ont augmenté. Outre ses capital actions et ses réserves, la banque s'est engagée dans les emprunts à long terme, principalement auprès des institutions financières de développement à l'étranger. Sur la totalité des nouveaux investissements approuvés en 1998, seuls 15 % correspondaient aux secteurs agricoles et liés à l'agriculture, contre une moyenne de 34 % pour les quatre années précédentes. Les principaux sous-secteurs qui ont accaparé les ressources sont le bétail, la production laitière et la culture des

fleurs d'exportation. La BRD n'accorde plus de prêts aux petits projets. En général, il est préférable d'avoir une garantie minimale correspondant à 30 à 40 % de la totalité de la somme investie.

Dans le but d'augmenter sa participation dans le secteur agro-industriel, la BRD étudie la possibilité d'investir dans :

- des projets de transformation des produits agricoles, y compris la mouture du grain pour la brasserie et la restructuration des entreprises existantes de sucre et de purée de tomate ;
- une société de location qui pourrait mettre le matériel à la disposition des entreprises moyennes rurales et autres à un coût réduit (par exemple les tracteurs, l'équipement pour le lait).

5) World Vision / Amizero (ONG)

Amizero a été créé par la World Vision comme une organisation chargée de répartir les micro-prêts à des personnes organisées en groupes sur la base de fonds renouvelables. Pour son financement, Amizero dépend entièrement des fonds envoyés par les filiales étrangères de son organisation mère. Amizero n'étant pas une banque, elle ne peut pas accepter de dépôts des personnes privées, en revanche, elle peut accepter des fonds des agences de développement.

Les prêts entre 200 et 400 dollars US sont accordés pour 6-8 mois. Ces restrictions, qui doivent être étudiées, sont dues à la faible quantité de fonds disponibles. Actuellement, Amizero a accordé des prêts équivalents à 71 000 dollars US à 600 bénéficiaires. Pour l'instant, les prêts à l'agriculture sont rejetés car considérés comme trop risqués et parce que ces activités qui semblent plus viables –notamment la production laitière- nécessitent des sommes très importantes empruntées pour de longs délais que l'organisation n'est pas prête à envisager dans le cadre des restrictions actuelles. Aucune garantie n'est exigée pour les emprunts. La priorité principale est pour l'instant de porter le nombre de bénéficiaires à 2 000 d'ici septembre 2000.

6) Banque nationale du Rwanda (BNR)

En sa qualité de banque centrale, la BNR est chargée non seulement de réglementer le secteur bancaire, mais aussi, cas exceptionnel en Afrique au sud du Sahara, de l'application de la politique monétaire. A ce jour, la BNR a montré peu d'empressement à considérer le secteur financier rural comme une priorité. Cette attitude, cependant, pourrait changer. Certains signes montrent que la BNR pourrait adopter un rôle plus actif dans le développement des investissements dans l'économie en général.

POSSIBILITES D'ACCROITRE LES INVESTISSEMENTS PRIVES DANS LES SECTEURS AGRICOLES ET CONNEXES

Les principaux problèmes relevés sont (pas nécessairement par ordre d'importance) :

- le faible revenu des ménages paysans, en partie en raison de la petite taille des exploitations agricoles et de la difficulté qui s'ensuit de produire un excédent commercialisable ;
- le manque d'information de la population rurale sur les conditions d'emprunt, car les ONG et autres donateurs ont généralement tendance à distribuer des financements sur une base non remboursable (notamment après le génocide de 1994) ;
- les infrastructures bancaires insuffisantes dans les zones rurales, entraînant des difficultés dans le traitement et le contrôle des prêts et des coûts élevés des transactions connexes ;
- l'insuffisance, voire l'absence totale de certains maillons dans la chaîne de production/commercialisation, par exemple la fourniture d'intrants, l'extension, le stockage, le transport ;
- les prix faibles, et parfois en baisse, des matières premières commercialisables ;
- la crainte de prendre des risques en raison des pertes enregistrées par le passé (pas seulement à cause de la guerre) et la persistance des conditions de marché incertaines ou non favorables dans les différents secteurs (par exemple le transport routier).

De manière générale, il est clair que la condition sine qua non permettant de mobiliser facilement des fonds pour un investissement rentable (que ce soit dans le secteur de l'agriculture ou non) au Rwanda, est de prendre des mesures visant à améliorer les conditions générales d'investissements, que ce soit au niveau local ou plus général. Il est impossible dans le cadre de cette étude de déterminer le type ou l'étendue des mesures à prendre ou des actions à mener pour atteindre cet objectif. Cependant, il ne fait aucun doute que pour favoriser des investissements suffisants dans les activités liées à l'agriculture, il est nécessaire de disposer d'informations complètes et actuelles sur la répartition des coûts et des recettes (des semences à la commercialisation des produits transformés). Tant que ces informations feront défaut, les mesures d'aide aux chaînes de produits risquent d'être peu profitables et les investissements des entreprises en grande partie spéculatifs.

SECTION I. PROFILES OF LENDING INSTITUTIONS

This report's aim is to provide background information on and analysis of the role of the financial sector in relation to the development of agricultural and related activities in Rwanda. Based on this analysis it also seeks to identify areas of possible intervention which might be included in an RFP to be drawn up for a project to support USAID/Rwanda's IR3.2. However, it should be stressed that it was not possible to develop any detailed proposals for USAID interventions in the context of the present rapid exercise, and that further work will be needed in order to formulate properly elaborated proposals.

In line with the terms of reference, the study incorporates profiles of key financial institutions based on interviews with senior management and analysis of financial reports where available. In the case of the micro-finance sector it was not possible to interview more than one institution – not necessarily representative – in the time available.

PROFILES OF LENDING INSTITUTIONS

A. Banques Populaires

The Union des Banques Populaires de Rwanda was founded in 1975 by a Swiss credit union organization, which continued to provide the Union with technical support and subsidies until 1980. In line with principles of credit unions (as pioneered in 19th century Germany by Friedrich Raiffeisen) it is organized on the basis of theoretically autonomous entities which are cooperatively owned and managed by their members / depositors. By 1994 (before the outbreak of war) the Union had extended its operations throughout the country, so that it comprised 131 associate banks. Because of its nationwide presence in rural areas (unique among banking institutions in Rwanda) the impact of the war was particularly catastrophic for the Union. However, with government help, as well as that of the Swiss government and the World Bank, the Union was able to resume operations from the end of 1995, permitting it to increase the number of member banks to 135 by end-1998, with a total of just over 162,000 individual members (depositors). Because of the damage to its balance sheet resulting from the war, compounded by a substantial volume of bad debts resulting from earlier management weakness, the Union's national management is currently pursuing an extremely conservative lending strategy. This translates into a portfolio of assets of which no less than 45 per cent comprises: a) deposits with the National Bank and other commercial banks and b) treasury bills. Loans to members accordingly account for only 42 per cent of the total (Rwf 4.6 bn out of Rwf 10.6 bn).

1. Sources of funds

The Union's loanable funds consist predominantly of members' deposits, which totaled Rwf 7.3 bn (69 per cent of total net liabilities) as of end-1998. Although it has been offered at least one line of credit - \$0.4 mn from IFAD, to be targeted at agro-processing and related marketing enterprises – this, not surprisingly, has been declined, since the Union is at present unable to advance more than about 40 per cent of its deposits in credits to its members consistent with its strict lending criteria (especially in respect of collateral).

2. Rural sector loan portfolios

Despite the fact that farmers account for 43 per cent of all deposits, their share of total credits outstanding at end-1998 - including emergency pre-harvest loans (credits de soudure) – was only 8 per cent, amounting to Rwf 361 mn (just over \$1 mn). Their share of new credits advanced in 1998 was slightly higher at 9.3 per cent, although this was lower than the share in 1992 (the last year for which records exist prior to 1998) of 10.8 per cent. This decline in the share of new credits, it should be noted, was entirely accounted for by a virtual halving in the value of seasonal credits for coffee growers over the period. In contrast the value of other new credits to farmers rose by around 20 per cent (in nominal terms) over the period, whereas the total of all new credits advanced by the Banques Populaires was almost 20 per cent lower in 1998 than in 1992.

3. Collateral / equity requirements

While the policy of the national management is to discourage advancing credits without the provision of sufficient collateral by the borrowers – equal in value to most of the sum borrowed – the extent to which this is followed naturally varies from one member bank to another, bearing in mind the autonomy of each unit in approving loans. The extent of such variation as between the different BPs is impossible to determine without the benefit of an in-depth survey, although it is understood that there are even instances of totally unsecured lending. However, it seems that individual bank managements are conscious of the need to minimize the risk of insolvency, bearing in mind that they cannot now expect to be bailed out by the Union if they get into difficulties. On the other hand, mindful perhaps of the inadequate level of lending relative to the size of deposits, the Union's management has initiated an examination of collateral requirements with a view to making them as flexible as possible.

4. Loan management capacity

Each member bank is responsible for appraising loan applications made to it. At the same time, in keeping with the principles of credit unions, each member/depositor of a local bank is supposed to participate, directly or indirectly, in the process of loan approval and management through the Supervisory Committee. In reality, however, this practice appears to have fallen into disuse in many instances (according to the Union's annual report) due to a decline in the training effort among members – occasioned by the disruptive effects of the war and a related weakening in the cooperative spirit. Because of this, there is felt to be a danger of significant abuse or mislending by local managements – in a situation where there is severe pressure to disburse finance in rural areas - threatening efforts to clean up BP balance sheets.

5. Strategy development

The main priority of the national management is to enhance the efficiency and security of existing operations rather than to expand lending in any specific areas. For this reason it is seeking external support for a) staff training and b) rural insurance (to enhance the security of farm loans).

6. Other potential sources of finance

As indicated above, the BP are at present less concerned with accessing additional funds than with finding ways to put their existing funds to more effective and more profitable use, notably in relation to the rural sector which is currently such an important source of their deposits. Once some progress has been made in this direction the Union's management will probably feel more able to entertain offers from IFAD and others for lines of credit, whether specifically targeted to the agricultural and related sectors or not.

B. Banque Commerciale de Rwanda (BCR)

The BCR, founded in 1963, is the largest of the five commercial banks in Rwanda. As of end-1998 it had total assets of Rwf 40.2 bn (\$ 121.6 mn) and accounted for some 35 per cent of all commercial lending in the country (a similar market share to that of the Banque de Kigali, the second largest bank). Previously wholly state-owned, its shares are now split between the government (45 per cent), Bank Bruxelles Lambert of Belgium (42 per cent) and private Rwandan shareholders (13 per cent). Following a recent independent audit of the bank requested by the National Bank it has been estimated that a minimum of about Rwf 3 bn of new capital is needed both to cover loan loss provisions and to meet the new minimum capital requirement specified under the new banking law – Rwf 1.4 bn (\$ 4 mn). It is assumed that this additional equity finance will have to be injected by the existing shareholders.

1. Sources of funds

Aside from capital and reserves, the bank's resources are derived from individual deposits (Rwf 27.5 bn as of end-1998) and those made by other banks and financial institutions (Rwf 3.6 bn). There is concern that the growth of deposits has started to level off since 1998, as real personal disposable incomes have been squeezed.

2. Rural sector loan portfolios

Lending to agricultural and related enterprises presently accounts for less than 5 per cent of all outstanding loans. Nearly all of these are for livestock enterprises in the vicinity of Kigali. This is because of the lack of capacity for appraising and supervising loans in more remote areas (see below) and the non-availability of livestock insurance. Non-livestock projects are generally perceived as unable to offer adequate security relative to the risks involved. In addition to these outstanding loans the BCR provides over 40 per cent of short-term finance for the coffee crop.

3. Collateral / equity requirements

There appear to be no rigid requirements, mainly because the difficulty of foreclosing on or disposing of many of the assets against which loans are nominally secured often means that collateral is somewhat theoretical. Thus, for example, leasehold title to land on which real estate loans are secured will normally only be granted by the government (the owner of the freehold) when building has been completed - due to the authorities' anxiety to discourage land speculation. Likewise many of the trucks on which transport loans are secured are

currently almost unsaleable because of the low profitability of this sector under present conditions and the excess stocks of new vehicles held by local distributors. In order to overcome these general constraints to secured lending the government has set up a number of "guarantee funds" – equivalent to rediscount facilities – which involve the government effectively underwriting loans to defined sectors (to date not including agriculture).

4. Loan management capacity

Although seemingly quite well equipped at head office, in terms of both human and other resources, to appraise and supervise loans, the BCR is seriously handicapped in relation to the management of loans away from the capital. This is only partly because of the small number of branches (5) in the provinces, but rather due to the difficulty of getting adequately qualified staff to live in these regions. Hence all loan applications are presently required to be processed at head office.

5. Strategy development

Management lays particular emphasis on the need to

- Access new sources of funds (see below);
- Increase its capacity to service the rural economy. In this connection it has sought (so far unsuccessfully) to develop collaboration with the Banques Populaires, with a view to combining the latter's extensive national network and proximity to rural communities with its own greater banking expertise;
- Diversify further into profitable financial services other than lending, such as international money transfer (Western Union) and insurance.

6. Other potential sources of finance

Aside from the substantial funds needed to restructure its balance sheet, the BCR is hoping to receive funds under one or more lines of credit currently under preparation by the European Investment Bank. However, it is understood that these are likely specifically to exclude agriculture from their sectoral coverage.

C. Banque de Commerce, de Développement et d'Industrie (BCDI)

The BCDI is the third largest of the five commercial banks in Rwanda. As of end-1998 it had total assets of Rwf 16.2 bn (\$ 49.2 mn) and its loan portfolio (Rwf 8 bn) accounted for some 15 per cent of all commercial lending in the country. However, the fact that around half of outstanding loans were in the form of overdrafts to depositors reflects a very weak demand for commercial borrowing and a general deterioration in the economy. The ownership of its shares is entirely in the private sector. Existing capital and reserves (shareholders' funds) amount to Rwf 1.04 mn, of which Rwf 649,000, or around \$ 2 mn, is subscribed capital. Notwithstanding the bank's conservative lending criteria (see below) it has recently had to make a substantial increase in provisions against bad debt, bringing the cumulative total to Rwf 1.2 bn (17 per cent of its loan portfolio) as of end-1998.

1. Sources of funds

Aside from capital and reserves the bank's resources are derived from individual deposits (Rwf 14.2 bn as of end-1998) and those made by other banks and financial institutions (Rwf 0.3 bn). Because of the weak demand for credit the bank actually felt obliged to turn away deposits from institutional investors in 1998.

2. Rural sector loan portfolios

Lending to agricultural and related enterprises presently accounts for less than 1 per cent of all outstanding loans (excluding seasonal credit for coffee marketing). In order to try and develop its portfolio in the rural sector the bank is beginning to provide technical assistance to some of the Banques Populaires in respect of the preparation of loan applications.

3. Collateral / equity requirements

BCDI management indicates that they normally require collateral equal to as much as 130 per cent of the value of any loan. This is doubtless a factor contributing to their difficulty in finding lending opportunities.

4. Loan management capacity

Like the BCR the BCDI is seriously handicapped in relation to the management of loans outside the capital. Also like BCR it is attempting to remedy this through collaboration with the Banques Populaires and training of the latter's officers in rural areas.

5. Strategy development

The main emphasis appears to be on the need to develop profitable financial services other than lending, notably automatic cash dispensing and money transfer (ATM and POS machines).

6. Other potential sources of finance

As noted above, the BCDI management has been trying, if anything, to reduce rather than increase its liabilities in the current unfavorable banking climate. Hence it is only likely to be interested in accepting any lines of credit – whether for agriculture or any other sector – if a high proportion of the funds are subject to a de facto official guarantee.

D. Banque Rwandaise de Développement (BRD)

Founded in 1967, the BRD is Rwanda's only development bank. As such it differs from commercial banks in being able not only to adopt less rigidly commercial criteria in its lending policy but also to take minority equity stakes in enterprises it is supporting with loans. Like all other financial institutions the bank suffered severe losses as a result of the tragic events of 1994, since when it has had to be substantially recapitalised. Its accounts for the year ended December 1998 show it had assets of Rwf 6.6 bn (\$ 20 mn), of which 39 per

cent comprised outstanding loans and 13 per cent equity investments. The difficult market conditions still confronting the bank were reflected in a more than halving of its earnings compared with 1997 (to Rwf 246 mn) due to an increase in the level of provisions made against bad and doubtful investments. The bank's share capital (Rwf 1.5 bn) is 55 per cent owned by the Rwandese state and other public sector bodies, with 34 per cent being held by foreign financial institutions (predominantly parastatal) and the remainder by 17 local financial institutions and other private enterprises.

1. Sources of funds

In addition to its share capital and reserves (totaling Rwf 2.7 bn), the bank has borrowings of Rwf 2.8 bn. The latter are predominantly long-term – i.e. at least 15 years – and are all from foreign development finance institutions - principally African Development Fund, IDA and KfW (Germany) - or the National Bank, bearing below-market interest rates.

2. Rural sector loan portfolios

Of total new investments approved in 1998 only 15 per cent by value (Rwf 258 mn) were in the agricultural and related sectors, compared with an average of 34 per cent in the preceding four years. Within these sectors the main sub-sectors in which resources have been concentrated are livestock and dairy production and flower cultivation for export (Highland Flowers, in which the bank has its only agro-related equity investment). In contrast to the pre-1994 position, when the bank had 3 branches in the provinces (all now closed), it no longer gives loans for small projects, a factor which obviously limits its capacity to support the rural sector, where the vast majority of enterprises are relatively small.

3. Collateral / equity requirements

Normally a minimum security of 30-40 per cent of the total investment amount is preferred. However, this may be less in cases where management has demonstrated a sound record of cash flow management, particularly where the client concerned has repaid earlier loans on time.

4. Loan management capacity

The bank's management considers it lacks adequate capability in respect of loan supervision. This is bound to be a particular handicap in relation to rural sector lending, since transaction costs incurred in appraising and administering such loans are inevitably above average – especially in view of the closure of BRD branches outside Kigali. The extent of this constraint is illustrated by the fact that all 20 dairy farms being supported by the bank are located close to Kigali.

5. Strategy development

With a view to expanding its participation in the agro-industrial sector the BRD is examining the possibility of investing in

- Agro-processing projects, including grain milling for the brewery sector and rehabilitation of existing sugar and tomato paste enterprises;

- A leasing company which could make equipment available to small and medium rural and other enterprises at minimal capital cost to the latter (e.g. tractors, dairy equipment).

6. Other potential sources of finance

The bank is in continuous discussion with the foreign development finance institutions that are its traditional financial backers with a view to maintaining or increasing lines of credit. It would appear that there will be little problem in obtaining funds from these sources for projects, which can be shown to have a reasonable prospect of attaining viability.

E. World Vision / Amizero (NGO)

Amizero has been created by World Vision (leading foreign-controlled NGO) as an entity to distribute micro loans to individuals organized in groups – along similar lines to the Grameen Bank of Bangladesh - on the basis of a revolving fund.

1. Sources of funds

In effect the entity is entirely dependent for funds on sums contributed by the various overseas branches of its parent organization (principally in North America and the UK), although the deposits provide a tiny additional source that borrowers are required to make as part of the terms of their loan repayment. Since the entity is not a bank it is unable to accept deposits from private individuals, although it can accept funds from other development agencies.

2. Rural sector loan portfolios

All loans are within the range \$200-400 and are for 6-8 months. The reason for these limitations, which are subject to review, is the small amount of loanable funds available through the parent organization and the desire to benefit as large a number of recipients as possible. The total amount currently outstanding is equivalent to \$71,000, loaned to 600 beneficiaries. The preferred sectors are small retail or service enterprises (e.g. carpentry). Agriculture-related lending has thus far been avoided both because it is considered too risky and because those operations which seem potentially most viable – notably dairy production – require larger sums for longer periods than the entity is able to consider within its present limitations.

3. Collateral / equity requirements

Not required. The sole “guarantee” of repayment is the solidarity and commitment of the group to ensuring each member’s loans are repaid on schedule.

4. Loan management capacity

Loans are appraised and administered by trained agents, each of whom operates in a defined area (travelling to meet clients by motor cycle). At present there are five such agents, of whom two cover Kigali-Ville. These agents, who are graduates of commercial school, are

trained by means of a training module, which the entity hopes to develop into a package, which can be made available (for a fee) to other organizations planning to offer microfinance.

5. Strategy development

The main priority at present is to expand the total number of loan beneficiaries to 2000 by September 2000. Once this goal is achieved and assuming more funds become available it is hoped to make slightly larger loans for longer periods, including ones for small-scale agricultural and agro-industrial projects.

6. Other potential sources of finance

As noted above, Amizero is in principle able to accept funds from other development agencies, and has already formulated requests for such support.

F. Banque Nationale du Rwanda (BNR)

As the central bank the BNR is responsible not only for bank regulation but, unusually among the countries of sub-Saharan Africa, for the conduct of monetary policy. Furthermore, like the central banks of many other developing countries, it has a key role in acting as a conduit for official development finance to the domestic economy – through commercial and other banks – from both the national government and international financial institutions and development agencies such as the World Bank. Thus the BNR obviously has a crucial role in official efforts to ensure a balance between the often conflicting demands of maintaining a sound banking system and making available sufficient affordable finance to meet the needs of a poor and severely damaged economy.

1. Regulatory role

In the continuing climate of extreme economic fragility since 1994 the BNR has been called on to maintain strong vigilance against a renewed weakening of the banking sector, whose balance sheets are still suffering the effects of losses resulting from the 1994 conflict. Thus, in the context of Rwanda's ESAF programme agreed with the IMF, it has undertaken external audits of the commercial banks and at the same time has been required to enforce tighter prudential standards for the banking sector, including proper provisioning for bad or doubtful loans, under the terms of the new Banking Law enacted in July 1999. It appears to be the official assumption that, by thus compelling banks to clean up their balance sheets and move towards international norms on capital adequacy, this process will enable the banking sector to meet the financing needs of the economy from a position of greater security. However, to the extent that bank shareholders perceive the opportunities for profitable lending to be limited relative to the continuing risks, they may be even more restrictive in their lending policies than at present, even assuming they prove willing to inject the extra capital needed to comply with the new standards.

2. Rural sector support

To date the BNR has shown little sign of treating rural sector finance as a matter of priority concern. However, this stance may be about to change, as evidenced by

- The recent designation of the BNR as intermediary for credits to be disbursed under the World Bank-financed Agricultural and Rural Market Development Project;
- Its expression of concern at the need to facilitate adequate financing of key export sectors (notably in respect of coffee replanting);
- Consideration of a guarantee fund for agriculture comparable to similar facilities already created for other sectors;
- Commissioning of a study on the cooperative / mutual banking sector, with a view to enabling it to serve the rural economy more effectively.

3. Strategy development

There are indications that the BNR may be intending to adopt a more proactive role towards investment promotion in the economy generally, in so far as

- it is developing the regulatory framework for the creation of venture capital institutions;
- it is understood to be considering the possible creation within its own organization of a Development Finance unit – along the lines of a similar entity set up by the Bank of Uganda.

SECTION II. THE POTENTIAL FOR INCREASED PRIVATE INVESTMENT IN THE AGRICULTURAL AND RELATED SECTORS

Based on the information gathered by the consultant on the performance and policies of the main financial institutions in relation to agro-related lending and investment it is clear that there are a number of major constraints inhibiting greater participation in the sector by banks and other investing organizations. It is equally clear that, while some of these constraints relate to deficiencies in the capacity and performance of the banks themselves, structural weaknesses in the rural economy and unfavorable conditions in the wider economic environment are at least as significant factors. The principal constraints identified are (not necessarily in order of importance):

- Low level of farm / rural household incomes, partly related to the small size of most agricultural holdings and the consequent difficulty of producing a marketable surplus;
- Limited cultural awareness among the rural population of the obligations involved in borrowing money, not least because of the widespread tendency of NGOs and other donors to distribute funds on a non-reimbursable basis (particularly in the aftermath of the 1994 genocide);
- Inadequate banking infrastructure in rural areas, leading to difficulties in processing and supervising loans and associated high transaction costs;
- Deficiencies in, or even total absence of, other key links in the production / marketing chain, e.g. input supply, extension, storage, transport;
- Low, and in some cases declining, real prices for marketed commodities;
- Strong risk aversion because of past losses (not only resulting from war) and persistently unfavorable or uncertain market conditions in different sectors (e.g. road haulage).

It may be regarded as in one sense a positive factor that there is no shortage of funds available for investment, whether from domestic sources or from lines of credit actually or potentially on offer from foreign donors. However, it also seems clear that this very abundance of finance may paradoxically be posing a threat to the health of the financial sector, since it only serves to intensify the pressure (already strong on political grounds) to advance loans to *impoverished individuals or enterprises who have little security and whose businesses are at best very risky.*

Another positive sign is that the informal financial sector, including a number of “Grameen Bank” type micro-credit schemes operated by NGOs – typically involving loans of under \$400 without security - appears to be relatively healthy, although a definitive judgment on their effectiveness is not possible without a more extensive enquiry than could be undertaken within the scope of the present consultancy. However, it seems likely – based on the information obtained from World Vision / Amizero (see above) – that the relatively high level of repayments achieved by such schemes is only attainable by virtue of the high degree

of preparation (including intensive instruction of groups) which is applied by the schemes' trained agents, while at the same time the amounts disbursed are by definition very small. This suggests that the overall level of lending achieved by these micro-credit operations is likely to be quite limited in relation to the need while the transaction costs are very high.

At one level the problem may be defined as how to bridge the gap between the informal and formal sectors in such a way as to permit the latter to increase viable lending to small and medium enterprises having limited security. One way of addressing the problem might be to subsidize the transaction costs of commercial banks (possibly through technical assistance) without necessarily guaranteeing any loans. At the same time the government could be pressed to take urgent steps to reform the land tenure system, such that farmers and others could more readily gain leasehold title to their land and thus acquire meaningful collateral for loans. Likewise the facilitation of leasing operations (by means of putting appropriate regulations in place) will help to limit enterprise capital costs relative to their available collateral. However, more work is needed in order to make a soundly based assessment of the potential impact of such interventions.

More broadly, it seems clear that the most essential requirement for facilitating the mobilization of funds for productive investment (agricultural or otherwise) in Rwanda is to take steps to improve the overall investment climate, whether at sectoral or macro-economic level. It is clearly beyond the scope of the present exercise to determine the type or scale of policies or interventions that might be necessary to achieve this. However, there can be no doubt that, in order to promote appropriate investment in agro-related activities detailed and up-to-date information on the cost and revenue structures (from crop planting to the final markets of processed products) must be assembled. In the absence of such information measures to support individual product chains are likely to be wasteful and ineffective and any enterprise investment largely speculative.

SECTION III. POSSIBLE PROJECT INTERVENTIONS

In the light of the preceding analysis, and bearing in mind the actions known to be under consideration or implementation by other agencies, it would appear that the most useful form of intervention relating to the financial sector that could be undertaken by the project may be in the areas of

- Support for training of commercial bank staff in respect of loan appraisal and supervision (possibly including provision of data processing hardware and software). This could extend to implicit subsidization (over an extended period) of banks' transaction costs in processing loans in remoter rural areas where these costs are highest.
- Development of an effective farm insurance scheme (for both crops and livestock). Support for a suitable cooperative or farmers' association on a pilot project basis (these would need to be related to, inter alia, consultant studies now being commissioned on the cooperative sector by the National Bank)
- Finance or other support for establishing a leasing operation, assuming this will not adequately catered for by BDR;
- Injection of funds into Amizero or other suitable micro-credit institutions.

ANNEX A: MATRIX ON FINANCIAL SECTOR

Name of institution	Union des Banques Populaires de Rwanda	Banque Commerciale de Rwanda	Banque de Commerce, de Développement et d'Industrie
Type	Credit union / cooperative (135 member banks)	Commercial bank	Commercial bank
Sources of funds	Members' deposits	Individual deposits Deposits from other banks (including Banques Populaires)	Individual deposits Deposits from other banks
Rural sector loan portfolio as % of total	8	Less than 5	Less than 1
Collateral / equity requirement	Variable, but prefer over 50 %	Variable	130
Loan management capacity	Very little at member bank level (i.e. outside Union headquarters)	Adequate in Kigali, but insufficient to cater for provincial / rural areas	Adequate in Kigali, but insufficient to cater for provincial / rural areas
Strategy development	Enhance staff capacity (especially at local level) and develop farm insurance scheme to help expand rural lending	Enhance capacity to service rural areas Diversify into non-lending financial services	Diversify into non-lending financial services
Other potential sources of finance	Lines of credit (but only when capacity has been enhanced and own deposits have been more fully invested)	Lines of credit (European Investment Bank)	Not seeking these at present ; rather trying to reduce deposits

Name of institution	Banque Rwandaise de Développement	World Vision / Amizero
Type	Development bank	Micro-credit scheme (NGO)
Sources of funds	Share capital and borrowings (lines of credit)	Revolving fund financed by parent bodies overseas
Rural sector loan portfolio as % of total	Not known, though about 15% of 1998 approvals	None to date
Collateral / equity requirement	Minimum 30-40%	Not required
Loan management capacity	Inadequate loan supervision capacity, particularly vis-à-vis projects remote from Kigali	Mobile agents – sufficient for management of limited resources
Strategy development	Invest in more agro-processing projects Create a leasing company	Increase funds so as to enable it to lend more to farmers
Other potential sources of finance	Further expand lines of credit	Other aid agencies