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THE IMPACT OF CREDIT UNIONS IN GUATEMALAN FINANCIAL MARKETS

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Cooperative Strengthening Project

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INTRODUCTION

The Cooperative Strengthening Project is a large institutional development program with Guatemala's cooperative movement. It was designed to improve the capability of selected credit unions and agricultural cooperatives to provide high-quality, competitively priced services to their members.

The Project has been underway since mid-1987 and is now working with 4 national federations, 20 credit unions, and 14 coffee cooperatives located around the country. All have been provided with a mix of technical and financial assistance to help remove existing obstacles to improved and more profitable services. Policy reform was linked to recapitalization assistance while training was used to improve staff and leadership skills. All organizations have shown greatly improved operations, but the credit unions have far surpassed original expectations of the project design. The growth of capital, assets, savings and total membership is significant, and they have demonstrated a unique capability to capture rural savings and to effectively make and recover large numbers of small loans.

In November 1992, the University of Wisconsin was contracted by the World Council of Credit Unions (WOCCU) to analyze the market niche and impact of credit unions in Guatemala's rural financial markets. Three different regions of the country (the Western Highlands, the South Coast, and the North) were included in the study to address the diverse geographic, ethnic and economic characteristics of existing credit union markets. Membership files were sampled in seven representative organizations, historical savings and loan trends examined, and surveys conducted to evaluate the importance of membership to family income. Credit union members were interviewed and results compared with two groups of non-credit union communities on the South Coast and the Western Highlands. Three (3) reports were prepared and provide the basis for this summary paper. The first described the policies and services of the Guatemalan credit unions, the second identified the demographic and economic characteristics of members, and the third examined the role of the credit union in mobilizing savings and providing credit to households engaged in small and medium-scale agriculture and commerce.

THE GUATEMALAN LANDSCAPE

The Guatemalan economy is characterized by its dependence on agriculture and a highly skewed distribution of land and national income. Agriculture employs over 50% of the population, and products such as coffee, cotton, bananas, sugar, vegetables and fruits generate 70-80% of annual export earnings. Large plantations possess the best farm lands, specialize in single products, and rely on cheap labor to produce. Small farms are concentrated in the densely-populated Highlands, are frequently too small to absorb 100% of family labor, and are normally planted in corn, beans, wheat, and more recently, vegetables. After agriculture, much of the remaining population is employed in manufacturing (food processing, cement & beverage production, textiles and clothing), the service industries (teachers, salesmen, clerks and accountants), and commerce.

Table 1: **LABOR FORCE by Activity**

Agriculture	*50.1%*
Service Industries	*14.6%*
Manufacturing	*13.6%*
Commerce	*13.1%*
Construction	*4.1%*
Transport/Storage	*2.6%*
Other	*1.9%*

In 1993, the population was estimated to total 9,775,000. Sixty-six percent (66%) of all Guatemalans have a monthly income below Q346 ($60) and are classified as "poor" by the Government. USAID/Guatemala estimates that 80% of the population is living below the poverty line. It is a low-income economy with a decidedly rural orientation. Employment opportunity is determined by the geographic, climatic and economic characteristics of each separate rural community. Farming and farm supply businesses, restaurants, hotels, stores, small and medium-scale industries, and many micro-enterprises provide the greatest sources of employment. One community is often very distinct from another, but all seem to share one common trait -- they have very limited access to financial services, and particularly credit. The absence of financing at reasonable rates of interests is one of the key constraints to increased economic activity in the rural areas. There are many small-scale entrepreneurs seeking to develop investment opportunities, but without the necessary financing, their efforts to develop and expand existing and new businesses will be prolonged and difficult.

The Economic Situation

The Guatemalan economy has always been one of the strongest in Central America and growth rates have traditionally surpassed those of neighboring countries. In 1993, however, the economic situation has begun to deteriorate and the prospects for a strong macro economic performance are not good. Economic growth is slowing, real incomes have not kept pace with inflation (currently at 13.5%), export volumes are falling, and both Government and private investment are expected to decline.[1] World market prices for the most important agricultural exports have been low since 1991, reducing the already low incomes of the rural population and placing increasing pressure on the exchange rate. This poor economic situation is accompanied by a high population growth rate (2.9% annually), increasing migration from rural to urban areas, severe unemployment and under-employment, low productivity, and an ever-increasing gap between the rich and the poor.

The Financial Sector

The Guatemalan financial sector is dominated by private commercial banks. In 1991, commercial banks accounted for 89% of total assets, 88% of total lending, and 93% of total savings.[2] Given the importance of the banking system, the government recently began a program to modernize the financial sector and free-up financial markets as the means to encourage greater investment in the productive sectors of the economy.

Financial sector reform and modernization is now a key component in the government's economic and social development strategy. The strategy is designed to increase the efficiency, availability and accessibility of financial services, as well as, to provide a sound regulatory policy framework which ensures the safety and prudential operation of the system.

The first steps in the modernization process were taken in 1991/92 when the government dropped interest rate controls, freed the exchange rate, and eliminated the stamp taxes charged on financial transactions. Among short-term results, capital was repatriated seeking higher domestic interest rates and the banking system grew and became more competitive. There are now 25 private banks operating (up from 20 in 1990) and six more are awaiting authorization from the Monetary Authorities. These banks have aggressively opened new branch agencies and the interest rates paid for savings have improved with greater competition.

The second phase of the modernization program has not yet begun and has been slowed by resistance from the private sector and internal political problems. The program is designed to ensure economic and monetary stability while promoting the growth and the development of the national economy. Steps are planned to control Government spending; diversify and make more competitive bank services and products; improve guidelines for prudential and safe operations while gradually reducing the currently high reserve requirements; tighten GOG regulatory and supervisory policies; and to regulate the stock market.

While these changes sound impressive, little has changed for the average Guatemalan. Short-term credit remains scarce, investment capital almost non-existent, and existing collateral requirements for bank loans virtually eliminate small and medium-scale producers from access to financing. Commercial banks remain the main source of agricultural credit, but over seventy-five percent (75%) of all lending is directed at the production of cotton, coffee, sugar cane, and livestock on large-scale farms. Furthermore, in 1993 commercial credit for agriculture has declined and only 14% of all bank system lending was directed at the agricultural sector.

The opening of new bank agencies has not improved the credit access problems of the rural population. There are now 392 bank branch agencies in the country (up from 262 in 1988), but 42% are located in the metropolitan area surrounding Guatemala City, and an additional 21% are centered in but eight other cities.[3] In addition, the branch agency networks of the commercial banks are only designed to capture rural savings, and in this, they have succeeded. In July 1993, 89% of total bank system savings were concentrated in accounts between Q1,000 and Q5,000 ($175-$877). Savings accounts for amounts smaller than Q1,000 are discouraged with high administrative fees and poor service. Bank managers comment that such smaller accounts are simply too costly to manage when administrative expenses are combined with the high reserve requirements established by the Central Bank.

The credit access problems of the average Guatemalan are much more readily apparent in bank system lending. Commercial bank credit remains highly concentrated among large borrowers -- 5% of loans granted in 1991 comprised 84% of total loan values. The banks discourage loans smaller than Q5,000 ($877.00) with high processing fees, excessive demands for collateral, and long delays in loan approvals. To date, none of the commercial bank branch agencies have credit approval authority and applications must be forwarded to Guatemala City for final authorization. In 1991, the private banks granted 3 loans for agriculture, 8 loans for manufacturing, and 14 loans for commerce in amounts less than Q1,000 ($175.00).[4] In 1993, the greatest growth in bank system lending occurred in industry, manufacturing and construction.

The banks appear unable or unwilling to increase lending to the rural areas for three reasons: overly restrictive banking legislation (primarily reserve and collateral requirements), a risk avoidance mentality which limits lending to short-term borrowers who possess secure loan guarantees, and the widespread perception of low profitability and high risk in such lending.

Informal Financial Markets

While formal institutions (commercial banks, public banks and finance companies) dominate financial markets with 85% of all transactions, Guatemala also has a widespread and fairly well-developed informal financial market. This market includes non-governmental organizations (NGO's), input suppliers, money-lenders, and the credit unions. These informal financial institutions are important sources of credit for much of the rural population.

There are approximately 20 non-governmental organizations (NGO's) with credit programs in rural areas. Several are important loan sources for micro-enterprise and small agricultural producers, but the programs are modest in scope, expensive to operate, and often very dependent on external donor funding. The most successful of the NGO programs (*FUNTEC/Genesis Empresarial*) concentrates on short-term, micro-enterprise lending through 22 regional offices located in 16 departments. In 1993, 6,300 loans were granted for a total of Q40 million ($7 million).[5] Loan interest rates are high (30% annually) but credit is relatively easy to obtain. The above-market lending rates are apparently necessary for two principal reasons: the high administrative cost of maintaining 22 regional offices and the use of commercial bank credit to finance the loan portfolio. In 1993, 52% of the *Genesis Empresarial* portfolio was financed with commercial bank loans. Bank financing is obtained at market rates (averaging 25%) and onlent to small entrepreneurs at 30%. The 5% margin is not sufficient to cover all operating costs, but the deficit has been offset by the earnings from capital contributions by AID/Guatemala totaling Q5.2 million ($913,000). The other NGO's have not been as fortunate. For example, the largest single program for micro-enterprise (the Government's *Programa SIMME*) is widely-known to be costly, inefficient, overly bureaucratic, and currently experiencing severe problems with loan delinquency.[6] Other smaller NGO programs are in somewhat better shape, but they remain small and wholly dependent on external sources of financing for continued operation.

Supplier credit and the financing provided by private money-lenders are among the most important sources of rural credit. For example, the forty (40) coffee exporting firms who advance payments to growers against the proceeds from the future sale of their crops have a combined volume that is equivalent to 35% of the market value of the country's annual coffee output.[7] In 1992 such lending totaled approximately Q375 million ($72 million). Interest rates are normally well-above the market, but demands for real collateral are few and turn-around time for loan approvals is rapid.

Finally, the input suppliers are also a significant source of credit to small-scale businesses in many rural communities, but estimates of total loan volumes are unavailable. The short-term (30-60 days) and product-based nature of such lending limits its usefulness for business start-up or expansion, but they are an important source of short-term credit.

THE COOPERATIVE STRENGTHENING PROJECT

The objective of the Cooperative Strengthening Project was to rebuild Guatemala's cooperative movement as an alternative to existing Government and private financing channels. Its goal was "to increase the availability of production and investment credit throughout the cooperative movement by stabilizing the financial situation of selected organizations, promoting the use of innovative resource mobilization and credit intermediation techniques, and upgrading the management and service delivery capabilities of the cooperatives".[8]

The Project began working with the National Credit Union Federation (FENACOAC) and the affiliated community credit unions in late-1987. The development strategy was designed to respond to the unmet demand for financial services outside Guatemala City by helping the Federation and a select group of Credit Unions develop and introduce new, high-quality savings and loan products. Initially, the process was slowed by the need to convince credit union leaders of the need to change existing policies. The credit unions were operating with outdated policy guidance, untrained staff, and the public perceived them as unsafe. They were borrower-dominated institutions, had high rates of loan delinquency, were undercapitalized, and rumors abounded about insider abuse and financial mismanagement.

During the first two years (1988/89), new policies and operating standards were developed to improve financial services and management skills. In 1990, this was followed with aggressive marketing programs to change public image and attract new members. Key policies included:

* competitive pricing for savings and loans;
* aggressive mobilization of local savings;
* maintenance of adequate liquidity to satisfy unanticipated withdrawals of savings;
* application of new lending criteria centered around capacity-to-pay analyses, credit history and the collateral offered;
* strict creation of loan/loss reserves in relation to delinquency;
* reduction of non-productive assets (i.e., those which produce no income for the credit union);
* capitalization of all net earnings; and
* use of marketing programs to improve public image.

The development strategy emphasized the viability of the credit unions as financial institutions while improving the delivery of services. Application of the new operating policies resulted in unprecedented credit union growth:

Table 2: **Growth of Key Indicators** (Millions of Quetzales)

	1988	1989	1990	1991	1992	Sept 93	%Var
ASSETS	35.4	46.1	62.3	81.1	112.5	139.4	294%
LOANS	22.7	29.6	35.3	49.3	68.1	94.3	316%
SHARES	16.1	20.3	24.4	30.7	39.3	46.9	191%
DEPOSITS	8.8	12.7	21.2	31.6	53.8	66.8	659%
CAPITAL	1.9	2.7	4.1	7.0	10.1	14.7	674%
MEMBERS	65,200	65,500	71,500	76,000	79,500	86,849	33%

The growth was accompanied by stronger financial health. In 1992, the safety and soundness ratios for the credit unions compared very favorably to those presented by the commercial banks.

Table 3: **1992 Safety and Soundness Ratios**

	CREDIT UNIONS	**BANKS**
Total Asset Growth	38.7%	25.9%
Assets in Loans	58.2%	44.0%
% Non-Productive Assets	10.8%	25.6%
Loan Delinquency *	6.9%	3.2%
Loan Loss Reserves/Delinquency	57.8%	14.2%
Capital/Assets	9.0%	5.2%

* The commercial banks understate loan delinquency by only reporting the amount of past-due loan payments. This differs from the credit unions who report an entire loan balance as delinquent after 30 days whenever a payment is missed.

The credit unions have better capital-to-asset ratios; loan delinquency is better controlled and reported more accurately; and, the creation of adequate reserves to protect against loan default is more systematic and disciplined.

The specific credit union policies for capitalization minimums, delinquency control and reporting, and reserve creation are far more stringent than those now required of the commercial banks by the Superintendent of Banks. The GOG hopes to apply similar policies in the second phase of the Bank Modernization program, but as yet, their introduction has been successfully resisted by the Bankers Association and little is likely to occur before 1994.

The Credit Union Market Niche

The market niche of the community credit unions represents a large cross-section of daily life in rural Guatemala. Communities are equally divided between men and women, and individuals are employed in a wide variety of occupations -- e.g., farmers, store owners, teachers, salesmen, clerks, administrators, managers, accountants, and housewives. Average monthly income is low, savings are limited, and virtually no one has access to credit at reasonable terms.

The most economically active individuals are between the ages of 16-60. They are either self-employed, salaried, or earn a daily wage that is low in comparison to household incomes in Guatemala City. They save for a variety of reasons: children's education, medical and social expenses, improved housing, personal retirement, and for a multitude of unforseen necessities. When they borrow, loans are sought for both productive and non-productive activities: micro-enterprise, trade, agricultural investment, consumer goods and services, home improvements, and education. Each segment of the market is important.

The credit unions are successfully working within these diverse market segments by offering small savers the opportunity to earn market rates of interest and by providing loans to borrowers of limited income at competitive costs. They are capturing large numbers of small savings accounts and are re-investing these resources into the same communities as loans. This balanced approach to financial services is unique in rural Guatemala because it penetrates a financial market untouched by the commercial banks and other informal institutions.

Member Characteristics

Guatemala's credit union movement began in the Western Highlands in the early 1960's and early membership was heavily weighted toward low-income, small farmers, a majority of whom were men. Savings were obligatory and earned no interest, credit union management was simple, and the principal service was the channeling of agricultural production credit to members.

Today, credit union members tend to be in the lower to middle-income ranges of Guatemala's population. They are employed in many different occupations and more recently, women are playing an increasingly important role. Credit union services are more sophisticated, savings earn competitive rates of return, and agricultural credit consumes only 17% of loan activity. Average monthly income is highly concentrated, with 67% of members reporting earnings in the Q300 to Q2,000 range ($53.00-$351.00).

Saver Profile

Credit union members exhibit a classic, life-cycle savings behavior. New or young members enter the credit union with low levels of assets and income. These are the same individuals who have the greatest difficulty acquiring credit from the commercial banks. They initially save in share accounts, since these are used to determine eligibility for credit union loans. Later in life, when loans are no longer so important, members begin to save more in deposit accounts which earn market rates of interest.

In the communities where they operate, the credit unions are rapidly capturing an increasing share of local savings accounts, normally the exclusive domain of commercial banks.

Table 4: **Percent of Market Share / Deposit Savings**

	Credit Union	Private Bank	Public Bank	Other
Volume of Savings	34%	45%	14%	7%

In a relatively short period (3-4 years) the credit unions have captured a 34% share of local savings. This has been done by presenting a professional public image, making improvements to infrastructure, offering the payment of competitive rates of interest (regardless of account size), and providing a non-threatening environment to members.

Total Membership	***86,849***
Avg. Monthly Income	***$141.00***
Avg. Savings Balance	***$ 75.00***
Avg. Loan Size	***$305.00***

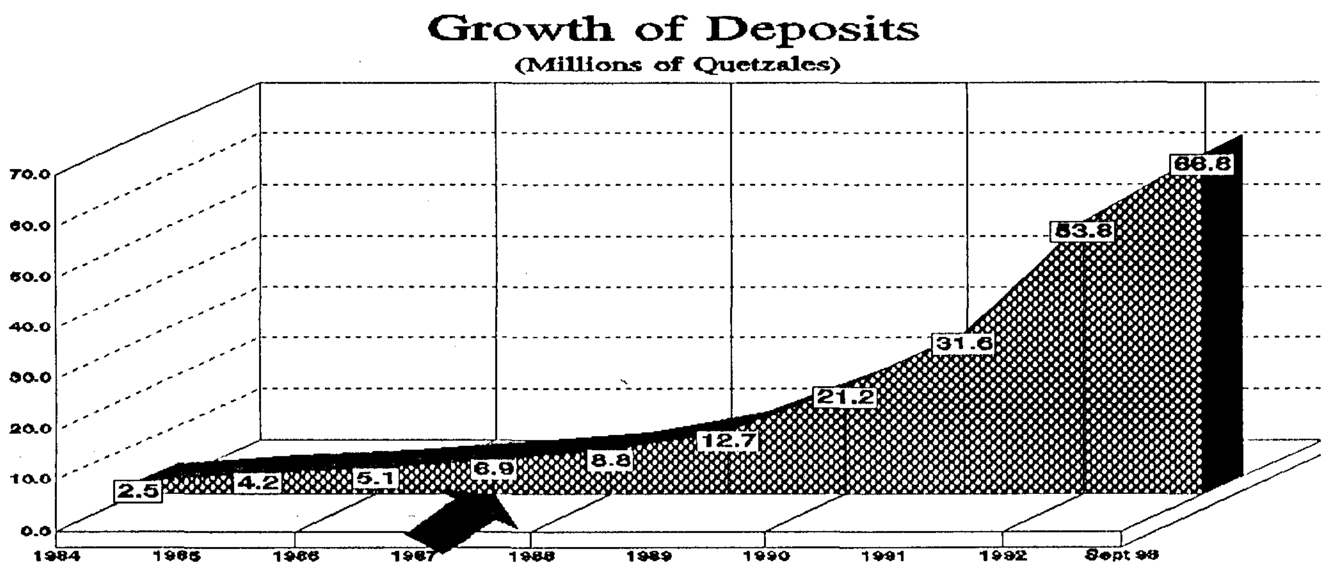
Monetary requirements are not a barrier to credit union membership. This has been a key factor in their ability to compete with the commercial banks for rural savings. The minimum required to open a credit union savings account averages Q20.00 ($3.50), much lower than the commercial bank minimum of Q250.00 ($44.00).

A majority of credit union savings accounts (89%) have less than Q500.00 ($88.00). Middle-income members between the ages of 41-50 have the highest savings levels and among these, salaried workers showed the most dynamic savings growth in 1992. Higher income members save less at the credit union and are likely using commercial banks where they have access to additional services (checking, money transfers, etc.).

Farmers represent those with the lowest incomes, but they are important savers. They have lower share levels and a lower average loan size, but they save more regularly and have higher savings than members engaged in commerce. Those who report commerce as their primary activity have the highest incomes of all credit union members, but they save less. In part, this is due to a tendency of the "*comerciantes*" to save in inventory.

The growth of credit union services is fueled by local savings. They have provided the credit unions with much greater financial independence and they represent an enormous pool of resources for investment. The historical dependence of the Guatemalan credit unions on external financing has been virtually eliminated and locally mobilized savings are now the largest and fastest growing source of credit union funds. In September 1993, only 2.7% of assets totaling Q140 million ($24.5 million) were financed with external loans.

The results of the savings mobilization campaigns far surpassed the expectations of the credit unions involved.



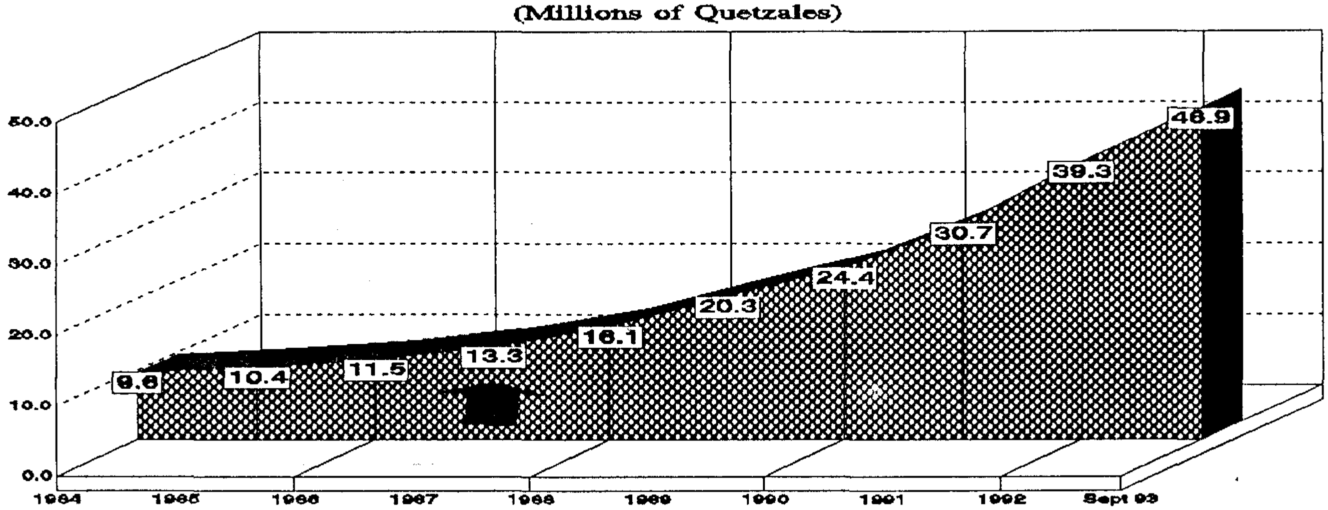
The credit unions establish the rates paid for savings by monitoring and pegging them to those offered by the commercial banks, however, their willingness to work with very small accounts has greatly increased their ability to compete.

Interest rates vary significantly across the credit unions indicating both the degree of competition and a marked geographic separation of markets. Rates are lower in rural areas where less competition exists and higher in urban areas.

Salaried employees and non-traditional crop producers appear to have the highest savings potential. They save more regularly and have the highest average savings balance. Traditional agricultural crop producers save less frequently and in the smallest amounts.

There are two ways to save in the credit union -- in deposit accounts which earn a market rate of interest, and in share accounts which earn less. Shares are one of the determinants of loan size, and members who expect to seek a loan tend to emphasize share savings.

Growth of Shares
(Millions of Quetzales)



The number of share accounts has increased rapidly in recent years with the greatest growth coming from among salaried employees and farmers. Salaried workers include salesmen, taxi drivers, accountants, mechanics, technicians, teachers and office workers. They are saving more than other members and are becoming a particularly important source of loan demand in both agriculture and commerce. Many such borrowers appear to be using credit to establish small enterprises as a secondary source of household income.

Borrower Profile

The credit unions have few competitors in rural credit markets, and in the communities where they operate, they have become the single most important source of credit.

Table 5: **Percent of Market Share / Loans**

	Credit Union	Private Bank	Public Bank	Other
Number of Loans	47%	3%	11%	39%
Volume of Loans Outstanding	51%	10%	15%	24%

A majority of credit union members would likely find commercial bank loans too difficult and costly to obtain. Factors appearing to limit private bank access include: illiteracy (25% of credit union members are estimated illiterate); high transaction costs in the form of formal deeds, assessments of value, and proof of income; and time-lags of many weeks for loan approvals.

There are wide disparities in loan size between credit unions, reflecting both the importance of economic activities and the differences in income levels. For example, farmers in Teculutan (the Eastern lowlands) are involved in commercial agriculture and livestock production. They have relatively high incomes. Conversely, farmers in Tactic (Northern Guatemala) are primarily engaged in corn production and income is low.

Average loan size rises rapidly with income, and there exists a concentration of loans among the higher income borrowers in agriculture and commerce. Farming still represents 17% of credit union loan portfolios, but the largest agricultural loans are now concentrated in commercial crops and livestock.

There are two categories of farmers in the credit unions -- those engaged in subsistence agriculture and those involved with intensive, commercial crops (e.g., fruits, vegetables, tobacco, sesame, and flowers). Farmers have the lowest average loan size (Q963.00) -- half as large as the average loan size for merchants and salaried employees -- but higher-income farmers now receive over 95% of the volume of livestock loans. Lending for land purchase and basic grain production has declined over the past several years, while lending for cattle has more than doubled and loans for cash crop production (coffee, tobacco and tomatoes) has also increased significantly.

Older members have higher incomes and a higher average loan size, particularly in commerce and agriculture. Newer members predominate in non-productive loans (housing and personal loans). This suggests that newer members obtain small personal or home improvement loans as a means of establishing a credit record before moving into the larger and more productive loans in commerce or agriculture.

Credit union lending patterns suggest a two-tier membership structure. One group is comprised of the wealthier members who own either land or a house. These members receive loans based on the value of the collateral pledged. The second, larger group is comprised of members with few assets. This group depends on income to build-up share levels and obtain access to loans. Loan size is determined by the amount of shares owned, credit record, repayment capacity, and the collateral offered. Typically, no mortgage collateral is required for loans smaller than Q5,000 ($877), thus permitting poorer members to obtain credit without requiring a guarantee. Credit union loans are usually small in comparison to commercial bank loans.

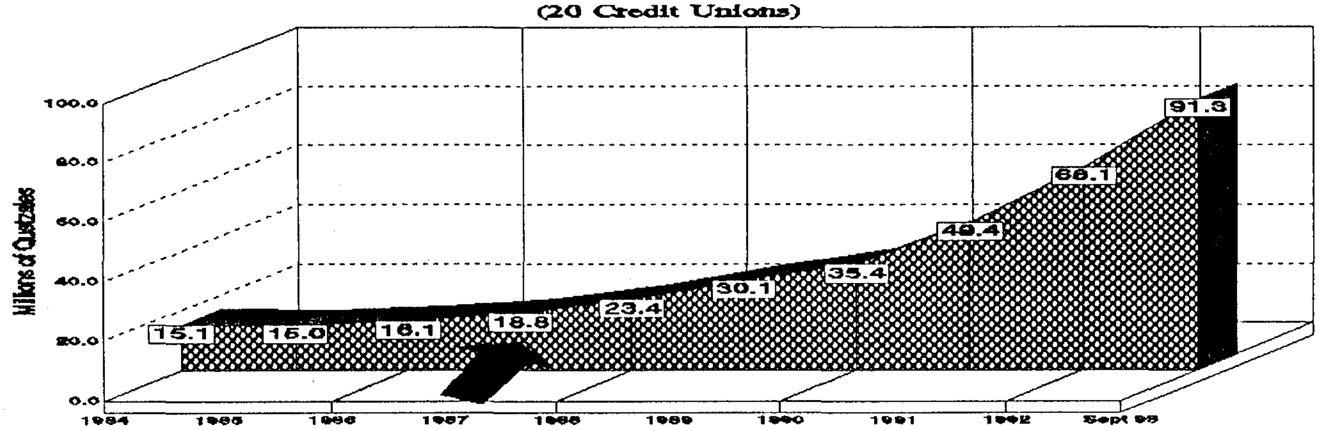
Table 6: **Average Loan Size / Banks vs. Credit Unions**

LOAN PURPOSE	**AVERAGE LOAN SIZE (Banks)**	**AVERAGE LOAN SIZE (Credit Unions)**
Agriculture	Q218,825	Q1,084
Commerce	Q193,158	Q4,433
Housing	Q6,137	Q4,247
Personal	Q107,667	Q615
Average	Q34,942	Q1,754

The difference in average loan size between the credit unions and the banks is particularly apparent in lending for commerce, agriculture, and personal consumption. The smaller difference in housing loan size indicated in Table 6 is primarily due to the existence of a government-guaranteed lending program for housing.[9]

The demand for and the real value of credit union loans is rising rapidly.

Loan Portfolio Growth
(20 Credit Unions)



Average loan size has increased in all credit unions and loan portfolios are more diversified. Credit unions located outside Guatemala City allocated more than 50% of their loans to commerce and agriculture in 1992. Loans for business and commerce represent the most dynamic components of credit union lending in all but Guatemala City, where housing loans have grown most rapidly.

The credit unions have successfully maintained loan delinquency rates below 10% for three consecutive years. With the increase in the average loan size, capacity-to-pay indicators have begun to play an increasing role in loan decisions as has the use of collateral to guarantee larger loans. Less collateral is required for commercial loans than agricultural loans where risks are perceived to be lower.

The Participation of Women

Women are important savers and borrowers in the community credit unions. In September 1993, membership totaled 86,849 individuals -- approximately 40% of members (34,739) are women. Women earn only 60% of the income earned by men, but their use of savings accounts has almost doubled over the past five years.

Table 7: **Member Use of Savings Accounts**

	1987	1991
Women	38%	63%
Men	44%	59%

The average size of deposit accounts for men ($306) is greater than those of women ($220), but women possess a 42% share of total credit union savings. Salaried employment (e.g., teaching and office jobs) appears to generate the highest household income for women, while self-employment in commerce and agriculture is a much more important income source for men.

Women borrow less frequently and in smaller amounts than men, a likely reflection of reduced repayment capacity and lower levels of collateral that can be pledged as a guarantee. They participate, however, just as actively as men in building up shares in order to leverage loans.

Table 8: **Percentage of Loans Granted**

	Agriculture	Commerce	Housing	Personal
Men	83%	60%	57%	73%
Women	17%	40%	43%	27%

Women are most active in borrowing for housing and commerce. They account for 63% of credit union members who report commerce as their primary source of income. Today, this is the fastest growing component of credit union loan activity. In agricultural lending, women represent only 19% of total loan values with an average loan size of $184. This is because men still dominate in agricultural activities.

Women have traditionally had difficulty obtaining larger credit union loans due to their lower earnings and a lessened ability to provide the required collateral. These constraints have been reduced in part by permitting a spouse to combine assets and income in support of larger loan requests. This is likely one of the reasons for the increased growth of commercial loans to women.

Small and Micro-Enterprise

Recent studies by the Inter-American Development Bank (IDB) conclude that 36% of Guatemala's economically active population is involved with small and micro-enterprise. Small businesses employ approximately 1 million Guatemalan's, and today, the credit unions are the single most important source of financing for this sector.

Small business lending is now the most dynamic and fastest growing component of credit union loan portfolios. Commercial loans represent 32.7% of total credit union lending, and in real terms, commercial lending grew by 81% over the past four years.

Monthly income for members who report commerce as their principal activity was 28% higher for men and 25% higher for women than the average monthly income reported from all other sources.

Business loans have the highest average loan size (Q4,433) and those members who identify themselves as "*comerciantes*" maintain the highest levels of savings in share accounts.

Table 9: **Distribution of Deposits & Shares by Occupation**

OCCUPATION	SHARES	DEPOSITS	TOTAL SAVINGS
Agriculture	Q807	Q362	Q1,169
Housewife	Q647	Q68	Q715
Salaried	Q1,310	Q208	Q1,518
Commerce	Q1,427	Q168	Q1,595

Only 11% of credit union members actually report commerce as their primary activity, but interview data suggests that this figure does not present an accurate picture of commercial borrowing. For example, many salaried workers and housewives are engaged in secondary commercial activities to supplement household income. The composition of these commercial loans is very broad.

Table 10: **Diversity of Typical Micro Enterprise Loans**

General Store	21%	Repair Shop	6%
Services	15%	Weavers	6%
Vendor	11%	Seamstress	5%
Food Processing	10%	Restaurant	5%
Carpentry	8%	Others	13%

CREDIT UNION DEEPENING OF RURAL FINANCIAL MARKETS

Guatemala's formal financial markets remain today as they were almost seven years ago. Small savings accounts provide the main source of financing for the national banking system, but access to credit is restricted to a very small percentage of the population.

In 1990, an optimistic assessment of Guatemala's rural financial markets projected that "the extension of commercial bank branch networks more widely throughout the country should help not only with deposit mobilization but also in providing improved deposit and credit services for lower-income individuals in rural areas".[10] This did not happen.

Since 1990, one hundred and thirty-two (132) new bank agencies have opened, and sixty-seven communities nationwide are now served by at least one commercial or public bank. It has become a little easier to open a savings account, but the small borrower still has little hope of getting a loan.

In 1992, the commercial banks made loans totaling Q3.392 billion ($595 million) throughout the country. Most of this financing is invested in large loans for industry, commerce, construction, agriculture, and consumption.

During the same period, the commercial banks made 1,136 loans for commerce and 192 loans for agriculture in amounts less than Q20,000 ($3,508).[11]

Table 11: **Commercial Banks -- # Loans below Q20,000**

	0 - Q10,000	Q10,001 -- Q20,000	TOTAL
Agriculture	98	94	192
Commerce	645	491	1,136

The situation improves a little when lending by public sector banks is included. Public banks (primarily BANDESA) made many more loans for agriculture under Q20,000 ($3,508) than did the commercial banks (10,881 vrs. 192 loans), but the total number of loans is still very small for a country which depends so much on the agricultural sector. Public bank lending for small-scale commerce (203 loans) is even more restricted than such commercial bank lending.[12]

Table 12: **Public Banks -- # Loans below Q20,000**

	0 - Q10,000	Q10,001 -- Q20,000	TOTAL
Agriculture	8,006	2,875	10,881
Commerce	123	80	203

The small borrower is often discouraged with formal collateral requirements, fees, and unfamiliar and time-consuming paperwork in both the private and the public banks. Finally, since none of the bank agencies has credit approval authority (September 1993), final loan approvals can easily take 5-6 weeks.

The credit unions deepen financial markets by providing rural communities with much greater access to a wider variety of financial services. They accept deposits and make loans in much smaller amounts than other formal financial intermediaries, and through this process, they are empowering a larger pool of "bankable" clients in the communities they serve.

In 1992, the 20 credit unions working with the Project had a combined loan portfolio totaling Q68.1 ($11.9 million). This portfolio included approximately 5,023 commercial loans and 10,554 loans for agriculture.

Table 13: **Credit Unions -- Distribution of Loan Portfolio (1992)**

	Portfolio Size	**Number of Loans**
Commerce	Q22,268,700	5,023
Agriculture	Q11,440,800	10,554
Housing	Q23,630,700	5,564
Personal	Q10,759,800	17,496
TOTALS:	Q68,100,000	38,637

The number of agricultural loans was equivalent to BANDESA's loan portfolio, and commercial lending was almost five times larger than the combined portfolios of the commercial banks. In September 1993, the loan portfolio of the credit unions had grown by 39% to Q94.3 million ($16.5 million), with the greatest growth occurring in commercial lending.

By working with small accounts, the credit unions provide a scale and a scope of financial intermediation to the lower and middle-income sectors of the population that is met by no other private or public institution. They are mobilizing high amounts of local savings by offering competitive rates and professional service, and, their willingness to work with and provide equal treatment to the small accounts has enabled them to capture an increasing share of the savings mobilized in their communities.

They fill a major gap in local financial markets by making small loans available to borrowers of limited means at competitive costs. In lending, the credit unions have few competitors. The average loan size (Q1,740 to Q4,500) is much smaller than the average commercial bank loan, interest rates are competitive, and loan approvals are rapid, averaging 15 days. They have become a reliable source of credit for borrowers with limited assets and low to moderate incomes, and they are the only significant source of credit for commerce in the areas where they operate.

The savings behavior of rural communities is a well-known indicator of wealth and economic activity. In comparisons with communities having no access to credit unions, members were found to be 3.5 times wealthier than non-members, and they save more regularly and in greater amounts than non-member households. In addition, 53% of the poorest credit union members have access to credit whereas only 22% of non-credit union members with similar wealth levels were found to have such access. Finally, credit union members have better access to basic health services, higher education levels, and they are more likely than non-members to be of "ladino" origin.

THE FUTURE OF CREDIT UNIONS IN GUATEMALA

In 1992, Guatemala had an estimated population of 9,745,000. Of the total population, 2,770,000 individuals are considered economically active, and two-thirds live in rural areas. Sixty-six percent (66%) of all households are below the poverty line with an average monthly income of Q346 ($60).[13]

The Guatemalan credit unions are successfully working within this relatively low-income market by offering their members competitive rates of return, maintaining a professional image, and keeping a member orientation to services. They do not discriminate against the small saver and they provide credit to members who have no other reasonably-priced alternative.

The newly acquired financial disciplines have helped the credit unions become financially healthy and profitable, but the movement remains small. The twenty credit unions vary greatly in size -- the smallest has 1,200 members and the largest 14,600. In September 1993, membership in the 20 credit unions totaled 86,849, approximately 3% of the economically active population. Sixty-seven percent (67%) of these members have a monthly income between Q300 and Q2,000 ($53.00-$351.00), parameters which fit approximately 85% of Guatemala's rural and urban population.

The potential market is therefore, without limit. The financial policies and disciplines are now in-place to permit the credit unions to grow and reach a larger percentage of Guatemala's population; however, several issues must be resolved for the expansion to occur.

Existing Constraints

Public Image
In the communities where they operate, the credit unions have changed the negative public image that existed, but nationally, they are still viewed as financially weak institutions with a social orientation. Many perceive them as organizations for the "poor", and as such, they are unwilling to invest their savings or to seek loans.

Staffing
All the credit unions are staffed by relatively young, inexperienced personnel. High staff turnover continues to be a problem caused by low salaries. Salary compensation has improved but is still well below comparative commercial bank salaries. The only way the credit unions can pay higher salaries is by increasing the volume of operations.

In addition to the salary issue, much more technical training is needed to sharpen staff skills. More sophisticated techniques for loan analysis, financial marketing, and internal administration are key to controlling costs while maintaining high-quality savings and loan services to a growing membership.

Electronic Data Processing
Most of the credit unions are operating using manual accounting and control systems. Uniform computer software is not available and remains a key constraint to managing thousands of small accounts efficiently. The need for computerized credit union software goes far beyond basic accounting. A program needs to be developed to include: liquidity and cash flow management, credit analysis and approval, delinquency control, financial planning and marketing, membership data base management, and PERLAS monitoring and reporting systems.

Services
Credit is the most important credit union service and will likely remain the key element in membership growth for the immediate future. However, to expand into new savings markets, the credit unions must develop new, improved services to attract members from the higher-income segment of the rural population. A key service is the need to provide more convincing assurances that member capital is safe and well-managed. In addition, higher-income savers and borrowers expect a full range of services (e.g., checking and funds transfers) from their principal financial institution. To date, the credit unions are prohibited from providing such services by banking legislation and the absence of government supervision.

The Opportunities for the Future

The community credit unions have demonstrated an impressive capacity to meet the needs of Guatemala's rural population in the absence of existing public and private financial institutions. Opportunities abound but in the short term, the credit unions must take decisive actions to address the existing constraints.

Staff Training
The Project and the Federation have begun a series of intensive training programs for credit union managers, credit analysts, marketing personnel, and clerks. These programs are designed to develop "executive teams" within the credit unions, a process that involves more staff in higher-level decision-making. Hopefully this will provide an incentive for some staff to remain for longer periods of time while also expanding their understanding of local savings and credit markets.

The cost of these training programs is relatively high in terms of staff time -- credit union personnel cannot dedicate more than 2-3 days per month for training without affecting internal operations. Nevertheless, the pay-off in improved services and increased membership growth has been unquestionably significant. Training will remain a key activity of the Project until the PACD in August 1994.

Electronic Data Processing
There is little doubt that an expansion of computer use and the development of new software will help the credit unions control costs and speed-up savings and loan transactions; however, the development of such software will not occur before the current end-

of-project deadline. Several off-the-shelf software packages have been tried and rejected, and plans are now being made to develop new software during the period 1994-95.

Market Expansion

Currently the credit unions are providing services to approximately 3% of the economically active population. Expansion of credit union services is now a short-term goal of the Federation. The twenty credit unions working with the Project embarked on a controlled program to develop branch agencies in 1991 and to date, 24 branch offices exist. New branches of existing credit unions will be opened in 1994 as market analyses identify new opportunities.

A very large, relatively untouched urban market is Guatemala City. One strong credit union is now operating in this market but the potential for new organizations is great. For example, employer-sponsored credit unions in public and private institutions could be developed relatively easily if time were available. The Project is supporting the opening of new branch agencies in the city, but the development of new credit unions is likely to remain a long-term goal of the Federation.

Public Image

In 1994, the Federation and a group of the strongest credit unions will launch the *Sistema Financiero Cooperativo (SIFFE)*. This new system will differentiate the elite credit unions from the rest of Guatemala's cooperative movement by offering a variety of new financial services coupled with strict financial discipline. The aggressive marketing slogan, "United through Excellence in Service" will provide a stiff challenge to SIFFE members to maintain high-quality services. In order to do this, SIFFE credit unions will be provided with advanced training, periodic reports on interest rate changes within the National Banking System, and improved service from FENACOAC's Central Liquidity Fund. Medium-term goals include member transfers of funds between credit unions and eventually, checking and credit card services.

In addition to the launch of the SIFFE system, plans are also underway to establish in early 1994 the "crown jewel" of credit union services: a Deposit Guarantee Program. This program will insure credit union members against any possible loss of savings, and will likely change the national image of Guatemala's credit unions. The guarantee facility will be the first such program to operate in Guatemala's financial markets, and the Project is now directing its technical assistance at the development of the SIFFE system and the Deposit Guarantee Program.

An Epilogue

This report has presented a wide array of data from many sources. The intent has been to eliminate the vestiges of doubt that may exist with regard to the power and impact that credit unions can have in fostering sustainable, financial market development. Guatemala is a poor country with relatively primitive financial markets. Broader access to financial services is key to any development initiative, and as one contemplates the opportunities for further advancement, it becomes clear that courageous and decisive action should be taken to support and expand the coverage of the Guatemalan Credit Unions.

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