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SUSTAINABLE SACCO DEVELOPMENT

TRAINING MATERIAL



September, 2006

This publication was produced for review by the United States Agency for International Development. It was prepared by Getachew Mergia Tache, Consultant for Chemonics International Inc.



Rural SPEED

Rural Savings Promotion & Enhancement of Enterprise Development

SUSTAINABLE SACCO DEVELOPMENT

TRAINING MATERIAL

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

Rural SPEED

A USAID funded project

Contract No. PCE-I-00-99-00003-00, TO 826

This report submitted by Chemonics International Inc. / September 2006

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SECTION 1

Introduction

SACCOs (SACCO) Societies or Credit Unions have been developed to meet the fundamental human need to find a way of saving and borrowing methods without taking risks and without handing over too much power to a moneylender. They were invented in south Germany in 1846 at the time of agricultural crisis and continues heavy drought in Europe, by two community business leaders: Freidrich W. Reifeisen and Herman schultze- Delitsche, who are considered as the founding fathers of the saving and credit cooperatives (SACCO) movement: Herman schultze- Delitsche, who established a saving and credit cooperatives for minor artisans and the urban middle classes, and Freidrich Reifeisen, the founder of the rural saving and credit cooperatives. In Italy, Luigi Luzzatti established saving and credit cooperatives, which combined the principles established by his two German predecessors. Both forms spread rapidly all over Europe, northern America, Latin America, Asia from 1900 to 1930 and to Ghana by one Catholic Bishop. Today SACCO societies have significant role in empowering their members Socio-Economic Status all over the world. To mention some, in Western Europe there are around 11,000 local and regional saving and credit cooperatives banks, with over 56,000 outlets, a 33 million strong membership and a staff of more than 400,000. Their market share is 17 percent of savings, ranking third after the commercial and savings banks.¹

The French SACCOs or *Credit Union Agricole* is the largest bank in the world outside of Japan, the German people's banks have over 28 percent of the savings market share, Rabobank Netherlands 25 percent. Ireland has a strong SACCOs or Credit unions movement, with 1.6 million people (44 percent of the population) in membership.²

Canada has one of the highest concentrations of SACCOs. In the French-speaking Quebec region, there are 1300 SACCOs, with five million members and more outlets than the banks. They have more than a third of the region's savings on deposit, and make a third of all consumer loans. In English-speaking Canada they have not such a large market share, but in Saskatchewan 57 percent of the population belong to SACCOs or Credit Unions.

In the USA, some very large cooperative banks account for about a quarter of the credit needs of US agriculture. Credit Unions are also well established; there are over 18,000 Credit Unions, serving 70 million members and with more than \$300 billions in assets. They have 13 percent of the consumer credit market and eight percent of consumer savings.³

It is not surprising that membership-based businesses have been so successful. Financial services such as savings and loans, lending for house purchase, life and non-life insurance, and pensions provision are all concerned with directing flows of money and spreading risks. They do not really need injections of capital from a separate class of investors. The mutual form, in which members lend, borrow, and agree to insure each other is effective, they do not take too many risks or invest too far from their core business.

In the last decade there has been a wave of demutualization of mutual insurance (UK, South Africa, Australia), building societies (UK), and savings and loans (USA). The reasons given are usually that more capital is needed, or that they need to escape regulatory restrictions, or that they will be more efficient after conversion. There is also a large amount of self-interest among managers who want to enrich themselves with higher salaries and share options, sometimes helped by members who will receive large 'windfall' payments on conversion. However, most of the SACCOs and Credit Unions sector has stood firm against this trend. In the UK, the building society sector has shrunk to around 30 percent of its previous size, but the remaining SACCOs and Credit Unions are outperforming the

¹ *Cooperatives and the Millennium Development Goals*, Dr. Birchall Johnston, Geneva, ILO, 2004.

² *Cooperatives and the Millennium Development Goals*, Dr. Birchall Johnston, Geneva, ILO, 2004.

³ *Cooperatives and the Millennium Development Goals*, Dr. Birchall Johnston, Geneva, ILO, 2004.

investor-owned banks and gaining new business. They are also considered by customers to be much more trustworthy than their competitors.

This is due to the fact that from the beginning in the above countries they did the promotion of the SACCOs and Credit Unions with system of building self supporting thinking and voluntary people established their SACCOs and Credit Unions based on the philosophy of building self-help society or “people helping people”. They did not expect any thing from the outside to be piped to them as financial resources except technical and training support.

The history of SACCO Societies or Credit unions shows that they were formed critically for the relief of the poverty among the poorer economic classes in Europe, United States, India, etc. They are outperforming competitive service providers of the developed world. Though in some countries of Africa they were promoted between 1965 and 1989 they were promoted to fulfill the government quota without the members understanding the objective, function, ownership of the SACCO Societies, without any capacity building and they were more depended on government funds and highly insulated by politicians, characterized by miss management, corruption, lack of transparency and lack of members internal control. Due to this fact the SACCO Societies lost their nature of democratic organizations and were controlled by few active members; members lost their right of setting their policies and making decisions on issues, this condition collapses the SACCO development in Africa.

In recent years, in developing countries consideration of the potential of SACCOs and Credit Unions as a tool for sustainable poverty alleviation has been increasingly recognized. Evidence from poverty eradication strategies shows that without empowering the poor by teaching them how to utilize limited resources in a wise manner and over focusing on provision of credit leads to excessive debt burdens and depressed income growth leaving borrowers even the level where they were before. Because credit first is more appropriate for high return activities but saving first is more appropriate for those who live in subsistence agriculture and low-return of activities, statistics reveal that far more poor people demand savings services than loans.⁴ To up-lift the poor teaching how to utilize his limited resource in a wise manner and developing saving culture is vital; savings are the prerogative of investment that generate the start-up capital that invites savers to think of saving-driven investments, that may lead to profit to be reinvested again and again. This increases self-financing and self-securing oriented households in the community.

SACCO Societies contribute to develop the local economies where the poor live through their unique and strong linkages with the community. They enable poor people to have their voices heard, in addition to improving their daily working and living conditions, because SACCOs are democratic organizations and owned by those who use their services. SACCOs are an ideal instruments to empower the poor in sustainable way. They are participatory, responsive to local needs and able to mobilize communities’ fund and help particularly vulnerable groups of people. SACCOs enable farmers to create economies of scale in bargaining with urban banks and other financial institutions; they provide access to sustainable financial services; and, they provide low-income families with safe place to save their income at their area or village and reasonably priced loans.

This manual is therefore, designed to give insight about SACCOs’ definition, objectives and purposes, operational system, members role for it’s achievement etc. to both promote and help flourish their movement in rural areas of Africa based on the philosophy of “people helping people”. The second part of this manual provides guidelines on how to start SACCOs.

⁴ Rural finance from unsustainable projects to sustainable institutions for the poor, IFAD, October 2000.

Section II

What is a SACCO?

SACCO is an abbreviation for Saving and Credit Cooperative.

SACCOs are user-owned financial institutions that offer both savings and credit services to their members. Members of these financial institutions can be both net savers and net borrowers.

Depending on a country's legal framework, SACCOs may be authorized to mobilize member savings and non-members savings or member savings only.

- SACCO Society is financial cooperative society established by voluntary people based on the philosophy of building self-help society or "people helping people".
- SACCO Society is owned, managed, controlled by members. Members have the right to decide on its issues, members have the right to benefit from its service.
- SACCO Society is formed initially for the poorer to provide financial services such as safe place for savings and providing easy accessible loans to members.
- SACCO Society is "not for profit or for charity" but serve members at fair profit margins.
- In SACCO Society members savings form a good pool of money, from which loans are made to members with fair lending interest and the interest rate is decided by members.
- In SACCO Society once overhead and other expenses are paid, reserve for cushion against any loss, and for expansion of services set aside, the remaining income from loans is returned back to members in the form of dividend on savings, share or both.
- In general SACCO Society are financial institutions designed for people, to have their own efficient financial service giving institutions that empowers themselves in building asset by teaching thrift culture and make themselves accessible to credit in sustainable way.

What are the objectives and purpose of a SACCO?

Objectives of any SACCO Society are:

- Encouraging and promoting to develop thrift culture within the members as well as the community by teaching wise use of their money and efficient management of their limited resources.
- Teaching people how to create an asset that helps them to have a guarantee and collateral for future loan access.
- Making finance more accessible for members when they need it.
- Developing a linkage between the rural people and urban banks in order to have broader financial flows into the community and a safe haven for rural peoples' savings.

Purposes of any SACCO Society are:

Understanding the SACCO Society from a functional perspective allows you to see the logic in its operation. It allows you to define, with great precision, what the operation should do and what it should not do as organization. Further, it allows you to define what are the necessary inputs to produce the desired outputs.

The two fundamental function of a SACCO Society are **financial intermediation** and **investment**. The most basic function of SACCO Society is financial intermediation. That is bringing savers and borrowers together in a system that enables them to pool their money as savings and shares, and after capturing funds transforming into loans by calculating all of the costs of doing this business to make profitable/useful to both parties (the SACCO Society and its members).

Specifically the financial intermediation function of a SACCO Society is:

- ❑ Encouraging and promoting members to develop their thrift culture, as well as the community by teaching wise use of their money and efficient management of their limited resources,
- ❑ Teaching people how to create an asset that helps them to have a guarantee and collateral for future loan access,
- ❑ Make members more accessible for finance when they need it,
- ❑ Develop a linkage between the rural people and urban banks in order to have sustainable financial flow.

The other essential function of a SACCO Society is **investment**. That is to allow and encourage members to develop formal business and investment, (the SACCO Society itself) by placing their capital at risk and to receive a return (profit) on that investment.

Specifically the investment function of a SACCO Society is:

- Allow and encourage members to develop formal business and investment, facilitate them with sustainable loan services,
- Encourage members to buy shares in the appropriate amounts by leveraging with their savings at the appropriate times; using those shares guarantee the savings and loans of the members, by providing the correct amount of liquidity in the SACCO Society to manage risk of withdrawal or late repayment;
- Retaining some profit from interest earned on the lending operation to pay dividend to the members on the basis of the shares owned; redistribute the profits to the members as dividend on the basis of shares owned.

Therefore, to be successful and sustainable the SACCO Society should function similar to banks as a market for money in a group sharing a common bond. SACCO Society is a financial institution that purely deals with mobilizing money from members as savings, shares and providing easy accessible loans to members on time.

Since SACCO Society deals with cash (the most liquid asset) that can be easily lost, it needs high quality management and special attention to minimize the risk. Therefore, to minimize the risk the function of the SACCO Society should not be mixed with other functions.

What are the principles the SACCO operates under?

- The pioneers of the Rochdale Cooperative Society formulated a code of cooperative ethics, referred as cooperative principles.
- These principles gave them strength and vision in time of darkness and exploitation.
- The International Cooperative Alliance (ICA) reviews these principles from time to time and adopted the revised principles which any genuine Cooperative Society must strictly adhere too and these are:
 - Voluntary and open membership
 - Democratic administration and members leadership
 - Member Economic Participation: -Service and Surplus return to members
 - Continuous education to members and leaders
 - Autonomous and self help
 - Concern for the community
 - Cooperation among cooperatives

1st Principle: Voluntary and open membership

- Membership in a SACCO Societies should be voluntary and open to all persons able to use their services and willing to accept the responsibilities of membership stated by General Assembly of members without gender, social, racial, political or religious discriminations.

However, this freedom to join the SACCO Society is not of absolute, The General Assembly of the SACCO Society may stipulate some requirements, which must be fulfilled by a person who is willing to join the SACCO Society for instance:

- The question of age,
- The question of character
- The question of mental uprightness
- The question of loyalty
- The question of ability to save etc.

2nd Principle: Democratic Control, Administration and members' leadership

- SACCO Societies are democratic organizations controlled by their members, who actively participate in setting their policies and making decisions on issues of maximum loan amount and maximum Loan period to members, determining interest rate, determining election period, determining duration of elected Boards and committee, etc.
- Every member has equal voting rights, which is "One member One Vote Principle." Accordingly one member has only one voting right, regardless of whether he/she has high or small amount of money in savings and shares.
- This equality gives the members the proper basis for democratic management of their resources within their SACCO.
- The members elect a Board of Directors and other committees from among the members and even they have the right to drop out inefficient and unfaithful elected Board of Directors at any time.
- The highest responsibility for the individual members in developing democratic administration within their SACCO is attending the meeting which will held at monthly bases.
- This meeting helps members to have the opportunity to:
 - Protect membership rights,
 - Monitor if there is fair sharing of benefits or not,
 - Assign tasks to further benefits to all,
 - Build transparency among the members,
 - To discuss problems together and identify solutions by themselves.

If members they did not do these, with no doubt the Board of Directors and elected committee will have the chance to misuse the SACCO resources.

Be careful SACCO is dealing with money the most liquid and attractive asset:

- "Remember money builds and destroys anything in this world." Therefore, every member should watch carefully, either every resolutions passed by members are correctly implemented by Board of Directors and Committees in a right way with no exploitation of the resource or not.

3rd Principle: Member Economic Participation

Service to members

Members contribute equitably participation of share, savings and borrow loans, and democratically control the activity of the share, savings and loans.

The SACCO Societies should serve their members to improve their livelihood by giving safe place to save, teaching people how to generate income, how they can develop thrift culture, wise use of resources.

- SACCO Societies should be able to provide accessible loan to needy members based on the loan policy regulations and procedures for any productive purpose such as seed; fertilizer, plough purchases, other business etc.

Surplus return to member

- SACCO Societies are peoples owned financial institution; it grows not by transacting a commodity, rather profit is earned by attracting more savings and from which distributing sound loan accounts to members.
- It is true that the main objectives of the SACCO Societies are not to make aggressive profit, but it is also true that a well-organized and successful SACCO Society should end up with a balance of funds that enable it to protect members share and savings from any risk and allow expanding its financial services in the future.
- After the over head costs and other expenses are paid, reserves for loss, for expansion services are put aside the remaining Net profit from loan is return back to the members as dividend.

4th Principle: Continuous education, Training and Information to members and leaders

- Cooperation requires the acceptance of new ideas, new standards, new habits of thought and behaviors in its own interest and for its own survival. This should be supported by educating its members in appropriate way.
- Educating members by education committee enlightened members to understand their rights correctly, inspire them to fulfill their responsibilities as a member.
- Education encourages member participation on their SACCO issues. This member's participation is a key for the success to their SACCO development.

5th Principle: Autonomous and self-help.

- SACCO Societies are autonomous and self help financial organizations controlled and managed by members.
- If SACCO Societies enter into agreement with government or NGOs to raise their capital from external sources, it should be with the full agreement and say of members.
- This Agreement should ensure that every activity of the SACCO democratically controlled by their members and maintain their autonomy.

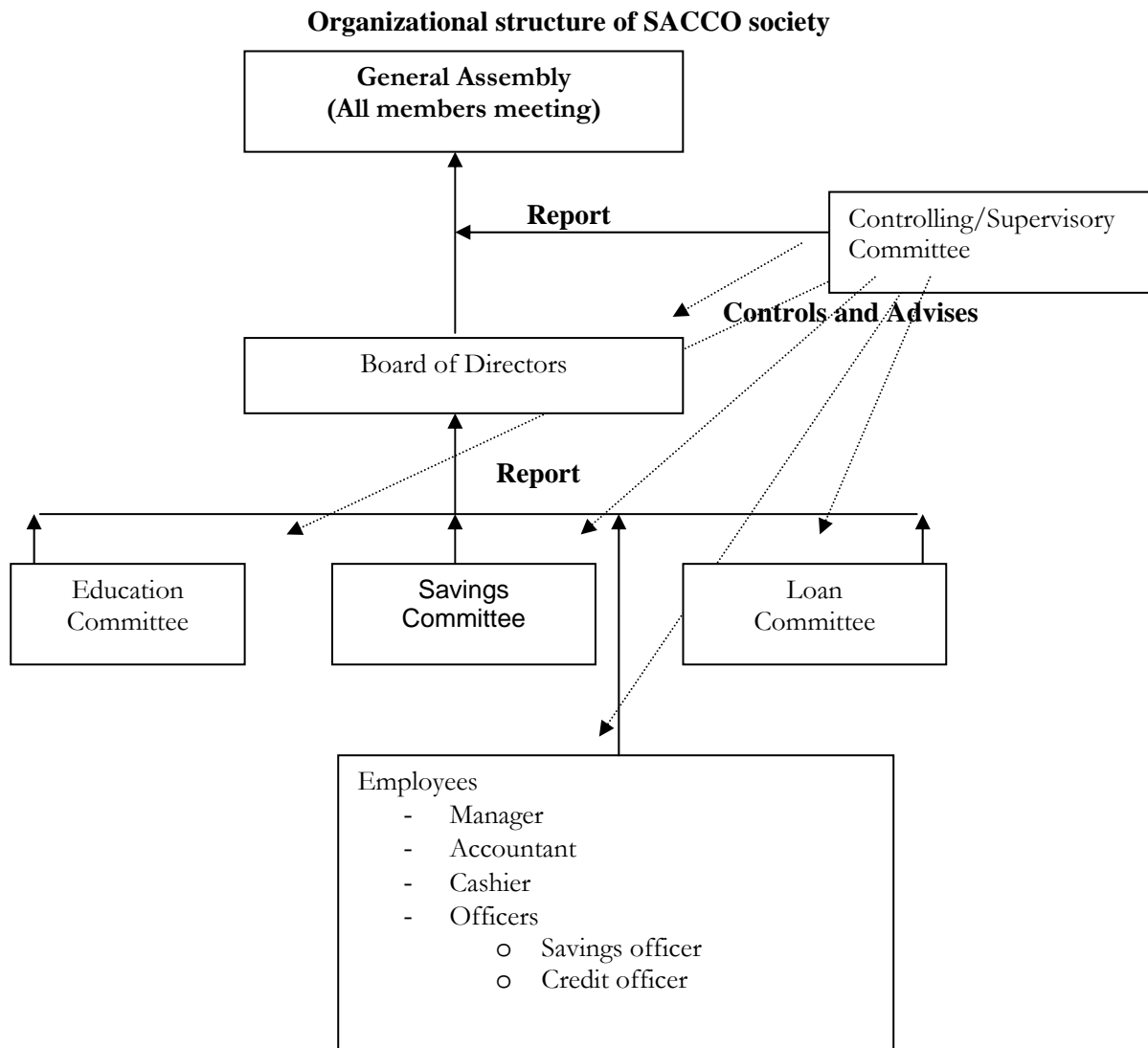
6th Principle: Cooperation among SACCO Societies.

- SACCO Societies should cooperate among them selves in order to best serve the interests of their members and the community at local, regional, national and international levels

7th Principle: Concern for the community.

- SACCO societies should work for the sustainable development of their communities through the policies approved by their members. That is:
- Teaching the youth to develop their saving culture
- Investing in school, hospital furniture improvements etc., from the social reserve fund.
- Intermediating and managing community fund, such as revolving fund given to the community from NGOs.

What is the Management Structure of the SACCO Societies?



- Based on the Organizational Structure each has specific roles and responsibilities in the over all operation of the SACCO Society, That is,

Members as owner-users,

- Board of directors and Committees as elected policy making and governing body,
- Hired Management as Supervisor and work force of the day-to-day activities.

Who runs and governs the SACCO?

The General Assembly -Owners meeting or Members as owner-users

- The General Assembly is the over all Superior Governing body of the ASCCO Society. Has the following power as an example: -
 - Adopt and amend the articles of the bylaws, policies and other internal regulations
 - Elect and if necessary remove elected board of directors and committees at any time.
 - Dissolve, unionize or merge their SACCO Societies.
 - Hold directors and officers liable for any damage injurious to members.
 - Examine activity, Audit reports and pass decisions on it.
 - Motivate active, honesty leaders, members and employees by reward.

Members responsibility

- i. In SACCO Society members' savings pool a lot of money that will lend to member.
- ii. Therefore, members should be serious in knowing and take the following responsibilities:

Patronize the SACCO Society with shares, savings and loans.

- i. Members must make a conscious decision to be committed and maintain that commitment even when competitors make more attractive loans with low interest rate than their SACCO,
- ii. Why? Members should make the commitment because of the following two basic reasons: -
 - a) In the first place the SACCO is their own financial institution, members can raise the problem and look at the options to solve it by their own participation.
 - b) Secondly the interest paid by the members goes back to the member as a dividend based on the capital participation, but the competitors never do this.

Be Informed about their SACCO

- i. To implement their responsibilities, members
 - o Must know what is a SACCO Society means?
 - o Must know what it can do for them?
 - o Must know the objectives, policies and problems that SACCO faces. Therefore, members should attend every month meeting to have adequate information about their SACCO.

Participate in selecting and evaluating elected directors and committees seriously and honestly

- i. Member should understand that electing the most popular or least controversial person is not the wisest choice for SACCO management.
- ii. Since SACCO deals with money, which is the most liquid asset, that expose easily to risk, members must study carefully to select those who have
 - o Skill of loyalty
 - o Integrity and truest worthy
 - o Willingness to work for Community development
- iii. Election does not mean the end of the member responsibility, members must keep in contact with the directors and committees to ask questions, make comments, request new services,
- iv. Member should observe and evaluate the directors and committee performance.

Understand and Adopt Legal papers

- i. Members are responsible to understand, adopt and amend the legal by law, policies and regulations of the SACCO Society; otherwise they will not benefit from their rights.
- ii. Therefore, members should read and understand each articles of the by law, policies and regulations to know how it operates and what services can they obtain from their SACCO.

Evaluate performance and Audit report: -

- i. Members should evaluate the annual performance and Audit reports, identifies the strength and weakens carefully.
- ii. Members should pass practical solution and decide their own roles for their Implementation.
- iii. Members should plan next year activities of the SACCO, that is potential members promotion, Saving mobilization, loan distribution and management, etc.

What are the duties and responsibilities of the Board of Directors and other committees?

- i. The Board of Directors
 - o It is true that SACCO Society is member owned, member controlled and run its service by member's leadership and wise decision.
 - o However, It is not possible for members perform directly all service activities of the Society. Therefore, The SACCO Society needs a key position to be held in between the members and hired management, which represents the members as user and owner of the SACCO Services.

- These representatives are the elected Board of Directors and Committee. We call it (BODC)
- The BODC have the power and Duties of managing and controlling the affairs of the SACCO in transparent way.
- The primary responsibilities of the directors are to hire the manager, other employees, establish operating environment and direct the SACCO to wards its overall objectives.
- The BODC have the duties of
 - ❑ Ensuring activities are carried out throughout the year to achieve the financial objectives and Goals.
 - ❑ Implementing resolutions passed by members at general meetings
 - ❑ Be honest, careful, reliable and hardworking members who have the interests of other members as a guide for all their action.
 - ❑ Not to be one of self-interest and exploitation of others.

There fore, in electing these BODC members should examine the following desirable qualifications carefully.

- ii. Trust worthy people who are interested in the development of their community, who have: -
 - Good judgment,
 - Sound moral character,
 - Respected by others,
 - Integrity skill,
 - Loyal for them self as well for their Duty,
 - And able to meet basic educational requirements.
- iii. Those who understand the constitution, by law of the SACCO and are capable to work as a team and willing to learn what the job requires i.e.
 - Requires willing to have the knowledge of the SACCO policies, procedures and acquisition of other skills such as committee work and planning,
 - It is very important to give due attention in having women director on the BODC with the same proportion as the number of males,
 - It is wise also to ensure that each part of the community is well represented on the BODC,
 - It is necessary and must all the members of the BODC are care fully defined powers, duties and should under stand them.
 - The SACCO members general meeting should elect: -
 - ❑ A chair person,
 - ❑ A vice- chair person,
 - ❑ A treasurer,
 - ❑ Chief accountant,
 - ❑ Secretary and if necessary other members that will work for emergency in Board of directors.
- iv. The other committees should have
 - Chair person,
 - Vice chairperson,
 - Secretary and if necessary other members.
 - ❑ According to the Cooperative Act and regulation of the country, the BODC should have specific period for their election, after that they must replaced totally,
 - ❑ After completing the specified years of work as BODC services in either the Committee, a person shall not be re-elected for any position by members. Members should not let them to be life time leaders of the SACCO Society
 - ❑ Members should figure out and clearly incorporate in their bylaw the period for how much years should the BODC is staying in the position of leadership.

The SACCO should elect a chairperson, a vice chairperson, a treasurer, a secretary and three to five more members. Ideally, the board would have between seven and nine members.

The chairperson is the team leader of the SACCO and the Board. He has many legal, management and leadership function. He should:

- Conduct meeting in an orderly, interesting manner, with Fact, fairness and without undue waste of time;
- Encourage soundboard group decisions and follow up on their implementation.
- Understand the management system and foster good relationships between members, board and staff;
- Be knowledgeable about co-operative principles, the SACCO operations and act as SACCO spokesman with the general public, government departments, and representatives of other organization connected with the SACCO.

The vice-chairperson is the “understudy” for the chairperson and should be familiar with all of his/her duties and have similar qualities as the chairperson. He /she stands ready to take over from chairperson, if at any time the chairperson is unable to perform his /her duties.

The secretary must have the ability to accurately record minutes of meetings, especially decisions and answer any correspondence for the board. Since the secretary is the recorder or writer for the SACCO, he/she should therefore be able to read and write well. Should record the members in membership registration book with detail history and open files for each member.

The treasurer should have some bookkeeping experience or be suitable and willing to be trained, so that he can understand the financial operations and position of the SACCO. He should be able to monitor and assist in the SACCO’s financial operations and understand the work of the manager, as necessary. The treasurer should be strictly honest, and willing to “blow the whistle” if he finds any mismanagement.

Chief accountant, should able to register all the transaction of the SACCO society on cash book, should able to follow the bank statement and report to chairperson with clear details of income statements and balance sheet, and should indicate the trend of the income to expense ratio with possible solutions, recommendation to correct over expenses and should work hard to minimize the expenses.

Should check the expense is within the monthly-approved budget and used for proper purpose of the SACCO, to protect from over expensing the SACCO.

Roles and Responsibilities of other SACCO Committees

Internal Control Committee (ICC)

In addition to the Board, each SACCO will have to put in place an Internal Control Committee (ICC). The ICC’s purpose is to monitor and verify the administrative and financial decisions made by the Board of Directors.

The Internal Control Committee (ICC) is selected at the annual general meeting and is independent of the Board of Directors.

It consists of a chairperson, Vice chairperson, secretary and other members. The ICC meets as required or at least monthly, to plan its work and prepare a report on its activities for the General Assembly. The SACCO shall strive to ensure that all of the members of the ICC have bookkeeping, accounting or auditing knowledge. If the members of the committee do not have this knowledge, the SACCO will take the necessary steps to provide this training. The Internal Control Committee (ICC)’s duties include:

- Periodic examination of member savings accounts to verify entries and balances;

- Checking that operations are being performed correctly by the Board, manager and cashier, according to predetermined routines, which including cash and bank reconciliation;
- Inspecting documents and auditing SACCO functions at least quarterly and more frequently as appropriate;
- Ensuring that loans are prudently handled, collected and repaid in a timely manner;
- Liaising with the bank regarding deposits, withdrawals or other internal audit matters;
- Verifying the credit committee's operations;
- Investigating complaints or appeals by members concerning their SACCO transactions;
- Calling special member meetings to consider any violation of the provisions of the constitution, by-laws or cooperative law, which it deems to be unsafe or unauthorized;
- Recommending to the board the suspension of any director, committee or staff member, pending a special general meeting of members to consider such suspension;
- Recording minutes for all meetings;
- Providing reports and making recommendations to improve policy and procedures;
- To ensure that the audit report is presented to the general assembly at least once per year;

Having strong internal Controlling committee in SACCO society means:

- Building transparency and trust of members on SACCO society,
- Building sense of ownership among the members,
- Avoiding risk to the elected committees, members and SACCO society savings,
- Giving more Benefits and equal service opportunity to members.

In addition to the ICC, three other standing committees are recommended; i.e., a Loan Committee and an Education Committee and a Saving Committee. Committee members are selected from among the board members. The roles and responsibilities of these committees are

Education and Saving Committee

The education and Savings committee (ESC) is selected at the annual general meeting and is responsible to report to the board of directors. It consists of a chairperson, Vice chairperson, secretary and other members. The education and Savings committee (ESC) even though they work very closely to attained the SACCO objectives; they are two different bodies, that is

The education committee mostly responsible to focus on sensitization and training of the SACCO members, elected leaders and hired staffs.

The savings committee mostly responsible to focus on saving promotion developing and introducing different kinds of Saving products; such as saving for kids, for school fees, etc. and following late savers and advising them.

The education and committee (EC) should prepare or update, annually, an organized education and training program to provide appropriate information, knowledge and skills of members as a team.

Topics will include:

- SACCO principles – self-help, mutual assistance, etc.
- Arrange members Discussion on by-law article by article at each month;
- Radio broadcasting on the advantage of SACCO for community development;
- Development – emphasis on human resources, development of leadership.
- Developing habits of thrift – prudent use of resources within the community by focusing on youth education.
- Constructive use of credit – resulting in economic, social, family betterment.

The EC will:

- Identify member educational needs and propose work plans to address those needs;
- Organize, facilitate and promote education and training of the members;
- Prepare a program for recruitment of new members;

- Identify, collect, disseminate and/or publish SACCO news for the benefit of the members;
- Develop and implement a program to promote the use of the savings and loan products;
- Create a favorable SACCO image.
- Make reports on its activities to the management and board.

Loan Committee

The Loan Committee (LC) selected at the annual general meeting and is responsible to report to the Board of Directors. It consists of a chairperson, Vice Chairperson, Secretary and other members.

The Loan Committee (LC) has the responsibility to ensure that SACCO funds are secure when granting a loan. The LC must be prudent when granting loans.

The LC recommends loan applications to members of reliable character for productive purposes. The SACCO Board will approve this recommendation for loan application.

Indiscriminate lending should be discouraged since it can be harmful to members and lead to unnecessary costs and loan delinquency. The LC will set standards for approving loan applications, which do not eliminate deserving applicants.

The LC should meet at least once a week to consider loan applications; however, more frequent meetings may be necessary, if the number of loan requests justifies it. The LC must have a quorum (simple majority) of its members before its deliberations and decisions are valid.

The LC's function is to analyze the loan requests by being able to answer two fundamental questions about each loan request:

- **Can** the member repay the loan?
- **Will** the member repay the loan?

To answer these questions, the LC must carefully evaluate each loan request, including all of the supporting documentation, in terms of:

Character: Personal integrity of the business owner(s) and family: -

- How is the business managed?
- Are they honest and trustworthy?
- What is the physical and mental health of the person(s) running the business?
- Have they repaid bills and previous loans on time?
- Do they have family problems (alcohol, frivolous spending, etc.)?
- What is the innovation and creativity of the business in creating new business and growth opportunities?

Capacity: Ability of the business to repay the loan: -

- What does the business plan indicate about income and profitability of the business?
- Can the business generate enough cash to make the loan payments with interest, including a margin of security?
- When can the loan be repaid?
- What are the family needs?
- What are the effects of seasonal fluctuation and production and price variations?
- How does the business compare to others within the same sector or activity?

Capital: Money invested in the business: -

- What money and assets are invested in the business?
- What is family contribution to the business?

Collateral: Backup sources of repayment for the loan: -

- Are the personal guarantees of the group or persons trustworthy?

- Are the assets of the business and personal guarantees adequate to cover the loan if necessary?

Conditions: Key economic factors that impact on the ability to repay the loan: -

- Is there an adequate and stable market to sustain the business?
- Is the loan terms (lengths, interest rate, etc.) adequate for repayment capacity of the loans?
- What are the price and production risks?

What are the general market trends of the sector? There fore the condition should be care fully examined the location, current customer, and market potentiality for the product cash flow, etc.

The LC will:

- Inquire carefully and diligently into the reputation and financial condition of each applicant for a loan and the quality of its collateral, if any, to ascertain its ability to repay fully and promptly;
- Recommend to the management the approval or denial of all loan applications;
- Maintain minutes of its meetings and records of its actions; and
- Make such reports to the management and the board as may be required.

The Loan committee has the responsibility to:

- Ensure the SACCO funds are secure
- Examine care fully and diligently into the reputation and financial condition of each applicant for a loan and the quality of its collateral and the ability to repay fully.
- Recommend to the management (BOD) to approve or denial of the application with justification
- Maintain minutes of meeting and records of its actions.
- Make such reports to the BOD
- Follow the borrower either the loan is doing for the requested application or not and report to his/her Guarantors
- Ensure that the Guarantors have the ability to enforce the borrower, when he/she will come to fail repaying the loan on time.

What are the duties and responsibilities of the hired management and employees?

The manager

- The manager is an employee of the SACCO society and accountable to the Board of directors for his/her action.
- There fore, the manager should not be part of the board that hires and set the salary for him/her.
- The manager should be required to attend all board meeting with all information for BODC Discussions and encountered problems that require BODC decisions, though he/she is an active non-voting participant.
- The manager is responsible for the overall operation of the SACCO Society delegated by the BODC.
- He/she is expected to do all management functions-
- Planning,
- Organizing,
- Directing,
- Coordinating,
- Controlling of all the SACCO resources and day-to-day activities including personnel's.
- He/she has the responsibility of
- Maintaining and revising all necessary book keeping and accounting system,
- Furnish information need for long or short term planning of the SACCO,
- Encourage membership promotion and active participation of members,
- Communicate the SACCO development and performance among members,
- Educate the public the importance of SACCO society by focusing on the youth using posters, organizing awareness workshops, and regular advertisings,

- Reporting current issues and problem with possible recommendations to the Board,
- Keeping informing the board about the current local state, federal regulations and pending legislations that might affect the SACCO,
- Encourage the employees to understand the objectives, goals and relationship of member's satisfaction with Success of the SACCO.

The Employees Duties and responsibilities:

- They should understand the purpose and objectives of the SACCO that helps them to improve members' relations with their SACCO,
- Fully perform their duties and make the SACCO profitable.
- Understand the relation ship of members with the SACCO and able to provide efficient services to members,
- Build members confidence and satisfaction on their SACCO to motivate them to be more committed for their SACCO.

What are the Norms and values expected from members?

- The philosophies of SACCO societies are founded on **“cooperation among peoples to help themselves”**. Based on this philosophy any man or women to be a member must believe in:

The values of

- Self-help, self-reliance and mutual-help
- Equity, equality
- Solidarity and
- Democratic control

The Norms of

- Honesty and loyalty
- Openness
- Concern for other members and the community by avoiding selfishness

What are the important factors for the success of the SACCO?

Strong and all rounded members participation.

SACCO societies are organization of voluntary people not money. There fore, the success of the SACCO society lies not on the money, which may be mobilized from members or Donated from NGOs. But the success of the SACCO society lays on the strong and all rounded members' participation.

- Wise and sound members have good participation in identifying and electing.
 - Dynamic and sound management committee
 - Dedicated, honest and hardworking committees.
- Wise and sound members have good participation in
 - Demanding, proposing, pushing
 - Criticizing, motivating and supporting the BODC.
 - Promoting potential members by teaching the importance of SACCO and saving giving special focus on youth
 - Pressurizing the defaulters and forced them to pay back the loan on time
- These participations are playing a major role for SACCO society success. Therefore, members should believe and participate in the SACCO society as
 - Owners
 - Leaders
 - Decision makers
 - Internal controlling body
 - Beneficiary
 - Promoters

Following strong financial concepts and building strong financial operations:

Viability: the SACCO should follow the principle of minimize operational expenses, minimize risks, cover its costs and increase its yearly fair financial margin in order to expand its future services.

Self-reliance: the SACCO should target to mobilize members and members saving aggressively every year. Members and elected committees should work closely to mobilize their own financial resources from members.

Members and elected committees should not depend on external fund, external fund brings many problems to the SACCO, It is not possible to access external fund without being influenced by their particular ingredients. Some features attached to external fund are negative, some are positive but others can be highly dangerous for SACCO as financial institutions depending on the situation, that is:

- **Interference of decision on SACCO issue by fund owners:** - the fund owners start to dictate the SACCO and direct it to wards of their interest that will violate the principle of autonomous, members decision, and members leadership in the SACCO, all decisions will be done to fulfill the interest of the fund owners not to fulfill the interest and benefit of members.
- **Unable to fund savings and loans on time:** if the fund owners follows very bureaucratic systems and fails to give the Fund as they promised, the SACCO will not able to give loan service to members on time, that contributes a lot for members dissatisfaction which will drive members to withdraw from their SACCO, that will lead immediately to the collapse of the SACCO.
- **High probability of loan defaults:** if the SACCO members aren't convinced to save their money in the SACCO, the SACCO will not be able to build strong collateral for members loan as well as the members will not have sense of ownership, and if members get loans from the external fund they are not ready to pay back the loan on time, because they start to think the loan will not repay back to the owner, this condition can quickly destroy the SACCO.
- **Encourages dependency:** instead of building and utilizing their own resource properly the members start to build dependency and less confidence on their own.

Therefore, Every SACCO as financial institution should analyze the specific impacts of each external fund on its aims, viability, sustainability and autonomy before rushing to accept it.

Sustainability: the Members and elected committee of the SACCO should work to build reserves from yearly financial margin and preserve them every year to protect from possible future unexpected risk. As well as; the elected committee should build transparent methods; encourage member's participation and member's sense of owner ship.

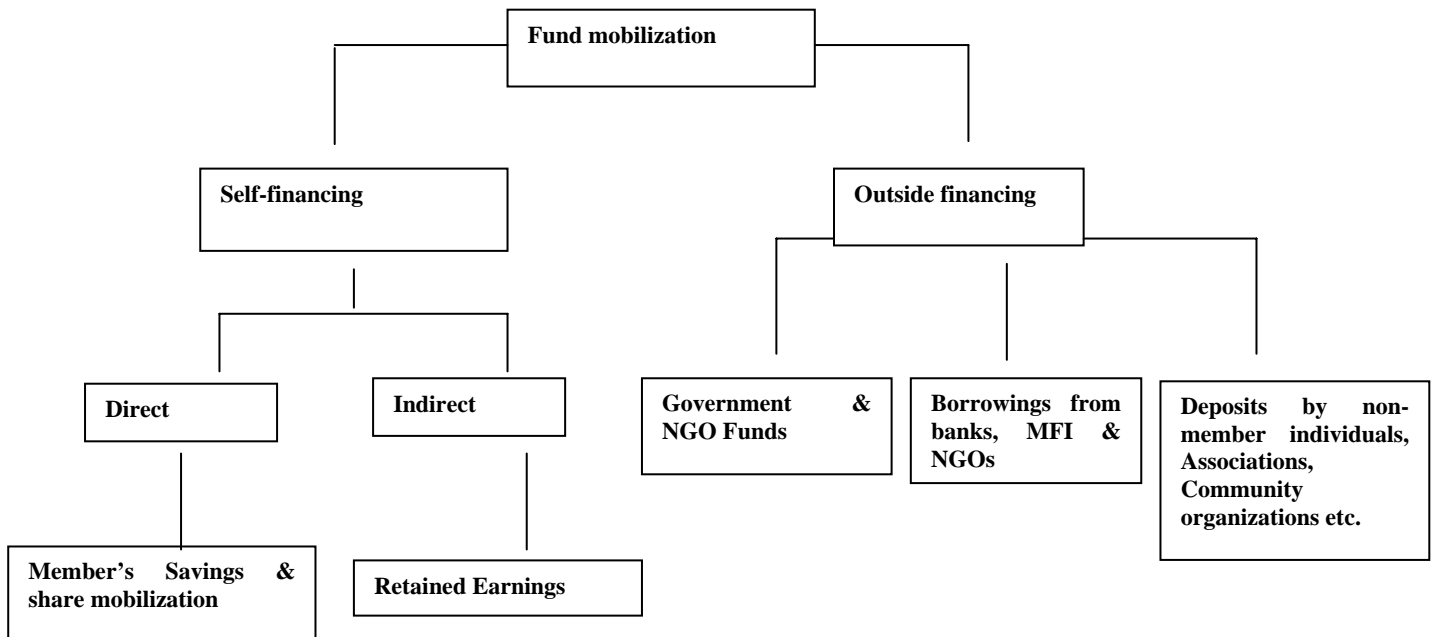
Outreach: - the SACCO should broaden its service by giving Safe place for savings, lending for various activities, and increasing the penetration rate within the society by encouraging women, the youth and the poor to be members.

Impact: - the SACCO should build self- help and self-financed society by promoting the saving culture of the society focusing on the poor and the youth.

What is the main source of finance in SACCO?

- SACCO Societies as financial institutions can raise their funds internally (self-financing) and externally (outside financing). However, SACCO Societies are basically advised to finance themselves internally from members Savings, share mobilization and retained earnings, to avoid interference of decision on SACCO issue by fund owners, to be self secured and sustainable in the future.

Finance in SACCO Societies can be mobilized as follows.



Who may join this a SACCO society as a member?

- SACCO society is founded by cooperation of voluntary people to help each other with voluntary and open to all principals.
- Based on these principles
 - Any one who is ready to accept the bylaws, policies and regulations of that SACCO may join and share its owner ship,
 - Any one who is able and willing to save the minimum of saving adopted by the society may join and share its owner ship,
 - Any one who is living around and participate actively may join and share its owner ship.
 - Any one who is able to use the services and willing to accept the responsibilities of membership stated by general Assembly may join and share its owner ship.

What are Savings and Shares and what is the relationship between them?

What is saving?

- Saving can be defined simply as holding something back from today's consumption.
- Saving means with holding some thing valuable to day for future use.
- Saving is not as simple as the word as we talk it. Saving is
 - A Discipline
 - A Sacrifice
 - Planning. What does it mean?
- Saving is **discipline**, because it teaches people to use their resource in a wise manner and develop an Asset in the future.
- Saving is a **sacrifice**, because it teaches people to give up today's expenses and to with hold valuable resource for future possible out coming instead of consuming immediately.
- Saving is **planning for tomorrow (future)**, because
 - Saving teaches people to anticipating, forecast and preparing for possible risks and emergencies (bad harvest, sickness and death)

- Saving teaches people to think on starting a new business or expanding existing once.
- Saving teaches people to anticipating and preparing for up coming events and expenditures (School fees, Marriage, old age, retirements etc).
- Therefore, saving is everything, which can empower human being to have bargaining power, makes him self secured and person with full confidence.
- In the SACCO society, saving is an asset to members, and a liability to the SACCO society.
- In the SACCO society, saving is collected from member to on lend to members.
- Saving is sources of income to the SACCO society because it lends to members with interest.
- This loan interest is the main source of income of the SACCO society
- For a SACCO society it is a must to have a regular Saving flow from members, to efficiently serve financial services to members.
- In SACCO societies we have three kinds of Savings
 - Compulsory Savings
 - Voluntary Savings
 - Contract Savings (Time Deposits)

Compulsory savings

- Compulsory saving is a saving that a member forced to save on regular basis; it is a membership saving i.e. must be saved on monthly basis.
- This compulsory saving is collected to on lend to members
- If members fail to save on time they will get penalized based on the saving policy of the society.
- Unless the member quits from membership, he should save on regular basis.
- If a member wants to with draw from the SACCO society, he has the right to take this compulsory saving with one-mouth priors notes to the Board of Directors.
- The society will provide interest for this savings.

Voluntary savings

If the potential SACCO members are farmers and only receive income once or twice a year, how can they save the appropriate amount at the appropriate time?

- This kind of saving is very important to farmers since they don't have regular income they can save as voluntary saving during harvest time, and transfer monthly to their compulsory saving accounts. Voluntary savings are deposited and withdrawn as the member sees fit. Farmers, and other individuals, can save the full amount for the coming year's compulsory savings in advance with the SACCO by depositing 12 months worth of saving in a voluntary account. Following that, each month on the appropriate day the member will come to the SACCO to withdraw the amount of one month's compulsory saving from the voluntary saving -account and deposit it in the compulsory saving account. This maintains the fundamental function of the SACCO and allows individuals with seasonal incomes to be members. Technically speaking, this is referred to as *saving up*.⁵
- This ensures regular flow of cash to the SACCO society and promotes members participation.
- This kind of saving can be withdrawn at any time when the owner needs it.
- The SACCO society may or may not provide saving interest for this voluntary savings.
- Farmers are highly advised to save on voluntary saving for small capital investment lick purchasing seed for cultivation.

Contract savings (time deposits) or fixed deposit

- This kind of saving will not be invited unless the SACCO society acquires good experience in managing their savings and loans properly.

⁵ Saving in advance for anticipated- future' obligations is called **saving up**. Borrowing to meet anticipated future obligations and repaying the loan in the future when the individual has money is called **saving down**. Saving down is considered as bad financial behavior because it is always less expensive to use once own money rather than borrowing someone else's money.

- This kind of saving will invited in the future when the SACCO society is in a good capacity and position of managing its savings and loans properly and if there is a shortage of feasible financial demand by members.
- This kind of saving can be collected from members and none members but the amount, period of collection and interest for this Saving should be decided by the General Assembly of members.
- Time deposit brings the opportunity of high interest rate on savings.

What is a share?

- Share is the capital of the SACCO society and an asset to members.
- Share is a risk protecting capital that collected from members in proportion to compulsory savings
- Since share is risk protecting capital it should be saved in a bank.
- If a member wants to with draw from the SACCO member ship he/she has the right to take it after 12 month or after Audit.
- This is to protect the SACCO from any loss and to give the member the chance of having dividend for the period he stays as a member with in the society.
- Therefore, every member should buy shares based on the amount of compulsory saving he/she deposits in the SACCO as it indicated in the following table.

Proportion of compulsory savings to share or 3.5:1 savings to share leverage ratio

	Compulsory savings 3.50	Share 1.00	Total monthly saving 4.50	Total per harvest saving	Total yearly saving 4.50
1	3,500	1,000	4,500	27,000	54,000
2	7,000	2,000	9,000	54,000	108,000
3	10,500	3,000	13,500	81,000	162,000
4	14,000	4,000	18,000	108,000	216,000
5	17,500	5,000	22,500	135,000	270,000
6	21,000	6,000	27,000	162,000	324,000
7	24,500	7,000	31,500	189,000	378,000
8	28,000	8,000	36,000	216,000	432,000
9	31,500	9,000	40,500	243,000	486,000
10	35,000	10,000	45,000	270,000	540,000
11	38,500	11,000	49,500	297,000	594,000
12	42,000	12,000	54,000	324,000	648,000
13	45,500	13,000	58,500	351,000	702,000
14	49,000	14,000	63,000	378,000	756,000
15	52,500	15,000	67,500	405,000	810,000
16	56,000	16,000	72,000	432,000	864,000
17	59,500	17,000	76,500	459,000	918,000
18	63,000	18,000	81,000	486,000	972,000
19	66,500	19,000	85,500	513,000	1,026,000
20	70,000	20,000	90,000	540,000	1,080,000
21	73,500	21,000	94,500	567,000	1,134,000
22	77,000	22,000	99,000	594,000	1,188,000
23	80,500	23,000	103,500	621,000	1,242,000
24	84,000	24,000	108,000	648,000	1,296,000

Based on the above example and based on their income Members they should decide to save the maximum amount, as much as they can. This decision will also have direct relationship with the chance of getting the maximum amount of loan from their SACCO society.

That is, if one member has the willing to save 27,000 per month in both the compulsory Saving and share, he/she will have the chance to accumulate 252,000 in Compulsory Saving and 72,000 in shares at the end of the year. If the SACCO loan policy qualifies members for loan of two folds of what they have in their Compulsory Saving, He/she will has the chance to get 504,000 loans at the end of the year.

On the other hand, if one member has the willing to save 36,000 per month in both the compulsory Saving and share, He/she will have the chance to accumulate 336,000 in Compulsory Saving and 96,000 in shares at the end of the year. If the SACCO loan policy qualifies members for loan of two folds of what they have in their Compulsory Saving, He/she will has the chance to get 672,000 loans at the end of the year.

If one member has the willing to save 45,000 per month in both the compulsory Saving and share, he/she will have the chance to accumulate 420,000 in Compulsory Saving and 120,000 in shares at the end of the year. If the SACCO loan policy qualifies members for loan of two folds of what they have in their Compulsory Saving, He/she will has the chance to get 840,000 loans at the end of the year.

There fore, members are highly advised to save to their maximum capacity as much as they can.

Can the poor save as a member?

SACCO services exist to help the poor to manage his/her savings with in his area, but what if s/he has no capacity to save? How can the poor, who have barely enough money to live on, possibly save?

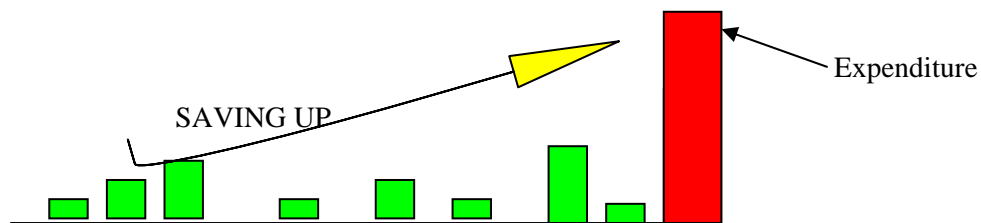
Research on how poor people in the developing world manage their money shows poor people can and do save.

The main objective SACCO Societies is to develop saving culture among a given society.

What is the Advantage of Saving first over Loan first?

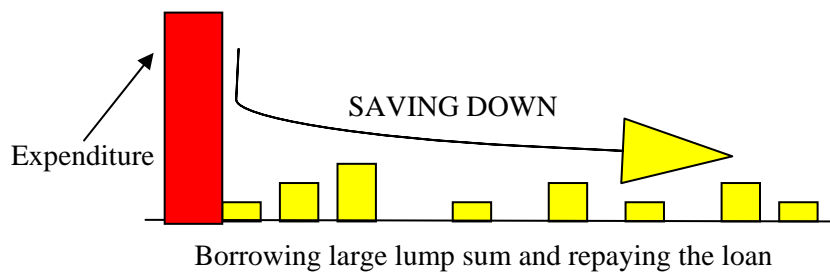
There are three basic patterns through which poor people savings can be converted into useful, large sums of money for spending: “saving up,” “saving down,” and “saving through.”

Saving up is savings are stored until they have accumulated into a sum large enough to serve some expenditure need. This could be in terms of cash, or in kind especially small size livestock rearing and fattening. But this kind of Saving doesn’t have continuity and he/she will start again from scratch no future improvement life will continue as usual.

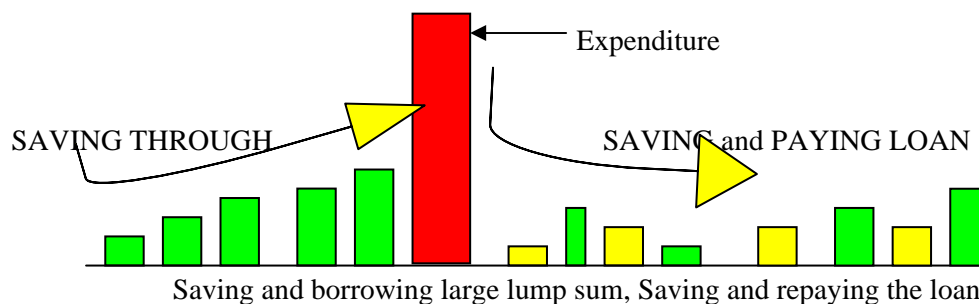


After several months savings become large lump sum and used for expenditure.

Saving down refers to borrowing and repaying the loan. Repaying loans depends just as much on the act of saving as does saving up. The only difference is the lump sum becomes available before, rather than after, a series of savings. The savings, of course, are used as repayments on the loan—either in intervals as income is realized or after a secondary process of saving up until enough has been accumulated to pay off the loan in a single balloon repayment.



Saving through is a mix of saving up and saving down. A lump sum becomes available at some point during a series of savings. Good examples can be found in many types of insurance coverage: saving is performed continuously as a series of, say, monthly automobile insurance premium payments, and the lump sum becomes available when you crash into a gatepost.



What is a loan?

- Loan is having some one's money for productive, for school fee, etc and that will pay back at agreed period with additional interest.
- Having a loan (borrowing)
 - Can be expensive
 - Can be risky
 - Can be difficult
 - Can be stressful.
- It can be expensive because borrower will have to pay the loan it self with additional interest more than or equal to what it produces.
- It can be risky because may exposed to risks caused by weather, in come fluctuations, disease and death, that may create a problem for repayment
- It can be difficult the poor has more difficulties in obtaining loans than the rich.
- Local moneylenders, friends, even families and banks are unwilling to lend to people they think will have problems to repay.
- It can be stressful because loan involves promise to repay to the lender
- Failure to repay may mean losing of valuable possessions (cow plot of land) etc or losing good reputation and resections.
- There fore loan (borrowing) must be examined and treated carefully and honestly in the SACCO society.
- The SACCO society should assigned people as a Loan committee.
- The Loan committee. (LC) must able to answer the two fundamental questions of each loan applicant i.e.
 - Can the member repay the loan?
 - Will the member repay the loan?
- To answer the two fundamental questions, the Loan committee needs to apply the above already mentioned 5'c of lending techniques:

What are the criteria's that qualifies a member for a loan?

- Saving regularly,

- Fulfilling his duties and responsibilities,
- Personal integrity of the business owner(s) and family,
- Honest and trustworthy,
- Ability of the business to repay the loan,

Should SACCO Societies give cheap loans to members?

- No, SACCO societies should not be expected to give cheap loans to members, because like any business organization, SACCO societies should give services to their members with fair interest rate of loan by covering their operational cost, fund cost, possible risk and predicting future sustainable services to members.
- On the other hand, study shows cheap loans attract the powerful and encourage corruption; the probability of the loan reaching the poor is low. Cheap loans are repaid last; cheap loans borrowed by anyhow without plan and are unprofitable. Therefore, the rate of repayment becomes very low because borrowers never use the money to generate income and so the organizations giving cheap loan become unsustainable.
- Therefore, members need to understand what will be the effect of cheap loan service to the future sustainable existence of their SACCO. If members need to have sustainable financial service, they should decide fair lending interest that could cover all its costs and risks.

How is lending interest rate determined?

- Since SACCO societies are founded, owned by members and operated by member's full participation and decision of members.
- The interest for lending should be determined by full understanding and stronger participation of members.
- Of course the board of directors can come up with their proposed lending interest to the member's general Assembly, for discussion and approval of the interest for lending. However, It has to be decided and approved by members.

What factors should be considered in determining the interest for lending?

- Interest for lending should be determined by considering the factors that has to be included in, very carefully.
- One cannot say banks and MFI around this area they lend money to beneficiaries at this interest rate per month or per year. There fore, our SACCO should be able to give us with less or equal interest rate of them.
- One can no longer rely on such guesses " we should check the time against a watch" there fore, in determining the lending interest the necessary factors that must be considered.
- in setting interest rates, the SACCO has to bear both its costs and the market conditions in mind.
- These factors are basic tools that will help your SACCO society to serve member by operating at break even and possible profit margin.
- These factors are able to make your SACCO to build strong financial institution.
- These factors are able your SACCO to have strong future reserves that makes to with stand harsh conditions.
- These factors should insure in
 - Preventing the erosion of the value of members savings,
 - Mobilizing their own financial resources in the future,
 - Charge rural market rate of interest on loan,
 - Cover all their costs, and
 - Make fair profit for future service expansion to members.

The factors for calculating lending interest are:

- Cost of fund (CF)
- Operational costs (OC)
- Profit (growth) (P)
- Loan loss reserve (LLR)
- Inflation cost (IC)

The formula to be used to determine lending interest is

$$\text{Lending interest} = \text{CF} + \text{OC} + \text{P} + \text{LLR} + \text{IC}$$

Let us see what these Factors in detail are: -

Funds Cost (FC)

- Funds Cost (FC) is the cost the SACCO will pay to the money collected from any source to on lend to members as a loan.
- Usually the SACCO will have multiple source of fund;
 - Mainly it mobilizes money from members as a Savings for which the SACCO will pay interest on savings to member’s savings, this is the cost to be paid to member’s savings.
 - The SACCO may borrow from a bank with fixed interest rate cost; this is the cost to be paid to bank.
 - The SACCO may receive capital donation from a donor agency with zero interest rate or zero cost.
- In order to treat all members fairly, it should average all the cost of funds coming from various sources as mentioned above.
- This can be done using weighted average. By this weighted average system every member gets the same interest rate and some are not favored with borrowing cheap funds while others borrow expensive funds.
- To understand this weighted average let us review the following example: -

The SACCO’s members’ demand for loan is 100,000,000 shilling.

- The SACCO able to raise 35,000,000 shilling from member’s savings for which it must pay 6.5% per year.
- The SACCO will borrow the balance 65,000,000 from a bank at 17% per year.
- If the SACCO borrows bank funds it must insure its collateral at a rate of an additional 1% per year only for the bank loan.
 - Calculate the weighted average fund cost for the SACCO.

Solution

- Because the SACCO must insure its collateral for the bank loan, we must first observe that the real cost of funds from the bank is the 17% per for the loan plus the 1% per year for the insurance, which equals 18% per year.
- Because the SACCO can use members’ saving funds for 6.5% per year and this is much less expensive than 18% per year from the bank, the SACCO will use the members’ saving funds to the greatest extent possible.
- To determine the cost of funds, we should take a weighted average of the two sources using the following formula:

$$\frac{\text{Loan Amount 1}}{\text{TOTAL CREDIT DEMAND}} \times (\text{Interest rate 1}) + \dots + \frac{\text{Loan Amount n}}{\text{TOTAL CREDIT DEMAND}} \times (\text{Interest rate n})$$

$$\frac{35,000,000}{100,000,000} \times (6.5\%/year) + \frac{65,000,000}{100,000,000} \times (18\%/year) =$$

$$0.35 \times (6.5\%/YEAR) + 0.65 \times (18\%/YEAR) =$$

$$0.35 \times 0.065 + 0.65 \times 0.18 =$$

$$0.02275 + 0.117 = 0.13975 \times 100\% = \underline{\underline{13.975\%/year}}$$

The SACCO's members' demand for loan is 100,000,000 shilling.

- The SACCO able to raise 35,000,000 shilling from member's savings for which it must pay 6.5% per year.
- The SACCO will borrow the balance 45,000,000 from a bank at 17% per year.
- If the SACCO borrows bank funds it must insure its collateral at a rate of an additional 1% per year only for the bank loan.
- The SACCO will get the balance 20,000,000 from an international NGO for five year by paying 2% per year for capital protection.
 - Calculate the weighted average fund cost for the SACCO.

Solution

- Because the SACCO must insure its collateral for the bank loan, we must first observe that the real cost of funds from the bank is the 17% per for the loan plus the 1% per year for the insurance, which equals 18% per year.
- Because the SACCO can use members' saving funds for 6.5% per year and this is much less expensive than 18% per year from the bank, the SACCO will use the members' saving funds to the greatest extent possible.
- Because the SACCO must pay 2% per year capital protecting fund for five year to get the fund from international NGO and this is much less expensive than 18% per year from the bank, and SACCO members' saving funds for 6.5% per year, the SACCO will use all funds to the greatest extent possible.
- To determine the cost of funds, we should take a weighted average of the two sources using the following formula:

$$\frac{\text{Loan Amount 1}}{\text{TOTAL CREDIT DEMAND}} \times (\text{Interest rate 1}) + \dots + \frac{\text{Loan Amount n}}{\text{TOTAL CREDIT DEMAND}} \times (\text{Interest rate n})$$

$$\frac{35,000,000}{100,000,000} \times (6.5\%/year) + \frac{45,000,000}{100,000,000} \times (18\%/year) + \frac{20,000,000}{100,000,000} \times (2\%/year) =$$

$$0.35 \times (6.5\%/YEAR) + 0.45 \times (18\%/YEAR) + 0.2 \times (2\%/YEAR) =$$

$$0.35 \times 0.065 + 0.45 \times 0.18 + 0.2 \times 0.02 =$$

$$0.02275 + 0.081 + 0.004 = 0.10775 \times 100\%$$

$$= \underline{\underline{10.775 \%/year}}$$

Operational cost (OC) is all costs incurred by the SACCO in doing its operation. That is mobilizing savings and credit business from members to members. Operational costs include stationary, Transportation, Building rent, electricity, depreciation cost, Employee salaries, advertisement and promotion cost, per diems, Auditing cost, etc. Therefore, the SACCO should include these costs and collect from the borrowers in the loan interest.

Normally, these costs are measured in cash values. These cash values must be converted into an annual percentage cost. We arrive at the percent cost by taking the ratio of total operation costs to the credit extended and multiplying by 100%.

Example

- Total operational costs for the SACCO Saving and credit operations are estimated to be 3,500,000/=
- The SACCO will extend 100,000,000/= in credit to members.

Calculate the operational cost of the SACCO, using the following formula

$\frac{\text{Total Annual estimated operational costs}}{\text{Total Credit demand}} \times 100\%$

$$= \frac{3,500,000}{100,000,000} \times 100\%$$

$$= 0.035 \times 100\%$$

$$= \underline{\underline{3.5\%/year}}$$

Profit is some times called Margin, Growth Premium, etc. it is the profit that enables the SACCO to grow in the future and extend greater services of savings and credit to members at lower cost in each subsequent years.

According to the Cooperative principles, members should receive limited return on their equity as dividend and retained a portion of the profit for reserve, expansion, and social fund in the equity of the SACCO.

As the SACCO increases its equity through retained profit, the fund cost for loan will lowered, because the SACCO will able to accumulate more money with zero cost from year to year, that can be on lend to members as a loan.

Remember the above example of fund cost calculation, we need to pay 6.5%/year for members' saving and 11.5%/year for the bank plus insurance 1%/year, 2% per year capital protecting fund for the international NGO fund.

As the SACCO increases its equity by retaining from the annual profit each year, the SACCO need to borrow from bank less and less. This makes credit less costly to the members and allows the SACCO to give more service to members in the future.

Therefore, the members should decide and set the annual profit level that allows aggressive growth to the credit operation of the SACCO, and also consider that the decision should encourage the members to apply for loan.

There is no absolute and ideal percentage of Profit, it can be decided by exercising in trial and error, and to make the SACCO self-financing institution in the future members decided fair Profit percentage.

Loan loss reserve (LLR)

Loan loss is one of the most common problems that can quickly destroy the SACCO if the member's general assembly doesn't allocate remedy ahead, such as proper loan policy and loan loss reserve (LLR).

Loan loss reserve (LLR) is the reserve used to replenish funds lost to the portfolio when loans are written off. It is very likely that not all members will repay their loan on time called **Arrears**, and some members will not repay at all called **Defaulters**. Both of these situations will result in losses to the credit operation and this loan loss is the main cause of collapse for any financial institution, if it is not well managed ahead.

Loan loss reserve is essential for any financial institution involved in lending money. The non-recoverable amounts lost from the portfolio are replaced by the income earned from loan interest. Normally, financial institutions estimate the amount of expected bad debt or loan loss on the basis of prior experience and estimated potential losses from the current portfolio, and express it as a percentage of the portfolio.

Most of the time well-managed SACCO should not have loan loss exceeding 3 percent of the average portfolio in any given year. Therefore, loan loss reserve should maintained annual losses at 3 percent of the average portfolio and the interest rate charged to borrowers should include 3 percent to maintain that loan loss reserve.

Loan loss is the main reason for SACCO faller. Therefore, The SACCO Manager or the Board of directors as a financial institution should submit suitable loan loss reserve proposal to the member's general assembly and show the risk which will expected if it is not managed ahead.

Inflation cost (IC)

Inflation is decreasing the purchasing power/value of a give currency or price rises of Commodities. SACCO has the objective of safeguarding the value of member's savings in real terms each year, to protect the value erosion of member's savings.

In most countries the inflation rate is higher than the interest rate for Savings, most people are unaware of this and lose money every year or the real value of their saving decrease every year. Therefore, to maintain the value of its member's savings and pay the real return to members, the SACCO should collect money from lenders. To collect money from lenders, inflation cost should include in the calculation of the interest for loan.

Inflation can be got from national bank on quarterly basis. If not it can be estimated by recording the price of goods each month and measure the change on quarterly basis using the formula of new price less old price divided by old price and multiply the result by hundred percent.

$$\text{Inflation} = \frac{\text{New Price} - \text{Old Price}}{\text{OLD PRICE}} \times 100\%$$

Since inflation is only an estimate of quarterly loss in purchasing power, it is reasonable to annualize this figure by multiplying it by four to get the yearly inflation rate.

Example, if inflation is estimated at 2% per quarter

The yearly inflation will be 2% per quarter X 4quarter per year = 8% per year

Therefore, Interest rate for lending should be determined by summing up the Cost of fund (CF), Operational costs (OC), Profit (growth) (P), Loan loss reserve (LLR) and Inflation cost (IC). That is:

$$\text{Interest rate} = \text{CF} + \text{OC} + \text{P} + \text{LLR} + \text{IC}$$

From the above examples we have Cost of fund (CF) **13.975%/year**, Operational costs (OC) **3.5%/year**, Profit (growth) (P) **5% growth per year**, Loan loss reserve (LLR) **3 percent** of the average portfolio, and inflation cost (IC) 8% per year.

$$\begin{aligned} \text{The first Interest rate} &= 13.975\% + 3.5\% + 5\% + 3\% + 8\% \\ &= \underline{33.475\%} \end{aligned}$$

$$\begin{aligned} \text{The second Interest rate} &= 10.775\% + 3.5\% + 5\% + 3\% + 8\% \\ &= \underline{30.275\%} \end{aligned}$$

What is the cost and benefit of being a SACCO member?

The Cost

- The cost to be paid from the member is nothing when it compares with the advantage he/she will receive after joining as a member. To be clear the cost of the member needs to pay to the SACCO will be

- Willingness to join the SACCO and Accept the laws, regulations and responsibilities, ready to spent time in the SACCO meetings,
- Registration fee,
- Strong participation in all the SACCO movement and assignments, ready to spent time in promotion of new members and creating pressure for defaulters.

The benefit

- Time minimization, cost of transport minimization, risk minimization,
- Wealth accumulation, Building Collateral and Guarantors for loan,
- Building easy accessible financial institution, i.e. save place for Savings and loan with in his/her village,
- Building bargaining power to negotiate with financial institutions to get long term investment loans,
- Ability to get knowledge on how to utilize his/her resources in a wise manner that increases their income.
- Get interest and dividend on their savings and share.
- In general, they will able to escape from the line of poverty and build self-confidence.

To summarize the Advantages the members will get after they join the SACCO are: -

Table 2: summary of Advantages the members will get after they join the SACCO

Advantages	Member	Family	Community/Country
1. Wealth Accumulation from continuous and regular savings.	✓Can essay accumulate	✓Can Benefit from	✓Can Benefit from
2. Easy Accessible Loan using their savings as collateral.	✓Can easily get	✓Can Benefit from	✓Can Benefit from
3. Investment opportunity	✓Can easily get	✓Can Benefit from	✓Can Benefit from
4. Job opportunity	✓Can easily get	✓Can Benefit from	✓Can Benefit from
5. Good flow of income	✓Can easily get	✓Can Benefit from	✓Can Benefit from
6. Build Risk protection	✓Can easily protect	✓Can Benefit from	✓Can Benefit from
7. Build self confidence and self reliance	✓Can easily get	✓Can Benefit from	✓Can Benefit from

Section III

Saving and credit cooperatives promotion

The second part of this manual provides guidelines on how to start the promotion and establishment of saving and credit cooperatives in Rural and Urban areas in the philosophy of creating self-help and self-financing society.

It is true that the economic, cultural and legal environments may vary considerably in each country's situation, each requiring a specific approach and solutions. However, we should follow the general steps of saving and credit cooperatives development systems to have sustainable self-help and self-financing society.

When we start the promotion activity of saving and credit cooperative society, we have to explain clearly the objectives, functions, principles, norms and values of cooperatives, structure and set-up, Ownership and controlling system, main source of finance of the saving and credit cooperatives in detail.

Since our main objective and philosophy in promoting SACCO is based on creating self-help and self-financing society, we have to be careful not to give any unpractical promises to the founder members or potential members rather than giving them technical support that can help them to capacitate their financial management and members promotion system.

Most of the time the saving and credit cooperatives promoted in rural area by NGOs and government agents without adequate technical support, and mostly in wrong way with full of unpractical promises, which creates high dependency syndromes among the members.

These high dependency syndromes destroy the sense of ownership of members, and members start to complain on the promises rather than pulling and building their own finance and managing their SACCO by them selves.

When we decided to promote SACCO within a given community, we need to have good information and technical knowledge that helps us in the promotion process. At this stage many questions will come up from the target community, which should be answered. Usually this is the most critical phase in determining the success or failure of the initiative.

Steps for Saving and Credit Cooperatives development

The formation of a member-controlled saving and credit cooperatives is a complicated and often time-consuming process in which many actors (stakeholders) are involved.

The best way to proceed is to undertake systematic and step-by-step preparation before starting the real business. These steps (see Table 3) form a kind of critical path that should be followed prior to the ultimate decision of the members to start the saving and credit cooperatives. In many respects, saving and credit cooperatives resemble other businesses. They Similarly established to fulfill the need of clients demand, need Similar physical facilities such as office, perform well, and must follow sound business practices. In this respect the preparations are the same as for every other type of enterprise active in the market.

As an organization, however, a saving and credit cooperative is distinctly different and more complex to start. The main differences compared to other businesses enterprise are found in the saving and credit cooperatives is the **purpose** (to benefit the members), the **ownership** (member-owned), the **control** (member-controlled), the **decision** (member-resolution), and the **distribution of benefits** (to users-members). This means that the prospective members jointly

have to develop and agree on the idea and plans for setting up a saving and credit cooperatives business with full understanding of the institution.

Starting a cooperative therefore is an interactive learning process of the initiators and other stakeholders including potential members, initial leaders, community members and promoters.

The complexity involves developing agreement on the feasibility, the vision and the mission, of the proposed saving and credit cooperative. In addition, a high level of trust and confidence in the initial leadership and promoters or advisers has to be developed. Without an adequate level of trust among the potential members in the emerging cooperative organization, it is difficult to secure the needed member commitment required to finance and support the saving and credit cooperative once it is operational. Use of promoters, advisers and/or consultants during the process is recommended to compensate for the lack of experience and to provide support in studies as facilitator and in explaining commercial, organizational, financial and legal issues not to replace them. In this way potential pitfalls can be avoided and members can start to develop their management capacity step by step from the very beginning.

The promoters, or advisers should to be carefully selected on the basis of their professional knowledge, experience and trust or should trained by experienced advisor with practice to make them skillful in supporting the SACCO technically.

The promoters could play a major role in advising and explaining to the potential members about the saving and credit cooperative **objective, function, principles, norms and values, basic philosophy, historical background, economic advantages and benefits, membership criteria, members right and responsibility, leadership, ownership and control**, the technical, institutional or financial matters, clearly to help members during the decision-making process.

The initial phase requires a step-by-step awareness and sensitization approach before the group arrives at its ultimate decision to start the saving and credit cooperative. A critical number of member-owners must agree to move ahead with full understanding on the general nature of it, before the saving and credit cooperative can start.

The entire process can be time consuming. It usually includes site selection, feasibility study, organization of many formal and informal meetings as well as considerable effort in coordinating the large group of individuals and organizations. Community, Local leaders, advisers, and development professionals, as well as organizational support from others can facilitate the process.

There is no hard and fast rule for forming a saving and credit cooperative. With that in mind, the steps common to the formation of new cooperatives are presented in the following. The table on the following page summarizes the sequence of events leading to the formation of a saving and credit cooperative and the activities to be taken and by whom in general.

The sequence of activities should be considered as an iterative process. Activities associated with each step must be completed before proceeding to the next phase. However, often it is advisable to go back to the previous step in light of new information. Revision of earlier preliminary decisions might be needed and the process should be partly repeated on the basis of the new facts. The group needs beforehand to agree on each step before moving to the following one a green light or a red light meaning it is time to abandon the process and explore other options.

The ultimate goal of starting a saving and credit cooperative can only be reached once preliminary objectives have been accomplished. The group must:

1. Develop the idea for a joint economic initiative after agreeing that there is a common problem to be solved or a promising opportunity;
2. Build consensus for the saving and credit cooperative by interesting potential members;
3. Identify potential leaders, select a steering committee and prepare plans;
4. Implement surveys and studies to investigate the feasibility of the saving and credit cooperative;
5. Work out an institutional structure and reach an adequate level of trust among potential members;
6. Secure commitment from members;
7. Secure commitment from other key stakeholders;
8. Assemble the staff and assets to start up the saving and credit cooperative.

Table 3: Eight steps for development of a cooperative

No.	Step	Activity	By whom
1	The feasibility study	<ul style="list-style-type: none"> - Discuss with local development experts, and the community about financial services in the area in participatory way to Explore market and economic need of SACCO. - Study economic and social aspects of problem 	<ul style="list-style-type: none"> - Promoter - Advisers or - Consultants
2	The initiative	<ul style="list-style-type: none"> - Work out proposed initiative - Define critical questions - Discuss/agree on scope and nature of business 	<ul style="list-style-type: none"> - Core group - Potential members - Community members - Promoter - Advisers or - Consultants
3	Building consensus	<ul style="list-style-type: none"> - Agree problem can be addressed by cooperative - Study organizational alternatives - Hold initial meetings to review detailed proposal - Discuss and agree on cooperative approach - Create initial budget 	<ul style="list-style-type: none"> - Core group - Potential members - Community members - Promoter - Advisers or - Consultants
4	Establishing a steering committee	<ul style="list-style-type: none"> - Identify leadership - Establish steering committee - Install working groups - Agree on time table and tasks - Assign tasks 	<ul style="list-style-type: none"> - Core group - Potential members - Community members - Promoter - Advisers or - Consultants
5	Developing proposed by law, policies, and studies on minimum saving by member	<ul style="list-style-type: none"> - Members survey - Agree on proposal, feasibility and inform stake holders 	<ul style="list-style-type: none"> - Core group - Potential members - Community members - Promoter - Advisers or - Consultants

No.	Step	Activity	By whom
	Institutional design	<ul style="list-style-type: none"> - Prepare institutional design - Prepare draft statutes and rules (by-laws) - Raise initial capital 	<ul style="list-style-type: none"> - Core group - Potential members - Community members - Promoter - Advisers or - Consultants
6	Securing member commitment	<ul style="list-style-type: none"> - Develop detailed business plan - Establish legal identity - Create interim board of directors - Set up books/accounting system - Conduct member-equity drive and signup - Formation meeting - 	<ul style="list-style-type: none"> - Board of directors - Members - Promoter - Advisers or - Consultants - Accountant - Managers/ Staff
7	Involving other Stakeholders	<ul style="list-style-type: none"> - Secure necessary financing - Retain manager - Formalize relations with customers/suppliers - Launch cooperative 	<ul style="list-style-type: none"> - Board of directors - Members - Promoter - Advisers or - Consultants - Accountant - Managers/ Staff
8	Starting up the enterprise	<ul style="list-style-type: none"> - Hold general meeting - Elect directors - Establish committees - Secure necessary assets - Hire staff 	<ul style="list-style-type: none"> - Board of directors - Members - Accountant - Managers/ Staff

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