Pakistan Journal of Social Sciences 5 (8): 734-738, 2008
ISSN: 1683-8831
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Resuscitating Cocoa Production Through the Informal Financial Sector in Ekiti State

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Abstract: Ekiti state has an agriculture based economy with the production of food and cash crops providing employment and income for more than 75% of the population. The men and women are predominantly farmers well known for the production of cash crops especially cocoa that has helped to alleviate poverty in some quarters but which output had nose dived due to various factors of which finance is paramount. The reason not far fetched, where available, the formal financial institutions have not cared to genuinely accommodate the financial needs of the farmers. Therefore, using primary data from the interviews conducted among 50 cocoa farmers, this study assesses the role of the informal financial sector in financing agricultural development to increase cocoa production in Ekiti state. The study revealed that the inability to improve on output of cocoa is a reflection of the lack of access to enough credit to finance the planting and maintenance of cocoa plantations. It further reveals that about 99% of the respondents that have access to finance apart from personal savings were able to obtain this through the informal financial sector. The study-concludes that giving the patronage of the informal financial institutions by the farmers, there is a better chance of improving cocoa production in Ekiti state. Therefore, establishing a linkage between the informal and the formal financial Sector will invariably improve credit facilities to the farmers, lift their status and increase the internally generated revenue from commodity taxes in the state.

Key words: Cocoa production, informal, financial sector, economy, Ekiti state

INTRODUCTION

Ekiti state has an agriculture-based economy, with the production of food and cash crops providing employment and income for more than 75% of the population. Ekiti men are predominantly farmers, while women engage in trading. Even for the many educated indigenes in formal sector employment, farming remains a major secondary occupation.

In the past, the areas of Ekiti state were well known for production of cash crops, especially cocoa which accounted for about 40% of total Nigeria export. Historically, cocoa was very important in Ekiti state. Besides, the fact that cocoa has been the major source of income for substantial number of peasant farmers in the state, it has also provided the main stream of revenue for the government through direct taxes, grading fees, produce sales tax and export duties at large (Adegeye, 1996). Buyers provided the seed. People paid off this by growing the crops. This is no longer the situation. Recently, the buyers are not so local, they are larger external companies. The farmers do not feel so loyal to them and in fact, if the price goes up, will sell their crops to others. Also, the growth of Malaysian cocoa has affected the price of cocoa in this part of Nigeria.

The Structural Adjustment Programme (SAP) beginning in ousted 1986 liberalized the marketing boards, which hitherto controlled the price of cocoa. The fluctuation of prices in the international cocoa market has kept people from staying in the cocoa trade. The result is that most cocoa farms have been abandoned in preference for white-collar, particularly civil service, jobs. The State civil service employs 60 per cent of the people in the labour market in the State. More than 90 per cent of the remaining 40 per cent, still long to join the civil service (CEDAR 2000). Those left in the sector are easily discouraged by a variety of factors, including low international market prices.

As may be expected, the people of Ekiti are essentially agriculturalists. The carving out of Ekiti State from the former Ondo State also excused it from the club of oil-producing States. Revenue allocation from the Federal Government to the State leaves little room for rural development. The wage bill of the State 'swallows up' its budget resources with little left for other programmes. The State, therefore, has had to fall back on its traditional agricultural base in which cocoa is the major cash crop for public revenue.

Cocoa production in Ekiti is constrained by the inability of the farmers to access institutional finance and

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where available is not sufficient, as well as poor communication, poor infrastructures including roads, poor housing and poor health facilities, unreliable water supply and storage facilities.

In addition, the poor state of infrastructures has adversely affected them, as access to individual farms is difficult. They also encounter problems of marketing, as there are no big markets within the state, while access to more distant markets is difficult due to lack of good roads. Besides, most farming activities are performed with crude implements in traditional farming systems and most household in the state rely on farming as their primary source of income thereby exposing them to income risk because of its fluctuating nature compared to people in other occupations (Oluwatayo, 2004). They lack improved seedlings and most importantly institutional credit facilities.

To confront the problem of finance with a view to helping themselves in the context of a prominent shortage of effective formal finance response, this led to the farmers devising various means of dealing with the situation at hand. They organized themselves into groups, ranging from cooperatives through social clubs, religious organizations to village and town development organizations, participation in local savings schemes (e.g. ajo, esusu, adashi etc.), visiting moneylenders and succors from families and friends. There are also associations of ethnic nationalities resident in many of the cocoa producing areas of Ekiti who are non-indigenous farm contractors and labourers from Osun, Oyo, Kwara, Kogi and Benue States of Nigeria.

Aims and objectives: Considering that there is still dissatisfaction with credit supply to the farmers from institutional source and having device means of solving the problem themselves, therefore, this stduy which to exploit the potentialities of the informal finance and what can be done to make it suitable to improve cocoa production in Ekiti state.

The rest of the study is divided as follows: Section two highlights the concepts of informal financial sector. It also shows how informal borrowing has evolved over time and some reasons for borrowing from informal sources. The sources of data and method of analyses are described in Section Three. In Section Four, analysis of the finding is undertaken with the aim of explaining the viability of informal sector to provide the necessary financial support for cocoa producers in Ekiti. Section Five concludes the paper and provides some policy recommendations.

Literature review: Access to external finance is important to all sectors of an economy. For instance, investment in fixed capital often requires a large lump sum of funds. The adoption and installation of new and better technology might demand external finance. Some farmers need access to working capital financing to smooth out fluctuations in income due to differences in the timing of production and sales. In many Sub-Saharan African (SSA) economies, however, financial and legal systems do not operate efficiently and therefore, credit may not be forthcoming.

In such a situation, it is unavoidable to seek alternative sources of finance. The alternative source of external finance considered in this study is the informal financial sector. Historically, SSA financial systems have been highly fragmented into dual markets, namely, a formal and an informal financial market (Seibel and Marx, 1987; Nissanke, 1992). Traditionally, the formal financial sector has been seen to serve the government, while the informal one serves the private sector.

There are two main views explaining the existence of informal finance. One is that informal finance is a reaction to policy distortions, or financial repression (Fry, 1995; Taylor, 1983). Since, the informal financial sector is not subject to regulation, it is more efficient than the formal one. The remedy for the relative inefficiency of the formal credit market may be seen in financial liberalization.

The second view maintains that the informal sector has a comparative advantage in some market segments, not with standing financial liberalization (Adams, 1992; Wai, 1992). While, it is costly for formal institutions to acquire information, informal agents can utilize local personal information, resulting in monopoly power. It is well known that a weak legal system inhibits contract enforcement, which results in credit rationing of potential borrowers without collateral. Informal agents can fill such market segments and collateral can be replaced by reputation, group responsibility and interlinked transactions (Steel *et al*., 1997).

Formal lenders were perceived as being overly risk-adverse and often belonged to government regulated loan programs. Loans were considered as an input to agriculture. The farmers were labeled as being conservative. Another assumption was that poor rural borrowers did not have any incentive to save and that the only way the farmers would adopt new technologies or invest in land improvements was if they had access to cheap loans. Usually large farmers and traders have better access to credit than the smallholders, who make up the majority of farmers in developing countries.

Poulton *et al.* (1998) studied smallholder cash-crop production in liberalized cotton and cashew markets in Ghana, Pakistan and Tanzania. They investigated the difficulties farmers face in financing seasonal crop inputs and the mechanisms developed by private traders to supply seasonal credit. It emerged from the study that farmers' limited access to capital is a critical constraint on crop production. Also, the willingness and ability of the private sector to supply farmers with loans was limited by the high risk of default on loan repayments and the high cost of information on potential borrowers. Such costs were too high to be recovered by the low returns on the normally small loans taken out by farmers.

Conceptual definition of informal finance: The institution of informal finance is ancient, dating back at least to the 16th century, when Yoruba slaves carried it to the Caribbean, as part of their institutional luggage-or social capital. Both the term 'esusu' and the practice have persisted to this day, as esu in the Bahamas, susu in Tobago or sou in Trinidad. Among the Yoruba in Nigeria today, there is hardly a single adult who is not a member in one or even several esusu, numbering anything between two and several dozen or even hundreds of members. The institution exists all over West Africa as well as in many other parts of the world, where it is an integral part of the local microeconomy and referred to with its own vernacular term (arisan in Indonesia, Paluwagan in the Philippines, gameya in Egypt, ekub in Ethiopia and cuchubal in Seibel and Damachi (1982)).

The activities of this sub-sector are mostly underground, unofficial, irregular, informal, shadowy and parallel. The most predominant type of informal finance in Nigeria is the Esusu. Among the Yoruba, it is called either Esusu or Ajo. Among the lgbo, it is called lsusu or Utu while the Edo call it Osusu. The Hausa call it Adashi', the Nupe Dashi, the Ibibio Etibe, while the Kalahari call it Oku. Some Esusu groups operate with written laws, while others operate with unwritten laws but on oath of allegiance and mutual trust. The general practice is that esusu associations contribute a fixed amount periodically and give all or part of the accumulated funds to one or more member (s) in rotation until all members have benefited from the pool.

There are also informal moneylenders, saving and credit associations and credit unions. Moneylenders are believed to be highly exploitative with high rates of interest through which they extract economic surplus provided by peasant labour, capital and land. The saving and credit associations as well as credit unions operate in more formalised ways than the esusu associations. They may or may not be registered under any legislation. However, savings and credit cooperatives must be registered under the co-operative association act. Credit societies often come together to form larger units called credit unions, when they modify their operations to include subscription of share capital, deposit-taking and lending. Credit unions are the precursors of the People's Bank.

The principal reason for the emergence of an informal financial market is the unwillingness of the formal financial sector to lend to some (relatively risky) categories of borrowers. Increased risk often stems from the difficulty to obtain accurate and reliable information about borrowers. Examples that hinder the flow of accurate information are geographical remoteness or illiteracy. Small clients are also effectively shut out from the formal market due to high collateral requirements and high minimum deposit requirements.

Another explanation for using informal sources may be that more funds can be raised at a lower cost and without collateral when the source is a relative or friend. Interest rates in the informal financial sector tend to be higher than in the formal financial sector, although among informal lenders, interest rates are seldom used as a discrimination device to screen borrowers. Aleem (1990) argues that lenders sometimes borrow from the informal market themselves and lend on at an even higher interest rate. The large cost of monitoring and administering informal contracts increases the cost of borrowing. Higher risks and costs of delinquency are other explanations for the relatively high interest rates, although the loan portfolios of the informal lenders compared with formal lenders had low delinquency and default rates (Steel *et al*., 1997).

Unlike commercial banks, informal lenders use personal, social and business relationships to pre-select clients. Rotating Savings and Credit Associations (ROSCAs) use group membership as a selection device, traders and landlords only lend to their customers and tenants, while savings collectors tend to lend to regular customers. Moreover, recommendations from previous clients and personal knowledge are important ingredients in the selection process.

Informal finance is sometimes taken as synonymous with moneylender activity, but Steel *et al.* (1997) show (for the cases of Ghana, Malawi, Nigeria and Tanzania) that families and friends are the most common informal creditors. Normally, such loans bear no interest and social and economic ties replace collateral as well as ease enforcement of the loan contracts. The relationship between the borrower and the families and friends reduces the involved moral hazard and hence the monitoring costs. Reciprocity is not uncommon, meaning that the borrower can sometimes become the lender and vice versa.

Moneylenders lend without tying the loans to other transactions. A moneylender, who for instance, could be a regular moneylender, a pawnbroker, or an indigenous banker, often, has intimate knowledge of the borrowers. Despite the high interest rates, small and medium-sized firms turn to moneylenders as a lender of last resort. Because of this, the moneylenders are sometimes in a monopolistic position.

In ROSCAs, individuals pool their savings on a regular basis to generate loanable funds, primarily for the members. The rotation of access to the funds differs among ROSCAs, but most seem to use lotteries and bidding. Without going into a detailed description of the bidding system, the outcome is lending at a market-determined interest rate. Organizational and monitoring costs of ROSCAs are very low; default rates by the very nature of ROSCAs are low as well. Members could be moneylenders as well as traders or manufacturers.

MATERIALS AND METHODS

The study is descriptive in nature. Data were collected through the conduct of unstructured interviews carried out among 50 cocoa farmers who are real owners not owners by inheritance in selected farm settlements in Ekiti state comprising of Ijumu and Ahere farms in Omu Ekiti, Kajola and Soso farms in Ikoro Ekiti, Ajeje and Ologboodu I and II in Ijero, Igi mokogo and Ago Aduloju in Ado Ekiti. This enables an in-depth study of the sources of financing cocoa production in the state. The interviews were conducted by asking open questions which encouraged the farmers to discuss their feelings freely.

RESULTS AND DISCUSSION

Participating farmers in cocoa production interviewed during the field work were 60% literates within the age bracket of 40 years old and above that planted this farms themselves. Response obtained revealed that the cocoa farmers do not usually make use of the traditional moneylenders to finance the planting of their cocoa farms. However, this was done through the combination of personal savings and efforts of relatives who trained them when they were growing up who usually assist mostly by providing land, seedlings and group of friends that comes together to work on the farms on rotational basis usually refer to as Oya in the local languages.

Analyzing the interviewed, it is further revealed that the farmers do not require much money during the growing period of the trees except for the weeding and do not participate in daily contribution because of the stock in trade. However, all that were interviewed participate in self help group and rotational credit association which comprised of about 10-300 members and a farmer may belong to as many as 2 or 3 different groups so far he has the capacity to fulfill the necessary obligations to the groups. Apart from satisfying financial needs it enables them to have access to chemicals and pesticides at reduced price which may be given in other cases till harvest or deducted from their savings with the group.

However, further revelations were made concerning the way most of their activities are financed. It is of general opinion among the farmers interviewed that due to seasonal nature of the crop there has been no support from the formal financial institutions except in terms of trade for only the produce marketers. In view of this, they participate mostly in farmers multipurpose cooperative societies which may be registered or not. They act as savings institutions and disburse credit based on personal recognition and on presentation of two sureties who must be members of the society in case of default. In the course of the study two crucial facts emerged, why the farmers should be left in the informal sector to source fund.

Firstly, the interest payment is far below the official rate i.e. is as low as 1% month or between 10-15% per annum for N1000 which makes it cheaper than the formal sources available.

Secondly, the rigor and the administrative process of obtaining loans from these groups formed are less cumbersome with two sureties and the beneficiary social relationship with the group is used as collateral security of the loans.

However, some of the cocoa farmers interviewed do not pray to have any course to go to money lenders who charges as much as 50% unless is to be used for other purposes rather than farming.

Other succor is gotten in kind through prospective buyers who give chemicals in return for cocoa beans at harvest, while some farmers receive cash without interest charges after a long year of relationship has been established between the farmers and the buyers. Farmers in this category do guarantee others for such assistance. All these are perfected at the ruling market price as at the time the transaction is made.

Although, this research is structured strictly on propelling cocoa production through the informal financial sector in Ekiti state. In concluding the interview, a probe was instituted on the efforts of government to increase cocoa production and agricultural sector in general. While the effort of government is lauded the implementation process of the programme is an abuse, according to the enlightened farmers beneficiaries are usually arranged by the officers in charge and politicians who divert the loans to other sources or outright embezzlement.

CONCLUSION AND RECOMMENDATIONS

Cocoa being a perennial crop is subject to adverse weather changes and pests attack which may eventual reduce productive ability of the trees. This makes it too risky for the type of formal financial institutions in Nigeria which had remained adamant to changing from their traditional practices to modern practice to finance. Formal finance is only extended to the produce buyers and marketers but not producers.

The various self-help groups formed by these farmers to help themselves had proved to be very successful in meeting their needs in cash and kind with very low default rate. The savings/contribution commitment of the members and charges/condition involved in treating and processing loan applications are more encouraging.

Participating in formal financial sector when it is not a special arrangement is not welcome by the farmers because of the interest rate and the other loan application requirements which is not reachable by an average cocoa farmer in Ekiti state.

Looking at the place of revenue from agriculture being used to supplement the federal allocations the following recommendations are proposed to improve both financial and material assistant to the farmers.

We are of the opinion that operations of the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB) should be reevaluated for farmers use and if possible relocate the branches from Local Government Areas headquarters to the interior where rural farmers that really needed it can make use of it.

There must equally be loan assessing and monitoring officers whose job should be 75% out door to make sure the beneficiaries are those that is meant for and are using it for the right purpose and organize campaigns to create awareness and usefulness of the NACRDB to farmers if utilized.

Finally, integration of the informal financial sector into the mainstream financial system as in some Asian countries will further alleviate the financial problems of the cocoa farmers and further increase their productive capability which is adversely affected by insufficiency of finance.

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