Course: From conception to management

Does Youth Microfinance have the potential of reducing rural youth migration? Limits & Opportunities

Abstract: *Young rural population is declining more and more over the years to migrate to big cities, mostly to find better work opportunities. Microfinance being a booming sector, does it have a role to play regarding this matter? In this paper we will see that youth suffer from lack of formal financial services, even if actually they do have some income, they save and borrow, generally using informal ways. We'll also learn that rural areas have been deserted by formal financial institutions. Knowing the financial needs of rural youth to access land and invest in it, we will see the limitations, such as the difficulty to reach rural settings for MFIs, the bad image of youth and some legal barriers; as well as some opportunities for MFIs to reduce rural youth migration providing financial services to access land and invest in productive activities.*

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European Microfinance Program

Academic year – 2016/2017

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Introduction:

"There is a largely untapped reservoir of employment opportunities in agriculture. Yet, the drudgery and poor remuneration associated with low-productivity family farming turn young people away from agriculture and make them more prone to migrate from rural areas". (FAO, 2016) This is the central issue discussed in this paper. We know that, despite the poor productivity of farming activities, it represents a potential work market for a lot of rural young people, which might prevent them to migrate to cities, where they won't have necessarily a better chance of employment and/or good work conditions.

"Financial services such as savings, loans and insurance are essential tools young people need to start an enterprise and increase farm productivity". (IFAD, 2015, p. 1) Are financial services a good way to prevent rural youth migration?

A. Rural youth migration:

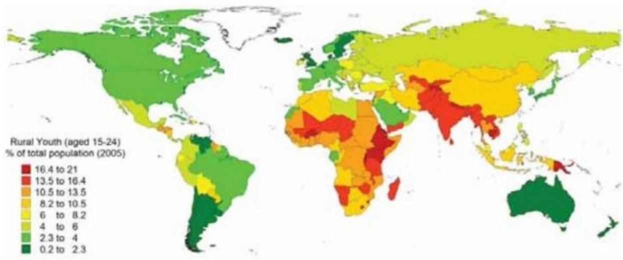
1. Youth

The UN defines youth has *"those persons between the ages of 15 and 24 years"*, for statistical purpose at least. This is a complex group to define, and each country has its own definition of youth. It can go between 14 and 35 years old. Since we are looking into the rural context in many different countries, we won't make a difference within every author or organization's definition. What we can say is that a "young person" is considered between childhood and adulthood, going through some specific phases of its life, which are similar in a lot of countries (transitions such as finding a home to live, starting a job, getting married, having children, etc.). (United Nations, 2007).

It is important to emphasise the fact that there are big differences between a young person of 15 years old attending secondary school and another young person of 29 years old, parent of 2 children and working. We should take into account the diversity of such a group. Rural and urban youth are different as well as Benell put it: *"Rural children in developing countries become adults quickly mainly because the transition from school to work usually occurs at an early age and is completed in a short space of time"*. (BENELL, 2007, p. 2)

It is well known that young people are usually a more vulnerable group. According to the FAO, 88% of the youth live in developing countries. Of those living in Africa, 70% are living on 2$/day or less. (FAO, 2016)

Concerning rural youth, we can observe on this map that some countries in Latin America have fewer than 2% of youth living in rural settings, and more than 16% in some countries in Asia or Africa. (Deotti & Estruch, FAO 2016)



Map 1 - Rural youth aged 15-24 as % of the total population of 186 countries (2005). Source: FAOSTAT and UNPD World Population Prospects, 2008 Revision.

We can see below that the tendency is a decrease in the proportion of the youth population in all subregions of the world, but in absolute numbers, it will increase in some region (Africa) and decrease in others (South East Asia). *“The decreasing numeric importance of rural youth is due to (1) urbanization and (2) a demographic transition towards lower fertility rates and lower mortality rates”.* (Van der Geest, 2010, p.9).

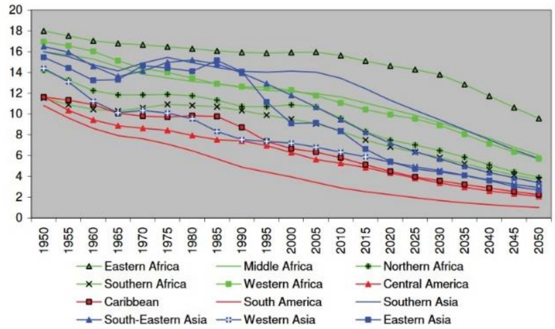


Table 1 - Rural youth (aged 15-24) as% of the total population by subregions (1950-2050). Source: FAOSTAT and UNPD World Population Prospects 2008 Revision.

2. Migration

Indeed urbanization is a key issue in this problematic. According to the UNICEF, young migrants (according to UN’s definition) represented 23.2 million in 1990 and were 28.2 million in 2013. (UNICEF, 2014) It is around 1/8th of the migrant workers. Although this figure is probably underestimated, especially if you extend youth’s definition to 30-35 years old, which wouldn’t be exaggerated. (Deotti & Estruch, FAO 2016) The World Bank stated that around one third of total migrants from developing countries are aged 12 to 24, and that young people were 40% more likely to move from rural areas to urban settings or across urban areas, than older people. (World Bank, 2006)

3. Challenges young people face in rural areas

As we see above, rural youth population has been decreasing in every region in the world, quite dramatically. What are the main difficulties young people face in rural areas?
We underlined some central arguments on rural youth migration:

<u>Economic opportunities</u>

Young people usually have lower wages, precarious contracts and are more represented in the informal sector, than adults. (MIJARC/IFAD/FAO, 2012) It is even more true for rural youth, especially the problem of unemployment (or more correctly underemployment), which obviously impact their economic and social life (World Bank, 2009). IFAD conducted a study about rural youth in Latin America, Asia and Africa and concluded that *"pluriactivity is used as an important risk-management strategy by young farmers and rural youth"*, meaning a majority has economic activities outside agriculture (MIJARC/IFAD/FAO, 2012, p. 2).

It seems that in rural settings of developing countries, young people consider migration (even a seasonal one) as a way to deal with low economic opportunities. *"Young people usually move out of rural areas towards urban areas, looking for employment in sectors other than agriculture".* (Ginsburg et al., 2014; Awumbila et al., 2015, in Deotti and Estruch, 2016, p. 4) Most migrants are indeed young people looking for better employment conditions. (FAO, 2016)

<u>Education</u>

Education is still a challenge for rural youth. In some developing countries, students need to move to the city in order to continue their studies, because they don't find higher level of education in the area (such as higher education or even secondary education) or they choose to migrate because the quality is rather poor. (Van der Geest, 2010)

<u>Agriculture</u>

Even if not all rural young people are in the farming business, still a high proportion is doing so. And it is widely known that agriculture does not have the highest return: *"Due to unfavourable agro-ecological conditions, low levels of technology, poor market access and lack of investment capital, the returns to farm labour are often low in developing countries".* (Van der Geest, 2010, p.28) Also, for young people working in farming activities, the agricultural cycle typically suggests there is high demand for labour at some period of the year and low demand at others, which also is a factor of seasonal migration. (Van der Geest, 2010)

Undeniably, rural youth faces various challenges that may lead them to urban settings. The most striking factors are low economic opportunities and underemployment, poor education institutions (if any), bad reputation of the farmer's profession, among others. Other factors are to be considered for youth migration, such as the poor infrastructure and provision of services, little mechanization and social facilities, as well as the bad reputation or valorisation of the job of farming has among society (Dirven, 2010 & World Bank, 2009).

The FAO suggested an interesting framework for the determinants of distress migration[1], *"which vary according to the local context and stage of structural transformation, as well as the household typology and individual characteristics of the migrant"*. (Deotti and Estruch, 2016, p. 9) The context includes the level of rural development in the area, the food security, the level of environmental degradation, poor job opportunities, the lack of social protection or access to markets and resources; the household typology consists of its characteristics (gender, age, education, size), its network and asset base; and the individual elements stand for their age, gender, status, personal ambitions, education level, etc. (Deotti and Estruch, 2016)

We don't want to stress youth migration as a negative process, but it is the only choice some have. It should be taken into account that rural youth sometimes lack education or skills, social capital and even cultural capital to adapt well to the urban market. In this case, they would be more vulnerable than urban youth on the same market. (Deotti and Estruch, 2016)

B. Youth and finance

1. Youth access to finance

Worldwide, around 60% of youth in developing countries do not have access to formal finance. Only 18% of them have saved in the past year and 6% have borrowed from a formal financial institution. This situation decreases their ability to start a business or remaining at school. (Demirguc-Kunt, Klapper, Kumar and Randall, 2013).

[1] FAO studied the roots of rural youth migration and especially the "distress migration", which is migration in *"(...) conditions where the individual and/or the household perceive that the only viable livelihood option for moving out of poverty is to migrate"* (Deotti & Estruch, FAO 2016, p. 1)

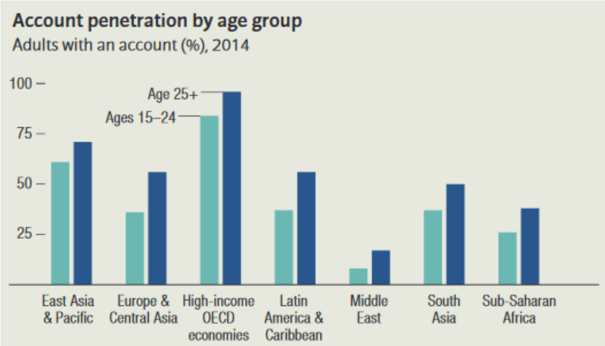


Table 2 - Global Findex database

We can observe a difference between youth and older people regarding the account penetration rate. In some countries, this gap exceeds 60% (Haiti, Senegal and Benin), which is huge. This gap becomes even greater in developing countries for the poorest of them. (Demirguc-Kunt, Klapper, Kumar and Randall, 2013)

2. Youth Financial Needs

The SEEP network conducted a global trend study to have more material on youth financial needs in developing countries. We should take this study with a pinch of salt since it mostly gives tendencies in a wide variety of contexts.

Income flow: Globally, young people have some similar characteristics about the income flow: they received small amount of money from their relatives, their income fluctuates strongly and comes from a variety of sources, formal and informal. *"In rural areas, income flows may be higher after either the harvest or the rainy season, when crops are sold"*. (SEEP, 2013, p. 11) Indeed, it is synchronized with their parents' income.

Savings: Young people do save. They may reduce their expenses to keep some money they were given, or work part-time or after school to increase their capital. They save small amounts, in unsafe places and irregularly. In rural areas, some buy crops when the prices are low, to sell at higher prices later on (speculation). They want to have access and control over their money. (SEEP, 2013, pp. 18-21)

Credit: A lot of young people borrow money for their economic activities (start a business, agriculture…), housing or education. They generally borrow from family and friends instead of financial institutions because it gives them much more flexibility in case of delay of payment and consideration in case of default (no penalties). (SEEP, 2013, pp. 22-23)

Informal versus formal: Young people think they lack understanding and access to financial services, but would be willing to take loans to finance their activities. Unfortunately, they still face quite a lot of barriers (that aren't always specific to youth), like high interest rates, lack of collateral and repayment schedule incompatible with the irregularity of their income. Indeed, informal finance might fill this gap more easily. Accordingly, youth often perceive formal finance (MFIs & banks) as inaccessible to them. Financial institutions are regularly seen as providers mostly for adults, workers and large deposits. (SEEP, 2013, pp. 25-32)

Rural versus urban: It struck out that various elements should be taken into account when understanding youth financial needs, such as the life stage, the gender, the enrolment (in school or not), rural or urban, etc. Indeed, the reality changes quite a lot depending on those elements (and depending on the country, obviously). For instance, younger people will be more dependent on their parents for income; older are more keen to invest in income-generating activities and spend more on basic needs and rent than younger people who spend on school supplies and transportation, etc. Regarding the geographical location, the income is higher for urban youth, but mostly diversified for rural youth between farming and self-employment. In terms of spending, urban youth might be more tempted to spend money on individual consumption items (probably due to more exposure), while rural spend more in income-generating activities (agriculture and livestock) and wedding in some regions. Urban youth usually have better knowledge and access of formal financial services because of the proximity of those services. So, it makes sense to suggest a better access to services for rural youth, such as mobile vans, mobile branches, etc. The costs of travelling long distances and the risks linked to it would therefore be avoided. (SEEP, 2013, pp. 49-51)

In conclusion, it seems that youth in developing countries are indeed quite active financially speaking, but mostly in the informal sector. The youth gap in financial services isn't easy to fill. The SEEP study showed that financial service providers should design products linked with the specificities of rural youth. Those main characteristics are: small amounts, high fluctuations, possibility of small savings, flexibility with credit loans, grace periods and focus on income generating activities since it's one of the youth's biggest challenge.

3. Rural finance

Now that it is acknowledged that youth lack access to finance and have specific needs, we will investigate rural finance.

Rural areas have been deserted from financial institutions for a long time. They indeed suffer from a lack of financial services.

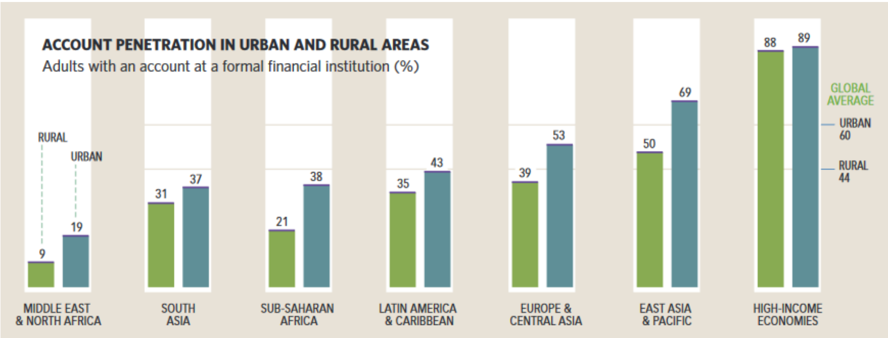


Table 3: The Global Findex Database 2011 (IBRD-BM, 2014)

The world average of rural people having an account in formal financial institutions is 44%, compared to 60% for urban areas. And this gap becomes greater than 16% depending on the region (17% in Sub-Saharan Africa and 19% in East-Asia and Pacific). (IBRD-BM, 2014)

Massimo Pera presumes it is because of the specificity of agricultural value chains (agriculture being the main sector in rural areas) that needs *"a more complex coordination among supply chain segments and service providers, necessary to manage effectively a wide range of risks"* (PERA, 2016, p. 7), and this is even more true for small and medium farmers. The author suggested 5 challenges to invest in agriculture:

1. Agriculture is quite dependent on the climate and the environment, such as drought, rainfalls, biodiversity and have specific biological risks (pests, diseases, etc.), inherent in this sector;
2. The value chain isn't well coordinated enough to be able to control it;
3. The difficulty of financing the long-term business cycle in agriculture and its seasonality;
4. Farmers don't often have the titles or rights regarding their land or water;
5. Private sector never really invested in agriculture because of the governmental involvement.

Also, agriculture is still seen as a sector with low return on investment, high risks, high transaction and operational costs. In clear, financial institutions are usually reluctant to deal with those barriers. And even if institutions might still invest in this sector, their products aren't well adapted to the farmers' reality (long-term, seasonality, lack of collateral or guaranty that institutions want to mitigate their risks, etc.). (PERA, 2016)

Other obstacles exist for rural areas in general: Transaction and operational costs in remote locations with low density of population and bad infrastructure make financial services quite costly for the providers; financial illiteracy being greater, this creates more problems for clients to understand well the financial products and/or to manage well the risks of their business, among others. (ILO, 2015)

It seems clear that microfinance still has work to do to expend its outreach in rural areas.

C. Limits of microfinance to reduce rural youth migration

We have established that young people have needs of financial services and have poor access to it, particularly in rural settings. What major constraints will microfinance encounters?

1. Rural Outreach

"There is a shortage of financial services in rural areas and existing products do not usually account for the needs and capacities of rural youth" (FAO et al., 2014 in FAO 2016, p. 12), such as land as a collateral or the skills to design a business plan or the financial knowledge needed. (FAO, 2016)

In general, microfinance is much more present and successful in urban areas and is still struggling to reach rural households. And even when it does, it isn't reaching the most common economic activity, agriculture. (PERA, 2016) As we have seen above, it is strongly linked to the specificities of agriculture: low return on investment, important fluctuations of income, long production cycles, dependence to climate variation, high operational costs due to the wide area, etc. Those specificities bring more risks for MFIs and they have difficulties to offer adapted products to it. (Morvant-Roux, 2011) This is not specific to rural youth, but those barriers exist for the rural areas in general, and impact youth's access to financial services particularly.

2. Image

Other limit: the perception of MFIs and its personnel regarding youth. Young people are sometimes perceived as more risky clients, with a lack of business and financial literacy or necessary collateral, and more costly for the MFIs (USAID, 2005).

3. Legal Barriers

Also, legal and/or political barriers may exist in some countries, such as a legal age to open a bank account or to have a financial contract with an institution (18 – 21 of age), which limits youth access to finance. (USAID, 2005)

For those 3 factors, the microfinance sector could do something (adapt its products to rural youth, lobby against legal barriers, raise awareness of MFI (and its personnel) regarding youth bad reputation, for example.

4. Political, Social and Economic Context

But as we know, many factors play a big part in the migration of rural youth to cities. It is not apparent how microfinance could reduce the youth depopulation of rural areas regarding the issue of lack of education institutions, lack of good infrastructure or personal aspirations. Regarding job creation, *"In Sub-Saharan Africa alone, more than 10 million new jobs per year will have to be created in rural areas in the next two decades to absorb the new entrants in the labour force".* (FAO, 2016, p. 1) Microfinance may give better opportunities to rural youth, but has clearly not the capacity itself to provide a job for everyone. Rural youth migration is a social phenomenon, which would need much more striking forces to have such an impact (government investments in rural development and economy, new public policies, value-chain approach, etc.).

D. Opportunities of microfinance to reduce youth rural exodus:

1. Access to land

In the survey done by IFAD in various regions, half on the young farmers struck access to land as one of the major challenges when they start farming. 50% of those that were not yet farmers have difficulty to enter the agricultural sector because of the same reason. They typically have access to land through inheritance, which may take a long time, especially with life expectancy getting greater and greater. Even if they inherit a piece of land, they may have siblings that are also entitled to it. Finally, plots are frequently fragmented and it is not easy to be productive on small surfaces. This lack of access to land is even more a bigger issue for women, partly due to the patriarchal system of inheritance. According to ActionAid report, fewer than 2% of the available land is owned by women. Financial service providers may play a part regarding this problem allowing a credit. (MIJARC/IFAD/FAO, 2012)

2. Access to finance

Still in IFAD's survey, their results showed that *"(...) rural youth severely lack access to rural finance. More than 70% of young farmers respondents to the survey stated access to finance as the biggest challenge they face when they start farming"*. Access to land is obviously necessary to start agricultural activities, but very frequently, investment in farming activities is necessary to be productive. Unfortunately, financial institutions might see a young farmer as a riskier client. Therefore, young people often turn to informal finance (family, friends, money lenders). (MIJARC/IFAD/FAO, 2012, p. 15.) This represents an unfulfilled demand and a potential market for microfinance.

3. Financial opportunity for microfinance sector

Financial performance: Recent studies on youth financial services showed that, even if the youth have less income (and savings) and do fewer transactions, it is possible to reach a break-even point within 3 to 5 years. (IFAD, 2015) And since rural areas are much less provided for in terms of financial services, it represents a market with potential growth and higher returns than in urban areas. It may help to balance the higher transaction costs or supposedly the risks of rural economic activities. (IFAD, 2015) Rural youth does not mean agricultural activities. Indeed, a lot of them are involved in non-farm activities (it is increasing). And if they are working in agriculture, they usually have a bigger income out of it than older households. (Van der Geest, 2010)

A market for the microfinance evidently exists with rural youth and it has some interesting growth potential. Focusing on youth is also a way to ensure future clients, creating a relationship with a MFI. If microfinance is able to provide financial services that would give the opportunity for rural youth to access to land and invest in it, it would definitely be one of the ways to play a role to limit youth migration.

Conclusion

Youth underemployment and youth migration from rural areas are a reality. Microfinance oriented towards them has a good potential. Of course, microfinance won't replace the role of the State and won't be able alone to strike the focus on developing the rural areas economically and socially. We have to be realistic; microfinance can't play a direct role in a lot of factors responsible for youth migration such as rural development, environmental

degradation, lack of social protection, infrastructure, education level, social network or personal goals.
What microfinance can do is offer financial services that would meet two neglected markets: youth and rurality. *"Offering appropriate financial products to young people in rural areas to help them meet their growing needs and give them more productive options to stay in rural areas is thus crucial for the development and economic growth of rural communities"*, (HAMP et al., IFAD, 2015, p. 2) Though we didn't focus on that in this paper (although the scope of this paper didn't permit a longer study), a lot could be said about non-financial services as well, to support youth in their lack of financial literacy or business skills, or mobile banking and its promises to reach rural areas.

To conclude, if the microfinance sector is really trying to be efficient socially speaking and therefore provide access to vulnerable people such as rural youth, it can (and should) develop some products that would support young people to access land, inputs to agricultural or non-farm activities and play one's part towards rural youth migration.

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