

Rural Informal Financial Markets System in Developing Economy: Challenges and Prospects in Kaltungo Local Government Area of Gombe State-Nigeria

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Abstract: *In searching for alternatives to formal sector finance, much attention is increasingly being paid to informal and semi-formal finance (including micro-finance) for meeting private sector credit demand, particularly from small enterprises. But the difficulties of making informal finance play a modified role quite different from the one it was used to, in terms of loan characteristics and uses, became apparent with the failures of these institutions. This study seeks to examine the challenges and prospects of the rural informal financial market in Kaltungo Local Government Area of Gombe State-Nigeria. The population of this study was 150 consisting of traders, farmers, businessmen/women and civil-servants patronizing the informal financial market in the study Area. The study utilized primary and secondary data and data was analyzed using simple percentage. The study revealed that the only (First Bank Nigeria PLC) existing in the local government area is inadequate to service the rural people and that 51.3% of the people depend on money lenders (informal financial market) for their source of business financing (loan). The study therefore, recommends among others that the rural banking programs in Nigeria should be reviewed with a view to establishing an avenue for effective rural banking that will help daily Adashe collection and the money generates from the rural savings through Adashe be deposited in the formal financial institution, with a corresponding rate of interest as in deposit money banks.*

Keywords; Informal finance, loan characteristics, private sector credit demand

1. INTRODUCTION

It is a known fact that the difficulties encountered by the rural informal financial market in Nigeria in their operations in rural areas seems to be similar with the formal financial institutions that exist in cities and urban area. The informal financial market has been in existence for as long as the Nigerian; indeed the African society has existed. Its evolution is solely rooted in the culture and the practice of the indigenous people.

It is believed of most developing countries to promote rural development through the extension of urban financial institutions services to rural areas. This is to mitigate access to modern financial systems for the rural populace, even though these institutions encounter problems when they operate in the rural areas.

Over time, resources allocation has been concentrated in the major cities and urban centres to the neglect of most rural areas. The inability of the formal financial institutions to provide financial services to the urban and rural populace (especially SMEs), coupled with the non-sustainability of government to finance development programs and projects contributed to the slow growth of private sector-led financial institutions in Nigeria. Before the emergence of formal financial institutions, informal microfinance activities flourished all over the country in areas of job creation and poverty alleviation (Wright, 2010). Hence, the poverty situation in most rural areas in Nigeria is worrisome. This has

triggered the rate of rural-urban migration with its associated problems.

The informal rural financial market is defined to include all classes and types of credit and savings markets outside the formal financial system. The markets under this arrangement is made up of heterogeneous lenders and savers and include landlords, merchants, professional moneylenders, relatives and friends, peer group and other informal credit thrift associations. The key features of these informal schemes are savings and credit components, informality of operations and lower interest rates in relation to the formal banking sector. The informal associations that operate traditional microfinance in various forms are found in all the rural communities in Nigeria (Otu, 2003). These informal financial arrangements operate under different names or nomenclature in different countries and even regions: In Ghana, for example, it is called 'Susu'; "Dajanggi" in Cameroon; "Gamiayah" in Egypt; in Northern Nigeria, it is called "Adashe" by the Hausas, Yoruba in Western Nigeria calls it "Ajo" or "Esusu", while in the Eastern part of Nigeria, the Igbos calls it "Etoto".

There are already several very useful surveys and edited volumes of articles covering the significant important of rural financial markets for sustainable development. A non-exhaustive list of key survey references might include Besley (1994), Stiglitz (1994), Townsend (1995), Morduch (1995), Meyer and Nagarajan(2000), Barry and Robison (2001), Banerjee (2003), Fafchamps (2003), Dercon (2004), Armendariz de Aghion and Morduch (2005) and Oloyede

(2008). For instance, the study of Oloyede (2008) on informal financial sector, savings mobilization and rural development evidence from Ekiti State-Nigeria shows the relative importance of the informal financial sector over its formal financial institutions in mobilizing funds for rural development. The study reveals that myriads of problems still beset their effective performance. He therefore, suggested that if these problems are realistically addressed by radical re-orientation of the sector with appropriate policy reforms, the sector will continue to play prominent role in harnessing the much needed rural finance for sustainable development in Nigeria.

Though, there are divergent views about rural informal financial markets, they are perceived by critics and financial analyst as a market characterized by usury and the purpose of which is to extort money from the rural poor to the advantage of its operators. Nevertheless, informal financial markets contribute around 85 percent of the total rural savings and credits in Nigeria, including moneylenders, daily-collectors, traders and indigenous credit institutions based on cooperative principles called “Esusu” (Adegoke, 2014). The question is, did the financial analysts ever care to ask or consider the prevailing market structure, the clientele, the instruments, and modus operandi and implication for the financial viability and subsistence of the rural people through the informal financial market?

In most rural settings, where conventional banking facilities are non-existence informal credits and savings markets dominates. Despite this, little fact is available to trace more conclusively the relative strength of the informal market due to inadequate statistics. This study, therefore, will examine the challenges and prospects of rural informal financial markets in Kaltungo local government area of Gombe state-Nigeria.

1.2 Statement of the Problem

It has been observed that little or no attention is given to the rural informal financial market operation in Nigeria considering the prominent role they play in sustainable development of rural areas. This is arguably attributed to the fact that the informal markets have been able to provide savings facilities and credits at much cheaper cost and on more favorable terms than that of formal institutions. However, despite the assumed beneficial impact of the informal institutions most especially at the grassroots, their optimal contribution to rural development are argued to still be crippled by a number of challenges such as smallness of their financial capability, inadequate standardized laws and appropriate framework for their regulatory operations, inability to repay loan as at when due, and poor and inadequate record keeping.

1.3 Research Questions

This research study wishes to address the below questions by examining the challenges and prospects of rural informal financial markets in Kaltungo LGA of Gombe state-Nigeria.

- I. The questions that come to the minds of many financial analysts are that, whether rural informal financial markets have persisted where urban financial market failed?
- II. To what extent do their financing mechanisms overcome the weakness in rural informal financial markets and what is the nature of financial services provided by these rural informal financial markets?
- III. What kind of reforms can be introduced to combine the advantages of rural informal markets with those of the formal specialized lending institutions?

1.4 Objectives of the Study

The main objective of the study is to examine the challenges and prospects of rural informal financial markets in Kaltungo Local Government Area of Gombe State-Nigeria. The specific objectives are to:

- a. Determine the level of rural informal financial market challenges and prospects of Kaltungo Local Government Area
- b. Examine whether the informal financial market contribute to economic development in Kaltungo Local Government Area

2 LITERATURE REVIEW

Informal financial market has received differing definitions from various writers and researchers. Shreiner (2000) defined the concept as contracts or agreements conducted without reference or recourse to the legal system, to exchange cash in the present with promise of cash in the future. Informal finance programme is a unique programme for the reduction of vulnerability, and hence the achievement of the Millennium Development Goals (Adamu, 2007). In the words of Osuntogun and Adeyemo (1981), the informal financial market is an indigenous system of saving in varying forms which can be broadly summarized as a situation in which a group of people come together, contribute fixed amount at fixed intervals and assign the total amount contributed to an individual member on rotational basis or offer credit to members and share their accumulated savings at certain time in the year rather than on rotation. Further, Chukwu (1990) described this type of finance as a kind of insurance coverage for the members of the family both extended and immediate. In such case, common purse exists into which every well-to-do family members is expected to contribute his or her own quota and the funds so contributed can be used to give financial support to any members of the family that is not well-to-do. The activities of the informal market, as evidenced by Ojo (1976), appeared to be more pronounced in the non-urban areas than

in the urban areas of the country. Economic indicators showed that over 70 percent of the Nigerian populace lived in rural areas and most of them had been denied access to banking facilities. The significance of this lack of access to banking facilities is better appreciated when one realizes that the bulk of the rural population engaged in agriculture, handicraft and other basic small-scale enterprises. Apart from the lack of access to bank credit to promote these essential sectors of the economy in which the rural population engages, the stock of money in their hands is kept outside the banking system (Olashore, 1988).

As pointed earlier, several studies have attested to the significant role of informal financial markets to sustainable development. Khandker (1998) employed a statistical method to assess the impact of Informal finance among three Bangladeshi programs and found that every additional taka lent to a woman add additional of 0.18 taka to annual household expenditure. Similarly, in an updated study using panel data in Bangladesh, Khandker (2005) found out that each additional 100 taka of credit to women increase total annual household expenditures by more than 20 taka. These studies showed the overwhelming benefit of an increase in income and reduction of vulnerability. Oloyede (2008) conducted a study on informal financial sector, savings mobilization and rural development evidence from Ekiti State-Nigeria. The study shows the relative importance of the informal financial sector over its formal financial institutions in mobilizing funds for rural development. The study reveals that myriads of problems still beset their effective performance. He therefore, suggested that if these problems are realistically addressed by radical re-orientation of the sector with appropriate policy reforms, the sector will continue to play prominent role in harnessing the much needed rural finance for sustainable development in Nigeria. Ijere (1986) also confirms further in a survey of Nsukka Local Government Area that 30% of farmers sampled got their loans from moneylenders, 40% got from Esusu clubs, 10% from supervised credit scheme and 20% from banks. Similarly, Ijaiye, Lawal and Osemene (2012), Alawaiye-Adams, Oluwafemi and Anthony (2014) and Adeusi and Ogunmakin (2014) in their studies stressed that formal sources of finance are inaccessible for households, they resort to the informal form of housing finance to provide a home where they and their families can live in security and comfort, the informal capital markets play an active role in small scale industries development and thereby help in the development of the economy at large and that environmental factors positively correlate with the informal capital markets performance.

3 METHODOLOGY

The population of the study consists of 150 respondents randomly selected from the farmers, traders, businessmen/women, and civil servants in Kaltungo Local Government Area. The instrument used for data collection was personal interview and questionnaire that helped

examined the contribution of rural informal financial markets towards economic viability of the area. The study used both open and closed-ended questionnaire so as to give the respondents the confidence to discuss the issue freely. This was achieved by administering fifteen (15) questionnaires in each of the ten (10) wards of the Local Government Area. The data were collected and collated by personal calls. The responses of the one hundred and fifty (150) questionnaires were used. In the case of decision rule, any response that falls below 50% is negative while any response that falls above 50% is considered positive.

4 DATA PRESENTATION AND ANALYSIS

Table 1: Occupation of Respondents

Occupation	No. of Respondents	Percentage %
Civil servants	29	19.33
Traders	70	46.66
Businessmen/women	25	16.66
Bankers	02	1.33
Farmers	24	16
Total	150	100

Source: Field Survey, 2018

From the table above, it could be depicted that the occupations of the respondents are mostly traders, which constituted the highest number of respondents with 70 (46.66%). This is because traders are the most people who are fully patronizing the informal financial market in Kaltungo Local Government Area. This is followed by civil servants as the next largest respondents with 29(19.33%). From the analysis, it is inferred that civil servants are actually utilizing the informal financial market because it is the only avenue to sourcing of credits from the operators of the informal financial market and repay at the end of the month with less interest rate or what they called commission which requires no collateral. Bankers make up the lowest respondents with 2(1.33%) due to the existence of a single or lone bank (First Bank Nigeria Plc) in Kaltungo Local Government Area.

Table 2: Sex Distribution of Respondents

Sex	No. of Respondents	Percent %
Male	119	79.3
Female	31	20.7
Total	150	100

Source: Field Survey, 2018

Table 2 above indicates that 119 (79.3%) respondents are male while 31 (20.7%) respondents are female. The male has the highest responses, which may not be unconnected to the fact that they are the breadwinners of the family and therefore scout for information regarding any economic activity in Kaltungo Local Government Area is attributed to them and are easily assessable because they are farmers, businessmen/women or civil servants.

Table 3: Responses on sources of business financing (loan accessibility)

Source	No. of Respondents	Proportion in %
Money lenders	77	51.3
Adashe	36	24
Bank	08	5.3
Cooperative Society	-	-
Mutual Aid Programme	18	12
Others	11	7.3
Total	150	100

Source: Field Survey, 2018

From the above table (table 3), majority of the rural dwellers of Kaltungo Local Government Area rely so heavily on the rural informal financial market as their source of financing their businesses as could be observed. An empirical analysis of this information reveals that many farmers patronize money lenders most especially at the beginning of farming season and as well for business transaction and credit. As could be observed from above 51.3% of the respondents source their business financing through moneylenders, 24% respondents from Adashe, 5.3% respondents from conventional bank (formal financing market)- this is due to high rate of interest on deposit money bank's loan and condition of collateral provision which is absent in informal financial market. Also, 12% respondents source their financing from mutual aid programs, while 7.3% respondents source from other sources.

As noted earlier, in terms of the relative effectiveness of the informal financial institutions, over the formal institutions, evidence shows that about 94.7 percent of the respondents patronize informal institutions, while about 0.7 percent only patronize formal institutions. This implies that if informal financial systems are given adequate attention and facilities, they are capable of effectively mobilizing adequate funds needed for the total transformation of the rural economy.

However, most respondents interviewed complained that in the informal financial market there is no fixed interest rate or what they usually referred to as commission charged by the moneylenders. The interest or commission charged seldom depends on the amount and the credit worthiness of the borrower. In general, most of the rural people interviewed in Kaltungo Local Government Area believed that there is too much exploitation from moneylenders which is characterized as usury and it is causing a major drawback in the progress of economic activities in the rural areas.

Table 4: Responses on assessment of the performance of banking operations in Kaltungo Local Government Area

Response	No. of Respondents	Proportion in %
Good	07	4.7
Fair	30	20
Poor	88	58.7
Don't know	25	16.7
Total	150	100

Source: Field Survey, 2018

Table 4 above indicates 58.7% of the respondents reveal poor banking performance, which shows that performance of Kaltungo banking operations do not adequately meet the needs of the rural people. 4.7% of the respondents respond with "Good" which is the least response in terms of the performance of the banking operations in Kaltungo Local Government Area. Sometimes the bank in the town is unable to honor customers' cheque in terms of payment of salaries to civil servants. The bank (First Bank) is not keeping up to the expectation of rural customers. Another problem of the bank is that the current level of cost of funds and transaction cost of formal financial marketers (Deposit Money Banks) already appear too high for the rural borrowers. Moreover, little scope exists for formal institutions (banks) to offer discriminatory interest rates in favor of the rural borrowers given current macroeconomic environment of interest rate liberalization. This has affected the confidence of the rural people in Kaltungo toward banking system supported by the failure of the Shongom Community Bank which made the community develop a negative attitude toward bank savings and general banking transactions.

Table 5: Response on Performance of informal financial market operations in Kaltungo Local Government Area

Response	No. of Respondents	Proportion in %
Good	95	63.3
Fair	39	26
Poor	16	10.7
Don't Know	-	-
Total	150	100

Source: Field Survey, 2018

Table 5 above reveals the performance of the informal financial market which show "Good" as the highest response with 95 (63.3%) respondents. 39 (26%) of respondents rated the performance of the informal financial market as "Fair". This is a clear indication that rural financial market outside banking operations has upper hand as compared to deposit money bank operation in Kaltungo L.G.A. This could be attributed to the easy access to facilitate of the informal financial market. This is evidenced in Table 3 which shows that 95% of the loans were gotten from the informal financial

market (non-banking financial market). This has particularly appears to be the last resort of the rural people particularly farmers seeking credit, this is because the informal financial market are easily accessible as long as the borrowers complied with the terms of repayment. The table further clarified to us that all the people sampled knows about the activities of the informal financial market operation as nobody answered “Don’t Know” on the performance of informal financial market.

Table 6: Response on per capita income in relation to Kaltungo Local Government Area economic activities

Response	No. of Respondents	Proportion in %
Good	17	11.3
Fair	13	8.7
Poor	99	66
Don’t Know	21	14
Total	150	100

Source: Field Survey, 2018

The table above (Table 6) shows a rated per capita income in relation to Kaltungo Local Government Area economic activities which indicated 99 respondents responded “Poor”, with a total percentage of 66%. Reasons of which may be attributed to such a lower rated performance could be lower non-participation in business activities that involves buying and selling as most of the traders in Kaltungo deals with cash crops and engage in the business of hoarding goods which requires an intelligent future forecast of prices.

4.1 Findings

The result indicates that there are four classes of rural informal financial markets namely moneylenders, Adashe, cooperative thrift society and mutual-aid programme. Moneylenders are individuals who possess excess loan able funds or with access to the same, are willing to lend them to needy persons at a fee. According to Ijere (1986), their interest rates range between 20-100 percent and sometimes more, but their loan is characterized by timeliness, regularity and ease of delivery in the place and amount desired collateral security accepted for such loans may be tree crops, farm, land, building and other chattels.

The operation of the moneylenders in Kaltungo L.G.A are confined to well-known persons or guarantee by a person of integrity known to the society or ward head. But how the credit will be used is immaterial to the creditor. This corroborates the finding of Karlsson (2001) that informal capital market intermediaries know their customers well and closely monitored their business payment records vis-a-vis formal lenders and overall prosperity, integrity and cash position of their customers.

The Adashe is the rotating savings and credit association that is popular in the rural areas in Nigeria (Northern part). The association comprises of mostly traders and government workers and very common among small savers in the commercial towns of Kaltungo LGA. In the Adashe system, an initiator who serves as a lender periodically collects a given amount from each member. The money collected is then given in a rotation to each member of the group. The modalities of operation varied from locality to locality. For example, the leaders may receive no special consideration other than collecting the fund first. Others may take commission, which may not reach the total funds collected. However, taking commission has its own default as contributors may hold him liable for any default.

The Cooperative thrift society is also a rotating program where only savings are mobilized and no credit extended to members. The operators are cooperative members who appoint a Secretary that serves as a leader and a collector. This job is done as an income-earning job as the Secretary is paid. He mobilized savings and gives to owners as if he lending it to the owners as this is done at a discount. It has been prove that, this association thrift among the low-income earners particularly traders that want to save even under trying circumstances. The cooperative-thrift society has proved very useful in inculcating savings habit in traders and small farmers who have very small idle cash balances at the end of each sales operation. This equally corroborates the study by Ntiedo (2016) that rural farmers attached relative high importance to informal sources of credits (such as family and friends, thrifts and moneylenders) than the formal sources

The mutual-aid program is more of a cash-in-kind mutual association than cash/credit organization. The members operating under this arrangement mostly and mutually assist each other on their farms through extension of services both in kind and cash. The members must display the willingness to reciprocate to other members the equivalent amount of cash and service when it is his/her turn to do so. A priori information indicated that many dwelling properties were established mainly through the mutual aid scheme.

4.2 Challenges and Prospects

The major challenge evolving from rural informal financial market in Kaltungo Local Government Area is the feasibility of lowering both the direct and transaction cost of financial services obtained. For instance, at current level both the cost of funds and transaction costs of formal financial market (deposit money banks) already appear too high for rural borrowers. Moreover, little hope exists for formal financial institutions to offer discriminatory interest rates in favor of the rural borrowers given current macroeconomic environment of interest rates liberalization. Yet, many rural financial market beneficiaries would like to access facilities at little or no cost. Indeed, financial services provided by friends, relatives and peer group associations are often given at no cost to the beneficiary. Another challenge is to develop a system whereby rural informal financial market

patronesses could derive some benefits from the formal financial system but would shun away from interest rates policy of the banking system. This is particularly an area of concern as direct cost of fund dictated by policy framework appears to be the key element in the current cost of doing business with rural formal financing.

While formal financing service have failed to meet the needs of the rural people adequately owing to inaccessibility and their urban behavior which infuriated them, the scope for progress with the current informal financial markets appears slim in spite of the fact that it had survived the test of time.

It is glaring to note that, the criteria for judging standard rural financial market performance have not been met. But the general aim of a sustainable rural financial market for better performance could be its ability to disburse credits to the rural farmers/businessmen without strict emphasis on ability to repay the credit. It is pertinent to say that, for any financial market to survive in a rural area, it requires different strategy of mobilization of savings to succeed. However, lack of savings mobilization tends to limit the array of services that could be provided to the rural populace.

5 CONCLUSION AND RECOMMENDATIONS

The study was able to identify the inability of the formal financial market to meet the demand of rural people in Kaltungo Local Government Area. While the existing rural informal financial market has been able to make the necessary impact on the credit demands of the rural people despite the problems associated with its operations. However, the few rural informal financial markets operating in Kaltungo Local Government Area have been proved to be assisting the rural people and they have a common base with the formal financial markets.

In view of the forgoing, the following recommendations were made:

- i. Government at all levels should establish a viable financial market that will be adequately beneficial to all rural people including facilitation of transfer of resources at reduced cost from those with surplus funds to those who can make use of them to promote viable financial transactions
- ii. The rural banking programs in Nigeria should be re-examined with a view to establishing an avenue for effective rural banking that will help daily Adashe collection and the money generates from the rural savings through Adashe be deposited in the formal financial institution, with corresponding rate of interest as practice in deposit money banks
- iii. Government should redesign her regulatory policies to formalize the operations of the major institutions in the informal financial sector. However, such regulations should not be carved in a way that will totally cripple institutions' activities, but effectively

enhance their performance for maximum contribution to sustainable development

- iv. The only deposit money bank (First bank) in Kaltungo Local Government Area should encourage rural savings from the informal financial market operators and the granting of credits to genuine customers in the rural areas.
- v. Further research should be encouraged in this area in some other parts of the country in order to improve the future position of both the formal and informal financing in Nigeria.

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