

Institutional voids and informal finance: Theoretical insights for regulating village banking in low-income economies

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ABSTRACT

This conceptual paper explains how institutional voids in formal financial systems shape the rise and persistence of village banking in Zambia and across Sub-Saharan Africa, and it advances a policy approach that protects members without weakening the informal features that make these groups work. Drawing on a structured desk review of peer-reviewed studies, programme reports, and policy documents, the paper applies institutional theory and institutional bricolage to show how village banking groups “piece together” locally workable rules, enforcement practices, and safeguards using trust, social norms, and simple governance arrangements. The synthesis shows a consistent pattern: village banking provides accessible savings and credit, strengthens resilience for low-income households (especially women), and fills service gaps left by rigid, costly, or distant formal providers, but it remains exposed to fraud, weak record-keeping, and limited recourse because it operates outside formal oversight. The paper’s theoretical contribution is to reframe village banking as a legitimate institutional substitute (not a stopgap) and to explain its durability through bricolage processes that blend informal norms with selectively adopted “formal-like” controls (e.g., constitutions, social funds, and basic bookkeeping). The policy innovation is an adaptive, bottom-up financial inclusion policy design: tiered recognition, co-created minimum standards, and voluntary registration with light-touch oversight, enabling consumer protection and safer linkages to wider financial infrastructure while preserving autonomy and flexibility.

Keywords: Financial Inclusion Policy, Institutional Bricolage, Institutional Theory, Sub-Saharan Africa, Village Banking

I. INTRODUCTION

The term village banking was coined by John Hatch in 1984 as a microcredit methodology where poor Bolivian farmers came together to borrow from banks that they shared and guaranteed repayment as a group (FINCA, 2025). In Zambia, village banking, practiced by village banking groups, is said to be an adaptation of the Grameen bank model, which was established by Muhammad Yunus in Bangladesh in the 1970s (as cited in Sishumba & Mulonda, 2019). Village banking groups, sometimes also referred to as savings groups, are informal, self-managed, and self-regulated community savings and credit groups mostly made of women (Mukulu & Qutieshat, 2022). The members of these groups are usually people who know each other because they belong to the same community or are involved in similar activities. They come together in groups of, on average, 10 to 30 members, to save their excess money and use this pool of savings to give credit to the members on a first-come first-served basis at an interest rate that is agreed upon by the group. The groups usually save over a set period of several months, a year, or more, after which the total savings, along with any interest earned on loans, are shared among members on a prorated basis, typically according to each member’s contributions to the total savings pool.

Although informal, village banking groups play an important role in providing financial services and advancing financial inclusion in Zambia (Bank of Zambia, 2020). The unbanked, making up about 30.6% of the Zambian population (FinMark Trust, 2020), turn to informal savings and lending groups like village banking groups, when they cannot access financial services from formal financial institutions (Simatele et al., 2021). Some of the reasons that village banking groups are formed include improving members’ livelihoods and alleviating poverty, particularly for women, as a result of having access to finances that they previously did not have access to (Mukulu & Qutieshat, 2022).

Their informal, self-regulated nature (Bank of Zambia, 2020) therefore reveals the institutional voids, weaknesses, and gaps (Palepu & Khanna, 1998) in the formal financial sector. This is because village banking groups are community-led work-around present solutions for people who are not able to access services from formal financial institutions. They do this by providing them, at the very least, services such as savings and credit which they need access

to for economic activity as well as social belonging which comes from them belonging to the village banking groups. Despite being a solution to the institutional voids in the formal financial sector, they also have institutional voids that stem from their lack of formal oversight. Because of this lack of formal regulation, village banking groups have developed rules and regulations that guide how they operate, and some groups have turned these internally developed rules and regulations into constitutions to which members must agree. However, they still face problems such as not being formally recognized, which limits their legal protection for their consumers and the integration into national policy. They also do not have standardized oversight and external monitoring of their operations, thereby excluding them from beneficial financial structures, such as credit bureaus and debt recovery mechanisms that would improve operational efficiency.

These institutional voids, therefore, raise a fundamental question of how regulation can be designed to support the strengths of informal finance financial initiatives such as village banking without compromising their contribution to advancing financial inclusion for the empowerment of the community by their adaptability and accessibility.

This paper proposes a theoretical framework for the sustainable regulation of village banking, drawing on Institutional Theory and extending the discourse on financial inclusion policy. It contributes by conceptualizing informal finance not as a temporary substitute, but as a legitimate institutional response to enduring governance failures in emerging economies.

1.1 Statement of the Problem

Village banking is a big part of making sure that more people in Zambia and other low-income areas have access to banking services, but it mostly works outside of official rules (Bank of Zambia, 2020; Sishumba & Mulonda, 2019). These groups form because there are gaps in the formal financial system, such as limited access, strict documentation requirements, and product designs that leave out low-income people (Palepu & Khanna, 1998; Simatele et al., 2021). Their informal, trust-based governance allows for flexibility, accessibility, and peer enforcement (Mukulu & Qutieshat, 2022; Laufer et al., 2019), but the lack of standardized oversight puts members at risk of fraud, poor record-keeping, and limited ways to settle disputes (Kalunga et al., 2023; Mwansakilwa et al., 2017).

So, the main question is not whether village banking should be regulated, but how regulation can make the system stronger and protect consumers without hurting the trust and flexible governance that keep these groups going (Kartal, 2021; Pensiri, 2023). Even with more focus on policies that promote financial inclusion, there is still not much theoretical guidance on how to make regulatory frameworks that are both fair and flexible in places where there are institutional voids (Palepu & Khanna, 1998; Pensiri, 2023). This study fills that gap by creating a theory-driven framework that brings together institutional voids, relational trust, institutional bricolage, and adaptive regulation.

1.2 Research Objectives

- i. Theorise village banking as a lasting institutional alternative that emerges in response to institutional voids in formal financial systems.
- ii. Describe how relational trust and informal governance enable the operational stability and legitimacy of village banking in the absence of formal enforcement structures.
- iii. Conceptualise institutional bricolage as the way that village banking groups build, change, and make their own rules and ways of enforcing them.
- iv. Develop an integrated conceptual model that delineates the causal pathways linking institutional voids, trust, informal financial innovation, adaptive regulation, and financial inclusion.
- v. Derive theoretically grounded policy propositions for adaptive and tiered regulatory approaches that enhance consumer protection and systemic resilience without eroding the embedded strengths of informal finance.

II. LITERATURE REVIEW

2.1 Theoretical Review

This study is grounded in Institutional Theory (DiMaggio & Powell, 1983) and its subsequent developments, particularly the concepts of institutional voids (Palepu & Khanna, 1998) and institutional bricolage (Cleaver, 2012). Institutional Theory provides a framework for understanding the emergence and stabilization of organizational forms in response to legitimacy pressures within their broader institutional contexts. The concept of institutional voids illustrates how deficiencies in formal financial systems create opportunities for alternative management approaches. Institutional bricolage explains how communities use existing social and relational resources to create, change, and confirm rules that come from their own communities. These perspectives collectively provide a unified framework for elucidating the persistent nature of village banking and the development of adaptive regulatory strategies that enhance rather than replace established governance frameworks. In Section 3, we create the theoretical framework and conceptual model.

The study of informal finance has employed New Institutional Economics and social capital theory. New Institutional Economics sees informal agreements as alternatives that make things work better when contracts aren't

being followed, with an emphasis on lowering transaction costs. Social capital theory underscores the importance of networks, norms, and trust in sustaining cooperation. While these methodologies provide considerable insights into governance and collective action, they offer a relatively static depiction of cooperation and do not fully clarify the processes through which rules are established, modified, and institutionalized over time. This study integrates Institutional Theory with institutional bricolage to formulate a versatile framework for comprehending the sustainability and adaptability of informal finance systems in response to evolving regulations.

2.2 Empirical Review

2.2.1 Institutional Voids and the Emergence of Informal Financial Substitutes

Empirical studies throughout Sub-Saharan Africa indicate that savings groups form in contexts where formal banking systems are either unavailable, prohibitively expensive, or incompatible with inconsistent income patterns (Palepu & Khanna, 1998; Sishumba & Mulonda, 2019; Simatele et al., 2021). Burlando et al. (2021) and The SEEP Network (2018) assert that VSLAs, SILCs, and analogous models consistently function in regions characterized by minimal formal penetration. These groups serve as alternatives by offering savings and small loans to individuals who are not able to access formal finance.

In Zambia, village banking mostly works outside of formal oversight systems (Bank of Zambia, 2020). This supports the idea that informal finance fills structural access gaps instead of being a short-term solution.

2.2.2 Relational Trust and Informal Governance Mechanisms

Empirical evidence indicates that savings groups depend on peer oversight, communal norms, and collective rule formulation instead of formal contracts (Laufer et al., 2019; Mukulu & Qutieshat, 2022). Groups usually make their own rules, agree on how to lend money, and set up ways to make sure everyone follows the rules, like putting pressure on them to do so.

Cycle-based models show strong internal discipline and high repayment rates in Uganda, Tanzania, and Zambia. This is because of social embeddedness and regular group meetings (Burlando et al., 2021; Flynn & Sumberg, 2018). These ways of governing lower the costs of transactions and make it possible for things to last in places where there isn't a formal enforcement system.

2.2.3 Operational Risks and Governance Vulnerabilities

Studies show that there are always weaknesses, even though governance is strong. Documented risks encompass manual record-keeping errors, exposure to fraud, leadership capture, and restricted legal recourse in disputes (Kalunga et al., 2023; Mwansakilwa et al., 2017). Concerns about sustainability also come up when groups don't have training or outside help (The SEEP Network, 2018). These results show that informal governance encourages flexibility, but it doesn't get rid of systemic risk.

2.2.4 Regulatory Approaches and Policy Tensions

Village banking in Zambia has very little legal involvement other than giving tax advice (Bank of Zambia, 2020; Zambia Revenue Authority, 2023). Experiences from different countries show that there are different ways to do things. The tiered framework in Uganda and the graduated oversight model in Tanzania show how proportionate recognition systems work (The Republic of Uganda, 2016; Ministry of Finance and Planning, 2017).

However, excessive formalization has been linked to diminished participation and the undermining of local legitimacy (Kartal, 2021; Pensiri, 2023). Research indicates that prudential standards intended for formal institutions may result in excessive compliance costs for informal groups (Kahuthu, 2016; Mukama, 2019). The empirical literature indicates that hybrid or adaptive regulatory frameworks may achieve greater coherence with informal governance structures compared to comprehensive formalization.

III. METHODOLOGY

3.1 Research Design

This study adopts a qualitative conceptual research design grounded in a systematic literature review. The objective of the design is to integrate current empirical and theoretical evidence regarding village banking and informal finance to formulate a theory-driven conceptual framework. Instead of collecting new data, the study systematically reviews and combines peer-reviewed studies, institutional reports, and policy documents that already exist to make a model that connects institutional voids, relational trust, institutional bricolage, and adaptive regulation.

3.2 Study Area

The study is centered on Zambia as the primary context. The analysis contextualizes village banking within Zambia's financial inclusion framework, utilizing comparative data from other low-income contexts in Sub-Saharan

Africa and specific emerging economies. Cross-national evidence is utilized to discern persistent governance trends and regulatory strategies pertinent to the Zambian context.

3.3 Target Population

The research does not include direct human subjects. Instead, the target population includes published academic studies, institutional reports, and policy documents that deal with savings groups, village banking, informal finance, governance mechanisms, and regulatory frameworks. These sources together show documented examples of how informal financial systems work in different situations.

3.4 Sampling Procedure and Sample Size

A purposive sampling strategy was employed to select literature directly pertinent to the study's conceptual framework. Sources were identified via systematic keyword searches and reverse citation analysis from seminal texts on institutional theory and savings groups. We also got more information from institutional repositories and academic databases like JSTOR and the University of Zambia repository, as well as reports from the Bank of Zambia, FinMark Trust, and the SEEP Network.

To ensure analytical relevance, sources were incorporated solely if they analyzed informal, community-based savings and lending structures such as village banking, VSLAs, SILCs, or analogous savings groups; tackled issues of governance, enforcement mechanisms, risks, consumer protection, inclusion outcomes, or regulatory strategies; and offered comprehensive analysis rather than cursory or fleeting references. Sources were omitted if they failed to provide substantive discourse on governance or regulation, replicated findings previously addressed in more comprehensive syntheses, or did not advance the study's conceptual aims. The last group of works looked at are the ones listed in the reference list.

3.5 Data Collection Instruments and Procedure

The main way to collect data was a structured literature review matrix that was made to pull out and organize information into set analytical groups. The matrix included the author, the context, the methodology, the governance mechanisms, the risks that were found, the regulatory approaches, and the main findings that were relevant to institutional voids, trust, informal innovation, and adaptive regulation.

We went over the literature several times. We started by searching for keywords and then used backward citation tracking to find important foundational works. Before being added to the review matrix, documents were checked to see if they met the criteria for inclusion.

3.6 Data Analysis

Thematic synthesis was used to look at the data. The study's main ideas were used to make an initial coding framework: institutional voids, relational trust and informal governance, informal financial innovation, and adaptive regulation. There were two steps to coding.

First, descriptive coding found the most important claims and findings in each source. Second, analytic clustering looked at how things came together and fell apart in different situations to find patterns and causal links that happened over and over again. This iterative process guided the formulation of advanced themes and the creation of the proposed conceptual model, encompassing the relational dynamics among the constructs.

3.7 Ethical Consideration

The research utilized solely publicly accessible secondary data and did not include human subjects. Because of this, formal ethical clearance was not needed. However, academic integrity was upheld through precise citation, accurate depiction of source material, and the avoidance of selective reporting.

The methodology has some flaws, such as the possibility of publication bias in the literature that is already out there, the fact that it relies on written evidence instead of lived experiences, and the fact that thematic synthesis is biased in its own way. Moreover, the suggested conceptual model has not undergone empirical validation and necessitates further examination through primary research.

IV. FINDINGS & DISCUSSION

This section summarises the results of the desk review in relation to the study's goals, with a focus on institutional substitution, relational trust, institutional bricolage, and regulatory implications.

4.1 Findings from the Desk Review

A review of literature across Sub-Saharan Africa and comparable low-income contexts reveals consistent patterns regarding the initiation, operation, risks, and regulatory environment of village banking and related savings group models. The results are organized based on the main ideas that this research is based on.

4.1.1 Institutional Voids as Drivers of Informal Financial Substitution

The literature indicates that savings groups arise in contexts where formal banks have restricted geographic reach, inflexible documentation requirements, collateral expectations, elevated transaction costs, and product designs that fail to accommodate irregular income patterns, aligning with the goal of conceptualizing village banking as a sustainable institutional alternative. Evidence consistently demonstrates that village banking serves as a locally recognized alternative in the absence or inaccessibility of formal financial systems (Palepu & Khanna, 1998; Pearce & Zulu, 2020; Sishumba & Mulonda, 2019).

These groups are not temporary solutions to problems. Their persistence across communities and replication over time indicate institutional stability rather than transient adaptation. Patterns of sustained participation show that village banking does more than just add to formal finance; it also fills in the gaps in services that are caused by institutional voids.

4.1.2 Relational Trust and Informal Governance as Stability Mechanisms

The review demonstrates that relational trust and informal governance contribute to operational stability by revealing consistent governance patterns across various countries. Savings groups are usually run by the members themselves, follow rules that everyone agrees on, meet on a regular basis, and use peer monitoring and reputational enforcement instead of formal contracts (Burlando et al., 2021; Mukulu & Qutieshat, 2022; Laufer et al., 2019).

Relational trust and social embeddedness lower the costs of enforcement and make it more likely that people will follow the rules. Shared norms, participatory decision-making, internal constitutions, and group accountability mechanisms serve as alternatives to external regulatory oversight. These governance arrangements support long-term stability, especially in rural and low-income areas where there aren't many or any formal legal enforcement systems.

4.1.3 Institutional Bricolage as the Mechanism of Operational Adaptation

The review shows that savings groups do not copy formal banking structures, which is in line with the goal of conceptualizing institutional bricolage. Instead, they slowly build governance frameworks with social and relational resources that are available in their area. When operational problems come up, groups make their rules clearer, write down their procedures in constitutions, set up social funds, improve their bookkeeping, and change their lending limits.

This adaptive process exemplifies institutional bricolage, wherein participants utilize existing norms and relational capital to construct viable governance frameworks amidst constraints (Clever, 2012). Bricolage elucidates the stability and functionality of informal finance systems in the absence of formal legal oversight.

Evidence indicates that these adaptive arrangements enhance access to savings and small loans for marginalized populations, especially women, rural households, and youth (The SEEP Network, 2018; Flynn & Sumberg, 2018). Members say they are better at managing their cash flow and are more resistant to shocks. Nonetheless, the literature suggests that, although short-term financial inclusion and resilience outcomes are uniform, long-term income mobility and structural poverty alleviation differ across contexts. Wider economic opportunities, group capacity, and conditions of external support affect whether participation leads to sustained upward mobility.

4.1.4 Persistent Governance Risks and Regulatory Tensions

The review reveals persistent operational vulnerabilities in savings groups, pertinent to the goal of formulating policy propositions for adaptive regulation. Some of the risks that have been written down are mistakes made when keeping records by hand, being open to fraud, leadership capture, not having enough money at the start of savings cycles, and not having many options for resolving disputes (Kalunga et al., 2023; Mwansakilwa et al., 2017). These weaknesses show how hard it is to run a business without formal oversight systems.

Comparative regulatory experiences illustrate that design is significant. Tiered and proportionate oversight frameworks, exemplified by those adopted in Uganda and Tanzania, suggest the potential to enhance transparency and depositor confidence while preserving informal governance structures (The Republic of Uganda, 2016; Ministry of Finance and Planning, 2017). Conversely, excessive or misaligned formalization may diminish participation and erode trust when regulatory frameworks do not conform to established community norms (Kartal, 2021; Pensiri, 2023).

The results indicate that the primary policy challenge is not the necessity of regulation, but rather how it can enhance consumer protection and systemic resilience without undermining the trust-based governance that underpins village banking.

The desk review shows that village banking fills long-term gaps in formal finance, that relational trust and internal governance are what keep things stable, that institutional bricolage allows rules to change over time, and that

regulatory intervention must be appropriate and take the situation into account. These insights constitute the empirical foundation for the theoretical framework and conceptual model delineated in the ensuing section.

4.2 Theoretical Framework and Conceptual Model Development

Building on the empirical patterns identified in Section 4.1, this study constructs a theoretical framework based on Institutional Theory (DiMaggio & Powell, 1983) and the literature on financial inclusion, building upon the empirical patterns identified in Section 4.1. The framework incorporates institutional voids and institutional bricolage into a dynamic regulatory model to elucidate the operation, stabilization, and evolution of village banking in contexts characterized by fragile formal financial infrastructure. Instead of seeing informal finance as a short-term solution, the framework sees village banking as a long-term institutional replacement that can only last if it is based on trust and has the right amount of regulatory support.

4.2.1 Institutional bricolage serves as the connecting mechanism.

Institutional theory explains why village banking persists in places with weak or inconsistent rule systems and unreachable formal finance. However, "why do alternatives emerge?" is only one important question in informal finance settings; another is "how do they become workable and legitimate in daily practice?" This paper extends the framework by introducing institutional bricolage as a means of bridging the gap between institutional voids and informal governance and regulatory design (Cleaver, 2012).

In this paper, the term "institutional bricolage" refers to how local resources are utilized by communities to create and continuously enhance beneficial regulations. This is evident in village banking, where groups create internally enforced rules and, in some cases, formalize them into constitutions to govern savings, lending, enforcement, and leadership, as there is no official oversight or standardized external monitoring. These locally formed agreements eventually become "the institution," which is recognized and upheld by its members. They are held together by frequent meetings, peer accountability, and trust rather than formal contracts.

The framework's incorporation of bricolage also clarifies the goals of regulations. If locally established rules have aided in a group's survival, regulations that ignore or replace them are likely to encounter opposition or non-compliance. Regulation that takes current practices as a starting point and strengthens them in particular ways is a more practical way to improve consumer protection without upsetting the social logic that keeps the groups operating.

4.2.2 The Four Concepts as a Dynamic System

The framework makes use of four fundamental ideas, but instead of treating them as distinct, fixed parts, it views them as a dynamic system that changes through institutional bricolage. First, because excluded groups are unable to comply with collateral, identification, cost, or access requirements, institutional gaps in formal finance foster group problem-solving. Second, in response, communities use institutional bricolage to put together practical local laws and customs that serve as the foundation for informal financial governance (such as established regulations, enforcement procedures, and constitutions), allowing village banking to function without official legal support. Third, these governance structures support community-based finance, which replaces formal contracts with transactions based on peer networks and social ties. Lastly, as the system expands, new risks (fraud, poor management, exclusion from wider infrastructure and dispute mechanisms) arise, putting pressure on the need for adaptive regulation.

Importantly, this system is not "external" to regulation. Regulation is another institutional input that groups use bricolage to interpret and incorporate after it is introduced. This indicates that the relationship is cyclical. That is voids lead to bricolage, which in turn leads to governance and community finance, outcomes and risks lead to regulatory response, regulation then modifies practices, which eventually leads to more bricolage.

4.2.2.1 Institutional Theory and the Rise of Informal Finance

DiMaggio and Powell (1983), in their work on Institutional Theory, suggested that organizations and systems change in response to broader institutional environments, not just based on efficiency or profit, but because they conform to what is seen as appropriate or legitimate in their context. In places where formal institutions fail or do not exist, alternative systems rise to fill the void, not just as temporary fixes but as locally accepted ways of doing things. Village banking has emerged as an alternative to fill the void that exists. Despite not being regulated, village banking assumes that it is indeed an alternative, one that is workable. In many cases, people turn to village banking not because they are unaware of formal banks but because the formal system simply does not work for them. The high levels of participation, trust, and voluntary compliance within the groups suggest that members consider the system legitimate. Because this is a conceptual paper, the key terms below are defined as used in this study: Informal finance: Financial arrangements operating outside formal banking regulation.

Savings groups: Self-managed, community-based collectives that pool savings and provide internal loans to members. Village banking: A structured form of savings group common in Zambia, operating through time-bound cycles, agreed rules, pooled lending, and end-of-cycle share-outs. In this paper, "village banking" refers specifically to

the Zambian model, while “savings groups” refers to the broader typology. Institutional voids: Gaps in formal financial infrastructure, including limited access, rigid documentation or collateral requirements, weak consumer protection, and misaligned financial products. These gaps create space for community-based financial alternatives. Adaptive regulation: Proportionate, context-sensitive oversight that reinforces informal governance structures rather than replacing them. It is distinct from full formalization and may include tiered recognition, co-created minimum standards, and light-touch supervision.

4.2.2.2 Relational Trust and the Role of Social Embeddedness

The village banking group operates on a system of trust, which is, what holds them together because they do not have any formal regulations in place. The groups are also self-selecting, usually from people belonging to the same community, which makes it much easier for them to trust each other. Their regular meetings make it so that they are held accountable to one another by doing what is expected of them. These regular meetings also allow the leadership to enforce rules using peer pressure, believing that members feel reputational pressure. This social embeddedness is a strength of village banking groups, which allows these systems to function with minimal costs in places where formal systems would collapse or be too expensive to maintain. However, the same informality that gives these systems flexibility also makes them vulnerable to vices such as fraud, mismanagement, and exclusion from wider financial structures such as credit bureaus and formal dispute mechanisms, which require participants to have formal systems in place. Therefore, it is necessary to preserve the trust-based nature of these systems while still offering safeguards against the vices that they may face.

4.2.2.3 Filling the Governance Gap, Not Replacing It

With regard to governance, the issue is not about whether village banking should be fully formalized or absorbed into the formal sector, which would risk them losing some of the features that make them unique and attractive to those who are members. The issue is rather about how village banking can be regarded as a formal institute and, therefore, a substitute in places where the formal sector cannot reach or where they are unable to operate. This is where adaptive regulation occurs. Therefore, instead of forcing informal systems into boxes that fit formal systems, regulations should be built around the realities and culture of informal systems.

4.2.2.4 Adaptive Regulation and Governance Reinforcement

Adaptive regulation is oversight that is proportional and takes into account the situation, and it strengthens informal governance instead of replacing it. In situations where there are gaps in institutions, regulation can't depend on strong enforcement or fully formalized systems. It needs to build on trust-based systems that are already in place.

Adaptive regulation interacts with informal financial innovation and relational trust in the model by adding minimum protections that lower the risk of fraud, poor record-keeping, and limited ways to settle disputes. Some examples are tiered recognition, voluntary registration, and standards for governance that were made by both parties.

Regulation is viewed as an integral component of a dynamic institutional process. After being introduced, it is understood and integrated through institutional bricolage. When it fits with community standards, it makes things more stable, gives depositors more confidence, and makes things more clear. It may hurt participation and trust if it is too rigid or not aligned properly.

Adaptive regulation works as a way to strengthen governance, protect consumers, and make them more resilient, all while keeping the social logic that makes village banking work.

4.2.3 Proposed Conceptual Model

The empirical patterns delineated in Section 4.1 serve as the foundation for developing a theory-driven elucidation of the emergence, stabilization, and evolution of village banking in contexts marked by institutional voids. This section transitions from descriptive synthesis to conceptual integration by structuring the recurring themes into a cohesive framework based on Institutional Theory and institutional bricolage.

The proposed conceptual model, built on the insights of DiMaggio and Powell (1983), Palepu and Khanna (1998), and literature from Sub-Saharan Africa, South and Southeast Asia, and the Middle East, explains how village banking, an informal financial system, responds to regulatory failures. The model has four components: institutional voids, community trust, informal innovation, and financial inclusion. The model also accounts for how adaptive regulation can strengthen the system without undermining the values that give them strength.

Figure 1 presents a causal, time-sequenced model rather than a set of static associations. The direction of causality runs from left to right. Institutional voids represent failures in formal financial systems, including limited access and rigid requirements that exclude low-income and rural populations. These voids create the initial conditions that push communities to rely on informal arrangements such as village banking (Palepu & Khanna, 1998; Bank of Zambia, 2020; Simatele et al., 2021). Community trust is positioned as a causal enabling factor because it makes collective saving and lending feasible without formal contracts. Trust supports member self-selection, peer monitoring,

and enforcement of group rules through social accountability and shared norms, which reduces transaction and enforcement costs within the group (Mukulu & Qutieshat, 2022; Laufer et al., 2019).

Institutional voids, community trust, and adaptive regulation influence financial inclusion primarily through informal financial innovation, which is treated as the mediating mechanism in the model. Informal financial innovation refers to the practical governance and operational adaptations that allow village banking groups to function and endure, including group constitutions, internal guidelines, social funds, and, in some settings, digital bookkeeping tools tailored to local needs (Burlando et al., 2021; Jarden & Rahamatali, 2018). These innovations improve the reliability and reach of savings, credit, and informal insurance, strengthening household resilience and supporting the inclusion of women and youth in financial activity (Flynn & Sumberg, 2018; FinMark Trust, 2022). The model therefore specifies that the pathway from institutional conditions to financial inclusion is not automatic; it depends on whether groups develop and sustain innovations that stabilize governance, strengthen discipline, and protect pooled resources (Burlando et al., 2021; Mukulu & Qutieshat, 2022).

Adaptive regulation enters the model as a policy input that shapes both the innovation pathway and the system’s evolution over time. It affects informal financial innovation by providing proportionate safeguards and recognition that strengthen transparency and basic consumer protection without undermining flexibility (Pensiri, 2023). Adaptive regulation also has feedback effects on earlier components. First, it can reduce the severity of institutional voids by partially substituting for missing formal protections through minimum standards, dispute resolution pathways, and clearer accountability mechanisms, thereby lowering exposure to fraud and collapse (Bank of Zambia, 2020; Pensiri, 2023). Second, it can strengthen community trust by increasing confidence in the safety and fairness of group processes where members perceive improved transparency and protection. Conversely, where regulation is experienced as top-down, capacity-heavy, or misaligned with local norms, it can weaken trust and participation, which is why the model emphasises adaptive rather than blanket formalisation (Pensiri, 2023; Jere, 2024). Over time, improved financial inclusion can further moderate institutional voids by reducing households’ reliance on the most risky informal coping strategies, but the model does not assume that inclusion eliminates voids; instead, it assumes incremental improvements that are amplified when regulation supports the trust and innovations that hold the system together (Palepu & Khanna, 1998; Pensiri, 2023).

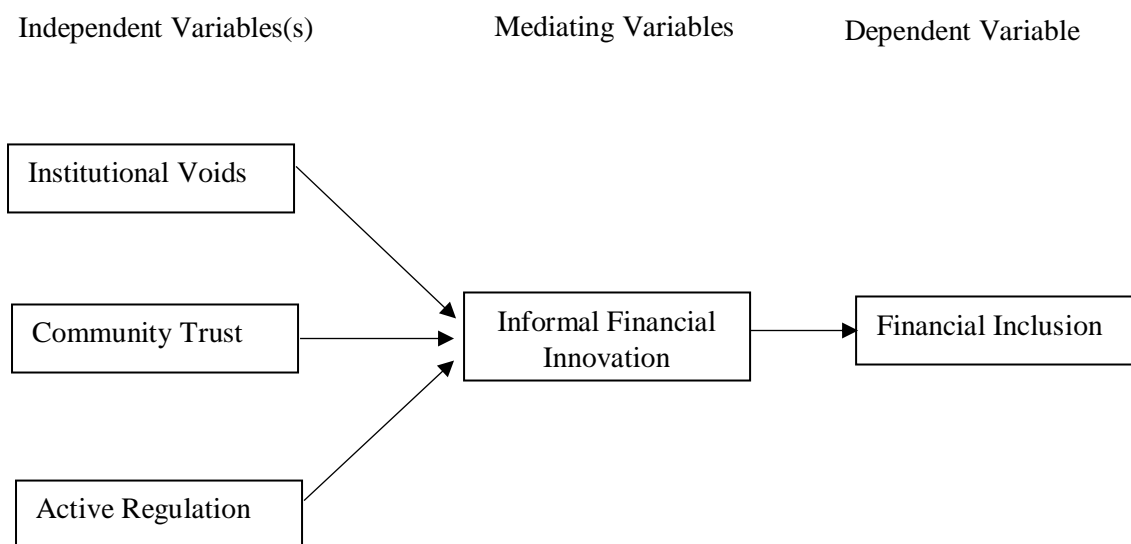


Figure 1
Conceptual model of institutional voids, trust, innovation, and adaptive regulation
 Researcher’s Design (2025)

4.2.3.1 Propositions from the Conceptual Model

The model gives rise to the following propositions, which reflect the causal pathways in Figure 1:

Proposition 1: Institutional voids in the formal financial system increase reliance on informal finance arrangements such as village banking as practical substitutes for excluded populations (Palepu & Khanna, 1998; Bank of Zambia, 2020; Pensiri, 2023).

Proposition 2: Community trust strengthens informal governance and compliance, which increases the feasibility and stability of village banking operations over time (Laufer et al., 2019; Mukulu & Qutieshat, 2022).

Proposition 3: Informal financial innovation mediates the relationship between institutional voids/community trust and

financial inclusion, because group-level innovations (e.g., constitutions, social funds, bookkeeping practices) are the mechanisms through which access to savings, credit, and informal insurance is delivered reliably (Burlando et al., 2021; Jarden & Rahamatali, 2018). Proposition 4: Adaptive regulation strengthens financial inclusion by reinforcing informal financial innovation and depositor protection without undermining autonomy; when misaligned or overly burdensome, it can weaken trust and participation (Pensiri, 2023; Kartal, 2021; Jere, 2024). Proposition 5: Where adaptive regulation is introduced through tiered and context-sensitive approaches, it supports consumer protection, scalability, and voluntary linkages to the broader financial infrastructure while allowing groups to maintain informal operating structures (The Republic of Uganda, 2016; Ministry of Finance and Planning, 2017).

In Zambia, village banking plays an important role in advancing financial inclusion by providing basic financial services to financially excluded groups, yet gaps in oversight create exposure to fraud and mismanagement, which can undermine trust and destabilise group operations (Bank of Zambia, 2020b; Lusakatimes, 2022; Jere, 2024). This study therefore treats regulation as a supporting function rather than an absorption mechanism: the objective is not to convert village banking into formal banking, but to introduce proportionate safeguards that preserve flexibility, autonomy, and trust-based governance. Evidence from Uganda and Tanzania suggests that tiered approaches can provide legal recognition and consumer protection while allowing groups to retain informal structures and graduate into higher compliance requirements at a manageable pace (The Republic of Uganda, 2016; Ministry of Finance and Planning, 2017). This is particularly important given evidence from other contexts, such as South Africa, where top-down or bureaucratic formalisation has been associated with community resistance and perceived loss of flexibility (Kartal, 2021).

4.2.4 Implications for Theory and Policy

4.2.4.1 Theoretical Implications

This study extends Institutional Theory by applying it to informal, community-led financial systems such as village banking. This demonstrates that, in contexts where formal institutions fail, informal finance is not a temporary workaround but a legitimate institutional substitute. The findings show that such systems develop governance, trust-based enforcement, and adaptive mechanisms. This challenges the idea that formalization must always replace informality, and instead support a model in which both systems can coexist and complement each other.

4.2.4.2 Policy Implications

This paper proposes that rather than trying to formalize village banking through rigid top-down regulation, policy should adopt a hybrid approach. This means combining light-touch oversight from the state with the existing group-level accountability structures. Governments and regulators should work with communities to co-create standards that reflect the functioning of informal systems. Practical options include tiered regulations and voluntary registration. Such policies would preserve the core strengths of these informal systems, such as trust, flexibility, and low transactional costs, while offering the necessary consumer protection against fraud and financial mismanagement.

4.3 Discussion

This research aimed to create a theory-based framework for comprehending and overseeing village banking in environments marked by institutional deficiencies. The results and conceptual framework collectively substantiate three principal arguments. First, village banking should not be seen as a temporary or marginal way to cope. The synthesis shows that these systems continue to exist because they fill in the gaps in formal financial services. Institutional gaps in access, documentation, enforcement, and product design create long-lasting situations where informal financial arrangements become accepted and rooted in the community. As a result, the model sees village banking as an institutional replacement instead of a leftover option. Second, trust alone does not explain why village banking lasts; institutional bricolage does. Relational trust helps people work together, while bricolage shows how governance structures are put together, changed, and made stable over time. Groups make internal rules more official, write constitutions, set up social funds, and change how they enforce rules when new risks come up. This dynamic adaptation explains why informal finance systems continue to exist even though they don't follow the rules set by the government.

Third, the analysis indicates that the regulatory inquiry is not about the formalization of village banking, but rather how regulation can enhance protection without compromising established governance. The conceptual model illustrates that adaptive regulation serves as an institutional input that engages with trust and innovation. When it is appropriate and takes the situation into account, regulation strengthens transparency, depositor trust, and scalability. When inflexible or misaligned, it jeopardizes participation and undermines trust. This study theoretically expands Institutional Theory into the realm of informal, community-driven finance. By combining institutional voids and institutional bricolage, it offers a dynamic explanation for how institutions last and how regulations change. The framework transcends static narratives of transaction cost reduction or social capital by elucidating the evolution and institutionalization of rules through practice.

The results back up a mixed regulatory approach from a policy point of view. Policymakers should not impose full prudential standards meant for licensed financial institutions. Instead, they should use tiered recognition, voluntary registration, and minimum standards that everyone agrees on. This method makes consumer protection stronger while keeping autonomy, flexibility, and governance based on trust. In general, informal and formal finance don't have to be seen as opposites. A complementary, adaptive regulatory model enables informal systems to preserve their inherent strengths while progressively incorporating protective mechanisms that bolster resilience and inclusivity.

V. CONCLUSIONS & RECOMMENDATIONS

5.1 Conclusions

This paper proposes a theory-based framework for comprehending and governing village banking in low-income economies. Utilizing Institutional Theory and institutional bricolage, it reconceptualizes village banking not merely as a transient coping mechanism but as a sustainable institutional alternative that arises in contexts where formal financial systems inadequately address marginalized populations. Institutional deficiencies in access, enforcement, and product design establish the structural prerequisites for informal financial innovation. Communities create governance systems that support savings, credit, and resilience without formal oversight by using relational trust and rules made by people in the community.

The study shows that village banking's long-lasting nature is not a coincidence. It is maintained by bricolage processes that let members change rules, add protections, and stabilize governance by using the social and relational resources they have. Simultaneously, enduring vulnerabilities, such as exposure to fraud, inadequate record-keeping, restricted dispute resolution, and exclusion from broader financial infrastructure, underscore the necessity for regulatory involvement.

The study's primary contribution is to reconceptualize regulation not as integration into formal banking frameworks, but as adaptive reinforcement of intrinsic governance. Adaptive regulation is seen as a cyclical institutional input that boosts innovation and protection without taking away autonomy or trust-based accountability. The paper presents a dynamic model that incorporates institutional voids, relational trust, informal innovation, and adaptive regulation, offering a structured framework for integrating informal finance into national financial inclusion strategies while maintaining its advantages. The framework thus transitions the policy discourse from the formalization of village banking to the formulation of regulations that bolster protection, scalability, and systemic resilience while preserving the institutional logic that underpins these systems.

5.2 Recommendations

Based on the conceptual model and propositions, the following policy directions are proposed: Adopt Tiered Regulatory Recognition – Introduce graduated recognition frameworks that distinguish between small, community-based savings groups and larger, semi-formal entities. Compliance requirements should scale with size, complexity, and risk exposure rather than impose uniform standards. Co-Create Minimum Governance Standards – Regulators should collaborate with savings group federations, NGOs, and community leaders to define minimum operational standards such as transparent record-keeping practices, basic dispute procedures, and leadership rotation guidelines. Standards should reinforce existing internal rules rather than replace them. Establish Voluntary Registration Mechanisms – Create voluntary, low-cost registration pathways that provide groups with legal recognition and access to dispute resolution mechanisms without imposing heavy prudential requirements.

Provide Capacity-Sensitive Support Tools – Develop simplified bookkeeping templates, digital record-keeping applications tailored to low-literacy contexts, and basic governance training programs to reduce operational risk while preserving group autonomy. Strengthen Consumer Protection through Light-Touch Oversight – Instead of direct supervision, regulators can implement complaint-reporting channels, awareness campaigns on fraud prevention, and community-level monitoring partnerships that enhance accountability without bureaucratic burden. Facilitate Safe Linkages to Formal Infrastructure – Enable savings groups to voluntarily connect to credit bureaus, mobile money platforms, and microfinance institutions through partnership models that respect group identity and decision-making structures. Pilot Adaptive Regulatory Models Before National Roll-Out – Conduct regulatory sandboxes or pilot programs in selected districts to test proportional oversight models before full-scale implementation.

Declaration of Interest

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