

Microfinance in Africa: How do we ensure the continent's poorest can share economic opportunities?

TAKE ACTION:

Our action this month is to build parliamentary support for microfinance and to ask our MPs to help ensure that the proposed 'Capacity-Building Fund for Microfinance in Africa' that is being developed by the UK Department for International Development (DFID) and the World Bank is as effective as possible at reaching the poor and improving their chances of getting out of poverty. Please write to your MP, covering the following points:

- Explain why there is a need to scale up access to financial services in Africa and why microfinance is a good tool to help alleviate poverty;
- Acknowledge DFID for partnering with the World Bank to explore the idea of a fund that will help to increase access to microfinance in Africa;
- Ask your MP to write to the Secretary of State for International Development and to the President of the World Bank Robert Zoellick encouraging the swift implementation of the 'Capacity-Building Fund for Microfinance in Africa', and to ensure that is designed with a strong poverty-focus and incorporates social performance indicators and monitoring of its impact on poverty alleviation;
- Ask your MP to recommend that at least \$200 million (the amount requested in ongoing communications between the US Senate and the World Bank) is allocated to the Fund to enable it to be effective with the potential for increases in size and support from other donors in the future;
- Ask your MP to commend the recent announcement that DFID will develop more microfinance programmes, to ask for more information about these and to push for them to explicitly target poverty reduction and to include robust impact monitoring strategies within their design.
- Ask your MP to share any responses that she/he receives from DFID and the World Bank.

Africa – the 'unbanked continent'

In the original 1970s hotbeds of microfinance, particularly India and Bangladesh, access to financial services has blossomed. But in other areas of the world, particularly Africa, access to financial services, and to microfinance as a sub-sector of this, remains very low. Africa is the most unbanked continent in the world, in which formal financial services have just not penetrated. For example in Ethiopia it is estimated that just 1% of rural households have a bank account.

A study in 2004 found that even when broadly defining microfinance to include postal savings banks, cooperatives and some other financial institutions, only 27 million accounts were held by clients of microfinance organisations in Africa – representing just 4% of the total population.¹ Because of this the majority of poor Africans remain reliant on money-lenders or other informal sources such as family and friends for access to credit, and similarly precarious savings systems such as rotating funds or reciprocal gifts or favours between relatives. Institutions as diverse as the IMF and charities like CARE which directly provide microfinance in Africa comment on the limitations that this places on African economies: 'This lack of access to financial services from the formal financial system is quite striking, when one considers that in many African

countries the poor represent the largest share of the population and that the informal sector is an important part of the economy.'²

Microfinance in Africa

While there are examples of very successful Microfinance Institutions (MFIs) in various countries in Africa – in 2007 Kenya had three MFIs that had over a million clients each – and there are many MFIs in existence in Africa, levels of access remain stubbornly low and there are a series of serious challenges for the sector. These include governmental issues such as weak legal and regulatory frameworks and political situations; issues within MFIs themselves, particularly lack of financial capacity and human capital; and geographic factors, such as the reliance of economies on agriculture, low population densities and weak infrastructure, which all make microfinance transactions more expensive and risky.

Because of these issues MFIs in Africa have tended to be relatively small, and in many cases they are not financially sustainable, which has led to the collapse of institutions, causing serious difficulties for clients and a consequent loss of confidence in microfinance as a sector. Many people in the microfinance industry believe that the biggest constraint to the growth of microfinance in Africa lies in the institutional issues. Particular

deficiencies that have been identified include: weak internal control systems and procedures, leading to a lack of financial transparency and viability; lack of sustainable funding; and insufficient training and scarcity of skilled manpower leading to staff shortages – especially in the roles of loan officer, middle management and leadership.

Support for individual MFIs to address these issues has not been forthcoming from donors, leaving many countries with weak, unaccountable and non-inclusive financial sectors even where MFIs do operate.

RESULTS and microfinance advocacy

RESULTS has been working to increase support for microfinance since the 1980s. In more recent years our advocacy has focused largely on two targets: our government and the World Bank. Just a few days ago the UK government announced that they plan to develop more microfinance programmes to ensure that UK aid supports economic development. Few details of these new programmes have emerged, but the announcement is very welcome.

As the largest international lender for developing countries, the World Bank has an enormous influence over whether the world will achieve the Millennium Development Goals. The Bank's stated mission is "global poverty reduction and the improvement of living standards" and "working for a world free of poverty." The World Bank's own research shows that microfinance is a proven, effective tool for addressing the worst aspects of poverty, even among the very poor.

In 2008 43 Members of the US Congress and 30 Senators signed a letter to the President of the World Bank, Robert Zoellick, which requested the Bank to: 1) create a new \$200 million grant facility for MFIs trying to reach the very poor, 2) create and support 'Centres of Excellence' at MFIs like Grameen Bank in Bangladesh where interested parties can learn how to reach the very poor with microfinance, 3) create a sub-Saharan African Apex Fund, a funding mechanism that will allow more MFIs focusing on the very poor to access capital. This has been followed up with an [additional letter sent in July 2010](#).

DFID and the World Bank plan a capacity-building fund for Africa

In response to the sustained pressure to support microfinance, in late 2009 the UK Department for International Development (DFID) and the World Bank joined together to establish a new 'Capacity-Building Fund for Microfinance in Africa'. This is planned to give support to existing and start-up microfinance institutions on the continent to strengthen their operations and be able to reach out sustainably to poorer customers. Currently, the UK has engaged a consultant to design the new Fund, and has undertaken a peer-review process.

A more detailed assessment of the most recent 'concept note' for the Fund is in Background Sheet 2. There are some major concerns with the direction the process is taking so far. Within the concept note there is a commendable focus on increasing access to financial services for 'poorer' clients, but there is no definition of what is meant by 'poorer' or details of how this will be achieved. It is crucial if the Fund is to relieve poverty that it targets those living on below \$1.25 a day. Most worryingly, there is no detail of whether and how impact monitoring will be carried out.

At RESULTS we believe that for microfinance to fully realise its potential to fight poverty, MFIs and donors supporting microfinance institutions must explicitly adopt a strategy that aims to have social impacts such as reducing poverty, and measures progress towards achieving them, as well as having strong financial strategies and controls. 'Most MFIs have explicit social goals within their mission statements, but these are rarely seen as part of a deliberate and managed strategy.'³ But it is crucial to know whether microfinance is actually helping customers to better manage their finances and to escape the poverty traps that the poor too often find themselves in.

The new Capacity-Building Fund is a vital step towards ensuring that the sector can reach its potential in Africa and help the estimated 230 million Africans who currently have no access to financial services, however it must be implemented in a way that enables it to have the biggest impact on poverty possible.

¹ R P Christen, R Rosenberg & V Jayadeva. *Financial institutions with a double-bottom line: implications for the future of microfinance*. CGAP Occasional Paper, July 2004

² A Basu, R Blavy, and M Yulek, *Microfinance in Africa: Experience and Lessons from Selected African Countries*. IMF Working Paper, 2004

³ Imp-Act Consortium, a group of researchers and practitioners working to make microfinance more effective for the poor.