

Maintaining growth in microfinance and ensuring benefits for the poor

SUMMARY: *The latest State of the Microcredit Summit Campaign report indicates that 128 million of the world's poorest families obtained credit by the end of 2009, showing that the Campaign is on target to provide credit and financial services to 175 million of the world's poorest families by 2015. However, the Campaign is demonstrating less progress towards the second goal of having 100 million families move above the poverty line, as measurement of the starting position of borrowers and their progress out of poverty is limited. To support an increase in the measurable impact of microfinance on poverty, our letters this month will request that the Australian Government increase funding to implement its microfinance strategy, and concentrate on assisting the poorest people and developing more specific measures of performance in implementing the Strategy.*

BACKGROUND: THE MICROCREDIT SUMMIT CAMPAIGN AND ITS PROGRESS

In the developing world, 2.7 billion adults (almost three quarters of the adult population) don't have access to any 'financial services due to their poverty, illiteracy, gender or because they live in a remote region. For these people, microfinance (provision of fair borrowing, safe saving, relevant and meaningful financial education and appropriate insurance products) can fill this gap.

Microfinance has proven to be a powerful tool to help the world's poorest people to lift themselves out of poverty, and improve their entire family's nutrition, education and housing¹. A review of around 100 impact studies of microfinance since 1986 found a wide range of evidence that microfinance programs can increase incomes and lift families out of poverty. Access to microfinance can improve children's nutrition and increase their school enrollment rates, among many other outcomes².

The Microcredit Summit Campaign, launched in 1997, seeks to extend these benefits to the hundreds of millions of the poorest people who cannot obtain financial services through the mainstream financial system. The original goal for the Microcredit Summit Campaign was to provide access to credit and other financial services to 100 million of the world's poorest families. This goal was achieved in 2007, only slightly later than the original target date of the end of 2005.

The second stage of the Campaign has two goals for 2015:

- To reach 175 million of the world's poorest families with credit and other financial services by 2015; and
- Having 100 million of the poorest families move above the poverty line of \$US 1 per day.

The *State of the Microcredit Summit Campaign 2011* report indicates that 128 million of the poorest families had current loans at the end of 2009, demonstrating good progress towards reaching 175 million of the poorest families by 2015. However, the report notes that it is difficult to demonstrate progress towards having 100 million families move above the poverty line, as few organisations are measuring the starting position of borrowers or their progress over time.

¹ Consultative Group to Assist the Poor (CGAP) focus note No.24 (January 2003): Is microfinance an effective strategy to reach the Millennium Development Goals?

² Goldberg, N. (2006), *Measuring the Impact of Microfinance: Taking Stock of What We Know*

The Campaign commissioned a study in Bangladesh which found that a net 1.8 million microfinance clients (or 9.4 million people including family members) have moved above the poverty line between 1990 and 2008, reflecting the benefits of microfinance.

Commercial Microfinance and a Backlash

Recently, commercial microfinance (run as businesses seeking to earn profits from an early stage) has received negative publicity and has been the target of regulatory restrictions, especially in the State of Andhra Pradesh in India. This state is one of the few locations where microfinance has reached saturation coverage, and some borrowers had a significant debt burden from taking loans from multiple lenders.

In Bangladesh, where microfinance also has a high coverage of the population, the government has also reacted by using its minority shareholding position in the Grameen Bank to seek to replace the founder of the Grameen Bank, Professor Muhammad Yunus, as Managing Director and possibly change the bank's lending focus. The attachment provides further details of these developments. The adverse attention to commercial microfinance increases the need for support for microfinance which provides benefits for people most in need.

IMPLEMENTING AN EFFECTIVE AUSTRALIAN STRATEGY

The Australian Government released its microfinance strategy, Financial Services for the Poor, in March 2010. RESULTS had welcomed several of the Strategy's features including: the recognition of the role of microfinance in achieving most of the MDGs; recognition that poorest clients need to be included, and social performance (and not just financial performance) of these institutions will be measured. However, the implementation of the Strategy needs to strengthen the focus on the following areas:

- **Increasing funding:** The Government indicated in the 2010-11 Budget it would double microfinance funding to up to \$20 million by 2012-13. However, the Government is likely to reach this funding level in 2010-11. Therefore, over the next two years, it would be appropriate to redouble funding to \$45 million per year by 2012-13.
- **Regular and specific measures of performance:** Measurement of progress towards achieving the strategy's outcomes will require baseline data on the programs currently being funded. AusAID will also need to develop numerical targets to demonstrate success. These targets would include encouraging the entry of a specific number of new microfinance service providers or having a specific number of service providers achieve positive financial and social impacts.

ACTION

Write a letter to the editor or media web site, referring to a recent article about poverty or debate about financial regulation in Australia; OR write to your Member of the House of Representatives or Senator from your State, asking him or her to pass the following points on to the Minister for Foreign Affairs:

1. Note the continued growth reported in the *State of the Microcredit Summit Campaign 2011* in the number of microfinance borrowers, to 128 million by the end of 2009.
2. Note that adverse publicity for commercial microfinance organisations creates an even larger demand for assistance for organisations that assist the poorest.
3. Call on the Australian Government to further increase its funding for microfinance and measure performance of its assistance to ensure it is benefiting the poorest people.

CURRENT CONTROVERSIES IN MICROFINANCE

Restrictive regulation in Andhra Pradesh

The Government of the State of Andhra Pradesh in India, a region which has seen rapid growth in microfinance in recent years, passed a regulation in late 2010 which has disrupted microfinance in that state and has implications for the viability of microfinance in other regions.

The regulation requires all microfinance organisations operating in the state to cease operations and apply for a new registration with the state government, and also sets a limit of 100% on the interest rate that microfinance organisations can charge. In addition, the state government has encouraged borrowers to cease repayments to microfinance organisations.

The basis for the regulation has been that newer entrants into the microfinance field in Andhra Pradesh are pursuing rapid growth in loans, resulting in poorer households taking on more debt than they can afford, and are taking an aggressive approach in seeking repayments.

While this regulatory response has occurred in one region in India, the publicity is leading to a debate about whether the rapid growth in microfinance has resulted in a loss of the original focus on creating opportunities for the poorest people, and could even be harming the poorest.

The problems in Andhra Pradesh appear to result from a large number of microfinance organisations operating in one region, competing for the same borrowers. This has resulted in some borrowers taking loans from multiple organisations, which they have difficulty repaying. However, the regulatory response by the Andhra Pradesh Government, which looks like it will damage both the commercially-oriented and the non-profit microfinance organisations, is not the appropriate response. Instead, promoting positive action by microfinance organisations would ensure that the poorest people obtain benefits rather than suffer from growth of microfinance.

Bangladesh Government action against Grameen Bank

In late 2010, Bangladesh Government started taking action against the Grameen Bank, initially in response to a Norwegian documentary that accused the Bank's founder, Professor Muhammad Yunus, of improperly diverting funds donated by Norway's aid agency in 1997. The Norwegian government investigated and found that, while funds were transferred internally from one Grameen-owned affiliate to another, there was no evidence of misuse of the funding.

The Bangladesh government owns 25% of Grameen Bank and has the right to appoint a quarter of its board members, including its chairperson. However, of the Grameen Bank's paid-up share capital, only 3.5% comes from the Bangladeshi government. The majority owners of the Bank are its borrowers, who control 75% of the board seats and they have supplied 96.5% of the paid up share capital.

Nevertheless, the Government has sought to remove Professor Yunus as Managing Director, on the basis that Professor Yunus is now 70, above the mandatory retirement age in government banks, and his original appointment as Managing Director was not approved by the Bank of Bangladesh.

It is important for the Grameen Bank to identify a successor to Professor Yunus, given his age. However, a forced removal of Professor Yunus which appears to be politically-motivated would reduce confidence in the Bank among both staff and borrowers.

The impact of the Government's action against the Grameen Bank may be to convert the Bank into a rural lending organisation, providing subsidised loans. The Prime Minister has indicated that she believes Grameen Bank interest rates are too high (in fact, Grameen's interest rates are relatively low among microlenders). Historically, rural lenders have directed subsidised loans to borrowers who are not poor, and repayment rates have been relatively low. Therefore, converting Grameen Bank into a rural lender providing subsidised loans could threaten both its financial viability and focus on the poorest borrowers.

Principal Source: David Bornstein, *Microfinance Under Fire*, New York Times, 21 March 2011

Further Information: www.microcreditsummit.org