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MICRO FINANCE
Is It Reaching the Poorest?

Bangladesh has gained world renown for its innovative micro finance programmes. But the key question of reaching the hard-core poor remains to be resolved. Matthew MacLean investigates

"I am an old, tired man," responds a haggard-looking man in Jamalpur, asked if he would join a BRAC Village Organization (VO) to get micro loans. "It would be very hard for me to make the payments, and what would happen if I die?" If that happened, his three daughters would inherit his debt. And they are even less able to pay than him. No, he is not able to join a VO, he says.

Too Poor for Credit

Until recently, such a thing was hard to imagine. After all, micro-credit (and microfinance more broadly speaking) has gained fame by successfully lending small amounts to millions of poor women in Bangladesh. But if the idea of someone being too poor for micro-credit seems surprising, for years it hasn't been anything new to people involved in the programmes.

"Those of us who have been involved for some time are aware of [the problem]," says Fazle Abed, executive director of BRAC, referring to micro-credit's inability to reach the poorest, the so-called "extreme poor" or "hardcore poor". So why is it only recently that there have been a spate of conferences and studies around the issue? NGOs have been quick to expand the upper-end of their lending portfolios giving larger loans to more well-off clients, so why have they been slow expanding reach to the poorest?

The main reason is that the actions required to reach them fly in the face of current trends. Reaching the hardcore poor requires a very different approach than the Grameen Bank-style micro-credit formula which gave micro finance its initial success and which, with few exceptions, continues to be the main offering of virtually every NGO involved in micro finance.

In addition, the current obsession with financial sustainability, and the increasing success micro finance practitioners have had in achieving it, has obscured the reality that reaching the hardcore poor has a price. With much of micro finance's explosive growth driving efforts to replicate more cost-effective Grameen-style programmes will this come at the expense of reaching those most in need?

Ceilings and Floors

A well-known criterion for membership in many NGOs disbursing the generic micro-loans is a ceiling on landholdings of no more than half an acre. No less real in practice, though it was not intentional, is a floor on the level of income. A combination of factors leads to this result, a list practically any well-informed micro finance practitioner can recite.

Laily Begum, a 12-year Grameen Bank member from a village near Nagarpur, along with her husband Aminur Rahman, explains one major reason the hardcore poor don't join micro-credit schemes: they are rejected by the other group members. "We would not have picked someone who had trouble repaying," says Begum of how she and her other group members first together. "[Grameen members must be] those who are landless but who are good people: those who won't eat up the money," she says.

As is documented in a study done last year by ASA, the hardcore poor are often perceived by other group members as being below them in social status or unable to repay, and therefore ineligible to join the group. Staff will also avoid people they think are unable to support even a tiny micro-loan.

The very structure of micro-credit programmes can be too rigid for many of the hardcore poor. The discipline, the meetings, the regular repayments; all these factors may make micro-loans unfeasible for the hardcore poor, says Rita Rashid, programme manager for Micro-Enterprise Development with USAID, the American aid agency. "It's hard if you're talking with someone who hasn't eaten all day," she says. Meetings can be especially intimidating to people already marginalised within their village. Often they themselves doubt their capacity to successfully use and pay back the loan.

Fazle Abed of BRAC agrees. With micro-credit, it takes a longer time for the investment to turn into income to support an entire family, so the hardcore poor may not be interested. "[The poorest] must earn something every day," he says. Like the man from Jamalpur, such people "self-selected" themselves out of the group.

What is Too Low?

Where to draw the line on who makes up the hardcore poor? There is no fixed income level that applies. Estimates from the Credit Development Forum (CDF) say that the hardcore poor comprise 10-15% of the population, while studies by the Bangladesh Institute of Development Studies (BIDS) have suggested more than 20%, approximately 26 million people.

While the hardcore poor are undoubtedly at the bottom of the income scale, they are more often identified based on their household characteristics. Families headed by women — widowed, divorced, or abandoned, or where the husband is disabled are often among the hardcore poor. Landless agriculture labourers, who often have no permanent home and move with the seasons, and those who live on the river banks, vulnerable to floods and river erosion form a large segment of the hardcore poor. Old pensioners and the disabled also often fall into this category.

A certain amount of confusion persists about the hardcore poor as a distinct social category. Unfortunately, failure to make the distinction helps perpetuate the belief that the generic micro-long product so widely featured in NGO programmes is equally versatile for all poor people. Thus, as in the view of Prof. HI Latifee, managing director of Grameen Trust, it becomes merely a question of motivation. "Once she sees it's OK, she can do it. It's a different experience," he says of a hypothetical female member of the hardcore poor. "The first step is critical, very critical."

And actually, to some extent, he is right: there is evidence that some of the hardcore poor make it in the regular micro-credit programmes. This, in combination with the great success that micro-credit has enjoyed with the "majority" poor, has made it difficult to believe that there is a need for anything else.

Sustainability

As a recent World Bank report on poverty trend and strategies put it, when microfinance started, the number of poor without access was so great that who was helped was not important. Reaching as many as possible was the dominant concern — and it remains so today. In order to do this, NGOs involved in microfinance aim to make their programme financially self-sustaining, since a programme that pays for itself can obviously reach more people with less money.

Microfinance programmes have had considerable success in this regard, so much so that financial sustainability is now often a requirement for funding. Palli Karma-Sahayak Foundation (PKSF), for example, an organisation set up specifically to provide funds to microfinance programmes in partner organisations, expects to be repaid for the capital it provides within three years. USAID states in its most recent policy paper on micro-enterprise development that prospective partner organisations are required to have a "credible written commitment" to achieving "full financial sustainability" of their activities within seven years.

Unfortunately, the headlong pursuit of financial sustainability is one of the factors that has prevented microfinance programmes from reaching the hardcore poor. The hardcore poor are more likely to use a loan to protect themselves from the dire consequences of a flood, or to recover from the enormous expense of marrying off a daughter. They tend to need smaller loan amounts (which raises cost per loan) and require a more flexible repayment schedule (making cost-recovery more difficult). But most regular programmes lend to promote income ventures, allowing a less costly programme structure. This tendency was criticized by a recent BIDS study on reaching the hardcore poor.

Still, as the popularity of micro finance has spread, expectations for sustainability have grown so high that no trade-off between sustainability and reaching the hardcore poor is even perceived. The USAID policy, for example, praises institutions that are financially sustainable as the same ones that have achieved "deep outreach," meaning services are provided to the "very poor."

A recent paper by Jonathan Morduch, a Harvard University economist, criticises this "win-win" proposition of microfinance, that improving financial sustainability will always reinforce the positive social impacts of programmes. Belief in such a proposition prevents consideration of when subsidies to programmes would be appropriate, he argues and so social impacts become secondary to financial bottom-lines. "It is not profit maximisation that makes a programme efficient," he writes. "Instead, what matters is having a hard budget constraint, something possible even with subsidies."

The BIDS study mentioned earlier supports Morduch's conclusions, saying that where there is a conflict between financial sustainability and the needs of beneficiaries, "a proper balance needs to be struck ... between [the] two." Unawareness of any trade-off whatsoever makes it impossible to properly address the problem.

A New Strategy

Despite its inertia, there are signs that microfinance is beginning to reckon with the issue of the hardcore poor. Over the last year, the CDF, Grameen Trust, and NOVIB, the Dutch aid agency, have all hosted conferences which looked at reaching the hardcore poor. A number of already existing initiatives have been brought to light as examples to be studied, and experimental programmes have been undertaken by a number of NGOs in efforts to make their programmes more inclusive of the hardcore poor.

One question that has been raised is to what extent microfinance — at least in the form of loans — is an appropriate programme for the poorest at all. Debt on any terms may cause more problems than it solves for those with very little capacity to earn, especially in the absence of any other kind of support. Because of this, in the future microfinance is likely to play a more marginal role, or be used in combination whither types of programmes, when focusing on the hardcore poor.

"I don't think micro finance is completely the answer," says David Cracknell of DFID, the British aid agency. He points to programmes that increase jobs, which the hardcore poor often prefer to self-employment financed by micro loans because of the lower risk. The new 10 million US dollar Job Opportunities and Business Support (JOBS) programme, for example, implemented by Proshika with USAID assistance, seeks to create 250,000 jobs by supporting the development of labour-intensive micro, small and medium-sized enterprises.

BRAC's Micro-Enterprise Lending and Assistance (MELA) programme is another programme in the same vein. Loans in the MELA programme range from Tk 20,000 to Tk 200,000. Launched in 1996, as of October 1997, 457 MELA enterprises were reported to have employed 2,353 people. These examples show how microfinance can be applied in an indirect fashion to improve the conditions of the hardcore poor. Such programmes have been quick to catch on in the NGO community, since the bigger loans provide more revenue and fit well within trends emphasising financial sustainability.

Direct Benefit

"[Some people] need more than micro-credit, they need a little help," says Abed of BRAC, summing up the essence of BRAC's Income Generation for Vulnerable Groups Development (IGVGD) programme. Extra help comes in the form of a wheat ration provided to participants over the 18-month duration of the programme, run in partnership with the Government of Bangladesh and the World Food Programme. The IGVGD programme exemplifies how microfinance can benefit the poorest directly, given adequate extra support. Besides the wheat ration, participants are also provided skill training in chick rearing or sericulture along with their credit. After 18 months, destitute women that are the target of the programme are expected to graduate from extreme poverty.

Since 1988 when BRAC started the IGVGD programme in its present form, nearly 925,000 women have benefited from participation — no small feat. To its credit, BRAC has maintained the programme throughout a period when credit programmes in general (including BRAC's own Rural Development Programme, the RDP) have increasingly marginalised the hardcore poor. However, a World Food Programme evaluation noted that two-fifths of IGVGD graduates joined regular NGO groups while a quarter of those who simply received wheat rations and no loans in another VGD programme did the same. It is unclear from this information what benefit the microfinance component was; this should surely be addressed before such efforts are endorsed and emulated by others.

Another credit-with-support type of programme is currently being tested by the Grameen Bank. Begun in 1996 and called the Nishyo project, this experimental programme represents quite a departure from the Grameen "essentials". Like BRAC's IGVGD, it targets destitute women, but no groups are formed, loans are much smaller, and repayment terms are relaxed. Non-credit support is given in the form of skills training and marketing support for all participants. It remains to be seen whether such a scheme will prove successful enough to run along with mainstream programmes; so far only a few hundred people have participated.

The Next Step

It remains to be seen how much priority is accorded to new strategies to reach the poorest. That the hardcore poor are a distinct category is increasingly recognised. There are also signs of increasing recognition that subsidies are necessary in most circumstances to reach them.

But achieving sustainability is still the first priority for many institutions. Where this goal comes into conflict with reaching the poorest, a compromise in favour of reaching the poorest seems unlikely. Microfinance is increasingly seeking to make itself attractive to private investors, to tap into a potentially much bigger pool of funds for future expansion. As microfinance becomes increasingly integrated with the formal financial sector, it is hard to imagine sustainability (read: Profitability) concerns not taking precedence over who is served.

Meanwhile, it is easier to continue expanding for the majority poor than to make fundamental adjustments to programmes, Zakir Hossain, executive director of BURO-Tangail, reflects the view of many in micro finance. While well aware of the problem of the hardcore poor, he is up front that first priority is expansion of the programme until 2001, when he expects membership to have reached 100,000. After 2001, he says, they will look at concrete attempts to reach the hardcore poor.

Clearly there are many possibilities for microfinance to benefit the hardcore poor. And as with the regular programmes, the hope is that microfinance, in conduction with other programmes, can offer people a way out of extreme poverty. But first, a concerted effort to correct the order of priorities in microfinance is necessary: Speed of growth will come down and the cost of loans will go up. There is no way around it.

Credit Overflow?

If an estimated 30 million people (six million families) are directly or indirectly linked to microfinance, that leaves at least another 40 million poor who do not currently have access to microfinance, using the most recent figures for national poverty from the Bangladesh Bureau of Statistics. There seems plenty of room for further expansion. Right?

Wrong. The 40 million gross figure actually belies a more complicated picture at the village level, one which shows that a simple expansion of existing credit schemes along the same lines as the past could be ineffective, or worse, cause additional problems. The reason: too much of the same thing, too often in the same place.

A Bangladesh Institution of Development Studies (BIDS) report of findings from its Palli Karma Sahayak Foundation (PKSF-MES) study indicate that 11% of surveyed households are members of more than one NGO. In the majority of cases, the husband and wife belong to separate NGOs. "Overlap" of NGO memberships is an issue of emerging concern, since it may not only represent potentially wasted efforts duplicating programmes for the same household, but it could mean a severe problem for credit management. "Debt pyramiding", where one loan is used to pay off another, risks submerging households under a mountain of debt, even leading to the collapse of the local credit market if such behaviour becomes too widespread.

"This is now really emerging, we are concerned about this," says Salehuddin Ahmed, managing director of PKSF, which partners with and provides funding for NGOs for their microfinance programmes. He says there are two problems: multiple memberships in certain areas, and then other areas where there are no NGOs working at all. Ahmed is optimistic the problems can be solved through better cooperation, and he says PKSF has already been talking with Grameen Bank, BRAC, ASA and Proshika, as well as local organisations in this regard.

It is still too early to conclusively explain what the reasons are for multiple memberships.

One explanation offered by A. Mustaque Chowdhury, director of research for BRAC, is that members of small NGOs also join larger ones because the smaller NGOs cannot provide them with big enough loans. "The problem is between small and large NGOs, not large and large," he says.

If this is true, it may be exacerbated by BRAC's current policy. While BRAC believes community people should have a choice among NGOs and programmes and is generally supportive of small NGOs, there is a problem when BRAC begins work in an area that has for ten years been served by a small, local NGO. The smaller NGO sometimes is unable to retain its members, who flock to the big package of services BRAC is able to provide. Chowdhury acknowledges the dilemma: "The rationale is that by not going to a certain village, you are depriving the people there of what you have to offer," he says, not denying problems sometimes arise.

How Much Credit?

Zakir Hossain, Executive Director of the Credit Development Forum (CDF), asks whether we know microfinance is really getting "total coverage" by lending to only one member per family. But if more than one membership per family means better coverage, does that mean the BIDS finding is actually a sign of microfinance's success?

A study undertaken last year by ASA looked at reasons for default on loan payments by members, with conclusions that do not support such a speculation. Being unable to earn enough to repay the loan for various reasons (due to lean season, high credit amount, bad project selection, uncooperative family members, etc.) is one key factor. Multiple memberships in a single family is one of the many other reasons identified.

Imran Matin is a researcher who has studied peer group lending in four villages where the Grameen Bank has been active since 1980. Peer group lending is the most popular form of micro-credit, using the group as a replacement for collateral through joint liability for loans. Matin found during 1995 that repayment rates for Grameen members fell drastically, and that the number of inactive borrowers went up. His research shows that peer group lending does not restrain members from taking loans that are too large for them to handle, leading to break down of the group when repayment is not possible. Clearly seeing the problem is made harder because the loans are often rescheduled, or "rolled over" (another loan is issued to repay the first). When members had access to their group fund, to which is paid a portion of each loan, many used the funds simply to repay existing loans. "Unjustified enthusiasm for expansion will lead to trouble," says Martin. Triggered by massive default, the results could be very costly, he warns.

On the balance of this evidence, it seems that in many cases an unfocused expansion of micro-credit leads borrowers into stagnation, and possibly crushing debt and recourse to the moneylenders. Some can absorb more and higher loans, but not all. Yet it seems that NGOs with the means will disburse the larger loans whether they are needed or not, regardless of future consequences. And they will set up shop in towns where there is plenty of micro-credit coverage already. Matin complains that BRAC opened a branch in his study area, despite the presence there already of Grameen Bank, SSS, and BURO-Tangail.

So much for a coordinated approach.

Fall-out for Others

Binayak Sen, on economist with BIDS, notes that the typical assumption is that loans made to members do not hurt anyone else; that is, the gains of the member do not come at the expense of someone else. A significant portion of households are involved in land leasing, he says. With micro-credit, families who are not farm owners get into leasing land, and that displaces the traditional land leasers — often small farmers, who while not as poor as the typical NGO member, are themselves poor. "Land is limited... and credit becomes a powerful advantage," says Sen.

NGO programmes sometimes aim to give poor people access to resources which are unfairly controlled by others such as government "khas" land held by a rich elite using hired musclemen. In such situations, gains made at the expense of others may not be a bad thing. But in Sen's example, is it good if the poor gain at the expense of other poor?

Like a Weed ...

Since the Micro-Credit Summit in Washington last year, the effort is underway to find 21 billion US dollars so that 100 million poor families may be reached through microfinance worldwide. NGOs have set high growth targets for themselves. A review of any annual report is instructive: number of members and village covered, and amount of loans disbursed invariably feature prominently. PKSF added 22 new partner organisations to its roster last year. Even ASA is now in the business of lending funds to start up microfinance programme, and as everywhere, business is booming.

None of this should inhibit microfinance from proceeding with a more focused, coordinated strategy. The warning signs indicate that a mad rush to simply increase loans and membership lists will make a mess. It has become important not to extend too much credit in the wrong place. Different families will have differing abilities to absorb the loans. In some cases, the majority in a village may have reached their limit, leaving only very few to take still larger loans. And, as Sen has pointed out, even in cases where the ability to take on larger loans is present, it may have a net negative effect on poverty by displacing others in the community.

The momentum behind the generic micro-loan style programmes makes dealing with these issues difficult. PKSF and CDF, for instance, along with the World Bank and CGAP (donor consortium also acting through the World Bank), all preach "best practices", a sort of evolving recipe book for lending based on "proven" techniques in management and delivery. Sustainability of the lending scheme is paramount, along with a clean, professional management style. Arguably these principles can be applied to any type of microfinance programme, but the conservatism of the approach tends to emphasise following the rules of tried-and-tested methods, leading to endless copies of generic model.

Salehuddin Ahmed of PKSF says: "We are encouraging our POs [partner organisations] ... to be much more innovative. For example, increasing the loan size provided there's demand, in fact advising them to explore new means of income generation for the poor that are much more productive." Hopefully the PKSF will be true to its word, funding innovations in partners that will help microfinance overcome its current dilemma. It is unlikely it will be so enthusiastic about the need for more costly programmes required though, since it must insist on full cost recovery of its own lending to partners.

Reaching Further

So what does an NGO do to respond to these problems in a practical way? How to shape future growth?

To begin with, large institutions like BRAC and Grameen Bank have already engaged in the exchange of their membership lists in an effort to control the overlap problem. But, "in practice, at the field level, this doesn't really happen," says Matin of his experience in Tangail district. "It's too time consuming... and you can benefit from it without actually contributing," so there's little incentive to play along.

Part of the solution should be obvious: lend in areas that are not currently covered. NGOs like to operate close to regional centers to keep costs down, for ease of communication and travel. Costs will inevitably rise serving more remote areas. Otherwise, NGOs are playing a bit of wait-and-see, to find out how research will explain the reasons for multiple membership.

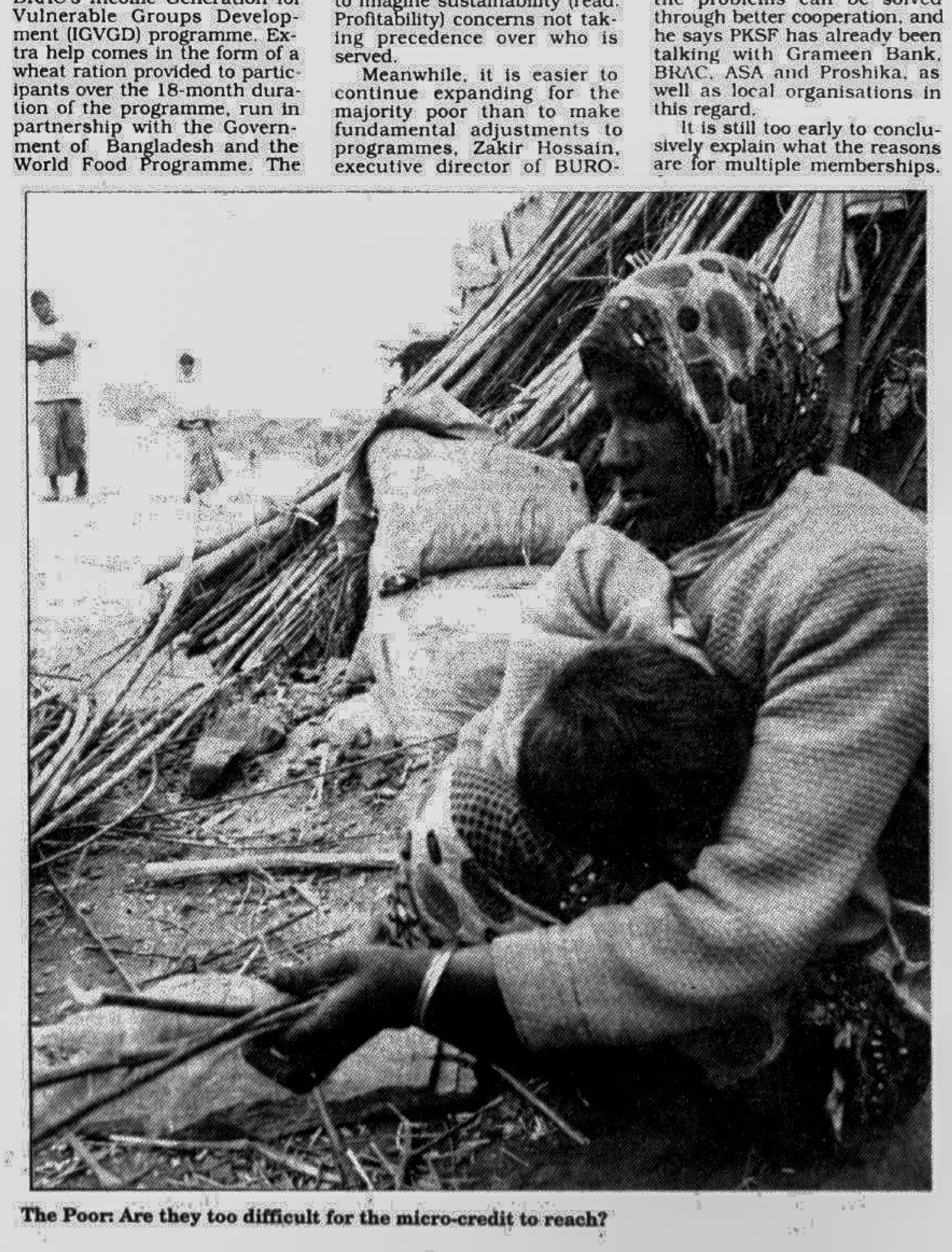
The other part of the solution lies in more precise targeting, using a more segmented approach. As is reflected in the newer aspects of microfinance programmes, there is room for expansion going up and down the income scale, lending to those above and below the usual micro-credit borrower. There are those who can take still larger loans, and there are those who are too poor to get access to the regular loan programmes.

Because of demand for the service, NGOs have, to some extent, already begun in these newer areas. Particularly at the higher end of lending, all the larger NGOs have developed programmes to build larger-scale micro-enterprises that offer more growth potential for the rural economy, and that can even create new wage jobs. For example, Proshika has been working with USAID and American partners on the JOBS programme since early this year (there is no lending involved as yet). The aim of the programme is specially job-creation, as opposed to self-employment, by developing micro, small and medium enterprises that will act as employers to other poor people.

Imran Matin talks about "new lending technologies" meaning that in order for NGOs to be successful in these new areas, they will have to develop different strategies of delivering credit. It cannot be based on a single, sustainable-in-three-years model. "Cross-subsidization by other programme areas can help reach the poor remote chars (islands)," Matin says. Lending must be cost-effective, but it will unavoidably be more expensive reaching some segments, such as the remote areas or the hardcore poor. NGOs seem to be in the process of acknowledging these issues, if the recent conferences on reaching the hardcore poor are any indication.

Growth in microfinance is no longer a simple question of outreach, signing up member to reach growth targets. It is time to be more selective. If all goes well, microfinance will show an increasing segmentation into different types of programmes for different target groups. If not, resources committee to microfinance will be needlessly wasted, and the benefits of programmes may even turn to enormous costs.

The author was recently in Bangladesh researching micro-credit.



The Poor: Are they too difficult for the micro-credit to reach?

Homing in on Savings

"If you're sure you can save 60 taka a week, you can take a loan," says Stuart Rutherford, a long-time micro finance practitioner based in Dhaka. "If you can't why get involved?" But, says Rutherford, just because you can't afford the loan installments doesn't mean you can't save. Any poor person can and will save given a convenient opportunity. And during from savings instead of borrowing fulfills the same need, whether it be for an emergency, some life-event, or an opportunity.

Rutherford, a long-time proponent of savings, runs a savings cooperative in Dhaka's slums called Safesave. It is largely due to the efforts of people like him that ASA and other smaller NGOs like BURO, Tangail now offer open-access savings, which means members may save as much or as little as they like, when they like, and withdraw from their account as much as desired at any time. This suits the unpredictable cashflow of the poorest much better thana fixed loan repayment schedule.

Savers also avoid typical problems for the hardcore poor in credit-based programmes: having to wait your turn for access to a loan, and being given a loan amount bigger than what is actually needed.

Microfinance services such as Safesave do not pretend to be attempts at transforming the situation of the hardcore poor, but they do provide a useful, needed service, and by concentrating exclusively on the financial aspect, they may even offer the possibility of running a sustainable programme, as Safesave has proved possible.

Growing Pains

In 1997, ASA, an up-and-coming microfinance provider, more than doubled its membership to over a million. The World Bank, in its fiscal year 1997, poured 105 million US dollars into microfinance programmes in Bangladesh.

"That may be the biggest sum given to micro-credit anywhere," says Pierre Landell-Mills, Country Director for the World Bank in Bangladesh.

At present, about a quarter of the national population is estimated to be connected to microfinance either directly or through a member of their family, roughly half of them joining programmes within the last five years.

By now, most people know about the explosion of microfinance programmes throughout the country. With its staggering growth, microfinance has come to dominate the poverty alleviation strategy of donors, the government and NGOs. Most of it is based on the same idea that made Grameen Bank world famous: providing small loans to poor women to invest in income generating projects.

Growing at such a furious pace, it's hard to stop and look around. But growth has brought with it its own problems, ones that at present may simply be hairline cracks visible in the foundation, but that threaten to become much larger, plunging microfinance into painful restructuring.

Now is the crucial time to ensure that symptoms visible in areas microfinance programmes have been active for more than ten years do not spread.