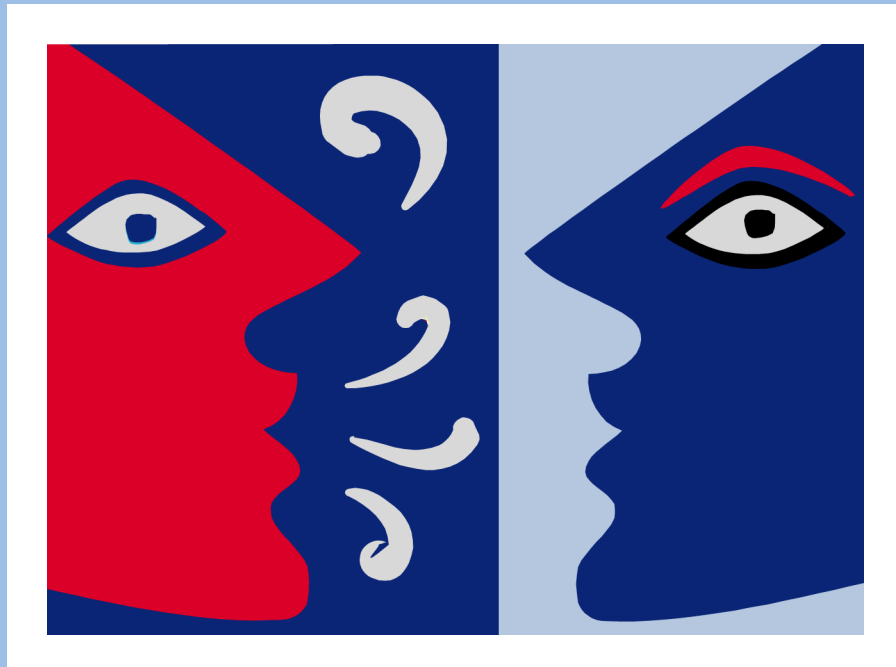




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Hype and Hope: The Worrisome State of the Microcredit Movement

AN ONLINE SPEAKER'S CORNER DISCUSSION LED BY THOMAS DICHTER AND
HOSTED BY MICROLINKS.ORG



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CONTENTS

Welcome	-2-
DAY ONE: Does Microfinance Contribute to Economic Development?	-2-
Summary	-9-
DAY TWO: Do Microfinance (microcredit) Services Target Clients Best Able to Contribute to Economic Growth?	-10-
Summary	-15-
DAY THREE: What if there were No MFI's to Provide Microcredit?	-17-
CONTRIBUTOR'S LIST	-19-
This page contains contact information for all microLINKS users who contributed to the speaker's corner discussion.	

WELCOME POST: Justin McFadden

Welcome to this three day Speaker's Corner event, "Hype and Hope: The Worrisome State of the Microcredit Movement"!

This discussion will focus on the article of the same title written by Thomas Dichter. To view this article please go to <http://www.microlinks.org/hype>.

The theme/question for today, DAY 1, will soon follow this posting and will be brought to you by our moderator for this event, Thomas Dichter.

Thomas Dichter's career in international development spans 40 years. He has lived and worked in over fifty developing countries. He was a U.S. Peace Corps Volunteer in Morocco in the early 1960s, and much later a Peace Corps Country Director in Yemen. He was vice president of an American NGO, a program officer at the Aga Khan Foundation in Geneva, a researcher on development issues for the Hudson Institute, and a consultant for many international agencies, including the UNDP, IFAD, USAID, the Asian Development Bank, and the World Bank. He has also done work for the Austrian and Philippine governments, Shorebank Corp. in Chicago, and the BASIX group in India.

Among his recent writings are his book: "Despite Good Intentions: Why Development Assistance to the Third World has Failed," published by the Univ. of Massachusetts Press in 2003, an Op Ed in the LA Times, Jan 30, 2005 called "What we need is Less but smarter Aid," a policy paper for the Cato Institute (Sept., 2005) entitled: "Time to Stop Fooling Ourselves About Foreign Aid," and the paper "Hype and Hope; the Worrisome State of the Microcredit Movement," published in Dec. 2005 in the journal "eAfrica." He holds a Ph.D. in anthropology from the University of Chicago.

Participants are welcome to speak their minds in a frank and open fashion. The next email will include today's discussion theme/question.

DAY ONE: Does Microfinance Contribute to Economic Development?

Post By: Tom Dichter

Hello to all participants, and especially to those of you who are practitioners in the field. We know you are all busy people.

Since I began working in microfinance 20 years ago I've grown increasingly concerned about how microfinance is presented to the world. Though there are good MFIs out there – serious, experienced, and highly professional, I think their work is becoming threatened by the growing hype around microfinance. And that hype centers on the question of what microfinance aimed at the poor can realistically be expected to accomplish. The majority of players, and especially the many new philanthropists and NGOs who are entering the field, present MF as a proven weapon against poverty. Last week the Michael and Susan Dell Foundation announced a major investment in a new Indian MFI called Ujjivan, and the press release added that the goal is to enable the projected 600,000 clients to be "free of poverty within five years." This is quite a claim.

In my view what ends poverty is a long and complex process called development. Too much of microfinance practice is aimed at short term bandaid solutions rather than long term development. I believe, therefore, that claims that microfinance can eliminate poverty are, to put it mildly, misleading. So my first question is:

Does microfinance (especially microcredit) contribute to economic development (defined as change that results in widespread wealth creation so that a large percentage of poor people have livelihoods (most of which will be in the form of jobs) that are sustainable over the long term, and thus become able to purchase goods and services (including health and education) which contribute to their security)? If so, how?

Post By: Herman Abels

I am wondering if the question is rightly formulated. You address practitioners in particular but, oddly perhaps, I know very few who would subscribe to the claim that microfinance has a direct link with poverty alleviation in the way you formulate that link. They are often cautious to claim results or impact beyond the lives of their clients.

The claims you refer to are mostly originating from the support industry: funding agencies and social investors in particular. Could it be that these claims have gone through the roof for reasons of rather a domestic nature, such as public profile, access to public and charitable funds back home and resulting inter-donor competition or rivalry?

Why not directly address those making these claims instead of asking practitioners if they would agree?

Post By: Monique Cohen

I am delighted you are promoting this discussion. It is sorely needed. I agree with you that there is little realism about what microcredit can and can not do. One observation over the years is that if you do a serious study and come out with less than expected 'hype' results your methodology is immediately criticized. Often anecdotes in the NY Times seem more important than serious numbers for justifying investment.

If we begin with the argument that microcredit is a necessary but not sufficient condition for development we can focus on a more realistic role of microcredit, consumption smoothing, a means to manage shocks, and to build assets. The attributable gains maybe small but are often significant for low income households. Access to lump sums of money is as valuable for the poor as it is for us, assuming that they have a use for it. As people think about impact of microcredit I suggest that they look at themselves and consider how it makes a difference to them.

Post By: Greg Pirie

The nub of the matter is the overly simplistic concepts used by the most vociferous promoters of MF as the poverty panacea -- "If we are looking for one single action which will enable the poor to overcome their poverty, I would go for credit." (Mohammed Yunus, Does the Capital System Have to Be the Handmaiden of the Rich?, the keynote speech to the 85th Rotary International Convention, June 1994)

Perhaps, as Herman suggests, this is a by-product of the need for those promoters to give MF supporters -- especially those providing substantial chunks of loan capital -- a straight-forward, easy-to-grasp, conceptual hook which they, in turn, can use to convince their sources of funding authorisation. Doing so as 'poverty fatigue' (or, more accurately, the dearth of pragmatic responses to the enduring causes of poverty) becomes ever stronger gives 'new hope' to those feeling increasingly desperate about the ineffectual history of development vis a vis poverty alleviation.

I agree with Herman that few on-the-ground MF people will make such claims. Yes, I am satisfied that a reasonable proportion of clients of competent MFIs are and will make a positive difference in the lives of themselves and their families, but to extrapolate that to the level of some of the more extreme rhetoric that's around is often going too far -- "Microcredit, and its connection to microenterprise, genuinely helps the poorest families in the world

emerge from poverty. And by extension, it has the potential to help create a more inclusive world economy." (R. Shapiro (CEO of Monsanto), opening the Corporate Microcredit Conference in June 1997.

To be fair, there are countervailing opinions -- "It is not clear if the extent to which microcredit has spread, or can potentially spread, can make a major dent in global poverty. In recent international meetings, it has been stated that a target to reach 100 million families by the year 2005 would require an additional annual outlay of about \$2.5 billion. This should be compared to the total GDP of all developing countries, which is now about \$6 trillion. A certain sense of proportion regarding microcredit would seem to be in order." (Observance of the International Year for the Eradication of Poverty (1996) and recommendations for the rest of the Decade, United Nations)

The key part of your question would seem to be the concept of "sustainable" -- an issue not limited to MF but that of development as a whole paradigm. Will 'development' have succeeded when the whole world looks like Madison, WI? What about the well-recognized inherent flaws of the consumption model upon which MF is based? As today's economically-active-poor/microentrepreneurs benefit from their MF participation by expanding their economic activity -- not only to their household's benefit but for those they subsequently employ as their enterprises experience the growth arising from the sale of goods and services to a market that in turn will be increasing its capacity to absorb an increasing volume of goods and services (a growth in capacity stimulated by the increasing wealth level of MF clients) -- will there be a concomitant increase in absolute volume of the consumption model we now 'enjoy'?

How will the infrastructural needs of vastly expanded economic activity and associated demands of households pursuing improved standards of living be met? How will electricity and other energy resources be produced and reticulated on the scale represented by the currently un- and underserved communities, as manually-powered process are replaced by machines? What impact on the chain of extraction and supply of resources that form the inputs for production will there be from an expanding number of microentrepreneurs wanting to take advantage of a growing market - for if they are to limit that expansion, to remain at the relatively low-impact level (a questionable characterisation!) of today's poor, will this counteract the poverty elimination process?

MF cannot escape - cannot be separated from - bigger questions concerning poverty (its causes, its relationship to other broad socioeconomic issues), which in turn cannot be separated from global concerns and trends. Poverty is too complex a social issue to be 'fixed' by the market-based intervention of MF alone.

Post By: Syed Hashemi

The question is suspect. No one asks if schooling ends poverty or immunization or housing or roads or new variety of seeds; most people know that just as poverty is multidimensional so too are potential strategies to end it. You need access to safe drinking water, and schooling, and infrastructure and political security etc etc etc AND access to financial services to create a pathway out of poverty. The reason that this question is asked in microfinance has more to do with ideological concerns rather than scientific queries. The intent is more to create a straw man argument and then demolish it. If one really wants to know whether mf has impact there are many ways to assess that; mf does assist in bringing about positive changes, but that depends also on a variety of other factors coming together. In other words mf has impact, not necessarily singularly, but as part of a more deliberate strategy involving other factors.

Post By: Arrigo della Gherardesca

I am an ex economist, investment banker and entrepreneur, now active in development finance.

In my view, Dichter says it all! Nearly.

His opinions are based on personal contacts with many poor who have been granted credit. These people - some of which I have met myself - bravely go as far as they can. But only a fraction of them have the additional know-how and "Spirit of Enterprise", necessary to create real growth, income and jobs.

Dichter's analysis of how economic development took place in rich countries is equally helpful.

Even in developed countries, only a fraction of the people have used credit for entrepreneurial, productive purposes. Most earn salaries and borrow (on their salaries) to purchase consumer durables (the house, car, etc.).

And - I add - in rich countries (where statistics are available), out of 5 new companies started, 4 fail within the first 5 years. That's one reason why most people are looking for a job, not trying to be entrepreneurs.

Put in another way, could we solve the big unemployment problem in Europe, by lending money to the unemployed? Not likely, is it?

But this is not so different from what MicroFinance is doing.

Why should the poor be better at setting up their own business, than the rest of us? They aren't. Most of them can only "copycat" someone else's activity, until there is no more incentive to do so.

Is this development? Aside for the fancy "business" and "success" imagery of MFI propaganda (probably mostly originating from the "support industry", as Mr. Abels says), it isn't.

This is not to say that MFIs don't have some positive impact on the life of the poor. They do.

But the success of credit for development should be measured not by how many people it reaches, but by how much Value Added and employment it generates, per 1,000 Dollars invested.

As Dichter says, "microfinance evangelism" makes it unlikely that those few true entrepreneurs, that need bigger loans to set up (and grow) Small-Medium Enterprises (able to create Value Added and jobs), might get the credit they need.

The old "production function" of the economists, based on capital and labour, is a misleading simplification; if we want to produce development, we have to introduce the other, fundamental, ingredients. For sake of simplicity, let's summarize them with "Sustainable Technology & Entrepreneurship" (ref. to Greg Pirie's posting).

As Syed Hashemi states, poverty is multidimensional and so too are potential strategies to end it. But if a cake is made up of five ingredients, to put in one today, one tomorrow, and forget the other three, doesn't seem particularly smart.

There are ways by which MFIs and the rest of the financial markets can help implement the complete, well functioning and sustainable "production function".

This might open a new, promising, frontier for development finance, truly helping people and countries escape from poverty.

So, Dichter says nearly all! But, in my opinion, it is whoever finds the practical solution to this "riddle", that will add the last, missing, word.

Post By: David Ellerman

I got four paragraphs into a comment and my electricity went off--as if I was in a developing country rather than Kalifornia! In the meantime, Dichter has replied and tried to raise the ante--so I will continue.

It seems to me that case that MF is not developmental is very strong. MF does not address (and it diverts resources away from addressing) the institutional and political problems that plague developing countries (--not to mention sporadic electricity supply). It provides short-term band-aids to people who are hurting, and, for many in the MF business, that is enough.

These arguments need to be placed in a broader context. Dichter does not argue against short-term humanitarian disaster relief. It will always have a role. The topic is international assistance to development, not disaster relief. Over the last half century when the "development business" has grown to its current enormous size, it has become rather clear to all who care to look that it has not been very successful (Bill Easterly's books are eloquent on this point). Where development has been successful (e.g., east Asia), it has been more a home-grown effort, and where the development assistance agencies have been thick upon the ground and had the most sway (e.g., sub-sahara Africa), it has been a rolling disaster.

One response to this is that more and more development organizations are quietly sliding into short-term poverty alleviation work—all the while touting it as being developmental. This is where the "micro-finance revolution" comes in. It is an almost perfect example of a poverty alleviation program—providing a form of "disaster relief" to the poorest of the poor in countries that seem stuck in a disaster mode—which is nonetheless justified to donors and the public as a developmental path. It is band-aids for people who need band-aids (and much more) provided by organizations who say they are providing cures. Dichter is calling for a little honesty in recognizing what MF really is and is not.

One honest response would be to say, "Yes, it is largely poverty alleviation but that is a good thing even without any development impact. Unfortunately, it cannot be sold to donors without presenting it as a path to development since they don't particularly want to part with their money for symptomatic relief. What's wrong with a few PR fantasies about micro-entrepreneurs taking off with growing businesses and providing a path to development?"

This honest response even has a more sophisticated form which emphasizes not only the failures of past developmental assistance but the negative consequences of much development aid. Hence, the argument continues, reorienting much aid to short-term poverty alleviation might not be such a bad idea regardless of how it has to be sold. Since we don't know how to fund genuine development assistance, what is so bad about reorienting donor funds to some heart-warming short-term relief to the poor?

Those are two examples of honest responses to Dichter's challenge, and trying to get the MF discussion to some level of honesty and realism is the limited goal of this discussion.

Post By: Sean Kline

Microfinance: over hyped relative to its demonstrated impact on poverty (so far)? Yes. Over hyped relative to its demonstrated outreach to massive numbers of very poor (so far)? Yes. An oversimplified means to address the complex dynamic of poverty? Yes. As Mark Twain said "for every complex problem, there's a simple solution and it's wrong".

But, who wouldn't hype and sell microfinance (or any other development intervention) like breakfast cereal or toothpaste if they thought they could make a 'business' of development in ways that were big and good for poor people?

And who wouldn't hype and sell microfinance if it seemed to represent a profound paradigm shift in development and potentially bucket loads of money from the capital markets, multinationals and the exorbitantly rich?

...Unless it led to bad phenomena:

(1) Public funds--taxpayer dollars--going to microfinance out of proportion to its impact on poverty relative to clean water and sanitation, healthcare, education, good government, etc.

(2) Private funds crowding out proven, high-impact microfinance for hyped ROI and simple approaches that scale well (good), but have questionable or little impact on those it claims to be helping (bad).

Regardless of ideology, the dynamism of the market nearly anywhere is a force that many of us in development want to shape to the developmental needs and market wants of poor people.

Khandker's study of Grameen Bank, BRAC and RD12 in Bangladesh found that each additional 100 Taka of credit to women increased total annual household expenditures by more than 20 Taka: 11.3 Taka in food expenditures and 9.2 Taka in nonfood expenditures. However, these impacts were the result of more than money. If this is some of what microfinance can yield, then we need more evidence of how to do microfinance in ways that achieve much higher impact than money achieves alone. And the 'support industry' needs to figure out what the frontiers are in this respect...and support them!

Post By: Herman Abels

It all is a bit more complicated than there being a hype out there. It may not be justified, but who really cares? The volume of response indicates that few do.

Microfinance is largely a defensive strategy, helping people to cope with the results of failed development efforts. From an economic growth perspective it may be little more than carrying water to the sea; you argued that convincingly years ago by qualifying it as a hedge. But that doesn't mean it is insignificant. As David explains it makes sense to invest donor resources in microfinance. It may not be perfect, doesn't perform miracles but it often works in that it helps people coping.

And it would be helpful if investors would present it as such, and it is a bit unfortunate that they don't. But there is little use in blaming Northern NGOs for taking lavish resources from the US or any European government to join the bandwagon: that is what they do. It represents a lifeline and good business on top of that, so why not take the money and do more of the same? After all, it helps.

Where it goes wrong is when microfinance is presented as a substitution or panacea for other crucial investments. A retired Mexican banker told me some time ago that Mexico had the perfect solution for dealing with its poverty and its poor. First, it sold the country's natural resources in the global market, inspired by popular Bretton Woods thinking, leading to a social breakdown but also to massive asset accumulation at the top of the pyramid. Resulting increase of poverty was then effectively dealt with by exporting the poor themselves. He claimed that although poverty had sharply increased over the last decade, the number of poor people is actually decreasing according to national statistics.

We could discuss all that in detail, but really, what has microfinance got to do with that? Let us then discuss globalization, WTO, protection of home markets in the West, increased global expenditure on arms, global warming, Kyoto, Iraq and what not. Practitioners have little time to get into all this as they are over-occupied with their difficult balancing acts to accommodate their investors' over-ambitious expectations such as achieving social impact, creating win-win scenarios, realizing double or even triple bottom lines, reaching the bottom half of the poorest and so on and so forth. Fortunately, perhaps, a wide variety of other NGOs take up those more developmental issues. Talk to them to get straight answers and be prepared to be grilled in the process.

Where it also goes wrong is where institutional interests, self-interests rather, become the major drive of the evangelical message. Has anybody in the West ever observed the virtual non-existence, for instance, of an African support industry in microfinance? And, if so, ever wondered why that is? Is there a particular reason why nearly all

technical assistance that is so generously provided to African microfinance at the end of the day arrives, or stays, in Western pockets? If you want honesty in the discussion, my advice is to track the flow of technical assistance.

Years back, when ACCION was sort of done in Latin America, its website ran a famous banner: "ACCION will bring microfinance to Africa", oddly ignoring the fact that it had been there for over a century and that nearly all African MFIs were firmly run by Africans. Probably just an over-the-top marketing slogan, but perhaps also indicative for a more common notion: in Africa it takes non-Africans or, more correctly, non-African institutions to make serious work of further growing the business. Such an approach would probably lead to rather instant expulsion from countries such as India, but for some strange reason one can still get away with such paternalism in Africa.

Where it also goes wrong is when microfinance is determined to be sub-standard when public capital is involved to smoothen interest rates for end-clients, particularly if such tough, 'market based' propositions are promoted by institutions that literally live off public capital investments and public subsidies themselves. Just observe: promoters of commercial approaches in the industry nearly invariably are subsidized themselves, one way or another.

Just three examples of how the essentially innocent hype can turn a bit sour or hypocritical. Buy you knew that already, I gather, so why not call a spade a spade and address hypocrisy when it manifests itself?

But then again, the hype does work in building a global constituency, as it were, for microfinance, as modest as its contribution to 'development' may be. I had been working in the industry for well over a decade without being able to really tell my family and kin, pretty straightforward rural folk from the East of Holland, what I was actually doing for a living. Then the Year of Microcredit arrived. And then our local Princess of Wales, so to speak, a very popular Argentinian NY banker, traveled to Kenya to visit some microfinance projects with all the Dutch papers and TV stations in her slipstream. After all that media exposure, my relatives responded by saying that they now completely understood what I did: small loans to good but poor people. Why didn't you say so in the first place and where can we put up some money for all that?

Anything wrong with that? I don't think so. Too much bad news, especially from Africa, has undercut the sense of international people-to-people solidarity and understanding for a long while. If the hype can help re-addressing that trend and generate a rejuvenated interest in day-to-day coping problems of common people in the South, all the better, I would say.

There is some merit in that which you may want to acknowledge.

Post By: Elissa McCarter

Yes, microfinance is not the end all be all solution to poverty. I think donors and "new comer investors" have to see through the hype. But if they don't, it doesn't seem all that late in the game to still channel hype in the right way. It's an opportunity, not a threat, to us.

We all stay in this game because there is evidence it works -- at least it's convincing to me on a personal level. Sure the empirical evidence is lacking, and certainly research could be improved if more time, effort and money were put behind it. But nearly every practitioner I know can name a personal example about how microfinance has made a radical difference in an individual client's life. It doesn't take much. A small sum makes a big difference when you are hovering at the poverty line. There is a place for the poverty approach to microfinance at least in its latest form -- access to a full range of financial tools that help households cope.

What I'd raise for discussion is the following:

We tend to assume that all world's poor wants to be a self-employed entrepreneur if they could just take out a microfinance loan. Most clients are not microentrepreneurs by choice and would take a nice factory job any old day. If we really want to use microfinance funds in a more strategic way, to create upward mobility and address economic growth, MFIs should be paying more attention to what they invest in.

Rather than perpetuating low-return businesses, we should invest more in the promising "upper micro" and SMEs that have a fighting chance to create jobs for our microentrepreneurs and employ their family members.

For this, the current focus on proving how we target the poor isn't so helpful. And certainly we should do a better job working in tandem with other services and interventions to help selectively advance business clients --the "missing middle" with most potential -- up the financial ladder. Access to finance is just one link in the chain.

DAY ONE SUMMARY: Tom Dichter

Well, after day one, with relatively little action (as Herman says, perhaps that suggests how little any one cares) we all seem to agree that there's a lot of hype around MF, but no one seems much bothered about that, since, a) we're all too busy doing our work; b) it's a small hypocrisy compared to the bigger ones in the development industry (and the world at large); and c) anyway MF does some good.

First let's be more clear about the somewhat soft impacts cited. Any debate about the value (relative or otherwise) of MF cannot do much but go around in circles unless we start to measure impact in serious ways. But we have avoided this for many reasons, including cost. (Though I suggest many MFIs really don't want to know). See Richard Meyer's paper for the ADB (Dec 2002) for an excellent summary of the impact measurement quandary. The studies we have, including the GB, BRAC and RD12 study Sean Kline cites, give mixed signals when compared to each other, and when we do see impacts they are small ones like an increase in household expenditures (again some of you are satisfied with just that, I am not). No, MF is evidently not totally insignificant but its results (to date) still don't warrant the claims and the kind of support from the press and the public and the insiders in the industry. Bangladesh after 30 years of MF (practically a state religion) is as a whole not much better off than it was before.

A key aspect of the impact debate is attribution. Yes we all have stories of individuals where a small sum made a big difference, but we cannot prove usually whether it was "our" small sum that made the difference, or whether, for example, some of the now \$120 to \$130 billion per year in remittance transfers from emigrant workers is the source. You have all heard it before, and no doubt you will come back and sigh at me, but money IS fungible.

And of course we need to look at the opportunity cost. If everyone is focusing on MF and so many donors (old and new - see Omidyar, Gates, the Dells, et al) jumping into it, there is a bit of zero sum here. Elissa McCarter echoes my paper perfectly by saying we need to invest more in the "upper micro" and the missing middle. And she adds that finance is but one link in the chain. In the 70 and 80s we used to do something called SED (Small enterprise development). It was fraught with problems and costly, but before we could even get very far with it, the field was drowned by the arrival of the "micro enterprise" and the accompanying microfinance. The old SED, interestingly did not involve much money for the clients - it was aimed at business training, equipment sourcing, matchmaking, and so on, what we called BAS (BUSINESS Advisory services). That is hardly done much these days - though new ventures like BASIX in India are taking this approach to the next, more sophisticated level, as is TechnoServe (full disclosure, for which I used to work).

As for microenterprises, again most of our institutions continue to convey the notion that the mF investment is in a tiny business (aka economic activity, aka income generating activity). But as Dr. Gherardesca says, (and I say in my paper) a tiny percentage of MF recipients are really entrepreneurs, and why should they be, not a one of us is. Again a little bit of hype that needs to be unhelped.

But again, who cares? Everyone will continue to play the game, since as Herman says, "where it goes wrong is where the institutional interests, self interests rather, become the major driver...." But this is what happens to virtually all the institutions we work for and with. (See my book *Despite Good Intentions* for the detail unpacking of the phenomenon.) It is great by the way that Herman's relatives now no longer bug him about what he does (thanks to the PR surrounding the Year of MC). But now that you've got them interested, perhaps you could take the time to enlighten them about the realities of what they think they have now "completely understood."

So on to the question of day two. .

Are the majority of microfinance (especially microcredit) services targeted to the clients best able to contribute to economic growth?

DAY TWO: Do Microfinance (microcredit) Services Target Clients Best Able to Contribute to Economic Growth?

Post By: Getaneh Gobezie

I am writing from northern Ethiopia, one of the poorest in the country, and working for a microfinance institution for nearly seven (7) years. I would like to share some of my experiences on some of the issues. In particular, I would like to re-emphasize that the very idea that just expanding "micro-credit" services in poor areas would solve the poverty problems and enhance growth is wrong in many respects.

Just making critical resources like credit available does not automatically make poor people 'business persons'. For the majority very poor people, with no or little skill and high risk aversion behaviour to start or expand business activities, enough persuasion has to go along with the credit service. In many microfinance programs, however, there is no in-built mechanism to provide such vital Business Development Services (BDS), or skill upgrading, market information, networking support, etc. Due to some cultural bias amongst the poor themselves towards some "non-traditional activities", the tendency is often to get on with such "traditional" activities as agriculture, trade, etc, which are somehow free from cultural taboos. Thus, non-traditional activities which could provide alternative employment opportunities (like blacksmithing, weaving, tannery, pottery, embroidery, other handicrafts, etc...) are rather frowned at, and not easily taken up by clients. In some areas,

Muslims do not take credit or save in banks or microfinance institutions because paying or receiving "interest" or earning money by the act of loaning is considered haram (in discord with the Islamic code).

Women also face a great time poverty because most domestic tasks such as grinding grain and food processing, water and fuel wood collection are highly arduous, labour-intensive and time-consuming, compounded by the fact that labour saving "appropriate" technology is largely unknown even by the standards of developing countries. An additional area of concern, in terms of the impact of loans of the poorest, concerns men's usurpation of loans targeted specifically to women. Survey indicates that only about 40% of the women who took credit from MFIs in the area use it themselves (in their own business) others either use it "in consultation with others" or totally hand it over to their male counterparts.

A related (and perhaps more problematic, but neglected) issue is also the low income perspective that prevail among most dwellers in many rural areas. Thus, after getting the additional "farm ox", that has been set as a target, or some level of income that provides for subsistence life (or the 'basic needs'), most clients would stop asking for more loan or only take a small amount. May be what economists would like to call the "Backward-bending Labour Supply Curve" is really at work in many poor areas?

In many cases, microfinance programmes face a key problem relating to sustainability of the services. Real financial intermediation (shifting purchasing power over time, as well as between net savers and net investors) cannot indefinitely rely on donor funding. The fact that money is being injected from outside (cold money) and not generated from within, or member contribution (warm money) provides little incentive to make full repayments by borrowers. Low repayment means that money cannot circulate for many years, thus shortening the “length of outreach”. Yet the poor need an on-going access to loan services to be out of poverty. Length of outreach also matters because society cares about the poor “both now and in the future”. Moreover where repayment is not expected, little effort would be made by borrowers to utilize scarce resources to projects with maximum economic/social benefit, resulting in serious capital misallocation.

There is also no guarantee that such money goes to the targeted people. Often, subsidized services induce excess demand from all types of applicants -- poor and non poor. Influence and patronage and better connections inevitably bias the distribution in favour of the better-off. Especially where targeting is relaxed, money can go to un-targeted people, who could have better chance of accessing resources from alternative sources. This creates market segmentation in the local economy (among same kind of people in terms of economic situation and risk profile) – some accessing subsidized funds, while others accessing it on market terms. The former can thus price their products lower than the latter, thus putting the latter at a disadvantage.

One can also list many other related and complex problems facing the microfinance industry particularly in very poor areas. I would like to hear your reactions.

Post By: Kiringai Kamau

Your posting is definitely of interest to majority of us that have an interest in microfinance particularly with a focus in Africa. The issue with microfinance is that there is a very huge appetite to learning about poverty rather than solving the problems of poverty. Donors seem to have a conspiracy to never create solutions to poverty, rather, they would rather watch and document what poverty is instead of supporting the poor get out of their problems.

The rationale for this statement is that when an initiative is spotted to be sustainable such as SED which Tom highlights, they are easily done away with, and in a haste, in favor of what is not sustainable.

Look at it this way: Capacity building means that you create independence among the poor from the well endowed. Any effort to create value addition and technology supported perspectives is not supported, with the argument that these will be far too removed from the poor, yet as it has been amplified here, not all poor people can be entrepreneurs.

If value addition initiatives are started to process the agricultural output that is never a taboo among any cultures, then the value addition entities would increase wealth through fair trade by the poor. Muslims would sell their output to the market at a margin that is not controlled at their level - and would indeed not be haram - and the investors in the value addition (who could be the poor from their sales) would earn a return on their investment.

There is nothing that seems to annoy as to hear -from donors - that a country like say Uganda has a very successful microfinance, and closely to their statement comes the Ugandan president saying that microfinance is not helping the country and the government would lend money for poverty alleviation through Savings and Credit Cooperatives. But donors will drum their success, their hype by hosting meetings to reflect on the success of Ugandan microfinance in South Africa. Why pray, would such a meeting not be in Uganda where the successes can be authenticated with testimonies from the country leaders and the poor microfinance beneficiaries? Does this not mean that the hype is only taking the beneficiaries of the microfinance funds (the advisors and donor representatives) to SA rather than create documentable successes that even a president can see as benefiting the poor for whom the funds were meant for?

Most microfinance reports, in my view, are a hype to hoodwink the suppliers of funds seated in their home countries rather than a reflection of the benefits to the poor. There is need to eliminate hypocrisy and support the pro-poor perspective that microfinance was intended to address. Unfortunately those that design microfinance do so with a very honest focus only to send individuals whose interests are to remain on a salary in a countries where they are held in awe! I am afraid there is too much human resource support accompanying pro-poor support initiatives. And for self perpetuation, there has to be the hype!

Here is what I would propose to help end this tyranny by the category I call poverty advisors and donor representatives.

Since most poor have plentiful supply of agricultural land - if we look at rural Africa - then microfinance should identify what the poor produce and help boost the production of the same through improved agricultural practices create value addition centres for the produce and ensure that the centres are manned by trained local people - most poor societies have one daughter or son who is trainable if none is trained already! create market linkages through fair trade to ensure the funds are channeled back to the poor create a savings and credit initiatives that is driven with resources earned from the market rather than from handouts from donor programmes. If donors have a need to pour in the cold money, they can put this in a Trust Fund or in an investment that is to generate resources and could then post technology support people rather than researchers who only churn out documents rather than value for the poor link the institutional infrastructure so developed to the national policy formulation institutions to ensure integration of the poverty support institutions to the national economic agenda.

My humble submission is that there is so much potential lost in the micro focus of microfinance funds that could easily be addressed if the micro output is aggregated for sustainable investment and enterprise creation focus that would be achieved if investment in value addition is made the focus of pro-poor initiatives.

Post By: Monique Cohen

You have certainly stimulated many of us to come out of the closet and get to the point. Am I looking at pent up frustration of experienced people who know what it is about but rarely have an audience.

One of the problems with the hype is that the promotions try to appeal to lots of different audiences. FINCA slogans are intended for private fund raisers; donor pronouncements are for their political patrons intended to ensure ongoing public budgets.

If only everything could be explained so simply. I keep being surprised that people state we have no idea what are the real impacts of microfinance, sorry microcredit/microdebt. We have evidence but the results either don't fit the academics standards of rigor, regardless of whether the results make sense for the industry, or they are about Bangladesh which does not apply elsewhere or they don't fulfill the donor's desire to be able to justify the hype. One other problem is that outsiders are often looking for the magic statistic that tells it all - income growth, education etc. Unfortunately it does not exist.

After all this time it seems to me that the power of microfinance, which is rarely articulated, is something we in the north take for granted and does not necessarily lend itself to quantification, choice to take advantage of opportunities. A steady income flow and a lump sum of money means that you can make a choice such as educate your child, build your house, take a risk if you are a microentrepreneur, or buy a TV so you can enjoy a little leisure. No one wants to discuss these issues but at the end of the day that is what we would want and that is the same thing poor people want.

Your day 2 question about the impact on economic growth is complex. The increments of change maybe small but the numbers are large. I feel we are primarily talking about credit. Lets not limit ourselves to just credit and think broader to include a larger array of financial services for the poor.

Viewed in this way does microfinance probably have the potential to have a much bigger impact on growth? I want to include here the issue of financial literacy. This industry is based on a premise that poor people know how to use the range of financial services offered to them. Our work shows that this is not the case. Maybe many of the poor would contribute better to growth if they were more effective users of financial services?

Post By: Sean Kline

I think Monique has captured the issue of promotion (hype) and impact well, the need to consider the possibilities and choices that small sums offer people of small means and the need, too, of equipping these people with the knowledge and skills to make good choices. Is an increase in household expenditure (a reflection of greater possibilities) really a small impact unworthy of attention, as you suggest?

I think we need to be clear that costly evaluation of MF is not something focused primarily on the information needs of MFI practitioners. Most MFIs probably don't care that much, or at least not more than they do about lower cost information that signals whether they are headed in the right direction so that they can improve practice. Evaluation is fundamentally about determining if MF is a worthy public good to invest in. I find impact research as onerous from a practitioner perspective as most others, but can't escape the logic of determining if public (or private) investment yields measurable benefits in one or more of the following areas (including your theme for today):

- * microenterprise development
- * financial systems development
- * financial sector deepening
- * innovation/investment promotion
- * consumption smoothing

..among others

P.S. I, too, have benefited from the popularization of microfinance, as some of my relatives now no longer believe that I work for the CIA. That's a relief!

Post By: Francois Rossier

I read with attention Thomas Dichter's article which reminded me my impact study on a Grameen Bank replication (PPPCR, Projet de Promotion du Petit Credit Rural) in East Burkina Faso in the mid nineties.

A positive impact of microfinance is that we move from giving to lending. Giving is ok for humanitarian issues (earth quakes) or to support political issues (human rights, freedom of speech, environment).

But disbursing a loan (or taking one) implies taking a risk which is more difficult to assess then giving a subsidy. And, paradoxically, it promotes autonomy (even thou the borrower has to repay the loan) because the borrower has to convince his banker to give him a loan and the banker has to be convinced by his borrower. While with a subsidy, you maintain a one way gift. As an African proverb says: "the hand which gives is always above the hand which takes". And how many donors of the North maintain their partners of the South dependant on subsidies in

order to control them or just to remain necessary? Consultants also copy/paste their previous reports and update the figures,...

Ok, it goes slowly but how much money West Germany had to pour into East Germany to fill the gap? The next challenge of microfinance will be to step ahead of the hype ("At the age of five she was selling fruits at the market, now her daughter goes to school" ACCION add) and address the needs of SMEs (because they create jobs) and rural areas (because a lot of people live there) with longer maturity, larger amount and lower interest rate :)

Microfinance provides the financial means for (some) people to change their situation and competition will push the MFIs to track the needs. Some MFIs will collapse and some borrowers will even commit suicide (like in India lately) but microfinance will play a key role in reshaping on a large scale the informal sector because it already lives by itself.

Post By: Herman Abels

Asking the question is answering it: no. The more interesting question is: should it? You obviously think so but the reasoning is one-dimensional. Economic growth is what is needed to beat poverty, so let's invest all resources available to that end.

As usual, money talks. If the bulk of the resources poured into MF would originate from stakeholders that are at liberty to apply opportunity cost considerations, you would have it your way. But that is not the case: a most important stakeholder in the industry is the saver. Together they put up a formidable share in overall capitalization and they would rightfully stick to the opinion that service delivery should work for them; not for the smart entrepreneur in their midst who could create jobs and make all contribute to economic growth. These stakeholders are primarily interested in growth of their own family assets and incomes; not somebody else's.

A second major shareholder is government. In some major MF markets governments play an active role in directing public capital to the sector mostly because of social concerns and sometimes out of election concerns. And as it is their capital, not ours, they can insist on reaching poor, non-entrepreneurial clients. Some Western governments work the same way, just see your Senate ruling on reaching the poorest.

Donor investments in MF are quite small, if not insignificant, on a global scale. Yet the donor community at large has positioned itself as the main stakeholder of the industry. It is quite vocal indeed, but it remains to be seen if it is really influential. Who is really listening? Those who depend, but there are less dependents than frequently suggested. Moreover, there is something like a buyer's market out there. BRAC, the largest non-governmental MFI, has conveniently ignored whatever wise lessons came out of the donor community for well over a decade and followed its own track. If they would have listened they wouldn't be where they are today.

And that track is not a bad one: 5 or 6 million people participate in the regular credit and savings programmes, substantial numbers will participate in its pro-poorest programme, at the same time credit programme graduates that show real entrepreneurial skill are serviced on a tailor-made basis in another programme and on top of it all there now is BRAC Bank that takes care of small and medium businesses and remittances (and sponsors the national cricket team, I believe). Just to show that it is not necessarily an either/or choice that needs to be made.

As regards your SED experiences, two observations. First, small and medium business development only works in a conducive environment, as you wrote years back. If the legal infrastructure is not in place, if the formal banking sector ignores SME clients, if competition is not fair, if the tax system is not fair, if formalisation of your business results in extortion, etc., that environment is not in place and entrepreneurial people have little options but to operate under the radar screen and keep their businesses small and informal.

Second, MF is not opposed to SME. German ProCredit Holding is concentrating on SME in Eastern Europe and Central Asia and increasingly in Latin America. They produce the impacts you would like to see: grow businesses, create jobs, contribute to economic growth. For ten years they have been bullied by donor agencies for not reaching the poorest but as they never took in donor money, they couldn't care less. They relied heavily on DFI investments and currently are shifting that sort of dependence to private sector capital, including savings from the general public. They have arrived where many can only dream of.

What I feel is missing in your reasoning is, first, a more comprehensive acknowledgement of the many faces of MF. You turn it into a caricature by only referring to pro-poor approaches and ignoring the rest that is going on. Second, you seem to suggest that 'all the money' that goes into MF would be better invested in SME development, ignoring the social values and concerns that drive many in the business. Moreover, there is a wealth of investment capital out there to support SME. Availability of capital is not the issue there (there is therefore no need to have microfinance investment capital carried over as you seem to suggest implicitly), but lack of abundant investment opportunity is.

My relatives, by the way, are nearly all entrepreneurs, as I am in a way. Traditionally they apply Chinese walls between investments and charity. Seems to me that they consider microfinance an area where both can be combined. Lower financial returns are compensated for by higher social returns. That is a positive result, or side-effect, of the hype. If I would tell them, as you suggest, that their social investments do not directly contribute to economic development, they would say: so what? That is not why we are in it in the first place. That, I think, is what is relevant for most stakeholders.

The point is not if microfinance contributes to economic growth. I don't think it was developed with that specific purpose in mind. So don't blame practitioners for not delivering what they never promised to deliver. Just blame those that are a bit over-hyped for not presenting a fair picture. That, to a large extent, is a domestic donor issue.

DAY TWO SUMMARY: Tom Dichter

We seem to be pretty much where we were after day one, with three former participants chiming in and two new ones.

What emerged more clearly this round is the defense of the social argument: we simply cannot ignore the poor. If we can make their lives better through financial services, then we should, plain and simply. And, many governments and donors are putting in their money for such reasons.

In addition, Herman brought up the following arguments - there are many more faces of MF than the ones I seem to have been referring to - those hyped aspects. SED and SME are not ignored by MF for example. Donor money is relatively small in MF and savings is a formidable share.

And Getaneh Gobezie from Ethiopia somewhat poignantly reminded us of the realities of MF in what Herman and I would call a non-conducive environment.- lack of sustainability, capture of loans by those other than the borrowers; low predilection and little opportunity to do real businesses, instead people using loans as a small hedge to survival concerns.

Several of the arguments that I make in my paper (and elsewhere) are being ignored here.

First the conducive environment issue is not just for SED and SME, or for MF ; it is for all aspects of development investment. In scores of countries the development industry (MF is a part of it) has made no difference whatsoever in improving poverty statistics despite 50 or 60 years of "investment" And yes, Herman, I am not really interested in helping the poor survive from one day to the next (I believe they will mostly do that anyway),

but in economic growth (which historically is the only way mass poverty has ever come down - check out the history of our own countries).

Instead in Malawi, Haiti, Guinea, Togo, Mauritania, and many other countries (unfortunately many are in Africa) one can make a strong evidential case for dependency. If we want to solve poverty over the long term (and not just respond to the “social concern” of “we must do something now!!!!) this issue of the counter-productivity of dependency must be dealt with. MF is part of that dynamic in those places, and I would argue Ethiopia too. James Shikwati a Kenyan economist has gone so far as to say to all of us - to simply pack up and go home. “leave us alone.” Is his cry. In this debate, see for example the face off between Sachs and Bill Easterly in the LA Times.

I also argue that we don't have historical evidence of a link between access to financial services and small business growth. In most advanced countries people financed their businesses at the beginning with informal resources (savings, borrowing from friends and family). We should not assume that financial services is a prerequisite to advancement at the stage of poverty we are talking about.

I question Herman's statement about the sources of MF capital being savings. If that were the case, I would pack up and keep my mouth shut. I could not possibly object to any thing that is funded by M.O.M (My own money) - that is, self-funded. I have no problem at all with a purely savings based set up and have seen many that take no money from anyone else (O.P.M = other people's money) . A credit union based on common bond and financed by savings initially, and then borrowing additional capital in the financial market is fine. Because they are self financed and operate within the market they can do what they like and that's fine, even if they screw up eventually.

But I do not think that it is so. In fact - of course we all need some hard statistics here - I believe the situation is going the other way - we have more and more donor money - more and more cold money. Again none of you has picked up my references to the new philanthropists - we are talking about HUGE never-before-seen amounts of money.

Indeed, as you all know, savings mobilization - especially among the MFIs which start out as NGOs ,is usually not talked about, in part because it is not legal for ngo mfis to take savings.

Again, I have no problem with MFIs that are banks, or with ops like German Pro Credit - indeed my admiration of Pro Credit is precisely because they do not listen to the political correctness of trying to reach the poorest. If all MF ops followed in that direction again I would have no argument to make.

So yes, Herman, I do not talk enough about the many other faces of MF, but I don't see anyone in this debate acknowledging the major face of MF that I am talking about - the thousands of MFIs who are out there (and their numbers are increasing) chasing donor money, operating poorly, remaining unsustainable, seeing chronic client drop-out , accomplishing little, etc. Nor the seriousness of the hype. I don't buy the idea (Monique) that it's somehow ok to have different messages to different audiences. MF is not about selling. Therefore we need one honest, sober message to all - the truth about what can be done and what cannot; about what kind of context makes an MF seed fertile and what kind of context does not; about what kinds of clients have potential to create jobs and what kind do not. When the message gets to be straight and honest (and more of you help to make it so), we will have advanced the field where we can focus on doing more things that make a difference. Until then, the hype is a threat to all of us.

The problem is too serious (and growing) to be dismissed as a “domestic donor issue.”

DAY THREE: What if there were No MFI's to Provide Microcredit?

Post By: Greg Pirie

Is it too predictable to say that it's now time for the revolution?

Tom, my apologies for skipping over your specific question, but it's the body of your comments that provoke me. You seem to be saying that once the curtain of hype is pulled aside, MF really doesn't have anything more to offer the chasers of the elimination of poverty than any of the multitude of other 'development' activities of the last 50 years. And, quite frankly, none of us who are participating in this conversation seem to be able to directly challenge your assertion -- perhaps because we agree, especially those who have effectively acknowledged that today's MF is nothing more than a coping mechanism?

So the issue is no longer MF per se, but what actually might do something of a permanent nature in eliminating mass poverty?

Does the economic growth argument suffer from the inherent nature of the economic model within which we're working to maldistribute the results of growth so that poverty remains?

I hate sounding like an aging Marxist, but I wonder if, despite the generally recognised intentions of this thing called 'development', it's inevitable that there will continue to be sufficient of a maldistribution to maintain a significant population of poverty-afflicted? 'Inevitable' as long as we have a social system centred around enduring exploitative relationships?

Or have I misunderstood you, and utopia is not your goal?

Post By: Arrigo della Gherardesca

Greg, it is not utopian to question things, including "the inherent nature of the economic model within which we're working", it is a sign of intelligence. But, being guests of the US Government, let's forget Karl Marx and remain "capitalists"!

I have already posted a message to this Forum, but it must have been too cryptic, because nobody picked up on it. In fact, I am an outsider, on MF...

I will try to make my point in another way (trying to be more clear this time).

In a globalized, competitive world, what kind of business can an illiterate woman, in a dusty village square, put up, with \$ 100? Honestly, what? A copycat potato stall? And a 100,000 of them? A 100,000 copycat potato stalls! Right!

You might say that if they hadn't the 100, they might earn even less... it is likely. (though, probably, they or someone else, would still be doing -- for less and without a stall -- the potato business..)

But now, what could happen if the same total amount, \$ 10 million, was granted to 1,000 clever entrepreneurs with viable, labor intensive, businesses, \$ 10,000 each...?

Actually, we don't know... it is not obvious by definition that the same amount of capital and the same amount of labor, but more brains and, probably, technology, would produce more income.. (though it's likely..) and that all the ladies would be employed..

But for sure, things would improve a lot, if we did BOTH things together (assuming:

- 1) as stated, that the entrepreneurs had viable businesses and
- 2) that they didn't compete with the ladies' potato businesses..).

So, if there is a lot of hype on MF, and a lot of money coming to it from donors and SRIs (not so much from local savings), let's use it!

But not for another 100,000 potato stalls!

In this scenario, wouldn't you think that the problem would become how to select clever entrepreneurs and help them set up viable, sustainable businesses, with low risk of insolvency? So that the MFIs could finance them?

As experts in the field, do you think this is done as much as it could be, or not?

If I understood right, Kiringai Kamou from Kenya was saying something similar....

In my limited experience, this isn't done that much. I think it can be done better and on a grander scale... I have seen money given on a "random" basis, to people who didn't know a clue... Let's all go into potato business!!!

As MF experts, which I am not, what problems (ideological, technical, - the size of the loans, \$ 10,000 in my example - , etc.) would you see for the MFIs opening (or expanding) this area of activity (again assuming that we were able to find viable entrepreneurs and businesses..)?

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