School of Financial Cooperation and Development - SFIDE
UnitelmaSapienza
Università degli Studi di Roma

MICROFINANCE IN THE AFRICAN CONTINENT

Donatella D'Agostini

The fundamental human rights for a more prosperous world

The Universal Declaration of Human Rights, a milestone document in the man's history adopted by the United Nations on December 1948, introduced for the first time the concept of "fundamental human rights" which are those rights inherent to all human well-being that principally include the right to life, and liberty, freedom from slavery and torture, freedom of opinion and expression and the right to work and education. It was established that everyone is entitled to these rights regardless of race, sex, nationality, ethnicity, language, religion, or any other status and that these new kinds of rights should have been universally protected from then on in order to foster a more prosperous world.

Since that date 72 years have passed and much has been undertaken in recent decades by the international community through the MDGs[1] and the SDGs[2], but unfortunately these fundamental rights continue to be ignored so that poverty and hunger persist in many countries of the world. Based on World Bank data still about 10% of world's population[3] (731 million people: about 400 million in Africa and about 200 million in South Asia) still lived on USD 1.90 a day in 2015.

Widespread studies showed that the foundation of a democratic system is the basis for the social, economic and cultural change and for the development of the living condition all over the world.

[1] The 8 "Millennium Development Goals" endorsed on 2000 by 189 countries of the UN to eradicate poverty and hunger and to develop a global partnership for development by 2015.
[2] The 17 "Sustainable Development Goals" (SDGs) set by the UN in 2015 in order to foster development in the world.
[3] In 1990 the percentage was around 36%.

sfide.unitelmasapienza.it
sfide@unitelmasapienza.it

KEY POINTS

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Microfinance: a tool to fight against poverty

Microfinance: The South Asian experience

Microfinance: The South African experience

The features of the financial sector in Africa

Which are the microfinance providers in Africa?

Which are the most common microfinance products in Africa?

Microfinance: a miraculous solution to stem poverty?

Donatella D'Agostini
Doctor in Political Science, Sapienza University of Rome, Master in International Cooperation Finance and Development UnitelmaSapienza, University of Rome. Conducted researches on the consequences of immigration and on racial discrimination in Great Britain, Germany and Sri Lanka and carried out an in-depth study on UN peace keeping operations in Rwanda. Currently working at Generali Italia SpA in the Antifinancial Crime Operational sector. Previous assignments: Cargo, Yachting and Art Exhibition Marine Underwriter and Claim Adjuster.

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They also showed that the international community must work on two different levels as follows:

1. a generic level to get more democracy, economic and social development, human rights awareness, women empowerment and freedom of all the people irrespective of race, education, tribe, religion and political status;

2. a specific level to get household sanitation, improvement of household incomes, new methods of farming, up-lifting of soil fertility and development of the social infrastructures.

By working in both directions it can stimulate the value chain tradeoff and the final defeat of poverty. While on the contrary the lack of social conscience in the society can encourage proliferation of moral hazard such as burglary, witchcraft, violence, low standard of development and poverty.

Microfinance: a tool to fight against poverty

For a long time, Western advanced countries of the western world, finding themselves in an advantageous position, considered appropriate to give charity to the developing countries which were and are still today poor countries. But all post-war economic development policies planned for the developing countries have not had the desired effect.

Over the past decades, various new tools have been developed to fight against poverty.

The most recently used tool is *microfinance* that provides to low-income people and to micro and small enterprises the following instruments:

- *microcredit*
- *microinsurance*
- *savings and money transfer products*

In the last decades microfinance managed to activate a virtuous circle capable of transporting poor people from the standard of the vicious circle *"low income, low savings, low investments"*, to the standard of *"low income, credit injection, investments, more income, more savings, more investments, more income"*:

- extending banking services to victims of financial exclusion financing their income-generating activities
- protecting against risks low-income people
- shrinking the exploitation by loan-sharks
- creating opportunities of self-employment for unemployed people in rural areas.

Microfinance: The South Asian experience

The birth of modern microfinance dates to the mid-70s when Professor Muhammad Yunus, started trying to lift his country, Bangladesh, out of poverty. In the village of Jobra he managed to focus on poor people's problem, when he met a woman in 1974 who, although carrying on a bamboo stool production business, was unable to get out of poverty because she could not access credit. The only way she had to carry on her business, was to borrow money from the local loan-sharks who, in exchange for the loan and for a few penny pay, net of the very high interest, forced her to resell them all the production at a bargain price. When Yunus realized that the debt of the woman was about USD 27, he granted her the small sum of money thus allowing the woman to continue running her business, to emancipate herself from loan-sharks and even repay the loan to Yunus.

Yunus kept on going on with this venture in the village with other families who were in similar conditions and in 1976 in collaboration with the University of Chittagong he transformed his microcredit program in a research project and asked a bank to open a special window for the poor to grant them loans. As the answer was negative since poor people could not give collaterals, Yunus decided to become the guarantor for the loans himself: the bank would provide a loan of money to Yunus and he would then distribute the money to the poor. The results he obtained were once again surprising: all the poor returned the loans in full and without delay.

In 1977, Bangladesh Krishi Bank opened a branch in Jobra to test the idea of lending to the poor. Again, the loans were always repaid. But despite the positive results of the experiments, the bankers still did not want to provide small loans to the poor. So that Yunus decided to ask the Government for permission to set up a special bank for the poor. In 1983 the Grameen Bank was founded.

According to statistics, 64% of clients who had dealings with the bank for five years or more managed to get out of poverty. Moreover, it was soon evident that women were more credible interlocutors for banks than men as not only credit repayment probability were very high, but they were also able to manage loans in a careful way, investing the sums obtained for the realization of profitable activities, for the home and for the education of children. This experience made it clear that poor people are not bankable, but reliable, and that to emancipate themselves from the state of poverty, they simply need to have access to official forms of credit and should not receive alms, but loans as loans can indeed leverage their dignity and their sense of responsibility pushing them to be solvent.

Even though Yunus experience managed to extend banking services to victims of financial exclusion, to shrink the exploitation of customers by loan-sharks, to create opportunities of self-employment for unemployed people in rural areas and to activate a virtuous circle, and even though the growth of microfinance industry was decisive to the social progress in South Asia in the past four decades, it was soon evident that microfinance can produce concrete positive effects only if it is effectively integrated with other economic and social programs aimed at satisfying the different needs of the poor.

The microfinance industry in India and Bangladesh is nowadays facing new challenges.

Microfinance: The South African experience

As far as Africa is concerned, in the last 50 years all the initiatives in favor of the fight against poverty have brought to the continent a thousand billion dollars, a remarkable amount which, however, has helped very little the development of the continent that continues to have a very slow economic growth and to possess a negative primacy in terms of wealth of its nations. Humanitarian aids therefore proved to be an inadequate tool to fight poverty. But in the recent decade, microfinance in Africa as in Asia turned out to be one of the most important instruments to tackle poverty, to contribute to food security and to improve social relations in the developing world helping the poor to find alternative sources of income, rebuild new income bases for the family after economic shocks, build new productive activities and reduce vulnerability to economic risks.

The features of the financial sector in Africa

The features of the financial sector in Africa, which influence the provision of microfinance, are:

- <u>small size of the microfinance sector and skills shortages</u> adversely affect low productivity and may prevent banks from exploiting economies of scale or making large investments in technology
- <u>inadequate depth and financial efficiency</u>
- <u>high exposure to economic and socio-political shocks</u>, including crop failures, sharp changes in prices of commodities, civil unrest, and unexpected changes in governments
- <u>high incidence of informality,</u> lack of documentation and of formal contracts excludes households and microentrepreneurs from credit;
- <u>regulatory deficiencies, weak governance system, risks of expropriation and heavy bureaucracy</u>.

Which are the microfinance providers in Africa?

The most common are the following:

- <u>Informal Providers</u>: such individuals and such as the “Tontines” in Cameroon, the “Susus” in Ghana or the “Banquiers Ambulants” in Benin working in rural areas and providing financial services on an artisanal basis. They charge very high interest rates on loans and operate without formal recognition. Due to their non-legal status, these microfinance providers have few opportunities to grow.

• Credit Unions: Credit Unions or Savings and Credit Cooperative Organizations (SACCOs) are cooperative financial institutions, based on the principle of a common bond, that provide savings and credit to their members.

• Banks: such as:

a) *"Savings Banks"*: introduced to Africa during the colonial days to assist poor people and small savers from North Africa to South Africa. It is estimated that Savings Banks had 40 million customers in Africa in 2010.

b) *"Development Banks"*: provide microfinance products mainly to NGO MFIs.

c) *"Rural Banks and Community Banks"* are very well established in Ghana, where they reach about 2.3 million clients, and in Tanzania, Sierra Leone and Nigeria.

d) *"Microfinance Banks"*, mostly widespread in Central and Southern Africa and in Nigeria.

e) *"National, Regional and International Commercial Banks"*.

• Deposit-taking MFIs: emerged as "Non-Bank Financial Institutions (NBFIs)".

• NGO MFIs: for humanitarian or social reasons.

• Community-managed Loan Funds: as "Village Savings and Loans Associations (VSLAs)".

• Consumer Lenders: that provide loans especially to salaried workers mainly in urban areas.

In Africa MFIs, present in over twenty countries, are concentrated in the sub-Saharan region, where only very low percentages of people (5%) have access to microfinance programs that correspond to 2% of the institutions of microfinance around the world. In some cases, the interest rates of MFIs are higher than those of commercial banks as it is more expensive to administer smaller loans. Moreover, the process of evaluating applications is particularly difficult as microfinance clients do not have regular salaries or collateral. So, despite the enormous development of MFIs in the last decades in the sub-Saharan region banks are still the kind of dominant institutions that provide financial services.

Which are the most common microfinance products in Africa?

There is a wide variety of products ranging from deposit services, loans of different types, money transfers, microinsurance and micro-leasing. The most common are:

• Saving Instruments: which are affordable

• Different credit facilities: offered by African MFIs to finance education, trade, agriculture, other household emergencies and housing finance.

• Local transfers and remittances: which are significant in terms of volume and in term of profitability. Some MFIs are developing new technology for money transfer, which is helping to reduce cost, to ensure security and successful outcome of transaction. For international transfers, some MFIs are partnering with international companies such as Western Union or MoneyGram.

• Microinsurance products: offered by ILO (International Labor Organization), UNCDF (United Nation Capital Development Fund) and other partners to help low-income people better manage risks and cope with crisis. But in North Africa microinsurance is mostly absent. The most common insurable risks are loans, life, burials, health (such as MicroCare in Uganda), property and crops (such as that offered by Opportunity International in Malawi to allow farmers to cope with the impact of drought).

Some research pointed out that for those who live in a developed country, a few hundred pounds loan may seem a small and useless amount. On the contrary loans of this size can make a huge difference to people running small businesses in developing countries where entrepreneurs can accomplish more with less money. It has indeed been proven that a loan given to an entrepreneur in Africa, or generally in a country of the developing world, can be worth almost 60 times what it would be worth in a developed country. For example, a loan of GBP 500 could be worth much more to a small business owner in Uganda than a loan of GBP 30,000 to a business in the UK. And subsequently a successful business in a developing country can affect the whole community much more than a successful business in a developed country. A loan in Africa can in fact help business owner to feed his family, access better healthcare, send his children to school and can also generate employment, bring new money and boost the local economy.

For people of the developing countries, who often don't have bank accounts, savings or investing and financial actions, it's very hard to apply for loans from traditional banks as they may often lack legal documents and may not have verifiable sources of income. Therefore, in most cases, credit bureaus and banks are unable to assess creditworthiness, and this makes banking services difficult to access despite this does not mean that these people are not creditworthy: indeed, it has been seen that many poor people have good business ideas, good entrepreneurial spirit and are capable of repaying loans if they are trusted. Conversely, in the developed countries credit bureaus can easily access information on about 80% of the population. This means that for most of the population it's quite easy to access credit and other essential banking services.

African countries are enjoying positive economic trends since the mid-1990s, during which higher economic growth has become widespread and vigorous over time. During the period 2000-2008, African real GDP rose by 4.9% per year on average, which represents twice its pace in the 1980s and 1990s. Even though the positive impetus in economic performance, the challenges of economic development in Africa remain enormous. Africa has in fact experienced a slow rate of decline in poverty in most African countries, so much that in 2013 it reached only 59% of the Millennium Development Goals. And moreover, the slowness with which Africa is trying to tackle poverty and to lift the masses towards the economic prosperity could create dangerous inequalities, eventually fuel instability and threaten economic progress.

The achievement of Africa's goal of improving the socio-economic conditions of its people is closely linked to the development of the private sector. It is in fact the African private sector that should lead to socio-economic development creating new jobs designed to alleviate poverty. But the private sector, still small today, is dominated by small businesses engaged in informal activities. The growth of these enterprises and the improvement of the socioeconomic conditions of the African poor people is hindered by their limited access to formal financial services. It is therefore clear that there is still much to be done. Microfinance presents in fact several risks that could limit its effectiveness in poverty reduction programs:

• politicians can attempt to use microfinance for their own ends

• microfinance can be misunderstood as a form of charity

• microfinance is somehow connected to other non-commercial governmental agendas with the risk of compromising the financial sustainability of the institutions.

Nevertheless, microfinance has significantly improved living conditions along with self-esteem and a sense of control, has proved to be very effective when joined with other social programs empowering individuals and micro-enterprises and enabling them to contribute to and benefit from economic development. It can therefore be effective for the development of the private sector, as it allows customers to seize economic opportunities and manage their vulnerabilities, while generating progress as well in the social and political sectors.

However, microfinance alone does not alleviate poverty and cannot lead to the achievement of the objectives set by the MDGs and SDGs. But in collaboration with governments, donors and key stakeholders and combined with other economic and social programs, it will be able to develop a series of strategies and activities aimed at reducing poverty, increasing education rates, quality of health care, housing, transport, agriculture.

Therefore, it can indeed help meet the diverse needs of the poor and enhance their economic capital (savings and assets) and their social capital (education and medical assistance). It has also been widely demonstrated that microfinance is more effective than other poverty reduction interventions such as targeted food interventions.

In developing countries, where poor families are often afflicted by fluctuations in income and by the need for emergency resources and where family-run micro-enterprises, in times of lean or in time of emergency, are often vulnerable as they have no money to draw on to cope with household consumption, access to financial services plays a fundamental role in keeping the income flows of the poor stable, enabling them not to reduce their working capital and consequently reducing their vulnerability to financial shocks. Microfinance in this way not only supports the creation of new work activities, but can also improve risk management, allow business development and improve money management, thereby promoting the protection of existing companies and thus relieving them from risk of bankruptcy.

It can therefore be said that access to financial services provides the poor with the opportunity to make their own choices in a self-determined way and therefore to get out of poverty.

Small loans meet the needs of poor micro-entrepreneurs, many of whom are often looking for working capital more to expand an existing sustenance business than to create a new one. Many of these micro-enterprises, managed by women of low-income households, constitute an additional source of family income, are seasonal and part-time.

Furthermore, the limited size of the initial loan and the repayment in small frequent installments help to make the repayment of the loan easier.

Microfinance also empowers women by reducing their marginalization in the socioeconomic system. Women's empowerment not only contributes to increase women's income, but also increases their education rates, their physical mobility, their access to information and participation in the activities of the microenterprise program, their economic security, their ability to make various purchases on their own, their freedom from domination and violence within the family, and gives them political and legal awareness by allowing them to participate in life and public protests and political campaigns. Microfinance, promoting women's empowerment, also contributes to reduce the fertility rate and to improve the living conditions of families, generating an additional source of income used to supply food and send children to school.

In addition to the mentioned economic benefits, microfinance can also contribute to the involvement of the poor in economic development by increasing their political awareness, social organization and participation in social life. Therefore, microfinance leads not only to economic benefits, but also to social benefits and to emancipation thus triggering a virtuous circle.

Microfinance: a miraculous solution to stem poverty?

In conclusion it can be said that the economic progress of a developing country is nowadays strongly linked to microfinance which is not only a tool that can free out of poverty large population groups and that can foster development from below, but it also serves to advance democracy, human rights and lasting peace. The right to the access to microfinance programs is therefore a fundamental right that allows every man to get out of isolation by developing his potential and by giving him back the freedom and dignity to decide about his life. The absence of such a right in a country is one of the main causes of underdevelopment of a population that, deprived of this resource, cannot increase its production, its income and its capacity to emancipate from poverty. In developing countries poor, or extremely poor people, who make up the majority of the population, are busy every day in the fight against survival and therefore even if they do not hate each other they are not dominated by feelings of mutual tolerance and respect and therefore cannot be the best supporters of social development.

For this reason, these countries must be helped through different appropriate instruments, one of which is precisely microfinance. But it must be highlighted that microfinance does not reach the most vulnerable members of a population, such as the elderly, the sick and the disabled, therefore it leads to a form of discrimination by the richest poor against the poorest poor. The poorest poor, scarcely succeeding to meet basic needs, cannot manage an entire company as they do not have enough education, enough management skills and enough knowledge of the social networks strictly required to participate in microfinance programs. It must be also highlighted that not all poor people are dynamic and ambitious businessmen/businesswomen who are just waiting for the chance to emerge if they only have access to credit. In fact, the poorest people, poorly educated and marginalized by society, hardly have the entrepreneurial drive necessary to start a business. It is also worth noting that while credit alone tends to be more relevant for medium-sized businesses operating in poverty (especially non-manufacturing livelihood firms such as trade and agro-processing), it is less relevant for the poorest of the poor for whom skills training, social and technological preparation and availability of inputs may be more important than credit alone.

Concluding, to achieve the important goal of tackling poverty, microfinance programs cannot be the same everywhere, but must be rather adapted to the local needs of each country and must necessarily be accompanied by other economic and social programs such as primary health care, environmental sanitation, education, nutrition, family planning, childcare and land reform programs. This means that microfinance may not be a miraculous solution, a joker capable of bringing magical solutions, but certainly it can be an effective tool which, combined with other effective policies, can certainly make its valuable contribution to stem poverty.

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UnitelmaSapienza
Università degli Studi di Roma

High School of Financial Cooperation and Development
- SFIDE -
UnitelmaSapienza, Università di Roma

sfide.unitelmasapienza.it
sfide@unitelmasapienza.it