The All-Party Parliamentary Group on Microfinance

Draft Summary of evidence submitted to APPG on Microfinance parliamentary inquiry 2011

Evidence and Evaluation

The submissions agreed that the evidence base in microfinance was problematic however there was some disagreement about how this should be dealt with.

- It was agreed by a majority that consistent monitoring of outcomes by Microfinance Institutions (MFIs) is important and should be encouraged. Long term studies are notoriously complicated and therefore long term data sources from MFIs would be an important resource for microfinance evaluation.
- A number of submissions suggested the need to add more nuance to studies. Most studies, particularly large scale studies, which are used to provide evidence for the efficacy of microfinance , do not differentiate between types of microfinance and this means that there is little evidentiary base for assertions about how best to employ microfinance funding, or what factors make microfinance effective at fighting poverty.

Microcredit:

The responses to the inquiry were most vocal on the issues of microcredit and were generally representative of the wider debates in the industry. We had a good mix of those that advocate the need for commercial microfinance and those who criticise it as predatory and poverty creating. Interestingly, while the submissions emphasise different aspects of microfinance- and different purposes- there are some clear indications of how microfinance could progress in the wake of the recent negative media coverage of some microfinancing organisations.

There are three major lines of debate to be found in the submissions:

- **Advocating Commercial microcredit:**
  - Commercial microfinance is inexpensive so its capacity for outreach is greater than for not-for-profits (NFPs) which are reliant on capricious donor funding.
  - It helps to build permanent solutions to financial inclusion.
- **Advocating Not-for-Profit microcredit**:
  - Commercial microfinance does extend services but does not always lend appropriately and their services can be too minimalistic to be of use to some clients (particularly the rural/ very poor)
  - When there is no drive to maximise profits efforts can be expended on maximising outcomes/creating enabling environments/procuring markets/targeting and evaluating potential clients.
- **Criticism of all microfinance forms:** There were some submissions that argued against microfinance more generally, arguing:
  - The industry is overselling the case for microfinance, focusing too much on the individualistic ‘micro’ level and getting people into debt.

- Since there are risks inherent in this intervention (possibility of people falling into debt) development funds would be better employed in alternative development interventions.
- That encouraging the financing of unviable businesses to the neglect of other forms of financial services, like small and medium enterprise (SME) financing, is damaging. The argument is that businesses have little chance of scaling up and providing jobs for those individuals who might be less inclined towards entrepreneurialism.

While it seems difficult to reconcile these issues there are some things that can be drawn out of these three competing ideas.

- Financial inclusion is important and those who have the ability to responsibly take out a loan and can reasonably expect to pay it back should have access to credit.
- Commercial microfinance is more capable of outreach and so has a place but there need to be regulations in place to ensure that commercial MFIs lend responsibly. It is also important that commercial microfinance is not viewed as a development intervention.
- There is a role for not-for profit (NFP) microfinance but this too needs to lend responsibly and cannot reasonably expect to be reducing poverty simply by providing capital – businesses have to be viable and not for profit organisations should be concerned with providing services which will improve the environment in which that loan operates. E.g. financial education/skills training, market procurement services.
- There is scope for a system of certification, whereby the services that NFP microfinancing organisations offer are ranked according to services or impacts. This would allow donors to make informed decisions about where to invest.
- The submissions were quite united in their belief that microfinance must be situated in an environment that is conducive to flourishing businesses. Legal frameworks e.g. contract law are important along with market procurement, SME financing and financial education.

Microsavings:

'Microsavings' was a more marginal issue in the submissions which generally focused on microcredit. That said, those who did mention savings were at a consensus over its importance and the need for the sector to build microsavings capacity. Unlike credit which requires careful monitoring of who is and is not a suitable client, and for which outcomes can vary, the inquiry submissions noted that microsavings are suitable for everyone.

Microsavings can:

- Reduce vulnerability to economic shocks (e.g. bad harvests, health problems etc.)
- Allow for investment which can possibly lead to increased poverty reduction.
- Provide for education of children

Current problems with Microsavings include:

- Relatively few organisations offer them, sometimes because they are barred from taking deposits (because they are not licensed banks) but also because taking savings is not particularly profitable for the organisation. Even fewer organisations offer savings that are not linked to credit (to provide collateral).
- For the rural poor access to banks is difficult and often (due to travel costs) expensive.
- Where savings products are available there is relatively little product variation meaning that demand for certain products is going unanswered.

Possible solutions:

- Savings need to be rolled out with urgency and should be offered to all people, regardless of whether they desire credit. This means capacity building in savings is important. Microfinance Organisations should either: (a) become licensed to accept deposits or (b) set up partnerships with banks so that they can facilitate savings.
- Technological innovation is required and particularly an increased focus on mobile banking.
- Innovation in savings products is needed so that the needs of clients can be met e.g. delayed access (illiquidity) savings accounts/ deposit collection services.