Partners for Development's Approach to Microfinance

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Introduction

Partners for Development (PfD) launched its first microfinance activities in Nigeria in 2001, and today integrates microfinance, and especially microcredit, into its development program portfolios in Africa and Asia. PfD delivers appropriately-scaled microfinance interventions because we know carefully designed, thoughtful programming giving people access to financial services can be an effective means of reducing poverty, and because integrating microfinance into its health, nutrition and agriculture activities *increases the effectiveness of all PfD's work*.

This paper describes PfD's general approach to microfinance–*why* and *how* PfD provides services, *where* and with *whom* PfD works–and presents evidence of the *outcomes* of its efforts to bring financial services to people who traditionally do not have access to the formal banking sector. Appended to the paper are several tools that PfD staff and partners can use when implementing microfinance activities in the field.

By the numbers: PfD Microfinance Portfolio 2001-2016	
Countries	6
Microfinance Partners	23
Borrowers	102,435
Total value of loans	$11,059,183

Why PfD Supports Microcredit

In launching microfinance activities in 2001, PfD joined a movement to bring professional financial products to the world's poor. The formal banking sector tends to ignore people who have few assets, seeing them as, at best, an unprofitable client base and at worst a risky investment. Moneylenders, by contrast, do deal with the poor and can meet clients' short-term emergency needs. But their high interest rates, which can approach or exceed 100 percent per annum, do not allow borrowers to build wealth and may plunge them further into poverty.

While PfD has experience in providing an array of microfinance services including savings and insurance products, its microfinance services focus on *microcredit:* the provision of small loans that poor borrowers can use to launch or expand small enterprise, agricultural production, processing or trade. Microcredit can help stabilize household economies by diversifying income sources and smoothing the seasonal variations experienced especially by small-scale farmers.

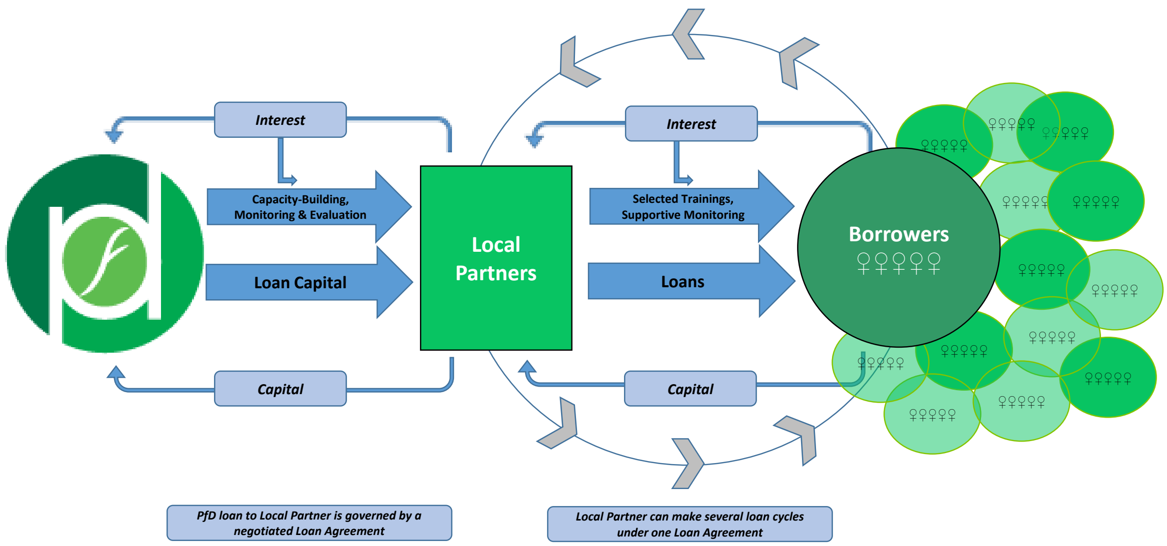
A number of PfD's projects center on the sustainable provision of microcredit to poor borrowers, but PfD also integrates microfinance into its projects in health, nutrition, renewable energy and more. This integration improves the performance of all PfD interventions, and increases the overall physical, economic and social wellbeing of participating households.

How PfD Supports Microcredit

In each country where it works, PfD works with and through partner organizations to deliver microcredit to clients. PfD channels capital (and capacity-building support as necessary) to these partners, which then on-lend and provide additional services to clients. This system has several distinct advantages:

1. It offers economies of scale. PfD's local partners have extensive, in-country networks, so PfD can reach far more households than if it provided direct service delivery.
2. It is contextually appropriate. PfD's partners have solid knowledge of the operating environment.
3. It is sustainable. With the capacity development that PfD provides, local partners can continue to provide services long after the end of PfD's formal involvement.

While the specifics of how PfD supports microcredit do vary according to the operating context of each country where it works, a generic picture of its microcredit approach is useful. The diagram below provides such a picture, and is followed by a description of how capital and support flow from PfD to local partners to clients, and how interest, capital and selected information move back to PfD.



Partner selection and support: In each country where PfD operates, it has carefully vetted and selected local partners, most of which are microfinance institutions but which also include local nonprofits or community-based groups with a specific interest in small-scale, economic development. In a few cases, the partners are international organizations with a strong, local presence.

PfD uses several templates[1] when conducting due diligence or vetting of its local partners. These tools capture an organization's level of development, and guide PfD as it designs capacity building, mentoring and supportive supervision of each local partner during the loan period. PfD covers most or all costs of this support with the interest that local partners pay on loan capital.

Loan capital and terms: PfD develops a formal Loan Agreement[2] with each local partner for each loan, and transfers the capital—which PfD obtains from donor grants, donor soft loans, or its own unrestricted funds—to them for on-lending to clients. Most of PfD's Loan Agreements are for 24 months, though some are as short as 12 months and others as long as 60 months.

Local partners pay interest to PfD, usually quarterly, from the start of the loan and at the rate specified in the Loan Agreement, which also stipulates the terms of repayment of principal. Repayment terms vary, largely due to local partner preferences: some partners prefer to make a single payment at the end of the loan period, while others stagger principal repayment over a maximum of three months at the end of the loan period. Once the principal is repaid, PfD and the local partner determine if a follow-on loan and new Loan Agreement are in order.

On-lending to borrowers: Meanwhile the loan period between PfD's local partners and actual borrowers is shorter: typically, from three to six months for loans made for petty trading, and from six to 12 months for loans made for agricultural production or processing. PfD's local partners can thus make several rounds of loans with the same loan capital from PfD.

The interest rate that local partners charge borrowers varies by country, but is always consistent with the local microfinance average, typically between two and three percent per month. Microfinance institutions

[1] See Appendix V, Appendix VII, and Appendix X
[2] See Appendix IX (for copy of general Loan Agreement)

worldwide charge, on average, about three percent per month, or between 30 and 40 percent if annualized. Although higher than the rates charged by commercial banks (typically 18 to 25 percent annualized) to which the poor have little access, the microfinance institution rate is still acceptable: data show that most borrowers can repay their loan plus interest and still grow their micro-enterprises. Of course, the microfinance rate is significantly lower than the annualized 100 percent or more charged by moneylenders.

With PfD's assistance, local partners identify and vet potential borrowers. Looking across all PfD projects that include microfinance, a picture of the typical borrower emerges: a woman living in a rural or peri-urban area, who is engaged in smallholder agriculture and/or petty trading, and who heads or co-heads a household (average size of six members).

The typical loan size is between $100 and $200.[3] As noted, borrowers use funds to increase their livelihood security by starting or expanding small businesses, and/or increasing their production, processing or trade of crops or livestock.

When identifying borrowers, and making loans, local partners often cluster borrowers into groups of about five people based on their existing affiliations or affinity. This makes monitoring and collections more efficient—typically during monthly meetings--and encourages mutual accountability among borrowers to repay their loans as agreed.

Building borrowers' skills and knowledge: Local partners' regular meetings with clusters of borrower groups are not only an occasion to collect interest and repayments. They are also an opportunity for PfD to provide education or capacity-building on topics that range from business and financial skills training[4], to health and family planning education and service referrals. These skills-building interventions are the key integration point between PfD's microfinance programming and its work towards improvements in other development sectors including agriculture, nutrition and health. In other words, PfD deploys microcredit and related trainings to leverage gains in other sectors that are essential to the wellbeing of borrowers and their families. The integration of microfinance, and its leverage for broader gains, is the topic of the next section.

How PfD Integrates Microfinance for Better Results in All Programming

The brief examples below illustrate how PfD blends microfinance activities with interventions in other development sectors to leverage better results for participants.

- PfD and local partners in Nigeria use the *Nigeria Agricultural Enterprise Curriculum*[5] to deliver business and financial skills training to borrowers in the agricultural sector. The experiential learning curriculum leads learners through important concepts and skills including planning, income projection, risk assessment, monitoring production costs, debt management, savings and profit maximization. It also helps them improve financial management (including cash flow), record-keeping and market analysis.

- Also in Nigeria, PfD weaves health messaging into routine meetings between borrowers and local partners. The latter are trained to provide basic health education and referrals to services as needed. In a health project in Nigeria that aimed to boost exclusive breastfeeding of infants, PfD reinforced meeting-based information by sending voice and text messages to borrowers' mobile phones, and by

[3] PfD's now-closed credit program in Bosnia-Herzegovina made substantially larger loans. Individual credits of between $500 and $2,500 reflected the nature of the local economy, and that many loans were made for housing.
[4] See Appendix IV (for manual on training)
[5] Jointly developed by PfD and Chemonics, GTZ, Nigeria Ministry of Agriculture and Making Cents International. PfD and partners developed and use a similar curriculum, called *Micro Enterprise Fundamentals* with borrowers who are not involved in non-agricultural businesses.

performing dramas and role plays. The project measured increased uptake (up to 20 percent) of exclusive breastfeeding attributable to the reinforcement messages[6].

- Microfinance is a basic component of PfD Benin's integrated model of agricultural enterprise development: PfD Benin uses microfinance loans to expand smallholder farmers' market oriented businesses. In the Growing Resources for Enhanced Agricultural Enterprises and Nutrition (GREEN) project, vegetable farmers learn what quality and varieties local markets demand and are trained to grow crops to meet the demand. Microfinance provides the agricultural inputs to support the crops. The small loans enable business growth cycles, with smallholders increasing production and sales over 150%. GREEN farmers have built positive credit ratings as the loans are repaid; paving the way for another growth cycle.

    - Credit is key to increasing business in PINEX: In the Pineapple Processing for Export (PINEX) project, PfD Benin will use its integrated model to significantly increase export sales of Benin's pineapple products. Trained pineapple farmers will use microfinance loans for inputs needed to increase fruit production and quality; processing companies will use credit to procure equipment needed to meet the growing demand for Benin's pineapple products in local, regional and international markets.

- In Cambodia, PfD implemented a pilot project by providing small loans ($100) to 12 Village Health Volunteers (VHV) in malaria high epidemic areas of Kratie Province. With the loan and support, PfD in turn conditioned and encouraged the VHVs to engage more education activities on malaria. PfD also worked closely with the local MFI (Kredit) to provide malaria education in Kratie province to Kredit's clients during the Kredit-Client loan management meetings.

Key Results of PfD's Microcredit Programming

Since launching microcredit activities in 2001, PfD has tailored its delivery model to the economic contexts and needs of six very different countries. The table below summarizes the scope of PfD's microcredit activities date, and the adaptability of its model to meet the exigencies of specific operating contexts.

[6] Flax V.L., Negerie M., Ibrahim A.U., Leatherman S., Daza E.J. & Bentley M.E. (2014) Integrating group counselling, cell phone messaging, and participant-generated songs and dramas into a microcredit program increases Nigerian women's adherence to international breastfeeding recommendations. *The Journal of Nutrition* 144, 1120-1124