

Financial Services for a Sustainable Rural Livelihood

Strategies, Lessons Learned and Policy for the Years 2011-2015



Photo cover: © James Ewen

A local NGO has set up several village savings schemes. Those schemes mean that farmers are less vulnerable to fluctuations in their income and can borrow and save money without paying exorbitant interest rates.

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Table of Contents

1 Introduction	5	6.3 Policy Objective 1: Oxfam Novib contributes to developing the rural financial sector	30
2 Actors and the Size of the Microfinance World	7	6.3.1 Financial Institutions for Rural Development	32
2.1 Providers, products and clients	7	6.3.2 Financial Services for the very poor: Member Owned Microfinance Institutions	33
2.2 Organisations in the South	7	6.3.3 Role of MFIs	34
2.3 Organisations in the North	8	6.3.4 Rural Banks, Co-operation with Commercial Banks	35
2.4 Investments of donors and investors	9	6.3.5 Micro-Insurance	36
3. Oxfam Novib and Microfinance	12	6.4 Policy Objective 2: Oxfam Novib contributes to strengthening the social character of microfinance	36
3.1 History up to 2004	12	6.4.1 Social Performance Management in MFIs	36
3.2 Oxfam Novib's policy from 2004 to 2010	13	6.4.2 Impact and the SIM tool	37
3.2.1 From A to B to C: Oxfam Novib's graduation model	13	6.5 Policy Objective 3: Oxfam Novib supports the institutional development of producers' organisations inside and outside the value chain	38
3.2.2 Oxfam Novib's investment profile	14	6.5.1 The missing middle	38
3.2.3 MicroNed	14	6.5.2 Value chains	38
3.2.4 Partos' Evaluation of Microfinance	16	6.6 Policy Objective 4: Oxfam Novib uses the Oxfam Novib Fund to contribute to the financial sustainability of MFIs and producers' organisations	40
3.2.5 Appreciation	17	6.6.1 Policy Objective 4a: The Oxfam Novib Fund focuses on Tier 3 MFIs and comparable producers' organizations	40
4 Recent Developments and Oxfam Novib's Role	19	6.6.2 Policy Objective 4b: Late 2015 80 percent of the funds from the Oxfam Novib Fund are released or spent in MFS-II countries	40
4.1 Rising Professionalization	19	6.6.3 Policy Objective 4c: The Oxfam Novib Fund stays at least the same size	40
4.2 The Social Mission of Microfinance	19	6.6.4 Products of the Oxfam Novib Fund	40
4.3 Impact	21	Annexes	
4.4 Savings	22	1 Conditions for reaching the (very) poor.....	43
4.5 Rural Finance	22	2 Client Protection Principles	44
4.6 The Graduation Model	23	3 Twelve Key challenges for Rural Financial Services Provision.....	45
5 Future Developments in Microfinance	25	4 Rural worlds in Oxfam Novib Strategic Plan 2011-2015	47
6 Rural Financial Sector Development, Policy 2011-2015	27	References	49
6.1 The Right Based Approach	27		
6.2 Basic Principles of a New Policy	28		
6.2.1 Target group approach	28		
6.2.2 Combining the Poverty Lending Approach and Micro-Banking Approach	28		
6.2.3 Emphasis on development of the local financial sector	29		
6.2.4 Combining Grant Making and Asset Management	30		



Mohammed Yusuf Ali is one of the farmers helped by Oxfam's Oxen Credit Scheme. His community worked with Oxfam to work out their key problems and the people most in need. This scheme has helped farmers like Mohammed to change how they farm and breed new oxen creating an asset and self-perpetuating programme.

1. Introduction

Oxfam Novib believes that contributing to a financial sector that offers poor people access to financial services, is an important condition for realising more investments by and for our target groups. In the past 15 years microfinance has been an important element of Oxfam Novib's programmes. The support to this sector was in different areas and with different tools. Grants, loans, guarantees and several investments in equity have been used to build microfinance organisations (MFIs), and grants have also been provided to other parts of the microfinance sector, such as MFI networks.

There are several reasons for renewing the old policy:

- The old policy, adopted in 2004, expires in 2011.
- In recent years we have seen huge developments in the world of microfinance, such as innovations in microfinance products, the continued professionalisation of the sector, the rise of private sector investments in the sector and the attention to new target groups.

It is clear that in the new Business Plan, with the reduction in the number of countries where Oxfam Novib works and the focus on rural areas, the scope of microfinance programmes will be different and smaller compared to recent years. We must also acknowledge that the growth of the microfinance sector and the search for new horizons (an important task of a civil society organisation like Oxfam Novib) presents us with new challenges. Building new organisations remains important, but maybe less than in previous years. Mainstreaming microfinance also raises ethical questions about the way the sector sometimes is functioning; the search for new forms to reach new target groups (i.e. people deeper below the poverty line). They are all questions that demand a reply. This paper makes a start in doing just that. The focus on rural areas also demands that attention be paid to new target groups that can be reached with grants and loans. The provision of good financial services to the target groups that Oxfam Novib has identified also demands the capacity building of

groups and partners. Therefore, in some instances this policy paper moves beyond the boundaries of pure financial services.

The policy for the years 2011 to 2016 is more differentiated than the microfinance policy to date. The goal is to have the microfinance programme connect better to the other dimensions of Oxfam Novib's Aim 1 Programme: the context is leading in selecting tools and the type of organisation. The basic principle is the focus on the target group as described in the policy paper *Right to a Rural Sustainable Livelihood*, and the different types of organisation and financial products that work best for these target groups. This policy paper must therefore be seen as an elaboration of *Strategy One: Building and Protecting Assets* of the policy paper *Right to a Rural Sustainable Livelihood*.

This policy paper describes these developments and sets lines on how Oxfam Novib responds to these challenges. It contains a rough description of the size of microfinance and the history of microfinance at Oxfam Novib. A number of recent developments will then be outlined, as will Oxfam Novib's positioning. Chapter 5 discusses future trends as analysed in a paper drawn up by MicroNed in co-operation with Triodos-Facet in 2009. Chapter 6 presents the outlines of the new policy for the coming years.



Zawidi Magashi tells Oxfam visitors and her fellow villagers about the internal lending scheme. She is holding her shares book which documents shares bought in the scheme and loans provided and paid back. Oxfam's training is helping chicken farmers form community groups, get credit and organize their finances effectively.

2. Actors and the Size of the Microfinance World

Before elaborating Oxfam Novib's past actions in microfinance, a picture of the current size of microfinance will be given.

2.1 Providers, products and clients

Microfinance is about extending financial services to poor people. The world of microfinance has a big variety of organisations, products and client's, see table 1.

Among the providers we see a wide range of organisations organised in formal and informal ways and organisations specialised in certain products. With regard to products, we are generally talking about credit and savings. Micro-insurance and leasing are on the rise, as are pensions. Remittances were popular for a while in the world of development co-operation. Huge amounts of money are transferred annually from the North to the South and between countries in the South (over 350 billion dollar a year). Technological change has made its entrance which expands the opportunities for financial services where they were impossible before.

Microfinance is mostly associated with small loans for which no collateral is required, other than a group

solidarity guarantee. That is a misconception. Individual loans in particular often also involve a personal guarantee or business collateral.

2.2 Organisations in the South

It is not clear how many microfinance institutions currently exist. Estimates range from 7,500 to 14,000. The estimated size of the total outstanding portfolio of microfinance worldwide is 50 billion dollar, with about 130 million people. We find the biggest microfinance institutions (MFIs) in Asia above all, see table 2 on page 8.

The MIX Market, a virtual market place for microfinance, has about 1,400 registered MFIs with over 70 million clients. The clients of the Self Help Groups (SHGs) and the Village Savings and Loans Associations (VSLAs) are not included. Of all MFIs about 250 to 300 are considered tier 1, i.e. large MFIs with a risk profile allowing them to attract funds from institutional investors.

Alongside MFIs we also find groups offering financial services, which are organised more or less informally and very much locally: the Self Help Groups (SHGs) in

Table 1: Providers, products and clients

Providers	Products	Clients
– Banks	– Micro loan	– (Poor) families
– Finance Companies	– Small loan	– Micro entrepreneurs
– NGOs	– Educational loan	– Small farmers
– Savings & Credit cooperatives	– Credit card	– Families in their different roles: consumers, house builders, parents, savers, insurance takers, part of money flow networks
– Village Savings and Loans Associations	– Mortgage	
– Big box consumer retailers	– Consumer loan	
– Insurance companies	– Checking account	
– Property developers	– Savings account	
– Money transfer agencies	– Foreign currency account	
– Mobile phone companies	– Remittances	
	– Supplier credit	
	– Leasing	

Table 2: The biggest MFI's (December 2008)

Name	Country	Legal Form	Number of clients
VBSP	Vietnam	Bank	6,793,443
Grameen	Bangladesh	Bank	6,707,000
BRAC	Bangladesh	Non-profit (NGO)	6,367,250
ASA	Bangladesh	Non-profit (NGO)	5,877,440
BRI	Indonesia	Bank	3,515,812
PROSHIKA	Bangladesh	Non-profit (NGO)	1,761,638
SKS	India	Non-Bank Financial Institution	1,629,474
Spandana	India	Non-Bank Financial Institution	1,188,861
Banco Compartamos	Mexico	Bank	1,155,850
SHARE	India	Non-Bank Financial Institution	989,641
Total			35,986,409
SHGs	India	Bank Linkage programmes	>35,000,000
VSLAs	Africa	Autonomous and informal	> 2,300,000

Table 3: Northern funders of microfinance

Donors	Investors
Bilateral organisations, e.g.: DFID, DGIS, SIDA, USAID	Development Finance Institutions, e.g.: Private sector organisations of multilateral and bilateral development organisations: KfW, IFC, FMO, etc.
Multilateral Development Banks and UN Organisations, e.g.: World Bank, regional development banks, UNCDF, IFAD	Individual investors, e.g.: Oikocredit, investment funds, peer-to-peer platforms (e.g. KIVA)
Foundations: Non-profit organisations, trust funds, e.g.: Bill and Melinda Gates Foundation, Ford Foundation, CRS	Institutional investors, e.g.: Commercial banks, pension funds, insurance companies, endowments, private equity funds, and sovereign wealth funds (Deutsche Bank, TIAA-CREF)
Other donors: (Inter)national NGOs (Oxfam Novib, etc.)	

India and the Village Savings and Loans Associations (VSLAs) found mostly in Africa, but also elsewhere, such as in El Salvador and Cambodia. Especially these last groups do not have strong links with northern financing, except in the case of building and supporting groups through grants. VSLAs accumulate their own funds mainly through clients' savings. The SHGs in India get funding mainly from local rural banks, in addition to savings they generate themselves.

2.3 Organisations in the North

Figures from 2008 show us that each year 3 to 4 billion dollar from the North is invested in microfinance. 61 institutions in the North¹ annually participate in a study of their investments in microfinance. The organisations can be categorised as shown in Table 3.

1 ABP, AECID, AFD Proparco, AfDB, AsDB, AusAID, BIO, CAF, CDC, CIDA, Citi Foundation, Cordaid, CSIF, DANIDA, DCA USAID, DFID, DOEN Foundation, EBRD, EC, EIB, Finland MoFA, Finnfund, FIRST, FMO, Fondation Sen'Finances, Ford Foundation, Gates Foundation, Grameen Foundation, Grameen Jameel, GTZ, Hivos, ICCO, IFAD, IFC, ILO, ING, IsDB, Italy MoFA, JICA, KfW, Kiva, Lux Dev, Mastercard Foundation, MCC, MIF IADB, MSDF, Netherlands MoFA, NORAD, Norfund, Oikocredit, Omidyar Network, OPIC, Oxfam Novib, PGGM, SDC, Sida, SIFEM, TIAA-CREF, UNCDF, USAID, World Bank.

2.4 Investments of donors and investors

On December 31, 2009 a total of 21.3 billion dollar was invested in microfinance. The regional distribution is presented in table 4.

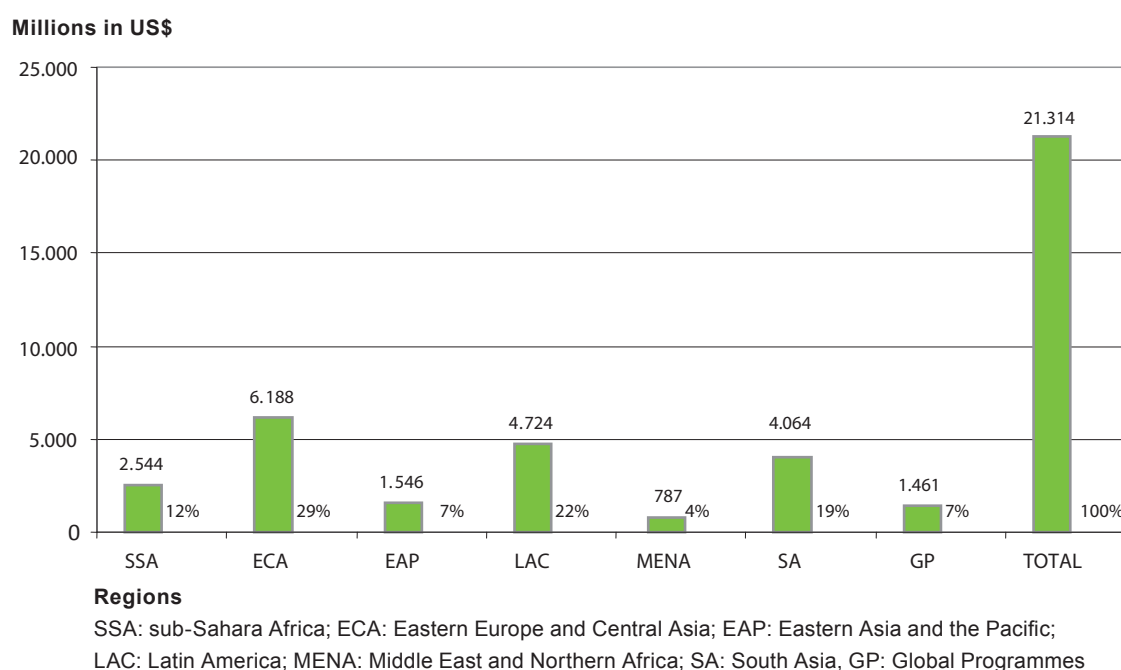
The distribution of investments by donor and investors differs a lot per region. Table 5 presents the percentages per region.

The majority of the investments are from the group of investors (52%). South Asia receives relatively speaking most investments, but mostly from donors. There are several reasons. The form microfinance takes in that

region is less suitable for investments (SHGs in India). Also, the interest rate MFIs charge their clients are often very low, which convert to low passive interest rates these MFIs can pay to their creditors. And, many MFI's also provide saving facilities, generating funds for their loan portfolio. Investors focus above all in those regions with low currency risks, acceptable returns on their portfolio and where donors have paved the road for them.

SSA only received 12% of total investments. We see that donors invest relatively much in SSA, but that this is not followed up by commercial investors. This reflects the weakness of microfinance on the continent caused by

Table 4: Investments committed in microfinance on December 31, 2009, by region*



* CGAP, Microfinance Funding Continues to Grow. Results of the 2009 Microfinance Funder Survey, November 2009.

Table 5: Distribution of investments per region between donors and investors (in %, 2008)

Region	Donors	Investors
SSA	75%	25%
ECA	12%	88%
EAP	60%	40%
LAC	22%	&+%
MENA	53%	47%
SA	85%	15%
GP	33%	37%
Total	48%	52%

weak MFIs, a politically volatile continent and currency risks that are difficult to cover.

It is noticeable that donors invest a lot per client in the regions ECA and MENA, whilst they are not the least developed regions. Investors do so too. The latter's

investments are big because of the quality of the MFIs. (See table 6)

In the next chapter we present the support of Oxfam Novib to the MFI sector in the past.

Table 6: Investments per client (2008)

Region	Donor \$ per client	Invester \$ per client	Total \$ per client
SSA	135	36	171
ECA	141	799	940
EAP	27	19	46
LAC	21	97	118
MENA	172	165	337
SA	56	4	60
Multi Regional	69	48	107



Kamah Sheriff (brown shirt), 40, invests the savings he has made from his cocoa business back in to the community savings and loan scheme, handing over his money to scheme secretary Morris Borbo to be counted. He received a loan from the scheme that he used to pay his sons' secondary school fees.

3. Oxfam Novib and Microfinance

3.1 History up to 2004

The history of microfinance at Oxfam Novib goes back to the late 1980s, when Novib began experimenting with loans, guarantees and investments in partner organisations' equity. A separate unit was set in 1997 in order to manage the lending programme and give it more substance. It had one full-time employee. In 1998 the ministries of Development Co-operation and Finances granted the four co-financing organisations permission to start a pilot and extend loans. In 2002 the Ministry of Development Co-operation gave its final permission to use this tool.

A policy document on loans was written in 1996. The policy was generally aimed at financing income generating activities and provided space for financing micro-credit organisations and other organisations working on the target group's economic activities. In the course of time this tool was almost exclusively deployed for microfinance. In September 2000 the unit, now with three full-time employees, was reorganised to become the more formal *Financial Services Unit* (Dutch acronym: FDE).

In 2001 the paper *Financial Services, Guidelines for Funding Microfinance Programmes and Projects for the Period 2002-2004* was published. This programme's general objective was given as:

“Novib’s financial services policy is aimed at building income security and increasing the incomes of self-employed poor people, by improving access to financial services. What distinguishes us is a strong emphasis on the development context for providing access to financial services. The provision of services is not a goal on its own, but serves the struggle against poverty, and the empowerment of people living in poverty.”

Where it was noted that:

“In the light of the discussed trends and paradigms in microfinance, it is of great importance to Novib to get the wishes of clients and users on the agenda in full. Client responsiveness is therefore a guide in appraising proposals.”

The same paper also discussed tools and guidelines for financing MFIs.

In 2002 FDE took over the management of the ASN Novib Fund from Oikocredit. In 2004 FDE managed 46 loans from the Oxfam Novib Fund in 24 countries, with an outstanding portfolio of € 11.8 million, and 7 loans from the ASN Novib Fund worth € 4.4 million. At that moment FDE was staffed by 7 persons.

The policy paper *Microfinance Global Thematic Programme* was published in 2004. There were two reasons for writing this paper. First, the focus debate raised the question if Oxfam Novib should be extending loans in all countries. In 2004 Oxfam Novib only had loans outstanding in 4 core countries, whilst there were plenty of opportunities for developing microfinance outside these countries. The idea to operate in multiple countries was based on the need for a good spread of risks, as Oxfam Novib focuses its work in the poorer countries with a weakly developed microfinance sector. The idea that investing in microfinance only in core countries would keep Oxfam Novib's portfolio small, also played a role. At the time the size of the portfolio also was a factor in the influence an organisation has in the world of microfinance.

Table 7: Countries where Oxfam Novib works

Region	Countries before 2007	New countries in the BP 2007-2010
Africa	Ethiopia, Tanzania, Uganda, Kenya, Mozambique	Ghana, Nigeria, Malawi, Mali, Burkina Faso, Niger, DRC, Rwanda, Burundi, Angola
Latin America	Peru, Bolivia, Colombia, Ecuador, Nicaragua, El Salvador, Mexico, Regional	Argentina, Brasil, Guatemala, Honduras, Paraguay
Asia	India, Sri Lanka, Bangladesh, Cambodia, Philippines	Vietnam, Tajikistan, Indonesia
Europe	Albania, Armenia, Bosnia, Bulgaria, Serbia and Montenegro	Georgia, Moldova

A team of representatives of the ILO, DFID, EDA² and CGAP,³ which did a so-called peer review in the Netherlands (CGAP members evaluating the activities of other CGAP members), said:

“The paradox is that the Netherlands is one of the biggest bilateral players in micro-finance, as measured by size of micro-finance portfolio. Yet, the lack of vision and strategic coherence within the system means that the Netherlands’ impact and reputation does not adequately reflect its significant investment in micro-finance.”

Oxfam Novib felt the urge to profile itself as co-financing agency in the field of microfinance, and specifically aim at building MFIs in the chain: start-up, expansion, maturity. That was finally implemented via the Microfinance Thematic Programme, a programme that could be implemented in different regions and even globally. The fact that FDE also managed the ASN Novib Fund, along with the Oxfam Novib Fund, hugely facilitated in making the chain-thinking operational.

The paper from 2004 also reaffirmed what Oxfam Novib had always been: not an organisation focusing on microfinance, but a general development organisation. Oxfam Novib only engages with microfinance when it falls within its broader development objectives. In the paper the objective was formulated as follows:

“Oxfam Novib aims to support strategic MFIs that contribute to building an inclusive microfinance sector.”

The MFI selection criteria that were identified were:

- 1 MFIs developing new markets

- 2 MFIs working in rural areas
- 3 MFIs that have to potential to scale up
- 4 MFIs engaged with product development (i.e. aimed at people living with HIV and AIDS, women, micro-insurance)
5. MFIs that contribute to developing legal structures for microfinance in the countries where they work.

In the end Oxfam Novib selected the countries shown in table 7.

It must be noted that Oxfam Novib withdrew from Albania, Bosnia, Serbia and Montenegro in 2007, due to the phasing-out of the programme in Eastern Europe.

3.2 Oxfam Novib’s policy from 2004 to 2010

3.2.1 From A to B to C: Oxfam Novib’s graduation model

After 2004 the chain-thinking characterised the policy. The regional bureaus supported starting organisations (called tier 4 MFIs) with grants to start up or to restart. FDE had a supporting and advising role for these activities. Once starting MFIs qualified for loans (from tier 4 to tier 3) FDE (now Triple Jump) assumed a more active role, and prepared a loan. When the MFI qualified for a loans from the ASN Novib Fund (tier 2 and tier 1), it gradually disappeared from the Oxfam Novib Fund’s portfolio. Alongside the regional bureaus FDE also identified MFI that would qualify for a loan from the Oxfam Novib Fund. The flow of starting MFIs to the Oxfam Novib Fund proved pretty meagre. Starting MFIs require support for a longer period and developments do

2 EDA Rural Systems, an Indian organisations focused on consultancies, research and capacity building in the field of microfinance in India, and Asia in general.

3 The Consultative Group to Assist the Poort (CGAP) is a thinktank of international donors (DGIS, e.g., is a member as are almost all bilateral donors, but also big organisations like Bill & Melinda Gates Foundation, etc.). CGAP does research, and has been instrumental in the past in developing analytical models of MFIs and benchmarks. Also see: www.cgap.org.

not always go linear, but with twists and turns. It was also the conclusion of the Partos Evaluation (see paragraph 3.2.4).

In 2005 Triple Jump Management BV and Foundation Triple Jump Advisory Services (TJAS) were founded. Triple Jump Management is a portfolio management organisation, which became operational in June 2006 when it assumed the management of the ASN Novib Fund. In March 2007 Triple Jump took over the management of the Oxfam Novib Fund. As a result loan management is now located outside Oxfam Novib. Triple Jump Advisory Services (TJAS) supports MFIs in their institutional development. TJAS's target group is made up of those MFIs that (almost) qualify for a loan, but still require technical assistance. TJAS is specialised in management information systems, internal control, governance, new products and social performance management (see paragraph 4.2).

With regard to grants by Oxfam Novib, the policy plan 2007-2010 paid specific attention to start-ups, with an original target of 60 starters, later reduced to 30 starters. The reason was the huge investment in time of the responsible programme officer in a start-up. Networks were also supported, and in some cases (such as India and Tanzania) also organisations facilitating target groups to get access to financial services (SHGs in India and small co-operatives in Tanzania). By supporting national works we ensure that, on the one hand, individual MFIs get the support and monitoring of their progress, and, on the other hand, lobby of the government is undertaken, especially with regard to legislation and regulation.

3.2.2 Oxfam Novib's investment profile

Total spending in the microfinance sector from 2003 until 2009 amounted to € 62.6 million in loans from the Oxfam Novib Fund and € 44.5 million in grants. On December 31, 2009 the Oxfam Novib Fund had a total size of € 30 million, and the portfolio of the ASN Novib Fund amounted to € 77 million. In 2009 a total of 7 million people were reached, of whom 750,000 through the grants programme, half of which in India, via micro-credit and micro-insurance.

The Oxfam Novib Fund is one of the funds investing in tier 3 MFIs. The fund distinguishes itself from similar funds in several important areas (table 8).

In terms of its risk profile the Oxfam Novib Fund distinguishes itself with regard to loans in local currencies and the regions of investments. Africa is as such prominently present in Oxfam Novib's portfolio compared to similar funds. Oxfam Novib's risk profile is also high compared to other funds. The MFIs borrowing from Oxfam Novib also have a very low average loan amount for their clients (€ 220), revealing that the partner MFI serves clients who live well below the poverty line. They are important indications of the value added of the Oxfam Novib Fund. The fund does have, as do others, invested a high percentage in Latin America. It is a market with a long tradition and good initiatives, and thus with good points of contact for support. The growth of the Oxfam Novib Fund is low in comparison with other funds. The reason is that the Oxfam Novib Fund is financed by Oxfam Novib's programme monies. Oxfam Novib is not a specialised microfinance organisation, but a broad development organisation.

Oxfam Novib's loans portfolio, sized € 29.3 million⁴ on December 31, 2009, is divided as presented in Pie 1. The distribution of the aggregated grants over 2007 to 2009 over the regions was as presented in Pie 2.

The bureaus South America and Central America, in 2005 merged to form the bureau Latin America, have always emphasised strongly the development of the financial sector, but the low percentage of grants does reveal it has had a good institutional development. The high percentage of grants in South Asia is mainly due to India, where much has been invested in SHGs, which were a focus area of the bureau. Both for loans and for grants, the relatively high percentage of financial sector support in sub-Saharan Africa is noticeable. With its grants too Oxfam Novib has a different profile from the average fund that extends grants.

3.2.3 MicroNed

MicroNed was launched in June 2006. The goal was a better co-ordination of the granting activities of Cordaid, Hivos, Icco and Oxfam Novib, and from 2008 those of the Rabobank Foundation too.

4 Excluding about € 800,000 in loans to E&Co and MDLF.

Table 8: Regional distribution of Oxfam Novib's and other funds' loans portfolio (December 2008)

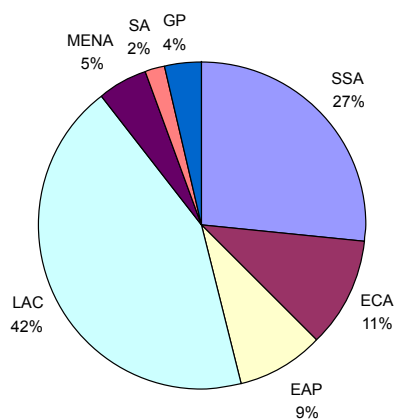
Averages	All Microfinance Funds (averages)	Social Funds* (averages)	ON Fund (averages)
Assets			
Total Assets	USD76.4 M	USD49.0 M	USD 33.5 M
Annual Growth of Total Assets	32%	13.3%	5%
Microfinance Portfolio			
Microfinance Portfolio in Debt	75%	85.6%	99.2%
Debt in Local Currency	20.3%	37.1%	52%
Unhedged Debt in Local Currency**	5.2%	10.9%	40%
Average Maturity of Debt Investments	32 months	27 months	–
Average Debt Investment Size	USD1.8 M	USD0.7 M	USD 0.45M
Gross Yield on MF Debt Portfolio	9.5%	10.1%	8.9%
Geographic Distribution			
Eastern Europe & Central Asia	47.0%	18.1%	17%
Latin America & the Caribbean	29.1%	39.6%	37%
East Asia & the Pacific	6.1%	18.7%	5%
South Asia	4.7%	6.4%	5%
Middle East and North Africa	1.0%	0.3%	2%
Sub Saharan Africa	6.2%	14.0%	25%

* The following investment funds have been categorized by CGAP as Socially Focussed MIVs: ADA – Luxmint, Alterfin cvba, Consorzio Etimos S.c., Deutsche Bank Microcredit Development Fund (DBMDF), DID – Partnership Fund, Emergency Liquidity Fund, Envest Microfinance Cooperative, Fonds International de Garantie, Global Partnerships Microfinance Fund 2005 LLC, Global Partnerships Microfinance Fund 2006 LLC, Hivos-Triodos Fund Foundation, Incofin cvso, MicroCredit Enterprises, Nicaraguan Credit Alternatives (NICA) Fund, Oikocredit, Opportunity Loan Guarantee Fund I, LLC, Planet MicroFund, International Solidarity For Development and Investment, Triodos-Doen Foundation, CRESUD SPA.

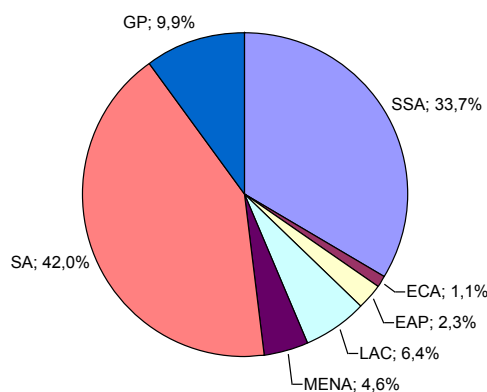
** This concerns loans in unhedged local currency. These loans are therefore high risk, as they are often loans to weak MFIs. Oxfam Novib considers this as its niche.

Source: David Kruijff: Exploring the Opportunities for the Future of the Oxfam Novib Microfinance Fund. Consultant's study for Oxfam Novib, 2010.

Pie 1 Regional distribution of the Oxfam Novib Fund per December 2010*



Pie 2: Regional distribution of donations by Oxfam Novib 2007-2009*



* LAC: Latin America and the Caribbean, SSA: Sub-Sahara Africa, ECA: Eastern Europe and Central Asia, EAP: Eastern Asia and the Pacific, MENA: Middle East and Northern Africa, SA: South Asia, GP: Global Programmes

MicroNed aims to improve efficiency and effectiveness of MFI support by a joint approach:

- harmonization of CFA policies, strategies and activities on microfinance;
- coordinating CFA support in countries and regions, and on microfinance themes;
- sharing of information among members and with others;
- joint monitoring and reporting of results;
- capacity building of MicroNed members.”⁵

The specific niche where MicroNed’s members want to operate is the same niche as Oxfam Novib’s. MicroNed provides members with the tools and makes proposals for aligning policies between members. It is not an operational organisation. MicroNed also gives training to microfinance officers of member organisations, and if possible of other organisations too.

Several country working groups are (were) active in MicroNed. A joint microfinance scan was undertaken of ten countries, with the goal of formulating common country policies. In the end joint country strategies were formulated for 2 countries.

Seven thematic working groups were set up at the start, which had to give an input to developing the contents-related capacities of the responsible staff inside MicroNed’s members: HIV and AIDS, microfinance in emergency situations, rural finance and co-operative development, social performance management,⁶ micro-insurance, lobby and remittances. The dynamics in the groups differed a lot. For different reasons some groups have ceased to exist. In 2008 the working group Capacity Building was set up to improve the quality of the support start-ups get. In 2009 the working group developed a monitoring and evaluation tool for this purpose. In 2009 it was also decided to continue with three working groups, namely Capacity Building, Rural Finance and Social Performance Management, considering the common strategic approach of the member organisations. Activities in the field of lobby and press liaison are also co-ordinated.

MicroNed’s members jointly finance, in consultation with the working group Social Performance Network, the Imp-Act network, which supports MFIs in introducing social performance management in their organisations.

Every member of MicroNed also finances a number of regional networks in the framework of social performance management. In 2008 Icco, Hivos and Oxfam Novib gave a start-up subsidy to the website *www.mftransparency.org* which maps the costs the MFIs charge their clients. In this way we want to contribute to transparency in the sector and exert pressure on MFIs that do not (want to) follow the trend of decreasing costs. There is a common policy in the field of supplying start-up capital to starting MFIs and in the field of multi-purpose organisations with a credit component. Agreements were also reached on jointly funding organisations, the so-called Code of Collaboration.

MicroNed is highly appreciated for the courses it organises. The subjects are those raised by the thematic groups, but the secretariat also organises courses in the field of financial and social analysis of MFIs. MicroNed has facilitated the growing collaboration between ‘the working floors’ of its members.

In May 2009 Triodos-Facet conducted an evaluation of the activities implemented since the launch. The conclusion was that MicroNed’s future is in capacity building of members’ staff, the joint funding of organisation at the meso and macro levels (networking at the national and regional levels), and in building and communicating a common vision on microfinance to the outside world.

Every year MicroNed organises a conference on a current issues, which those interested in microfinance in the Netherlands can attend. The intention for this annual meeting is to develop into a substance-focused microfinance afternoon in the Netherlands. In June 2010 the first microfinance week was organised for members. During this week the focus is on conducting training sessions and working group meetings.

3.2.4 Partos’ Evaluation of Microfinance

In 2010 Partos’ evaluation on MFOs’ microfinance operating from 2003 and 2007 was published. The evaluation’s objectives were the following:

- To what extent did the co-finance agencies (CFAs) succeed in supporting the Microfinance Institutes

5 Cordaid, ICCO, Hivos and Novib: Inception Plan MicroNed 2006-2007 Netherlands’ Partnership for Poverty Outreach in Microfinance, p. 3.

6 For more see paragraph 4.2.

(MFIs) to go from start-up, emerging to mature and commercially viable MFIs?

- To what extent have CFAs and the supported MFIs been able to maintain the poverty focus? To what extent is there a correlation between question 1 and 2?
- To what extent have the CFA supported activities been able to change the enabling environment for poverty-oriented micro finance? Were they efficient, effective and relevant within the context?

The choice was deliberate not to include the impact of microfinance in the study, because reliable studies on this issue are expensive and complicated, and can take a long time. Besides, many studies already exist. The evaluation therefore only focused on the MFOs' contribution to financial sector developments that benefit poor people.

In general, one can say that Oxfam Novib has followed the best practices as formulated in the world of microfinance: grants for starting MFIs and MFIs not yet financially sustainable, and loans with commercial conditions for MFIs that are. There were exceptions to this rule at Oxfam Novib (and at the other MFOs). It was recommended that the motivation behind a divergent choice of tool should be presented more clearly. The partners' focus on poverty is beyond dispute, and there is no trade-off between the social focus and the financial and organisational development of an MFI. The financial products are also available to poor people, except for farmers wanting to invest in agriculture. It must be noted that the clients are the enterprising poor, not all poor people. In order to reach them too more attention should be paid to savings and insurance products. Regarding the activities in the field of enabling environment,⁷ the conclusion is that MFOs' partners (Oxfam Novib's too) are relevant, giving a value added to the MFOs.

There were also several weak points:

1. The evaluation report observes that MFOs have been very instrumental in the growth of the organisations and the outreach, but less so in increasing the quality of governance and management of the MFIs. Oxfam Novib is therefore studying, together with Triple Jump, the possibilities for raising quality.
2. The evaluation mission observes that MFOs have achieved insufficient results in tackling gender

inequality in accessing financial services, and that financial criteria receive more attention than the social aspects of microfinance. Oxfam Novib and Triple Jump developed an analytical tool in 2008/09 to be used in Triple Jump's due diligence. Part of that tool is the Gender Traffic Light (GTL), as used in appraising all proposals. This tool was evaluated separately in 2010, with a positive result. It was revealed, though, that using the GTL could yet improve:

- a. There is still too little depth in the analysis of the social aspects of MFIs. During the assessment little time is reserved for the social aspects, leading to answers with little depth;
- b. The gender analysis must be aligned more with the analytical frameworks of Oxfam Novib.

3.2.5 Appreciation

In the past Oxfam Novib has had a coherent policy on microfinance. The emphasis of the past decade on supporting MFIs has led to the recognition of Oxfam Novib in the world of microfinance. There are not many funds for young MFIs. The Oxfam Novib Fund is known as one of the few funds that supports the bottom of the MFI market in a qualitatively good manner. Triple Jump can be considered a good fund manager in microfinance, where the management of multiple funds (ranging from the risk-taking Oxfam Novib Fund to the risk-minimising commercial SNS fund) gives it an excellent market position. It is the opportunity of getting a first funding from a single fund manager, technical support from an allied organisation and the option of graduating to more commercial funds that has proven to be a good concept. Furthermore, the use of the social analysis developed by Oxfam Novib and Triple Jump is ahead in the world of microfinance. TJAS was recently evaluated, revealing the excellent quality of the advice it gives young MFIs. Oxfam Novib and Triple Jump have thus become reliable partners of MFIs in the market in which they move.

In recent years Oxfam Novib has had a huge outreach with the microfinance programme. The objective of reaching 4.1 million people with financial services has been amply surpassed by 3 million people. That is very much due to the strong growth of the Oxfam Novib Fund and the ASN Novib Fund. The support of SHGs in India has also contributed considerably to this result.

⁷ The enabling environment is formed by all institutions that each in its own way contribute to an optimal performance of the microfinance sector: governments (legislation and regulation), MFI networks (lobby and quality control by their members), credit rating agencies, knowledge development, etc.



"I used to be very poor, but then I took a credit from BRAC since I believed I could lead a better life out of poverty and I had to provide education for my two sons. This made me work real hard and the efforts led to success. Now I have 13 cows, a lot of goats, chickens and ducks. I am a successful business woman now!"

4. Recent Developments and Oxfam Novib's Role

In the world of development co-operation, there is no theme that has received more of the public's attention as microfinance. It is generally considered one of the success stories, one that ensures a real structural contribution to solving the poverty issue. Even critics of development co-operation call microfinance an example of what development co-operation could achieve. And, the remarkable fact is that the critique of microfinance began inside 'the world', and not outside.

In recent years the world of microfinance has developed at dizzying speed. It is right to keep an eye on these developments, as they raise several fundamental questions. Over the past 10 years Oxfam Novib's policy hasn't changed a lot. It has always been focused on the classical MFI. The capacity developed in recent years by Oxfam Novib focused on that direction. Consistency in policy is generally good, but dangerous in a fast-changing world. What are these changes?

4.1 Rising Professionalization

There is no other sector in development co-operation that has professionalised as fast as microfinance. Launched by the NGO sector in the South (Bangladesh, but the precursors can also be found in the programmes of many NGOs in the South in general), billions of Euros are now turned over in this world, and funders range from NGOs to pension funds. Microcredit has become mainstream. That creates other relationships. Portfolio management is no longer merely about extending and recovering loans, but has expanded to include professional risk management, exchange rate management, investments in MFIs' equity, take-overs, initial public offerings (IPOs), etc. The industry has become surrounded by professional organisations specialising in MFI credit rating, consultancy agencies staffed by (former) bankers and other financial experts, and you can graduate in microfinance. Oxfam Novib has followed that trend by (co) founding Triple Jump.

4.2 The Social Mission of Microfinance

In 2003 the idea of Social Performance Management (SPM) emerged. In SPM, the organisational set-up is analysed in view of its mission, vision and target group. Does it have the right people, the right procedures and the right products for the target group? Is it, in other words, designed in such a way that it can reach its objectives?

Reaching extremely poor people is not a given in microfinance. It depends, e.g., on the conditions you create within your own institution. On the basis of several case studies, Simanowitz highlights them (see annex 1). These conditions are the object of an analysis of an MFI's Social Performance Management.

Until several years ago little attention was being paid to the social aspects of microfinance. Social Performance Management, social rating, www.mftransparency.org, WEMAN (see page 19), they are all expressions of efforts of the microfinance world to catch up with its original social mission. Recovering a loan is no longer enough. The awareness has grown that more than just the use of financial ratios and financing tools is needed to support MFIs. Also investors are interested to know what the social impact of their investments is. They need to tell the right story to their stakeholders, especially when it concerns a fund that was certified a 'social-ethical investment fund'. Today it is a broad movement, in which Oxfam Novib also plays a role. Oxfam Novib and Triple Jump are one of the first making an analysis of the social aspects of an MFI's during a due diligence.

An important concern is the "over-indebtedness" of clients. This is already the case in a number of countries, mostly in urban areas with a large supply of MFIs and fierce competition. The need to grow does not always lead to balanced credit analyses. In countries like Bolivia, Peru, Morocco, Bosnia and Cambodia these problems are at the head of the queue. In Nicaragua 40% of the

population has access to microfinance. This would mean that 60% does not yet have access. It remains the question if these 60% really exist. Calculations for Nicaragua reveal an effective demand with 40 to 50% (not all micro-enterprises want an MFI credit).⁸ The increasing saturation of the market makes this problem more acute.

Oxfam Novib plays an important role in the Social Performance Task Force (SPTF, www.sptf.info). It is a platform of 600 organisations, donors, investors and MFIs (networks). This forum is used to determine criteria for the social aspects of microfinance, and to develop tools to monitor them. For a while Oxfam Novib was a member of this initiative's steering group. Where possible, Oxfam Novib uses grants to development MFIs in this field.

In recent years much work has gone into the so-called Client Protection Principles,⁹ an international code of conduct drawn up by CGAP. Oxfam Novib has signed this declaration. It contains six principles the MFI must follow in its interaction with the client. The Dutch Microfinance Platform (NPM in Dutch) has drawn up a declaration, in which it takes a stand against MFIs only aimed at making profits and little interested in the impact of microfinance on their clients' poverty.¹⁰ Oxfam Novib had a seat in the group that wrote the statement. It became necessary by the rising number of stories doing the rounds about the bad treatment of clients by MFIs. Many view the story of microfinance as one of success, but cracks are beginning to appear in the building. The increasing commercialisation of microcredit also causes nasty elements: high rates of interest, bad treatment of clients, excessive profits, over-indebtedness of clients, and less attention to microfinance as a tool in fighting poverty.

The disproportionately high interest some MFIs charged prompted the launch of the website www.mftransparency.org, which does research into the costs MFI clients pay. The real costs an MFI charges are then published on the website. A benchmark of comparable MFIs indicates if the costs charged are out of step. By publicising these data we hope that the pressure increases on MFIs to adjust their interest rates. Oxfam Novib, Icco and Hivos (as MicroNed members) were the ones first to contribute finances to launching the website.

8 CDR: Microfinance in Nicaragua (2002)

9 See annex 2 for the Client Protection Principles

10 See www.microfinance.nl

Oxfam Novib is also one of the initiators of the 'Rating Initiative' (RI, www.ratinginitiative.org). This initiative subsidises young and small MFIs who want to undergo a rating. This is not only a financial rating, but also a social rating. The RI has been in close contact with the rating agencies in the development of this product. The objective is for small MFIs to be able to translate their social objectives into their organisation's development, and to have them monitored on this. Oxfam Novib is part of the steering committee of this initiative.

In 2007 Oxfam Novib launched the WEMAN programme (Women's Empowerment Mainstreaming and Networking for Gender in Economic Development). The programme has two objectives:

1. Empowerment and improvements in livelihoods which are significant and sustainable for women, their families and communities, particularly from low income and vulnerable groups.
2. Gender justice mainstreamed in economic development interventions and institutions including: financial services, livelihood/market/value chain development and economic policy and decision-making.

The WEMAN programme has great potential to influence the world of microfinance with regard to gender. Work is continuous on further expanding the number of partners participating in analysing how gender can be formulated better in projects like Client Principles and Social Performance Management. Experience has shown that organisations that are not partners of Oxfam Novib are also interested in participating in the global network. It is necessary, though, that we look intensively for where to slot the WEMAN discourse in with the current world of microfinance, thus to engender a useful dialogue.

Conclusion

The role of civil society is gradually changing. MicroNed is pushed more and more into the role of 'watchdog' now that the sector has become mainstream. This has also been defined as one of MicroNed's tasks for the future.

4.3 Impact

As in other development co-operation sectors, measuring the impact of microfinance has proved difficult.¹¹ In the past there have been many studies into the impact of microfinance. Recent analyses of the methodologies

reveal that they often fail to arrive at reliable results. There now is also the recognition that not everybody invests her/his loan in productive activities only, but also uses a loan for cash flow management with consumptive purposes.¹² The fact that poor people often have multiple (in)formal loans and other financial products, makes it problematic to isolate the effects of that one loan. GCAP now prefers to speak of outcome instead of impact, because the indicators for measuring outcome cannot be linked statistically with the intervention. The problem, therefore, is not only whether the methodology is right, but also whether we are measuring the right change processes.

Since 2007 Oxfam Novib has worked with the network organisation INAFI International and the ICT businesses Ordina on a tool for measuring impact, the SIM tool. It is a web-based tool that can measure changes in client's living conditions using different methods. In this regard, it is important to report that INAFI wants to continue working with the SIM tool, and does not want to start a separate collaboration with Oxfam Novib and Ordina.

Microfinance has always had the implicit assumption that enterprising poor people lacked a financial infrastructure that would enable them to start an enterprise. Supporting an MFI would automatically bring this goal closer. A number of studies has indeed shown that better financial systems promote growth.¹³ It was also revealed that better formal financial systems would in due course lead to poverty reduction as a result of the economic growth they promote. However, that does not mean to say that *all* financial systems promote economic growth. There are no studies that demonstrate the relationship between a strong microfinance sector and economic growth, in the same way as the World Bank's studies of financial systems other than microfinance. There is, though, research into the influence of a large informal sector of micro-enterprises on economic dynamics. Based on a study in Bosnia, Bateman sees several limitations of a big growth of the informal sector for economic development.¹⁴ There is a rise in the number of

enterprises working in the same sector, thereby reducing profitability.¹⁵ In this way micro-enterprises never grow beyond a minimal size for take-off. Furthermore, very few horizontal and vertical relations between enterprises are created, which is crucial for economic development. Low profitability, high costs and short lending terms for micro-credit make it hard for micro-enterprises to achieve a technological leap forward. The high costs they charge prevent the technological development of small and medium-sized enterprises. And, where production needs most support, i.e. in small-scale agriculture, microfinance is inappropriate.

It is difficult to establish a direct connection between growth in the informal sector and economic development. It is therefore also difficult to establish a connection between microfinance and economic development. It remains the question however, if Bateman is exaggerating the weight of microfinance in the growth of the informal sector is. He supposes too easily a direct relation between the growth of the informal sector and microfinance. In many countries the outreach of microfinance is still very low, and can therefore not explain the sometimes huge increase in the number of informal enterprises. For instance, in the 1990s and early 2000s the number of formal jobs (government and private sector) has dropped enormously. Considering the then limited outreach of microfinance, microcredit cannot explain the huge growth in the informal sector.

The impact study of three MFIs in Maputo, Mozambique¹⁶ presented a varied picture. Many clients left the MFIs in the first years, and it is suspected that they were mostly the poorer clients. The clients linked to MFIs for several years did benefit from the loans, especially when they already had entrepreneurial skills.

In the world of microfinance this has led to a debate on how to move on. In some opinions working on responsible finance with transparency and client protection, is sufficient for serving poor people well. Others believe that microfinance was started to support

11 For the theoretical argument see Richard L. Meyer, *Measuring the Impact of Microfinance*. In: Thomas Dichter and Malcom Harper (eds), *What's Wrong with Microfinance?* Intermediate Technology Publications 2007. In the same book: David Ellerman, *Microfinance, Some Conceptual and Methodological Problems*. Also see R. Rosenberg, *Does Microcredit Really Help Poor People?* CGAP, Focus Note 59, 2010.

12 For the extensive analysis see Dary Collins et al., *Portfolios of the Poor. How the World's Poor live on \$2 a Day*. Princeton University Press, 2009.

13 The World Bank has commissioned several studies. Among others Thorsten Beck, Asli Demirgüç-Kunt and Ross Levine in *Finance, Inequality and Poverty, Cross-Country Evidence*, World Bank Policy Research Working Paper 3338, June 2004. DGIS among others has used this study to base its policy for financial sector development on. See the ministry's policy paper: *Financial Sector Development – access to financial services for effective poverty reduction* (2008).

14 See among others: M. Bateman, *De-industrialization and Disintegration in Bosnia*, in: Thomas Dichter and Malcolm Hareper (eds), *What's Wrong with Microfinance?* Intermediate Technology Publications, 2007. By the same author: *The Microfinance Illusion* (2009).

15 This was also one of the outcomes of the impact study in Mozambique, executed by Oxfam Novib, Hivos, Stichting Doen and FMO. G. Athmer and F. de Vletter: *The Microfinance Market in Maputo, Mozambique: Supply, Demand and Impact* (2006).

poor people to overcome their poverty, and that we should hold on to that.

Conclusion

The world of microfinance struggles to show the impact of its activities. Measuring the impact of microfinance at the level of the enterprise is problematic and the contribution to economic growth remains unclear. As a financing tool microfinance can play a role in setting up and expanding enterprises in the informal sector and in poor people's cash flow management. In *Portfolios of the Poor*, Dary Collins and others pleaded for more tailor-made credit and other financial products for poor people, and for the gradual departure from the one-size-fits-all principle, which currently only benefits enterprises that can quickly turn over expensive loans (due to the short lending term). Product development could also overcome several of the problems Bateman analyses. This certainly applies to financing agriculture. Oxfam Novib wants to make this an explicit component of future policy.

4.4 Savings

The study "Portfolios of the Poor" found that all poor families who earn less than 1 and 2 dollar a day have savings. It is an important way of coping with unexpected expenses or with big expected expenses, like school fees and burials. Savings are on the rise in the mainstream world of microfinance. In 2009 the Ministry of International Co-operation commissioned a study into the experiences of Dutch players. One of the objectives of national networks is to promote regulations for attracting and using savings in the more formalised MFIs. Oxfam Novib is specifically involved with savings in India and Mozambique, by means of supporting organisations that support SHGs and their outreach of about half a million women. By supporting networks we are attempting to influence government policy into making it possible for MFIs to attract and manage savings.

Several years ago a movement arose, savings-led microfinance, based on the idea that savings precede credit. Organisations working based on this idea include

CRS, CARE, PLAN, Freedom from Hunger and Oxfam America. By supporting local VSLAs they can reach people (mostly women) who live far below the poverty line and in very remote areas. The methodology is based on people's local resources ("people always save") that can be used for local economic activities, but also for consumption purposes (school fees, healthcare, cash flow, etc.). This methodology makes it possible to reach many people in a relatively short time. Oxfam America and Oxfam Novib want to join hands and work with this methodology in West Africa (for the moment in Senegal and Niger). Another example of this methodology is the SHGs in India, of our longstanding partners DHAN and Myrada).

4.5 Rural Finance

In recent years the awareness has re-emerged (after an unjust rejection lasting decades) that rural development and agricultural development are pillars on which sustainable growth must rest. The ministry has assigned MFOs an important task in this.¹⁷ The paper *Agriculture, Rural Enterprise and Food Security in Developing Countries*¹⁸ gave a new impulse to civil society organisations working in the field of farmer-led (men and women) agricultural development.

The financing of off-farm and non-farm activities¹⁹ in rural areas is of crucial importance to developing the entire rural sector, including the crop and cattle farming sectors.

The developments inside the microfinance sector are very ambivalent. On the one hand competition between MFIs in urban areas and the oversupply of financial services for urban poor, force MFIs to spread their wings to rural areas. On the other hand, investing in rural areas is not very attractive when you want to make returns that are interesting to other institutional investors seeking to invest commercial capital. The rural sector is still very much underserved in terms of access to financial services. Precise figures of the number of MFIs serving rural areas do not exist. However, in Africa the rule of thumb is that the percentage of rural people enjoying the financial services of MFIs is about half the percentage of

¹⁶ Athmer et al., 2006.

¹⁷ Ministry of Development Co-operation, Policy Paper Civil Society Organisations, April 2009.

¹⁸ Landbouw, rurale bedrijvigheid en voedselzekerheid. Joint paper of the ministries of Agriculture and Development Co-operation, May 2008.

¹⁹ The difference between non-farm activities and off-farm activities depends on the sector. Non-farm activities are those activities farmers undertake outside their farm business. Off-farm activities are activities taking place outside the farm business, but still pertaining to crop or cattle farming.

urban people who are MFI clients. In Africa only 5 to 10% of rural people have access to formal financial services. It must be emphasised that most rural people do avail of informal financial services (see below the heading 'Savings').

It demands analysis to see how the financial sector in rural areas can be supported. Rural Finance means operating in a complex field of very different production systems and very different target groups for which different tools must be used. Furthermore, the funding of agricultural activities is one of a kind, not comparable with funding small enterprises in cities. Financial institutions, including MFIs, often lack the requisite knowledge. Oxfam Novib is currently working out the policy proposed in the subsidy proposal. Funding of the value chain and informal forms of financial services are explicitly subjects of this study.

4.6 The Graduation Model

Several years ago CGAP and the Ford Foundation started a research and several pilots into methods for reaching people living far below the poverty line. It is an attempt to understand how safety nets, livelihoods and microfinance can be used to develop a way of helping the poorest people to escape poverty. To this end they are using an adaptation of BRACs methodology. At the moment nine pilot projects are being implemented in seven countries, in collaboration with local partner organisations.



Women about to receive loans from Oxfam partner Tanzania Home Economics Association (TAHEA). (Jennifer Juma is second from right.) The women, predominantly widows, belong to groups in Shinyanga town. Many are accustomed to seek a living by winnowing rice waste outside the Shinyanga's rice mills, to harvest the few grains which slip through processing. A loan of 50,000 Tanzania shillings ('25) is given to each member of each group, after a three-day training in business.

5. Future Developments in Microfinance

In 2009 MicroNed researched trends in microfinance for the coming years.²⁰ It delivered the following results:

- a. At the micro-level we are witnessing a growing commercialisation of microfinance, accompanied by a growing size of MFIs. In order to attract commercial capital many MFIs will change their NGO-status for a status of non-bank financial institutions (NBFIs). These are organisations with a special legal status, neither bank nor NGO. They are often Limited Liability Companies.
Much depends on national legislation and regulation. The developments in this area are different between the continents. Much has already taken place in Latin America; Africa and Asia are lagging behind in this regard. Supporting networks to lobby for proper legislation and regulation is very instrumental for this purpose.
The graduation model, as Oxfam Novib has applied in recent years (from A to B to C), will become less relevant. The importance of start-ups will drop and medium-sized and large MFIs will grow at the expense of small MFIs. The share of the small MFIs has dropped in the course of time (from 46 percent in 2005 to 33 percent in 2007). This trend has continued since.
- b. The importance of networks and associations is rising. There is a number of Northern networks with an ever-more important role in developing the quality and outreach of microfinance, such as FINCA and Opportunity. Membership of a network could become an important factor in an MFIs survival. It is expected that national and regional networks could play a less prominent role. The question still remains, if the lobby for national legislation and regulation is appropriately located with international networks that also often have their origins in the North. We therefore foresee a

continuing importance of national and regional networks.

Another reason for supporting national and regional networks is also to give Southern MFIs a voice in the development of the financial sector. Our support of INAFI has always been motivated by this.

- c. More Southern initiatives will appear, such as BRAC being active in different countries in Africa, several Bolivian MFIs working in Argentina too, and DHAN from India working in Tanzania. It does well to monitor this trend. BRAC, for instance, has become hugely efficient after a short while in expanding its outreach whilst keeping an eye out on a positive return.
- d. It is not expected that this all is accompanied by mission drift, the scale up from poor to lesser poor clients, thus to raise profitability. The reason is that both the organisations and the investors have the aim to invest more in the triple bottom line. A recent study²¹ does raise questions. It found a negative relationship between the age of an MFI and its social performance, both in reaching the poorer clients and in reaching female clients. That is related to the fact that it is more expensive to reach poorer and female clients on the one hand, whilst on the other hand there is the imperative to have good returns in order to attract commercial capital. Network members, however, proved better able to hold on to their mission. Supporting network is therefore of great importance, and within this area above all support in the area of SPM.
Of the target group Oxfam Novib reaches through credit 85 percent is women. For the ASN Novib Fund it is 72 percent (figures December 2009).

20 MicroNed and Triodos Facet: Trends in Microfinance 2010-2015, May 2009.

21 Pim Engels: Mission Drift in Microfinance. The influence of institutional and country risk on the trade-off between the financial and social performance of microfinance institutions. Master Programme Economics: Growth, Development and Resources, Tilburg, 2009.

- e. Regarding the networks, we will witness a shift from the influence of national and regional networks towards the influence of global MFI networks. These networks are becoming more important in technical assistance of their members. However, the more professionalised an MFI, the less its dependence of national networks, because, as they mature and become more regulated, they get other interests than the networks with NGO type MFI members. That means, following what was said under a, rising pressure on social performance management. MFIs that are not members of networks will become marginalised in terms of growth, because it is more difficult for them to achieve technological innovation on their own.
- f. Technological innovation will play a very important role. Mobile banking will change rural areas in Africa, because of its ability to penetrate deep into marginalised areas.
- g. Credit bureaus are becoming more important, and will (we hope?) play an important role in monitoring the quality of MFIs and representing the interests of MFI clients. The Consumer Protection Principles hopefully herald legislation and regulation.
- h. It is expected that the growth of funds on the supply side of microfinance will continue. That means that national coverage will increase also in countries with a limited MFI outreach. This will lead to a higher risk of over-indebtedness, but also (hopefully) to more products for clients, a better alignment of these products with the clients' wishes. This could, despite all attempts to reduce costs for the client (and to keep them low), lead to upward pressure on interest rates. MFIs charge a higher interest on loans than mainstream banks. Interests may be falling, but more tailor-made products could translate into higher costs for MFIs, and thus into pressure on profitability and therefore also pressure on the supply of commercial capital.

In short, there are various trends that are not equally straightforward. The whole does point at an important role in safeguarding the social face of microfinance, a task Oxfam Novib will continue to take seriously. Supporting national and regional networks remains important, not only regarding the quality of MFIs, but also regarding legislation and regulation. Legislation and regulation have a big influence on the development and quality of the financial sector, and is of great importance to clients' rights (credit bureaus, Client Protection Principles).

6. Rural Financial Sector Development, Policy 2011-2015

“A useful perspective on constraints is provided from the observation of how development generally occurs in the frontier economy: progress customarily results from small, incremental actions over time rather than through a ‘big push’. An incremental approach permits the investor’s management skills, risk-bearing capacity, and organizational efforts to inch forward along with the investor’s financial situation. This progress deals with shifting constraints and requires creative responses to keep progress in balance. Success is not the result of a single transaction, but of a continuing activity.”²²

In the previous chapters we have outlined how the world of microfinance has changed in recent years. This has necessarily consequences for Oxfam Novib’s policy on financial services for poor people. The emergence of financial products better geared to satisfying the wishes of the different categories of poor people, the professionalisation of microfinance, the growing interest of the commercial world, the awareness that returns can also be at the expense of the social mission. They are developments Oxfam Novib cannot afford to ignore. Now that Oxfam Novib is specifically focused on rural development, its policy must also focus on its specific problems and on finding connections for supporting developments with the rich variety of institutions. They will not be the same in all countries. An analysis at the country level will reveal the most appropriate roads to take. The policy on financial services is therefore one that differentiates.

6.1 The Right Based Approach

According to Oxfam Novib sustainable livelihoods are a right, encoded in international human rights law. Oxfam Novib has two objectives to achieve the right to sustainable livelihoods. The first is achieving food and income security. The second is securing decent employment conditions. Both of these are critical for overcoming poverty. Predominantly, the focus of Oxfam Novib’s work is in rural areas and agriculture.²³ In the policy document *“The Right to a Sustainable Rural Livelihood”* Microfinance is seen as a tool for

development, with the ultimate aim to empower poor people and contribute to global equity and social justice. Microfinance especially targets Aim 1: *The Right to a Sustainable Livelihood*. The objective of the work of Oxfam Novib in rural areas is to develop different types of capital of the poor: human capital, social capital, natural capital, physical capital and financial capital. Stabilising and raising incomes is a major component of this aim, and microfinance is one of the major instruments available for achieving this.²⁴ The rights based approach means that Oxfam Novib puts special emphasis on addressing the unmet demand of groups of micro entrepreneurs and farmers. This also means a focus on emerging MFIs in countries, regions and sectors currently not covered.

Oxfam Novib is not an organization specialized in microfinance. It views microfinance as an instrument in the fight of poverty alleviation. The policy paper *Microfinance Global Thematic Programme* from 2004 also reaffirmed what Oxfam Novib had always been: not an organisation focusing on microfinance, but a general development organisation. Oxfam Novib only engages with microfinance when it falls within its broader development objectives. Access to financial capital for the poor means that they are enabled to develop the other types of capital: human capital, as an increase of income means better access to services like education and health and better nutrition; social capital, as they are in a position to use networks in a more focused way to build a sustainable livelihood; natural capital, as finance can enable the poor to access and use natural resources

22 J.D. von Pischke: Finance at the Frontier. Debt Capacity and the Role of Credit in the Private Economy. EDI Development Studies, The World Bank, Washington D.C., 1991, p.64.

23 ON Position Paper: The Right to a Sustainable Rural Livelihood: Strategies, Lessons Learned and Actions (2007 – 2010).

24 Microfinance Global Thematic Program, 2004.

by which they live; and physical assets, as they use the infrastructure that they need to provide themselves for food and income.

Oxfam Novib aims to support strategic MFIs that contribute to building an inclusive microfinance sector. In this context inclusive means that MFIs provide access to financial services to poor people who cannot access financial services of commercial banks. Inclusive also means that the aim of Oxfam Novib is that the poor can access the financial services they need, be it credit, savings or insurance.

6.2 Basic Principles of a New Policy

Despite this differentiated policy, there are several basic principles for the entire policy.

6.2.1 Target group approach

The subsidy request 2011-2015 places the development of the rural space centre stage. The general objective of the Aim 1 Programme concerning the financial dimension has been defined as follows:

1. Improved access to financial services, markets and trade
2. Increasing the opportunities for people living in poverty to participate actively in and benefit from trade systems and markets.
3. Enhance the resilience of people living in poverty against the damaging effects of the current financial and trade systems.

It is specifically mentioned that financial services are about sustainable financial services and products for people living in poverty. Not the tool, but the target group is at the centre of the policy, whereby tools are developed that connect with the specific questions and needs of the target group.

In its new policy Oxfam Novib distinguishes different categories within the target group (Rural Worlds, Oxfam Novib, 2008).²⁵ In Rural World 4 the people *hanging in* try to hold on to enough livelihood resources for surviving; in Rural World 3, the people *stepping up* invest to increase the return of existing activities; in Rural World 2, the people *stepping out* use existing activities to

accumulate resources and invest in new activities with higher returns. It is a people centred approach, because it starts with the challenge that several segments of the rural population face daily. The different organisation forms also connect with the management capacities of the different segments in the target group. Depending on the progress, these connections will change.

In addition there is the distinction between crop and cattle farming on the one hand and other (off-farm and non-farm) economic activities of importance. Barret et al. (2000) show that in large parts of rural Africa, 45 percent of income is derived from off-farm and non-farm activities including remittances. Job promotion for poor people earning a living outside agriculture is therefore important to integrated rural development.

This vertical and horizontal categorisation of the rural target group demands a differentiated policy with regard to the tools used in structural poverty reduction. It also means that different actors in the north play a role in supporting the development of the financial sector in rural areas.

6.2.2 Combining the Poverty Lending Approach and Micro-Banking Approach

In the course of time two approaches to microfinance have emerged, which we can distinguish analytically as the 'Poverty Lending Approach' and the 'Micro-Banking Approach'.

The Micro-Banking Approach has the objective to deliver financial services to people with low incomes, and not as much to the poorest people, in a sustainable manner. When loans are demanded and paid back, there is a market. The binding force in this approach is the promotion of sufficient institutional capacity to achieve a large outreach and access to commercial capital, both to allow for sustainable investments. This approach puts the emphasis above all on creating sustainable financial institutions. It has a huge potential of achieving a large outreach. It is the arrival of commercial capital that makes this possible. The disadvantage, however, is that many financial products are not developed for specific target groups. It is an important reason why rural areas are underserved by the classical MFIs. By offering a reasonable homogeneous financial product these

²⁵ See annex 4 for a description of the Rural Worlds as used by Oxfam Novib.

classical MFIs can achieve returns and keep commercial investors interested.

The Poverty Lending Approach emphasises poverty reduction as the most important objective of microfinance. Financial sustainability is of little importance when this objective is not being reached. Financing is a means, with products and services of relevance to the target group, and should be supported by complementary services. A diversified supply of financial services is central in this approach, as activities are based on the needs of the target group. For many proponents of this approach a lack of credit is not the most important bottleneck many poor people face.²⁶ Saving opportunities are especially important to the poorer population segments. In its paper²⁷ Oxfam GB also advocates an integrated approach to finance for small-scale agriculture.

To date Oxfam Novib has mainly followed the first approach. Attention was indeed paid to matters like outreach to women and poor people, using the indicator of average loan-size, but little use is made of complementary services for the target group to align the financial services better with the demand. The Poverty Lending Approach therefore fits better in the target group approach, because it is directed at the poorest segments of the target group. It also has the advantage that different risks in rural financing²⁸ can be analysed separately.

At the organisational level this also means more interaction between the different experts in the regional bureaus.

MicroNeds²⁹ study makes the following comment:

“Support to MFIs and support to rural economic development are two specialisations, and therefore mostly covered by different CFA staff. The microfinance promoters are sometimes supported by the Microfinance experts of the CFAs, sometimes by the rural development specialists. Sometimes this staff is from the same department, sometimes from another department and

sometimes partly from another specialised organisation linked to the CFAs. Interaction between the Microfinance specialists and the rural market development specialists can lead to innovative and technically sound approaches in rural finance. Therefore, one of the recommendations of CGAP to donor agencies with regard to rural finance is to encourage interaction between microfinance/finance staff and rural development/agricultural staff.”³⁰

Alongside the Poverty Lending Approach the Financial System Approach also remains important. Outside the agricultural sector in rural areas the off-farm and non-farm sectors are very important to employment. Barret et al. (2001) reveal that the share of wage labour in income is on average bigger than income from micro-enterprise. This is true of regions with climatically favourable conditions for agriculture, and for regions with more unfavourable conditions (arid regions). Total dependence on agriculture appears to be rare. In order to finance enterprise outside agriculture, formal financial services are important and therefore sustainable financial institutions, such as banks and MFIs.

6.2.3 Emphasis on development of the local financial sector

In the Ministry's policy for economic development the development of the financial sector in countries in the South is one of the most important issues on the agenda.³¹ For a good reason. Studies reveal that the development of the financial sector is of great importance to developing the private sector.³² Developing the private sector even leads, according to Beck, Demirgüç and Levine, in due course to a reduction of poverty, as the result of increased enterprise (Beck et al., 2004). If this is true, it will still take considerable time to happen and there is no guarantee that our target groups notice the effects. The effectiveness depends on a whole series of factors, including the institutional and business environments. A sound business environment includes a good legal framework, like clearly defined property rights, enforceable contracts, efficient and cheap

26 Adams, Dale W. & Pischke, J.D. von, “Microenterprise Programs: Déjà vu”, *World Development* 20(10), pp. 1463-70, 1992.

27 Alan Doran et al.: *The Missing Middle in Agricultural Finance. Relieving the Capital Constraint on Smallholder Groups and Other Agricultural SME's*. Oxfam GB Research Paper, 2009

28 See annex 3.

29 MicroNed (2008): *Rural finance Study, an inventory of policies, practices and challenges regarding support to rural (micro)finance among Netherland's MicroNed members*

30 CGAP 2006: “Good practice guidelines for funders of microfinance. Microfinance consensus Guidelines”. Pg. 29.

31 MinBuza: *Financiële sector ontwikkeling – toegang tot financiële diensten voor effectieve armoedebestrijding*, 2008

32 See among others: *Adviesraad Internationale Vraagstukken, 'Private sector ontwikkeling en armoedebestrijding'*, nr 50, 2006; Beck, Demirgüç-Kunt and Levine, 'Finance, Inequality and Poverty: Cross country evidence', World Bank Policy Research paper 3338, 2004; Worldbank: *Finance for All?: policies and pitfalls in expanding access*, World Bank Policy Research Report, 2008

registration of businesses.³³ Security, corruption and a lack of credit feature each as the number 1 problem businesses face with about 30 percent of all businesses.

An analysis of the financial sector in Africa reveals a bleak picture.³⁴ The sector is not explicitly directed at financing productive sectors in the country, and the legal structures give insufficient hold to the financial sector to be active. The amount of credit, as percentage of the gross national product (often used as indicator of the financial market's development), is low in Africa. The weakness of the sector in Africa is also highlighted by the fact that 48 percent of the outreach of financial sector is in the NGO sector, whilst the global figure for this is 23 percent.³⁵

The development of the financial sector is therefore important to poverty reduction, but it is not something that happens automatically. A pro-poor approach matters in order to relay the effects better to our target groups. By using loans Oxfam Novib has above all focused on building sustainable financial systems in the South. Without a good financial sector there will be no growth, and without a financial sector focused on our target groups, growth will happen but with only a very indirect impact on our target groups. Investment funds do not generate sustainable financial markets. Oxfam Novib therefore does not invest in principle in Northern funds that directly invest in productive activities. Oxfam Novib's policy continues to focus on building an inclusive financial sector, aimed at production growth in agriculture and employment in the off-farm and non-farm sectors in rural areas.

6.2.4 Combining Grant Making and Asset Management

There is an important difference between grant making and asset management. In grant making a budget is made available to support activities and programmes. It is not the intention that a money flow emerges from the partner organisation to the donating organisation. In asset management it is about managing capital, equity. The idea is to maintain the capital and return it to its owner when the investments in particular sectors are returned, plus a certain anticipated return. Grant making

and asset management are two different fields of operation. This was one of the basic reasons for setting up FDE, and later Triple Jump. The consequence was that the appraisal of partner organisations by the regional bureaus was different in character from the appraisal by FDE/Triple Jump. In grant making the emphasis was on outreach and the social aspects of impact; in lending and extending guarantees the emphasis was on risk management and financial analysis and the social aspects were not analysed intensively for a long time, except when counting the outreach, number of women and rural vs. urban. In grant making the emphasis is on taking risks and the opportunity of financing new development methods; in asset management the emphasis is on roads well trodden and calculated financial risks in the market niche where you are active.

This difference in dynamics lies at the basis of microfinance programmes and country programmes growing apart. Many promising MFIs may exist somewhere, but they did not always contribute directly to the activities for the target group of the partners in the country programmes. And when perhaps more integration between income generating activities and microfinance was desirable, there were sometimes few MFIs with great perspectives. The need is emerging to connect these programmes closer and bring the poverty focus more explicitly to the foreground. This can be achieved in various ways, which will be sketched in the following paragraphs.

The fact that grant making and asset management are two separate fields of operation means that the management of these two tools must be in the hands of specialised organisations. Oxfam Novib will therefore continue to co-operate with Triple Jump.

6.3 Policy Objective 1

Oxfam Novib contributes to developing the rural financial sector

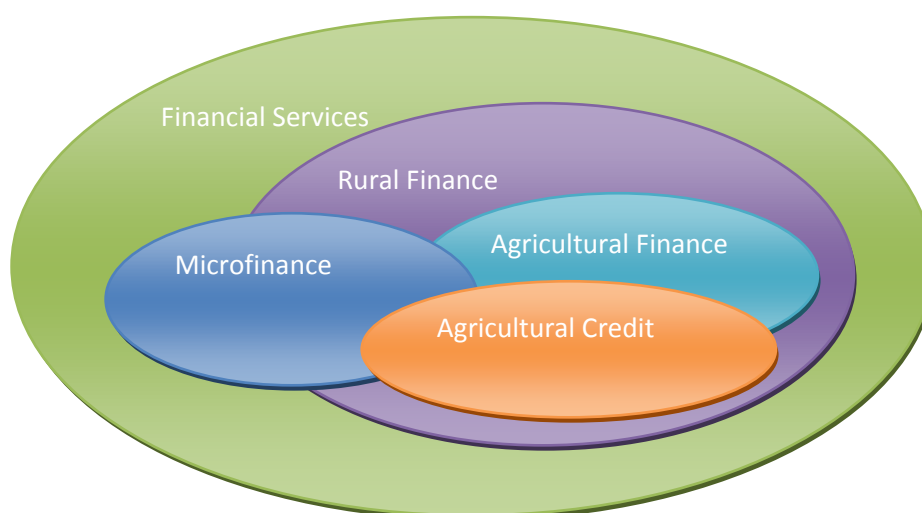
After an undeserved rejection for decades, in the recent years the awareness has returned that rural development and agricultural development are pillars of sustainable

33 Beck, Thorsten, Aslı Demirgüç-Kunt, Luc Laeven, and Ross Levine. 2005. "Finance, Firm Size, and Growth." World Bank Policy Research Working Paper 3485. Thorsten Beck: Financing Constraints of SMEs in Developing Countries: Evidence, Determinants and Solutions. World Bank, Development Research Group (2007)

34 Patrick Honohan and Thorsten Beck: Making Finance Work for Africa. The Worldbank, 2007

35 Idem, p. 166.

Figure 1: Rural finance in perspective



growth and poverty reduction. The Ministry has given the MFOs an important task in this.³⁶ The paper *Agriculture, Rural Enterprise and Food Security in Developing Countries*³⁷ gives a new impulse to civil society organisations in the field of farmer-led (men and women) agricultural development. It also prompts us to analyse how to support the financing of rural development.

Oxfam Novib too wants to focus above all on rural areas in the coming period. This policy is a response to the need of more investments in this sector. In order to feed the entire world's population of 9.1 billion people in 2040, the FAO estimates that annually 83 billion dollars worth of investments are needed in agriculture. In addition to the importance of the rural sector to the national economy, we must also consider that the greater number of poor people lives in rural areas. More than 70% of the poorest people who live on less than 2 dollars a day live in rural areas, making them directly dependent on agriculture.³⁸

In rural areas the demand for financing is huge, and the supply scarce. Remote areas, bad infrastructure and the risk of small-scale farming lead financial institutions to find their fortune elsewhere.

Funding activities must be directed at economic activities in a rural setting, and developing the financial sector must therefore be relevant to rural financial institutions. For rural financing we will use the definition given by Nagarajan & Meyer:³⁹

“Rural finance is the provision of financial services to a heterogeneous, rural, farm and non-farm population at all income levels through a variety of formal, informal, and semiformal institutional arrangements and diverse types of products and services, such as loans, deposits, insurance, and remittances.”

Figure 1 gives an idea of the diversity in rural financing.

Microfinance is only a part of rural financing and agricultural credit is only one financial service to benefit the population.

The population in rural areas is very diverse. For the different population segments different types of organisation have developed in the course of time, which meet the demand for financial services.

36 Ministry of Development Co-operation, Policy Paper Civil Society Organisations, April 2009.

37 Agriculture, Rural Enterprise and Food Security. Joint paper of the Ministries of Agriculture and Development Co-operation, May 2008.

38 IAASTD: Agriculture at a Cross Roads. Global Report (2008).

39 Nagarajan, G. and Meyer, R.L. (2005) 'Rural Finance: Recent Advances and Emerging Lessons, Debates, and Opportunities'. Reformatted version of Working Paper AEDE-WP-0041-05. Department of Agricultural, Environmental, and Development Economics, The Ohio State University.

6.3.1 Financial Institutions for Rural Development

Over time the MFOs have been involved with a multiplicity of financial institutions, see table 9.

Considering the diversity of the rural population and of Oxfam Novib's target group, one-size-fits-all is not an option.

The following organisations, if relevant, will be supported. See table 10a and 10b for the relevance of the organizations in terms of products and target group.

Regarding suppliers of insurance, it needs mentioning that only commercial and co-operative insurers can be suppliers of insurance products. Other organisations would only be able to function as intermediaries.

Table 9: Development of the rural financial sector by MFOs

Approach	1. Support to Credit-led Microfinance Institutions	2. Support to member owned microfinance institutions (MOMFIs)	3. Support for the provision of financial services to actors in the value chain
Focus	Building financially and operationally sustainable microfinance institutions that provide financial services to their clients	Building institutional sustainability – directly or through an NGO – or MOMFIs to provide financial services tailored to their members	Include or strengthen the position of the target group of the CFA in value chains
Partner organisations	MFIs, networks of MFIs	SACCOs** / Credit Unions, promoters of VSLAs and SHGs,*** networks of MOMFIs and TA providers of MOMFIs	NGO's, MFIs, trading companies, farmer organisations

* MicroNed: Rural finance Study, an inventory of policies, practices and challenges regarding support to rural (micro)finance among Netherland's MicroNed members. 2008.

** Savings and Credit Cooperatives.

*** VSLAs: Village Savings and Loans Associations. SHGs: Self Help Groups.

Table 10a: Support to the development of the rural financial sector at a glance: suppliers

Suppliers	Credit	Saving Facilities	Insurance
Local rural banks	X	X	X
MFIs	X	X	X
MFI networks			
Saving & credit co-operatives	X	X	X
VSLAs	X	X	X
Commercial insurers			X
Co-operative insurers			X

Table 10b: Support to the development of the rural financial sector at a glance: clients

Suppliers	Rural World 2	Rural World 3	Rural World 4
Local rural banks	X	X	
MFIs	X	X	X
MFI networks			
Saving & credit co-operatives	X	X	X
VSLAs		X	X
Commercial insurers	X	X	X
Co-operative insurers	X	X	X

Table 11: Financial pros and cons of VSLAs

Positive consequences	Negative consequences
<ol style="list-style-type: none"> 1. High returns on member savings (better thought of as invested capital), since costs are negligible. 2. Accessible financial services (it all happens in the community). 3. Product flexibility, particularly with respect to loan repayment schedules. 4. High degree of transparency as all transactions are witnessed by the entire membership. 5. Accountability. 6. Tolerance for a large number of very small savings and loan transactions. 	<ol style="list-style-type: none"> 1. Small scale limits the capital base of the SG (yet, groups spontaneously split into smaller groups when there are over 30 members to limit the length of their meeting and maintain simplicity of management) 2. Loan sizes are limited by the small pool into which savings and loan interest income is deposited. 3. Limited benefits payable by group-based insurance systems (i.e. the Social Fund). 4. Risk of elite capture, although there is no compelling evidence that this is happening on a significant scale.

6.3.2 Financial Services for the very poor: Member Owned Microfinance Institutions

Village Savings and Loans Associations, Self Help Groups

The story is still around that 2.7 billion people have no access to formal financial services, which hinders them in their development. This observation is often translated into the need to support more MFIs, whereby the lack of access to formal financial services is translated into a lack of credit. Be this as it may, the majority of the people has access to informal financial services. The literature presents a lot of proof to support the notion that many poor people have more need for savings products and transfer services than credit. One of the thoughts behind this policy plan is that development not only can be enhanced by indebtedness, but that assets building through saving products is a good, and often, better way.

For the rural worlds 3 and 4 the Village Savings and Loans Associations (VSLAs) can be a response to the demand for savings and credit products. In the last decade much work was done on new methods to reach people, women especially, who have no access to MFI financial services. The reasons could be that they are too poor to get a loan, that they do not have a business, or that they live in very remote areas. It is a mostly a combination of reasons. Needed above all is cash management in the family, to be able to pay costs other than those of the first necessities, such as education, healthcare, funerals and weddings. In recent years some experience was acquired with expanding the more

informal financing systems, such as VSLAs. In Mozambique Oxfam Novib has been supporting Ophavela for years. It supports VSLAs in their start and expansion. Self Help Groups (SHGs) in India can be viewed as a more developed form of this. VSLAs can be seen as a more developed form of the traditional rotating savings and credit associations (ROSCAs), which were active in the South under many names. Freedom from Hunger, Catholic Relief Services, CARE, Plan and Oxfam America work a lot with VSLAs in Africa, and are currently reaching more than 2 million people in this way.⁴⁰ In countries like Cambodia, Laos and in several countries in Latin America, organisations are working with this method. The opportunities of reaching poor people in remote areas are bigger through this form of microfinance, than through the classical MFI. Table 11 presents the financial pros and cons of VSLAs (Allen et al., 2010, p.10).

Alongside these advantages and disadvantages there is also social impact that many studies have documented, such as: big ownership because the members can understand the system because it is simple, more solidarity, less isolation of women, joint activities at the community level.

Oxfam Novib already has much experience with working with Self Help Groups in India, with organisations like MYRADA and DHAN. The way in which these SGs work is in several aspects different from VSLAs, but comparable. The biggest difference with the VSLA is that SHGs can get loans from a bank after some time.

40 Allen, Hugh and Panetta, David (2010): Savings Groups: What they are, how they vary, how they are promoted and how their performance is measured. The SEEP Network (forthcoming). This paper gives an extensive description of the performance of these associations, including the pros and cons.

This approach to microfinance, the so-called savings-led microfinance, will be taken as basic principle in reaching the extreme poor, mainly women, in rural areas. Oxfam America and Oxfam Novib will co-operate in expanding this activity. MicroNeds Rural Finance Working Group also has plans to build knowledge and experience in this area.

A discussion is happening in the world of savings-led microfinance about linking VSLAs with broader financial structures, such as MFIs. Opponents argue that VSLAs prevent money from leaving the village as interest payments, and people are not forced to take part in something they do not understand. Proponents believe that linking different sectors will happen anyhow and that groups can be better supported in this development. These are positions that need to be handled with care. The discussion is currently conducted on the basis of participants' own experiences. They are indeed very different. Niger has examples of falling numbers of women participating in VSLA when the VSLAs are linked with MFIs, for the reason that these women lose their sense of ownership. Elsewhere there are examples of successful linkages with broader financial structures. Examples also exist of VSLA using the services of small SACCOs in rural areas.

Oxfam Novib will pursue the policy of preparing local VSLAs to linking up with bigger financial structures. Rural areas in Africa and Asia will change rapidly and the technological innovation will leave their mark on rural areas. VSLAs will be included in this development. This is sufficient reason for paying attention to further integration.

Savings and Credit Co-operatives

Another form of savings-led microfinance Oxfam Novib wants to work with is the Savings and Credit Co-operatives (SACCO). This form of rural financing occurs in a number of country strategies. MicroNed's study on rural finance indicates that the outreach of SACCOs is potentially huge, and by far most members are active in agriculture. More than 90 percent of SACCO members live in rural areas. Oxfam Novib already has experience with supporting these organisations, such as FAIDERS in Tanzania and CREAM West Nile in Uganda, which coaches SACCOs towards a financially sustainable status by means of providing Business Development

Services. This kind of support does not so much demand funds for microfinance, but demands development funds to develop further the management capacities of these types of groups. SACCOs can serve as retail organisation for the financial services of MFIs, or for banks' investments in rural areas, and in particular in agriculture. In the Partos evaluation on microfinance working through organisations like FAIDERS emerges as a very good intervention strategy. SACCOs can also be suitable for the maturation path which was the cornerstone of Oxfam Novib's policy until 2010 (from A to B to C). The asset management approach can play a role here. Many SACCOs lack management capacities and their financial performance is insufficient. TJAS can also play a meaningful role.

6.3.3 Role of MFIs

MFIs have an important role to play in rural areas. The fact that MFIs generally only move to rural areas with great difficulty, means that one of the drivers of rural development, i.e. small-scale non-farm activities, rarely qualifies for funding.

Within the policy lines as formulated in the country papers, much attention is paid to rural people without assets like land or a business. There is no unequivocal vision on how to reach this category. Providing support to promoting people's own enterprise or job-creating enterprise is one way, and MFIs working in rural areas can be a good means of providing financial services. Small enterprises promote the circulation of capital in rural areas, and thereby also work for those that hang in. Continuing the work with MFIs is therefore important.⁴¹ The micro-banking approach has an important role to play in this regard. Efforts must be undertaken to promote saving as much as lending. The connections between the different financial institutions can be interesting (credit from the MFI, saving with the bank, in due course VSLAs can start using the MFIs services). Saving via MFIs should also be a lobby issue for networks working on legislation and regulation. It is also important to support national networks advocating regulations that enable MFIs to attract savings in rural areas.

A different story is the role of MFIs in extending credit for agricultural purposes. Microfinance and farmers don't

⁴¹ Oxfam Novib: The Right to a Sustainable Rural Livelihood, 2008.

match,⁴² Although it must be said that this rule does not apply always. In general the high interest rates MFIs charge, the high risks in agriculture and the short loan terms form barriers. The rate of interest is usually higher than the returns on agricultural activities and the risks are high (see annex 3). The loan terms needed are at least medium, and the direct repayment of loans is not an option in agriculture. Many MFIs that finance agricultural activities have seen the need to diversify to (semi) urban areas. Oxfam Novib will co-operate with MFIs that finance agricultural activities, in order to develop forms of financing that link up with popular demand (saving products, remittances and mobile banking). Certainly so when we can speak of an integrated production of food crops and cash crops, it would do right to investigate opportunities for better linking the supply of MFI financial services with the demand. MFIs working in urban areas and clearly with services for marketing agricultural products in the towns will also be candidates for support from Oxfam Novib. An MFI has no role to play in the production purely for subsistence agriculture. VSLA and financial co-operatives are more suitable for this, not so much for financing agricultural activities, but for cash flow management for families through savings and credit.

The support of MFIs will happen in co-operation with Triple Jump. Triple Jump Management BV will manage the loans portfolio. The policy of coaching MFIs in the first phases of their growth (category A and category B) will be continued. This will mostly concern MFIs that want to play a role in rural areas. The goal of moulding tighter connections between the different players in rural areas and financial services providers will demand greater co-operation between the regional bureaus and the partners in Triple Jump's portfolio. As supporting MFIs in their initial phases demand specialised expertise, the co-operation with TJAS will be expanded, whereby TJAS gets a role in building starting MFIs and in expanding MFIs in Oxfam Novib's loans portfolio.

Because of developments in the microfinance sector, in many countries it is no longer of strategic value to focus on starting MFIs. Sometimes it is better to support an expanding MFI through grants, because a new MFI would then add nothing to increasing access to financial services. With TJAS we will also investigate what strategic funding means in certain countries, to prevent

us from contributing to a sector with many small and weak MFIs.

Networks of MFIs

Oxfam Novib has ample experience in supporting MFI networks. Networks are very important. Networks are instrumental in improving the quality of their members, and many networks practice their own system of supervision, in the absence of financial supervision by a country's authorities. In doing this they provide valuable information on microfinance in their country.

Furthermore, networks are important in the lobby of national governments, related to legislation and regulation in the area of microfinance. In the struggle against over-indebtedness credit rating agencies, where loans are registered, are an important solution. But this requires legislation. Finally, many networks are active in promoting Social Performance Management (SPM) among their members. Oxfam Novib is already supporting several networks on these areas, and will continue to do so in the future.

6.3.4 Rural Banks, Co-operation with Commercial Banks

Currently there are only few local formal banks that deliver services to the rural sector. It is possible to point out many causes (see annex 3). The result is that local formal banks know little about the rural sector, and have little practical experience with the risks in this sector. Especially crop and cattle farming are left out.

Oxfam Novib still has little experience in co-operating with local formal banks for the benefit of rural development. However, with an eye on the objective, namely developing the financial sector for rural areas, co-operation in this area is warranted. A possible collaboration with Rabobank Development offers good perspectives. Rabobank is expanding its activities in Africa, by buying equity of banks with rural outlets with the goal to change them into financing institutions for rural development, specifically for agricultural production. One of the problems these banks face is the lack of a creditworthy demand. Small farmers form explicitly a target of the Rabobank, but are difficult to reach directly for the bank. SACCOs and (to a lesser extent) MFIs can serve as vehicles. The bank lends to a SACCO which in

42 See Malcolm Harper: Microfinance and farmers, do they fit? in: Thomas Dichter and Malcolm Harper (eds.): What's wrong with Microfinance? Intermediate Technology Publications, 2007. The World Bank too, in its report on the financial situation in Africa, presents a negative picture of MFIs and small-scale agriculture (Honohan, 2007, p. 20). Bateman presents an extensive analysis of this problem (Bateman, 2010, pp. 78-91).

turn lends the money on to its members. The capacity development of SACCOs and MFIs is a requirement here, something in which Oxfam Novib has a lot of experience. Rabobank Development has already invested in Mozambique (Banco Terra, where Oxfam Novib is also involved), Zambia, Rwanda and Tanzania. It is planning to invest in about ten other countries in Africa and Asia.

Oxfam Novib will explore collaboration with the Rabobank in this area.

6.3.5 Micro-Insurance

In the course of implementing the previous Business Plan the interest for micro-insurance as a complementary financial product has gradually increased. Seven counterparts in 7 countries (India, Indonesia, Bangladesh, Burkina Faso, Armenia, Georgia and Peru) are supported in this specific area, with a total outreach of 516,000 persons.

Nevertheless, Oxfam Novib's efforts in this area lag behind the expectations that existed at the start of the Business Plan. There are three important reasons for this:

1. Our current microfinance counterparts, mostly MFIs, have a limited interest in insurance. This is in part due to the specific knowledge insurance demands, and the fear of MFIs of taking risks that are too big.
2. Several MFIs interested in this issue often start their own activities in collaboration with insurers (e.g. ESPOIR in Ecuador and PRISMA in Peru). This is possible because micro-insurance does not demand huge capital inputs. It demands in particular an investment in expertise for developing new appropriate products.
3. Existing micro-insurance schemes still provide too little client value (real financial protection) due to high transaction costs, but also due to the product's inflexibility when compared with lending and saving (usually only a single specific risk is covered).

There is therefore a certain reserve on the part of Oxfam Novib and counterparts to supply these products.

The choice of partners to co-operate on micro-insurance could be different from the one for other financial products. MFIs could play a role in distributing insurance, but are often not the appropriate actor for risk-taking. In most cases it is the combination of a commercial and

public insurance company that in the end bears the insured risks. As they have problems in reaching poor groups, it is often necessary to invest in intermediary organisations that assume a role in developing appropriate products, in organising and informing the target group and in collecting the thousands of mini-premiums. This partner-agent model is very common in micro-insurance, and facilitates the operations within existing legal frameworks. An alternative, and equally successful, is the co-operative insurance or mutual insurance scheme. In agriculture, but also in health care and life insurance, in developing countries co-operative insurers play an important role. The strength of this form of organisation is that they are often members of a network of co-operative organisations they can use to distribute their products. Besides, these organisations are often characterised by a degree of internal solidarity and trust, of crucial importance for scaling up micro-insurance.

In the transition to the new Business Plan the focus on microfinance, and therefore the focus on micro-insurance, has changed somewhat. The basic principle is that financial services must connect with the needs of rural populations, especially with regard to their vulnerability and assets protection. It is therefore interesting to view micro-insurance not only as a financial services, but to see which role it can play to complement, e.g., disaster risk reduction (DDR) and the adaptation of agricultural systems.

6.4 Policy Objective 2

Oxfam Novib contributes to strengthening the social character of microfinance

Based on Oxfam Novib's experiences in Social Performance Management and in activities around impact measurement, as described in paragraphs 3.2 and 3.3, Oxfam Novib will continue to play an active role in promoting the social character of microfinance.

6.4.1 Social Performance Management in MFIs

Oxfam Novib, together with Triple Jump, has developed a tool for analysing the social aspects of MFIs, both with regard to MFIs' relationships with their clients and with their employees. The 2010 evaluation of the use of this

tool was mostly positive.⁴³ This does not mean that the tool's development is finished. Oxfam Novib and Triple Jump will have to adapt the tool continuously to new insights. Client Protection Principles are currently being elaborated by the SMART Campaign.⁴⁴ The gender analyses made with the tool must also connect better with the framework Oxfam Novib uses to appraise gender within other partner organisations. With TJAS we will look what role it can play in this field.

Regional bureaus have the task to support improvements in the Social Performance Management (SPM) of MFIs.

SPM has been identified as a strategic theme inside MicroNed. Together with its partners of MicroNed Oxfam Novib will continue to be committed to further developing the thematic group, and continue to play a role in international forums, such as the Social Performance Task Force.

The Rating Initiative, founded with the co-operation of Oxfam Novib, is instrumental in benchmarking the social dimensions of MFIs. This initiative has a limited duration (until September 2012), as it is hoped that the demand for social *and* financial ratings will increase, not needing any support from donors. Oxfam Novib will continue to support this initiative, and decide if support beyond 2012 will still be needed.

Transparency is an important element of SPM. This importance has two aspects. First, the client must have clear what she or he is paying for financial services. Secondly, transparency in an MFI is important to investors, especially for funds with a social-ethical certificate. Oxfam Novib will continue to support initiatives that promote this, such as the website www.mftransparency.org.

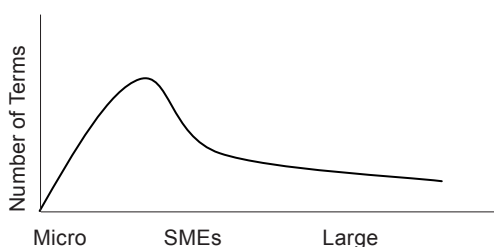
In the world of microfinance gender remains a neglected theme. Alongside the social analysis tool developed with Triple Jump, Oxfam Novib is working on this along two tracks, in MicroNeds thematic working group SPM Impact, and in WEMAN. Oxfam Novib will remain engaged with both tracks, and establish linkages between both initiatives.

6.4.2 Impact and the SIM tool

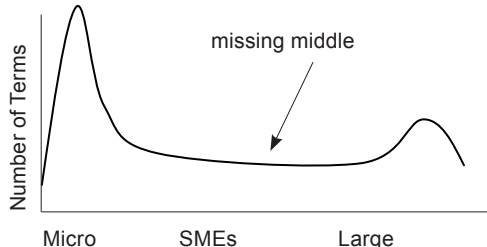
Earlier in this paper we described the struggle of the world of microfinance with measuring the impact of financial services on poverty reduction. The SIM tool, developed by Oxfam Novib, INAFI and Ordina, offers big possibilities of measuring changes with the target groups of MFIs. Investigation is ongoing into the SIM tool's possibilities for measuring changes, not only in microfinance, but also in other sectors where Oxfam Novib has activities.

Graph 1: Distribution by size of businesses in high and low income countries

High Income Countries



Low Income Countries



Harvard Kennedy School – Entrepreneurial Financial Lab:

http://www.hks.harvard.edu/centers/cid/programs/entrepreneurial-finance-lab/the-missing-middle#heading_01

43 Leo Roggeveen (2010): Evaluation of the use by MFIs of the social tool, by Triple Jump.

44 The Smart Campaign is a global effort to unite microfinance leaders around a common goal: to keep clients as the driving force of the industry. To help the microfinance industry remain both socially focused and financially sound, The Smart Campaign is working with microfinance leaders from around the world to provide microfinance institutions with the tools and resources they need to deliver transparent, respectful, and prudent financial services to all clients. Principle tool is the Client Protection Principles, adopted by the microfinance industry in 2008.

6.5 Policy Objective 3

Oxfam Novib supports the institutional development of producers' organisations inside and outside the value chain

In addition to contributing to the development of the financial sector in rural areas, Oxfam Novib also wants to contribute to the institutional development of organisations and systems crucial to rural development, namely farmers' organisations and the value chain.

6.5.1 The missing middle

What to do with another important engine of the economy, certainly so for the rural economy, namely small and medium enterprises? If there is a sector that can generate economic growth, it is this one. The micro-business sector will not have this effect, although it is important for small-scale informal enterprise. The sector of small and medium enterprises (SME) in the South is also called the 'missing middle'. Graph 1 shows why.

It is not only about the absence of a relevant SME sector, but also about the lack of financial services for this sector. Too big to be ignored, too small to be counted. The missing middle qualifies neither for MFI financing, nor for bank financing. MFIs extend the smaller loans and always short-term loans, whilst the SME sector needs long-term loans for investments alongside short-term loans for working capital. In addition, loans based on solidarity between borrowers are not suitable for SMEs, their returns are often not high enough to cover the interest rates that keep an MFI afloat and the risks are too big for MFIs. Small and medium sized businesses often carry too many risks for banks. Meanwhile, the amount that this sector could potentially invest in agriculture is estimated to be in the tens of billions of dollars. It is a huge market.

Earlier in this paper we discussed that the development of the financial sector can have a beneficial impact on economic growth. One conclusion of the studies of Beck and others is that the positive effects of financial sector development are usually more significant for SMEs than for large enterprises, in terms of turnover and labour.⁴⁵

Alongside its contribution to developing the financial sector in rural areas, Oxfam Novib also wants to contribute to the institutional development of organisations crucial to rural development, namely producers' organisations inside and outside the value chain.

Many measures to create the conditions for a safe investment climate are on the tables of governments and international donors, and they will only deliver results in the long term: regulations, legal certainties, government financial policy. Other things could be supported that deliver results in the short term, such as financial literacy and product development. In this regard, the NGO sector can make itself useful in different ways.⁴⁶

1. Supporting the administrative systems of farmers' organisations.
2. Training the management of organisations.
3. Training the staff of local financial institutions.
4. Possibilities for covering first risks via loans or guarantees.
5. Networking between producers, buyers and financial institutions.
6. Research and pilots of new financial products for small-scale agriculture.

6.5.2 Value chains

The concept of 'value chain' is not new. It emerged in the 1950s when USAID coined the phrase. Yet 'value chain' is experiencing resurgence. What exactly is the difference between the use of 'value chain' in the early years and its use today? That difference can be reduced to one big development in recent decades: the far-reaching integration of agriculture in the global economic and global trade, including small-scale agriculture. Small producers used to sell the products they produced; today they depend on markets that are much more demand-driven than supply-driven. It has become a consumers' market. The prices of many bulk products small farmers produce are now set more or less by the national and global markets. Ken Shwedel shows the changes in agricultural perspectives that have occurred over the years. (See table 12)⁴⁷

45 Beck at al. 2004 and 2005, Beck 2007.

46 Also see e.g. Oxfam GB's paper: Alan Doran et al. (2009).

47 Shwedel, Ken (2006): Value Chain Financing: A Strategy for an Orderly, Competitive, Integrated Market. In: Quiros, Rodolfo (ed.) (2006): Agricultural Value Chain Finance. Summary of the conference "Agricultural Value Chain Finance", Costa Rica, May 16-18, 2006.

Table 12: Changes in the Agri-food System

Traditional Agriculture	New Agriculture
1. Separate segment	1. Integrated system
2. Bulk production	2. Differentiated production
3. Price Risk	3. Risk management
4. Need for Capital	4. Need for information
5. Independent producer	5. Interdependent producer

The need to participate is therefore rising. That does not only apply, as is often thought, to high value products. The opportunities in the value chain of products sold in local and regional markets are increasing. There are many examples of this happening.

For several stakeholders, and certainly for funders, it is crucial to know the entire chain. Funders want to know the road the products travel, so as to be able to estimate the risks they are taking. Wholesalers and retailers want to know the chain because of the quality assessment (growing) and the products' origins. Chains are part of a 'business strategy'. Among the more formal forms of financing we find the following organisations, each with its own target group. (See figure 2)

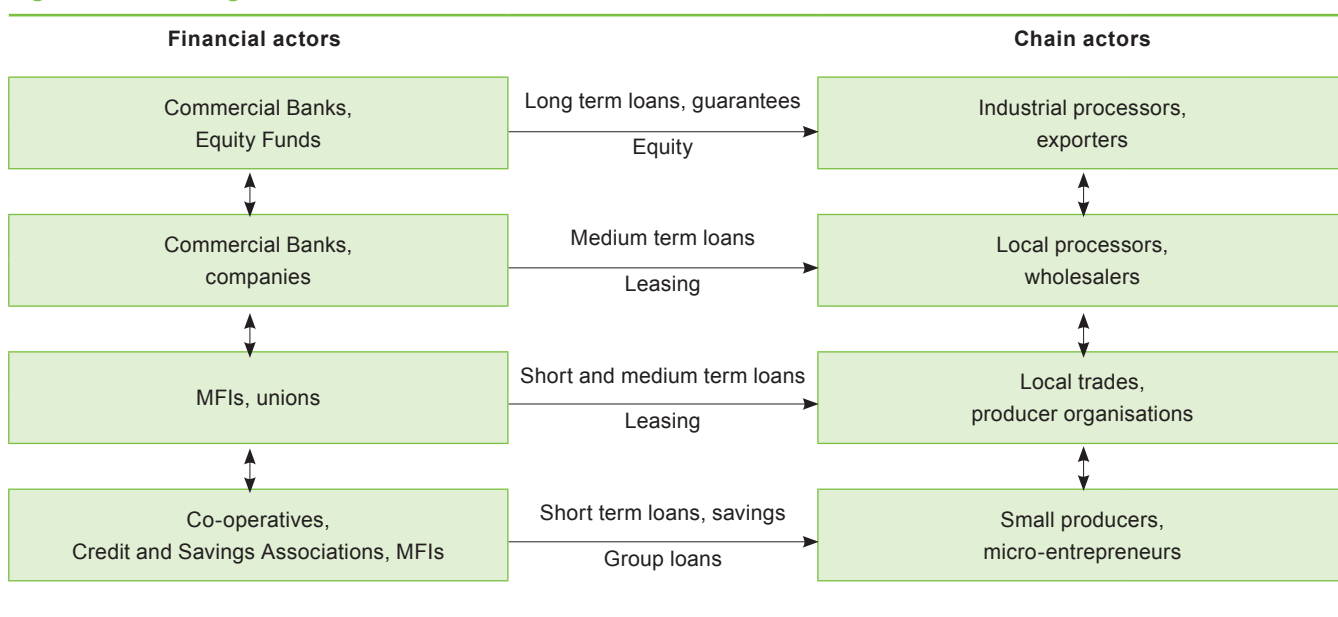
Wholesalers and importers provide much finance, which can be efficient for the client. Input supplier credit, warehouse receipt credit and trader credit, they are all tools that have a function in the value chain. We will investigate to what extent local financial institutions, such as MFIs, SACCO's and local banks, can take this up.

Studies and experiences point to the place financing productive activities should take. The need of a value chain must be derived from the desire to produce competitively and improve the quality and diversity of the products, and not from the desire to make credit delivery easier. The most important problems are not of a financial nature, but are more about a lack of technique and knowledge, insufficient post-harvest management, lack of (market) information, distribution problems and related financing and marketing problems. Business training and training to prepare for product certification can be important elements in these processes. In the end, credit is only a facility enabling the user to make better and more efficient use of other facilities (input, marketing, storage, etc.). Building a value chain therefore costs time, and we cannot expect that a responsible funding will begin soon after starting the value chain.

Value chains are often initiated by facilitating organisations from outside. In addition to the problems inherent in building value chains, this adds the complicating factor that the facilitating organisation often has a limited presence in the chain. Initiating organisation with a commercial interest can have a long lasting influence on chain's sustainability. Despite MFIs' problems in financing agricultural activities, we must acknowledge the good examples of MFIs with a beneficial influence on the chain's sustainability.

Through its Private Sector Group Oxfam Novib is active in several chains: cocoa and palm oil. Opportunities are emerging for developing projects enabling the further

Figure 2: Financing the Value Chain



development of these chains. These projects also link up with the different campaigns Oxfam Novib is currently conducting in the Netherlands, and offers opportunities for co-operating with various actors in the private sector.

6.6 Policy Objective 4

Oxfam Novib uses the Oxfam Novib Fund to contribute to the financial sustainability of MFIs and producers' organisations

Since 1996 Oxfam Novib has been active in lending and has built a loans portfolio of about € 40 million by the end of 2010. Over 92 percent of this was invested in microfinance. The remaining 8 percent was invested in setting up organisations working on and with the media. In 2011 Oxfam Novib is considerably reducing the number of countries where it works. Most of them are low income countries where, in general, the microfinance sector is not strongly developed. Late 2009 the share of these countries in the portfolio was about one third of the total portfolio of the Oxfam Novib Fund.

In order to create coherence between the Oxfam Novib Fund and the policy on financing income generating activities, policy objective 4 has several derived objectives.

6.6.1 Policy Objective 4a

The Oxfam Novib Fund focuses on Tier 3 MFIs and comparable producers' organizations

The Oxfam Novib Fund merges two basic principles of the financing policy 2011-2015, namely the micro-banking and the asset management as tools for supporting the building of the financial sector. This approach is crucial, because it enables MFIs to adapt to market needs and the demands of commercial investment funds interested in microfinance. This policy, which has characterised Oxfam Novib's policy in recent years, will be continued with organisations serving rural areas. As indicated earlier, MFIs are an important link in rural financing, one that however still has to be developed. The maturation path from A to B to C is therefore important. An important condition for the good performance of this policy is therefore a combination of grant making for capacity and institution building of MFIs and asset managements for financing MFIs through loans.

Oxfam Novib directs itself at rural financial markets, but will also support producers' organisations and the value

chain via local rural systems. The most appropriate mechanisms for doing so will be investigated.

6.6.2 Policy Objective 4b

Late 2015 80 percent of the funds from the Oxfam Novib Fund are released or spent in MFS-II countries

Oxfam Novib cannot invest more in countries where it is not developing activities in the context of MFS-2. In this context, in 2015, when MFS-2 ends, Oxfam Novib will have reserved and spent 80% of its funds in MFS-2 countries. Oxfam Novib will be phasing out gradually from regions where it is no longer active. By the end of 2010 almost half the Oxfam Novib Fund will be invested in Latin America, with terms of 2 to 5 years. From 2011 new loans will not be extended in these countries.

6.6.3 Policy Objective 4c

The Oxfam Novib Fund stays at least the same size

The microfinance sectors in the countries where Oxfam Novib works have a limited absorption capacity. In addition the risk profile of MFIs in these countries is big, due to the still weak development of the microfinance sectors in these countries and the often restless political situation. This combination means that Oxfam Novib is going to lose the advantage of an acceptable risk profile resulting from size and the risk-spread. The portfolio in Latin America has very much compensated the risks Oxfam Novib runs in Africa.

Oxfam Novib is currently investigating possibilities for sharing the management of part of the portfolio in Latin America with Oxfam Mexico and to achieve leverage over that share. The goal is to maintain the global character of the Oxfam Novib Fund, and maintain the advantage of scale because of the risk-spread. The fund must also offer the possibility of offering the maturation part (from A to B to C) as a central component.

6.6.4 Products of the Oxfam Novib Fund

Loans and guarantees

The products the Oxfam Novib Fund will use in implementing its policy are loans in different forms (with or without security, subordinated or not, in local currency or not, covered or not) and guarantees. Guarantees will be used when real leverage can be realised with local financial institutions. Their height will depend on the country and the risks to take.

Investments in private equity

For some time several people have expressed the wish to let the Oxfam Novib Fund invest in the private equity of MFIs. Proponents have two advantages in mind. First of all investing in the private equity of MFIs gives it the opportunity to grow whilst maintaining an acceptable solvency. MFIs in Oxfam Novib's niche have problems to acquire equity, considering the big risks these organisations have for investors. An organisation like Oxfam Novib could bear this risk, considering its mission. Besides, a share in the private equity would enable Oxfam Novib to take a seat on the Board of Governors of the MFI.

In recent years the share of northern funds in the private equity of MFIs has grown considerably. ADA's sample of MFIs revealed that the share of foreign funds in the private equity of MFIs had grown by 383 percent from 2002 to 2007, compared to a growth in local funds of 154 percent.⁴⁸ Although this concerns a sample of mature MFIs, it does give some insight in the fact that big MFIs are falling into foreign hands more and more. This study does not indicate the investors' motives for buying shares in southern MFIs. However, there is a study on the pros and cons.⁴⁹ The advantages are:

- a. access to more funds
- b. access to more knowledge
- c. a better image for the MFI
- d. foreign shareholders are often able to address issues local shareholders cannot

There are however also several disadvantages that need to be taken into account:

- a. shareholders must travel abroad often, which is expensive and not always possible
- b. foreign shareholders do not know the local situation
- c. profits are repatriated as dividend, which, together with interest payments, can add to considerable amounts
- d. many investors have a short-term vision
- e. foreign members of the Board of Governors more often view the MFI as part of their fund portfolio management, and do not view themselves as protecting the MFI's interests

The danger is real that an MFI is viewed as a foreign institution. Studies, quoted in ADA's study, present the picture that locally generated funds, through savings, and local investors and local management, are more durable in the long term than foreign funds. However, the

problem is often that local investors are not prepared to join an MFI, because once invested in an MFI the funds are made liquid again with difficulty.

Should Oxfam Novib decide to invest in an MFI, several conditions need to be met:

- a. The decision needs to be based on an analysis of the development potential, and not be based on an analysis of return and portfolio management.
- b. It would have to be a temporary participation.
- c. Oxfam Novib must request a local expert to sit on the Board of Governors, not as representative of Oxfam Novib, but as external expert, without having to confer all the time. In this way Oxfam Novib can avoid the MFI getting too big a foreign image.

The fact that Oxfam Novib would invest in an MFI in its niche also means that the investment cannot be converted quickly to liquid assets. Confianza in Peru serves as an example of a very good MFI finding it difficult to buy out Oxfam Novib. Because condition b is not always easy to realise, investments in private equity will there be the exception and not the rule, in order to prevent Oxfam Novib from getting stuck with part of its portfolio, which is then difficult to recuperate.



Mamie Famba, one of the Cash Counters (female, burgundy) from a Village Savings and Loans Scheme in Nyandehun Village, double checks that the amount of money recorded in member bank books is correct in the presence of Hawa Mansaray (female seated) and Morris Borbo, scheme Secretaries (male, water t-shirt), during their weekly meeting.

Annex 1 Conditions for reaching the (very) poor

Improving outreach

- Market forces operate to serve the less-poor first. Very poor people are excluded through self-exclusion, deliberate or unintentional MFI policy, exclusion by other clients, or by leaving the programme.
- MFIs should understand whom they do reach or exclude, and why.
- MFIs should target poorer areas in the countries they work through rigorous geographic targeting.
- MFIs wishing to have an exclusive poverty focus should target and motivate poorer people in the areas where they work – active targeting leads to a greater focus and inclusion of the very poor;
- To reach the poorest MFIs need a ‘culture of poverty’ – organisational vision and commitment felt by staff at all levels and by clients.

Appropriate products

- Design of products should be based on their potential to reduce poverty, risk and vulnerability, not on its attractiveness to clients.
- Very poor clients need a range of financial services, including both credit and savings. The very poor are economically active and can often use credit.
- Access to credit should be linked to the ability to repay – either through demonstrating savings capacity or business profits.
- A range of other financial and non-financial products, such as emergency loans, insurance or educational inputs can help clients cope with emergencies, smooth consumption, and generally reduce their risk and vulnerability.
- Client need for flexibility and a range of products needs to be balanced with a MFIs capacity to manage an increasingly complex and diverse portfolio.

Delivery

- Very poor clients are vulnerable and often experience problems. MFIs should support clients in coping with these, rather than coercing them into making loan instalments.
- An organisational culture of poverty-focus and impact in an MFI is key to achieving positive impact.
- There should be no compulsion to take out a loan
- Client support and skills-sharing should be encouraged.
- Lessons should be learned from community-based organisations and other models of microfinance.
- Gender awareness should be integrated into programme practice at the level of field staff-client relations, and within organisations’ procedures and culture.

Annex 2 Client Protection Principles

- *Avoidance of Over-indebtedness.* Providers will take reasonable steps to ensure that credit will be extended only if borrowers have demonstrated an adequate ability to repay and loans will not put the borrowers at significant risk of over-indebtedness. Similarly, providers will take adequate care that non-credit, financial products, (such as insurance) extended to low-income clients are appropriate.
- *Transparent Pricing.* The pricing, terms and conditions of financial products (including interest charges, insurance premiums, all fees, etc.) will be transparent and will be adequately disclosed in a form understandable to clients.
- *Appropriate Collections Practices.* Debt collection practices of providers will not be abusive or coercive.
- *Ethical Staff Behaviour.* Staff of financial service providers will comply with high ethical standards in their interaction with microfinance clients and such providers will ensure that adequate safeguards are in place to detect and correct corruption or mistreatment of clients.
- *Mechanisms for Redress of Grievances.* Providers will have in place timely and responsive mechanisms for complaints and problem resolution for their clients.
- *Privacy of Client Data.* The privacy of individual client data will be respected, and such data cannot be used for other purposes without the express permission of the client (while recognizing that providers of financial services can play an important role in helping clients achieve the benefits of establishing credit histories).

Annex 3 Twelve Key challenges for Rural Financial Services Provision

Vulnerability Constraints

1. *Systemic risk* – rural incomes, especially among the agriculturalists, are highly susceptible to similar risks at the same time. Weather is the most uncontrolled and often devastating risk, but disease and plagues are similarly important. Failures in agriculture affect not only the farmer household and the production and marketing linkages, but also the rural non-farm economies that revolve around and depend upon those income flows. Even so, the most problematic is farm credit because of higher risk.
2. *Market Risk* – especially in developing countries, there is both cyclical and seasonal price fluctuations of agricultural commodities, not only due to local production but also affected by “outside forces”, such as political price and exchange controls, subsidies and globalization.
3. *Credit risk* – collateral, especially mortgages, is a missing element in most rural finance, hence increasing the risk of the lender. Similarly collateral subsidies may be costly in both financial terms as well as social stigma risk terms as can be the case with peer lending. Other support services and information networks such as credit bureaus are often not available to help lower the risk. For lending, a financial gap risk between sources and uses of funds poses another risk constraint.

Operational Constraints

1. *Investment returns* – rural capital revolves slowly, with often one, or less frequently, two crops per year. For investment capital, the returns are even slower and in spite of that are often faces with very low profit margins. Hence the margins for error are much less than for example in commerce or most microfinance which tend to have high returns per unit of funds invested and higher profits.
2. *Low Investment and Assets* – the relative poverty in rural areas causes common crises to become major crises due to lack of asset “cushion”. Any loss of expected income through sickness or production

losses cause significant impact. In compensation, traditional networks and production risk minimization become more important than profit maximization. The small asset base also reduces savings and borrowing capacity, thus constraining economies of scale in the use of provision of services.

3. *Geographic Dispersion* – rural areas are characterized by low density of population and high dispersion, which is coupled with a relatively low market potential, makes access and communication difficult and hence high costs of operation for both production and marketing and for access and delivery of services.

Capacity Constraints

1. *Infrastructural Capacity* – poor communication, pitiful roads, unequipped schools and missing social and health services decrease efficiency of operations, discourage new services and increase the outflow of the most talented and resourceful persons and a reluctance of educated families to live in rural communities.
2. *Technical Capacity and Training* – a relative unskilled rural population reduces opportunity for ready access and adaptation to new technologies and employment. The lack of capacity affects not only the productivity and competitiveness in the changing market place but also the ability to find trained staff for service provision.
3. *Social Exclusion* – cultural, linguistic, gender, racial, religious and educational constraints affect market and financial integration. Such barriers reduce production and marketing efficiencies. These are required in order to compete effectively in the marketplace and thereby generate income and levels of assets needed to reduce poverty and vulnerability. HIV/AIDS makes this even worse in many countries.
4. *Institutional Capacity* – while there is an abundance of organizations in rural areas, the relative capacity is lacking. This includes management and technical capacity, size/economies of scale, competitive viability, economic integration and often risk-bearing

capacity. Even when urban based institutions have the capacity to reach into rural areas, there is little incentive to do so. An exception to the capacity constraints is at the micro level where the social fabric is able strong and is sufficient for the level of operations undertaken and may also form linkages with intermediaries of higher institutional capacity.

Political and Regulatory Constraints

1. *Political and Social Interference* – loans can be forgiven, savings, can be withheld, interest rates can be capped, mortgages can be rendered useless and payments can be suspended due to decree. Even danger is not uncommon hence uncertainty can become an insurmountable hurdle.
2. *Regulatory* – regulations and/or lack of enforcement of them hinder rural as well as urban environments. Land tenure regulations, banking laws, exchange rate manipulation and tax considerations are examples of such constraints that destabilize and/or hinder viability of business and financial operations in rural areas.

Annex 4 Rural worlds in Oxfam Novib Strategic Plan 2011-2015

1. *Rural World 1*: Large-scale commercial agricultural households and enterprises with an influential voice in national policies, political affairs and ties to buyer driven value chains. These enterprises also provide employment for members of the other worlds.
2. *Rural World 2*: Traditional agricultural households and enterprises, not internationally competitive but with sizeable landholdings devoted to both commercial and subsistence production. They have few ties to agribusiness supply chains, although some are learning from Rural World 1 and becoming more commercial.
3. *Rural World 3*: Agricultural households and micro-enterprises, including those with limited assets (land, credit), living in fragile ecosystems, with small units producing food for consumption and for sale on local markets. Members of this group, which include many women and female-headed households, are dependent on off-farm and non-farm employment for a significant part of their incomes.
4. *Rural World 4*: Landless rural households and micro-enterprises, whose labour and community ties are their major assets. Women head many of these households. Sharecropping and migration are livelihood options. Rural World 4 relies on Rural Worlds 1 and 2 for employment and income-generating opportunities.
5. *Rural World 5*: Chronically poor rural households, many of which are no longer economically active, and have sold off or have lost their assets during periods of crisis. Increasing numbers of households find themselves in this situation due to HIV/AIDS. Social exclusion and gender inequalities are rife. Safety nets for this group are essential.

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