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Do Microfinance Institutions Reach the Poorest?

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RESEARCH PROGRAM MISSION

The research program titled Rural Financial Policies for Food Security of the Poor seeks to identify policies and institutional arrangements that help the poor integrate themselves into sustainable savings and credit systems in order to increase capacity to invest, bear risk, and preserve livelihoods.

FOCUS COUNTRIES

- Bangladesh
- Cameroon
- China
- Egypt
- Ghana
- Madagascar
- Malawi
- Nepal
- Pakistan

ABOUT THE AUTHORS

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The question raised in the title is an important one to the microfinance sector, especially since the Microcredit Summit held in Washington, DC, in 1997. In order to gain more transparency on the depth of poverty outreach, the Consultative Group to Assist the Poorest (CGAP) supported research at IFPRI during 1999 and 2000 to design and test a simple, low-cost operational tool to measure the poverty level of MFI clients relative to nonclients. This policy brief informs about the results from recent case studies on the poverty outreach of four selected microfinance institutions (for more information, see Sharma et al. 2000).

All four institutions were found to reach clients that were as poor as the poorest third of nonclients residing in the operational area of the MFI. However, there were large differences in the depth of poverty outreach between the MFIs.

Characteristics of the Selected Microfinance Institutions

The case studies were conducted for four MFIs worldwide: MFI A (Central America), MFI B (East Africa), MFI C (Southern Africa), and MFI D (South Asia). In each country, 300 nonclients and 200 new clients of MFIs were randomly selected. The nonclients were used as a comparison group, and resided in the operational area of the MFI. On average, about six to eight enumerators in each country carried out the field research in a time span of four to six weeks. The field research cost, including data entry, ranged between US$5,000 and US$14,000. The selected four MFIs constituted a heterogeneous group serving a diverse set of clientele and using different approaches to service delivery. A brief background of each MFI is provided next and summarized in Table 1.

Founded in 1989, MFI A is the largest microfinance institution in this Central American country. By 1999, MFI A counted 11 branches and served around 14,500 clients, mostly in urban and semi-urban locations. The stated objective of the MFI is to reach all segments of the population that demand financial services for the development of their micro-, small-, and medium-scale enterprises. To reach this diverse clientele, MFI A offers a range of loan and savings products. Loan sizes range from US$20 to several thousand dollars. Apart from credit services, a number of savings products seek to also address poorer segments of the population. MFI A uses an individual loan methodology and does not directly employ targeting methods to reach poorer clientele.

An NGO founded in 1981, MFI B, located in Eastern Africa, provides loans specifically to women in business. In 1997 MFI B established four regional offices, all located in areas with above average population density and high levels of small business activity, and established both urban- and rural-based lending groups. MFI B now provides services to nearly 17,000 women entrepreneurs. To qualify for MFI B services, prospective clients must organize into groups of approximately 20 members, guarantee one another and save a certain amount each week. In addition, individuals must receive a favorable business assessment from both MFI B and other group members.

Operating in a Southern African country, MFI C is a credit and savings cooperative founded in 1993. In 1999, MFI C counted four branches and 58 local units, serving around 22,000 members, in both urban and rural locations. As a cooperative, MFI C requires its members to purchase shares and save for six months before receiving a loan. MFI C uses no explicit targeting methods and draws members from all segments of the population. MFI C employs an individual loan methodology. Since the beginning of the year 1999, however, MFI C launched a new program that specifically targets poor women. This new program requires that women clients form solidarity groups of five members and loans are provided without any prerequisite savings.

MFI D, established in 1989 in a South Asian country, provides credit and saving services to a targeted group of around 31,000 clients, mainly poor rural women, through a network of 19 branch offices in one particular state of the country. Eligibility for the program is tested using a household questionnaire and, following the Grameen Bank methodology, loans are provided without any collateral to clients who form groups of five. Clients are also required to make weekly contributions to a savings account.

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Table 1. Summary characteristics of case study MFIs

Case study MFI	MFI characteristics: Location	Year of establishment	Stated mission/ goals	Number of branches	Areas served	Methodology	Target clients	Products	Number of clients (1999)
MFI A	Central America	1989	Provide services to micro, small, and medium enterprises	11 branches	Mostly urban and semi-urban locations	Individual loan contracts	No explicit targeting; some services specifically tailored to poor	Loan size varies from $20 to several thousand; savings products for the poor	14,500
MFI B	East Africa	1981	Provide services to women in business	4 regional branches	Areas with high population density and high levels of business activity	Group guarantee; compulsory savings	Women in business only; business plan must be approved	Loan size varies from $285-429	17,000
MFI C	Southern Africa	1993	Provide services to all segments of population + recently started program for poor women	4 branches and 58 local units	Urban and rural	Shareholders entitled to loan amount four times the amount of saving deposit. Women's program requires group formation.	No explicit targeting for ordinary share-owning members. A recently initiated program specifically targets poor women.	Loans of $25 and above for women's groups. Share paying members can access loans equal to 4 times the amount saved.	22,000
MFI D	South Asia	1989	Provides services specifically to poor women	19 branch offices	Mostly rural	Loans based on group guarantee; compulsory saving plan.	Specifically targets poor women only	Loan size varies from $100-300.	31,000

A Brief Narrative of the Methodology

Poverty has many dimensions, and a range of poverty indicators is required to capture these dimensions. Using various statistical techniques described in the manual for the poverty assessment tool (see Henry et al. 2000), a poverty index is used to aggregate the information contained in each of the poverty indicators. This index weighs the relative poverty of each household relative to all others and provides a ranking score. The ranking score indicates how each household's estimated poverty level compares with those of all other households surveyed. The higher the score is, the relatively less poor the household is.

To use the poverty index for making comparisons, the nonclient sample is first sorted in an ascending order according to its index score. Once sorted, nonclient households are divided in terciles based on their index score: the top third of the nonclient households are grouped in the "less poor" group, the middle third grouped in the "poor" group, and the bottom third in the "poorest" group. Since there are 300 nonclients, each group contains 100 households each. The cutoff scores for each tercile define the limits of each poverty group. Client households are then categorized into the three groups based on their household scores.

If the pattern of clients' poverty matches that of the nonclients, clients would divide equally among the three relative poverty groups just as the nonclients, with 33 percent falling in each group. Hence any deviation from this equal proportion signals a difference between the client and the nonclient population. For instance, if 60 percent of the client households fall into the first tercile or poorest category, the MFI reaches a disproportionate number of very poor clients relative to the general population.

The Poverty Indicators Used to Compute the Poverty Index

Each of the four case studies uses 15-20 indicators that are used to construct the country-specific poverty index. These indicators combine different dimensions of poverty concerning human resources, housing conditions, assets, and food security and vulnerability. Nine indicators were commonly used in at least three of the four country case studies.

Human resources. Eight indicators related to human resources are used in the four case studies. These indicators reflect the level of education in the household and the presence of unskilled labor force. The percentage of wage laborers in the household seems to be particularly important in the relatively poorer countries of Southern Africa and South Asia (MFI C and MFI D). The indicator expressing whether the household head achieved the secondary school level is important in countries with relatively high literacy rates (MFI A and MFI B).

Dwelling. Dwelling indicators discriminated among relative poverty levels well. In the case of MFI D in South Asia, 8 out of 20 indicators related to housing quality. The importance of dwelling indicators in South Asia supports the use of the housing index as an important indicator of poverty in that region. However, in the African cases (MFI B and MFI C), where housing is relatively homogenous, only four or five housing indicators were used. The presence or quality of latrines appears in all the case studies. House size (number of rooms per person) is used in three countries.

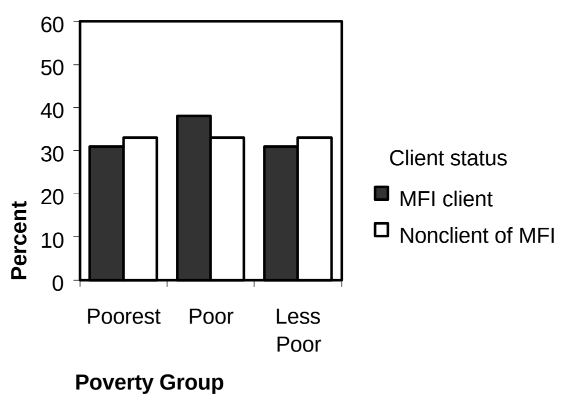
Assets. A total of 15 indicators on the number or value of assets are included in the four case studies. They are particularly important (5 out of 17 indicators) in the Central American country (MFI A), the most well-off country of the sample. The amount of land possessed is important only for MFIs serving rural and agricultural areas, as is the case in MFI D.

Food security and vulnerability. These indicators turn out to be very important in explaining differences in relative poverty in all four studies, particularly in the Southern African country (MFI C), which is the poorest among the four according to its value for the Human Development Index published by the UNDP. The indicator of chronic hunger (enough to eat in the last 12 months) appears in all four cases. Indicators of short-term hunger (enough to eat in the last 30 days) and of consumption of luxury food during the week appear in three cases.

The Results

Figure 1 presents the results for MFI A. The distribution of its clients across the three poverty groups closely mirrors the distribution of nonclients, indicating that MFI A serves a clientele that is quite similar to the general population in its operational area. This result is consistent with MFI A's stated objective of reaching micro, small, and medium enterprises and the diversity in the financial products that it offers.

Figure 1
MFI A: Distribution of client and nonclient households across poverty groups

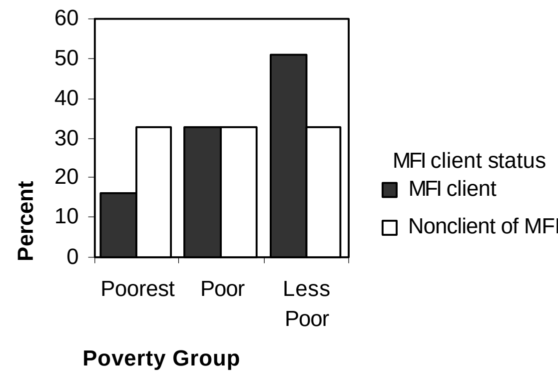


	% Client households	% Nonclient households
Poorest	31	33
Poor	38	33
Less Poor	31	33

Figure 2 shows that the poorest households are underrepresented among MFI B clients. However, about one-half of the clients fall into the two poorest categories, which is remarkable considering the mission of the institution (to reach all women in business), the focus of the product (to finance businesses after submitting a business plan), and the lack of overt targeting.

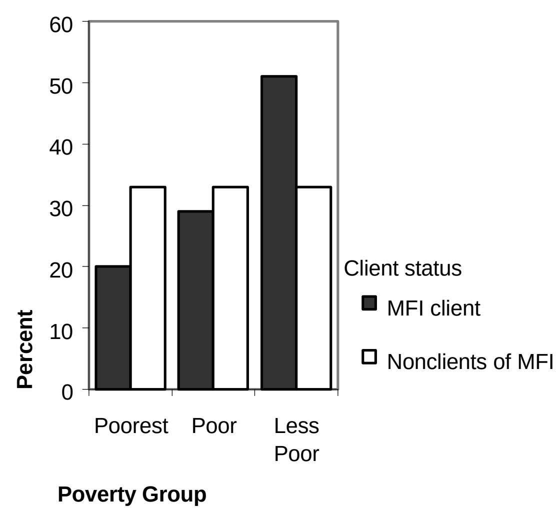
About half of MFI C's clients belong to the "less poor" group while they are underrepresented in the poorest group (Figure 3). This result reflects the fact that MFI C's membership is share-based and open to all individuals. However, poverty outreach is significantly higher when considering only clients belonging to the new program for women. Nearly one-half (45.2 percent) of these clients belonged to the "poorest" group, and only 19 percent of the new women clients belong to the "less poor" group.

Figure 2
MFI B: Distribution of client and nonclient households across the poverty groups



	% Client households	% Nonclient households
Poorest	16	33
Poor	33	33
Less Poor	51	33

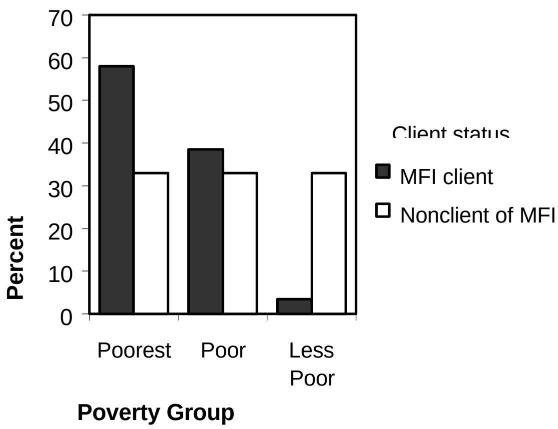
Figure 3
MFI C: Distribution of client and nonclient households across poverty groups



	% Client households		% Nonclient households
	Typical clients	Women's program	
Poorest	20	45	33
Poor	29	36	33
Less Poor	51	19	33

Figure 4 indicates quite clearly that the poorest groups are strongly overrepresented and that less poor households are underrepresented among MFI D's clients. This result is not only consistent with MFI D's explicit aim to serve the poorest households in its operational area but also indicates considerable success in its targeting practices.

Figure 4
MFI D: Distribution of client and nonclient households across poverty groups



	% Client households	% Nonclient households
Poorest	58	33
Poor	38.5	33
Less Poor	3.5	33

Concluding Remarks

A comprehensive assessment of an MFI must include an evaluation of how its poverty outreach record reconciles with its mission and program objectives. As the case studies have shown, MFIs differ in terms of geography, their stated mission, the type of market niche they seek, and a host of other factors, such as the relative development level of the area in which the MFI operates in relation to the national average. Moreover, reaching moderately poor people in a very poor country may be more difficult to achieve than reaching the poorest in a relatively wealthy country that has well-developed institutions and infrastructure. Ignoring these considerations or providing incomplete information on institutional details fails to tell a complete story.

The case studies have contributed to the development and testing of a relatively simple tool that can be used to assess the poverty level of MFI clients. The four case study MFI managers unanimously considered the results to be credible and comprehensive for their institutions. The results also are consistent with the mission, priorities, and targeting practices of the case study MFIs. The Consultative Group to Assist the Poorest (CGAP) looks forward to testing the poverty measurement tool with a number of other MFIs over the coming year to further refine and improve the tool. ■

Selected References

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ABOUT IFPRI

IFPRI's mission is to identify and analyze strategies for meeting food needs of the developing world, with particular emphasis on low-income countries and the poor.

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