

FIELD ASSESSMENT REPORT
OF
THE NIGERIAN MICROFINANCE
INDUSTRY

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I. EXECUTIVE SUMMARY

This report is based on a visit to Nigeria the week of February 28, 2000, by Katharine McKee, Director of the Office of Microenterprise Development (G/EGAD/MD) and John Berry, a consultant with Weidemann Associates, Inc. It draws upon a desk study on microfinance in Nigeria conducted in October 1999 by Weidemann Associates and a December 1999 sector assessment mission that focused on potential USAID program opportunities in agriculture, rural development, and microfinance. McKee and Berry met with representatives of several leading microfinance institutions (MFIs), two wholesale institutions created to provide grants and loans to MFIs, the national network of Nigerian MFIs, commercial banks, and other donors.

The renaissance of democracy in Nigeria and USAID's recent re-entry into the country present a unique set of opportunities and challenges. USAID could play a significant role in helping the Nigerian NGOs engaged in microfinance to professionalize their operations, scale up, and increase their capacity to provide high-quality savings and loan services to rural and urban citizens of modest means. There also appear to be opportunities to strengthen the MFI sector as a whole and encourage the entry of commercial banks into microfinance through retail or wholesale operations.

Through USAID's long experience in microfinance development, the Agency has developed an impressive set of tools and capacities that can have a major impact on the development of the microfinance sector in Nigeria. No other donor currently in Nigeria has comparable financial and human resources available to bring to bear. The short-term challenge during this transition period is to demonstrate that strengthening the sector is relevant to national priorities of stabilization and economic opportunity. Over the longer term, USAID's engagement in Nigerian microfinance could have an appreciable impact on job and wealth creation, on the poor's access to much-needed financial services, and on the vitality of the financial sector. This strategy should reflect local realities and complement local initiatives rather than crowd them out. By implementing high-impact activities in the short term while assessing opportunities for further longer-term interventions in coordination with other donors and the Nigerian microenterprise community, USAID will be in an excellent position to have an important and measurable influence on the development of this vital sector.

We propose a strategy that emphasizes capacity-building, professionalism, and measured growth, innovation and geographic expansion. In the short term, USAID will have greatest impact by building the capacity and improving the reach of the two largest retail MFIs (which are among the largest NGO MFIs in the world) and the stronger of the second-tier institutions, providing capital and technical assistance. In addition to direct support to retail institutions, it might prove efficient to invest in existing apex and wholesale lending institutions. We also propose activities that would build the capacity of the field as a whole, such as training in best practices, assistance with developing performance benchmarks and standards for Nigerian microfinance. In addition, we suggest ways for USAID/Nigeria to explore the potential interest of commercial banks in lending to MFIs and/or developing their own microfinance activities. Finally, we note the need for ongoing USAID/N involvement in policy dialogue around microfinance and microenterprise development, and underscore the need for donor coordination.

II. FINDINGS

During years of military rule, a homegrown Nigerian microfinance community has evolved and established itself in relative isolation from the worldwide microfinance industry. Although few microfinance institutions have reached the scope and scale seen in other developing countries, many of these institutions represent indigenous grassroots efforts to overcome a legacy of rural poverty, poor government, endemic corruption and a crumbling infrastructure. Two Nigerian MFIs, the Farmers Development Union (FADU) and Countrywomen's Association of Nigeria (COWAN) have more microfinance clients than all but a handful of MFIs worldwide.

Despite their isolation and the difficult political and economic environment in which they have operated, the Nigerian microfinance sector has organized itself into a national network which has begun to grapple with many of the key issues of international microfinance best practices (e.g. standards and regulation). Several MFIs are ready to move towards a higher level of financial intermediation. This presents USAID with a unique opportunity to help the industry identify and support Nigerian best practices and selectively introduce international best practices to Nigeria. There is a significant need for capacity building in Nigeria, both among retail and wholesale MFIs, and USAID could have a major role in providing this assistance.

A. Nigerian Microfinance Institutions

This field assessment found a mixed lot of MFIs in need of varied forms of support. As noted above, the microfinance industry in Nigeria is dominated by two MFIs serving hundreds of thousands of clients, while a dozen MFIs serve clients numbering in the thousands and a score of smaller MFIs serve hundreds of entrepreneurs (Annex 1). All of these MFIs are dealing with issues of institutional development (e.g., structure, governance, growth management, controls), professionalism (of staff, systems, etc.), and access to capital. Most of them pursue multi-sector, socially oriented approaches to community economic development, offering training, education and health services in addition to micro-finance lending and business development services. While microfinance may be their dominant activity, to date their mission has been much broader and they have yet to fully wrestle with the decision to specialize in microfinance and the full implications of such a decision (whether through spin-off of microfinance operations into a separate entity or creation of a rather independent division within the parent organization).

Two microfinance wholesalers have been established (the Community Development Foundation, supported by the Ford Foundation and the German ecumenical funder EZE, and the newly-formed Growing Business Foundation, supported by the three largest banks and a half-dozen private companies). The former has had a substantial grants and loans program for MFIs and village-level lending groups for more than 4 years. The latter is just getting started, and is currently its first potential investment, the Lift Above Poverty Program (LAPO). There are also two MFI networks, with the Ford Foundation-supported Community Development and Microfinance Roundtable (CDMR) having the largest membership, range of services, and credibility.

The potential market for microfinance and microenterprise services in Nigeria is huge. In a recent study, the Seed Capital Development Fund (SCDF) estimated the unmet demand for microfinance loans to be greater than \$214 million. Evidence of this unmet demand is clearly demonstrated by the fact that because of lack of lending capital, several of the largest MFIs interviewed by the assessment team stated they were only able to offer loans to 25% of their members who wanted them (even though the loans appear to be priced somewhat below a fully cost-covering rate, unmet demand seems clear). More evidence can be found in the fact that only one Nigerian MFI is headquartered in Lagos to serve a population of more than 12 million people.

Other team findings regarding the MFI sector include:

- Strong tradition of informal and semi-formal savings and credit (e.g., *susus*, rotating savings and credit societies, etc.) – NGOs have often based their methodologies on these traditions.
- Large areas of Nigeria virtually unserved by MFIs (particularly northwest and northeast Nigeria)
- State-sponsored cheap credit has distorted market, crowded out private lenders – ditto likely true as well for grants and highly-subsidized loan programs offered through oil company sponsorship in parts of the Delta
- Savings mobilizations remains underdeveloped, with savings used as collateral rather than as a source of lending capital or a service valued in and of itself by clients
- Small entrepreneurs and rural households are often reluctant to save in formal institutions because of past experience with failed government financial institutions such as community banks.

The level of institutional development among Nigerian MFIs is mixed, but several trends are apparent. Even in the very large MFIs, there is a low level of institutionalization, and many MFIs are still strongly dominated by their founders. MIS are widely recognized as inadequate, and other systems have failed to keep pace with growth. Some MFIs have experienced rapid growth, and FADU and COWAN have extensive branches and structures organized at the state level and below. As noted above, specialization is limited, with many MFIs offering a variety of non-financial services (e.g. training, education, health services); along with the management challenges of offering such diverse services in a high-quality way, this lack of separation of activities makes it difficult to sort out the true level of self-sufficiency of the microfinance operations. Most MFIs have not achieved significant market penetration and only a few have reached national scale. Although only a few donors (particularly Ford and EZE, and to a much lesser extent, UNDP) have had a sustained engagement in microfinance, their awardees have been quite dependent on their operating and capital grants to support their growth and development.

The assessment team found both strengths and weaknesses in the MFI sector. These include:

1. Strengths of MFIs

- Grassroots organizations with strong popular support
- Several very large institutions and industry-wide numbers of clients rivaling those of the most-developed microfinance sectors in Latin America
- Successful home grown financial models building on traditional forms of organization and financial services
- Best practices being adapted ad hoc by top performing MFIs (e.g. inviting a well-known international rating firm to rate their institution)
- Willingness of some MFI managers to learn from and adopt best practices methodology
- Desire of some MFIs to professionalize/specialize in the microfinance field
- Innovative approaches and products being tested (e.g., FADU's efforts to serve new areas through a system of "replicators")
- Proactive effort to develop performance standards, rating, self-regulation, code of ethics
- Infrastructure of support institutions in place (CDMR network, wholesalers)
- Proactive nascent efforts to develop common positions on microfinance policy and regulation and pursue advocacy with the Ministry of Finance, Central Bank, etc.

2. Weaknesses of MFIs

- Limited management depth and capacity to manage growth, specialization, institutional transformation
- Underdeveloped or potentially problematic governance structures
- Underdeveloped performance measures and systems
- Relatively little organized market research and new product development
- Human capital strained by growth and requiring ongoing training and professionalism
- Relatively little competition for clients
- Inadequate MIS and other management systems
- Liquidity constraints limit MFI expansion
- Interest rates probably not cost-covering -- limits ability to achieve sustainability, offer attractive savings products, etc.
- Lack of specialization in finance (social services and training in addition to credit)

B. Government of Nigeria's Role in the Microenterprise Sector

While support by the Government of Nigeria (GON) for the microenterprise sector per se has been limited, its involvement in rural finance and poverty alleviation has been extensive at times. This has posed some challenges for private lenders, including NGO MFIs. On the one hand, the NGO MFI sector has been able to evolve relatively undisturbed. On the other, the lack of a coherent policy framework in which to operate creates uncertainty, and NGO MFI leaders are concerned that the lack of a clear legal and regulatory status for their institutions could invite

sudden regulation of their activities by the government. They also point to some regulations that hinder their activities.

More significant by far, however, is that fact that the government's direct involvement in the sector through its poverty reduction grant schemes and unsustainable state-sponsored rural financial institutions such as the National Agricultural Development Bank and People's Bank of Nigeria has undermined the private microfinance market subsidized interest rates, lack of focus on loan collection, and politically motivated lending. The GON is in the process of developing a \$10 million poverty alleviation program that may have an important impact on the sector. Dialogue with the GON is essential in order to ensure that this project and ongoing restructuring of state-sponsored banks does not further distort the market for small credit. The GON is also considering imposing requirements on commercial banks that a percentage of their portfolio be earmarked for small business lending, but the eventual form and impact of these requirements remains to be seen.

C. Donor Support for the Microenterprise Sector

During the years of military rule, donor support to the microenterprise sector was limited, with only a handful of donors maintaining a long-term presence in Nigeria (e.g. Ford Foundation, EZE, UNDP, IFAD). With the advent of democracy in Nigeria, numbers of donors are now expressing interest in supporting MFIs or starting new enterprise/community development finance activities that could affect NGO MFIs (e.g., the EU's proposal to make grants to microbusinesses in targeted parts of the Delta and capitalize community loan funds). The Ford Foundation has played by far the most important role in developing the NGO MFI sector, followed by and often in partnership with EZE.

Possible synergies exist for USAID collaboration with other donor programs, particularly with Ford's ongoing technical and financial assistance to top performing Nigerian MFIs. Over the next several months, Ford will be providing grants to FADU and COWAN to prepare themselves for Program-Related Investments (long-term, low-interest loans) from the Foundation, and it also plans to provide follow-on support to . . . (list MFIs) Another attractive option to be explored is partnership with the UNDP's MicroStart program in its second phase. This program has brought senior management of ASA, a top-flight Bangladeshi MFI (which is particularly renowned for its savings-led orientation and strong branch-level profitability focus) to Nigeria for 3 years to strengthen a number of the second-tier NGO MFIs. We discussed on a very preliminary basis with the ASA team leader the possibility of USAID supporting expansion and further development of these MFIs (possibly as soon as next year), a prospect that he seemed to welcome, since UNDP follow-on funding will be quite limited for each institution.

If one steps back and looks at the entire financial services industry, and where various donors will want to focus, the following picture seems to emerge. The World Bank has focused its energies to date primarily at the top, with the state-sponsored banks such as the newly-merged NADB-PBN entity. Given the importance of government policy to restructure the thousand-plus community banks, this is also a potential World Bank priority. These two levels might also be the ones of greatest interest to IFAD, judging from brief conversations with the rural finance technical advisor and Nigeria country portfolio manager. USAID and Ford would be the leading

donors focused on the larger NGO MFIs; EZE might wish to continue its engagement at this level. UNDP's MicroStart program is concentrating its efforts on the smaller, second-tier NGO MFIs. The stronger of these have received Ford and EZE support in the past and might in the future; as noted above, depending on their performance in the first round of MicroStart assistance, some might also be attractive targets for USAID assistance in FYs 2001 or 2002. Future patterns of donor support for the wholesale institutions is more difficult to discern at this point, and USAID will require more due diligence to determine whether and where they might fit in our program strategy. In terms of other bilateral organizations, we should follow up to see if the French, Dutch, Germans, Nordics, etc. have an interest in Nigeria. We were told that DfID has decided to focus on priorities other than microfinance at this point. The AMINA microfinance unit of the African Development Bank is undergoing staffing changes at the moment, but they would likely have some interest in the sector as well.

Coordination with other donors and with the Government of Nigeria will be essential in order to leverage USAID's resources, to ensure the application of best practices, and to improve the policy environment. Donor coordination will be particularly important in encouraging the Government to reduce market distortions (such as interest rate caps and subsidized lending) and to create a supportive legal and regulatory environment for MFIs.

D. Commercial Bank Support for the Microfinance Sector

Interest by the commercial banking sector in partnerships with MFIs has been limited but is growing. At least two MFIs have taken commercial bank loans, and as noted above, the 3 largest banks and a number of corporations took the initiative to create the Growing Business Foundation, with the explicit goal of on lending to MFIs. In terms of direct retail provision of microfinance services, the commercial banks have not been active but may have some interest in the future. Many have unprofitable rural branches that the government is not permitting them to close. Furthermore, they anticipate that competition could push them down-market. In addition, the government has announced its intention to create incentives (whether sticks or carrots was unclear to us) to lend to micro and small enterprises, either directly or through intermediaries such as MFIs.

We believe that there could be sufficient interest in both retail and wholesale commercial bank services for microenterprise to justify further exploration by the MSED/DCA team in the Credit and Investment Office, which could lead to one or more workshops for bankers on MSME lending and MFI partnerships. This could also lay the groundwork for eventual application of DCA or MSED tools, e.g., portable guarantees for MFIs seeking commercial credit or loan portfolio guarantees for banks. The Ford Foundation has expressed some interest in such initiatives to promote modest commercialization of microfinance. We also heard that Seed Capital Development Fund has had very preliminary discussions about a possible start-up regulated institution in Lagos State.

III. RECOMMENDATIONS

The current status of the MFI sector in Nigeria presents USAID with a number of important opportunities. In carefully analyzing these opportunities and the technical and financial resources available, we recommend that the Nigeria Mission, with the assistance of the Global Bureau should develop a microfinance sector support strategy that exploits USAID's comparative advantages in institutional capacity-building, innovation, and expansion. This would include support for best practices development and diffusion, market research and new product development, systems and organizational development, and selective financing of portfolio growth.

This strategy should be based on the four goals of improving service delivery by MFIs, assisting the development of the sector as a whole, improving the policy environment and leveraging support through coordination with other donors. Each element would require a good deal of further analysis and legwork, to be carried out by MicroServe consultants, USAID/N staff, and the SEGIR contractor. Institutional assessment of each MFI receiving grant support would be necessary, carried out at a level appropriate to the amount of funding being provided; the Ford Foundation's contract with Seed Capital Development Fund/MicroRate to carry out in-depth ratings of FADU, COWAN, LAPO, DEC, and CDF should greatly aid this due diligence process.

1. Expand and Improve Service Delivery by Retail Institutions
 - Provide performance-based support to top-performing MFIs (e.g., FADU, COWAN, DEC, LAPO)
 - Encourage specialization (financial services only, separate cost center or entity)
 - Systems development (e.g. MIS, accounting, financial management)
 - Finance rational portfolio growth
 - Explore ways to increase scope and scale (replication, decentralization), reach underserved markets (e.g. northwest and northeast Nigeria)
 - Support market research and new product development and launch, as appropriate (e.g. demand-driven savings products, equipment loans, individual loans, inventory credit, housing loans)
 - Facilitate preparation for access to commercial funds.
 - Provide performance-based support for top-performing mid-sized MFIs (e.g., MicroStart partners) – similar activities to those listed above
 - Support Nigerian wholesalers (CDF and GBF). Priorities might include:
 - New product development (commercial bank loans, loan guarantees, institutional mentoring)
 - Reach underserved markets (e.g. smaller MFIs, subregional MFIs)
 - Encourage specialization (financial services only)
 - Encourage MFIs to seek credit and equity investments

- Explore potential direct role for commercial banks in supporting retail and wholesale MFIs
 - Facilitate dialogue between banks and MFIs
 - Train bankers in MF lending (e.g., MAS training program)
2. Improve MFI Sector
 - Develop best practices framework (likely partner – CDMR)
 - Encourage Nigerian MFIs to agree on definitions, indicators and standards
 - Measure performance using definitions and indicators
 - Define Nigerian best practices with reference to global best practices
 - Set best practices benchmarks
 - Technical Assistance and training (e.g., best practices, institutional development, managing growth, improved governance, systems development (accounting, MIS) financial management, marketing, monitoring and follow up)
 - Training of trainers for microfinance support institutions (e.g., CDF, CDMR, EfDI, etc.)
 - Competitive contracts to deliver MFI training
 - Support market research and new product development
 - Training on relevant tools (e.g. Microenterprise Best Practices new product development manual, MicroSave market research and NPD tools, AIMS tools)
 - Competitive mini-grants for tools application
 - Competitive mini-grants for new product launch
 3. Support Nigerian MFI network (e.g., CDMR)
 - Technical assistance for improved member services
 - Support exchange with other networks (e.g. build on existing MBP-supported relationship with SEEP network)
 4. Improve the Policy Environment
 - Work with other donors and government officials to discourage subsidized state lending programs, political interference in credit allocation
 - Engage government in dialogue on MFI regulation and supervision
 5. Improve Donor Coordination
 - Participate in donor coordination group (World Bank has taken some initiative to convene -- members to include DFID, Ford, EZE, IFAD, USAID, UNDP, EU and others who engage in the sector)
 - Coordinate support to retail and wholesale MFIs
 - Support implementation of best practices
 - Coordinate policy dialogue with GFN as appropriate

IV. CONCLUSIONS

The Nigerian MFI sector has great potential and shows great promise for the future. In the absence of large amounts of donor assistance, Nigerian MFIs have built a critical mass of dynamic leaders who are committed to strengthening their institutions and growing the industry. Using indigenous Nigerian models and approaches, a number of strong institutions have emerged and the MFI industry as a whole is moving towards consolidating and disseminating Nigerian best practices for microfinance.

The market for microfinance services in Nigeria is huge, both in the urban and rural sectors, and support for the microfinance sector could be a strategic key mechanism for achieving the Mission's agricultural and rural sector development goals. By using existing contracting mechanisms and resources, an effective microfinance support program can be developed in the short-term, to launch significant activities during the transition period. This should lay the base for expanded longer-term involvement by USAID in the sector. We recommend that this program and a companion effort focused on business development services for microenterprises be managed by one or two PSCs. The recommended implementing mechanisms include an umbrella capacity-building contract, grants and cooperative agreements made by USAID/N, and technical and financial support from the Global Bureau through mechanisms of the Microenterprise Development Office.

**ANNEX 1
NIGERIAN MICROFINANCE INSTITUTIONS**

MAJOR NIGERIAN MICROFINANCE DEVELOPMENT INSTITUTIONS		
SCALE	NAME	MEMBERS
Large MFIs	Farmers Development Union (FADU)	550,000
	Country Women Association of Nigeria (COWAN)	250,000
Mid-sized MFIs	Women Health & Economic Development Association (WHEDA)	12,300
	Lift Above Poverty Organization (LAPO)	8,737
	<i>Community Development Trust Fund (CDTF)</i>	5,963
	Nalt United Self-Help Organization (NUSHO)	5,150
	Justice Development & Peace Commission (JDPC)	5,124
	<i>Widow's Organization International</i>	5,000
	Country Women and Development (COWAD)	4,672
	<i>Palorie Organization (PA)</i>	4,500
	<i>Patphil International</i>	3,527
	<i>United Uwani Community Bank</i>	3,300
	<i>Anglican Family Income Project (AFIP)</i>	3,100
	Development Exchange Centre (DEC)	3,071
	<i>Ndikom Progressive Association (NPA)</i>	3,060
	Peasants Dragnet (P-DNET)	2,500
	Women Development & Education Centre (WDC)	2,200
	Human Management and Agricultural Resources Development Organization (HUMARDO)	2,000
	Nigerian Association of Women in Agricultural Development (NAWAD)	2,000
Forward Africa (FA)	2,000	
<i>Women Economic Development Action</i>	2,000	
Imo Self-Help Organization (ISHO)	1,520	
Otia Development Foundation (ODF)	1,006	
Small MFIs	Anambra Self-Help Organization (ASHO)	938
	Women Management Training and Outreach Program (WMTOP)	600
	Kakeme Development Association (KDA)	550
	(ERDU)	500
	Outreach Foundation (OF)	361
	Rahama Women Cooperative (RWC)	357
	Community Development Initiative (CDI)	300
	Bethel Development Initiative (BDI)	240
	Abakaliki United Self-Help Organization (AUSHO)	120
	Rural Finance and Development Consultancy (RFDC)	91
TOTAL		886,787

Organizations in *italics* are not members of Community Development and Microfinance Roundtable.

Figures in *italics* from Microenterprise Summit MFI list 1998. All other figures from Ford Foundation Country Briefing Document 2000.

**ANNEX 2
INDIVIDUALS AND INSTITUTIONS CONTACTED**

ORGANIZATION	CONTACT	PHONE
Ford Foundation	Adhiambo Odaga	262-3971, home 269-5087
World Bank	Sam Eremie Folusu Okunmadewa	09-314-5269 thru 74 09-234-5269 thru 74
United Nations Development Programme	Nancy Asanga Godwin Nwabunka	269-3396, 269-2141/2/3, 269-5963/4
ASA Foundation	Aminur Rashid	
European Union	Curijn Hasselaar	09-52-33-146, 09-52-33-148
Farmers Development Union	Adedoja	
Technoserve	Tony Grant	
Enterprise for Development International	Charles Akinola	
Community Development and Microenterprise Roundtable	Yinka Lajorin-Eniola	052-258-275 cdmr@fordwa.linkserve. org
Community Development Foundation	Akinyemi Akintola Edna Jones	49-74-508, 49-74-882 cdf@infoweb.abs.net
USAID	Tom Hobgood Carl Harris	
Growing Business Foundation	Ndidi Edozien	774-3126 Newberry House, 13 th fl.
United Bank of Africa	Nigel Lardner, Deputy GM, Consumer Banking	264-4785, 264-4651