

**Gender, Poverty and Micro-enterprise Services**  
**in Ethiopia: Why only Few Women are**  
**Joining?**

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***"... This meeting is for serious people. Here we have to be serious about business. Somebody who is only selling a few vegetables is not serious about business. ... "***

[From: Sam Daley-Harris (2003): State of Microcredit Summit Campaign Report, 2003]

## **ACCRONYMS**

**ACSI:** Amhara Credit and Saving Institution

**AIMS:** Assessing Impact of Microenterprise Services

**BDS:** Business Development Services

**DECSI:** Dedebit Credit & Saving Institution

**GGLM:** Group Guarantee Lending Model

**HHEP:** Household Economic Portfolio Model

**IFAD:** International Fund for Agricultural Development

**MFIs:** Microfinance Institutions

**MGD:** Millennium Development Goals

**NBE:** National Bank of Ethiopia

**NGOs:** Non Governmental Organizations

**PWR:** Participatory Wealth Ranking

**REMSEDA:** Regional Micro and Small Enterprises Development

**SACCOs:** Saving and Credit Cooperatives

**SHG:** Self Help Groups

**SIDA:** Sweden International Development Agency

**WDIP:** Women Development Initiative Programme

**WDR:** World Development Report

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### Summary

Rural financial intermediation currently constitutes a key development intervention in many poor countries, focusing primarily on women. There are many different rationale that explain the **priority on women's access** to micro-enterprise services: 1<sup>st</sup>: growing evidence that gender inequalities in developing societies inhibit economic growth and development; 2<sup>nd</sup>: women are disproportionately represented among the world's poorest people; 3<sup>rd</sup>: Women Spend More of Their Income on Their Families; 4<sup>th</sup>: women's repayment records and cooperativeness, leading to service efficiency and sustainability; 5<sup>th</sup>: microfinance is an effective means for empowering.

Empowerment is an implicit, if not explicit, goal of a great number of microfinance institutions around the world. Empowerment is defined as *the process by which women take control and ownership of their lives through expansion of their strategic life choices* (Kabeer, 2004). It is composed of three dimensions: **resources** which form the conditions under which choices are made (credit, property, and money,...); **agency**, the ability (or the internal aspect of feeling capable) to define one's goals and act upon them, constituting the potential for action; and **achievements**, the valued ways of "being and doing", which are **realized** by different individuals (e.g. being well nourished, having long life expectancy, and being fully integrated and active member of one's community). There are two widely used modalities for delivering microenterprise services like credit for poor women; the Group Guarantee Lending Model and the Self-Help Group approach.

The **GROUP GUARANTEE LENDING MODEL (GGLM)** views microcredit as the single most critical input for poverty reduction; the key bottleneck to poverty alleviation is seen as **ongoing access** to finance; implicitly assumes the poor has some income generating activities, thus targets the productive poor. In the past one decade or so, the service outreach has indeed seen rapid expansion all over the country. Currently about 12-15% of the poor in Amhara region are assumed to have the access to such services. However, unlike in other countries implementing similar programmes, the proportion of women joining the programme is only about 35%, in spite of efforts to create the "access" to credit, by reaching areas where the poor lives, penetrating into remote villages, in different areas of the highlands of Amhara region where infrastructure (particularly the road net-work) is so poor. Currently more than 75% of the villages (P.As) in the region have the access.

But, **distance** between financial service providers and consumers is not just physical or geographical one: it can also include barriers of service methodologies, policies, the terms and conditions, etc., of the services being delivered. For example, the Group Guarantee Lending Model (GGLM) has been a great opportunity for the majority poor as it removes the main entry barrier for those with no collateral, limited literacy, weak technical knowledge and narrow prior money management experience. But it has also its own limitations. The dynamics of joint liability implies that groups screen and self-select their own members to form relatively homogeneous groups; i.e. the members share very *similar probability of defaulting a loan*. It is assumed that social solidarity and mutual support will ensure that successful members cover for the defaulters. This increases the likelihood that the poorer and more vulnerable will be excluded, since a partially formed peer group looking for more reliable members with whom to share risk is more likely to reject candidates they consider most risky, namely the very poor. This is more so in cases where there is low gender awareness among those involved in the selection and screening.

Alternative methodologies are not developed for the poor. For example, it is clear that the main problem (of lending to many) is not that the poor actually lack capital, but that many lack the legal title to assets they already hold. ... "They have houses but not titles; land but not titles; crops, but not deeds; business but not statutes of incorporation; etc..." (de Soto, 2003). Giving them the legal title will unleash the *"dead capital"* so that it can be used as collateral for loans to fund new business or expand existing ones. Other terms and conditions are not necessarily gender focused (*loan size, the loan term, repayment rhythms*) with detailed investigation of households' income or cash flow.

Moreover, just making critical resources like credit available does not automatically make poor people, especially women, business persons. For the majority very poor people, with no or little skill and high risk aversion behaviour to start or expand business activities, *enough persuasion* has to go along with the credit service. There is no in-built mechanism to provide such vital *Business Development Services*. Due to some *cultural bias* towards some activities, the tendency (and the attendant competition for resources) is often to get on with such activities as agriculture, trade, etc, which are somehow free from cultural taboos. Some non-traditional activities which could provide alternative employment opportunities (like blacksmithing, weaving, tannery, pottery, embroidery, other handicrafts, etc...) are rather frowned at, and not easily taken up by clients. In some areas Muslims do not take credit or save in banks or microfinance institutions because paying or receiving "interest" or earning money by the act of loaning is considered *haram* (in discord with the Islamic code).

Women also face a great *time poverty* because most domestic tasks such as grinding grain and food processing, water and fuel wood collection are highly arduous, labour-intensive and time-consuming, compounded by the fact that *labour saving "appropriate" technology* is largely unknown even by the standards of developing countries. An additional area of concern, in terms of the impact of loans of the poorest, concerns *men's usurpation of loans* targeted specifically to women. Survey indicates that only about 40% of the women who took credit from ACSI use it themselves (in their own business) others either use it "in consultation with others" or totally hand it over to their male counterparts.

A related and more problematic issue is also the *low income perspective* that prevail among most dwellers in many rural areas. Thus, after getting the additional ox that has been set as a target, or some level of income that provides for subsistence life, most would stop asking for more loan or only take a small amount. So, apart from the credit delivery, more attempt need to be made to enhance the *capabilities* of women, improving the potential to be engaged in economic activity.

Yet, the resources and the agency need to be transformed into *realized achievements* such as: being well-nourished, having long life-expectancy, and being fully integrated and active member of one's community. For example, there is a significant difference between "*increasing income*" and "*reducing poverty*". Clearly, the "*use*" to which income is put is as important in determining poverty and welfare as the level of income itself -- increased income can be (and often is) gambled away. The assumption of a "*rational consumer*" is often unattainable. Indications are that a good deal of clients enjoyed improved food security. Yet, no one can tell whether such a food is nutritious (with nutrients, protein, iodine,...contents), and with "*fair distribution*" for the child, mother and other household members.

Majority poor (and also the non-poor) also face the problem of *vulnerability* to sustain a certain livelihoods. *Micro-saving*, which is proving elsewhere to be as important, if not more important, as microcredit service in terms of guarding the poor against vulnerability, to the extent of playing the role of children born as an old-age security, seems to be given little accord. There are also no mechanism to avail financial services required by the poor in times of emergency, and in extreme difficult circumstances. Moreover, since the loan are agricultural loans affected by drought, there is higher risk both for the clients and the institutions. The Ethiopian MFIs do not offer *insurance services* be it life, disability, health, crop damage insurance to their clients.

By contrast, the **SELF HELP GROUP APPROACH**, while also facing much of the 'environmental' obstacles faced by GGLM in making credit an 'empowerment' tool, it has obviously some key advantages to women. Foremost among them is the fact that it aims to reach poor women, and women only. So, whereas there are big chances of the benefits being siphoned-off by better-off women (and not poorer women) this is an achievement by itself. Moreover, unlike the GGLM, it integrates BDS and skill training, which poor women badly need, thus potentially enhancing the ability of women to use the credit to their advantages. The effectiveness of such skill trainings, however, have to be confirmed. Moreover, once the external money, supplemented by savings, is in the hands of women, they can establish their own terms and conditions as *best fits* their local circumstances, rather than accepting whatever is imposed upon them by external credit delivering organization.

Yet, such programmes face a key problem relating to *sustainability of the services*. Real financial intermediation (shifting purchasing power over time, as well as between net savers and net investors) cannot indefinitely rely on donor funding. The fact that money is being injected from outside (**cold money**) and not generated from within, or member contribution (**warm money**) provides *little incentive* to make full repayments, which is the basis of success for MFIs. Low repayment means that money cannot circulate for many years, thus shortening the length of outreach. Yet the poor need an on-going access to loan services to be out of poverty; moreover, length of outreach matters because society cares about the poor “both now and in the future”. Moreover where repayment is not expected, little effort would be made to utilize scarce resources to projects with maximum economic/social benefit, resulting in serious *capital misallocation*.

There is also no guarantee that such money goes to the targeted poor women. Often, subsidized services induce excess demand from all types of applicants -- poor and non poor. Influence and patronage and better connections inevitably bias the distribution in favour of the better-off. Especially where targeting is relaxed, money can go to un-targeted people, who could have better chance of accessing resources from alternative sources. This creates *market segmentation* in the local economy (among same kind of people in terms of economic situation and risk profile) – some accessing subsidized funds, while others accessing it on market terms. The former can thus price their products lower than the latter, thus putting the latter at a disadvantage.

**WAY FORWARD?** Self help groups need strengthening through capacity development. But also there is a need to link such programmes to mainstream banks or microfinance institutions, for the poor to be out of poverty, they need continued (on-going) access to capital (not just 18 months!). The *Income Generation for Vulnerable Group Development (IGVGD)* of BRAC can provide good example. Perhaps the most important problems relating to such “subsidized” services is targeting. Thus it would be very helpful if coordinated effort is made to pool resources together and establishing a mutually agreed-upon targeting principle, to ensure sustainable use of scarce resources. New lending models based on serious market research is a must for the programmes. More important, focus need to be given to “integrate” service provision (“Credit with Education”), for credit ‘in isolation’ cannot solve the problems of the poor facing multiple dimensions of poverty. For rural finance to succeed rural infrastructure (road, etc) need attention. Women work need to be supported by labour-saving technologies. Financial education, for those in other development sectors, NGOs, donors, etc has to be enhanced for the smooth operation of “modern” financial intermediation in the country. **[END]**

## **OUTLINE**

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## 1) BACKGROUND

### *Micro-enterprise Services for Growth and Poverty Alleviation*

Poverty and ill-being in Ethiopia are abysmal. The Amhara region in particular, has been prone to much suffering in the past, and was one of the hardest hit areas in the 1973, 1984 and more recent famines of Ethiopia. The Government has undertaken series of economic reform programmes aimed at re-orienting the economy from command to market economy, rationalizing the role of the state and creating legal, institutional and policy environment to enhance private sector investment. The Rural Development Strategy, the Poverty Reduction Strategy Paper as well as the “Sustainable Development and Poverty Reduction Programme (2002) have more clearly articulated the objectives in revitalizing development in the country.

Given that poverty reduction will continue to be the core of the agenda of the country's development, the strategy is built on *four pillars* (building blocks). These are: Agricultural Development Led Industrialization (ADLI), Justice system and civil service reform, decentralization and empowerment, and capacity building in public and private sectors. Such a four-pronged approach is believed to be effective in a fight against poverty and ensure sustainable development.

Of all the four “pillars”, the ADLI strategy emphasizes rural finance. The Ethiopia's existing realities reveal that there is an acute shortage of capital. In contrast, the country is endowed with a large number of working age population and a potentially cultivable land although land is still relatively scarce in some part of the country, particularly the northern and central highlands. It is believed that faster growth and hence economic development could be realized if the country adopts a strategy that helps raise the employability of labour resources and enhance productivity of land resources aimed at capital accumulation.

In turn, for agriculture to continue serving as an engine of growth in the coming years, through the domestic economy and international trade, there has to be progress in terms of commercialization, with more intensive farming, increasing proportion of marketable output and correspondingly decreasing ratios of production for own consumption. Aside from deepening technological progress, it will mean greater market interaction on the part of the farmer, more research and extension, application of inputs, irrigation, production of tools and equipment, rural roads will need to have more emphasis. Extension of credit to the small farmer has to gain importance with commercialization of agriculture and give impetus to the establishment of rural banks (FDRE, 2002).

On the other hand, as employment and traditional livelihood strategies for men disappear, poor women in increasing numbers have had to make their ways into the informal sector, primarily in low paying and often menial work -- piece work, vending, petty trading, agricultural labour, collecting garbage, cleaning toilets, and factory employment. It is

now believed that about 40% of the households in Ethiopia are headed, *de-jure* and *de-facto*, by women (IFAD 2001). Concerted efforts to enhance self-employment and income generation schemes, through expanding micro-enterprise services appear very vital to avert this undesirable situation. Indeed, NGOs or government agencies, with different primary objectives like promoting literacy and education, or maternal, child health and nutrition, reducing female infanticide or child labour, encouraging watershed development, taking up women's empowerment, etc., have used micro-credit as an *entry point* or as a complementary activity, recognizing that it is harder to mobilize people and sustain interest around other issues in poverty situations<sup>1</sup>.

### ***Why Target Women?***

There are many different rationale that explain the priority on women's access to micro-enterprise services<sup>2</sup>.

*Gender and Development* One of the rational for specifically targeting women comes from growing evidence that gender inequalities in developing societies inhibit economic growth and development. Societies that discriminate on the basis of gender pay the cost of greater poverty, slower economic growth, weaker governance, and a lower living standard of their people. Micro-enterprise services like microfinance has come to play a major role in many of these donors' gender and development strategies because of its direct relationship to both poverty alleviation and women<sup>3</sup>. As part of their poverty reduction priority, donors support programs that provide "increased access to productive assets (especially land, capital, and credit), processing, and marketing for women." By giving women access to working capital and training, microfinance helps mobilize women's productive capacity to alleviate poverty and maximize economic output.

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<sup>1</sup> Honohan (2004) graphically illustrates that the "Poverty Gap" (i.e. the minimum aggregate amount, expressed as a percentage of GDP which, if appropriately distributed, would bring all people up to the poverty line) is very large for an important subset of poor countries in Africa. For these countries, achieving greater financial depth seems particularly important if the *poverty gap* is to be closed. These countries include: Burkina Faso, Burundi, Cameroon, Central African Republic, Ethiopia, The Gambia, Ghana, Lesotho, Madagascar, Malawi, Mauritania, Nicaragua, Niger, Sierra Leone, Uganda and Zambia.

<sup>2</sup> Mayoux (2005) elaborates on three paradigms: The feminist empowerment paradigm, poverty reduction paradigm, and financial sustainability paradigm. The arguments are quite similar to this.

<sup>3</sup> Although the increase in women's participation in micro-enterprise was to some extent a result of better recording of seasonal, unpaid family and casual labour, it also reflected a number of real changes (UNDAW, 2001, p.16). First, more women now have to work to ensure family survival in the face of declining real wages and the increased monetary costs of subsistence resulting from *cutbacks* in both public services and subsidies for staple foods. Second, the number of women-headed households in which women are required to meet the monetary costs of household survival from their own labour has increased. Third, the demand for women workers in particular sectors of the economy experiencing long-term growth has grown. Many industries employing a high proportion of women have expanded rapidly in response to globalization. Much of this is low-skilled manufacturing – notably in garments, footwear and electronic products – and 'non-traditional' agricultural products such as cut flowers, seasonal fruits and vegetables. Changing social norms, increasing levels of education among women and declines in fertility, are other important factors behind the increase in women's labour force participation.

*Women are the Poorest of the Poor:* The basic argument in this case is that women are disproportionately represented among the world's poorest people. The assumption is that increasing women's access to micro-enterprise services will enable women to make a greater contribution to household income and this will translate into improved well being for women. Moreover, although women are not always poorer than men, because of the weaker basis of their entitlements, they are generally more vulnerable and, once poor, may have less options in terms of escape. By providing access to financing for income-generating activities, microfinance institutions can significantly reduce women's vulnerability to poverty.

*Women spend more of their income on their families* By helping women increase their incomes, you are improving the welfare of the whole family. Women's success benefits more than one person. Several institutions confirmed the well-documented fact that women are more likely than men to spend their profits on household and family needs. Assisting women therefore generates a multiplier effect that enlarges the impact of the institutions' activities." A number of studies that lend credibility to the commonly held belief that women spend a greater percentage of their income on their households than do men.

*Efficiency and Sustainability* Proponents of targeting women for sustainability reasons cite women's repayment records and cooperativeness. A collective wisdom has emerged that women's repayment rates are typically far superior to those of men. Lower arrears, loan loss rates have an important effect on the efficiency and sustainability of the institution. Many programs have also found women to be more cooperative and prefer to work with them for that reason as well.

*Empowering Women* Last, but not least, one of the often articulated rationales for supporting microfinance and the targeting of women by microfinance programs is that microfinance is an effective means for empowering women. By putting financial resources in the hands of women, microfinance institutions help ***level the playing field*** and promote gender equality.

### ***Empowerment: Resources, Agency and Achievements***

Empowerment is an implicit, if not explicit, goal of a great number of microfinance institutions around the world. The concept of empowerment has been the subject of much intellectual discourse and analysis. For the purpose of this discussion, the conceptual framework expounded by United Nations is a useful starting point (United Nations 2001). Empowerment is defined as *the process by which women take control and ownership of their lives through expansion of their choices. Thus, it is the process of acquiring the ability to make strategic life choices in a context where this ability has previously been denied.* (Kabeer, 2004).

As such, empowerment is a process of change that can only be driven by women themselves. On the other hand, although empowerment can not be given to somebody by someone else, the process of empowerment can be facilitated by others through, *inter*

*alia*, education, capacity building, political mobilization, changes in systems of property rights and the social and legal institutions that marginalize women. According to Kabeer (2004), changes in the ability to exercise choice can be thought of in terms of changes in three inter-related dimensions which make up choice: *resources* which form the conditions under which choices are made; *agency* which is at the heart of the process by which choices are made; and *achievements*, which are the outcomes of choices.

These dimensions are inter-dependent because changes in each contributes to, and benefits from, changes in others. Thus the achievements of a particular moment are translated into enhanced resources or agency, and hence capacity for making choices, at a latter moment in time. First: In order for a woman to be empowered, she needs access to the material, human, and social *resources* necessary to make strategic choices in her life. Women have been historically disadvantaged in access not only to material resources like credit, property, and money, but they have also been excluded from social resources like education or insider knowledge of some businesses.

On the other hand, *agency* is the ability to define one's goals and act upon them, and the sense of agency is the *internal aspect of feeling capable of acting* upon one's goals, and as such constitutes the potential for action (Kabeer, 2004). Access to resources alone does not automatically translate into empowerment or equality, however, since women must also have the ability to use the resources to meet their goals. In order for resources to empower women, they must be able to use them for a purpose that they choose. Naila Kabeer uses the term *agency* to describe the *processes* of decision-making, negotiation, and manipulation required for women to effectively use resources. Women who have been excluded from decision-making for most of their lives often lack this *sense of agency* that allows them to define goals and act effectively to achieve them<sup>4</sup>. However, these goals also can be heavily influenced by the values of the society in which they live and so may sometimes replicate rather than challenge the structures of injustice. The influence of *society and culture* over the range and exercise of choice also means that if we seek to promote empowerment, we must also consider factors affecting women's status and rights as a group. With some support, groups of economically empowered women can take steps to address the cultural and legal barriers that limit their social and political empowerment. For example, a study by Dreze and Sen (Cheston, et. Al, 2002) shows us that structural variables making up gender relations in different parts of India are far more important in determining the extent to which the girl child is valued within the family than the individual characteristics of their parents.

Resources and agency together constitute what Sen refers to as capabilities (Kabeer 2004) the potential that people have for living the lives they want, of achieving valued ways of "being and doing". Sen uses the idea of "functionings" to refer to all the possible way of "being and doing" which are valued by people in a given context and of "functioning

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<sup>4</sup> Many feminists recognize that poor men are almost as powerless as poor women in access to material resources in the public domain, but remain privileged within the patriarchal structure of the family. In some societies, being seen by neighbours as in control of his family and wife is a key element of men's social prestige—particularly in impoverished communities where men may be able to boast of few other status symbols. (Cheston, et. Al, 2002)

achievements" to refer to the particular ways of being and doing which are realised by different individuals. These realised "**achievements**" (such as being well-nourished, having long life expectancy, and being fully integrated and active member of one's community (Chant, 2003), or the failure to do so, constitute our third dimension of power. Clearly, where the failure to achieve valued ways of "being and doing" can be traced to laziness, incompetence or some other reasons particular to an individual, then the issue of power is not relevant. When, however, the failure to achieve reflects *asymmetries* in the underlying distributions of capabilities it can be taken as a manifestation of disempowerment.

Different approaches have been utilized to bring about empowerment through delivery of micro-enterprise services, like micro-finance. There are practical problems faced on the ground in realizing the objectives contained in development programmes. The following section details the two most popular once; namely: the Group Guarantee Lending Model (GGLM), and the Self-Help Group (SHG) model.

## **2) THE GROUP GUARANTEE LENDING MODEL (GGLM)**

### ***Perspectives on micro-credit, Targeting Principles and Operational Modalities***

#### ***Perspectives on the role and functions of micro-credit***

MFIs view microcredit as the single most critical input for poverty reduction. The perspective is as follows: the poor has been excluded by formal financial system; they have no physical or financial collateral; government sponsored programmes are largely subsidy based, attracting people for *one-time benefits*; the poor are driven to local money lenders where credit is exorbitantly priced, ensuring that the borrower never comes out of poverty; the poor are unable to utilize what skills they have for lack of capital. The main bottleneck to poverty alleviation is seen as ongoing access to finance. Hence, **regular access** to micro-credit on reasonable terms with simple procedures, quick disbursements with full and frequent (weekly) repayments, is seen as the critical input for poverty reduction. Access to micro-credit enables households to use their skills in income generating activities, helps them generate surpluses, slowly expand into multiple activities with additional loans and owns resources, thus countering seasonal and activity based risks.

#### ***Targeting Principles***

Given the scarcity of loan-able fund and the limited capacity to serve all the credit demand in the region, essentially the service is delivered on a *priority* basis. Focus is thus on the poorest, particularly women, as this is believed to have the highest impact on poverty /food insecurity through bringing about improvements upon both the **rate** as well as **depth** of poverty/food insecurity. Targeting is therefore at area as well as household level and gender focused. ACSI, for example, seeks to reduce poverty by targeting financial services to the poor both *directly* (through means-testing) and *indirectly*

(through product and service designed to attract the poor): a) *Area Targeting*: Priority is given to those areas which are more food insecure. This is conducted in consultation with the *Woreda* and *Kebele* administration. Thus, within a given *Woreda*, the most food insecure *Kebele* (suffering from "chronic" food insecurity) is given the priority. b) *House hold Targeting*: a combination of poverty assessment and targeting methods are used: The loan size, as one of the targeting tools, has been limited to a maximum of 5000 Birr. While the loan size ceiling is relaxed currently, the dominant principle is still not ignoring serving the poor, looking for smaller loans for income generation. Moreover, as a Rapid Assessment (RA) method, priority is given for those with one or less oxen values, with possession of one ox serving as the local poverty line. A sort of Participatory Wealth Ranking (PWR) is also carried out, whereby representatives from the community (Credit and Saving Committee) exercise further rankings of those who should be first beneficiaries of the services.

At *Individual level*, generally, the lending programme essentially targets the *productive poor*: those if appropriately assisted could by themselves create the activities that could enable them to get out of poverty -- the entrepreneurial poor. This derives from institutional values and principles. Specifically, the individual targeting criteria are: The individual looking for credit must be in the productive age group, those who are already engaged (or ready to be engaged) in some productive activity, but are handicapped due to lack of capital, good reputation in the community about his/her general characters, honesty, mentally healthy, free from other debts, from government, cooperatives, permanent residence in the *Kebele*.

Special focus is given to **women** as they are the ones who most suffer from all kinds of poverty and deprivation, and at the same time improvement in women's income can have immediate impact on household poverty and nutrition. Women are encouraged to start some business activities so as to improve their *bargaining power* within the household through enhancing their "breakdown position". ACSI has a target of delivering at least 50% of the credit service to women.

### *Operational Modalities*

The objective of maintaining good portfolio quality can only be guaranteed if one follow demand-based, quality lending products that maximize value to clients. Thus the Institution always strives to provide diversified lending products with suitable terms and conditions in terms of: *loan size, repayment period, repayment frequency, collateral, transaction cost*, etc. The modalities, loan terms and conditions would have to be such as to fit in the very circumstances of the poor, while ensuring full repayment:

Since the poor shall not be required to avail any collateral, candidates are required to exercise a peer group self-selection and organize groups for the purpose of sharing a mutual loan repayment guarantee. ACSI follows the ***Group Guarantee and Lending Model (GGLM)***. Credit delivery through very small, affinity-based groups of 5-7 members each, with about 10-15 groups getting together at one center, meeting monthly for savings, repayment and loan processing is the model. The microfinance terms and

conditions are planned with a view to meeting the needs and requirements of the poor, though there are emerging problems over time (more on this below).

### ***Achieving the Empowerment Objective?***

#### *Extending the Microfinance "Opportunities" to Poor Women*

In terms of *Outreach*, currently, there are about 484,000 active credit clients (**about 35% women**), with an active credit balance. But, given the number of economically active people outside of the reach of the conventional financial service, estimated at about 3 Mill, the outreach is clearly minimal. It is only 12-15% of demand taking only the number of the very poor. Presently, ACSI is operating in all *Woredas* of the Region, and has covered about some 75% of total *Kebeles*. There are many economically active poor people still un-reached. Given the very poor infrastructure in the region, attending all such clients would undoubtedly increase operation cost. There are, however, many challenges that constrain the achievement of the targets.

For the given level of outreach, the **group lending methodology** has been a great opportunity for the majority poor as it removes the main entry barrier for those with no collateral, limited literacy, weak technical knowledge and narrow prior money management experience. It provides a great chance to communicate with people, develop social networks (hence social asset), develop the skill to speak in public, learn something more from neighbors, etc.

It has advantages for MFIs in terms of screening those who are not credit worthy. Research on Grameen Bank clearly pointed out the great significance of the group in screening out the non-credit worthy in the localities: "Women who are really disorganized and cannot "manage" their households, women who are considered foolish or lacking in common sense, women who are "belligerent" and cannot get along with others, women with many small children, with husbands who are "lazy" and gamble and waste money or are "bad", are generally considered "high risk". It is felt that these women will be unable to use loans "wisely"; they would be unable to save and invest and increase incomes. These women, even if provided with membership, would drop out and would have negative influence on others." (Hashemi, 1997).

Yet, the methodology is not without problems. The advantages of peer monitoring over traditional practices lies in its social connectedness, as local knowledge about others' assets, capabilities, and characters is used to sort and self select. In theory, the dynamics of joint liability implies that groups screen and self-select their own members to form relatively homogeneous groups; i.e. the members share very similar probability of defaulting a loan. It is assumed that social solidarity and mutual support will ensure that the successful members cover for the defaulters<sup>5</sup>. This increases the likelihood that the

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<sup>5</sup> In terms of ensuring repayments, **group lending** can have both positive and negative effects. It increases loan repayment because successful borrowers may help repay loans of less successful borrowers unable to repay. Group lending may also reduce the repayment rate if the "entire" group defaults (i.e when some

poorer and more vulnerable will be excluded, since a partially formed peer group looking for more reliable members with whom to share risk is more likely to reject candidates they consider most risky, namely the very poor<sup>6</sup>. Furthermore, with little gender awareness and/or commitment, the community "representatives" (the "Committee"), who may latter on be involved in guaranteeing repayment process, also tend to focus on the less poor. There are also psychological barriers developed among the poor themselves<sup>7</sup>. The combined effect results in endangering the very objective of serving the very poorest section of the population<sup>8</sup>. In the extreme case, 'group lending' may have the un-intended negative effect on the existing traditional social ties among the local population<sup>9</sup>.

Not only is outreach low, but also the *terms and conditions* of the service need revisiting. The very poor requires *diversified/flexible terms/conditions*: diversified loan size, flexible repayment period, repayment frequency, availability of loan on time, lower transaction costs, diversified collateral, etc. For example, there are people who have the ability to offer collateral, but cannot do so simply because the collateral don't have legal title. It is clear that the main problem (of lending to many) is not that the poor actually lack capital, but that many lack the legal title to assets they already hold. "...They have houses but not titles; land but not titles; crops, but not deeds; business but not statutes of incorporation; etc..." (de Soto, 2003). Giving them the legal title will unleash the "*dead capital*" so that it can be used as collateral for loans to fund new business or expand existing ones. The next step involves transforming property into collateral, collateral into credit, and credit into higher incomes. Apparently, much remains to be done on this.

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borrowers who would have paid default because other group members have done so). (See Khandker, Shahidure 1998:p.15).

<sup>6</sup> As Sam Daley Harris (2003) summarily put it, some of the expressions can go like "... This meeting is for serious people. Here we have to be serious about business. Somebody who is only selling a few vegetables is not serious about business. ... "

<sup>7</sup> "... The poor people see who goes to the programmes, and would just say 'this programme is not for us; it is for those better off people'..." (Sam Daley Harris (2003). The ASA (1997) study of 626 respondents (drawn from a mixture of ASA staff and clients) revealed different perspectives, perhaps as a result of focusing on the exclusion of the absolutely destitute. Almost all (98.8%) of respondents, and all the clients, said that lack of minimum clothing (*to leave the bari and attend a public meeting*) excludes the 'hardcore poor'. (Morduch, et. Al 2002).

<sup>8</sup> Johnson & Rogelly, (1997) p.12; reported similar serious "targeting errors" or "leakages" for the big micro-finance Institutions in Bangladesh, which in principle target loans away from the better-off, but the poorest, who are often landless (where the "poverty line" is .5 acre), are in fact left-out.

<sup>9</sup> Some authors advise that the methodology may also distract and **crowd-out** existing traditional mutual support networks particularly in times of repayment problems. They contend that in majority of poor communities, the rural poor have much less information on the behaviour of their immediate neighbours when it comes to "financial matters. Ana Marr (2001) in her study of microfinance clients in Peru, found that only 4% of all participants have prior relationships based on issues of borrowing and lending, i.e., they are members of common ROSCAs. All this means that the vast majority of participants are unfamiliar with financial issues when they first join the programme. When these group members are then confronted with *an alien way of relating to one another* – in this particular case, monitoring colleagues' loans, investments, returns, risks, and so on --, they tend to react very strongly and may resort to acts of intimidation, threats and even physical abuse in order to repress information about their financial affairs.



The *loan size* has been limited (until recently) to a maximum of Br. 5000, with a view to limiting it to the requirements of the poor. But some, having been clients to MFIs and having developed business skill, require loan size beyond this limit. There are policy revision in this regard currently. But on the other hand, it would be administratively too costly to retail very small loan sizes which might of course be welcome by the very poor, especially women. There are, for example, those very poor entrepreneurs who require very small loans (as small as Br. 100, 75,... or even below), for such activities as spinning, weaving, etc. Similar problems are also faced on the *loan term*.

Moreover, since frequently settling part of the borrowed money reduces the risk of repayment both for the client as well as for the lender, installment based repayments are encouraged. More efforts and *flexibility* are, however, needed to suit the *repayment rhythms* with the needs and income flows of the poor. For example, while setting repayment rhythms, it is clear that no serious attempt has been made to establish it on a detailed investigation and *market research* of households' income or cash flow using PRA tools like Seasonal Calendar, etc<sup>10</sup>. Rigid repayment schedules do not necessarily correspond to cash availability at the poor household.

As indicated above, *distance* is one of the most important determinants of transaction costs. Geography, ethnicity, culture, and social class create distance between borrowers and lenders. Much effort is being made to avail the services where the poor lives, thus reducing transaction costs incurred by poor clients, especially women. More importantly, given the high level of illiteracy among clients, maximum effort is made in order to establish *simple procedures* avoid cumbersome appraisal process that require sophisticated project proposal and other written applications that conventional banks require – clients only need to show that they have real business plan (new or on going), for which they need to fill in a simple (one page) format, indicating the loan amount, the input cost, output value, net return (profit), etc.

On the other hand, anecdotal evidence suggests that while male loan officers treating women clients with respect and dignity is empowering in and of itself, yet other women clients say they can relate more easily to a *female loan officer*, and that female loan officers provide a role model of achievement. Female loan officers are especially valued by women clients as role models for their daughters, showing an unplanned secondary impact of the program. Yet, there are only few female officers (about 20 %), especially at field level. These negatively affects the proportion of women beneficiaries joining the programme.

### *Improving Capabilities and Realized Achievements*

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<sup>10</sup> See in Graham Wright (2000): *Market Research and Client Responsive Product Development* MicroSave-Africa

As indicated above, resources and agency together constitutes “*capabilities*”, the potential that people have for living the lives they want, of achieving valued ways of ‘being and doing’, and “*achievements*” are particular ways of ‘being and doing’ which are realized by different individuals (Kabeer, 2004). The following paragraphs will elaborate some facts on both.

Minimalist Credit programmes are implicitly or explicitly based on the assumption that rural women are conversant with non-farm income generating activities, have sufficient time and labour to expand traditional, or start new, income generating activities. On the clients end, however, the most practical problem faced by MFIs is the very *low absorptive capacity* of the majority poor in rural areas, greatly constraining the potential positive impacts of access to microfinance programmes. Many rightly argue that credit alone, without the necessary infrastructure to enhance the skill capacity of the potential borrower, would often end up without achieving the intended goal of enabling the poor get out of poverty. This might sound more true given the objective reality in the rural areas of the region. There is no in-built mechanism to provide such vital ***Business Development Services*** that can enhance business development services for the poor women and men.

Thus, many clients, as can be expected, are very much *risk-averse* that even with the availability of credit service, they do not like to venture into activities other than those inherited from their fathers or for-fathers. In a recent interview of about 300 clients, over 78% responded that they only want to be engaged in activities that they know something about previously. Similar responses have been obtained from micro-finance clients in Tigray region, Adigudom (See Fiona, 2001).

There is also the problem of *cultural bias* towards some activities. The tendency (and the attendant competition for resources) is often to get on with such activities as agriculture, trade, etc, which are somehow free from cultural taboos. Some non-traditional activities which could provide alternative employment opportunities (like blacksmithing, weaving, tannery, pottery, embroidery, other handicrafts, etc...) are rather frowned at, and not easily taken up by clients. Experience suggests that they offer many advantages: they employ indigenous technology/local input, they are not land-based and are environmentally friendly. They enjoy less competition and are otherwise much more rewarding -- the data indicates that there is a statistically significant difference in profitability between these activities than traditional ones like agriculture. Yet, as indicated above, the total loan that went to finance such activities is less than 5%.

Demand for financial services also remains constrained for some cultural specificities. In some localities, for example, Muslims do not take credit or save in banks or microfinance institutions because paying or receiving “interest” is forbidden by religion. According to Muslim scholars, if someone indulges in trading (undertakes risk), the profit earned on it will be permissible. But earning money by the act of loaning is *haram*<sup>11</sup> (in discord with

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<sup>11</sup> Thus, most Islamic banking strategies have tried to remove all forms of fixed nominal interest rates. But the abolishment of fixed interest rate does not mean that no remuneration is paid on capital (nor does it encourage reverting to an all-cash or barter economy). Profit making is acceptable in Islamic society as

the Islamic code) (See Dhulmale and Sapcanin, 1999). This is more so particularly in the Muslim dominated areas of Oromia Zone in Amhara region, as well as in parts of south Wollo.

A related and more problematic issue is also the *low income perspective*<sup>12</sup> that prevail among most dwellers in many rural areas. Thus, after getting the additional ox that has been set as a target, or some level of income that provides for subsistence life, most would stop asking for more loan or only take a small amount<sup>13</sup>.

We can also discuss important issues related to *time poverty* women face. Generally, most domestic tasks such as grinding grain and food processing, water and fuel wood collection are known to be highly arduous, labour-intensive and time-consuming. And this applies to many women in developing countries in general. The burden of women in Ethiopia is compounded by the fact that *labour saving "appropriate" technology* is largely unknown even by the standards of developing countries. Access to clean water, grain mills, roads, energy saving devices, etc., is extremely limited. Some Ethiopian authors take the issue a bit further to argue the burden on women as relating to some cultural factors. Dejene (2000), for one, noted that Ethiopian rural women face significantly higher domestic labour burden (especially in the areas of food processing and cooking) than their counter parts in most of sub-Saharan Africa<sup>14</sup>.

Yet, not all loan destined to women is utilized by themselves. To encourage more women participation in business, ACSI has a target of delivering at least 50% of the credit service to women, which seems to have been attained. However, whether they are actually

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long as these profits are not unrestricted or driven by the activities of a monopoly or cartel. Islam deems profit, rather than interest, to be closer to its sense of morality and equity because earning profits inherently involves sharing risks and rewards. Thus, depositors in Islamic Banking can be compared to investors or shareholders, who earn dividends when the bank makes a profit or lose part of their savings if the bank posts a loss. Profit-making addresses the Islamic ideals of social justice because both the entrepreneur and the lender bear the risk of the investment..... But for some, although Islamic financial practices are founded on the core belief that money is not an earning asset in and of itself, there is more to the system's underlying tenets. Islamic religious law – that is, sharia – emphasizes ethical, moral, social, and religious factors to promote equality and fairness for the good of society as a whole which derives from the wider context of Islamic attitudes towards ethics, wealth distribution, social and economic justice, and the role of the state. Principles encouraging risk sharing, individual rights and duties, property rights, and the sanctity of contracts are all parts of the Islamic code underlying the banking system. In this light, many elements of microfinance could be considered consistent with the broader goals of Islamic Banking. Both systems advocate entrepreneurship and risk sharing and believe that the poor should take part in such activities. At a very basic level, the disbursement of collateral-free loans is an example of how Islamic banking and microfinance share common aims. (See Dhulmale and Sapcanin, 1999).

<sup>12</sup> See also the Federal Democratic Republic of Ethiopia (2002): *Rural Development Strategies, Policies and Instruments* paper.

<sup>13</sup> One may further enquire whether the famous theory of “Backward-bending Labour Supply Curve” is at work here in rural Ethiopia.

<sup>14</sup> Dejene hypothesizes that this is partly due to the sophisticated and labour intensive nature of domestic production arising from Ethiopian Highland *culinary culture*. For example, *teff* (the favorite food grain in Northern highlands) is not only labour intensive in its cultivation but also the preparation of *injera* out of *teff* is an equally labour and energy (fuel) intensive process. The preparation of home made spices (e.g., red pepper) is similarly a labour intensive task.

making use of the loan themselves, thereby improving their business skill and their *breakdown position*<sup>15</sup> is an issue requiring closer scrutiny. In fact, an additional area of concern, in terms of the impact of loans of the poorest, concerns *men's usurpation of loans* targeted specifically to women<sup>16</sup>. In a recent survey, the above issue has been directly posed to married women respondents. It is interesting to note that only less than 40% said that they themselves manage the loan, the rest either used it "jointly" with or totally hand it over to their male counterparts.<sup>17</sup> Yet, it seems that the mere fact that they are the sources of the credit access have improved their empowerment at least at the household level.

Thus, the above discussions would make it clear that availing resources, with appropriate terms and conditions suitable to poor people, especially women, and supporting them to take steps to address (the agency) barriers at individual and even community level that limit empowerment would only constitute capability or the potential that people have for living valued ways of being and doing. This has to be *realized into achievements* such as: being well-nourished, having long life-expectancy, and being fully integrated and active member of one's community. The following provides some evidence in this direction, focusing on issues related to food security.

For example, the previous surveys suggest that clients were to some extent able to increase their *food security* situation, and send their children to school. Yet, when examining the income impacts of microfinance programmes, it is important to recognise that there is a significant difference between "*increasing income*" and "*reducing poverty*". Despite the prevalent emphasis on raising incomes as the central objective of

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<sup>15</sup> Women's relative well-being depends on the relative bargaining power of the spouses. The bargaining power, in turn depends on the individual's *breakdown position*, which represents the welfare level which individuals (husband or wife) would have to face if this cooperation, or marriage, eventually breakdown (See Lutfun N. Khan Osmani 1998: p.32)

<sup>16</sup> As such increased income may come at the cost of depletion of other valued resources such as time, health and general well-being. Moreover, accepting that there may be many positive impacts of increased incidence of earnings among women, such as more autonomy and personal power, not to mention reduced poverty, this does not necessarily apply where women's wages remain low, or they are pressurized into surrendering their earnings to fathers, husbands, or other relatives. In turn, the market value of women's work may not be particularly important to women themselves compared with other aspects of their employment which, in a given social and cultural context, may be strongly valued at a personal level, such as modesty, respect, acceptability to husbands and kin, job fulfillment and/or the ability to reconcile paid work with childcare. (See in Sylvia Chant (2003)

<sup>17</sup> Similar impact study of credit programmes on women carried out on four credit programmes in Bangladesh: the Grameen Bank, BRAK, a large government scheme (the Rural Poor Programme RD-12), and a small NGO (Thangemare Mahila Senbuj Sengstha) by Goetz and Sen Gupt (1995) suggest that women retained significant control over the use to which the loan was put in 37% of cases; 63% fell into the category of "partial", limited or no control over loan use. Furthermore, women were found to have greater control over small loans made for purposes which did not challenge the *existing gender division* of labour (See Johnson & Rogaley (1997), p.13

development programmes, the two are not synonymous<sup>18</sup>. Clearly, the “use” to which income is put is as important in determining poverty and welfare as the level of income itself -- increased income can be (and often is) gambled away. The assumption of a “rational consumer” is often unattainable<sup>19</sup>. Indications are that a good deal of clients enjoyed improved food security. Yet, no one can tell whether such a food is nutritious (with nutrients, protein, iodine,...contents), for the child, mother and other household members. Apparently, the majority poor being served by microfinance has little access to such information on nutrition<sup>20</sup>.

These facts strongly suggest that the delivery of credit and other microfinance services in isolation leads to no where in terms of helping the poor, especially women, to enjoy realized achievements of being well-nourished, having long life expectancy, etc (See Chant, S. 2003).

### *Reducing Vulnerability*

Microfinance can potentially reduce vulnerability by helping microentrepreneurs diversify their sources of household income, increase their savings, expand their options for credit, and improve household money management. It also plays a protective role by helping to accumulate physical assets, increase expenditures on housing, and strengthen women’s role in collaborative economic decision making. The positive protective role of microfinance is related to the fungibility of credit within households and the common use of credit beyond the enterprise. The achievements so far are not so laudable.

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<sup>18</sup> See Graham A.N Wright (2000?): *The Impact of Microfinance Services: Increasing Income or Reducing Poverty*, MicroSave Africa.

<sup>19</sup> Christopher Dunford (2001): *Building Better Lives: Sustainable Integration of Microfinance and Education in Child Survival, Reproductive Health, and HIV/AIDS Prevention for the Poorest Entrepreneurs*, Freedom From Hunger discussion paper commissioned by the Microcredit Summit Campaign.

<sup>20</sup> The Conventional measure of poverty is based on the FGT (1984) model given by:

$$P_{\alpha} = \frac{1}{n} \sum_{i=1}^q \left( \frac{z - y_i}{z} \right)^{\alpha} \quad \text{where } \alpha \geq 0; z = \text{Total Poverty Line}; y_i = \text{Per capita consumption}$$

of household  $i$ ;  $q$  = number of people below the poverty line;  $n$  = total population. The issue is that the level of income attained by the household that can cover the cost indicated by the “Total Poverty line” or the “Food Poverty Line” simply doesn’t guarantee that the income goes to the purchase of food (and nutritious food) or other *basic need items* to the household and its members, unless additional information is provided. ...Indeed the “Capability Poverty Measure” (CPM) developed on the basis of the work of the economist, Amartya Sen, stresses that “Income and commodities were important only in as much as they contributed to people’s *capabilities* to achieve the lives they wanted (“functioning achievements”). The UNDP (1997) defines “functionings” as referring to the “valuable things that a person *can do or be*”, such as being well-nourished, having long life-expectancy, and being fully integrated and active member of one’s community. In turn, the “capability” of a person “stands for the different combinations of functionings the person can achieve”, and their freedom to achieve various functionings. (See Sylvia Chant (2003: 16): *New Contributions to the analysis of poverty: methodological and conceptual challenges to understanding poverty from a gender perspective*, United Nations, Women and Development Unit, Santiago, Chile).

As stated earlier, the potential for the microfinance service to enable the client to *diversify microenterprise* activities has been very limited. The survey for the Strategic Business Plan indicates that more than 78% of the clients actually are engaged in activities they already know. As indicated above, several factors dictate this very outcome. First and foremost, the opportunity to be engaged in other alternative employment is very much limited, simply because the BDS service is non-existent. The client, still very much risk-averse, do not want to be engaged in new activities with which they are not very familiar, even with the existence of the credit facility. Non-traditional activities that could provide such alternative are frowned upon, for cultural reasons.

Microfinance can also play a big role in reducing vulnerability of the poor by availing suitable *saving products*, and enhancing self-insurance. The need to save in cash for the poor is indeed very high for spending requirements related not just for *emergencies* but also to: *life cycle needs*, and economic *opportunities*. Thus, poor people, living in straw hut in a village or in an urban slum, run into problems with money management, and finding a safe place to store savings. The physical risks are the least of the problem. Much tougher is keeping the cash safe from the many claims on it - claims by relatives who have fallen on hard times, by importunate neighbors, by hungry or sick children or alcoholic husbands, and by creditors and beggars. Finally, even when one does have a little cash left over at the day's end, if one doesn't have somewhere safe to put it he/she will most probably spend it in some trivial way<sup>21</sup>.

Indeed, the poor *can* save, *do* save, and *want*<sup>22</sup> to save money. Only those so poor that they have left the cash economy altogether - the elderly, the disabled..., for example, who live by begging food from neighbours - cannot save money. Indeed most poor people want to save most of the time, while they do not want to borrow most of the time. Many people may not want to borrow at all because they have few things that they would like to borrow for, because they feel that saving before undertaking major expenditure is less risky or for moral or religious reasons. Moreover, often, it is when saving "in cash" is not convenient that the poor resort to saving in real asset<sup>23</sup>. The achievements in saving

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<sup>21</sup> Details are very well narrated in Stuart Rutherford (1999): *The Poor and Their Money*, Institute of Development Policy & Management, University of Manchester. For the different kinds of savings: "Saving Up", "Saving Down", and "Saving Through", see in Stuart Rutherford (2002?): *The Economics of Poverty: How Poor People Manage Their Money*, SafeSave, Bangladesh.

<sup>22</sup> Some argue that saving facilities for the poor serve very important social objective. According to the "Security Theory" children in developing countries are produced partly to provide informal social security. In situations with overcrowding and in cases in which parents do not take into account the negative externalities imposed by their children (through congestion, and environmental degradation, for instance), social welfare may be enhanced by shifting to alternative social security programmes. For example, establishing secure, convenient savings programmes may allow households to reduce the number of children they have without undermining their ability to cope with less income in old age and can provide a second round of benefits to the community through reductions in negative population-related externalities. (See: Jonathan Morduch (1999): *Between the State and the Market: Can Informal Insurance Patch the Safety Net?* The World Bank Research Observer, Volume 14, No. 2.

<sup>23</sup> The form of holding wealth or *capital formation* which a rural economic unit chooses depends on the return, the risk, the convenience and the flexibility or liquidity of the alternative investment opportunities. When saving "in cash" is not convenient, the poor resort to saving in real asset (crops put into storage, a

mobilization, however, leaves much to be desired, given the potential in the region. So far the number of voluntary savers is only about 160000. This is a very small achievement in a region with over 18 Mill population, about 3 Mill. households (over 90% living in rural areas with very little access to formal bank). Problems are multi-dimensional, yet the absence of aggressive *promotional work* is believed to be the key.

Like micro-saving, **micro-insurance** is a powerful poverty/vulnerability reducing tool, as well as a means for the institution to reduce risk<sup>24</sup>. In the Ethiopian case, since the loan are agricultural loans affected by drought, there is higher risk both for the clients and the institutions. The Ethiopian MFIs do not offer insurance services be it life, disability, health, crop damage insurance to their clients. The poor in Ethiopia are left out of the formal insurance market. However, as an MFI matures and the average loan size increases, providing loans become increasingly risky. Thus, developing insurance products will help address institutional long term profitability issues and provide protection for members against large and more destabilizing shocks. Insurance provision helps to minimize the risks associated with lending money to the poor.

*Emergency Loans* also provide solutions of last resort for the poor in extreme difficult circumstances. Just because a loan is used for emergencies (e.g consumption) purposes does not necessarily imply that repayment will falter. A significant number of poor households experience real constraints in the financial markets in the sense that they are unable to borrow as much as they would like at the prevailing transaction terms. Given that most of the poor attempt to borrow in order to finance consumption of food and other basic goods that enhance health and labour productivity, such constraints may force poor households to eat less food or cheaper foods with lower nutritional value. Also, when consumption levels are already precariously low, they may be forced to cancel or postpone profitable investments or sell assets -- sometimes at a substantial loss -- to meet *irreducible consumption needs*. This may lead to greater impoverishment in the long run. Such loans are so far no part of ACSI's microfinance programmes.

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house constructed, a pig fattened -- hence the idea of "piggy bank" -- a tree planted, or children raised (and educated) as an investment in human capital, helping one's neighbours and putting on a feast to raise claim for future assistance (social capital). But the return on such investments are not always very large since investments are made in order to save, and not vice versa, when other saving opportunities are unavailable (Schmidt and Kropp, 1987: 26).

<sup>24</sup> The Grameen experience is very interesting. Borrowers always worry what will happen to their debt if they die. Will the family members pay off their debt? They believe that if their debt remains unpaid after their death, their soul cannot rest in peace. Inclusion of loan insurance programme in GGS has made them very happy. This has become another popular feature of GGS. The insurance programme is very simple. Once a year, on the last day of the year, the borrower is required to put in a small amount of money in a loan insurance savings account. It is calculated on the basis of the outstanding loan and interest of the borrower on that day. She deposits 2.5% of the outstanding amount. If a borrower dies any time during the next year, her entire outstanding amount is paid up by the insurance fund which is created by the interest income of the loan insurance saving account. In addition, her family receives back the amount she saved in the loan insurance saving account. Borrowers find it unbelievably generous. Everybody loves it. (See Mohamed Yunus (2003?): *Grameen Bank II: Designed to Open New Possibilities* GRAMEEN FOUNDATION USA

One risk associated with taking a loan is that if household income flows are interrupted, a client may have to sell off productive assets to make loan repayment. There was some evidence that poor borrowers were forced into this *negative coping strategy* when hit by repeated shocks. MFIs might consider policies that allow poor households to *reschedule loans* when they are hit by sudden and devastating financial shocks. This could help clients protect their productive assets, avoid default, and remain in programs. It could also help reduce the risk to the MFI's portfolio. Evidence suggests that some 3.7% of the interviewed clients have in fact been more indebted because of taking loan. The skill and expertise is lacking on the part of field staff to accommodate all such demands of clients who might go to negative coping strategies. But more effort needs to be made to this end.

### 3) THE WDIP “SELF-HELP GROUP” APPROACH

#### *Perspectives on micro-credit*

The main objective of the **Women's Development Initiative Project (WDIP)** project is to empower women economically and socially and thus enable them play a great role in the development of the country. The target group of this project is *destitute women* who have the potential to run their business but lack the means. These women are encouraged to come up with their own business initiative. Their initiatives are evaluated and those who come up with realistic and smart business ideas are organized into groups and are given training. The training covers business skills, bookkeeping, financial management and gender, family planning, HIV/AIDS, environmental protection, nutrition, legal literacy and harmful traditional practices. On completing their training, each group constituting 10-20 individuals is given a maximum of 4000USD grant to start business. Some of the groups are engaged in group-based business activities while others work at individual level after borrowing money from their group capital.

As explained above, minimalist credit programmes are implicitly or explicitly based on the assumption that rural women are conversant with income generating activities. On the hand, the most practical problem faced by lenders is the very *low absorptive capacity* of the majority poor in rural areas, greatly constraining the potential positive impacts of access to microfinance programmes. Not every one is a business person. Indeed, most poor people want to save most of the time, while they do not want to borrow most of the time. Many people may not want to borrow at all because they have few things that they would like to borrow for.

In recognition of this, the self-help-group approach provides an integrated microenterprise services, not just credit and saving services, but also skill training, business development services as well as other advises. This provides an opportunity for poor people, especially women, to utilize the credit they are provided in a most effective manner. Thus, in comparison to the mainstream microfinance approach, the self-help group approach has some positive values in terms of delivering the microenterprise services to the poorest section of the population, especially women.



## ***Achieving the Empowerment Objective?***

### *Extending the Microfinance “Opportunities” to Poor Women*

Unlike in the case of MFIs which specifically target only the “productive poor”, there seems to be a need to specifically target people with less economic power, and support them until they reach a position where they can join the mainstream financial sector. One contribution to empowerment that *self-help groups* and other savings-based community groups offer to members is the pride of ownership and autonomy. Even though some self-help groups are given training and support from NGOs, the majority of even these externally supported groups rely primarily on member savings for their capital instead of on external capital as most village banks or solidarity groups do. Savings-based approaches that rely on minimal external support have several advantages. Women are proud to own their capital and have savings they can rely on. The capital stays in the community, and the women manage it themselves to *best fit their own needs and interests*. Because the external support costs are minimal, women are able to charge a lower rate of interest, and even a large percentage of that interest goes back to the women in the form of interest on their savings and community projects.

However, the empowerment benefits derived from independence and autonomy are often partially offset by weaker economic empowerment benefits. By depending on the savings of very poor community members, capital is more limited than it would be with external support, which in turn limits the growth potential of women’s enterprises and income. Although independent, savings-based self-help groups are viable alternatives for reaching remote, impoverished rural areas, and women, the very poverty of these areas may make it difficult to amass the savings necessary to extend credit in the amounts necessary to stimulate the development of a vibrant microenterprise sector.

Currently, the total number of ‘beneficiaries’ being served under the programme is about **11,000 women** (organized under 621 groups) although operation has been going on since 2001, in all regions of the country, 28 Zones, and 346 Kebeles.

### *Improving Capabilities and realized Achievements?*

This is another important feature of the self help group programmes like the ones promoted by WDIP. Indeed for the majority of the poor, entering into the business world is a very difficult challenge that they cannot manage by themselves, unless enough persuasion is done motivating them to start one. The most practical problem faced by MFIs is the very *low absorptive capacity* of the majority poor in rural areas, greatly constraining the potential positive impacts of access to microfinance programmes. Many rightly argue that credit alone, without the necessary infrastructure to enhance the skill capacity of the potential borrower, would often end up without achieving the intended goal of enabling the poor get out of poverty. Credit alone tends to be used to increase the *scale* of existing activities rather than to move into new, more sophisticated or higher value added areas. It was unusual for credit to trigger a continuous increase in technical sophistication, output or employment: it was much commoner for each of these variables

to reach a plateau after one or two loans and remain in a *steady state*<sup>25</sup>. Having been in operation for the last 9-10 years, and with a clear policy allowing for a loan size progression of individual enterprise (+100%, 75%, 50%, 25% additions from the 2nd loan cycle onwards), the average loan size for ACSI clients still stagnates at about Br. 1000.

Clearly, the fact that business development services are given along side the credit service is the right approach for poor women who have no previous experience in business. Groups become platforms for literacy, health, business education, disaster preparedness and improved agricultural practices (See Ashe 2005, Annex). This can potentially lead to the realization of achievement such as being well nourished, having long life expectancy, and being fully integrated and active member of of once community. However, the effectiveness of the business development service by WDIP need to be further investigated, and measures taken to make it *more appropriate* to the needs and requirement of very poor women.

### *Sustainability*

In the microfinance discussion, the '***double bottom line***' of institutional sustainability (financial returns to MFIs) and depth of outreach (social returns) constitutes the central issue. More recent arguments on the contribution of microfinance on enhancing social welfare, based on the traditional economists' tool of 'cost-benefit analysis', focuses the discussion on the net increase in total social welfare over and above the benefit to (private) customer that result from consumption of financial services. The net social benefit is determined by the depth, breadth, and length of outreach. Depth of outreach matters because society places greater value on helping the poor people than the better-off. Breadth of outreach matters because society values helping more people than fewer people. Finally, length of outreach matters, because society cares about the poor both now and in the future. Other things remaining equal, the greater the depth, breadth, and length of outreach, the greater the net social benefit (see Woller and Schreiner, 2004).

In terms of ***Depth of Outreach***: the fact that programmes are working in rural areas reaching rural villages, targeting very poor people, and giving priority to women, demonstrate the depth of outreach. Whether the target poor women actually received the subsidized services would, however, need to be examined with more data and analysis (some observations below).

However, since the programmes focus on the poorest of poor women, and only limited to few geographical areas serving few clients, it lacks in "***breadth of outreach***" and it cannot enjoy the advantages of *economies of scale* that most MFIs enjoy. Wider outreach

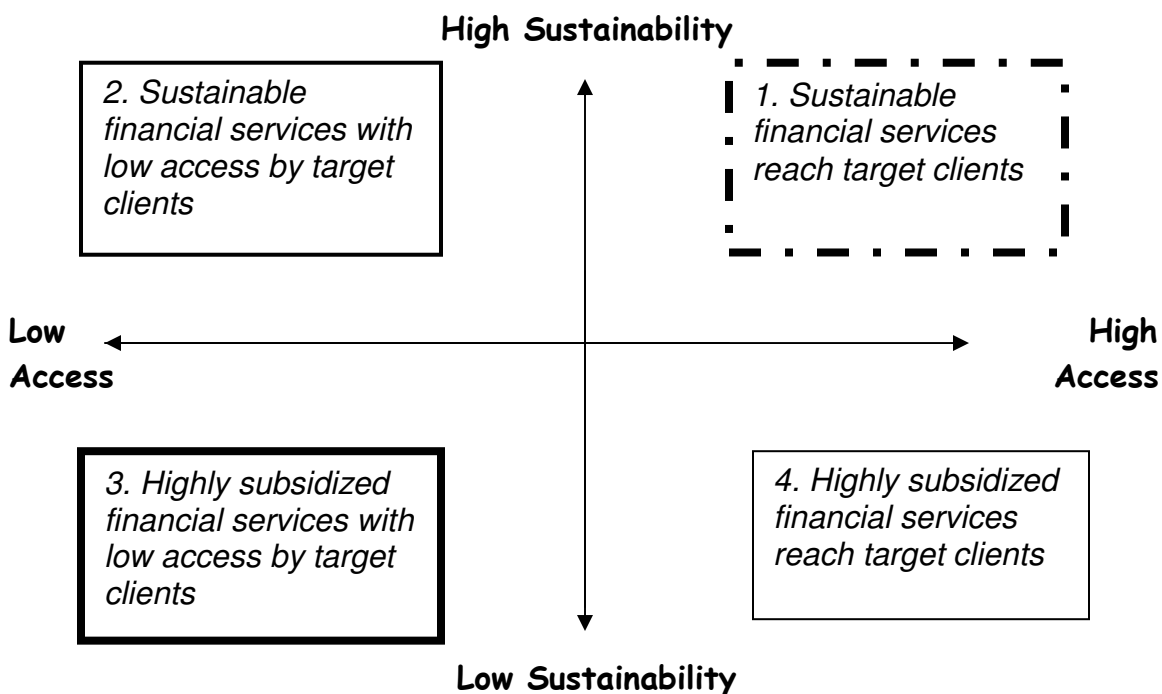
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<sup>25</sup> Jonatan Dawson with Andy Jeans (1997): Looking Beyond Credit: Business development services and the promotion of innovation among small producers, Intermediate Technology [p: Summary]

implies that the costs of having to serve poorest areas and very poor people, taking only very small size loans and saving in smaller amounts would be covered by the better earnings of operating in areas with good infrastructure and serving clients who can take larger loans or saving bigger amounts.

On the other hand, the ability to survive without looking for donations or other subsidies matter for sustainability. For the poor to get out of poverty, they require sustained microenterprise services like credit<sup>26</sup>, and thus the ***length of outreach*** matters very much. This requires ensuring profitability and full repayment. MFIs currently can maintain a repayment rate of over 98%, and a Portfolio at Risk (which compares the remaining outstanding balance with at least one installment overdue to the total loan portfolio) of less than 5%. The following chart illustrates the sustainability issue more vividly (World Bank, 2003).

### Optimizing Performance



*N.B: The micro-credit industry has sought to resolve the tensions between a focus on poverty and a commitment to sustainability by integrating them within a matrix defined by two axes, or outreach (or access) and financial sustainability. The formal financial sector may achieve financial sustainability, but has little outreach to poor clients (quadrant 2). Traditional efforts by non-governmental organizations (NGOs) may reach poor clients, but are often unsustainable (quadrant 4). Good microfinance practice, on*

<sup>26</sup> A World Bank study conducted in the early 1990's based on an intensive survey found that it takes about five years for Grameen Bank programme participants to rise above the poverty line income level and about eight years to reach a situation where they do not require loans from targeted credit programme. (See Hashemi 1997, p.113).

*the other hand, combines both outreach and sustainability in the virtuous quadrant 1. Such practice is perhaps most clearly embodied in the microfinance bank, which marries the best of the formal financial sector in terms of sustainability with the outreach to the poor clients of the development NGO.*

The **incentive structure** often have a serious impact on the **length of outreach** and thus and sustainability of the service. Indeed, the current effort by MFIs to generate the loanable fund from within the local areas has served to create loan clients' sense of ownership and prompt repayment by inculcating the feeling that what is in their hand in the form of credit is a saving mobilized from their neighbors ("warm money"). According to Fiebig (Fiebig, et al 1999, p8), the term "**warm money**" refers to the fact that depositors consider themselves "quasi-shareholders" of financial institutions whose funds are exclusively constituted of locally mobilized savings. Because customers invest their own money in the financial institution that provides financial services exclusively to them, it is in their own interest that an efficient intermediation of their financial resources takes place. Therefore, "warm money" creates responsibility and financial discipline through savings in comparison to an injection of money from external sources ("**cold money**"). For the mainstream self-help groups which mobilize members' savings for re-lending for other members the incentive problem would have been largely averted. But as long as these groups remain dependent on external resources, the incentive problem would exist.

Moreover, since repayment is linked to the profitability of the activity being financed, borrowers who expect to have to repay their loans tend to be more careful in their choice of micro-projects than those who do not expect to repay. Low repayment, like low interest rate, may lead to **capital mis-allocation**, since borrowers can make money even from socially unprofitable projects. (See Inter-American Development Bank, 2001, World Bank 2003).

#### *Does the Subsidy Reach the Poor? The problem of (Mis)Targeting*

The objective of reaching poor people, especially women, through micro-enterprise services is a holistic task worth undertaking. However, there are often "targeting errors" and the services which are intended to reach poor and "marginalized" people would end up in the hands of the better-off, or those who can access alternative services. Subsidies would induce excess demand from **all** types of applicants, poor and non-poor, Influence and patronage and better connections inevitably bias the distribution of the "subsidized" credit in favour of the better off -- more so when the local *targeting* mechanism is lax (See also Braverman and Guasch, 1993).

And this is not just limited to the case of credit delivery. Any trade which involves any kind of subsidy, is prone to some kind of corruption, or black-marketing. A good example of this is the one of the sugar supply in local *Kebele* shops which is subsidised by the government, with the good intention of supporting the poor through lower prices. Who manages to buy this commodity and ultimately benefits from the subsidy? More often than not, the better-off. The delivery of health services targeted to the poor is yet

another example. To take advantage of this service, individuals need to carry a proof of their poverty in the form of a letter from their local administration (the *Kebele* administration). Again, it is more often the better off who manage to obtain these letters thus benefiting from the subsidised health delivery. The World Development Report 2000/2001 (World Bank, 2001) reports a similar story: a large study in two African countries - Guinea and Mozambique - found that eliminating food subsidies did not hurt poor people because the subsidies had not reached them in the first place!

Moreover, if same type of people (in terms of income and risk profile) receive different terms and conditions for credit and other micro-enterprise services, this results in unfair competition in the market, by creating market segmentation. Such **market segmentation** and lack of competition also results in inefficiency. Clients with *identical loan demand and risk profiles* can receive different terms and conditions depending on source of funding (Inter-American Development Bank, 2001). Thus, for example, a producer that has access to subsidized credit can price her/his product lower than the one who borrowed at market interest rate, and thus the latter will be placed at a disadvantaged position. ... In fact, if such programmes do not follow strict business discipline and price their services properly, the "subsidized" fund pumped in the economy will affect the economy as a whole.

#### 4) THE WAY FORWARD?

Some tentative conclusions and recommendations are provided below:

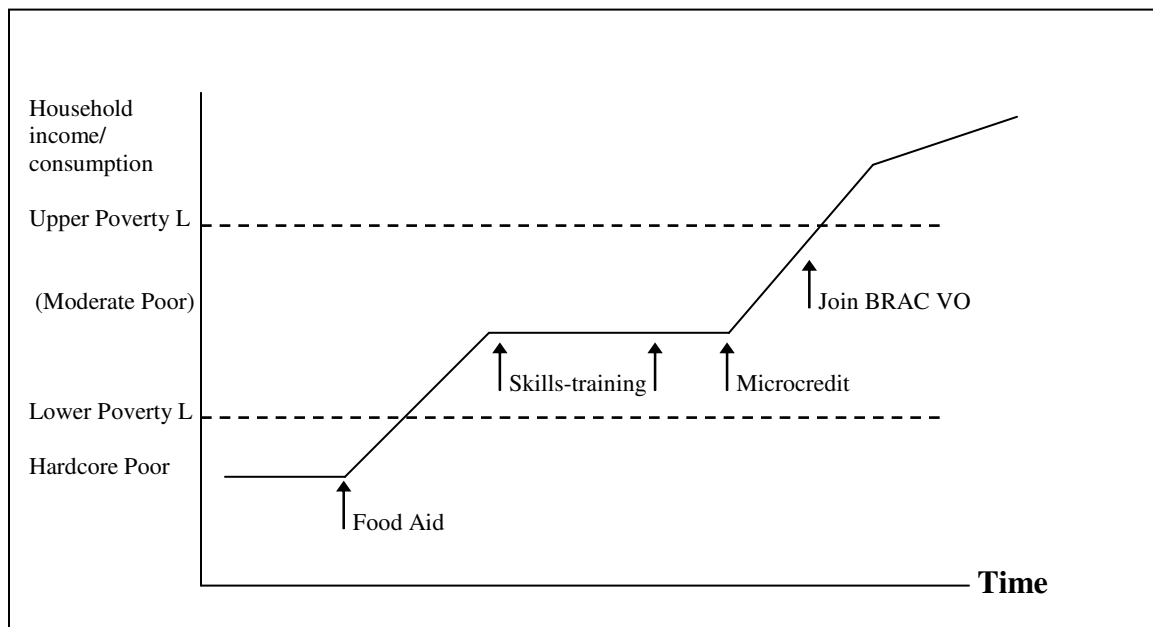
*Savings-based self-help groups* are viable alternatives for reaching remote, impoverished rural areas, and women, they also offer to members the pride of ownership and autonomy. This would be true as long as the groups rely primarily on member savings for their capital instead of on external capital. They need genuine support, particularly **capacity building**, to reach this level of independence. They are often prone to corruption and manipulation. Skills in liquidity management, finance, corporate governance, cooperative development, etc, are prerequisites for the success and sustainability objectives. Moreover, if indeed we seek to promote empowerment, we must also consider factors affecting women's status and rights **as a group**. With some support, groups of economically empowered women can take steps to address the cultural and legal barriers that limit their social and political empowerment.

However, the objective of lifting them out of poverty in just **18 months** may not be achievable for the majority of cases. One of the requirements for the poor to escape poverty through self-employment is sustained micro-enterprise services, like micro-finance. Thus, a way has to be sought whereby the beneficiaries can access an on-going services by linking these programmes with the on-going mainstream or micro-finance programmes.

The *Income Generation for Vulnerable Groups Development (IGVGD)* program of BRAC (Bangladesh) provides the best documented evidence for a **Productive Safety Net**, that the poorest can be bankable if provided sufficient non-financial support services. The

program *targets destitute*, rural Bangladeshi women who have few or no income-earning opportunities. The IGVDG program has provided food grain assistance and savings and credit services to nearly a million participants over a ten-year period. About 85 percent of its members also received training and support in poultry and livestock rearing, vegetable gardening, agriculture, fishery production, or grocery business. They get this “special support” for about 18-24 months, and they are expected to join the “mainstream” financial sector afterwards. Two-thirds of these women have graduated from absolute poverty to become microfinance clients, and have not slipped back into requiring government handouts. The IGVDG experience confirms that programs that combine livelihood protection (food aid) and livelihood promotion (skills training and microfinance) can reach deeper than purely promotional schemes to benefit the chronic poor (See CGAP: 2000 for a detailed presentation).

### *The idea Behind the Strategic Linkage Approach*



Both kinds of programmes need to undertake important improvements in their programmes, kinds of products they deliver, the terms and conditions, etc.

a) *Diversify lending methodology*: The *Group Guarantee Lending Model (GGLM)* is the dominant methodology, for MFIs in particular. But more options need consideration and appropriate steps and capacity building efforts should go in appropriate direction. Among them, the ***warehouse receipts system***, whereby stored agricultural commodities (crops, etc..) can serve as collateral can facilitate credit for inventory or products held in storage. The ***titles to land*** are currently non-existent, and therefore land cannot be used as collateral. The tenure security, if formalized and governed by legal rules, affords certificate holders indisputable proof of right to land, and in this way land can also be a base for mortgage system for provision of credit facility. On the other hand, ***leasing*** is a

financing tool that overcomes many constraint. In leasing, the provider (lessor) owns the equipment and permits the client (lessee) to use the equipment in exchange for periodic lease payments. The *loan guarantee scheme* can also play key role in expanding services. The majority of the financial institutions in rural areas are conservative, relying heavily on heavy asset and collateral-based requirements; they are reluctant to lend to potentially risky smaller enterprises and especially to sectors where they have little or no lending experience. Creditworthy private farmers and small agribusinesses, especially women, have difficulty meeting such conditions. Loan Guarantee Schemes, accompanied by skill upgrading of Banks/MFIs in risk assessment of borrowers will be a step in the right direction.

b) *Credit with Education*: Credit must, above all, be accompanied by some kind of marketable skill development, which the poor seriously lack. Credit alone can only increase the "scale" of existing activities rather than enabling the poor to move into new or higher value activities. Some kind of *cultural transformation* may also be called for at this particular juncture in order to change the attitudes of some otherwise poor people who are reluctant, for cultural reasons (including religion), to engage themselves in non-traditional activities which are much more rewarding indeed. Integrating *Credit with Education* programmes provides the right alternative. In particular, in a group-based lending, the borrowers' meeting provides good *forum for education*, with a "regular" face-to-face contact with an educator. Center/group meetings of micro-credit clients, would provide convenient, low cost method to provide: Health/Nutrition (Family Planning, Immunization, Child Nutrition, Sources of Vitamin A, Breast Feeding, Diarrhea prevention and management); Socio-economic/Legal Issues (Business Management – Increase your sales – Constitutional rights, property rights, prevent early marriage, domestic violence, etc (See Dunford (2001), Mcknelly, et., al (2002), and Sebstad, et., al (2003). Moreover, the solidarity structure, joint guarantee mechanism fosters a supportive atmosphere of collective self-interest among the group members, and clients' successful management of the loans is likely to boost their confidence and thereby their willingness to try new practices for better health and other benefits (See Credit with Education design in Annex).

Government, donors, NGOs and others need to take attention for the following points:

a) *Rural infrastructure*, particularly the road net-work needs special attention by government and others for a healthy microfinance operations. Given that the poor are largely involved in few enterprises, the risk is indeed high if similar products cater only for the small market nearby, which easily saturates, diminishing potential profitability. Relevant *market information* and networks are also vital. In particular, women stand at the crossroads between 'productive' activities and the care of human beings (the care economy). *Labour-saving technologies* need to expand in rural areas. Subsidized childcare and elderly care facilities, public health care programmes, public transport and piped water/electricity help women meet their dual responsibilities and facilitate their participation in *capability building activities*.

*b) Education about microfinance* also needs to be enhanced. Policy makers, experts in the government sector, NGOs, donors, researchers, and the public – in Ethiopia and elsewhere – have limited knowledge of the regulation of microfinance. For example, other departments of the federal government also working in poverty alleviation projects hardly understand the role and objectives of MFIs in Ethiopia. As such, increased education about microfinance in Ethiopia would help other policymakers understand its role in a comprehensive poverty alleviation strategy, thus garnering their collaboration and support for these initiatives.



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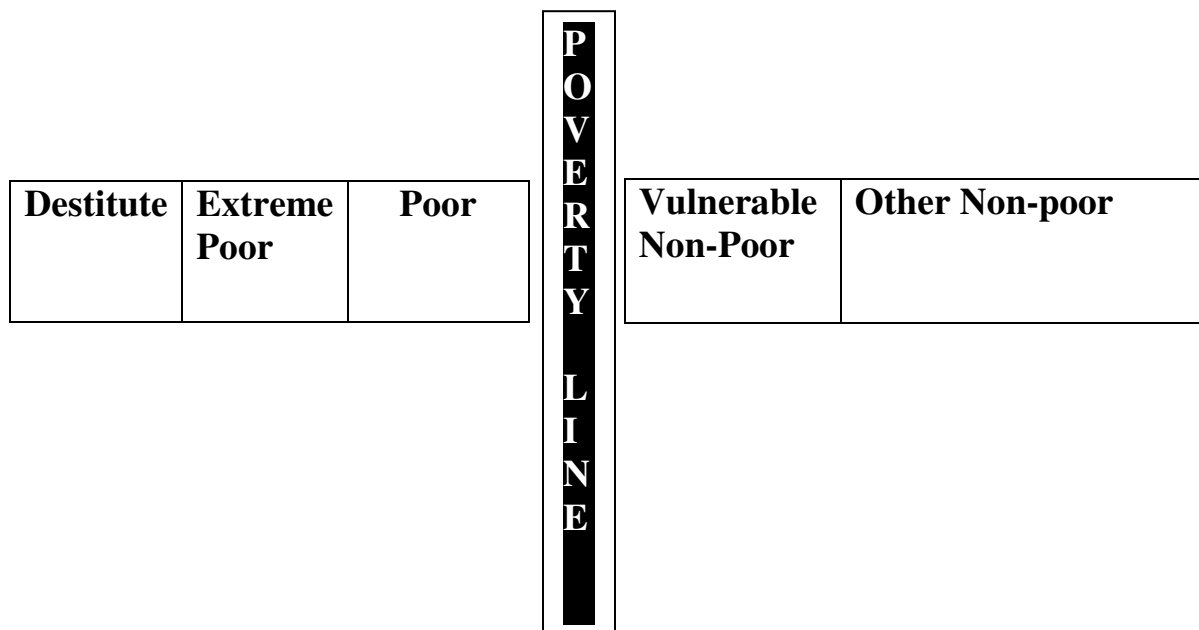
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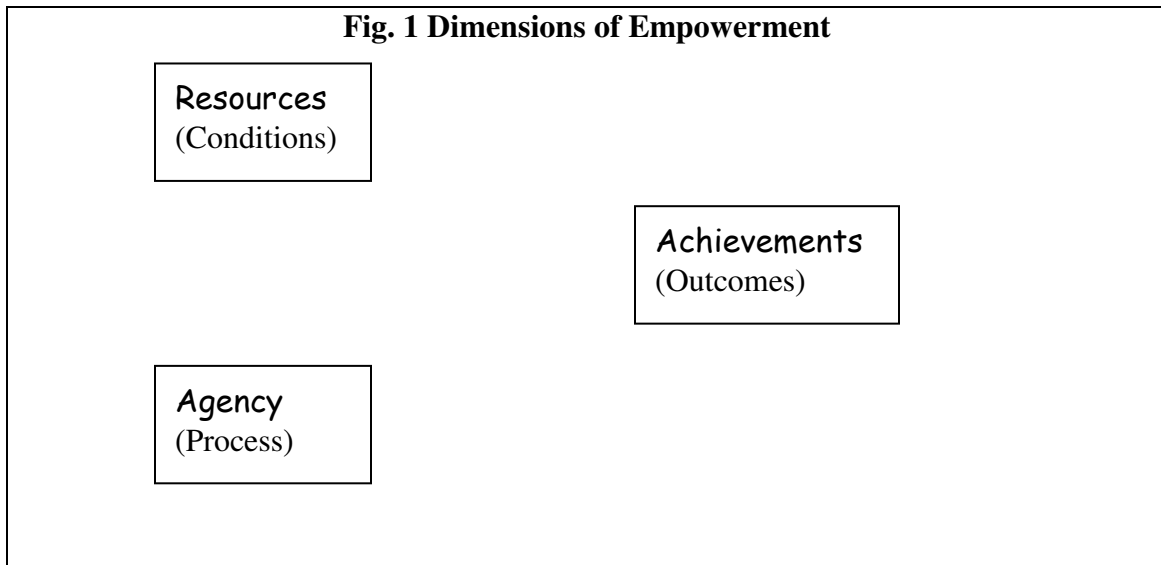
Figure

### Defining Poverty



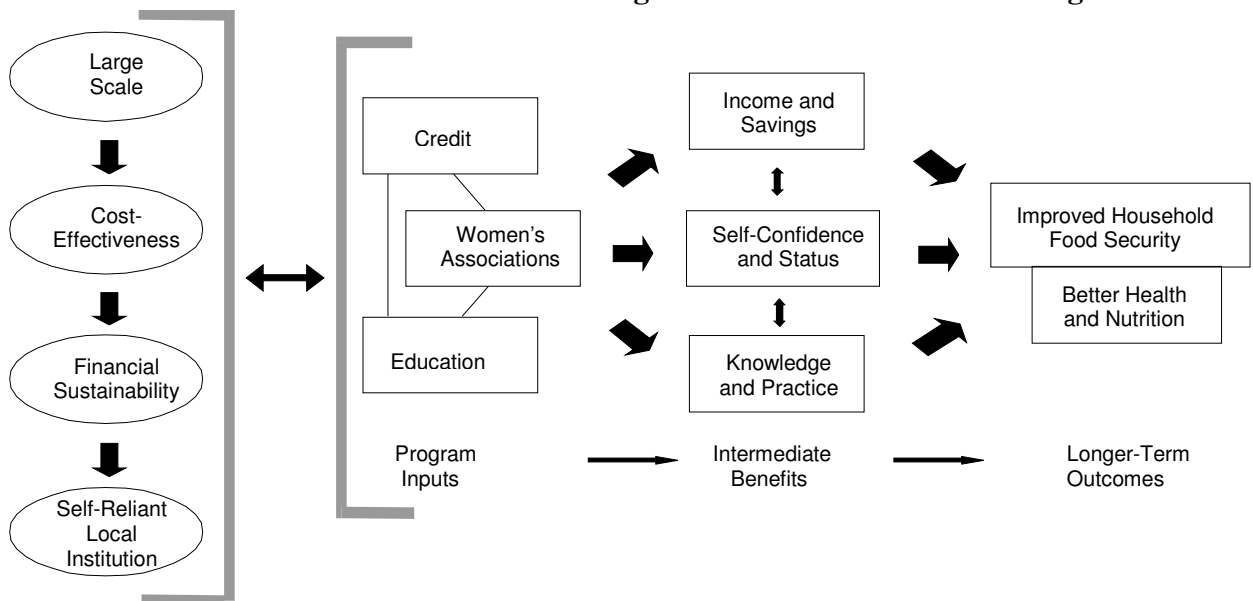
**ONE OX**  
**(Microfinance Targeting)**

***Resources, Agency, Achievement:***



Kabeer, Naila (2004): *Resources, Agency, Achievements: Reflections on the Measurement of Women's Empowerment*, in "Discussing Women's Empowerment: Theory and Practice" Sida-Studies no.3

### The Original *Credit with Education* Design





<b>ROSCAS AND BANKING ON THE POOR SELF-HELP GROUPS COMPARED</b>	
<b>TYPICAL ROSCA</b>	<b>BANKING ON THE POOR SELF- HELP GROUPS</b>
<ul style="list-style-type: none"> <li>Members wait their turn for their pay out even if they need money earlier.</li> </ul>	<ul style="list-style-type: none"> <li>Members take out a loan when they need it (if funds are available).</li> </ul>
<ul style="list-style-type: none"> <li>No interest charged and no return on savings.</li> </ul>	<ul style="list-style-type: none"> <li>Group fund grows with loan interest. The return on savings depends on the interest rate and the percentage of the fund loaned out</li> </ul>
<ul style="list-style-type: none"> <li>No review of how pay out is used.</li> </ul>	<ul style="list-style-type: none"> <li>Members discuss how loans will be used.</li> </ul>
<ul style="list-style-type: none"> <li>Group disbands when the last member receives her pay out.</li> </ul>	<ul style="list-style-type: none"> <li>Group decides if it will disband and distribute the fund at the end of the cycle or continue saving to grow the groups' resources.</li> </ul>
<ul style="list-style-type: none"> <li>The poorest are often excluded because they do not have a regular income and/or the payments are too high for them.</li> </ul>	<ul style="list-style-type: none"> <li>Groups can suspend or decrease payments during the "hungry season" and save more after the harvest reflecting the variability in income of poor villagers. Each group sets its own savings rate.</li> </ul>
<ul style="list-style-type: none"> <li>Little flexibility because records are very simple or non- existent.</li> </ul>	<ul style="list-style-type: none"> <li>Better record keeping makes it possible to build in variable savings, savings withdrawals and loans of different lengths and amounts.</li> </ul>
<ul style="list-style-type: none"> <li>Groups have little formal structure other than the group leader</li> </ul>	<ul style="list-style-type: none"> <li>Group goal setting, bylaws, electing officers, holding officers accountable and problem solving training lead to stronger groups.</li> </ul>
<ul style="list-style-type: none"> <li>Traditional groups with poor or no records have little chance of accessing external loans.</li> </ul>	<ul style="list-style-type: none"> <li>Well organized groups may be able to secure loans from credit unions and MFIs if they need more capital.</li> </ul>
<ul style="list-style-type: none"> <li>Little or no link to other development inputs.</li> </ul>	<ul style="list-style-type: none"> <li>Groups become platforms for literacy, health, business education, disaster preparedness and improved agricultural practices. Malaria prevention will be the first topic introduced to the groups. Oxfam America and Freedom from Hunger are carrying out BOP jointly</li> </ul>
<ul style="list-style-type: none"> <li>Exchange of ideas b/n groups occurs informally through exchanges in markets or among friends.</li> </ul>	<ul style="list-style-type: none"> <li>Strong groups share innovations through meetings and exchanges organized by animators.</li> </ul>
<ul style="list-style-type: none"> <li>Each group operates independently.</li> </ul>	<ul style="list-style-type: none"> <li>Groups are organized into associations that take on roles such as caring for the neediest or the sick, campaigns to encourage women's rights, community projects, or disaster preparedness.</li> </ul>
<ul style="list-style-type: none"> <li>Since payouts are taken in turn, members often use money lenders for emergencies.</li> </ul>	<ul style="list-style-type: none"> <li>Risk is mitigated through loans for emergencies; health training; business education; loan reviews; and increased cooperation between members.</li> </ul>
<b>SOURCE: Jeffrey Ashe (2005): <u>BANKING ON THE POOR: SAVING AND LENDING GROUPS FOR THE POOR</u>, Community Finance, Oxfam America March 5, 2005</b>	

<b>Examples of Financial Education Topics</b>	
Basic Principles of money management	Assessing your financial situation Setting financial goals Distinguishing between needs and wants Assessing your financial ‘personality’ or ‘style’
Managing cash flow	Making a financial plan Developing budget Following a budget Spending wisely – stretching your money
Building assets	Housing, land, property, and other physical assets Investing in a business Protecting assets
Dealing with life cycle events	Marriage Household formation Birth of children Children’s education Retirement/old age Death
‘Interfacing’ with formal and informal financial institutions	Saving – opening a saving account; setting saving goals; participating in ROSCAs Borrowing – when to (and not to) borrow; risk associated with borrowing money; comparing loan terms and conditions; calculating interest; how to manage debt Insurance – understanding what it is and can do
Dealing with special challenges	Illness of family members Death of family members Own illness Extending help to other families Divorce or family breakdown Job loss Natural disasters/calamities
Financial decision making process	Joint decisions Independent decisions
Planning ahead for the future	Investment Old age/retirement Death
Earning money	Money making ideas Looking for a job (paid employment) Starting and managing your own business Career planning
<b>SOURCE:</b> Sebstad, Jennefer and Monique Cohen (2003): <i>Financial Education for the Poor</i> , Microfinance Opportunities, <a href="http://www.microfinanceopportunities.org">www.microfinanceopportunities.org</a>	