



GRAMEEN FOUNDATION

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Microfinance: A Platform for Social Change

by Marge Magner

March 2007

Grameen Foundation Publication Series

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Foreword

Microfinance began as a series of experiments in how to use finance to empower the poor, and has now evolved into a robust movement and industry. Today, microcredit for investment (particularly for working capital) remains the sector's core product, but other financial services such as microsavings and microinsurance are emerging as powerful complements to loans.

As we observe the recent waves of innovation in microfinance, particularly in Bangladesh where the “Grameen Family of Companies” is an especially robust laboratory for pioneering approaches to social business enterprise, we at Grameen Foundation have begun to talk about microfinance as a platform for multiple development and business ventures, rather than as a financial product or suite of products. We stand in awe of what Professor Muhammad Yunus has accomplished and continue to celebrate his richly deserved Nobel Peace Prize. Furthermore, we believe that the collective infrastructure of people, facilities, relationships, and knowledge that the microfinance movement has amassed can and should be used for more than provision of financial products.

The potential of microfinance to serve as a platform for launching complementary approaches to addressing the needs and opportunities facing poor families, particularly their health and educational attainment, is not obvious to everyone. I was therefore very pleased when, during my initial conversations with Marge Magner, she immediately grasped the potential of this paradigm and was one of the most articulate proponents of it I had ever heard. As arguably the most accomplished female banker in world history, I was eager to have her go on record with her views since I thought it could influence the dialogue going on in the microfinance sector about this and related issues. Her roles as a business and philanthropic leader (who chaired the Citigroup Foundation for many years) make her uniquely credible and informed on this issue. This paper is the outcome of my request that she make the case for microfinance as a platform. It is beyond my expectations and a tribute to her dedication to a more just world. I wish to thank GF Board member Rosanna Ramos-Velita for bringing this issue to Marge's attention and for adding her ideas along the way.

This paper was a team effort. On behalf of Marge and our senior management and board, I would like to thank Jay Bakhru, who served as the leader of a research team that assisted Marge with this project. He had an invigorating and challenging job, and one cannot think of someone coordinating such an effort in a volunteer capacity and doing it with so much intelligence and grace. The others on the research team were Diego Berta, Farhana Choudhury, Shikshya Khatiwada and Seema Vora. Each added unique and important perspectives and passion to this project. Trang Tran provided invaluable assistance in the editing process.

During the course of the research, the team interviewed many microfinance practitioners, including Professor Muhammad Yunus (a few weeks before his Nobel Peace Prize was announced), Anne Hastings of Fonkoze and Carmen Velasco of Pro Mujer. The team also consulted with business leaders including Ed Scott, the founder of BEA Systems. Each

interviewee articulated their vision of microfinance and how it can be a platform and network to support social change, and in so doing shaped this paper. Given time and additional resources we would have talked to many others who believe in this approach. We encourage further research and dialogue that builds on what Marge has written here in her characteristically concise, incisive and understated manner.

If we are going to reach the Millennium Development Goal of halving poverty by 2015, we will need to not only grow the microfinance movement but also reimagine it. We see latent and yet unexplored capacities of the network of 113 million poor families currently served by MFIs, and the MFIs themselves, to be a force in shaping the political economy of the 21st century. We therefore call on microfinance practitioners, academics, business leaders and others to think and act with creativity and urgency in leveraging this capacity to accelerate progress.

We remain mired in a global poverty crisis. But there is hope. Our sector has quietly assembled arguably the largest network of poor people in world history, a network that is touched by the microfinance institutions that serve them on a weekly basis in most cases. Let Marge's words inspire us to seize the opportunities before us and bring closer to reality Dr. Yunus' vision of putting "poverty in a museum" as this generation's legacy to the next.

Alex Counts, President
Grameen Foundation USA
March 20, 2007
Washington, DC

About the Author

Ms. Magner is a founding member and general partner at Brysam Global Partners, a private-equity firm that invests in consumer financial services in emerging markets, an area where she has extensive experience based on her accomplishments in banking and international development.

Prior to the formation of Brysam Global Partners, Ms. Magner served as chairman and CEO of the Global Consumer Group at Citigroup from 2003 to October 2005. In this position, she was responsible for the company's operations serving consumers through retail banking, cards and consumer finance, as well as for finance, credit and other staff functions. During this time, Ms. Magner was named to *Fortune* magazine's list of the "Most Powerful Women in Business" from 2001 to 2004, and was also ranked on *Forbes* magazine's list of the "World's Most Powerful Women" (#19), and the *U.S. Banker's* list of the "Most Powerful Women in Banking" (#1) among others.

In addition to achievements in business and banking, Ms. Magner is a passionate advocate on issues affecting consumers, women, and youth. From starting Community Development and Microfinance business units at Citigroup to championing issues such as global poverty, microfinance, and children, Ms. Magner helps to bring a more integrated, innovative business approach to the philanthropic world.

Currently, she is a director of Accenture, Gannett Company, Inc., and The Charles Schwab Corporation.

She also serves as chairman of the Brooklyn College Foundation, and is a member of the Dean's Advisory Council for the Krannert School of Management at Purdue University, as well as the boards of Millennium Promise and Do Something.

Ms. Magner holds a B.S. degree in psychology from Brooklyn College and an MSIA degree from the Krannert School of Management, Purdue University.

Acknowledgements

Ms. Magner would like to thank Grameen Foundation for providing her with the opportunity to contribute to their mission of fighting global poverty with microfinance, and also the staff for their support throughout the process. She would also like to thank the many contributors to this paper: Jay Bakhru, who did a terrific job leading the research team from interviewing leading thinkers and practitioners of microfinance to generating great insights into the development of this paper to make it possible; Seema Vora, who provided us with valuable research; a talented team of Brooklyn College students—Diego Bertra, Farhana Choudhury, and Shikshya Khatiwada—who spent many hours enthusiastically researching, learning, and sharing ideas on this topic; and Trang Tran, who shares a passion for microfinance and helped shape the paper.

About the Contributors

Jay Bakhru is a vice president in Citigroup's Global Consumer Group. He holds a B.A. with Honors from Brown University and an MBA from the Wharton School at the University of Pennsylvania. Jay is from Philadelphia, Pennsylvania.

Diego Berta is an associate research analyst at ThinkEquity Partners, LLC. He graduated with honors from City University of New York – Brooklyn College, where he received a B.S. in Business and Finance. Diego is from Mendoza, Argentina.

Farhana Choudhury has attained a B.S in Business Management & Finance and a B.A in Economics from Brooklyn College, City University of New York. She is from Brooklyn, New York and is currently pursuing a M.A in Developmental Economics.

Shikshya Khatiwada is a graduating senior at Brooklyn College pursuing a degree in Business Management and Finance. She will join Goldman Sachs and Co. as an analyst upon graduating this summer. Shikshya is originally from Nepal and is a current resident of Brooklyn, New York.

Seema Vora is a Campaign Coordinator with Team and Training at the Leukemia Lymphoma Society. She graduated Magna Cum Laude from American University where she received a B.A. in International Relations. Seema is from Long Island, New York.

“There is no conflict in having microcredit, education, health, empowerment, [and] training together; they support each other. If you laid out the foundation of the financial system, it makes other interventions so much more powerful. If you come with education, health, and training, everything will make much more sense, and you get much more mileage out of it, provided you have the microcredit framework already built into it.”

- Dr. Muhammad Yunus, Founder of Grameen Bank and Nobel Peace Prize Winner 2006¹

I. Introduction

The phrase “Customer is King” may be an oversimplified cliché in business, but – stripped of all its bells and whistles – this phrase represents the essence of a consumer business. A business’s survival depends on serving and meeting customer needs and demands. Businesses have to focus on their customers, their needs, their behaviors, and a multitude of other factors that impact their lives. A successful, thriving business can no longer be an isolated business; it must adapt to customers and the marketplace. Increasingly, businesses from differing sectors— from technology to entertainment to retail and even to banking—are partnering with each other to cater to the same customer base or extend their own client access. Today, people can access banking products and services practically anywhere – post offices, online, and through mobile devices. In addition, financial service providers offer financial education, consumer awareness, and even training and seminars on managing personal finances as well as small businesses. Based on this same concept, we believe that microfinance can better serve its clients by extending services to meet their life demands.

Over the years, microfinance has demonstrated that its impact goes beyond providing individuals with access to capital; it has also helped to protect, diversify and increase their sources of income and assets that enable them to make their way out of poverty. It has shown that when we provide capital to poor individuals with entrepreneurial ideas and spirit, they will utilize that capital to generate income for themselves and their families – offering them the potential of a life that is poverty free. To date, microfinance has touched the lives and communities of more than 100 million families, and has helped lift many of them out of poverty or at least put them on a pathway to a poverty-free life. However, more than three billion people still live on less than two dollars a day; more than a billion have no access to electricity; and three billion have no access to safe sanitation. For these individuals, microfinance is a tool that must continue to be deployed and leveraged to its maximum potential.

Access to capital has provided people with the opportunity to climb the economic ladder. Nonetheless, we have witnessed that simple access to capital, while paramount, is often not enough to realize the kind of rapid poverty reduction that is needed to reach the Millennium Development Goals. For some, capital is the missing element in their struggles against poverty. For others, capital is overshadowed by non-financial factors that also contribute to poverty. Therefore, to create solutions that address poverty and to enhance the existing use of microfinance, we need to understand that poverty is a result of a multitude of factors that encompass more than merely a limited income. According to the Chronic Poverty Research Centre, “chronic poverty is typically characterized not only by low income and assets, but also by

¹ Interview with Dr. Muhammad Yunus (September 2006).

hunger and malnutrition, illiteracy, the lack of access to basic necessities such as safe drinking water and health services, and social isolation and exploitation.”²

Because poverty encompasses more than just finance, microfinance—a purpose-driven business—needs to look beyond just offering credit or banking services to the poor. To properly serve clients’ needs and fulfill its purpose, microfinance needs to do more to address the underlying factors of poverty than simply providing access to capital. This paper argues that although microfinance is an effective poverty alleviation tool, it should be utilized as a platform for multiple empowerment approaches, building on the successful models being pioneered by a few microfinance practitioners. In other words, microfinance should leverage its position in the field and relationships with clients to deliver other social and development services. By integrating different approaches and models to deliver a variety of basic poverty alleviation services to the poor, these individuals will have a greater chance of lifting themselves out of poverty, and, more importantly, staying out of poverty.

II. Overview of Microfinance

Because the term microfinance is used in many different contexts, it can sometimes be oversimplified and viewed in a skewed or narrow perspective. At its core, microfinance can be viewed as an innovative segment of the banking sector to provide financial products and services, primarily credit, to the poor – bridging the gap that commercial banking has not been able to fulfill, and where philanthropy has not been able to go beyond pilot approaches to reach meaningful scale. However, microfinance itself was conceived with a different purpose than just providing the



poor with access to capital. Microfinance and microcredit do not provide consumers with loans to simply increase their consumption; instead, they provide loans for the specific purpose of creating self-employment for the poor, thereby enabling the poor to build their own microenterprises and move themselves out of poverty. In short, microfinance is an income producing tool rather than a consumption aid.

What was simply thought of as just providing poor individuals with access to capital has revolutionized the development world, proving that loans as small as \$50 or \$100 in the poorest countries, and somewhat larger ones in middle-income developing countries, can transform

² Chronic Poverty Research Centre (2006), http://www.chronicpoverty.org/about/what_is_chronic_poverty.html.

lives.³ Through microfinance, we have witnessed that poor individuals, when given the opportunity to start their own business, can provide for themselves and their family with basic necessities and also generate sustainable income. If they can maintain that income, it can lead to improved living standards, and for some, a means to escape poverty. If individuals achieve economic freedom, it can lead to a series of improvements—improving the well-being of families, communities and society-at-large.

The exact benefits that microfinance brings to individuals and society may be difficult to measure from a technical standpoint, which is why there are relatively few rigorous studies about impact compared to the reach of microfinance. From studies and research, however, it is apparent that microfinance is an important catalyst for poverty alleviation. One such study on two major microfinance institutions, BRAC and Grameen Bank, found that participants who have continued access to loans have a lower rate of poverty than those without access, 57 percent compared to 76 percent, respectively.⁴ Another study, by S.R. Khandker, found that the poverty levels in villages with microfinance programs have declined more than in villages without these programs. Among program participants who had been members for six consecutive years, poverty rates declined by more than 20 percent (about 3 percent per year). Khandker estimated that more than half of this reduction could be directly attributed to microfinance. He had calculated that microfinance accounted for 40 percent of the entire reduction of moderate poverty in rural Bangladesh.⁵ These studies and numerous others⁶ indicate that microfinance can improve overall income, increase decision-making power, and provide general self-empowerment.

From its tremendous success as a poverty alleviation tool, microfinance as an industry has gained momentum and expanded its scope and reach. The awarding of the Nobel Peace Prize to Muhammad Yunus and the Grameen Bank will only accelerate its growth. To ensure that the poor not only have access to credit but other financial services, microcredit has expanded over the years to include a variety of financial products such as savings, insurance, transfer payments, and even micro-pensions. Where regulations permit, savings can be a very powerful tool since it allows the poor to conveniently amass liquid assets that can be used to self-finance education, health care, or disaster relief while also giving the MFI a source of capital for on-lending. Microcredit, or what is now more aptly called “microfinance,” attempts to address the multitude of the poor’s financial needs. With this expansion of purpose, the field itself has increased its reach. By the end of 2005, according to the Microcredit Summit Campaign, there were over 3,000 MFIs serving over 112 million people worldwide, of which more than 82 million were among the poorest people in the world (i.e., earning less than \$1/day) when they became clients.⁷

As the sector has evolved to meet the growing demands for its services, it has been reinventing itself to ensure sustainability at the institutional level. MFIs and the organizations that support them have taken lessons learned from the banking sector and the business world to improve efficiency and sustainability. (Perhaps no reinvention has been as dramatic and

³ The best survey of existing impact literature is “Measuring the Impact of Microfinance: Taking Stock of What We Know”, authored by Nathanael Goldberg (Washington, D.C.: Grameen Foundation, 2005), <http://www.grameenfoundation.org/pubdownload/~pubid=29>.

⁴ S.R. Khandker and O.H. Chowdhury, *Targeted Credit Programme and Rural Poverty in Bangladesh*, (Washington D.C: World Bank: 1996), 17.

⁵ S.R. Khandker, “Microfinance and Poverty: Evidence Using Panel Data from Bangladesh.” *The World Bank Economic Review*, 19, no. 2 (2005).

⁶ Goldberg, *Measuring the Impact of Microfinance*.

⁷ Interview with Grameen Foundation Chair Susan Davis (September 2006).

influential as the launch of Grameen II in 2003, and its rigorous but highly favorable evaluation by SafeSave.) We have witnessed firsthand MFIs improving their loan disbursement and collection methods in order to reach more clients faster and better. They are becoming better trained and better run to meet the growing demands for their services. As the field continues to evolve in its business model and operations to increase institutional efficiency, it is also critically important that the field focus on its client success and effectiveness.

III. Inhibitors to Success

At its core, microfinance is not terribly different from mainstream consumer finance. From accessing funding to managing the disbursement and collection of funds, microfinance operates like any consumer finance business. But because microfinance serves a very different client segment – the world’s poor – we cannot ignore the different set of challenges these clients face and the implications these challenges have on the organizations serving them. Unlike customers of mainstream consumer finance, who tend to be middle class and live in relatively stable environments, microfinance customers live under more dire circumstances and contend with a different set of factors, such as poor health, lack of education and access to basic necessities, and unexpected threats such as natural disasters that endanger their everyday lives. Because these factors are so entrenched in their lives, we cannot ignore their influence on an individual’s economic ability to access, use and repay a microfinance loan.

Clients may be able to gain access to microfinance and may even start a business, but they may be unable to convert this credit into sustainable income. According to one study of three large MFIs in Bangladesh, approximately 5 percent of microfinance program participants lift their families out of poverty each year.^{8*} This finding of impact in particular does bring to our attention that microfinance does not result in overnight success for many clients; with current product offerings and costs, progress for most clients appears steady, but slow. In the current models being used, a certain percentage of clients are never able to generate sufficient profits to completely escape poverty or even to improve their conditions at the margins. An alarmingly high percentage drop out (5-30 percent annually in many cases) and many ultra-poor families never join in the first place (i.e., they self-select out).⁹ According to some studies, it takes 5 to 10 years for a poor client to work her way up above the poverty line, and even longer before she has sufficient productive assets to function independently from the microcredit institution (although continued participation with an MFI is not necessarily an indicator of failure on the part of the client or MFI, and in fact may be correlated with the success of both, in the sense that it may be

⁸ Human Development Report, Millennium Development Goals: A Compact among Nations to End Human Poverty, (New York: Oxford University Press, 2003), 93.

* This number probably understates the success rate of clients for a variety of reasons. First, clients are often unwilling to tell researchers of their success in a program for fear of being disqualified from the program (i.e., now being too well-off to receive loans). Additionally, while not all participants move out of poverty, many do improve their economic status.

⁹ Christopher Dunford, “Building Better Lives: Sustainable Integration of Microfinance with Education in Child Survival Reproductive Health, and HIV/AIDS Prevention for the Poorest Entrepreneurs,” in *Pathways out of Poverty*, ed. Sam Haley-Harris (Connecticut: Kumarian Press, 2002).

that many formerly poor clients continue to have robust investment opportunities and the MFI has products that are relevant to those opportunities).

What are the factors that hold back microfinance clients from overcoming poverty more quickly than is currently the case? In other words, why do some people move out of poverty and others fail to do so or make progress slowly – even though both participate in a microfinance program? In assessing the research and speaking with numerous practitioners, we identified three elements that diminish microfinance participants’ chances for being successful in a program: poor health, natural disasters, and lack of education. Because the poor live in a state where even the smallest misfortunes threaten their survival, these three elements are critical factors in determining the performance of their loans, their progress out of poverty or lack thereof, and ultimately the long-term sustainability and profitability of the MFI.

Health

The loss of income due to sickness and incapacitation of a borrower or a family member, and the high cost of health treatment are detrimental to individuals and families in the developing world. Therefore, it is not surprising that illness and death of family members are among the most common reasons why microfinance participants remain mired in poverty, default on their loans and/or drop out of a microfinance program. According to a survey of Zakoura Microcredit Program, problems beyond clients’ immediate control, which were most frequently an illness or a death in the family, were the principal cause of client drop out in 28.6 percent of cases in one sample.¹⁰ In a study of long-term clients of the Grameen Bank by Helen Todd, ill health was the key factor differentiating those families that had emerged from poverty and those who had not. She writes: “[A] serious illness in the family...almost always forced them to liquidate assets in order to pay for medical treatment and/or keep the family afloat... The disaster of illness struck ten of the 17 Grameen Bank families who are still in the poverty group, or 50 percent. Among the families who are no longer poor...only 18 percent...[had] been hit with a serious illness.”¹¹

While the figures above are alarming, they are not surprising. Illness and injury are common drivers of bankruptcy in the developed world as well. According to a 2005 study conducted jointly by Harvard Medical School and Harvard Law School, approximately half of all individuals declaring bankruptcy in the United States cite illness and medical bills as the primary factors leading to bankruptcy.¹² The major difference between these two groups (borrowers in developed countries and microfinance borrowers) is one of vulnerability. For an individual in a developed country, bankruptcy can be an enormous life challenge leading to significant lifestyle changes. But developed countries have safety nets and established legal and social infrastructures such as bankruptcy laws, as well as other public and private institutions that help people to get re-established and get back onto their feet. In developing countries, these types of infrastructures and programs either do not exist or are limited in their reach. Therefore, for a

¹⁰ Fouzi Mourji, *Impact Study of Zakoura Microcredit Program*, (New York: United Nations Capital Development Fund, Microstart Program: 2000), 110.

¹¹ Helen Todd, *Women at the Center* (Boulder: Westview Press, 1996), 124-125. See also: Khalilur Rahman, “Poverty, Microcredit and Health-What Role can WHO Play?” in *Regional Health Forum 4*, http://www.searo.who.int/EN/Section1243/Section1310/Section1343/Section1344/Section1352_5261.htm.

¹² Josh Fischman, “Medical Bills Lead to Personal Bankruptcy,” US News and World Report, February 2, 2005, <http://www.usnews.com/usnews/health/briefs/publichealth/hb050202c.htm>.

microfinance borrower living on one to two dollars a day, illness can lead to hunger, deprivation, or even death.

Natural Disasters

Like ill health, natural disasters are another area of vulnerability for the poor. Research shows that when disaster strikes, the poor are not only in a greater danger of falling victim, but suffer disproportionately greater losses. For poor people, the resulting lost income may force them to sell their land, livestock or their tools, send their children to work rather than to school, or eat less. Such drastic measures may mean survival, but they make it much harder for vulnerable households to escape poverty.¹³ According to Salvano Briceño, Director of the UN/ISDR Secretariat, “Investing in disaster risk reduction reduces the vulnerability of people to hazards and helps break the vicious cycle of poverty. We need to engage the microfinance community into a dialogue on reducing the impact of natural hazards on populations and livelihoods.”

Education

The third critical factor that prevents some borrowers from sustaining a successful business is lack of education. Most borrowers of microfinance are incurring debt and operating a business for the first time. And, as we know, the responsibilities that go along with these two endeavors are great. It requires understanding the fundamentals of credit and how to manage a complex business. Without the appropriate support and education, a borrower can find herself unable to manage a growing business, which can contribute to backsliding into poverty and/or defaulting on a loan. Providing adult literacy and/or financial literacy modules to microfinance clients can therefore represent a long-term investment in the well-being of the client and the MFI that serves them, even if it increases costs in the short run. In addition, facilitating higher educational attainment among clients’ children, arguably a more cost-effective and realistic goal in most cases, can help ensure that at least one household member involved with the family business is literate, and that a wage-earning offspring is available to support a client when they reach old age.

Because these three factors, among others, are key impediments to a borrower’s success in the microfinance context, it only makes sense that microfinance incorporates some prevention and mitigation measures into its business model. Improving the health of clients as well as helping the poor to prevent and/or respond more effectively to these inhibiting factors can contribute to sustainability at both the client level and the institution level. A healthy client is more capable of managing her business and generating income for her family. This income generation translates to an increased ability to make payments on the microfinance loan. This improved repayment should benefit the lender as much as it does the borrower – leading to a cycle of economic strength for both.

¹³ Announcement for 2005 World Disaster Reduction awareness campaign by the International Strategy for Disaster Reduction, http://www.unisdr.org/eng/public_aware/world_camp/2005/2005-announcement.htm.

IV. Improving Microfinance as an Anti-Poverty Tool

As Father Joseph Philippe, the co-founder of the Haitian MFI Fonkoze, states: “You can’t just give a woman a loan and then send her on her way - you have to accompany her as she struggles to make her way out of poverty.” Over the years, microfinance has been quite effective in addressing one aspect of poverty—lack of access to capital. By creating opportunities for the poor to have a chance to earn their own income, the impact has been impressive, and the potential with further refinements to the business model even more tantalizing.

But as other factors such as health, natural disasters, and education have just as much impact on an individual’s ability to generate and sustain a living, we encourage microfinance institutions to rethink its approach and to include other critical services. Some visionary MFIs such as the Grameen Bank, BRAC, Pro Mujer and Fonkoze are already doing this with some success.



Just as consumer banking should ensure that clients are credit ready before they get their first loan or are extended additional loans or other financial products, microfinance institutions and the sector as a whole have the responsibility to their clients to ensure that they are adequately prepared to engage in and derive meaningful long-term value from a microfinance program. By enhancing their models to include services such as health care, education, and disaster prevention and mitigation, MFIs and social organizations can make more significant and deeper contributions to the world’s poor and to help achieve their overall mission. However, before microfinance can leverage this platform, microfinance service providers need to assess their client segments, their needs, and the environment in which they operate to design the right model to address the clients’ needs.

Different approaches may be required depending on the client segments the MFIs and social service providers serve. To understand the many layers of microfinance, we need to identify the different segments of the poor. Generally speaking, microfinance serves individuals living below the poverty line as defined for that particular society, though an increasing number of long-term clients are no longer poor. But there are various levels of the “poor.” In this paper, we will focus on the three segments of poverty consisting of the destitute poor (bottom 10 percent living below the poverty line), the extreme poor (those in the bottom 10 – 50 percent of households below the poverty line), and the moderate poor (the top 50 percent of the households living below the poverty line) as defined by a report from the Grameen Trust.¹⁴ It is important to separate these segments, as well as others such as formerly poor and vulnerable non-poor,

¹⁴ H. I Latifée, “Micro-credit and Poverty Reduction” (paper presented at international conference on “Poverty Reduction Through Micro-credit”, Taksim-Instanbul, Turkey, June 9-10, 2003).

because each has different circumstances and needs, and MFIs have different approaches to reach or serve them.

A. Increasing Microfinance's Reach with Integrated Services

The destitute—individuals at the very bottom of the socioeconomic scale—are still outside the current scope of most microfinance institutions. These individuals are left without any access to financial means for a few reasons: self-exclusion from fear of incurring debt, exclusion from loan groups unwilling to take on a potentially risky member, or exclusion from MFIs so they can better control their loan portfolio and default rates.¹⁵ But perhaps the most important reason why this population is without access to credit or other financial products is that most of the destitute need other forms of assistance in their daily lives – such as food, shelter, training and education, access to health care, emergency aid – before they can make progress using a typical microfinance loan. If microfinance is to be fully leveraged as a poverty-alleviation tool, then it cannot ignore these vital issues and this particular segment.

To service this segment of the population and help graduate them to become “microfinance-ready,” MFIs have no choice but to expand their offerings to include non-financial services. To date, many microfinance organizations have yet to expand their target market to include social services for reasons such as cost and specialization of services. But for the few that have adopted creative solutions to link microfinance with social services or even offer social services as a platform to get clients onto the microfinance track, the results show that it is possible for microfinance to reach the poorest of the poor. Two pioneers in creating innovative solutions to reach those at the bottom of the poverty ladder are Grameen Bank and BRAC.

Grameen Bank—Alternative Microfinance Approaches

Grameen Bank operates on the premise that the poor remain poor not because they do not have the skills or do not work hard, but because the institutions created around them keep them poor. By challenging the conventional belief that the poor are not bankable, Grameen Bank has been able to serve over seven million borrowers since its creation in 1976 by Dr. Muhammad Yunus through many creative programs such as its Housing and Education programs, Village Phone Program, and Pension Fund and Other Savings Program. Dr. Yunus once again challenged common belief in 2003 when he started a new program, the Struggling Members Program (popularly known as the “Beggars Program”), to serve individuals who are currently at the lowest rung of the poverty ladder, proving that microfinance can be adapted and combined with other essential services to help improve the livelihood of individuals struggling with poverty.

Grameen leveraged the basic microfinance model and coupled it with creative solutions to fit the needs of the clients of its Struggling Members Program. First, the nature and size of the loan are different than generic microfinance loans. A typical loan to a beggar member is \$9 (collateral and interest free) and the repayment schedule is also more flexible where installments can be paid according to her convenience and earning capability — but not with money she

¹⁵ Syed Hashemi and Richard Rosenberg, *Graduating the Poorest into Microfinance: Linking Safety Nets and Financial Services*, Focus Note 34 (Washington, D.C.: CGAP, 2006).

receives from begging. Second, some rules and regulations that apply to the regular members were modified to accommodate these clients, such as eliminating the need to form solidarity groups and the obligation to attend weekly meetings. Grameen goes beyond providing the loans to help their clients achieve a life free from begging. It supports its members by making arrangements with local shops to provide items for them to sell such as bread, candy, and toys and will guarantee payments to these shops in case of defaults. In addition, the bank provides its members with other financial and non-financial products such as insurance schemes and blankets, mosquito nets and umbrellas on credit to be repaid as interest free loans. Although there is no compulsion for the struggling members to give up begging, many do and move on to becoming business people. As of December 2006, the number of people covered by the program total 87,329. Of this number, 6,206 beggars have already given up begging and 3,042 have graduated to become regular members of the Grameen Bank – a truly amazing accomplishment.¹⁶

BRAC—Linking Food and Training with Microfinance

BRAC, the world's largest NGO with a large microfinance program serving more than five million Bangladeshi families, is another example demonstrating that microfinance can and should serve the world's poorest. Through their Income Generation for Vulnerable Groups Development (IGVGD) Program, it is able to reach the destitute poor and graduate them to full-fledged, long-term microfinance clients. The IGVGD Program is a collaboration between BRAC, the World Food Program and the Bangladesh government to serve destitute rural women who have little or no income-earning opportunity by offering them free grain, skills training, and microloans. Participants receive 18 months of free grain as basic nourishment from the government. Then a BRAC unit specializing in training organizes the participants into groups, collects savings, and provides them with skills training such as raising poultry and livestock. Upon completion of training, participants receive tiny loans of about \$50 to fund a small-scale income generating activity. In addition, the program provides participants with BRAC's essential health care services that incorporate annual check-up, basic curative care and family planning among other vital services.¹⁷

The results of BRAC's IGVGD Program are very impressive. To date, the program has served 1.6 million destitute women, and nearly two-thirds of these participants have "graduated" from absolute poverty to become microfinance clients who have not slipped back into requiring further relief assistance.¹⁸ Overall, longitudinal studies of the IGVGD Program shows that the economic and social conditions of participants have improved based on measurements of income and assets, land and homestead ownership, ownership of beds and blankets, and food security.¹⁹

¹⁶ Statement by Muhammad Yunus on Grameen Bank's website, <http://www.grameen-info.org/bank/BeggerProgram.html>. Additional information also came through email communication with Dipal Chandal Barua of Grameen Bank on January 24, 2007.

¹⁷ Khadija Rehman, "Thinking beyond micro finance: BRAC reaches out to the ultra poor," *Holiday*, Friday, September 23, 2005.

¹⁸ Hashemi and Rosenberg, *Graduating the Poorest into Microfinance*.

¹⁹ Syed Hashemi, *Linking Microfinance and Safety Net Programs to Include the Poorest*, Focus Note 21 (Washington, D.C., CGAP: 2001).

B. Enhancing Microfinance Efficacy through Integrated Services

Most microfinance organizations serve what we define as the extreme and the moderate poor. These are individuals living below the poverty line earning less than \$1 per day in the poorest countries and less than \$2 in middle-income developing countries. Unlike the destitute poor, these individuals may not have to worry about the basic necessities such as food, water, shelter, and clothing all year round, but they are still vulnerable to adverse effects that interrupt their income such as ill health, lack of education, and natural disasters as described earlier. While they are served by microfinance organizations, they can benefit from additional support to help them become more sustainable clients and have an increased likelihood of success. Incorporating elements of Grameen Bank and BRAC's successes at synergizing various empowerment interventions with the provision of microfinance (often through related companies), organizations such as Pro Mujer and Fonkoze and others have attempted to link microfinance with health, education, and natural disaster relief and prevention.

Pro Mujer—Providing Clients with Essential Health Care

Pro Mujer, an international microfinance network composed of partner MFIs in several Latin American countries, is a believer and a practitioner of “Microfinance Plus”—a term that has come to capture the concept of offering integrated services to its clients. Through their work with clients, the leaders of Pro Mujer realized that existing health care services, as inadequate as they are, are often underutilized by their clients. In addition to the lack of access, Pro Mujer clients also did not use public and private health services because they were afraid and uncomfortable, had been mistreated, and/or were also dissatisfied with the quality of services.²⁰ Recognizing that health is important for the well-being of their clients and for building a strong support and solidarity network among their clients, Pro Mujer decided to offer health services themselves or help their clients gain access to health services that fit their needs.

To deliver health services, Pro Mujer uses different strategies depending on the needs of their clients, and the resources they have available. In some countries, such as Bolivia, Pro Mujer has its own healthcare facilities located in the Focal Center where women repay their loans and are able to receive counseling and basic medical care. If they need more sophisticated care, they are then referred to local providers, with whom Pro Mujer has already established linkages, to treat more complicated needs. In other countries, such as Peru, Pro Mujer does not offer health services in-house. Instead, they refer clients to partnering local healthcare facilities. Along with health services, Pro Mujer is continuously trying to integrate other products, such as health insurance, into its model to help provide a more comprehensive set of products and services that help clients to become more healthy and self-sufficient. Though the strategies may differ to maximize their effectiveness, the goal is the same: to facilitate access to health care and to help clients assume responsibility for taking care of their own and their families' health.²¹

The results from Pro Mujer's program show improved client health but also improved overall client confidence and awareness. A study conducted in Bolivia in 2005 shows that young

²⁰ Carmen Velasco and Saiko Chiba, *Expanding Impact: Innovations in Cost-Effectively Integrating Microfinance with Education in Health*: November 2004.

²¹ Ibid.

children of clients participating in the program for a longer period are less likely to get sick (70 percent vs. 77 percent) than children of non-members, and if children do get sick, 91 percent of the long-term women clients get them medical attention versus 82 percent of newer clients. Though no substantial differences were found among adult clients, members who are long-term clients are less likely to fall sick compared to new clients. What is more compelling is that having training and access to health care over time changes clients' health practices. As Carmen Velasco states, "Pro Mujer is contributing not only to the knowledge of clients, but it is making them more aware of their rights [and], more empowered to fight for them, while also changing their health practices."

Fonkoze—Educating Individuals to Become Self Sustaining

Fonkoze, Haiti's largest microfinance institution, is another good example of integrating microfinance with other services such as medical treatment, remittances, empowerment, insurance against risk and natural disasters, health insurance, and in particular, education to help improve clients' situations and contribute to the overall economy. Fonkoze was founded by Father Joseph Philippe in 1994, when Haiti was in the midst of struggling for freedom and equality, with the goal of providing Haitians with the means to develop themselves economically. As a result, the foundation devoted itself to delivering microfinance and related educational services to the most economically disadvantaged of Haiti—mostly women.

The organization believes that education is the cornerstone of economic democracy. Since 52 percent of the Haitian population and over 60 percent of Fonkoze's clients are illiterate, Fonkoze offers literacy and educational programs in their 250 literacy centers throughout Haiti. Their programs consist of four modules: two on reading and writing, one on business skills, and one on sexual and reproductive health issues. Fonkoze is working on developing new additional programs to focus on human rights and environmental protection. By March 2005, Fonkoze had trained 22,000 individuals to read and write.²² These education programs, coupled with the many microfinance products that Fonkoze offers, we believe will provide clients with more knowledge, confidence, and tools to help them overcome all dimensions of the poverty that affects them.

MFI's: A Critical Partner in Disaster Mitigation and Relief

Natural disasters are indiscriminate in their impact, but for poor communities – many of which are home to microfinance clients – the effects can be devastating. Because MFIs are interconnected with the impact of natural disaster devastation, whether or not they choose to be, many have discovered that when faced with a disaster, such as the recent tsunami in Asia, they have to participate and contribute to helping clients prepare for and cope with the aftermath of natural disasters. Sareeram, an MFI that operates in Batticaloa, Sri Lanka, was quick to respond when the tsunami struck. It did not attempt to replace or duplicate efforts by disaster management agencies or relief efforts, but rather facilitated the delivery of relief efforts. It leveraged its resources such as vehicles and local staff to help deliver food and essential supplies to those who needed them. Because the MFI's staff were familiar with the landscape and the

²² Interview with Anne Hastings, Director of Fonkoze (June 2006).

people, it was much easier for them to help track individuals affected by devastation and connect them to the much-needed resources from government and agency programs for disaster relief.²³ Through the support of the Abdul Latif Jameel Group and others, Grameen Foundation also surveyed the four countries impacted by the tsunami and has supported five MFIs in implementing rehabilitation strategies using microfinance. This is another positive example of what can be done.

We are not proposing that MFIs become natural disaster relief agencies by any means. Rather, by learning more about the effects of these events on their clients and by participating in some relief efforts, they are better positioned to ensure the viability of their organization as well as their clients' sustainability. By working with disaster management and relief agencies, MFIs can understand how clients are affected economically, and develop repayment programs, temporary relief, emergency loans, and even insurance plans that will help them deal with this disaster and also prepare for the next one.

From the examples provided, the benefits of leveraging microfinance as a platform to deliver other social services are many. By offering health care services, Pro Mujer is helping its clients stay healthy and teaching them the importance of modern healthcare – services that they use now in greater numbers than before. By offering education programs, Fonkoze is contributing to a more knowledgeable client base that is better equipped to manage their loans and their businesses, and therefore increasing their chances of success. And when partnering with other organizations to deliver additional services to clients – such as disaster prevention and relief – MFIs are helping the social service and development field by leveraging resources and reaching clients more efficiently and effectively. Overall, an integrated approach to microfinance to deliver more value-added services could lead to more services to clients, higher and accelerated success rates, and ultimately a more rapid reduction in poverty.

We acknowledge that there may be some criticisms and arguments against leveraging MFIs' infrastructure to provide other empowerment services. These arguments are based on cost and efficiency. It can be argued that it is too costly to provide additional services particularly for a business that is trying to offer services where the margins are often low and there are upward pressures on costs and competitive and regulatory pressures to reduce interest rates and fees. Offering health or education to microfinance clients will add to the cost of service providers as it does for Pro Mujer and Fonkoze, but the results also strongly suggest that the long-term benefits to the client and the MFI outweigh the costs. The services may be an additional cost to clients, but it is often more cost-effective for them to do so compared to using external service providers of comparable quality. In addition, the advantage of having microfinance organizations provide these services instead of a separate provider is two-fold: the cost is structured in a way that is still affordable for clients, and clients actually use and benefit from these services because it comes from a convenient and trusted provider.

Instead of trying to evaluate microfinance as a stand-alone business measured purely on cost-efficiency and specialization, we encourage the field to look at it from a different point of view—one of poverty alleviation. In measuring or analyzing the effectiveness of microfinance models or strategies, microfinance institutions and experts should continue to serve their clients with microfinance's purpose in mind. If offering crucial services to microfinance clients contributes to healthier, more educated clients who are better-prepared for potential disasters

²³ Banking with the Poor Network, "Microfinance Institutions and Disaster Relief" (2006), http://www.bwtp.org/arcm/mfdm/Web%20Resources/Briefs/Brief_1.pdf.

without compromising microfinance's ability to increase access to financial products and services, then we believe that it is a strategy worth pursuing.

V. Partnership Models

The examples cited are just some of the models where microfinance can be used as a platform to offer and deliver integrated services to clients. Like any business model, there is no single right way to offer services.²⁴ MFIs can provide additional services themselves, partner with other social service providers, or use service agents who will perform certain functions on their behalf. In today's environment, given the heightened awareness of microfinance and its role in poverty alleviation, there are many players interested in participating, which could lead to interesting hybrid models as well.



If organizations pursue an in-house model (i.e., they provide the services themselves), they can either increase the scope of the existing business model to include other services (unified approach) or build a separate arm to deliver the services in parallel with offering loans (parallel approach). The organizational structure will depend on the resources available, their staff's skills and expertise, the mode of delivering the services, and the needs of their clients. A unified approach requires a strong staff that is knowledgeable in all the products and services offered. A parallel approach will require greater organizational capacity as well as internal coordination and external collaboration. Regardless of which approach, MFIs ought to ensure that the delivery of additional services does not compromise its capacity to lend and administer loans on a cost-effective and sustainable basis.

For organizations that do not have the capacity or prefer to specialize only in lending, they can provide their clients with additional services by engaging in partnerships or alliances (linked approach) similar to BRAC and their IGVDG Program. Each partner can provide complementary services or they can collectively offer more comprehensive services to their clients. It depends on what each partner brings to the table and the opportunities for shared or leveraged resources. A key ingredient in engaging in a partnership or strategic alliance is whether the interests of both parties align. It is critically important that both parties have the

²⁴ Christopher Dunford has developed a very good classification for integrated service delivery in microfinance: linked, parallel and unified and this is the framework used in this paper. The following paper, which was published in the Microcredit Summit Campaign's book *Pathways Out of Poverty* (Kumarian Press, 2002) provides more details: "Building Better Lives: Sustainable Integration of Microfinance with Education In Health, Family Planning, and HIV/AIDS Prevention for the Poorest Entrepreneurs" (2001).

same end goals in mind and are in agreement on the roles and responsibilities of each during the process. In this particular case, MFIs, when choosing their partners, have to keep in mind the evolving needs of their clients and how the alliance will impact them in the short term and over time. Because microfinance and this client segment require a high-touch, high-service level model, the partnership has to be well developed and tested before being rolled out to an MFI's entire network of clients.

As the microfinance field grows, more opportunities will arise to outsource particular functions and services. MFIs do not have to do everything themselves, particularly in the areas of offering health, educational or other social services not within their area of expertise. They can use a service agent on their behalf or outsource certain services. Like a partnership though, they still have to make sure that the various parties involved are clear in the rules of engagement and the end goal. This model is beneficial because it increases the scope of offerings to clients by leveraging resources and providers. If it is not well managed or executed, however, it could lead to substantial problems.

Each of these models mentioned above or a hybrid of them can help microfinance institutions offer clients more value-added services. Organizations should develop a model that works for them and their marketplace. The idea is for MFIs to leverage their infrastructure and their attractiveness to potential strategic allies. Whether it is access to tangible resources (e.g., distribution networks and complementary services) or more intangible resources (e.g., organizational capacity, knowledge and skills, or even brand and reputation), organizations seeking to partner with MFIs should put long-term business considerations above short-term profit maximization or public relations value. We encourage organizations to look beyond the obvious partner choice, however. It is easier to network with and collaborate with more similar organizations such as other MFIs, foundations, and NGOs. But often, more value can be gained when MFIs can engage and motivate other actors including businesses to see how their long-term business goals will be realized faster if they partner with MFIs and the platform they have created. Because poverty alleviation is a global issue, which can only be sufficiently addressed if more parties lend a hand, we encourage MFIs to reach out to less obvious players—including social ventures, private businesses, government organizations, and yes, even large corporations—and serve as a platform for them to help in this important cause.

VI. Conclusion

We firmly believe that an integrated approach to servicing clients can enhance microfinance's effectiveness as a poverty alleviation tool. The benefits of this approach are two-fold. First, by acting as a platform to deliver important social services along with credit and financial services, MFIs can contribute to greater sustainability at the client level. Integrating microfinance with social services such as health, education and natural disaster relief or prevention addresses the other contributing factors to poverty beyond the economic factor. In doing so, we are providing clients with a comprehensive solution to minimize the risks they face. By addressing the very issues that inhibit a client's chances of succeeding with microfinance, microfinance can increase its overall efficacy. Focusing on client sustainability instead of institutional sustainability is how the field can ensure that we are not just reaching more

individuals, but that we are providing them with the services they really need once we do reach them, and that we accompany them throughout their journey to economic freedom.

Second, using microfinance as a platform to offer integrated services increases economies of scope for all the organizations involved in trying to service the same base of clientele. With leveraged resources – assets, infrastructure, knowledge, distribution channels, etc. – we can increase the capacity of the service offerings to reach more clients and to reach them more effectively. By partnering with other critical social providers and businesses and serving as a platform, microfinance can offer other organizations with a distribution channel to reach individuals in need, share experiences in working in a particular region and community, and offer countless other tangible and intangible products and services. This only makes sense because microfinance is not in the business of maximizing profits but rather of maximizing lives touched and transformed.

With that said, we encourage microfinance institutions to follow in the steps of pioneers, such as the Grameen Bank, BRAC, Pro Mujer, Fonkoze and Sareeram, in offering integrated services to their clients and to partner wherever it makes sense. The fight to alleviate poverty is too great a task for anyone or any one discipline to combat it alone. As an entrenched and recognized leader in this mission, microfinance can serve as a bridge beyond banking and development. It can be the link that brings together the services and products available today to the people who need them most. Only through a collective effort will we have the best chance of succeeding.

About Grameen Foundation

Grameen Foundation is a global non-profit organization that combines microfinance, technology, and innovation to empower the world's poorest people to escape poverty. Founded in 1997 by a group of friends who were inspired by the work of 2006 Peace Prize Laureate Dr. Muhammad Yunus and Grameen Bank in Bangladesh, our global network of microfinance partners has impacted an estimated 16 million lives in 22 countries across Asia, Africa, the Americas, and the Middle East. Dr. Yunus is also a founding and current member of Grameen Foundation's board of directors. For more information on Grameen Foundation, please visit www.grameenfoundation.org.



Front cover: Clients of Pro Mujer Bolivia, Grameen Foundation 2006 Pioneer in Microfinance award winner
Back cover: Clients of LAPO, Nigeria, Grameen Foundation 2006 Excellence in Microfinance award winner

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