Tackling the 'frontier' of microfinance provision in Kenya:

reaching remoter areas with financial services

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Decentralised Financial Systems

Centre for Development Studies

Outline

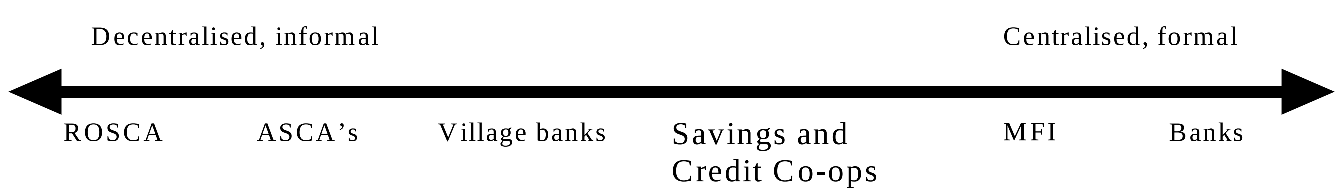
1. Microfinance in Kenya: the story so far
2. Review of five models
3. Challenges for decentralised systems
4. Challenges for centralised systems

The story so far

- 1990s concentration on turning credit programmes into sustainable MFIs
  - Limited products: compulsory savings and working capital loans
  - Limited outreach: traders/business in town/urban areas
  - Kenyan mainstream MFI outreach: approx. 200,000
    - KREP, KWFT, FAULU, SMEP, PRIDE
- Now emphasis on commercialisation:
  - transformation of MFIs
  - bank downscaling
- Challenge to extend coverage:
  - remoter areas
  - different clients: rural/ agricultural/poorer people

Models reaching rural areas

- Five models:
  - Equity Building Society
  - WEDCO
  - Nyeri Farmers SACCO
  - Financial services associations (FSAs)
  - Managed ASCAs - WEDI



Equity Building Society (1)

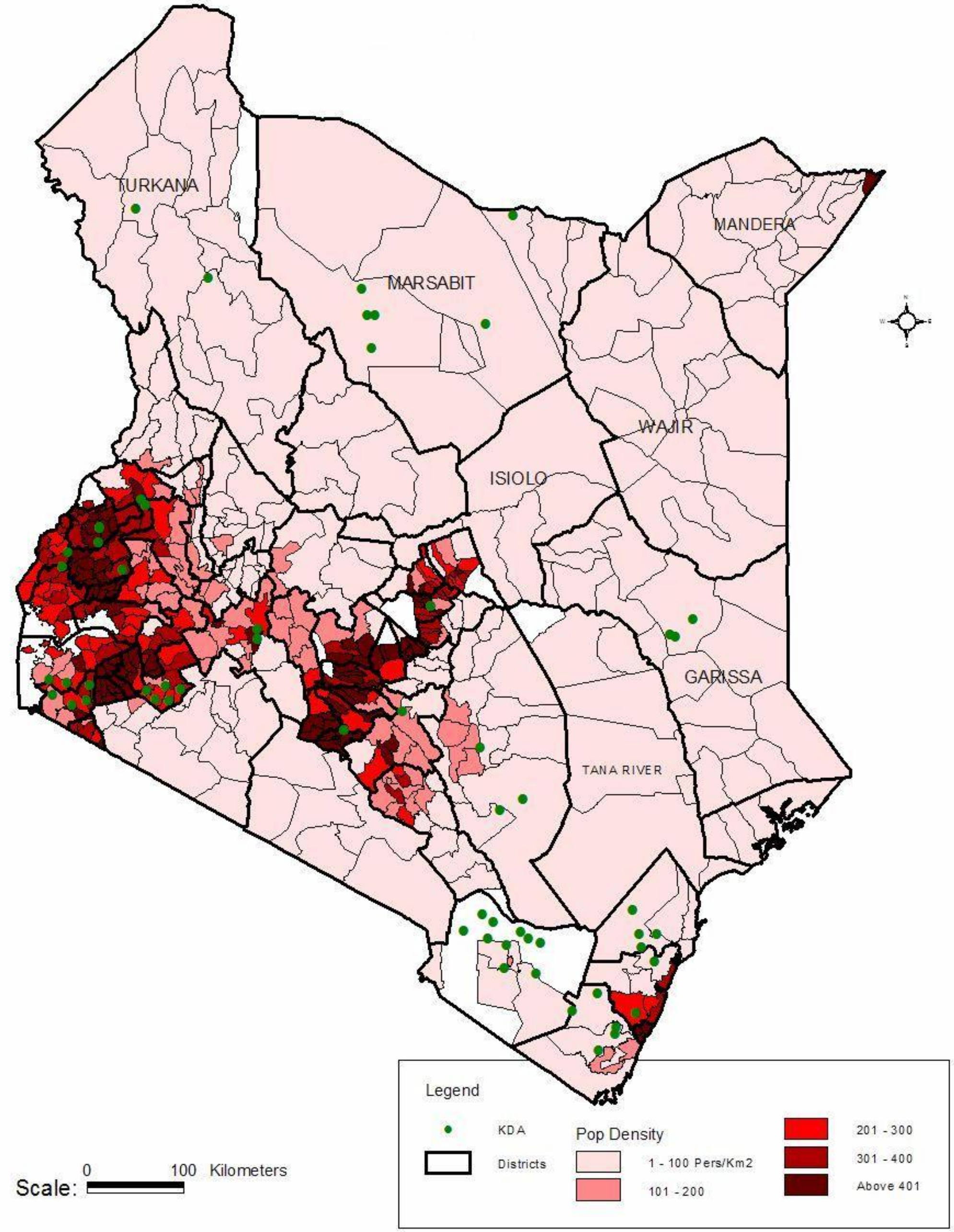
- Ownership and governance:
  - privately owned, board includes invitees
  - managers are shareholders
  - fast growing c.300,000 savers
  - context of 1990s banking sector
  - Central Kenya and Nairobi
  - rural outreach through mobile units
- Services:
  - savings services as in branches, plus a mobile fee
  - now starting loans <US$666 from mobile units
  - Interest rates – went up! 1.5-2% p.m flat

Equity Building Society (2)

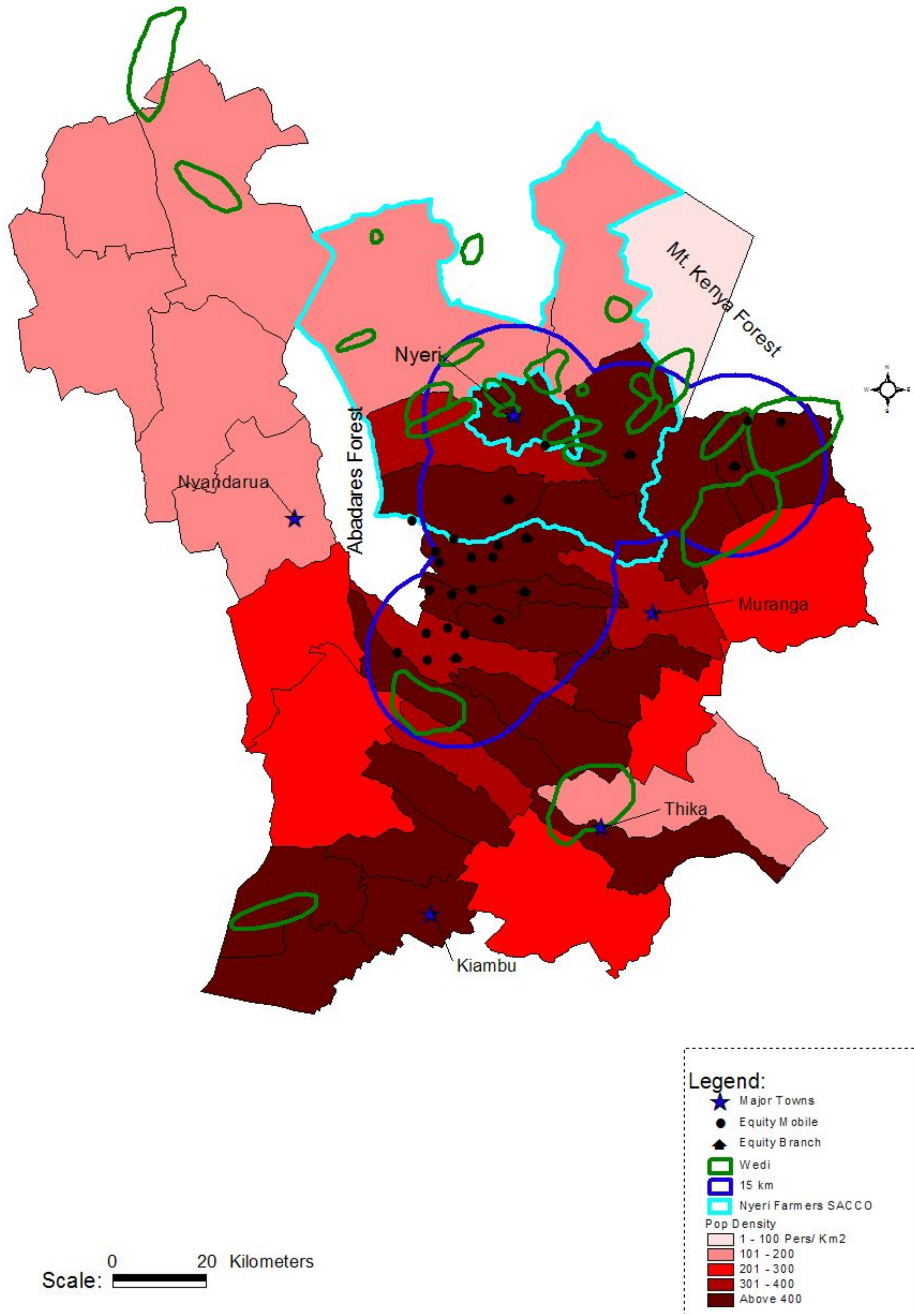
- Outreach:
  - 12,000 clients but pop densities >400/sq km
  - 6-65kms from branches; 29 locations
  - Richest districts - Middle income and relatively wealthy
  - avg balance US$65, approx half avg for all customers
  - loans – avg loan o/s US$130 (half overall avg)
- Sustainability: OSS = 102%
- Strengths:
  - Savings safe; min balance low
  - Loans require collateral - but flexible eg guarantors
- Weaknesses:
  - not proven - need for improved efficiency

MAP 12

Kenya FSA & Population Density



Central Kenya : Population Density, Nyeri Farmers SACCO, Equity & Wedi Operational Zones



WEDCO (1)

- MFI:
  - originated by CARE, transformed to company in 1999
  - standard group lending methodology
- Ownership and governance:
  - investors (donors)
  - management: increasingly professional
- Services:
  - compulsory savings
  - working capital loan one year
  - emergency and school fees loans
  - Interest rate (?) 20% flat

WEDCO (2)

- Outreach:
  - 12,000 clients, <10% men
  - Western and Nyanza Provinces:
  - Poverty incidence high >60%
  - 20% of clients in areas of density 200-300/sq km
  - Avg loan o/s US$192
  - Middle income and relatively wealthy
- Sustainability: OSS not comfortable yet (98%)
- Strengths:
  - Relatively well managed, savings safe
- Weaknesses:
  - credit led
  - to reduce costs has withdrawn motorbikes and moved meetings to market centres

Nyeri Farmers SACCO (1)

- SACCO model since 1999:
  - 1990s transition from Union Banking Sections
  - Context of co-op liberalisation and “splits”
- Ownership and governance:
  - shareholders - coffee farmers plus….expanding common bond
  - board elected by shareholders’ delegates
- Services:
  - Savings - shares against which can borrow
  - voluntary savings services expanding
  - Interest of 3% paid in 2002; 7% on shares
  - Loans: short, medium and longer term (ie 3 years)
  - Interest rate   - 16% declining balance

Nyeri SACCO (2)

- Outreach:
  - 111,000 members, c.40% active
  - Nyeri a rich district : poverty incidence <40%
  - Approx. 10% in drier zones
  - Middle income and relatively wealthy
  - Avg loan o/s US$550
- Sustainability: very problematic portfolio
- Strengths:
  - low cost services – both savings and loans
- Weaknesses:
  - coffee prices >> poor portfolio performance
  - heavy competition – other SACCOs: tea, teachers…
  - politics

Financial Service Associations (1)

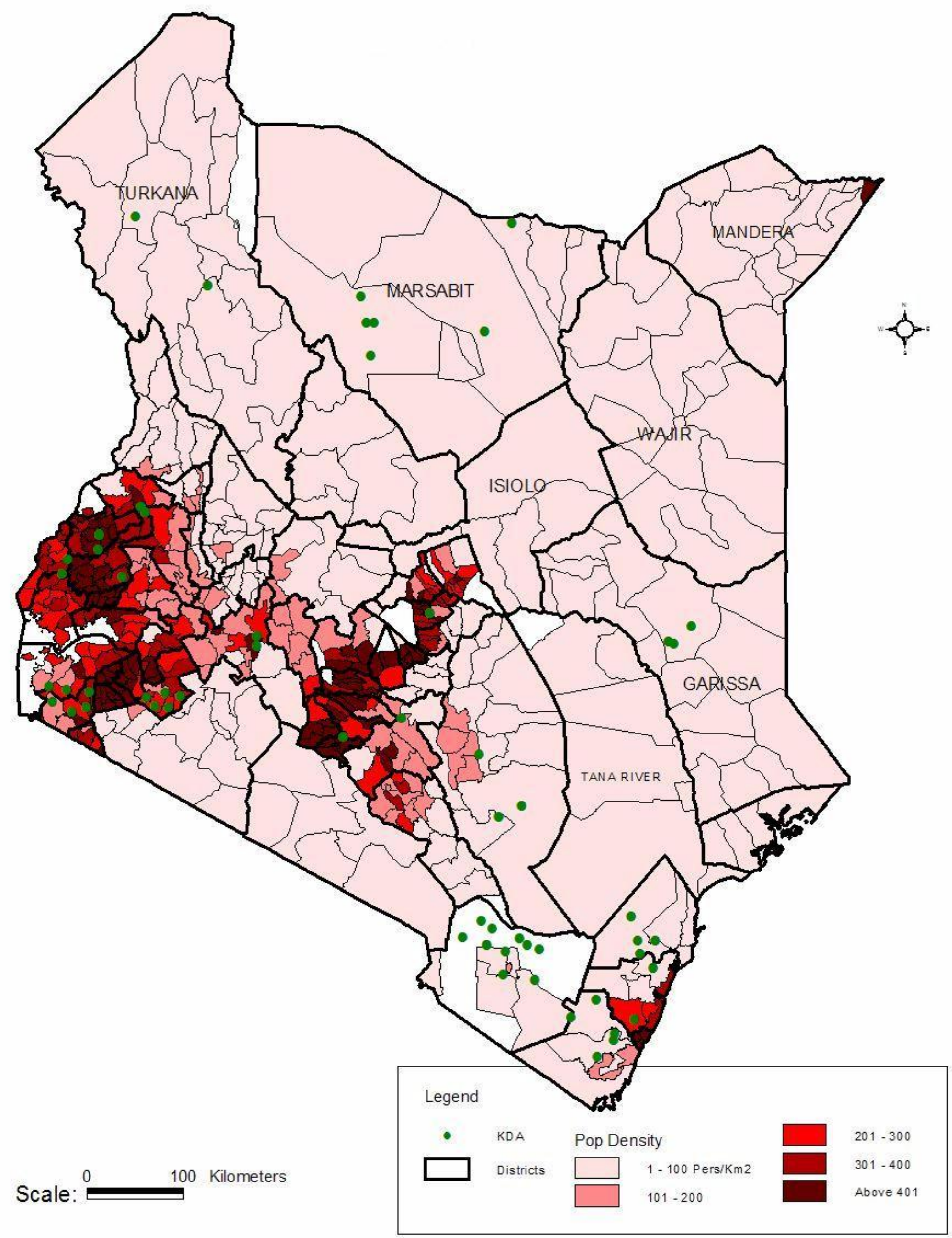
- Ownership:
  - Shareholders – minimum 300
  - Share price approx. US$5
- Governance:
  - Elected board of directors
  - Shareholding votes capped at 10 shares
- Management:
  - Local manager, cashier employed
- Services:
  - 3 month loans (10% p.m) at start
  - voluntary savings; fixed deposits etc
  - money transfer

Financial Services Associations (2)

- Outreach: 39,000 clients in 67 FSAs
  - 53% of clients in areas where pop density < 300
  - Operating in districts with high poverty incidence
  - Relatively wealthy, middle and some poor
  - Avg loan in Mkongani = US$55
- Sustainability:
  - 14 out of 20 analysed covered own costs
  - Poor in very remote districts
  - but KDA support and supervision is subsidised
- Strengths: outreach, range of services
- Weaknesses:
  - Fraud, bad debts
  - testing external management contracts

MAP 12

Kenya FSA & Population Density

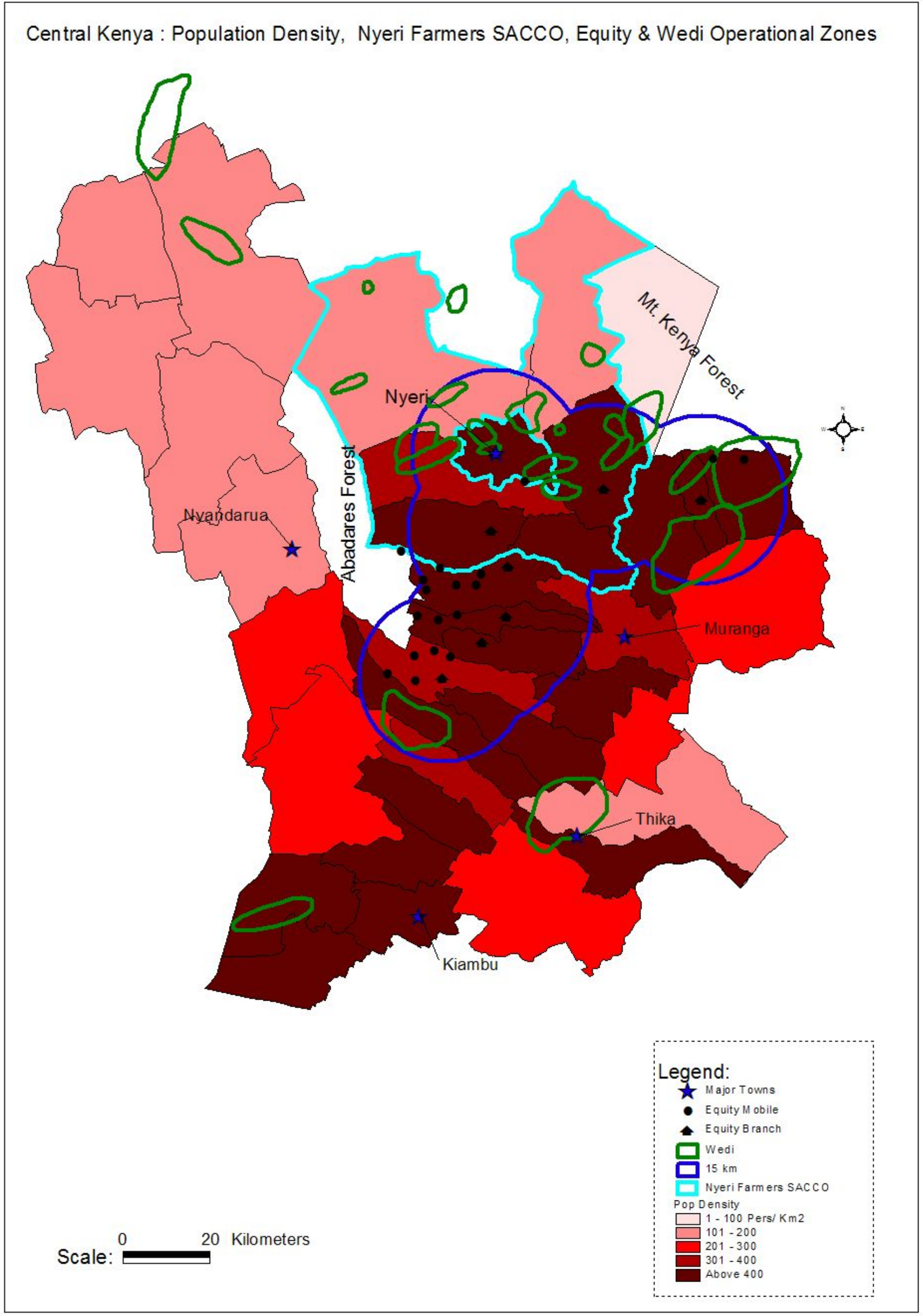


Managed ASCAs (1)

- Groups (ASCAs) managed by privately owned NGO
  - shares mobilised and on-lent - short term (10% p.m.)
    - Dividends paid at year end
  - Fee: 1% of revolving fund per month
- Governance:
  - groups have BOD but rely on NGO
  - ASCA managers - no accountability
- Services:
  - Minimum savings US$1.3 p.m and withdrawable
  - Short term advances
  - Interest rate 10% p.m.
  - Long term loans up to 2 years (liquidity permitting)

Managed ASCAs (2)

- Outreach:
  - Central Kenya – 9 orgs: 36,000 clients
  - WEDI - Approx. 25-30,000 clients
  - 45% in areas of pop density <200/sq km
  - Mainly in low poverty incidence districts of Central
  - Mostly poor, some middle income
  - Avg loan o/s US$100
- Sustainability:
  - ASCA managers self-sustaining (OSS=113%)
- Strengths: strong outreach
- Weaknesses:
  - portfolio performance and group collapse
  - Incentive structures



Central Kenya : Population Density, Nyeri Farmers SACCO, Equity & Wedi Operational Zones
Mt. Kenya Forest
Nyeri
Abadares Forest
Nyandarua
Muranga
Thika
Kiambu
Legend:
Major Towns
Equity Mobile
Equity Branch
Wedi
15 km
Nyeri Farmers SACCO
Pop Density
1 - 100 Pers/ Km2
101 - 200
201 - 300
301 - 400
Above 400
Scale:
0
20 Kilometers

Geographical Frontier

Poverty incidence \ Population density	1-100	101-200	201-300	301-400	400+
81-1000%					
61-80%	FSAs	FSAs	*WEDCO* SAGA	*WEDCO* SAGA	*WEDCO* SAGA
41-60%	FSAs	*WEDI* FSAs	FSAs	*WEDCO* FSAs	*WEDCO* FSAs
21-40%	*WEDI*	*WEDI*	*WEDI* Nyeri SACCO	*WEDI* *Equity* Nyeri SACCO FSAs	*WEDI* *Equity* Nyeri SACCO FSAs
0-20%					

Poverty Frontier

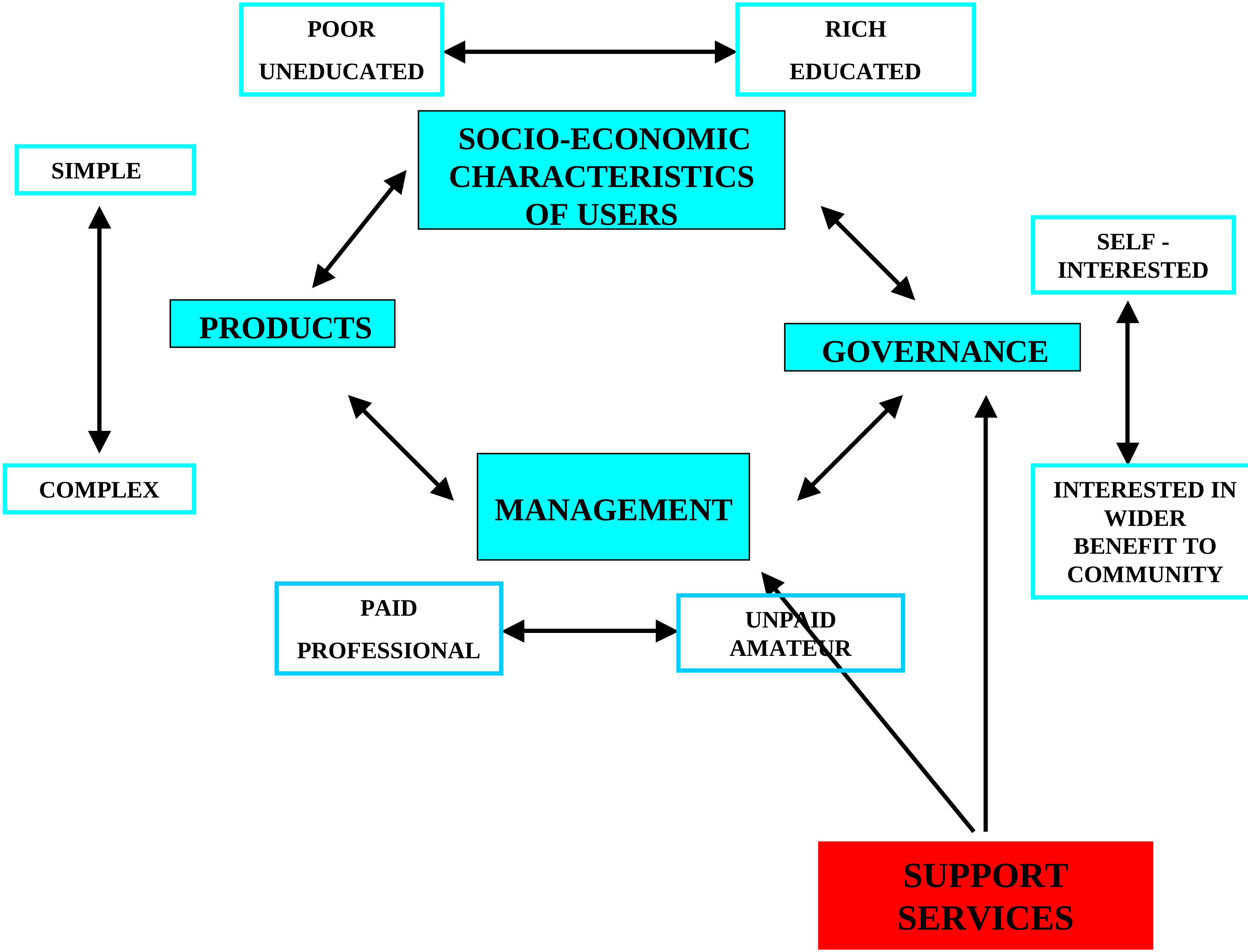
NB: Organisations in *italics* are financially sustainable

Reaching further out

- Those reaching furthest across geographical frontier - FSAs and WEDI
- Decentralised (user-owned) lowers costs because:
  - Own savings mobilised
  - Profits can remain in fund
  - Voluntary inputs of members
  - Overheads low: rented offices; low salaries

Systems with user-ownership

- Advantages
  - Products respond to member’s needs (direct feedback)
  - Interest rates are set by the members
  - Dividends paid to members
  - Default problems can be negotiated in ‘genuine’ cases
  - Social welfare in event of death, illness etc
- Disadvantages
  - Seasonal demand peaks outstrip supply of credit
  - powerful individuals can manipulate
  - …..many fail due to default and fraud


POOR
UNEDUCATED
RICH
EDUCATED
SOCIO-ECONOMIC CHARACTERISTICS OF USERS
SIMPLE
COMPLEX
PRODUCTS
GOVERNANCE
SELF - INTERESTED
INTERESTED IN WIDER BENEFIT TO COMMUNITY
MANAGEMENT
PAID
PROFESSIONAL
UNPAID
AMATEUR
SUPPORT SERVICES

Challenges for decentralised systems

- Improve governance and management through
- Training: need for simple tools
- Simplify systems eg. book keeping
  - MMD programme in Niger and replicates
- Engage with NGOs working in these areas
  - Lack discipline in lending methodologies
- Sustainable support and supervision systems:
  - Fee for service:
    - Upgrade ASCA management systems
    - address incentive problems
  - APEX organisations: user owned & fee paying
  - SACCOs as APEX – fees & implicit in interest rates
  - Potential for ratings systems to signal quality?

Decentralised financial systems: action research project

- Work with decentralised providers to address the challenges
- Approx. 300,000 members in NGO groups
- Strengthen governance and management through toolkits:
  - Self-assessment tool
  - Governance: Board and member education
  - Management: bookkeeping; internal controls; audit; management information systems; savings and credit methodology; portfolio and default management; legal issues for default and recovery
- Action research: design tools; test; get feedback; revise; test again…

CHENRO MAR
RACH
OK BER
BER MOROMO
BER AHINYA
1) Bedo gi Sotelo
2 Luwo chik bura
3 Biro e bura
4 Bedo e Adhil
5) Bedo gi records
6. Timo Kinda e Kamo
7) Chulo loan e wang saa.
7.) Bedo thuolo e bura.

Centralised systems

- High quality services: WEDCO and Equity
  - but outreach constrained by cost
  - MFI outreach constrained by services:
    - min loan sizes US$67 too high
    - Flexible savings
  - First reach poor in high density areas
  - Potential for information technology?
- Banking sector:
  - down market movement: lending against salary
  - competition from liberalised SACCOs
  - but agriculture still difficult
    - Constraints to use of rural land as collateral

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