

Graduating the Poorest into microfinance: Why and How?

Munshi Sulaiman,
BRAC and LSE

December 03, 2009

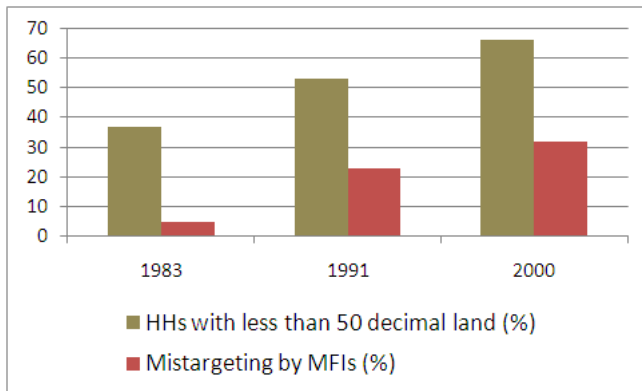
- 1 BRAC and the ultra poor
- 2 Why do we need a separate approach
 - The poorest do not participate in microfinance
 - The poorest do not benefit even if they participate
- 3 Graduating the poorest into Microfinance
 - The basic premises
 - Graduation approach
 - Emerging challenges

BRAC's experience with the ultra poor

- Started microcredit in 1974 as part of their 'holistic approach'
- Reached over 69,000 villages in 1990s
- Launched targeted programme for the ultra poor in 1983 in collaboration with WFP and the Government of Bangladesh
- Reached nationwide with the Income Generation for Vulnerable Group Development (IGVGD) programme
- Launched the 'Targeting Ultra Poor' programme in 2002
- The programme is now in its the second phase (2007-2011)

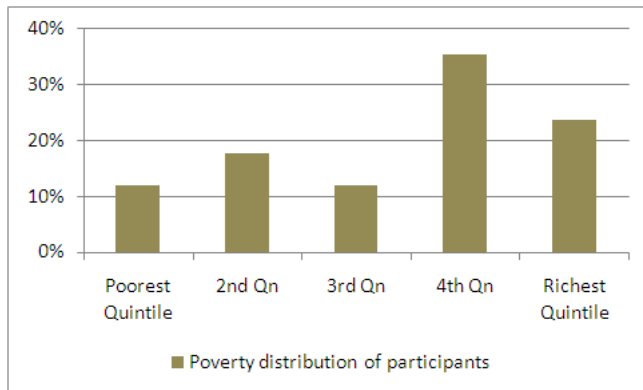
Microfinance participation rate of the poorest

Target clients in Bangladesh till ~2000:
Households with <50 decimal land



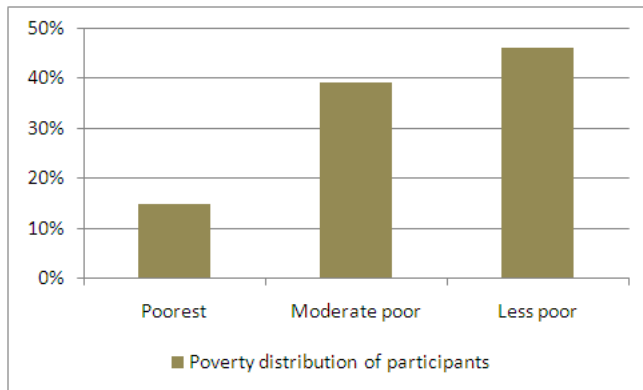
Microfinance participation rate of the poorest

'Relative' poverty outreach of microfinance institutions in Peru in 2004 (Zeller, 2006)



Participation rate for the poorest

'Relative' poverty outreach of microfinance institutions in Ghana in 2007 (Adjei and Arun, 2009)



Key features of microfinance participation of the poorest

- Very low participation rate
- Frequent exit and re-entry
- Lower level of borrowing
- Smaller loan size
- Difficulties in repayments
- Often “passive participants”

Impact of microfinance

- Rigorous impact assessments are surprisingly limited

Impact of microfinance

- Rigorous impact assessments are surprisingly limited
- Findings are sometimes mixed

Impact of microfinance

- Rigorous impact assessments are surprisingly limited
- Findings are sometimes mixed
- Early evidence on impact from Bangladesh (1990s)
 - Khandker and Pitt (2003) found positive impact of microcredit on income
 - Morduch (1998) found impact only on vulnerability

Impact of microfinance

- Rigorous impact assessments are surprisingly limited
- Findings are sometimes mixed
- Early evidence on impact from Bangladesh (1990s)
 - Khandker and Pitt (2003) found positive impact of microcredit on income
 - Morduch (1998) found impact only on vulnerability
- Evidence on BRAC (Zaman, 2000)
 - Microfinance participation has positive impact on both income and vulnerability of the **moderate poor**
 - No impact is observed for the **extreme poor**

Impact of microfinance

- Rigorous impact assessments are surprisingly limited
- Findings are sometimes mixed
- Early evidence on impact from Bangladesh (1990s)
 - Khandker and Pitt (2003) found positive impact of microcredit on income
 - Morduch (1998) found impact only on vulnerability
- Evidence on BRAC (Zaman, 2000)
 - Microfinance participation has positive impact on both income and vulnerability of the **moderate poor**
 - No impact is observed for the **extreme poor**
- Razzaque and Rahman (2004)
 - Non-participation in microfinance leads to exclusion of the poorest from non-financial services

Recent evidence of impact

- Banarjee et al (2009)
 - Microfinance participation increases profit *if* the participants have an enterprise before joining
 - Microfinance participation increases consumption of non-durable goods *if* they do not have an enterprise

Recent evidence of impact

- Banarjee et al (2009)
 - Microfinance participation increases profit *if* the participants have an enterprise before joining
 - Microfinance participation increases consumption of non-durable goods *if* they do not have an enterprise
- Karlan and Zinman (2009)
 - Effects of microfinance are stronger for higher income entrepreneurs

Why does conventional microfinance fail the poorest?

- Demand side factors
 - Limited entrepreneurial ability
 - Risk aversion
 - Vulnerable income source
 - Group exclusion
 - **Inability to aspire**
- Structural rigidities within institutions
 - Lack of flexibility in repayment
 - Non-responsive to idiosyncratic shocks
 - Non-alignment with the economic opportunities of the poorest

Structural breaks between the poor and the poorest

They are not just poorer but differently so

Variable	'Poorest'	'Just above'
Widow (percentage)	20	6
Households with no adult male	21	3
Households with child labour	12	7
Households no cultivable land	90	76
Households not owning homestead land	44	24

RED, BRAC (2004)

Structural breaks between the poor and the poorest

- They rely almost entirely on unskilled day labour
- They cannot trade down by buying cheaper calories and maintain level
- They are more prone the forms of mortality, illness and inadequate physical and mental performance associated with severe anthropometric shortfalls
- Age specific Labour Force Participation, though steadily increases as income per person falls, ceases to rise among the poorest
- These factors limit their capacity to work their way out of poverty.

The poorest are twice disadvantaged

Description of Activities	Productivity of Time (Tk/hour)			Fraction of Time Allocated to Each Activity (%)		
	Moderate Non-Poor	Moderate Poor	Extreme Poor	Moderate Non-Poor	Moderate Poor	Extreme Poor
Other Trade	12.22	10.09	7.28	26.79	25.34	8.58
Road Transport	10.34	8.54	7.40	10.13	17.87	10.64
Fishery	18.12	9.60	8.84	6.71	8.52	2.42
Food Processing	10.36	7.80	4.28	5.50	3.89	2.02
Construction	10.27	8.99	8.93	5.40	6.45	3.57
Educational Services	13.65	13.72	8.71	5.23	2.75	1.00
Cloth Production	8.50	7.55	6.52	5.05	5.09	4.40

Osmani and Sen, 2003

Need to work on multiple fronts simultaneously

- Narratives of discontinuities, traps and adverse incorporation

Need to work on multiple fronts simultaneously

- Narratives of discontinuities, traps and adverse incorporation
 - For us, life is like desperately trying to mend an old, tattered quilt. You stitch one hole only to discover another...
sometimes, if you are not careful, mending one also creates another... you just feel like giving up... a stitch in time saves nine doesn't work when you are like us

Need to work on multiple fronts simultaneously

- Narratives of discontinuities, traps and adverse incorporation
 - For us, life is like desperately trying to mend an old, tattered quilt. You stitch one hole only to discover another...
sometimes, if you are not careful, mending one also creates another... you just feel like giving up... a stitch in time saves nine doesn't work when you are like us
 - We are caught up in a **complex knot** — other poor people also get caught up from time to time in a knot, **but their knots are simpler**... you can easily detect the source of the knot and do something about it **our knots have many sources... often pulling on one carelessly only makes the knot more complex**

Conventional approaches are only responsive

- Food aid, the traditional instrument for the poorest, is designed as a “crisis management instrument”
- They fail to create the foundations for sustainable livelihood change

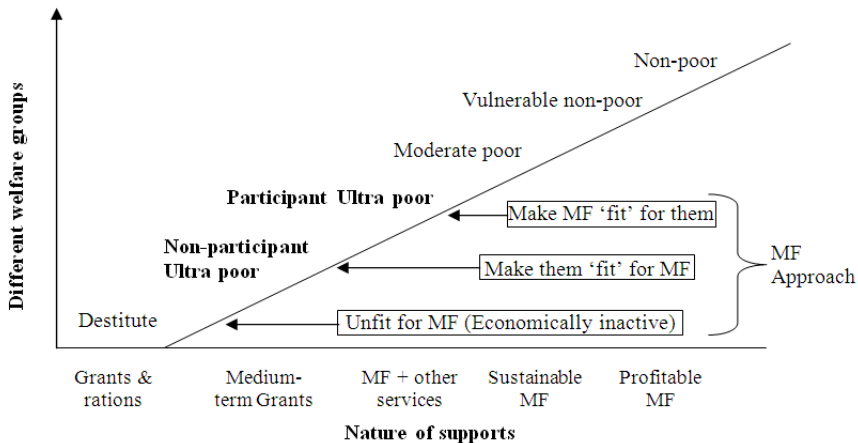
Conventional approaches are only responsive

- Food aid, the traditional instrument for the poorest, is designed as a “crisis management instrument”
- They fail to create the foundations for sustainable livelihood change
- They fail to address aspirational constraints
 - The experience of extreme poverty is one of having nothing as well as of being nothing

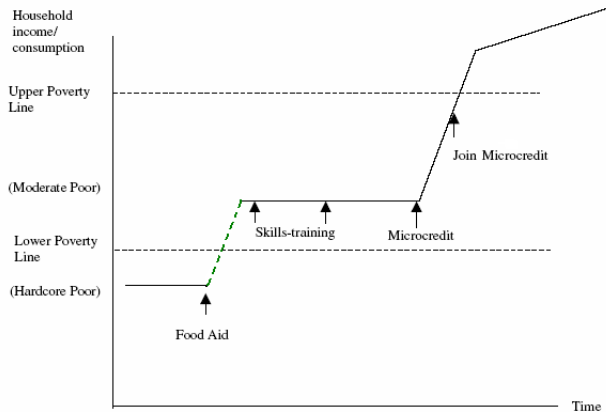
Conventional approaches are only responsive

- Food aid, the traditional instrument for the poorest, is designed as a “crisis management instrument”
- They fail to create the foundations for sustainable livelihood change
- They fail to address aspirational constraints
 - The experience of extreme poverty is one of having nothing as well as of being nothing
 - The role of a person’s identity as instruments of development has been vastly underestimated in the literature in economics. ... What the poor and the marginalized in society lack is a sense of “participatory equity.” [Kaushik Basu]

Microfinance approaches for the ultra poor



Food transfer as the entry point for graduation: IGVGD

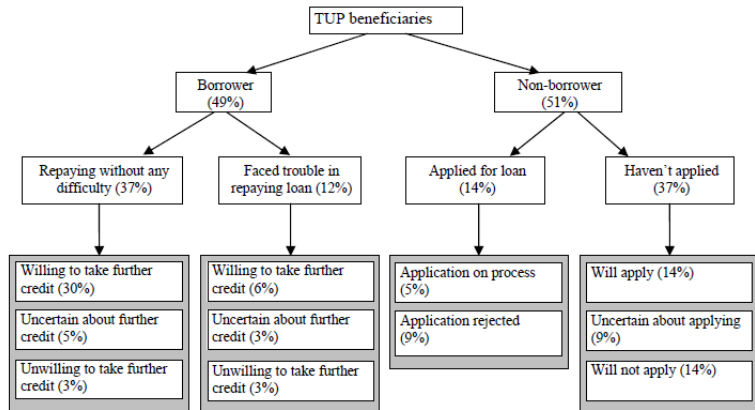


Asset transfer as the entry point for graduation

- Directly addressing enterprise development
- Avoid dependency
- Alignment of services to craft a pathway
- combine promotional (building opportunities) and protectional (addressing risk and vulnerabilities) measures

Defining graduation

MF participation of BRAC's CFPR/TUP beneficiaries after 2 years



Institutional challenges

- Ultra poverty as popular rhetoric in national politics
- Beneficiary selection and voting considerations
- Govt. service delivery at local level
- Partnering with microfinance institutions for graduating the poorest into microfinance

Rigorous impact assessment

It is important to conduct comprehensive and continuous evaluation.

Especially to identify potential unintended consequences early.
e.g. BRAC's CFPR shows strong impact on income, consumption and investment. However, it had weak impact on investment in education.