

Understanding and Assessing the Demand for Microfinance

prepared for
Expanding Access to Microfinance: Challenges and Actors
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Introduction

Globally, over a billion poor people are still without access to formal financial services. Some 200-400 million of these people live in India and another 200-400 million live in China. Microfinance, the provision of a wide range of financial services to poor people, has proved a very successful way of providing immensely valuable services to poor people on a sustainable basis. Access to financial services has allowed many families throughout the developing world (and indeed in poorer parts of the developed world) to make significant progress in their own efforts to escape poverty.

Meet The Clients

To understand how best to serve the poor, we first need to ensure that we have a clear understanding of their “financial behaviour” and the “financial landscape” within which they live. Let us learn from Prudence a market trader in Karatina in Kenya and then at Amina a housewife who lives in Pathrail in Bangladesh.

Diversified and Informal Prudence



Like many women in Kenya, Prudence, belongs to more than one Rotating Savings Credit Association (RoSCA) or as Prudence calls them “merry-go-round”. Prudence’s first merry-go-round involves four people and requires a daily contribution of \$0.29 per person. The daily contribution (6 days per week) goes to one person for a whole month in rotation. The monthly aggregate “prize” is around \$31.00. Prudence uses this to pay school fees for her grandchildren – for whom she cares after the death of their parents from AIDS. Her second merry-go-round consists of four people and requires a \$2.90 weekly contribution per person resulting in \$11.60 “prize” per week. Prudence uses this to re-stock her market stall. “I like the first one better because it forces me to put aside that amount everyday,” she says, “Other women save much more this way.”

In addition, Prudence belongs to an Accumulating Savings Credit Association (ASCA), known as a *kiama*, organised within her 40-member MFI solidarity group. The weekly contribution to Prudence’s *kiama* is just over a dollar. *Kiama* members take loans for a variety of reasons that vary from meeting emergency and consumption needs, responding to business opportunities, or simply paying MFIs’ weekly loan instalment. The loan sizes range between around \$5 and \$250, attract 5% weekly interest rate and are repayable in three weeks. In an average cycle about 10 members out of 40 members in the MFI’s centre will take a loan from the *kiama* with some members borrowing more than once. The entire *kiama* fund is distributed amongst the members just before Christmas each year – last year Prudence received \$109: “It allowed our family to really enjoy the festive season.”

Prudence also belongs to an informal insurance group organised along ethnic lines in order to cover funeral related expenses. This is extremely common and important amongst poor Kenyans, especially for those who have to transport their dead to distant parts of the country. Prudence's group has approximately hundred members. Every member contributes \$11.40 per month and is then assured of financing in the event of a funeral or (in some special cases like a marriage or a graduation) a celebration within their immediate family. A rigorous background check is done on prospective members to establish their character prior to admittance to the group. "It is very important to get a decent burial in my tribe" she says, "this means taking the body to our land of origin. That is why I joined the group so that just in case of an emergency, I have a source of money and people to help me".

Prudence also has a small secret fund of cash (typically of around \$3-5) that she keeps in her house to meet emergencies requiring rapid response. For longer-term savings, Prudence has a cow that is looked after by her brother back in her home village some 250 km from Karatina where she now lives. "I have to think about when I am older and this is a start ..."

As part of that process Prudence is now borrowing from Faulu an NGO-MFI. With her modest loan, she is building a simple addition to her house that she will rent out for a few dollars a month. These "rental units" are a common way of securing small amounts of regular income with relative ease – and are commonly used to provide for old age by people throughout East Africa.



Resourceful and Collaborative Amina

Amina relies primarily on collaboration to manage her financial affairs. She often lends to and then borrows from her neighbours in a complex web of reciprocal arrangements. She uses these arrangements to respond to short-term emergencies, to smooth her family's consumption and to help close family members seize small business opportunities as and when they arise. However, these arrangements are somewhat unreliable – some times the neighbours do not have money to lend, or will do so only at quite high interest rates; and at other times when has lent Amina she has struggled to recover her money.

Amina is also member of a savings club into which the ten members save \$0.40 each week and from which they can borrow at 5% per month. Amina borrows from this club only when her neighbours cannot help (which is increasingly often) but many of the savings club members borrow even more often than she does. The savings club "completes" and is liquidated every year two weeks before the main Eid festival – this provides Amina with a useful lump sum of around \$41.00 just before this important annual event ... just when social obligations are very high.

Amina also has some savings \$1.67 in a mud bank that is hidden in the thatch roof of her house. These are for emergencies only and the mud bank is a carefully kept secret from her husband, since she fears that he would fritter the precious money on tea and playing cards with his friends.

For larger amounts, Amina is a member of BURO, Tangail one of the more flexible microfinance institutions in Bangladesh. From BURO, Tangail, Amina cannot not only borrow for her husband's rickshaw business, but also for larger scale emergencies that cannot be financed through the informal mechanisms outlined above. Amina has been with BURO, Tangail for three years now and has borrowed twice for emergencies (once when her husband was sick and once when she did not have the money for her children's school fees) and twice for business (to buy her husband's rickshaw and to lease a small patch of land on which she grows vegetables). Amina is also thinking of taking out one of BURO, Tangail's contractual savings agreements to begin saving up for her daughter's wedding which she expects to take place in around five years' time.

Informal Systems Dominate ...

As can be seen from the examples of Prudence and Amina, the informal systems continue to dominate the financial systems they use. Indeed in Bangladesh, where there are often as many as ten different NGO-MFIs offering loans in every village, Stuart Rutherford notes "... the households in our study are each year 'managing' (pushing and pulling through financial instruments) an amount of money (\$839) equivalent to about 60% of their annual income." Furthermore, Rutherford continues, "MFIs carried out one fifth as many lending deals with our households as just *one* of the informal systems with which they compete – interest-free lending (and one eighth as many deals as interest-free and interest-bearing loans put together). Their share of transaction-flow values is less than 15% of the total, so although they may fairly claim that they do fewer but bigger deals than the informal sector, the aggregate value resulting from this strategy is still small" (Rutherford, 2002).

Rutherford continues to assess why the MFIs seem to be playing such a minor role and concludes that the key issues are the lack of flexibility and reliability amongst MFIs:

- **Flexibility:** "MFI products and delivery systems – in the form they took in our research areas in 1999-2000 – were designed to answer one kind of perceived financial need, and were then further designed to minimise the risks that MFIs face in offering them. The product is a 'micro-business' loan intended to introduce fresh capital into new and (mostly) existing small businesses that have a particular cash-flow pattern which combines high internal rates of return with year-round consistent and rapid turn-over."
- **Reliability:** "Many of our households talked to us about the reliability (and unreliability) of the financial services and devices they use. It seems to this writer that too many of the MFIs that featured in our study have failed to understand that reliability is one of their natural advantages. Too many of them are failing to capitalise on it.

State-owned banks [in Bangladesh, but often elsewhere too] are notoriously unreliable. They make lengthy delays, they extract unpredictable bribes, and their officers behave in arbitrary ways with scant regard to rules. Informal devices and services can be unreliable in many different ways (see the next section). MFIs, emerging from the NGO tradition in Bangladesh, are well-placed to tread the narrow line between these two failings: their systems and personnel have not institutionalised corruption in the way that state institutions have, and they have the resources – money, systems, educated staff, powerful backers – that should allow them to deliver reliable (even if inflexible) services. But too many don't, at least according to the testimony of our respondents" (Rutherford, 2002).

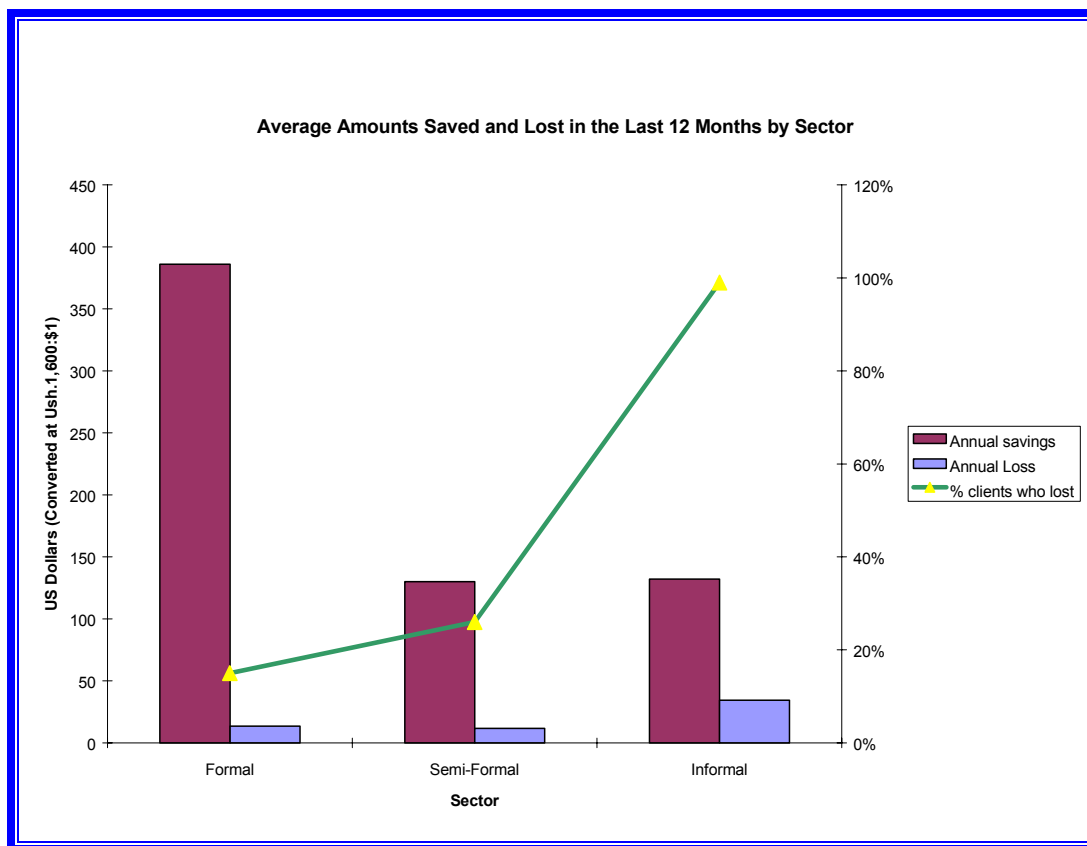
... But Present High Risk To Their Users

Poor people have limited access to formal, regulated financial services (indeed this is the basic rationale for the development of the microfinance industry). Poor people therefore lack formal financial service alternatives to the semi-formal MFIs. If MFIs are prohibited from (or unable to) offering savings services to poor people, those poor people are forced to resort to the informal sector in order to save.

It is clear, and now generally accepted, that poor people want, need and do indeed save. There is also increasing evidence that poor people are facing an extremely risky environment when they save in the informal sector. Thus it is clear that when discussing the risk to poor people's savings, this has to be evaluated on a relative basis. Very often all the alternative savings systems available to poor people are risky ... thus poor people are left facing decisions on the **relative risk** (or relative security/safety) of the various semi- and informal savings systems open to them.

In Uganda, 99% of clients saving in the informal sector report that they have lost some of their savings and on average they had lost 22% of the amount they had saved in the last year. 15% of those saving in the formal sector report that they had lost some savings and 26% reported that they had lost savings in the semi-

formal sector. Thus the formal sector, for those lucky enough to have access to it, is safer both in terms of likelihood of losing any savings and in terms of the relative loss (amount lost to amount saved). Those with no option but to save in the informal sector are almost bound to lose some money – probably around one quarter of what they save there. By contrast, people who have access to the formal sector reported saving three times as much (\$386) in the last 12 months than those who saved in the semi- and informal sectors. The people saving in the formal sector also reported a lower incidence (15%) of loss and a lower rate (3.5%) of loss in the last year (Wright and Mutesasira, 2001).



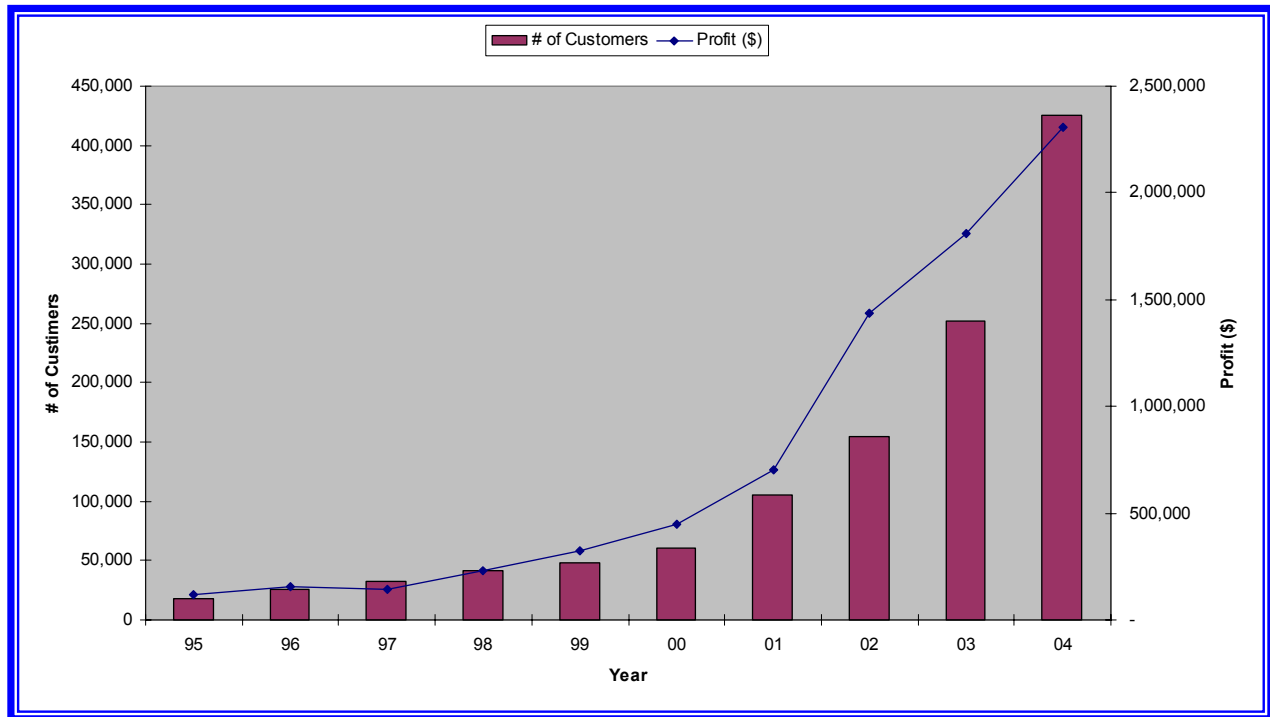
When A Flexible/Reliable Institution Arrives ...

Given the problems facing poor people who seek either to save, or to borrow for activities that cannot support a weekly repayment schedule (as well as emergencies and other short-term financing needs), it is hardly surprising that when a flexible and reliable institutions opens its doors to them, they flock in. Equity Bank has experienced exponential growth since it introduced a computerised banking system and moved to a market-led approach in 2000. Equity Bank has created a range of flexible products (including agricultural loans, emergency loans, salary advance, business development loans, ordinary and contractual savings accounts, money transfer etc.) tailored to the needs of its clients with the help of market research. In addition, Equity's focus on customer service has meant that it has a reputation in the market place as a reliable, listening, caring financial partner. The results have been remarkable.

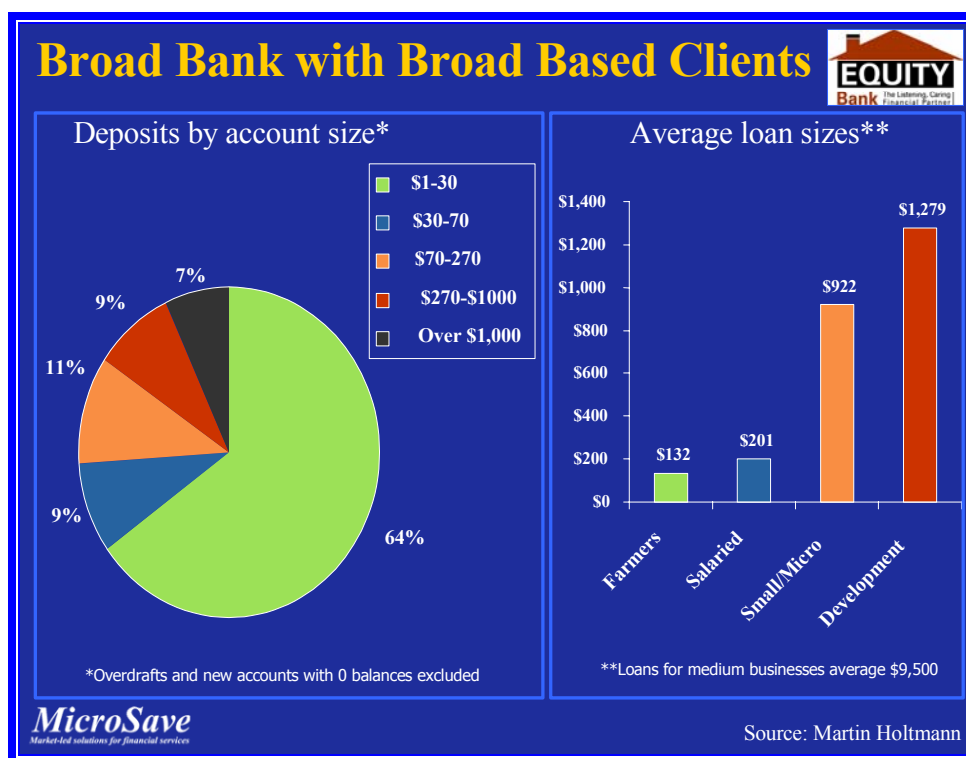
In the last four years the number of clients served by Equity Bank has risen from 75,000 to nearly 450,000 by the end of 2004 ... and the trend continues with around 50,000 new customers joining the bank in the first quarter of 2005. With a return on equity of 29.8% and a return on assets of 3.6% in 2003, Equity has demonstrated a successful business model for microfinance. The model is driven by a market-led approach and meticulous attention to clients' perceptions and customer care linked to charging for this high quality service – on both the savings and loan accounts. Equity is exciting proof of the profitability of high-quality

microfinance activities tailored for the low-income market ... and that this market will happily pay for such services.

This extraordinary growth was achieved with no subsidy except for the provision of a grant to support the introduction of the banking software and on-going technical assistance from *MicroSave* as well as a change management consultant from Stepwise Management.



Part of Equity Bank’s success is that it is a broad-based bank offering a diverse range of financial services to the low-income market that does not otherwise have access to financial services from commercial banks. Although Equity Bank does have a small number of relatively well-off clients, 64% of its clients have less than Ksh. 2,250 (\$30) savings account. Similarly, while Equity does make some larger loans to entrepreneurs and business people, the vast majority of the bank’s loans are made to farmers and low-scale salaried staff, and the amount advanced is less than Ksh. 15,000 (\$200).



Broad Services, Clients and Needs

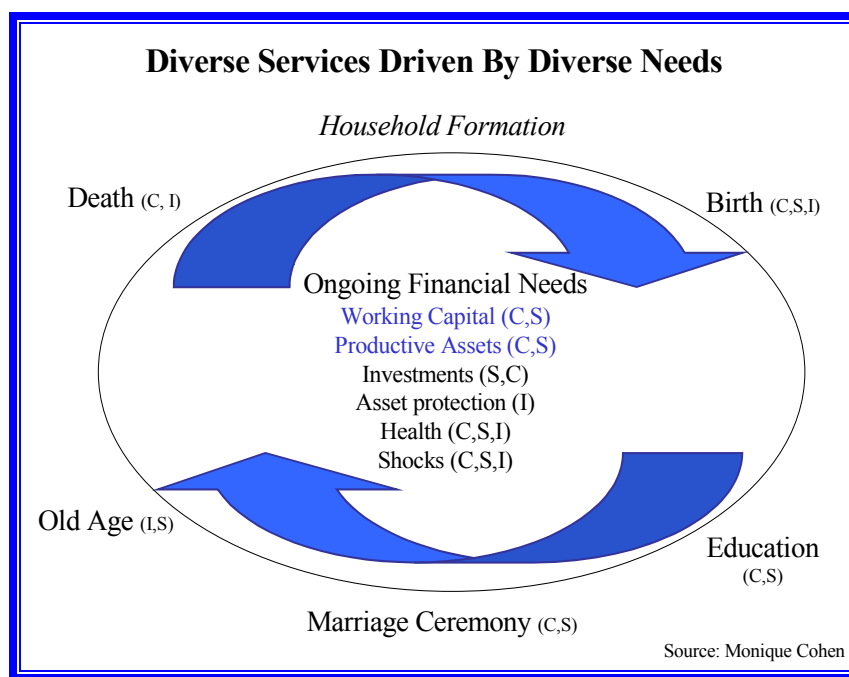
The breadth of the services offered by Equity Bank allow it to respond the needs of a diverse clientele which in turn allows it to cross-subsidise services to its lower income clients in the belief that they too will grow into profitable customers.

Advocates of targeting often insist on focusing exclusively on the “poorest of the poor” and excluding the non-poor (however vulnerable they are). This results in a rather extreme position. Those that place emphasis on only serving the “poorest of the poor” are effectively saying: “According to our survey, you are not-so-poor: go away and have a serious crisis in your household and come back to us when you are really one of the poorest of the poor, ideally destitute, then we will serve you”. By excluding the “not-so-poor” from access to financial services, the advocates of targeting are making them several times more vulnerable to such crises. And so it is probably only a matter of time before they are adequately poor to be allowed into the programme, or so destitute that it is no longer useful to them. Furthermore, of course, when the vulnerable non-poor become poor enough to qualify for MFIs dedicated to targeting the poorest, serving them with appropriate products and delivery systems is much more difficult: group-based guarantee loans for enterprise, repayable in weekly instalments rarely suit the needs of the poorest.

The challenge before us is to build inclusive financial systems that provide affordable, flexible and reliable financial services not just to the rich, not just to the “poorest of the poor”, but to all.

Diverse Services Driven By Diverse Needs

The microfinance industry has traditionally seen poor people’s needs for financial services simply as “credit for enterprise”. Today however, it is generally accepted that poor people also need access to lump sums of money to send their children to school, to buy medicines, to respond to other shocks and emergencies that beset their households, for social and religious festivals, to save up for old age etc. Thus that poor people need a range of “financial services” not just the traditional, mono-product, working capital loan.



C = Credit, S = Savings, I = Insurance

Thus, the typical 4-12 month working capital loan repayable in equal, immutable, weekly instalments does not adequately reflect the changing realities of poor households – whose income and expenditure flows can change significantly according to the season, the advent of festivals or shocks to the household economy. Low-income households need prompt access to emergency loans (a role played by family/friends or the informal sector moneylenders in most countries) or to increased flexibility in the repayment schedules set by financial institutions seeking to serve them.

In common with Equity Bank, growing numbers of financial institutions have started thinking about developing and delivering a range of financial products tailored to meet these needs.

Microfinance and the Millennium Development Goals

The growing understanding of the needs of poor people for a diverse range of financial services has led to a market-led revolution in microfinance with financial institutions initiating the development and delivery of a range of financial products. This reflects the Millennium Development Goals, or “MDGs”, that offer broadly accepted, measurable indicators of poverty reduction that are focused on poverty, education, health and empowerment.

In recognition of the potential of microfinance to address the diverse aspects poverty, the United Nations launched the International Year of Microcredit 2005. The Year, in the words of the Secretary General, Kofi Annan, “underscores the importance of microfinance as an integral part of our collective effort to meet the Millennium Development Goals. The challenge before us is to address the constraints that exclude people from full participation in the financial sector. ... Together, we can and must build inclusive financial sectors that help people improve their lives.”

Elizabeth Littlefield, the head of the CGAP notes, “Access to financial services forms a fundamental basis on which many of the other essential interventions depend. Moreover, improvements in health care, nutritional advice, and education can be sustained only when households have increased earnings and greater control over financial resources. Financial services thus reduce poverty and its effects in multiple, concrete ways. And the beauty and impact of microfinance is that, as programs approach financial sustainability, they can reach far beyond the limits of scarce donor resources.”

So how does microfinance contribute to the MDGs? The International Year of Microcredit 2005's Fact Sheet, "Microfinance and the Millennium Development Goals", notes that a review of microfinance literature points to several specific, illustrative conclusions about the impact of microfinance on poverty reduction and several other MDGs.

- **Eradicate extreme poverty and hunger.** Extensive evidence demonstrates that microfinance helps reduce poverty through increases in income, allowing the poor to build assets and reduce their vulnerability. For example, Khandker's 1998 seminal study for the World Bank notes that: "In Bangladesh, 5% of the Grameen Bank's clients graduated out of poverty *every year* by participating in microfinance programmes and, more importantly, households were able to sustain these gains over time."

Perhaps as a result, Todd and Gibbons worked with Grameen members who had been borrowing for a decade in Tangail. They concluded: "Perhaps their most significant finding was that, compared with 18 percent of non members, 58 percent of the Grameen borrowers had crossed over the extreme poverty line (defined as an annual income sufficient to provide each family member with a daily intake of 1,800 calories.) Of the 42 percent of the Grameen borrowers who failed to cross the poverty line, fully 60 percent had experienced a serious illness in the family - most commonly tuberculosis, typhoid, jaundice, and gastric ulcer. Grameen loans prevented these families from becoming destitute, but they were insufficient to overcome their crises" (Bornstein, 1996).

In their synthesis paper for World Development Report (WDR) 2000/1, Sebstad and Cohen conclude, "Findings from a growing number of impact studies support the proposition that microcredit reduces vulnerability by building a strong and diversified base of household assets." They go on to note that, "Impact research on BRAC members suggests that positive impacts on income poverty are driven by investments in productive assets. This process, however, is conditioned by cumulative loan size, which generally is associated with length of time in the program. Zaman (1998) found that income impacts occur for moderate poor Bangladesh households after a cumulative loan size of 10,000 *taka* and following investments of early loans in productive assets such as livestock or poultry. Montgomery, Battacharya, and Hulme's (1996) clients found greater improvements in household income and a sharp growth in productive assets for third-time borrowers. They also found that successive loans lead to a buildup of assets over time and that the structure of assets shifts in favor of more productive assets. Mustafa et al. (1995) found that older members have asset values 112 percent higher and expenditures 26 percent greater than newer members" (Sebstad and Cohen, 2001).

In Uganda, Wright et al. in a study prepared as a background paper for the WDR 2000/1 conducted in Uganda, concluded, "On the basis of the research, it is indeed fair to conclude that, "Financial services reduce the vulnerability of poor individuals and households by providing access to "chunks" of money to protect against risk and cope with shocks" (Wright et al., 1999).

- **Achieve universal education.** Households that have access to microfinance spend more on education than non-client households. Improvements in school attendance and the provision of educational materials are widely reported in microfinance households. Participation in credit and savings programs has enabled many families to send several children at a time to school, and has reduced drop-out rates in higher primary grades. For example, Save the Children's 1999 study in Honduras showed that microfinance clients increased earnings, which enabled them to send their children to school and lower drop-out rates from schools.

Similarly, results from the BRAC-ICDDR,B studies (Chowdhury and Bhuiya, 1998) give us an indication of positive trends. The percentage distribution of children (11-14 years) achieving "basic education" (pre-determined level of mastery in reading, writing and arithmetic, as well as "life skills") rose from 12.4% in 1992 (before the BRAC programme began in the area) to 24.0% in 1995

among the children of BRAC members. By comparison, only 14.0% of the children of those who had not joined BRAC achieved “basic education”. On the other hand, the influence of the BRAC pre-primary and primary schools on these statistics are not recorded.

Furthermore, Sebstad and Cohen note that, “One study from Indonesia shows that credit contributes to increased expenditure on education, another from Kenya shows that program borrowers are more likely than those in a control group to spend a portion of their enterprise profits for school fees (Sutoro 1990; Buckley 1996a.)” in Sebstad and Cohen (2001).

- **Promote gender equality and women’s empowerment.** Microfinance clients are overwhelmingly female. Microfinance has been widely credited for empowering women by increasing their contribution to household income, the value of their assets, and control over decisions that affect their lives. In their 2002 study for UNIFEM, Cheston and Kuhn found that microfinance programmes from different regions report increasing decision-making roles of women clients. For example, the Women’s Empowerment Programme in Nepal found that 68% of its members were making decisions on property, family planning and daughters’ education, and also negotiating their children’s marriages.

Evidence from Bangladesh corroborates this: “Mizan (1994) found that “On average, women contribute 38 percent to the total household income ...” and concluded that “Grameen Bank participation has a positive and significant effect on women's decision-making both in bivariate and multivariate context. This finding indicates significant success of Grameen Bank programs in affecting women's status relative to men in Bangladesh. ... Bank participation benefits women by providing them with important monetary resources as well as non-monetary. For example, more years of participation enable women to acquire resources, including income, negotiating skills, social network affiliations, and knowledge, helping them to gain more decision-making power. ... In Bangladesh, where structural and cultural factors have hindered women from realizing their earning and household decision-making potential, Grameen Bank's contributions may be regarded as revolutionary.”

Wright and Ahmed (1992) noted the same development among the members of the Concern and Action Aid savings and credit schemes they studied. “Concern Mirpur members report improved social status as a result of participation in the programme. Husbands and other relatives are described as showing more respect, members are more confident in their dealings with the outside world and are showing greater awareness of their rights. Many are learning to read and write, and there is a real sense of determination among group members to “stand on their own feet””.

Beyond Bangladesh, there is little additional evidence, although Wright et al. (1999) found positive effects in Uganda and Hulme and Montgomery’s (1996) study in Sri Lanka found that loans contributed to women’s independent income, which gave them more bargaining power in their relations with male family members.

- **Reduce child mortality, improve maternal health, and combat disease.** Microfinance contributes to improved nutrition, housing, and health, especially among women clients. For example, a 2001 USAID-AIMS study notes that in Uganda, FOCCAS microfinance programme has seen 95% of clients engaged in improved health and nutrition practices for their children, compared to 72% for non-clients. Also 32% of clients had tried at least one AIDS-prevention practice, compared to 18% for non-clients.

Many would argue that the poor's primary obstacle to accessing good health (and indeed education) is money, and that if the poor have the cash, they can and would buy the services. They would argue that good nutrition is about having the money to buy adequate food, that reducing diarrhoeal disease is about having the money to install tubewells and latrines, that increasing family planning is

dependent on having the money not to have to depend on many children as a “pension plan” to look after their elderly parents and so on. These arguments are attractive and not without some substance.

They are reflected in the WDR 2000/1 Uganda report, which concluded, “it is interesting and important to note that Uganda Women’s Finance Trust’s services are allowing clients to make substantial investments in sending children to school and curative health care. Indeed, these (and particularly education) repeatedly emerge as some of the most valued results of access to credit. While acknowledging (as has been done above) that the poorer members of the community are not benefiting from access to most MFIs’ services, and therefore that support for the health and education of these people is necessary, it is also important to recognise that microfinance has a significant role to play. This is particularly so as developing countries move toward the “privatisation” of health and education and to encouraging communities to purchase these services ... money makes the market go round” (Wright et al., 1999).

Turning again to Bangladesh where most of the substantive work has been done. Schuler and Hashemi (1992) concluded that Grameen Bank members were statistically more likely to be using contraceptives (59% of Grameen members as opposed to 43% of a matched control group). Rahman and de Vanzo reached similar conclusions as a result of their work in Tangail (pending publication). Similarly, a recent Asian Development Bank report noted that, “Contraceptive use goes up among members because they are better able to overcome the barriers to obtaining access to contraceptive services (lack of mobility, cash, information, among others). Contraceptive use goes up among non members because of the diffusion effect of changing fertility norms in the village as a whole.”

Nutritional indicators also seem to improve where MicroFinance institutions have been working. Hashemi and Morshed (1997) cite a study conducted by the World Bank in collaboration with the Bangladesh Institute of Development Studies, which showed that the Grameen Bank not only “reduced poverty and improved welfare of participating households, but also enhanced the household’s capacity to sustain their gains over time. This was accompanied by an increased caloric intake and better nutritional status of children in households of Grameen Bank participants.”

Regionally Speaking ...

(This section draws extensively on Elizabeth Littlefield’s presentation “Global Trends in the Microbanking Industry”) The major less developed regions of the world have distinct characteristics in terms of economic development, demographics/population density, history and financial institutions, and as a result in the type and extent microfinance services available.

Asia

The largest and most profitable banks/NGO-MFIs (including BRI in Indonesia and ASA in Bangladesh) are located in Asia. Nonetheless, large numbers of weak NGO-MFIs still exist – thus demonstrating the nature and size of the under-served market. The economic environment means that the Asian financial institutions are often the most cost efficient (the best perform at 5% operating efficiency). Around 550 million clients are served throughout Asia, but 200-400 million remain un-served in India and similar number are also un-served in China alone ... in these times when the donor community is choosing to focus so strongly on Africa, it is important to note that the numbers of poor people in South Asia alone (470 million) significantly exceed those in Africa (250 million).

Africa

Many diverse institutional models are functioning in Africa, but most clients are served by credit unions and co-operatives – often based (particularly in East Africa) on the agricultural commodities their members sell (e.g. coffee, tea, cotton etc.) or the nature of their employment (teachers etc.). In West and Central Africa however, savings and credit cooperatives are generally more community-based. In contrast to Asia, the lack of population density means that rural and agricultural finance is particularly challenging, and thus many MFIs are urban-based and focused. Perhaps as a result the July 2003 MicroBanking Bulletin identified only 8 sustainable institutions and estimated that only around 25 million clients are being served throughout the continent. However, these numbers may under-estimate or ignore the large numbers being served by cooperatives and postal banks. Nonetheless both international and domestic banks are starting to take an interest in the potential of the low-income market in Africa.

Middle East

The 48 million estimated clients in the Middle East/NorthAfrica region are typically served by NGO-MFIs that remain heavily dependent on donor subsidy. These NGO-MFIs are typically in the infant stages of their development and continue only to provide small working capital loans to their clients.

Latin America

Some markets in small countries in Latin America are saturated. The sub-continent is full of nascent commercial markets with strong consumer credit and microenterprise lending and institutions that are less focused on social agenda. As a result of this it contains numerous (27) profitable MFIs serving an estimated 13 million clients. However, recent part of the region have also seen a backlash against high rates.

Europe and Central Asia

In the transition economies of Europe and Central Asia, the focus is on new enterprises, and on job creation. Overall, there is relatively little financial intermediation and much of this is provided by the Credit Unions, which tend to serve relatively wealthier clients. In this region there are only about 17 million estimated low-income clients with access to financial services.

Conclusion

Internationally, the microfinance industry has had remarkable success in extending financial services to the poor; and has demonstrated a significant capacity to contribute to the Millennium Development Goals. But the industry has a long way to go – and over a billion low-income people remain unable to access formal financial services.

Internationally several key principles for microfinance are emerging and increasingly accepted.¹ These principles are:

1. Microfinance is a powerful instrument against poverty.
2. The poor need a variety of financial services - not just loans
3. Interest rate ceilings can damage poor people's access to financial services.
4. Financial sustainability is necessary to reach significant numbers of poor people.
5. Microfinance is about building permanent financial institutions and systems that serve the poor.
6. These financial institutions are varied in nature and form from NGO-MFIS to commercial banks.
7. The lack of institutional and human capacity is the key constraint and to scale up and provide a wide range of sustainable financial services to the poor - microfinance must continuously improve/refine systems, products and delivery mechanisms and also make appropriate investments in human and institutional capacity to ensure 'organisational sustainability'.

Microfinance can play a key, cost-effective and sustainable role in achieving the MDGs if we build flexible and reliable financial services that respond to the real, diverse needs of the poor and vulnerable non-poor. Billions of people are waiting for us to do so ... **References**

¹ Adapted from CGAP's "Key Principles of Microfinance", CGAP, Washington, 2004

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