Bank of Uganda - German Technical Co-operation
Financial System Development (FSD) Project

# RURAL MICROFINANCE CLIENTS IN UGANDA

# FINCA CLIENT ANALYSIS

Barbara Grimpe

FSD Series No. 6

# RURAL MICROFINANCE CLIENTS IN UGANDA
# FINCA CLIENT ANALYSIS

**Barbara Grimpe**

**FSD Series No. 6**

Responsible:
A. Hannig

Publisher:
Bank of Uganda – German Technical Co-operation
Financial System Development (FSD) Project
37/43 Kampala Road
P.O. Box 27650
Kampala, Uganda

Printer:
United Printers Ltd.
Plot 143/5 6th Street, Industrial Area
P.O. Box 1726
Kampala, Uganda

## Contents



### Annexes



### Abbreviations

| | |
|---|---|
| BoU | Bank of Uganda |
| FINCA | Foundation for International Community Assistance |
| FSD | Financial System Development Project |
| GTZ | Deutsche Gesellschaft fuer Technische Zusammenarbeit (German Technical Co-operation) |
| MFI | Microfinance Institution |
| NGO | Non-Governmental Organisation |
| Ush | Ugandan Shilling |
| US$ | US Dollar |

# 1 Introduction

This paper presents the findings of a three-week field research on rural microfinance clients of the Foundation for International Community Assistance (FINCA) in Masindi town, around 200km from Kampala in the North of Uganda. This research, to assess impact on poverty alleviation, was carried out in course of an internship in the Financial Systems Development (FSD) Project of Bank of Uganda and German Technical Co-operation (GTZ), from 18 February to 21 April 2000. FSD, co-operating with different actors in the financial sector, aims to improve access to financial services, particularly for poorer segments of the population in rural areas. While creating an enabling environment for microfinance through the development of a legal framework for the regulation and supervision of microfinance institutions (MFIs) and a microfinance training centre in co-operation with the Uganda Institute of Bankers, FSD wanted to investigate the impact of microfinance on the project target group. FINCA, in turn, supported the study to learn more about the needs of its clients and thereby improving existing products and introducing new ones.

To deepen and broaden the financial sector to include poorer and hitherto unserved people, microfinance institutions are of special importance as they strive to provide poorer parts of the population and micro and small enterprises with savings facilities and loans through the use of innovative financial technologies.[1] They are still mainly NGOs and rely on donor funding. FINCA is also incorporated as an NGO, but has begun to borrow commercially from one of the local banks.

Under the financial system approach, the focus changed from delivery of loans to the viability of the institution itself. In case of MFIs it is relatively difficult to attain sustainability, because credit for microentrepreneur's is usually relatively low, thus transaction costs are relatively high. The main purpose of the group lending methodology, as also FINCA applies it, is to lower these costs: individual repayment of the loans is submitted to group self- regulation. If a member of the lending group does not repay in time, or not at all, the group has to recover the money. In addition, bookkeeping is partly delegated to the group. Moreover, FINCA, like other MFIs, tends to rely on already existing informal groups, which also helps to diminish transaction costs.

However, the concentration on financial sustainability might reduce impact assessment to no more than what is called the willingness-to-pay test.[2] According to this test, impact is approximated through repayment and arrears rates, arguing that "if clients use the services repeatedly and, therefore, pay for them repeatedly, it is evident that they value the services more than the cost. One can surmise, therefore, that the client believes that the benefits of the service on their lives exceeds the costs."

This being an anthropological study, the term to "value the services" is a very vague expression. Moreover, "benefits" as well as "costs" of the provision of microfinance services cannot be expressed by (monetary) figures only. Loan amounts, repayment rates and arrears as well as, for example, drop out rates, investment rates and outreach are just hints of a complex field of economic activities and a deep social network of needs, constraints and effects. These indices are indispensable analytical tools, but they cannot adequately represent complex socio-economic phenomena. Accordingly, they do not provide a sufficient answer of whether and how sustainably poverty is alleviated, how this is done and how far social relations are affected.

This study cannot furnish the definite answers to these last questions because experience has shown that it is difficult to measure the impact of microfinance, especially after three weeks of field research. A particular problem in this regard is the fungibility of money, i.e. the attribution dilemma.[3] The origin, destination, temporal ownership etc. , that constitute the flow of money within the respective household unit, including business and agricultural activities, are difficult to detect. Thus the loan use can only be approximated, and largely depends on the information given by the clients themselves. Additionally, although this study does not directly address the gender dimensions of microfinance, it attempts to raise pertinent issues that should be looked at not only by academicians but by the practitioners.

Nevertheless, some findings will be presented, taking into account the just mentioned complexity of the field. These findings are tentative answers to the general question: What is hidden behind the loan-repayment-process? The institution disburses loans at the beginning of each cycle and collects the repayments for it weekly, until the whole amount is repaid at the end of the cycle. Nevertheless, what is known about the clients, besides the fact that they repay the loan and save at prescribed times?

As a first step of utmost importance, a thorough analysis of the socio-economic activities of the clients has to be carried out. Thus, a great part of this presentation is devoted to this general analysis. The second part is about some findings related to the lending group, and comments are made about potential institutional weaknesses on part of the microfinance institution. Some tentative conclusions with regard to the question of the impact of microfinance will be drawn. This study also builds upon some of the observations made by Michael Fiebig (GTZ) and Luke Okumu (Bank of Uganda) during

[1] See also the World Bank goals, in a study of 1996, cited in Ledgerwood, p. 34: "to create employment and income opportunities through the creation and expansion of microenterprises; to increase the productivity and incomes of vulnerable groups, especially women and the poor; to reduce rural families' dependence on drought-prone crops through diversification of their income generating activities."

[2] Ledgerwood, p. 49

[3] Ledgerwood, p. 51.

earlier research on FINCA clients.

I would like to thank FINCA Uganda Headquarters and the field staff for their openness and generous support in carrying out this survey. Most importantly, however, my thanks go to all the women interviewed for their time and effort in answering my questions -only their contributions made this paper possible.

## 2 Methodology

Information was collected in formal interviews during home or business visits, usually lasting a few hours up to one day. Often the same person was interviewed twice or thrice, striving for participant observation, the central method of anthropology. According to this method, research is based on the following principles:

- Holistic perspective: Borrowing and saving were considered part of the wider social context, interdependent with some of its features. Emphasis was laid on financial features under the aspect of how they are linked to daily needs of clients.
- Basis of trust: To get reliable information, it is necessary to establish a trustful relationship between interviewer and interviewee. Instead of taking notes during the interviews, information was recorded afterwards in a field diary. This method increases the trustworthiness of the interviewer in the eyes of the interviewee. Nevertheless, this proved difficult.[4]
- Constant adaptation of the research plan: It is essential to begin field research with a conceptual outline, but the researcher also has to be ready to take over - sometimes surprising – new leads during the field study itself. The grounded theory claims the constant reorientation of the researcher in the field. This theory takes into account that reality is too complex for one to know the critical points of an analysis in advance. This approach requires phases of reflection on the collected data during the entire period of research, so that the same field can be re-entered again with a better overview and adapted research questions. The study was carried out accordingly.

Amongst others, this qualitative approach meant to concentrate in depth on a small sample of interviewees. FINCA only admits female group members; therefore all the seven interviewed clients were women. In addition, four group visits were undertaken in Masindi: three meetings of one lending group, in the following chapters called group 1, where six of the seven women were interviewed, and one meeting of a second lending group, referred to as group 2, where one woman was interviewed. Furthermore, one credit officer in Masindi was interviewed. Additionally, in Kampala, I attended two lending group meetings and interviewed a supervisor. As I do not speak any of the local languages, all interviews had to be conducted in English and therefore only with English-speaking women, who have had some basic education.



[4] It generally requires a trustful relationship to ask someone about his/her financial situation and problems.

# 3 General Features of Socio-Economic Activity

## 3.1 Profile of the Microfinance Clients

All women in the research sample are involved in commerce. Except for one woman, who is the director of a primary school, owns a boarding school, and undertakes or plans many business projects of relatively large scale and relatively long-term orientation, they have flexible businesses with relatively unstable income and thus medium-term orientation in their planning, and medium-scale orientation in the quantities they trade. Common features are:

- The products mostly do not stem from own production, but are bought for resale;
- They are bought in “stocks”, e.g. 50-l-sacks, 10-l-basins;
- The turnover and net gain are mainly accounted for in these units;
- Mostly durable goods are traded.

The women deal in two main product lines: clothes, mainly second-hand, and agricultural products, mainly durable food or long-life derivatives of agricultural products, for instance different types of flour. Medium-term and medium-scale orientation will be discussed in chapter 3.5 in more detail.

Apart from the small-scale business, they also engage in agricultural production, mostly for subsistence, but sometimes also for sale. Expenses arise from school fees, medical treatments, clothes and other family or household-related necessities. While these three economic spheres of commercial business, agriculture and specific expenses can be distinguished in theory, the women usually do not differentiate between them:[5] in general, any income in these spheres is used for any expense in any other sphere. Separate bookkeeping is not common. This implies that the use of a loan is not restricted to the business only.

Considering gender relations and business, five out of seven women keep their business totally independent from their husbands. One woman is not married but partly works together with a friend. The other woman partly works together with her husband. At least half of the women have experiences hardships early in their life,[6] probably nourishing the strong desire for income-generating activities independent from the husband. Accordingly, the tendency to avoid having to share the generated income with the husband prevails in all cases. In two cases, having an own business was explicitly understood as a strategy of complete emancipation from the husband. Altogether, the opportunity to have a business is probably the result of as well as one of the stimulating factors for women empowerment. The possibility to take FINCA loans as well as its restriction to women is likely to sustain this emancipation process, although immediate effects could not be observed as it is very difficult to establish a direct causal relations**hip.**

## 3.2 Costs and Benefits

To a certain degree, it is possible to measure benefits and costs of economic performance quantitatively, as shown by the following two examples:

(1) A woman sells new clothes in different markets. Her costs and benefits of a specific day:

- 12 hours of business-related activities (including six hours of transport);
- A turnover of approx. USh 14,500;
- A net gain of approx. USh 7,000, i.e. of around USh 580 per hour.[7]

(2) A woman sells onions at the Masindi market. Her costs and benefits per week:

- Nine hours of business activity per day, seven days a week;
- One basin of onions costing USh 8,000 is sold in one or one and a half days, with a net gain of USh 3,500-4,000 per basin;
- The weekly net gain amounts to USh 17,500-28,000, which translates into an hourly net gain of around USh 270-USh 444.

The above given examples show astonishingly low daily and weekly incomes. However, in interpreting theese figures one has to take into account that the incomes are subject to seasonal fluctuations (see chapter 3.4) as well as the

[5] See also Fiebig/Okumu p. 19

[6] For instance, two women had to leave school and marry because of pregnancies at the age of 14 and 15 respectively. One woman had to drop out of school prematurely because of the early death of her mother. Another one was forced into early marriage by the civil war conditions in the late seventies.

[7] To estimate the weekly income of this woman: She travels to different markets around four days a week, although the other markets are not as far as in the mentioned case. One day of the week she usually travels to Kampala to buy more clothes. Hence estimating a daily net gain of USh 11,000 and considering four working days plus one day of travel to Kampala without selling anything, in 60 working hours she earns USh 55,000, that is around USh 900 per hour.

woman might have other sources of income like for example from agriculture. Furthermore, the figures leave out one important feature that can only be grasped by qualitative considerations:the impact of the business on health.

## 3.3 “Health Costs”

Illness is not only a reason for failure in weekly repayment or drop out. It is also a result of the way business is performed to maintain or reach a certain income level. Of course, the abject state of medical infrastructure in some suburban and rural parts of Uganda contributes to relatively poor health. However, the nature of the business itself as well as market competition are also physically extremely demanding. As many market women have to change market places regularly and do not own a market stall, they spend nearly the whole day to dire weather conditions and must rely on dangerous transport. The experiences of the two women outlined in the cost-benefit-analysis in the last chapter suggest high, even if hardly quantifiable “health costs”.

## 3.4 Seasonal Changes in Demand

According to some interviewees, a great part of the businesses pursued is subject to seasonal changes in demand, although it varies according to the products sold: Sale of new clothes is highly seasonal, whereas the demand for second-hand clothes and durable food, e.g. flour, beans, is much more stable.

The demands depend largely on the seasonal changes in agriculture. As most of the agricultural products are harvested in June and July, the demand for clothes peaks in these months. A second peak in demand is in November and December when the second main harvesting season takes place. Moreover, the demand before Christmas is very high since it is a widespread habit to give clothes as presents. This tendency is more for expensive new clothes than for second-hand items.

In contrast, in June and July as well as November and December, the demand for the second main product line, i.e. durable food, is low because potential customers tend to rely on their own harvested crop. An increase in the demand for some agricultural products occurs the days before the heavy rains of the rainy season in February or March and October when people buy beans and peanuts as seeds for sowing.

A general strategy in times low demand, when business tends to stagnate, is to switch over to agricultural activities, i.e. to substitute trade with subsistence farming on the plot of land the woman or her family owns, out of which a possible surplus is sometimes sold. But it is important to mention that it is also common not to follow any strategy: Just wait and “muddle through” until better times come. This “muddling through” is consistent with some features of individual bookkeeping and business planning discussed in the following chapter.

## 3.5 Medium-Term and Medium-Scale Orientation

### 3.5.1 Ranking of Businesses

It was earlier mentioned that the women tend to act and plan based on mid-term and medium-scale orientation. This assumption derives firstly from a ranking of types of businesses established by reference to some comments of the interviewed women. The ranking reflects the subjective perception of the women, but contains a high degree of objectivity, as will become clear later. However, it is not complete and further investigations will be necessary.

1) shop selling many different items;
2) new clothes;
3) second-hand clothes;
4) durable food; onions; fruits and vegetables;
5) cooked food; fruits and vegetables.

According to this ranking, the majority of the interviewed women as well as a lot of other lending group members fall in the middle since they mainly sell clothes (second-hand and new) and durable food like beans and different types of flour. The top of the hierarchy at the same time stands for:

- long-term orientation;
- large need of capital/investment;
- large-scale business;

- high revenue;
- high desirability.

The bottom stands, accordingly, at the same time for:

- short-term orientation;
- few need of capital/investment;
- small-scale business;
- low revenue;
- low desirability.

The traded goods can be characterised as follows:

- Cooked food (level 5) requires low capital and perishes from one day to the other, thus small quantities are needed. Hence it can be classified as a small-scale business of short-term orientation since planning takes place on a daily basis. None of the interviewed women, however, sold cooked food.
- Durable food (level 4), and fruits and vegetables (level 4 or 5): One woman stated that she would rather sell beans, peanuts and peas than fruits and vegetables since the former can stored for longer periods of time. This indicates a medium-term orientation, as the process of replenishing the stock and selling it takes some days. However, this market woman works in a part of the market where the market sellers do not have permanent market stalls. In another part of the market some vendors sell a high quantity of fruits and vegetables in such rented market stalls, thus it seems to be possible to run the fruits and vegetable business on a higher scale basis with an accordingly higher income. For this reason, one might also allocate these goods to a higher level, e.g. of durable food, as shown in the ranking scheme. The onion business (level 4) also goes beyond planning on daily basis: Selling onions requires little capital to start the business, but onions are durable, and the time span between buying and selling them can therefore be longer. By selling onions, one woman hopes to slowly increase her profit so that in the next cycle she will be able to get a higher loan. Through this loan, she intends to progress to the business of selling second-hand clothes (level 3) from one of the wooden market stalls. Amongst others, this is mo!e desirable to her because a market stall would protect her against the scorching sun (see also chapter 3.3).
- Second-hand (level 3) and new clothes (level 2): One woman selling new clothes on different markets said that she had started her business with selling second-hand clothes. Second-hand clothes cost less, thus require lower capital. Additionally, the second-hand clothes business is less dependent on seasonal changes than selling new clothes, as people can afford the low prices practically throughout the year, while new clothes are too expensive so that customers mostly buy them in the harvesting season. Assuming an entire business year, the turnover is thus apparently still higher than in case of second-hand clothes. Therefore, the new-clothes-business is relatively risky, but also has times of high revenue: The woman argued that in bad seasons she sells nearly nothing,[8] while she expects very high turnover rates of up to USh250, 000 on a single day in the harvesting season. Other advantages are that customers do not bargain that much as they do with used clothes since the new ones do not have any defaults, and transport is more convenient as smaller quantities are needed for the same turnover.
- The shop (level 1): One woman's dream is to own a shop in town. For the time being, she sells beans and different types of flour, thus belonging to the fourth level of the categorisation above. The shop is still unattainable for her, as she argues: With rent at about USh 600,000, it would be too expensive to run especially since the whole amount would have to be paid in advance. Moreover, she would need a licence from the local council and have to pay several taxes. Running a shop therefore has high market entr**y barriers.**

### 3.5.2 Individual Bookkeeping

The interviewed clients are to a certain extent aware of seasonal changes, and they have rough expectations concerning their future business activity. This shows a certain long-term orientation. However, other information, as presented in the preceding chapter, suggests that these women are to be located in the medium-term and medium-scale orientation. The observation of their accounting skill confirms this:

- Stocks, e.g. 50-l-sacks or basins, are the planning units accounted for. A stock is broken down and sold off in smaller units. When the stock is depleted, another cycle of buying in bulk and selling in smaller units begins.In conclusion, this business activity is based upon a principle of repeated rounds, i.e. of hardly interrelated planning units. These rounds vary in length according to the respective demand for the product on sale.
- By requiring weekly repayments FINCA introduces a supplementary system of repeated rounds. The date of weekly repayment is the deadline of each round: After having reached the repayment date without loan default, another round with a new deadline begins. Nevertheless, this second system of repeated rounds does not go in line with the first one, which is the one the businesswomen usually stick to. In contrast to the business cycle in the loan cycle the length of rounds is strictly defined. In addition, aclearly defined quantity of money, i.e. the instalment and interest,



[8] She is woman (1) cited in chapter 3.2, and her working day the cost-benefit-analysis bases upon was in the dry season.

has to be paid. Some women stress that they often have to struggle to reach the demanded weekly amount. Especially the clothing business seems to demand longer repayment periods. It appears that in bad seasons a good portion of the stock can only be sold weeks after receiving the loan, whereas one can sell almost nothing in the first week. Two womenm, therefore proposed longer repayment schedules.[9] In the following as well as later chapters this strict system of loan repayment will be discussed in more detail. The question which arises is whether the incongruence of the two, the loan and the business cycle, has to be seen as a disadvantage or not.

- The extent to which individual books are kept confirms these observations. In brief, bookkeeping actually mostly does not take place: Most of the women stated that they have it all "in mind".[10]
- In general, the women do not have a long-term business strategy, but make use of any circumstance that promises income. Thus business decisions do not follow an elaborate plan, but often arise spontaneously and reflect a „muddling through", as already mentioned in chapter 3.4 [11]. Again, this may conflict with the rigid FINCA repayment requirements.
- Finally, the women do not differentiate between socio-economic spheres of incomes and expenses, e.g. between household and business, as mentioned previously. Income is transferred from one sphere to another according to financial bottlenecks. Similarly, it is common to switch from business activity to agricultural production when the demand is low in the former.[12]
- However, according to one interviewee, some women do differentiate between socio-economic spheres as they distinguish their home in town from their home in the village. The home in the town is apparently the place where the business starts, while the home in the village is probably associated with subsistence agriculture, although sometimes the plot of land is situated at yet another location. It is unclear whether this is a distinction mainly in spatial terms, or whether it is of specific socio-economic relevance. At least three of the interviewed women have second homes. Without knowing that a second home exists, the interviewer might over- or underestimate the living conditions of the interviewee by visiting only one of the two places the woman equally refers to as „her home". This is a striking example for the problem of hidden assets.

From the above findings, the following conclusions can be made:

1) No specific business strategies are followed: decisions are taken spontaneously, and the common practice is "muddling through".
2) Planning either occurs on day-to-day basis or, even if encompassing longer periods of time, is stock-oriented.
3) It is often difficult to repay on a weekly basis as scheduled.
4) The loan thus imposes a strict repayment time schedule that often does not correspond to the nature of the b**usiness.**

## 3.6 Financial Bottlenecks and Reciprocity

More than western societies, African people are actors within a social network of strong reciprocal commitments. Social bonds mainly exist in relation to kinship.Yet friendship as well as being part of the same lending group means being bound to somebody else, as some findings suggest. These bonds partly determine the way the individual spends or obtains money, including the money of the lending process.[13]

Only few findings could be made as people do not easily talk about their financial commitments to an external visitor. Nevertheless, these findings hint at the important role of social bonds in financial transactions, including microfinance:

- A woman reported that members who are unable yo pay back their loans on time sometimes address other group members known to be wealthier or the ones being their guarantors.
- When facing a problem of repayment, one woman usually approaches her friend (her working colleague, selling clothes as she does) or directly addresses the friends of that friend. In turn, she also lends to others.
- As a general problem, one woman reported: „As soon as friends or relatives become aware that you recently managed to earn some more money, they approach you to share it with you. Even distant relatives then become very close relatives".

[9] Fiebig/Okumu, p.19, made the same observation.
[10] Two women referred to the type of business as a reason for not keeping books: only the people owning a shop with a certain visible stock inside would work with, for example, an inventory lists.
[11] Fiebig/Okumu, p. 20, call this a "trial and error process"
[12] A similar observation was made by Kurt Beck studying the economic activity of farmers in the North of the Sudan (Beck, p.85). He stresses that a bad infrastructure, illness and seasonal changes result in the habit of taking the money out of one economic sphere to finance another one. This money transfer would not be regular and well-planned but, according to the urgency of the situation, would be like "filling holes". According to Beck, in such situations it is common to run into debt, for example amongst neighbours, relatives or friends. This connection between unforeseen events, financial bottlenecks and indebtedness also seems to be experiences by the women analysed in this study.
[13] Fiebig/Okumu mention this problem, p. 19/20, as a potential threat to repayment capacity by informal lending.

The following conclusions can be drawn:

1) The FINCA technology and methodology, through fixed repayment rates according to a fixed time schedule increases the number of reciprocal commitments within or outside the lending group. Thus one consequence of borrowing could be (multi-) indebtedness in case borrowers do not have the necessary repayment capacity to meet their obligations and therefore have to turn to other sources of credit to pay back the first loan. it is difficult to decide whether this is a negative or positive impact. Reciprocal commitments can be both advantageous and disadvanageous to the involved individuals depending on who is committed to whom. Moreover, one might argue that for the group as a whole, solidarity is increased. Further investigation might provide an answer to this question..

2) The need to lend or donate money to others is a social duty that probably hinders individuals from freely accumulating mone**y.**

# 4 Findings Related to the Lending Group and the Microfinance Institution

## 4.1 Bookkeeping Skills Within the Lending Group

In the weekly meetings lasting between one and two hours, the mandatory loan instalments and savings of each member are collected and registered: Each member's book contains the individual data,[14] while different account books keep the group data, summing up the individual figures in lists and tables. The entire money collection process within the group as well as its recording in both member books and group account books is done by the group members, preferably, but not always, by members of the presiding group committee. All members involved in recording showed a certain degree of routine in the procedures. Problems in recording were mostly discussed amongst the members and then cleared up.

On all days of group meetings, the credit officer or, in case of group 2, the supervisor in Masindi, joined the group only at the end of the two hours. He then mainly dealt with aggregated figures, i.e. he checked in the lists whether all members have paid. He also calculated the cash flow, i.e. loan repayment and savings, from the whole group. In Kampala, the credit officer joined the meeting from the beginning onwards and was far more involved in the process of recording.

This self-regulation diminishes transaction costs for FINCA. Yet a particular observation suggests that the members lack a basic understanding of accounting principles, so mistakes are bound to occur.

The recording in the individual member books is partly done independently from the recording in the group account books, as observed in one meeting. Immediately after the collected money had been counted, the member books were filled with the new figures of the individual savings. But the group account books were filled in without consideration of the actually collected money: The woman who was in charge of writing down the savings referred to the record of the last week and merely copied the figures from that list. However, in reality, most of the members do not save the same amount each week.

In the next meeting, the credit officer cross-checked the figures in the group account book with the figures in the individual member books. In nearly half of the cases he had to correct the figures, not only of the last, but also of the current week. This incident is particularly remarkable as the mistake was not only done by the treasurer, but she also claimed to have learnt accounting at school as well as during a FINCA course.In this case additional transaction costs occured on the part of FINCA since the credit officer had to correct the figures in the group account books.

In conclusion, the overall organisation as well as the money collection and registration process, contributes to self-regulation in the lending groups. Nevertheless, relatively hravy mistakes occur in bookkeeping.

## 4.2 Loan Development and Savings Potential on the Group Level

During the weekly meetings of the lending groups 1 and 2, the majority of the member books were analysed with regard to four questions.

1) What is the average loan amount of each group in the current cycle?

2) In regard to the total loan amount of each member, is there a difference in loan amounts between the former cycle(s) (either one or two) and the current cycle? If there is a difference, is the current loan higher or lower than in the former cycle(s)?

3) How has the rate of weekly savings developed so far in course of the current cycle (group 1) or in course of the last cycle respectively (group 2)? Did it increase, decrease or stagnate?

[14] Total loan amount, weekly loan instalment, the amount of the weekly savings as well as both the balances of loan repayment and savings.

4) How much is the actual weekly savings rate in comparison to the amount required by the FINCA lending conditions? Is it higher, lower or equal?

Due to a different degree of access to the data, the findings on group 2 are more exact and specific than on group 1. [15]

**Question 1:** Comparing the total loan amounts taken by the two groups in this cycle, group 2 with around USh 260,000 has a much higher average than group 1 with around USh 192,000. The reason for this is unclear. It might be due to a difference in the average age of the group, referring to the number of cycles the respective member already passed through. It would have meant in this case that group 2 is much older than group 1, but this could not be verified.

Another possible reason for the higher loan amounts in group 2 are mechanisms of group self-regulation that strive to decrease the risk of non-repayment for the entire group. Groups tend to admit those members that are of the same background with regard to income, type of business, habits etc. as this establishes more trust. New members are mainly admitted by introduction through other members, often through those who are their future guarantors. Thus the group is kept relatively homogenous. One might particularly conclude that a higher level of income will also translate into higher loan amounts. But this conclusion is a thesis that still requires more investigation.

**Question 2:** With regard to the development of the amount borrowed by each member, it is striking that in both groups, almost half of the members had decreasing loans over the time.[16]

**Development of the Loan Amount**

| | No. of members | |
|---|---|---|
| | **Group 1*** | **Group 2** |
| **Lower loan amount** | 9 | 7 |
| **Higher loan amount** | 7 | 6 |
| **Same loan amount** | 3 | 2 |
| **TOTAL** | 20 | 15 |

* one case not known

To discuss this result: It is doubtful to conclude from a decreasing loan amount that the income must have deteriorated to the same extent before, a conclusion one might think of first. The development of the loan amount does not (only) result from the business performance, but may have other reasons. There is a lot to be said in favour of that. For example, the women do not clearly distinguish between business, agricultural and household expenses, as already mentioned above. Hence a loan decrease might be due to any problem in one of the other socio-economic spheres, but it might also result from a change in the appreciation of the loan being just one amongst other financial sources, and therefore indicate a lower demand. In any case it remains an open question why so many women had lower loans at the same time. Much more research is needed to answer this question.

**Question 3:** In the development of the savings rate during the current cycle in the case of group 1, or the last cycle in case of group 2, both groups show a clear negative tendency. In group 2 particularly, more than 50% of the members had a decrease in the weekly savings amount.[17]

**Development of the Savings Amount**

| | No. of members | |
|---|---|---|
| | **Group 1** | **Group 2*** |
| **Lower savings amount** | 7 | 11 |
| **Higher savings amount** | 3 | 0 |
| **Same savings amount** | 10 | 3 |
| **TOTAL** | 20 | 15 |

* one case not known

The following conclusions can be drawn: The members probably face more problems of repayment towards the end of the loan cycle. Hence borrowing does not necessarily increase the savings potential in the long run. This seems to suggest weak savings potential. Nonetheless, it must be kept in mind that assuming any causal connection between

[15] The FINCA member books leave space for recording of only few cycles and FINCA distributes new member books when the old ones are completely filled. In particular, in case of group 1 some member books contained records of the two former cycles, while in case of group 2, the last cycle was the only one recorded. In addition, some women have just recently become members of the group so that question 1 on the development of the total loan amount was not relevant in these cases.

[16] This was confirmed by Fiebig/Okumu: “Interviews with credit officers and headquarters’ staff underlined that no stringent graduation to higher loan amounts occurs throughout loan cycles.”

[17] One must be aware of the fact that in case of the total loan amount, the time span of the analysis was from the former cycle(s) to the current cycle, while in case of the development of the savings rate, the current cycle was analysed. Thus, the conclusion that has been drawn is the same ( = a tendency towards a decrease), but not for the same time. Hence no *immediate* causal connection between both decreases should be assumed.

taking a loan and saving is difficult, as surplus will not necessarily be paid into the group's savings account. It can also be kept in cash or be spent immediately.

**Question 4***:* As the analysis of the savings performance of group 2 in its first week after loan disbursement shows, out of 20 members, 14 members, i.e. the majority, had a higher amount of savings than expected and six saved at least the required amount.

Answers to this question support the above thesis on the weak savings potential, since one might conclude that:

1) Towards the end of the cycle, it is apparently difficult to save. The loan has probably been used up without having earned enough profit in turn.

2) Members may use part of their initial loan to make savings in the first weeks.

It could also be possible that former savings cannot be easily withdrawn for a potential "re-use" as weekly savings towards the end of a cycle. The reason for this is, as some findings suggest, that the bank account is "blocked", a thesis that will now be explained: members do not have immediate access to their own savings not only because savings must be withdrawn in front of the group. In addition, while money can easily be paid in at the group bank account (as it is done every week by one of the members who brings all the savings of the group to the bank), it cannot be withdrawn with similar ease. One member mentioned that the authorisation for access would be given from FINCA in Kampala. She added that this is one of the problems resulting from the fact that FINCA is too centralised, i.e. authorisation cannot be given quickly by the branch in Masindi.

Even if some observations suggest that there is some truth in it, I could not entirely confirm the thesis on the blocked savings and leave it as an open question for further investigations. Supposing such an institutional blcoking, the initial high savings thus cannot easily be turned into liquid again, so as to make impossible a potential re-use of that surplus money, e.g. for the required weekly savings at the end of the cycle. And, of course, more importantly, the members cannot use their savings for the later weekly repayment of the loan.[18]

## 4.3 Drop-Out Reasons

It was not possible to directly ask former members who, voluntarily or by group decision, withdrew from membership. Two interviewees of group 2, however, knew of eight cases:

1) Misuse of funds:
- One ran away with the money.
- One used the loan for her son's business.
- One was expected to bring the group's collected weekly repayments to the bank, but this delayed for three weeks. Until now, the group has not succeeded in recovering the entire amount from her.

2) Gender issues:
- One woman was forbidden by her business to maintain her business and take FINCA loans.
- As a Muslim, one woman was (principally) forbidden to have her own business. Therefore, her brother took over her loan, but then ran away with it.

3) Illness:
- One had to spend the loan for the treatment of her husband who had had an accident. She then could not repay the loan in time.

4) Voluntary withdrawal:
- One did not accept that she was given a total loan lower than she had expected.

5) Other reason:
- After having shifted her business to another village where she was less well-known, one woman's business deteriorated so that she could not repay the loan.

Misuse of funds and gender problems seem to be the main reasons for dropping out. In addition. illness and the need for costly treatment of relatives for which members are often responsible are problem - not only with regard to dropouts, but also with regard to the attendance of the weekly meetings and repayment.



[18] This questions the observation of Fiebig/Okumu, p. 23, that "clients (...) appear to clearly acknowledge the rapid access to savings (...) available from FINCA".

## 4.4 Registration and Assessment of Members

The assessment of the clients is apparently a shared task of both group and microfinance institution. New members are introduced by existing members and are often relatively well-known to the latter, as the group or at least the two guarantors are responsible if the member fails to repay the loan. On the part of the institution, identification of the members is done by an informal feasibility study lasting two weeks, as a credit officer reported. Then each member would be interviewed individually, and the business would be inspected.

These statements could not be proved by own observations. However, some other findings raise the question whether FINCA is sufficiently informed about its members:

On the day of my arrival in Masindi, I tried to find the teacher with whom I was to be in contact. FINCA offices in Kampala and Masindi had given me her name, profession, the name of the school and the name of the group she belonged to. Despite several attempts. it was neither possible to find the teacher in the school mentioned nor in another school. By coincidence, the lending group I came to join two weeks later was the group that teacher also belonged to. Only then I found out that she was currently unemployed. Thus FINCA was not informed about this recent change.

Interviewing of the supervisor in Kampala brought two probably interconnected findings: FINCA probably faces a problem of “ghost members”, i.e. members showing up on the day of disbursement of the new loan but then disappearing without repayment. As the FINCA members are only registered with their name and a passport photo, not with their address and location, it is impossible to find a certain group member by reference to the books.[19] The informal knowledge of the group members themselves as well as of the credit officer and the FINCA office keeper in Masindi then becomes important.

## 4.5 Members’ Critique on the FINCA Technology

As mentioned earlier, FINCA prescribes a strict time schedule for loan repayment that does not account for the fact that business income is unstable and that some businesses apparently require longer periods of time before sufficient income is generated. This seems to be the case for selling clothes. As some clients mentioned, it is therefore sometimes difficult for them to repay in time.

Thus two women proposed to prolong the period of time between the disbursement of the loan and its repayment: instead of weekly repayments, they want two-weekly or monthly repayments. Even periods of five or six months would be appreciated. The two women are aware of the problems linked to such conditions: The repayment discipline of the group would have to be very high, in the FINCA terminology “grade A”. As they consider a lot of the other women in their group not reliable enough, they propose a group size of five to ten women with regard to this particular lending product.

Another problem mentioned was that new loans are disbursed only after the prescribed 16-week-cycle. It was proposed to shorten the period from 16 to 10 weeks. In addition it was criticised that the initial loan starts at USh 100,000 only and not for example at USh 200,000. Furthermore, interest rates are considered too high.[20]

In sum, some clients prefer higher loans, longer periods of time before repayment as well as complete repayment at once instead of instalments. From the few findings it is difficult to conclude whether FINCA indeed should change its technology, and if so, how. While it is important to meet client demands, the women maybe underestimate the risk arising from such a different loan product. As outlined above, they are not long-term oriented and do not keep books about business development. Accordingly, they will probably not be able to measure risks and take decisions regarding long periods of time. One might suppose that they desire higher loan amounts because they associate them with an equally high profit.



[19] Fiebig/Okumu, p. 20, mention the lack of a “well-functioning personal identification system”.
[20] Also see Fiebig/Okumu, p. 19.

## 5 Conclusions on the Impact of Microfinance

The conclusions to be drawn are few. This is mainly due to the short period of research, as already mentioned in the introduction and in the context of specific findings above.

1) It seems that there is no long-term positive impact in the sense of a constant development in business, agriculture or household spheres. This assumption derives from the observation that clients tend to “muddle through” in their daily life and do not clearly distinguish between income and expenses in the respective spheres. Accordingly, the loan is not exclusively used for either of these spheres, and books are kept neither to control business performance in general nor to control own loan repayment and saving performance in particular. The loan is apparently treated like any other income source.

2) Alternatively, interpreting the same observation more positively, the loan helps to “muddle through”, i.e. is a short-term relief. This explanation is confirmed by Fiebig/Okumu remark, p.18: “Clients seem to see FINCA as a steady and reliable source of short term loans, which do not necessarily lead to the economic growth of clients’ business, but rather provide an instrument for smoothening income and expenditure cash flows over time.”

3) Tthe lending technology makes more muddling-through necessary by imposing a strict time schedule of repayment while weekly repayment is often difficult. The nature of some businesses apparently requires longer periods of time before sufficient income is generated; accordingly, some clients mentioned the problem of repayment in time. As clients then tend to borrow from others to cope with the repayment requirements, (multi-) indebtedness becomes a problem. In general, the strict time schedule increases the number of reciprocal commitments of the individual. In the end it is difficult to decide whether this is a positive or negative impact, considering society as a whole.

4) If it is true, as own observations suggest, that savings are institutionally blocked, then the women cannot freely decide over the use of their savings and face financial problems in case of unforeseen events. As blocked savings are part of the FINCA financial technology, this can be considered a negative impact.

5) However, the FINCA loan is apparently a crucial means to empower women by supporting their independence from their husband, particularly in cases of conflict between husband and wife. This however needs to be critically analysed before a conclusion can be reached, as is shown in the following section.

# 6 Overall Conclusion

In addition to the above conclusions drawn from individual client-on-the-ground observation, it is necessary to aggregate the findings in order to arrive at the extent of poverty alleviation of microfinance in the society as a whole. FINCA clients, having qualified in the first place for FINCA loans, are somewhat better off than the majority in the community and therefore, bear heavier social burdens that are inherent in African extended families. They incur great individual costs of having to “share out” their loans, which they perceive as income sources, between social as well as FINCA obligations. This explains the multi-indebtness observed as well as their apparent inability to grow their loan and savings amounts.

In this situation, clients treasure microfinance not only as smoothening out their funding needs but also as an essential part of a survival kit to “muddle through” their finances. This appreciation was confirmed by the reasons for drop out noted, i.e. misuse of funds, gender problems and illness rather than the programme itself. Clients also understood FINCA’s strict methodology in the need to first grade clients before modifying the standard product. Solutions to poverty alleviation in addition to microfinance are broadening the formal financial sector with the latter as an integral part of it as well as investments in health and education.

In conclusion, microfinance is a significant tool in poverty alleviation. Its challenge is to expand to remote areas with such small loan amounts, work with a large section of the less literate population, which require a significant client supervision while at the same time making most efficient use of financial and human resources. This combination can be achieved with government policy on poverty alleviation long-term targets and the results of its commitment to crucial sectors such as agriculture, education and health.

## 7 Gender Analysis in Microfinance - Recommendations

The scope of this study did not include any gender analysis of microfinance. In future studies, there is need to highlight an essential yet until recently, largely overlooked aspect in microfinance namely the gender issue. The rural microfinance client, and especially the woman is in a unique position and as mentioned in the introduction, it is not possible to provide exact answers about the impact of microfinance especially on women within three weeks. It might be worthwhile to understand why FINCA has decided to lend specifically to women. Questions arise such as, is it to avail money to the poor? Is it to make profits? Is it for sustainability purposes? Alternatively, do all three questions point to the decision to lend to the poor?

Indeed the main argument has been that the women endure livelihood for their families, but there are also other angles. It could be argued that FINCA lends specifically to women either because they usually pay back on a timely basis or because of their situation vis a vis men. Understanding why the women trade in these and not other businesses is essential, as is the reason why the women do not have strategic long term plans. Other issues would need to be looked at, such as the implications of microfinance on marriage or the positive and negative effects of women keeping their businesses and their loans independent of their husbands. The relationship between having a loan and emancipation from the husband also needs to be analysed. Further questions arise with regard to the children or those for whom the women take loans. It would be interesting to understand how the costs and benefits relate to weekly payments taking into account the fact that some of the women have to use the money earned to feed their children. Additionally, it is crucial to understand what the health implications to the children whose mothers do not have time to feed them properly and keep them exposed to adverse weather conditions.

Overall, a more comprehensive analysis can be undertaken to incorporate views from men, community opinion leaders to gain a wholesome understanding, and therefore approach to microfinance.

# 8 References

Beck, Kurt: Die Verbäuerlichung der Bank - Oder: Von den Niltalbauern lernen. In: Manfred Schulz (ed.): Entwicklung: Theorie - Empirie - Strategie. Festschrift für Volker Lühr. p. 81-98.

Financial System Development Project: Microfinance in Uganda - Lessons from FINCA. FSD Series No. 4 Kampala: Bank of Uganda - German Technical Co-operation. Financial System Development (FSD) Project 2000.

GTZ: Angebot zur Bearbeitung des Vorschlags/Projektdurchführung (TZ), Projekt-/Auftragsnr. 96.2250.7. 6.September 1999.

GTZ: Technische Zusammenarbeit mit Uganda. Projektspiegel. Finanzsystementwicklung in Uganda. 1. Februar 2000.

Hannig, Alfred: Finanzsystemreformen. Konzept, Erfahrungen und Perspektiven am Beispiel Boliviens. DIE Band 114. Köln: Weltforum. 1998. p. 50-82.

Ledgerwood, Joanna: Microfinance Handbook. An Institutional and Financial Perspective. Washington D.C.: World Bank. 1999. p. 1-61.

Marpmann, H.-W. et al.: Förderung des Aufbaus privatwirtschaftlich getragener Finanzsystementwicklung. Länderstudie Uganda im Rahmen des Sektorprojekts im Auftrag der GTZ. Juni 1996.

## Group 1

- no. of members: 28
- size of the sample of the member book analysis: 20
- at the time of analysis, the group was in the fifth week of loan repayment

*ad question 1:*

Most members in this cycle have loans between USh 130,000 and USh 200,000; approx. two have USh 550,000. Thus the rough average is USh 192,500.

*ad question 2* (on loan development within 2/3 cycles):

- Decrease: 9
- Increase: 7
- Stagnation: 3

(one case unknown)

*ad question 3* (on weekly savings development within the current cycle):

- Decrease: 7
- Increase: 3
- Stagnation: 10

*ad question 4* (the weekly savings rate in comparison to the required amount)

*no data available*

## Group 2

- no. of members: approx. 25
- size of the sample of the member book analysis: 15
- at the time of analysis, the group was in the first week of group repayment

*ad question 1:*

- one member with USh 150,000
- six with USh 200,000
- one with USh 230,000
- one with USh 240,000
- three with USh 300,000
- three with USh 400,000
- group average: USh 260,000

*ad question 2* (on loan development from the last to the current cycle):

- Decrease: 7
- Increase: 6
- Stagnation: 2

*ad question 3* (on weekly savings development within the last cycle):

- Decrease: 11
- Increase: 0
- Stagnation: 3

(one case unknown)

*ad question 4* (the weekly savings amount in comparison to the required amount):

As group 2 was in the first week of repayment at the time of analysis, only the first week's savings rate could be considered. The individual savings rate required by FINCA is calculated by reference to the loan the member receives. A high loan means a relatively high rate the member has to save weekly a.s.o. The lowest required savings amount was at USh 1,900, the highest at USh 5,300.

- Higher than the required amount: 14
- Lower: 0
- Equal: 7

In detail, out of the 14, the respective savings amounts were higher to the following extent:

- eight between 10 and 20% more
- five at each 40%, 50%, 60%, 70%, 80% more
- two at each 110% and 120% more