

ANNEXES

To the Devfinance quarterly Review

February – March 2003

Publications

➤ [Microcredit Summit E-News \(1 mail\)](#)

From: Anna Awimbo [mailto:awimbo@microcreditsummit.org]
Sent: Donnerstag, 6. März 2003 21:01
Subject: Devfinance: Microcredit Summit E-News, Issue 1 - March, 2003

Introduction

Welcome to the inaugural issue of **Microcredit Summit E-News**, a publication of the Microcredit Summit Campaign. On November 10, 2002, more than 2,000 participants from more than 100 countries gathered at the Microcredit Summit +5 in New York City. Six papers were commissioned for the Microcredit Summit +5 and published by [Kumarian Press](#) in a book titled, ***Pathways Out of Poverty: Innovations in Microfinance for the Poorest Families***. Each paper was discussed in plenary session. This and future issues of the newsletter will include excerpts from each of the Microcredit Summit +5 plenaries and from selected workshop sessions.

We trust you will enjoy this issue. We welcome your comments about our newsletter and your suggestions for how we can better serve you.

Speech Excerpts from the Microcredit Summit +5

HE Vicente Fox, President of Mexico and Chair of the Microcredit Summit +5:

"I am fully convinced that the fight against poverty concerns the world over, and not only a few countries... microcredit may be one of the best tools to overcome poverty in a dignified manner..."

[Click here to read more from President Fox and other speakers at the +5.](#)

Plenary Session: Ensuring Impact

A panel discussion on the paper ***Ensuring Impact: Reaching the Poorest while Building Financially Self-Sufficient Institutions, and Showing Improvement in the Lives of the Poorest Women and Their Families***, authored by Anton Simanowitz, Coordinator of ImpAct and chaired by Susan Whelan, Canadian Minister for International Cooperation. Discussants were Elizabeth Littlefield, CGAP, Lennart Båge, IFAD, Udaia Kumar, SHARE, and Evelyn Grandi, CRECER.

"This excellent paper really could not have come at a more crucial time for us. Donor interest in microfinance appears to be suddenly and curiously waning.... The paper provides very excellent guidance that with the right product, services, attitudes and program design, the very poor can be reached, and impact achieved, sustainably."

Elizabeth Littlefield, CGAP

[Click here to read more from the Ensuring Impact Plenary Session.](#)

➤ [Ongoing reforming of traditional development banks \(1 mail\)](#)

From: Dale W. Adams [mailto:dwadams@burgoyne.com]
Sent: Mittwoch, 19. Februar 2003 19:46
Subject: Devfinance: Silk purses out of pigs' ears

Some good stuff continues to dribble out about reforming traditional development banks. Again, the main potential advantages of reforming these banks are two: quick scale and deposit mobilization.

I much enjoyed reading the following recent article:

Robert Dressen, Jay Dyer and Zan Northrip, "Turning Around State-Owned Banks in Underserved Markets," <<Small Enterprise Development>> Vol. 13, No. 4, December 2002.

Authors report on bank reform efforts in Mongolia and Tanzania. As previously reported on the dfn, the Agricultural Bank of Mongolia was successfully reformed over the past 3 three years and was recently sold to a private concern in Japan. The bank has 350 points of service, made 200 thousand small loans, and has opened over 160 thousand new deposit accounts. I believe that is called scale.

The National Microfinance Bank in Tanzania is likewise being reformed with an eye to privatizing the bank. It has over 100 points of service, is starting to mobilize lots more deposits, and is making many more small loans. It, like the bank in Mongolia, is an important vehicle for processing government payments in rural areas.

What I especially like about the article is that the authors attempt to draw lessons from these two reforms that might be applied in other countries. They suggest four pre-conditions that are necessary to carry out reforms. First, the bank to be reformed must have access to an underserved market with untapped demand sufficient to support a reformed bank (basically rural areas). Second, the government must turn over operations of the bank to the technical assistance team that is reforming the bank. Third, the bank must have access to funds, either through deposit mobilization or deposit of government funds. Fourth, international support for the technical assistance team is also critical. After all, donors helped to created the messes in these development banks and certainly have a moral obligation to help clean up same.

The authors haven't given us a fool proof formula for reforming these banks in all countries, but they have certainly laid out an excellent first draft.

Jane

➤ [News from MicroSave-Africa](#)

From: Willis Osemo [mailto:willis@afcap.or.ke] Sent: Dienstag, 25. März 2003 11:51 Subject: MicroSave-Africa's Current Issues in microfinance - Product Development

New from *MicroSave-Africa*, a bi-monthly thematic e-bulletin featuring current issues in microfinance. In this issue, we look at Product Development and have provided links to various *MicroSave-Africa* resources.

You are welcome to distribute and re-produce any of the materials but kindly acknowledge the source.

Lillian K. Otieno
Knowledge Management Officer

MicroSave-Africa **"Promoting high-quality financial services for poor people"**

Current Issues in Microfinance # 1 **Product Development**

Microfinance is probably the only remaining "product-driven" business in the world. All other industries have long since moved from producing something and then trying to sell it to a "market-driven" approach under which they identify and meet customers' needs on a profitable basis. In the commercial world, companies that have simply marketed a product without reference to the customers' requirements have soon closed. The "market-driven" approach recognises that there is more value in retaining customers than attracting new customers who cost more. In microfinance, the value of retaining clients is particularly clear. Typically, retained customers are the ones with extensive credit history and who are

accessing larger, higher value loans; whereas new customers require induction training and can often weaken the solidarity of groups.

And yet, many MFIs suffer chronic problems with clients leaving their programmes. Careful analysis of the reasons for these "drop outs" almost invariably points to inappropriately designed products that fail to meet the needs of the MFIs' clients. Much of this problem is driven by the attempts to "replicate" models and products from foreign cultures and lands without reference to the economic or socio-cultural environment into which they are being imported.

Market research is an activity designed to understand the environment in which the MFI is operating and to identify the needs of the MFI's clients and potential clients. Market research is usually conducted with a view to responding to those to the needs and opportunities by:

- Improving current marketing/promotion/outreach activities;
- Refining existing products;
- Developing new products;
- Re-engineering delivery systems.

The process of market research and product development can be described as follows. The research objective is usually driven by initial analysis of secondary data and then focuses the market research effort on the specific issues to be examined. This in turn allows the development of a qualitative market research plan typically involving a variety of qualitative research techniques including focus group discussions and Participatory Rapid Appraisal (PRA) sessions. The results of this work then allows the product development team to develop a product concept which is subjected to appropriate costing and pricing analysis to ready it for the process of refining the concept into a prototype. In some cases the product prototype is subjected to quantitative research to provide a final check of the marketability of the prototype before investing in the pilot test. Once the pilot test is completed and the Letter of Recommendation has been completed, the product can be rolled-out and taken to scale.

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Subjects of Interest

➤ Demand for micro finance and debt capacity (5 mails)

From: Development Finance [mailto:devfinance@ag.ohio-state.edu] On Behalf Of John Conroy Sent: Monday, February 03, 2003 6:42 PM Subject: Devfinance: The Demand for Microfinance and Debt Capacity: does Microeconomics 101 help?
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Those of us who took microeconomics 101 at any time in the last half century still tend to think of demand and supply in terms of the classic diagram (remember? price on the vertical axis and quantity on the horizontal axis?) Price in the case of credit is the rate of interest and quantity is the amount lenders are willing to lend (and borrowers are willing to borrow) at each rate of interest (ie, price).

Try sketching the demand/supply diagram on the back of an envelope to assist your recollection. You'll recall that at a high price (high rate of interest) the borrowers are willing to purchase (ie, borrow) a certain quantity, but that as the price (interest rate) falls they are generally prepared to borrow more (or more borrowers come into the market, which amounts to the same thing). So the demand 'curve' tends to slope down from left to right, reflecting the commonsense observation that the demand for most commodities tends to increase as their price falls. While we are fond of saying that access to credit is more important to the poor than the price of credit (the rate of interest) that's not at all the same as saying that the poor are indifferent to the rate of interest. They certainly are not, even if their demand for credit is relatively inelastic (ie, unresponsive or relatively unaffected by price changes) over certain ranges of interest rates (say, over the range between 20 and 30 per cent per annum).

Marguerite Robinson makes use of the idea of a downward-sloping demand curve for credit from village moneylenders in explaining how a form of 'monopolistic competition' exists among moneylenders in those societies where they continue

to thrive. You can check out the argument in chapter 6 of the first volume of her 'The Microfinance Revolution'. The notion that the demand for credit is responsive to price makes nonsense of what JD Von Pischke refers to as 'mechanistic' approaches to estimating demand for credit in some unexplored territory which an MFI is considering for entry or expansion. As JD knows, you can't possibly say how much demand there will be for credit without specifying in advance what price (rate of interest) will be charged for it. Even if we do specify the price in advance, there isn't a set of tables we can read off to see what the level of demand will be in any particular market. It's a matter for empirical investigation in each new territory ('testing the market').

The other side of the market represented in our diagram from Microeconomics 101 is the 'supply side'. The normal assumption about the behaviour of lenders (the suppliers of credit) is that as interest rates rise they will be willing to lend more (or more lenders will appear). So the supply 'curve' for credit is shown as sloping upwards from left to right. In a freely operating market an 'equilibrium' price for credit is established, shown in our diagram as the point of intersection of the demand and supply curves. This is the unique price (interest rate) at which the amount lenders are willing to make available is exactly equal to the amount for which borrowers are willing to contract. If interest rates are held down by government regulation to a level below the equilibrium (or 'market') level, we find that the value of potential borrowings exceeds the amount lenders are willing to offer. The result is that there are 'queues' of borrowers lining up for credit. The problem is solved by credit-rationing, or by allocation of credit on some other criterion than price (say, political affiliation, or influence). Or the level of bribes required to persuade loans officers to approve loans will rise to the point where the real cost of credit approximates that which would prevail in a competitive market. QED.

In his description of how the size of the market for formal microcredit is determined, JD Von Pischke refers to the process in these terms: 'there are different lending technologies, ways of structuring deals, means of creating confidence, and incentives that can engage a clientele. These will involve different term structures, transaction costs and ideas of what the lender is lending against'. Here JD seems to be talking about the supply side of the equation, about how the 'product' is produced and presented. These factors appear to be what in Microeconomics 101 would be described as the 'conditions of supply', the underlying forces which influence the shape and location of the supply curve. He speaks of a 'frontier' between the formal and informal credit markets which moves back and forth as conditions change. Thus: 'the frontier is fluid. Sometimes it moves backward when a formal institution fails. As a consequence fewer people are served and less formal credit is used. Sometimes it moves outward as innovation produces sustainability that serves more and more borrowers'. This description of a moving frontier would seem to the alert student of Micro 101 to resemble the phenomenon of a shift in the supply curve due to a change in the underlying conditions of supply (as distinct from a move along the supply curve, due to a change in the price of credit).

JD then turns to the demand side of the equation: he notes that: 'Each different configuration [of production] will attract certain types of clients who have the debt capacity to deal with any particular lender. (Debt capacity is the amount of debt a borrower can service on a sustainable basis.)' From this account I understood 'debt capacity' to be an element in what in Micro 101 would be called the 'conditions of demand', the set of underlying factors which influence the shape and position of the demand curve for formal credit. I presumed debt capacity would be influenced by factors such as the size and variability of the potential borrower's income and by the set of economic opportunities confronting her in light of having access to credit. Such factors would determine the borrower's decision on whether to borrow and how much, given the availability to her of credit at a particular rate of interest. Of course, as JD points out, 'credit' is not a single undifferentiated product. It will be offered to the client with 'different lending technologies' and 'term structures', etc, but I presumed that the 'debt capacity' is nonetheless something inherent in the borrower, and hence a demand side phenomenon.

However I became confused at the point where JD said that 'The purpose of financial innovation is to increase debt capacity, to bring more people into the formal system because that system should be able to deliver services in a way that goes beyond the capacity of the informal market'. Does this mean that supply side innovations actually increase 'debt capacity', which I had thought was a demand side concept inherent in the circumstances, including preferences, of the potential purchasers? Or is it a case of supply creating its own demand, Say's law (invariably discussed in Micro 101 as a means to encourage students to sort out cause and effect in the neo-classical economic paradigm) at work in microfinance? JD gives the example of an African economy where a particular MFI decided not to set up shop because it 'could not create debt capacity in that environment because its cost structure and lending technology were not appropriate'. So from this it appears that creation of debt capacity is a supply side phenomenon. But in another instance, the success of an MFI in a transitional economy was due to the fact that 'it could offer a service that many prospective borrowers eagerly sought'. This appears to demonstrate, as does the earlier African example, the importance of the underlying conditions of demand, including the debt capacity of potential borrowers, in determining the size of a market.

So is 'debt capacity' a demand side or a supply side phenomenon? Or is Microeconomics 101 not up to the job of explaining it?

John Conroy
The Foundation for Development Cooperation

From: Drew Tulchin [mailto:drew@tulchin.com]
Sent: Wednesday, 5 February 2003 6:55 AM
Subject: Devfinance: The Demand for Microfinance and Debt Capacity: does Microeconomics 101 help?

How about price elasticity and inelasticity from econ 101 to help with this thinking?

Regards
Drew Tulchin
Drew Tulchin Services
617-872-0194

From: John Conroy [jdcon@ozemail.com.au]
Sent: Wednesday 05.02.2003 05:51
Subject: Devfinance: The Demand for Microfinance and Debt Capacity: does Microeconomics 101 help?

Drew Tulchin asks whether the discussion of the demand for microfinance and debt capacity would benefit from consideration of the price elasticities of demand and supply in the market for credit. It would, although it would require a much longer piece to explore the subject. My posting dealt only incidentally with elasticities.

The approach to estimating the quantum of demand for credit which JD Von Pischke correctly describes as 'mechanistic' involves multiplying some assumed number of borrowers by some assumed average level of 'need' for credit, expressed in dollar terms. The price (or range of prices) at which credit might be made available to borrowers is not taken into account. If we were to impute to the people who make such calculations any assumption about the elasticity of demand for credit it should probably be that the demand for credit is completely inelastic (ie, the price elasticity is zero and the demand curve is a vertical straight line).

I did refer to elasticity of demand in considering the common observation that access to credit (ie, the availability of supply) is more important to the poor than its price. I agreed with that observation in general, but added "that's not at all the same as saying that the poor are indifferent to the rate of interest. They certainly are not, even if their demand for credit is relatively inelastic (ie, unresponsive or relatively unaffected by price changes) over certain ranges of interest rates (say, over the range between 20 and 30 per cent per annum)".

I plucked those figures (20 to 30 per cent) out of the air, and I suspect that many MFIs are actually charging interest rates within the range over which their clients' demand is relatively inelastic. Again it would be a matter of empirical observation to discover in any particular field situation how borrowers behave in the face of interest rate changes. I imagine that demand would become quite elastic outside a zone such as I have posited.

I didn't say any more about elasticities because my second objective was to pick up on JD Von Pischke's concept of 'debt capacity'. For this purpose I made the distinction between demand side and supply side factors and asked whether debt capacity is a demand- or a supply-side phenomenon. It doesn't seem to me that the discussion of this issue would be clarified by considering the elasticities.

John Conroy
The Foundation for Development Cooperation

From: Nimal A. Fernando [nfernando@adb.org]
Sent: Wednesday 05.02.2003 08:27
Subject: Devfinance: Demand Curves for Microfinance

Dear DFNers:

I read with interest the posting by John Conroy through which he refreshed our memory of basics in Econ 101. But I have several problems with his demand side discussion (although he admits that credit is not a single undifferentiated product) for a number of reasons. I will just list two of these:

1. Interest rate is just one element of the price of credit. As we know there are other important elements. Borrower transaction cost is one. There is an unfortunate tendency among many to neglect this important element when we talk about microcredit. (This is in a way not surprising. I checked the CGAP's Donor Brief [No. 6] "Making Sense of Microcredit Interest Rates". Not a single direct reference to borrower transaction costs there). I do not know why. May be one guess is that many assume these costs are minimal for the borrowers of MFIs. I have serious doubts about that assumption ! In my view, we must talk about both interest rate and borrower transaction costs or borrowing costs that include both, not just interest rate. The position of the curves that you may draw differ substantially depending on the significance of the transaction cost! s.
2. There are other elements in loan contracts that have a bearing on the actual price. The term structure, repayment schedule etc . Often these are forgotten when we discuss microcredit. As Damian (MicroRate) put it some time ago, it is high time that " we bring finance into microfinance"..

We just cannot meaningfully compare "interest rate of one loan product" with that of another. We need to compare the total package of terms and conditions, together with borrower transaction costs. Otherwise we may be comparing apples with oranges.

Nimal A. Fernando
Asian Development Bank

From: J. D. Von Pischke [jdvp@erols.com]
Sent: Thursday 06.02.2003 05:03
Subject: Devfinance: Re: Looking for MF Demand Info

Dear friends,

A number of issues have been raised about the meaning of debt capacity and how it fits into Neo-Classical models. Mr Dougherty asks three reasonable and important questions:

- 1) How can the frontier's limit be estimated or defined?

I have generally limited myself to the microeconomic dimension of credit and financial sector development, as things can really spin out of control when the macro side gets revved up in the design of credit projects and institutions. I do not think it is helpful to relate micro or other retail credit to macro indicators, other than rather harmless measures such as average loan size relative to GDP. From time to time comparisons are made in the literature or by development organizations that suggest, for example, that ag contributes 60% of GDP but receives only 5% of a nation's formal credit. This is meant to suggest that ag is getting a raw deal in financial markets. Quite convenient, but efforts to find out why this is so might be more helpful, but even that degree of attention would give the measure some credibility and so I resist getting involved in such discussions. What would repayment be like if ag actually got 60% of the credit?

There has always been the temptation to suggest that credit at the small end of the market will lift all ships, change the configuration of the economy, release large numbers of people from poverty, even help combat AIDS. These things may and should happen, but why then is it that CGAP is now saying that funding for microfinance is drying up a little because it is not directly related to the Millennium effort? Donors are shifting their focus, as they do periodically, probably because things are not working out as planned or as touted. Why did ag finance drop off the map around 1990, when in 1980 it was going to transform small scale agriculture, pay school fees, improve nutrition, etc.?

I also have a concern about the concept of demand for credit. This is based on the fact that credit involves open contracts. Performance can be evaluated only when the loan is repaid. This makes the demand for credit (whatever that might be) different from the demand for soap or cement, in which payment and transfer of the goods are largely or nearly simultaneous. Sayre Schatz long ago made the distinction between true demand (good projects backed by credible sponsors with appropriate financing) and false demand (crazy projects, unreliable sponsors, inappropriate financing). I do not know of any other efforts to measure each of these together in any given situation: Schatz did total all credit applications submitted to certain institutions in Nigeria and tried to find how many represented "true" demand. I do know that the false demand is real -- it is the currency of political involvement in credit markets, especially in poor countries, and in some donor agencies on a delicious spring day.

2) How can increases in demand be estimated?

I am not sure that this question can be answered in any definitive way. What I believe can be done is market research. Marguerite Robinson has been involved with this on a large scale, and many microfinance institutions, consulting firms and researchers conduct market studies. These make it possible to decide whether to enter a market, what scale might be feasible, how to design a new service, how to make your customers love you even more, etc. These are quite practical when they are devoted to a specific purpose. I hope that more of them are undertaken so that information problems at the small end of financial markets can be diminished. I see no problem in extrapolation from results from a limited set if the work is done well and if a target is not prescribed in advance in such a way that skews good practice. As the Thorners said, "If progress has to be reported in India, it will be."

3) Is there a gap between the supply and demand for microfinance or any other type of finance at the small end?

I am not sure how this could be measured or even if it is conceivable to do so. Should we even try? It is always argued that there is a big gap. In the past, action based on this assumption led to lots of really bad credit projects, unsustainable institutions, political intervention, etc. I have argued that the problem in certain markets is that there has been too much credit, i.e., some sort of yawning gap between feasibility and wishful thinking. The demise of many donor-supported institutions and projects provides good evidence.

In summary, debt capacity and the frontier of financial markets are concepts. Debt capacity is of course reduced to numbers every time a loan is made. This may be done by anything between a crude process and a highly refined approach. Debt capacity is based on the lender's view of things, which range from the hard headed to the fanciful; the loan applicant's situation, which may range from the tenuous to the rock-solid or dynamic; and how things work generally in an economy. As I indicated in my earlier posting in response to Amy, innovation in finance creates debt capacity, and that's where our attention can most usefully be focused. At the same time, debt capacity is created by improvements in productivity on farms, in households and by firms. Government also is a factor: stability, titling of assets within effective legal or conflict resolution systems (de Soto here), low rates of inflation, etc., can have a huge positive impact.

The frontier may be more difficult to define -- does a bank or NGO really know who its marginal client is?

J.D. Von Pischke

➤ **Part II of a feedback round on WOCCU's new book (4 mails)**

From: Rosenberg@worldbank.org Sent: Friday 31.01.2003 01:16 Subject: Devfinance: WOCCU and its Savings Book

I want to second Jane's recommendation of the new WOCCU book. I thought Lucy Ito's foreword alone was worth the price of the volume. (Well, actually.... they sent me one free. But I would have paid!) I especially admired her candid appraisal of WOCCU's approach up until the '90s. I also was struck by the following sentence:

"Notwithstanding the clear merits of savings mobilization, not all MFIs should engage in savings mobilization[,] for three reasons: (1) it puts people's money at risk, (2) it puts people's money at risk, and (3) it puts people's money at risk."

By way of interesting contrast, I just read a recent speech by Prof. Yunus in which a lengthy discussion of licensing MFIs never mentioned the risk to depositors, especially poor depositors. To be fair, he did mention "a long and hard quality check of the microcredit operation of an NGO." But in a lot of the talk about licensing these days emanating from the "microfinance clique" (in which I proudly include myself), one doesn't detect a tone of especially deep worry over the prospect of losses to savers. That's why I liked the WOCCU book's emphasis on safety, which made good on its rhetoric by offering nuts-and-bolts advice and tools.

The book wasn't perfect. There was a lot of repetition. Some of this is probably hard to avoid when you're getting chapters from different authors, each of whom wants to write a stand-alone piece and feels obliged to report on the experience that s/he is working out of.

My impression is that WOCCU has gotten its formula right in recent years. Results of their engagements are generally strong. Where the results have been weak (the project they ran for USAID in Bolivia was certainly no star), it seems to have been due more to unevenness in strength of the technical advisors than to flawed design or strategy. (When somebody finds a formula to guarantee the performance of all technical advisors, I hope they'll share it with the rest of us.)

One change from years past is that WOCCU staff that I've worked with lately talk about credit unions more as a business and less as a religion. They remain highly committed to credit unions and their clients. But they express that commitment by getting tough on performance standards.

Another change which has in my view been hugely important is that they no longer feel obliged to work through federations in all cases, and have abandoned the effort to lift all boats--i.e., to work with all the credit unions in a country. When they went in to Guatemala's very sick credit union system, their approach was rigorous enough to scare off all but a small minority of the credit unions from substantial involvement in their project, but the ones who chose to take the WOCCU medicine got healthy (a lot healthier than the country's banks, in fact), grew like crazy, and now account for something like 90% of the total volume of credit unions services in the country.

Finally, they have decided that effective TA isn't enough, and that reformed credit unions won't stay healthy unless there is competent external supervision. After their TA success in Guatemala, USAID declared victory and moved on to new battlegrounds. But WOCCU and its partners wanted supervision by the government financial authorities, and chased around to find funding for this crucial second half of the work. When the government refused, they turned to the (hopefully temporary) expedient of creating an independent rating agency, NOT controlled by the credit unions being supervised. WOCCU's decision to put its name and international credibility at risk in this rating agency cannot have been an easy decision, but it was a refreshing example of being willing to put one's money where one's mouth was.

Some years back, Brian Branch (one of the authors) invited me to address a WOCCU meeting to tell staff about WOCCU's reputation among donor specialists. I told them that it was bad. I would certainly have a different message today.

Rich Rosenberg
CGAP

From: Zvi Galor [copgalor@actcom.co.il] Sent: Friday 31.01.2003 06:00 Subject: Devfinance: WOCCU and its Savings Book

Hello,
We have been informed about the emphasize put recently by WOCCU on the importance of saving. I would like to share with the list members some of my thoughts about WOCCU and the SACCOs created in the developing world in light of the approach extended for many years by WOCCU.

**Review of the Role of WOCCU in the MicroCredit Practice.
By Zvi Galor**

It is very important also to examine the role of WOCCU to advance Saving and Credit Cooperatives around the world. We have had at the International Institute more than hundreds of participants, coming from most of the developing

countries around the world and in various languages. We have had the privilege to learn the results of WOCCU work from first hand participants.

Let see what WOCCU is proposing:

- The creation of Saving and credit Cooperatives (SACCOs).
- A member enters to these SACCOs is buying share or shares. These shares have the same value, and they are kept in the coop books in their nominal value. This means that if a member has shares during ten to twenties years, their real value after this period is almost none.

A very efficient way to turn good money into bad money.

These shares, or so-called shares, since they represent nothing of the fixed assets value of the cooperative, are getting, according to WOCCU recommendation, at the end of the financial year of the coop, Dividends!!!

Dividends are: "That part of the earnings of a corporation that is distributed to its shareholders", as it given in one of the dictionaries.

So, to my understanding, those who recommend dividends are turning cooperatives, where rewards goes to recompense participation, into capitalistic enterprises, and I am not against capitalistic enterprises, where people investing their money and get dividends for.

What WOCCU calls Shares are practically LONG TERM DEPOSITS, made by members when entering the cooperative, or during their membership period. Out of these "shares" the cooperative allocating credit to members. Nothing to do with the fixed assets of the cooperative.

WOCCU recommends that members are not the owners of their cooperative.

WOCCU recommended to their SACCOs affiliates a policy through which members will get credit from the cooperative, and will repay this credit by monthly installment with an interest rate of 1% per month on reducing balance, which brings on average to about 12% annually. This policy was proposed to all members no matter in which country they lived. This policy has never taken into consideration the Annual Inflation Rate in the given country. At least, this was never explained in WOCCU publications or training activities to the knowledge of members and leaders of SACCOs, participating during many years, in our training programs. I am afraid this was never explained elsewhere as well.

This policy means that members are getting credit from their SACCOs, are receiving a big present: reimbursing their cooperatives less money, in real terms, than what they have received. Someone is benefiting out of this situation - the members who get credit from their cooperative receiving a big present: returning to their cooperatives less money, in real terms, than what they have received. Someone should pay the bill - the members who save their money in the cooperative.

I can't understand a policy which recommends members to turn good money into bad money.

Now lets see how these WOCCU SACCOs work. The total income of the SACCO which comes mainly out of interest charged on credit allocation to members and out of interest out of depositing members money in banks or in cooperative banks. In both cases, the income of the SACCO in percentages, is much below level of internal inflation in that given country.

Now, WOCCU recommends to its affiliates to do the following financial actions:

First: Out of the total income of the SACCO paying all the operational expenses of the cooperative. There is no incentive to the manager to cut down expenses, since they are paid in any case.

Then: With what is left - money is transferred to:

Reserved fund
Indivisible reserve fund
Future investment in the cooperative
Education

As well as ETC. (I can't explain what it is, but it is part of many cooperatives routine) what left is paid to members as Interest on their long term deposits, which WOCCU wrongly calls dividends on share capital.

Generally, what is left is only a small piece of the money that composed the total income of the SACCO, and what is paid to each member, as percentage is much below rate of internal inflation in the given country.

This is taking good money of members and turning it into bad money.

Some supplementary remarks:

It is unclear why WOCCU recommends SACCOs to create reserve funds. First, when these funds are created, this money is utilized to cover the operation expenses of the cooperative, as is the case in many SACCOs. When the money is not going there, it is kept in the bank and in fixed deposits, where it always gets an inferior rate of interest than the level of inflation. The outcomes are that after years, when this money, might be needed, its real value will be near to zero. A very efficient way to turn good money of members into bad money.

Indivisible reserve funds are recommended to cooperatives by the international ICA cooperative principles.

Why?

The outcome of this principle is that cooperatives creating, during years of activities, more and more financial assets and fixed assets, which are indivisible, and do not belong to members. When a member quit the cooperative he has no right to this property. The cooperative practically doesn't belong to him, and this is the situation in most SACCOs worldwide.

When a SACCO is dissolved, its financial assets, after selling all its fixed assets, paying all debts, and returning to members their shares in their nominal value, would be divided not to members, but will be transferred according to ICA recommendations, and to many countries cooperative legislation, to others, be it other cooperative federations, be it cooperative registrar, be it charity.

Why a member doesn't have the right to inherit to its descendant his property. This is an incomprehensible policy of ICA and WOCCU.

To sum-up: WOCCU is doing very important work in many developing countries, but doing it on a wrong basis.

Best regards

Zvi Galor
www.coopgalor.com

From: Zvi Galor [copgalor@actcom.co.il] Sent: Monday 03.02.2003 08:41 Subject: Devfinance: WOCCU and its Savings Book

>On February 02 2003, <dcr@bwn.net> wrote:

>Brother Zvi:

>... If you are trying to promote your own ideas on how to preserve the real value of our member's money, then by all means, tell us how you would do it. That's what this listserve is all about.

Hello,

I bring below part of a discussion ran in the MicroFinancePractice listserve nearly two years ago:

Some examples how real value of members' money was not preserved. It didn't happen in WOCCU headquarter where pins are distributed to those who know to behave themselves....

Regards

Zvi Galor
www.coopgalor.com

Message Index Msg # From: "Murray Gardiner" >
Date: Wed
Aug 1, 2001 9:27 pm
Subject: RE: [MFP] Return on Savings

I find your argument a compelling case for financial markets deepening. A few years ago I participated in a study of rural finance in Lesotho and found that over a 15 year period livestock (cattle) provided a positive real rate of return to inflation

in excess of 3% while financial savings products available in rural credit unions and banks was negative to inflation by 8%. Were we surprised that there was a scarcity of liquidity in the credit union system to fund loan demand? Well no. Would I advise a person to store wealth in tangible assets? Well yes, under these conditions. Just an observation,
Murray Replies Name/Email Yahoo! ID Date Size 435 Re: Return on Savings W Hiemann Fri 8/3/2001 4 KB 436 Re: Return on Savings
Murray Gardiner Fri 8/3/2001

From: Scott Graham <scgraham@m...>
Date: Tue Jul 31, 2001 5:30 pm
Subject: Return on Savings

I share the view that there is a benefit to savings which can outweigh return considerations, but I don't think we can adopt a "who cares?" attitude about return. I worked with an MFI in Malawi, and saw our savers lose 50% of their value through inflation in two months. I couldn't help wondering whether we had really helped our clients at all. Cash investments are not the ONLY form of storing value: livestock, stock of other sorts, land...such things can at least hold "real" value in an economy where economic policies and trends can wipe out the value of cash savings in a heartbeat. By encouraging clients to MONETIZE their assets through cash savings, we expose them to such risks, and we should not do so without carefully considering the consequences and tradeoffs.

Cheers,

Scott Graham

From: "Dean Mahon" <Dean_Mahon@j...>
Date: Wed Jul 11, 2001 10:28 pm
Subject: Re: [MFP] Credit and Savings

I must salute Zvi Galor for raising issues by way of direct or implied statements which practitioners know to have been proven otherwise.

First, his use of the term "Credit and Savings" very deftly draws our attention to the fact that we are all now aware that savings comes first when dealing with microfinance (since, for example, we have seen on countless occasions that all credit ultimately comes from someone's savings). reminding us of the old juxtaposition of these key terms is indeed a clever way to draw our attention to this microfinance basic.

I must admit that Mr Galor's description of the lending process as credit "allocation" was an almost humorous way of reminding us that credit is not something which can be rationed. Rather - as we have learned - best practices in this area are driven by performance.

The implication that real rates of interest are not used by savings and credit cooperatives, but are used for loans given by producer cooperatives is again a nicely subtle way of reminding us that, historically, multipurpose cooperatives have found financial services to individuals too challenging and, within cooperative structures, members have been best served (for over 150 years) by savings and credit cooperatives focused on individuals and whatever their needs may be.

I was also very pleased to see Mr. Galor's several references to the necessity that credit be linked to production or income generation. This reminds us all of the need to take into account fungibility, as well as the fact that social needs must be met through microfinance institutions. Indeed, I am sure that Mr. Galor is also trying to remind us that within cooperative structures one cannot dictate or restrict the borrowing purposes of a member.

These are but some examples of what I have received as Mr. Galor's underlying message. I, for one, have found this message to be refreshingly enlightening and a well-timed reminder of a number of our basic lessons learned. However, if I might, I would like to suggest to Mr. Galor that in the future he consider not being so subtle, as there is the possibility that others may not have properly gotten the point.

Dean Mahon
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>>> Galor <Galor@p...> 07/10 11:52 PM >>>

Hello,

I have just read, in a very interesting paper written by G.A.N.

Wright, about MFIs in East Africa, where it mentions the fact that 25%-60% of members of these projects are Drop Outs. It is very interesting to note that many of those who have reported on this list about their respective projects have not hesitated to mention that the rate of return of MF credit in their respective projects is around 100%. I am sure that such figures are the dream of every one, but my question is to what extent they are representing the reality. To my understanding, many of the MFIs projects in various part of the world those which are presenting wonderful results, but to which comes my question: to what extent this is the reality. My belief is that only giving credit to poor people is not enough. Credit allocation, which should be given in a rate of interest reflecting the level of the country rate of inflation, should be bound to the ability to save money, at a rate of interest above rate of inflation in that country. (Most of SACCOs' are out of this practice, to my knowledge) This can be realized in cooperatives belonging to producers. Credit allocation should be linked, in one way or another, to income generating projects. That say means that the beneficiary should acquire the necessary skills and know-how of how to produce before getting the credit. Credit allocation means that producers should be able to be supplied of the necessary inputs at the lowest possible costs. It may be done by cooperatives belonging to the producers. Credit allocation means that the beneficiary should have an appropriate network to market his produce at highest possible return. This will enable him to reimburse credit allocation. This can be done by a cooperative belonging to the producers. Credit allocation should take into account, not only the beneficiary financial needs for the process of production, especially farming production, but also his needs to feed his family during the period of production, until the point where he can sell the produce, and with the income reimburse all his financial obligations. Without these pre-conditions, I doubt to the degree of sustainable success of credit allocation.

Thanks and regards

Zvi GALOR

Academic Director

The International Institute - Histadrut, Israel

Galor@p...

www.peoples.org.il

From: Dave Richardson [dcr@bwn.net] Sent: Tuesday 04.02.2003 09:05 Subject: Devfinance: WOCCU and its Savings Book
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Mr. Galor:

This has become quite an African safari. You have unleashed NINE postings upon us all and each one is a wild elephant that is charging in a different direction. You'd better be careful or you might make us all wonder WHAT it is that you preach.

The following paragraph, taken from a WOCCU resolution in 1984 that you cite below should clearly show how incorrect your statements are.

Distribution to Members

To encourage thrift through savings and thus to provide loans and other services, a fair rate of interest is paid on savings and deposits within the capability of the SACCO. The surplus arising out of the operations of the SACCO, after ensuring appropriate reserve levels and after payment of limited dividends on permanent ownership capital where it exists, belong to and benefits all members with no member or group of members benefiting to the detriment of others. This surplus may be distributed among members in proportion to their transactions with the SACCO as interest or patronage refunds, or directed to improved or additional services required by the members.

In summary:

1. WOCCU preaches that SACCOS should charge a "fair rate of interest" to encourage thrift, not the 1% per month that you allege.
2. WOCCU preaches that "appropriate reserve levels should be created". (this is ironically to protect members money from losing its value!)
3. WOCCU preaches that "limited dividends" should be paid to members. This hardly seems that we are turning them into capitalistic enterprises as you allege.
4. WOCCU preaches that any surplus should be used to "improved or additional services required by the members". This is the voice of the people (the owners) who you say have no ownership or voice in the management of the Credit Union.

Let me add a couple of other WOCCU guidelines since you have raised them in your earlier expose...

5. WOCCU preaches that fixed assets should be financed with the capital reserves of the credit union and should not exceed 5% of the total assets of the credit union. (that means that 80% are in loans and 15% in liquid reserves!). Those reserves are not buried in a safebox six feet under the ground nor should they sit in the bank earning 1% as you allege. Member shares don't finance fixed assets either, because if someone withdraws from the credit union, we redeem their shares at par value in CASH, not bricks and mortar!
6. WOCCU preaches that operational expenses of a credit union should not exceed 10% of the total average assets. If you study the Microbanking Bulletin, you will find that credit unions have one of the best operating expense ratios in the microfinance industry. We are not as inefficient as you allege.

Finally, you seem to confuse the actions of WOCCU with actions of individual SACCOS. Just because Harambe SACCO is affiliated to KUSCCO and KUSCCO is affiliated to WOCCU, you assume that Harambe is following all of the guidelines of WOCCU. That is a preposterous assumption. It is like saying that because many Catholics use birth control, the Catholic Church must preach that birth control is o.k.

I hope that this brief post will answer your questions, inasmuch as you have spurned my offer to come to Madison to straighten out your story and at the same time, receive your very own credit union lapel pin!

It's time to move on to other elephants outside of Africa.

Dave Richardson
World Council of Credit Unions
dcr@bwn.net

-----Original Message-----

From: Development Finance [mailto:devfinance@ag.ohio-state.edu] On Behalf Of Zvi Galor
Sent: Monday, February 03, 2003 3:30 AM
To: Development Finance
Subject: Devfinance: Re: WOCCU and its Savings Book

From: "Zvi Galor" <copgalor@actcom.co.il>
Date: Mon, 03 Feb 2003 12:00:03 +0200

On February 01 2003, Dave Richardson <dcr@bwn.net> wrote:

To the elephants killer,

On February 01 2003, Dave Richardson <dcr@bwn.net> wrote:

4. "WOCCU recommends to its affiliates to do the following financial actions: First: Out of the total income of the SACCO paying all the operational expenses of the cooperative. There is no incentive to the manager to cut down expenses, since they are paid in any case. Then: With what is left - money is transferred to:

Reserved fund
Indivisible reserve fund
Future investment in the cooperative
Education”

I bring a citation from a WOCCU affiliate:

<http://www.saccol.org.za/saccos.htm>

And there, there exists a recommendation which goes like this:

Distribution to Members

..... The surplus arising out of the operations of the SACCO, after ensuring appropriate reserve levels and after payment of limited dividends on permanent ownership capital where it exists, belong to and benefits all members with no member or group of members benefiting to the detriment of others. This surplus may be distributed among members in proportion to their transactions with the SACCO as interest or patronage refunds, or directed to improved or additional services required by the members.

Regards

Zvi Galor
www.coopgalor.com