ENUGU FORUM POLICY PAPER 7

DEBATING POLICY OPTIONS FOR NATIONAL DEVELOPMENT

POLICY CHALLENGES FOR MICROFINANCE DESIGN AND PRACTICE IN NIGERIA

aiae AFRICAN INSTITUTE FOR APPLIED ECONOMICS

Table of Contents

About Enugu Forum

INTRODUCTION

Opening new spaces for domestic policy dialogue is one of the most important potential gains of democratic governance. Democratic space creates public policy arena in which government can be engaged by private sector and civil society on what it is doing or not doing, and hence be pressured to perform. Since the return to democratic rule in 1999, there has been an upsurge of private sector and civil society engagement with governments on economic policy and development issues. But, the upsurge of civic advocacy on economic and development issues has not been matched with commensurate improvements in the quality of debates on policy alternatives and roadmaps for national development.

Enugu Forum is intended to provide a civic arena for proposing and debating policy alternatives and roadmaps towards social, economic and political progress of the country. It is hoped that the forum will foster interaction between government and non-state actors towards good governance, accountability and participatory democracy.

IDENTITY AND MISSION

Enugu Forum is a civic platform devoted to intellectual conversation and of policy issues affecting the growth and development of the country. It was founded in 2001 to promote informed and credible avenues of stakeholder dialogue and policy advocacy. It seeks to improve the policy process through high quality debate and non-partisan discourse of alternative solutions to contemporary development questions.

The Forum deploys both intellectual and empirical insight to nurture a shared understanding and objective scrutiny of policy issues on social, economic and political development of the country.

ACTIVITIES

Enugu Forum's activities take several forms:

- Public Lectures
- Seminars
- Workshops
- Conferences
- Roundtables

The activities bring together diverse stakeholders including government officials, private sector operators, independent think-pots and civil society to exchange and constructively critique perspectives and experiences on critical policy imperatives.

OUTPUTS

The outputs of the Forum's activities take the form of communiqué outlining key outcomes of discussions, conclusions and recommendations. The presentations and proceedings are further developed into Occasional Papers, Working Papers or Policy Briefs widely circulated to inform, sensitise and enlighten stakeholders.

STRUCTURE AND ORGANISATION

Enugu Forum is structured into a Steering Committee, a Coordinating Committee and the General Members. The Steering Committee governs the Forum through guides and policies agreed in consultation with the General Members. The Coordinating Committee executes the activities and programmes.

MEMBERSHIP

There are two classes of membership: individual and corporate. The Forum's activities are open and can be attended by all interested persons but formal invitations are issued to only members and designated guests. To be a member, one needs to register in the appropriate category. Registration can be done during the Forum's events, or at the Host Organization—African Institute for Applied Economics, Enugu.

SPONSORSHIP

Ownership of the Forum resides in the members. It is run on the goodwill contributions from corporate bodies and individuals. Sponsorship includes provision of venue, refreshments, logistics, and facilitation of guest speakers.

HOST INSTITUTION

The Enugu Forum is hosted by the African Institute for Applied Economics (AIAE) Enugu. AIAE is a non-governmental, not-for-profit and independent organization devoted to economic policy research for the purpose of promoting evidence-based decision making. It is located at 128 Park Avenue, GRA, Enugu, Phone: (042) 256644, 256035, 300096; Fax: (042) 256035. e-mail: aiaeinfo@aiae-nigeria.org, aiae@infoweb.com.ng; website: http://www.aiae-nigeria.org

Enugu Forum Policy Papers

Enugu Forum Policy Paper Series publishes the proceedings and outcomes of workshops, conferences, seminars or public lectures held by the Enugu Forum. The Series provides documentation of the topical presentations, debate, comments and perhaps consensus at the Forum.

It is intended to disseminate the Forum's intellectual discourse to a wider audience. The essence is to stimulate broader policy debate and promote multi-perspective dialogue on policy options.

Enugu Forum Policy Papers constitute an advocacy instrument to canvass alternative development solutions and policy roadmaps, for the overall purpose of enriching the policy discourse in the country. The Series also draws attention of government, private sector and civil society to salient dimensions of contemporary development challenges in Nigeria.

Foreword

The ongoing economic reforms in Nigeria—the National Economic empowerment and Development Strategy (NEEDS) and the State Economic Empowerment and Development Strategy (SEEDS) emphasise microfinance as an important ingredient of the economic empowerment, enterprise development and employment creation. Microfinance is also critical to the attainment of the Millennium Development Goals, particularly regarding poverty reduction, gender equality and sustainable livelihoods for vulnerable groups. In recognition of these objectives, the Nigerian government, international development partners, and NGOs in Nigeria are promoting the design, supply and administration of microfinance in Nigeria. For instance, the Central Bank of Nigeria is drafting a microfinance policy for Nigeria; and the USAID, under the reforms programme (to be managed by Development Alternative incorporated), has microfinance as a segment of the Policy Reforms component.

The purpose of this special Enugu Forum was to scrutinize existing microfinance systems, examine their inherent challenges and generate critical inputs that will form the key policy agenda for the Microfinance component of the REFORMS programme and other Microfinance policies in the country.

The process of generating these valuable inputs for microfinance policy in Nigeria was through a policy dialogue involving development practitioners, professionals, academic, policy makers, development/donor agencies, and the interested public. It consisted of seminar paper presentations in plenary by a microfinance banker, and a microfinance researcher; breakout sessions for in-depth discussions of the papers presented and experiences shared; and a second plenary session to discuss reports from workgroups and harmonise positions.

Prof. Eric Eboh
Executive Director
African Institute for Applied Economics
Enugu

FIRST PLENARY SESSION

PAPER 1: Challenges of Microfinance Supply and Administration

Engr. (Sir) Chris Okoye

Introduction

What is Microfinance?

Microfinance is described as "banking for the poor." Microfinance programmes provide loans, savings and other financial services to low-income and poor people for use in small businesses. People living in poverty, like everyone else, need a diverse range of financial instruments to run their businesses, build assets, stabilize consumption and shield themselves against risks. A poor person can use his or her "micro-loan" to start a small business (such as selling chicken eggs or repairing bicycles) and work his or her way out of poverty.

Originally based on traditional forms of community financing (a cross between finance and development assistance) microfinance is found all over the world in places such as Africa, Latin America and Asia. The microfinance movement began in earnest in the early 1980's in places like Bangladesh and Bolivia and has, over the last 20 years, captured the interest of multilateral donor agencies and private sector bankers.

In Nigeria, most commercial banks are very reluctant to get involved in microfinance. The widespread perception is that microfinance is the responsibility of the public sector. Experience elsewhere indicates that serving the poor through microfinance can be a profitable business.

To underscore the importance of microcredit as an instrument of economic development and poverty reduction, the United Nation's General Assembly designated 2005 "International Year of Microcredit." This has given a new global and national impetus to microfinance programmes. The United Nations, governments, regional organizations and non-governmental organizations are coming up with a plethora of microcredit programmes to address problems of economic development and poverty alleviation.

The Role of Microfinance in Poverty Reduction

Most economies categorized as Least Developed Countries (LDCs) suffer from a "Vicious Circle of Poverty"

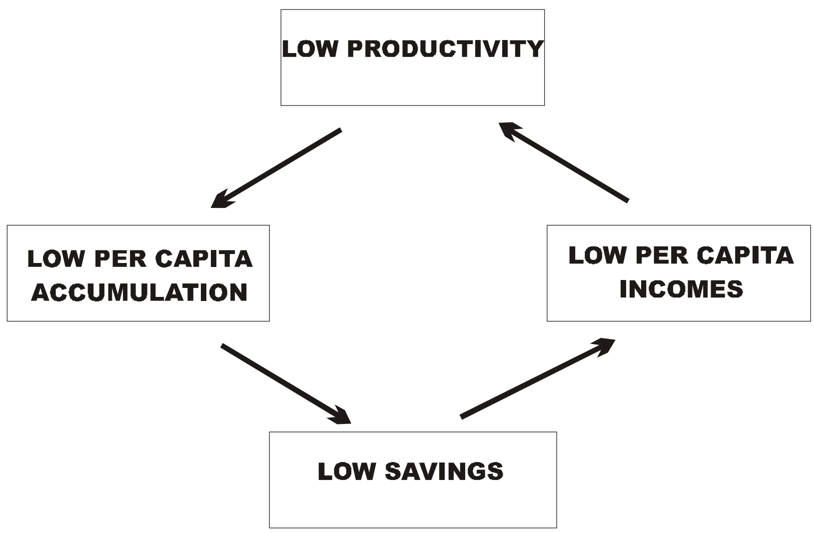


Fig. 1.1 Vicious Circle of Poverty

The poverty circle in LDCs is vicious because savings are generally low and therefore it is difficult to accumulate capital for investment purposes. Lack of investment leads in turn to low productivity. This in its turn leads to low per capita income. Low per capita income obviously leads to low savings and the cycle repeats itself.

A 1990 World Bank Development Report indicates that microfinance can assist immensely in poverty alleviation through promotion of the productive use of the greatest asset accessible to the poor—their labour. This can be achieved through wage employment, raising agricultural productivity among low and marginal farmers as well as increasing opportunities for self-employment in diverse areas.

The report further states that for all these to be realized, there has to be an improvement in social services (e.g. family health care, family planning, nutrition and education).

It is in the light of the foregoing that microfinance in the Least Developing Countries (LDCs) has been seen as an intervention strategy that helps the poor expand their economic activities, and increase their incomes and assets. It also helps to improve their health and nutrition as well as build an enabling environment for the growth of political participation and democracy.

Our survey of countries where microfinance programmes have recorded enormous success indicates that they have been applied in the following areas:

- Housing and investments in agricultural inputs such as rice, seeds, fertilizers and agricultural tools
- Dairy products, cow raising, cattle fattening, poultry farming, weaving, basket making, leasing farm and other capital machinery and woodworking.
- Collective enterprises such as irrigation pumps, building sanitary latrines, power looms leasing land for cooperative farming.
- Crop and animal trading, cloth trading and pottery manufacture.
- Transportation
- Repair workshops

Benefits and Drawbacks of Microfinance

Benefits

Research has shown that the application of microfinance has the following benefits:

1. **Reduction of Vulnerability**: One of the most important benefits of microcredit programmes is their ability to reduce vulnerability among the poor. Microcredit programmes help borrowers to insure themselves against crises by building up assets. Such assets can be sold if necessary. They can also be used as security or proof of credit worthiness when dealing with businessmen or more traditional lending agencies. Finally, the diversification of assets can reduce the risk of catastrophic loss. A family that relies on sharecropping could easily be bankrupted by a single crop loss, whereas a family with a diversified base of crops and livestock or handicraft income could survive until the next harvest.
2. **Increased Consumption**: Another benefit of microcredit programmes is the increase in household consumption. Even small increases in consumption and increased regularity in consumption can lead to better health and nutrition, and enhance the ability to make long-range plans for the family.
3. **Reduced Income Poverty**: Microcredit programmes also reduce income poverty. This means that borrowers actually tend to make more money over time. Once the cycle of poverty has been arrested and some stability provided, many borrowers go on to make profitable investments and even lift themselves out of poverty all together.
4. **Microclusters**: The main selling point for clustering is the collective efficiency it produces. Microcredit-funded business ventures are frequently plagued by the problems of size and isolation. With microcredit clusters however, these problems are partly overcome. Traders are attracted by the possibility of making bulk sales. The close proximity of a number of businesses in the same line of work also allows for labour sharing, order sharing and subcontracting within a cluster. Other major advantages include the ease of sharing information and technological innovations within clusters.

Drawbacks

On the other side of the coin, there are a variety of problems and shortcomings associated with microcredit.

1. **Turning a Profit on the Loan**: One of the most fundamental problems associated with microcredit programmes is the difficulty involved in actually turning a profit on the loans. In the first place, borrowers must bear not just the cost of the loan and interest payments, they also need to invest a significant part of their time in the group activities mandated by their programmes.

   Investments do not always yield profits. In this event, the money to repay the loans must come from reduced consumption or borrowing from other sources usually on worse terms. The loans obtained may not be used for the purposes intended and the obligation to repay fully can never be wished away.
2. **Inability to reach the extremely poor:** Where the institutional framework for microfinance administration and supply is weak and dispersed, microcredit programmes do not reach the poorest members of the society. The poorest have a number of constraints, which prevent them from investing the loan in high return activity.

   There appears to be a growing consensus that moderately poor microcredit borrowers benefit more than extremely poor borrowers. The poorest need tiny loans that are not cost-effective even for microcredit programmes. The poorest also place the greatest demands on microcredit training programmes. This makes the cost of lending even higher. As microcredit programmes are pressured to become more self-sufficient, the incentive to lend to such desperately poor borrowers evaporates.
3. **Microcredit Dependency**: Some researchers have proposed the idea that high repayment rates, repeated borrowing and low dropout rates indicate a dependency on microcredit programmes rather than an attraction to successful microcredit programmes on the part of poor borrowers. Many borrowers have no alternative to

borrowing from microcredit programmes and consequently cannot afford to default. They have nowhere else to go.

4. **Durability of Poverty Reduction**: A related problem is the durability of poverty reduction. Infusions of capital in almost any amount are bound to have some effect on poverty-stricken borrowers. This does not mean that the effect will be permanent. The poverty reduction may be rolled back in two ways. Borrowers may use loans for consumption purposes, which result in a momentary increase in living standards, but which must be paid for by cuts in future consumption. Secondly, borrowers must make a net profit on their investments. Otherwise, as noted above, they may become dependent on the creditor programmes.

   Other factors that may reduce durability of poverty reduction include crises and poor macroeconomic policies. When there is a natural disaster or crises most loan beneficiaries tend to see the loan as a "grant". In such circumstances, the facility is misapplied.

Lessons from Other Countries

In this segment, we shall attempt to look at how some countries supply and administer their microfinance schemes. The essence is to learn a few lessons from their practice.

a) Bangladesh

The microfinance industry in Bangladesh has been able to provide microcredit to about 13 million poor households. There are around 1,200 microfinance institutions in Bangladesh. However, only four of them predominated—Grameen Bank, Bangladesh Rural Advancement Committee (BRAC), Association for Social Advancement (ASA) and Proskika. These cover about 90% of all clients.

Over the last three decades, access to microfinance in Bangladesh has been growing in several distinct phases. It all began in the 1970's with action research conducted by academics and practitioners in organizations that were created to deal with the relief and rehabilitation needs of post-independence Bangladesh. The new government was unable to cope with the scale of destitution thus providing the foundation for the emergence of non-governmental organizations (NGO's) experimenting with different modalities of delivering credit to the poor. In the 1980's, the number of NGO's involved in microfinance grew by leaps and bounds. The predominant model has become one of providing individual loans to a target group of households rather than providing loans for group projects. The last decade has witnessed a sharp increase in microcredit.

The growth has come from specialized microfinance NGO's and Grameen Bank. What began with a few small grants and loans from international donors has now provided over 100 million dollars in loans.

The most distinctive feature of the credit delivery system is the absence of middlemen between the credit supplier and the end user. The bank's cumulative recovery rate is an astounding 98%. Grameen Bank has its own special legal structure and does not fall under the regulatory oversight of the central bank. The bank also aims to raise health and environmental consciousness. Each of its members must plant at least one sapling a year as part of a reforestation programme. Grameen is perhaps the only bank in the world that encourages birth control, sanitation and a clean environment as a part of its lending policy.

b) Bolivia

In Bolivia, a non-bank special charter was introduced recently to encourage the formalization of MFIs and non-bank financial intermediates, and to place them under the supervision of the Superintendency of Banks.

Under the new charter, MFIs are allowed to operate with lower minimum capital requirements than commercial banks and to mobilize deposits, with the exception of checking. In recent years, several MFIs have been able to formalize their operations improving their outreach and cost-effectiveness with the technical and financial support from international networks and donors. These include Caja Los Andes and Centro de Fomento a Iniciativas Economicas (FIE), two MFIs recently incorporated as non-bank financial intermediaries, and BancoSol which was allowed to incorporate as a commercial bank.

c) Benin

In Benin, prudential regulations on MFIs are less comprehensive and stringent than for commercial banks. Current prudential regulations for deposit taking MFIs include six ratios relating to liquidity and stability of resources, risk concentration, and limits on activities other than saving and credit. MFIs are not subject to capital adequacy requirements, but liquidity requirements and the coverage of medium and long-term liabilities are broadly similar to those that apply for commercial banks. On the other hand, limits on concentration risks on a single member are substantially less stringent than for commercial banks. At the institutional level, the supervision and monitoring of MFIs is conducted by the Microfinance Unit (MFU) of the Ministry of Economy and Finance, with cooperation from the regional central bank. Besides monitoring the annual financial tables received from the microfinance institutions, the MFU conducts an increasing number of on-site inspection visits each year, although the resources to conduct sound supervision of MFIs are insufficient.

d) Ghana

In Ghana, the rural microfinance sector (RMF) has evolved into a three-tiered structure—formal, semi-formal, and informal—with a strong savings orientation and a much greater role of licensed institutions, relative to nongovernmental organizations (NGOs), than in many countries. Banking institutions—in particular the Rural and Community Banks (RCBs)—and formal Savings and Loans Companies account for most microfinance activities. The regulatory approach has been gradually adapted to the diverse structure of the RMF sector in Ghana. Currently, the regulatory framework provides a strong licensing system for the formal sector, formal registration for the semi-formal sector, and a relative laissez-faire stance for informal institutions. Given the high costs of supervising a large number of Rural and Microfinance practitioners (RMFs) and the limited supervision capacity of the Bank of Ghana, the authorities have decided to rely on regulatory requirements to offset their supervisory limitations. This includes high reserve requirement for Rural Community Banks (RCBs), minimum capital requirements for S & Ls, and relying on self-regulation of semi-formal deposit-taker MFIs through an apex body.

Lessons Learned from Bangladesh

Five lessons from Bangladesh could be relevant to microfinance growth and impact in other countries:

1. First, is the importance of the "enabling environment" for microfinance, especially maintaining a stable macro-environment in which interest rates and inflation are kept at reasonable levels. Government regulations and policies are needed to create an appropriate environment for the growth of the sector, where regulatory policies strike a balance among protecting the interests of depositors, supervising microfinance institutions that collect savings, and not excessively regulating the sector with unnecessary red tape.

   While this long relationship has not been free from tensions on both sides, the Government of Bangladesh has thus far been able to place the interests of the poor foremost in its mind while dealing with NGO issues.
2. Second lesson is that microcredit may be a more effective remedy against poverty and vulnerability if it is complemented by other interventions. These interventions may be especially important for the poorest households,

which face the greatest risk of income fluctuations and have the greatest need for a range of financial and non-financial services.

3. Third, there is a role for donor financial assistance in expanding the capital base of emerging microfinance institutions, as well as developing the technical capacity necessary for organizational sustainability. Northern NGO's, such as the Ford Foundation, Oxfam and the Aga Khan Foundation, played an important role at the initial stages of the NGO-MFI industry in Bangladesh. The subsequent expansion and consolidation stages were funded largely by official bilateral and later by multilateral agencies, as Northern NGO's could not match the growing resource requirements of the larger MFIs. Hence, subsidies can be justified to support microfinance institutions in their early stages, as long as there is a viable route to institutional sustainability.
4. A fourth lesson is that, while visionary leadership cannot simply be "franchised", the systems and formal rules that govern the successful microfinance industry in Bangladesh can to an extent be replicated. These may vary according to the size of the organization, but by and large, the successful organizations delegated significant decision-making authority away from head offices, monitored individual staff performance, and linked staff incentives to programme targets. Client feedback and programme monitoring are also crucial. As organization grows, the willingness to change products based on client need and demand and to create products tailored to niche markets is crucial for success.
5. Fifth, one of the lessons unique to the Bangladesh experience was the critical role played by a microfinance wholesaler that channels funds for microfinance to MFIs and was critical in the expansion and improved professionalism of the microcredit industry in Bangladesh. There is a growing degree of experience with setting up apex institutions worldwide, such as the Pakistan Poverty Alleviation Fund (PPAF) in Pakistan, Rural Microfinance Development Centre (RMDC) in Nepal, Fondo de Capital Social (FONCAP) in Argentina, LID in Bosnia-Herzegovina. One of the fundamental factors behind the success or failure of an apex is the underlying retail capacity in a particular country. However, apex bodies are not a panacea, and a rigorous analysis of the underlying retention capacity and demand for funds must be carried out before they are established.

Other Lessons

In Bolivia, Benin and Ghana, governments are following a practical approach, adopting flexible rules for licensing, regulating, and supervising MFIs to reflect their reliance on deposit-taking and potential system impact. In addition, regulatory frameworks of MFIs are sometimes adapted to promote microfinance activities, seeking to balance the benefits of an increased supervision with the associated costs.

The next segment examines various institutions responsible for microfinance supply and administration in Nigeria. It also makes some critical observations on their roles.

Current State of Microfinance Supply and Administration in Nigeria

The present global emphasis on microfinance institutions stems from a recognition of their potentials in poverty alleviation, development of small businesses and economic growth.

Many countries in the developing world have developed various patterns of microfinance supply and administration. Some have been outstandingly successful in this process whereas structures and systems set up in other countries seem to wobble and do not achieve intended results.

This segment therefore intends to look at various policies, institutions and structures set up for the purpose of microfinance supply and administration in Nigeria. We shall attempt to address the following issues in this segment:

1. What are the various institutions and policies for microcredit administration in Nigeria?
2. To what extent have they been able to perform their primary role of microfinance supply and administration?
3. What are the factors militating against their effective performance? Are these constraints located in the institutions themselves or in the wider operating environment?

4. What lessons can we draw from the policies and practices of other countries with well-established microfinance schemes?

It is in light of the aforementioned issues that we shall examine some microfinance institutions in Nigeria.

Bank of Industry (BOI)

The Nigerian Industrial Development Bank was restructured into the Bank of Industry (BOI) in 2000 and it formally took off in 2001. It has an authorized share capital of ₦10.0 Billion. The nature of the funding of the microfinance sector by BOI has been in the form of loans, debentures and equity.

With interest rates ranging from 10 to 20 percent per annum, BOI loans repayment periods range from three to seven years with one-year moratorium.

However, its loan disbursement from inception in 2001 shows an undeniable discrimination against small businesses. For instance, out of a total of ₦1.72 billion given out as loans from 2001–31 March, 2004, only about ₦0.46 billion went to smaller enterprises while an astonishing ₦1.26 billion went to big enterprises. This goes to show a great level of unwillingness on the part of microfinance administrators to finance small businesses, which for the most part touches on the poverty level in the country. This also brings to question the sincerity of both institutions and administrators on the quest to eradicate poverty and foster development of small businesses.

Small and Medium Industries Equity Investment Scheme (SMIEIS)

The setting up of this fund arose from the decision of the banking industry in Nigeria to set aside 10 percent of their pre-tax profit for equity investment in small and medium industries. To further enhance their effectiveness in financing SMEs, the Bankers' agreed that 10 percent of the funds accruing to the scheme should be channelled to microenterprises through registered microfinance institutions. At the end of June 2004 over ₦24 billion had been set aside under the scheme while less then ₦10 billion had been invested.

However, 2001 World Bank survey on Nigeria showed that although 85 percent of firms had relationships with the SMIEIs, not all of them had access to credit. This makes it abundantly clear that SMIEIS cannot satisfy the financial needs of SMEs, which may also not be unconnected with its bias for short-term projects. This further reveals evidence of selective disbursement of loans in the SMIEIS. Besides, many of the SMEs that have benefited from its programmes are for the greater part in the urban areas. It does not seem to give rural dwellers much consideration in loan disbursement.

Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB)

The Nigerian Agricultural Cooperative and Rural development Bank Limited (NACRDB) is an amalgam of the former Peoples Bank of Nigeria, Nigerian Agricultural and Cooperative Bank (NACB) and the Family Economic Advancement Programme (FEAP). It was set up in 2000 primarily to finance agriculture as well as small and medium enterprises. The NACRDB is structured to accept deposits and offer loans or advances in which the interest rates are stratified according to the purpose of the loan. The bank offers a number of services that include targets saving, start up as well as smallholder loan schemes. The authorized share capital was initially ₦1 billion, but now reviewed upwards to ₦50 billion. The sources of NACRDB's funding are mainly equity as well as interest on loans and investments.

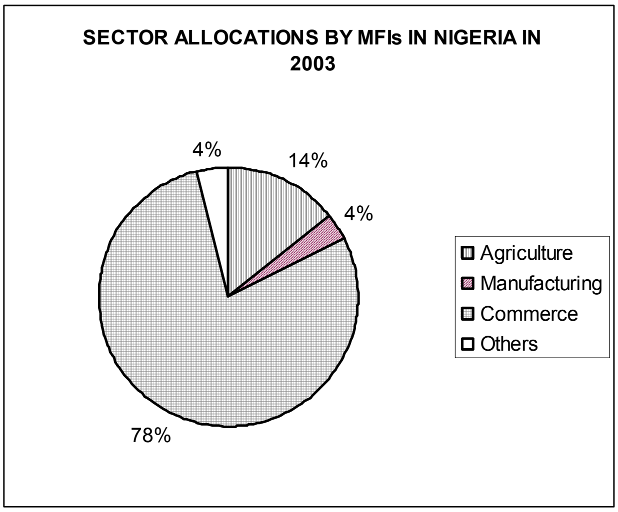
The financial assistance extended by the NACRDB can be classified into direct microcredit, on lending credit and macro credit. Form the inception of the bank in July 2001 to December 2003, the total sum of ₦4.6 billion had been invested in loans and venture capital.

The Informal Sector

The unwillingness and inability of formal financial institutions to provide financial services to the urban and rural poor, coupled with the unsustainability of government-sponsored development programme, led to the emergence of traditional groups that work together for the mutual benefits of their members. These groups provide savings and credit services to their members. They operate under different names such as "esusu" among the Yorubas of Western Nigeria, "etoto" for the Igbos in the East and "adoshi" in the North for Hausas.

These associations operate traditional microfinance in various forms in rural communities and urban centres.

Having examined some key institutions responsible for microfinance supply and administration in Nigeria, it is important that we bring to the fore certain salient observations on their activities. The issues highlighted shall then form the basis of our recommendations in the last segment.



Observations on Microfinance Supply and Administration in Nigeria

1. Inability of MFIs to get to the poor. A 2001 CBN survey indicated that MFI client base was about 600,000 in 2001 and there are indications that they may not have been above 1.5 million in 2003. This is far too small for a country that has over 60 million people that require microfinance services. The government and its institutions should work in concert to promote this sector as a means of mobilizing domestic savings, widening financial system, promoting enterprises, creating employment and income and reducing poverty.
2. The attitude of commercial banks as regards microcredit is unfavourable to MFIs. According to a 2003 CBN survey, commercial banks fund to MFIs accounted for a meagre 1.9 per cent of total funding. This is grossly inadequate. Commercial banks are wary of using short-term funds in financing long-term projects of these SMES, which most of the time are not re-serviced by the beneficiaries. This contrasts sharply with the experience of Bangladesh where banks are actively involved in microfinance programmes.

Fig. 1.2 Sources of MFI funding in Nigeria (2003)

3. The potential beneficiaries of these funds are largely unorganized. As a result, it becomes difficult for banks to entrust them with the needed funds for fear of not recovering their loans.
4. The institutional framework for administering microfinance, despite their phenomenal growth in the last decade, is still very weak and ineffective. This has two adverse implications: they are unable to attract sufficient level of funding from donors and international agencies; the scope of their activities is narrowed so that they cannot fund activities in the real sector. According to a 2003 CBN survey, only about 14.1 and 3.5 per cent of total MFI

funding went into agriculture and manufacturing respectively while the bulk of 78.4 per cent funded commerce. (See Fig 1.3)

5. The issue of sustainability is crucial to the continued operations of the MFIs. Although the indicators have not been computed, there are indications that the level of financial self-sufficiency is low. The level of grants as a source of funding is very high, while the contribution of loans from Commercial Banks is low. Capacity for deposit mobilization is still very weak.
6. The Nigerian environment is not enabling. For instance, most rural and urban communities have bad roads, very poor power and water supplies systems, weak primary health care delivery system, and low literacy rate. As a result, it is difficult for individuals to sustain the growth of small businesses in such environment.
7. Microfinancing is still largely perceived as public sector-led activity. For instance, government initiates and implements activities of these MFIs. These are evident in public sector projects like the National Poverty Eradication Programme (NAPEP), whose funds go to alleviate poverty levels by providing vehicles (Keke-NAPEP); and the National Directorate of Employment (NDE), which equips people with skills thereby encouraging entrepreneurial development. Experience of other countries such as Indonesia and Bangladesh show that the private sector can profitably participate in microfinancing.
8. The general level of awareness of the activities of MFIs is abysmally low. This has gross negative implications for the number of people that benefit from their activities.
9. Most poor rural dwellers lack collateral for various loans schemes from microfinance institutions. It is difficult for them to use their lands for this purpose because the lands are not properly registered with the government.

Recommendations

In the light of the observations made in the preceding segments, we make the following recommendations:

1. There is the need to establish more community and mortgage banks, as vehicles for making microfinance more accessible to the poor. The Central Bank's supervision of these institutions should emphasize accountability and transparency, establishing appropriate structures and modes of operation, as well as capacity building.
2. Commercial Banks in the post-consolidation era should begin to play the role of wholesalers of microfinance in Nigeria. They should mobilize funds for this purpose from diverse sources which they in turn lend to MFIs for on-lending to end users. This approach has been successful in Bangladesh, Indonesia and China.
3. Enterprise Development Agencies should be established in each of the six geopolitical zones. The state governments within each zone should be responsible for the creation of this body.

   This agency should be responsible for guiding and advising microfinance institutions in Nigeria as well as the management and disbursement of the Apex Microfinance Development Fund. The agency shall also monitor and evaluate the deployment and application of these funds to ensure that they comply with laid-down parameters for management of the fund

   It should be an independent agency free from political manipulation. Consequently, the procedure for appointing its members must be thorough. We recommend that a Committee of Community and Mortgage Banks operating in Nigeria should make the initial nominations. Appointments are then made by governors to be ratified by the state assemblies. There should also be a public hearing prior to the ratification.
4. Enterprise Training Institutes should be established at local levels. The institute should serve as consultants to potential beneficiaries of various microfinance schemes. The institute should teach them how to organize their businesses, basic accounting and budgeting, computer application, among others. The institute should also monitor and evaluate the activities of loan beneficiaries at the local levels. The state government in the local communities where these Enterprise Training Institutes are to be located should be responsible for setting up the institutes.

5. Town Unions and Traditional Councils should be institutionalized and mobilized for microfinance administration and economic development in Nigeria. Anyone familiar with Nigerian's political history can easily recall the critical role town unions played in the 1940's, 1950's and 1960's particularly in the southeast geographical zone of Nigeria. In some parts of Nigeria, they are still important in the development programmes undertaken by various communities. It is therefore necessary that we mobilize the platform provided by these bodies in the process of microfinance administration in Nigeria.

   Town Unions and Traditional Councils could be made to assist in identifying potential beneficiaries, guaranteeing their loans and monitoring their activities. Most state governments usually have a ministry or parastatal that oversees town unions and traditional council matters. Such ministries and parastatals could regulate activities of traditional councils and town unions in the process of microfinance administration.
6. The Church is one institution that has remained very stable and reliable over the years. The platform it provides could be mobilized for microfinance administration in Nigeria. Church members tend to know each other intimately and therefore can give reliable information on the character of one another. The church can therefore be used to identify potential beneficiaries of microfinance programmes, in addition to guarantee loans to them.
7. The literacy level in rural communities is still very low. Adult education scheme should be setup by town unions, and assisted by the churches. The relevant ministry or parastatal responsible for adult education matters should play a regulatory role. These schemes should cover reading and writing arithmetic, basic hygiene and sanitation, civics and moral instruction.
8. An apex Microfinance Development Fund should be created. Companies operating in Nigeria should pay 0.5 per cent of their profits before tax into this fund. This fund is to be shared on a zonal basis and managed by the zonal Enterprise Development Agency. Microfinance institutions operating in the zone can then draw long-term loans from this fund for on-lending to end users.
9. An enabling environment for small businesses to thrive should be created. This entails a number of issues:
   a. Our political system needs to be restructured to give other tiers of government (state and local governments) more power and resources so as to discharge their responsibilities more effectively.
   b. We should provide the right macroeconomic framework that would enable small businesses to thrive. For instance, interest rates should be low and predictable.
   c. Basic social infrastructure should be provided. Prominent among this is steady power supply. We can begin to develop renewable sources of energy such as solar system to augment what we already have. Other social infrastructure includes good road network and adequate water supply. Primary Health Centres should be established in the rural areas.
10. NGOs and Civil Organizations should be actively involved in microfinance administration in Nigeria. They could assist in training and monitoring potential beneficiaries of microfinance loans. They could also play a vital role in corruption reduction activities.
11. The state governments in collaboration with the local governments and traditional institutions should work out a programme of voluntary registration of lands belonging to poor rural dwellers so as to ensure that these lands can be used as collaterals when they need loans from microfinance institutions.

Conclusion

I have attempted to provide background information on microfinance in this paper. Our examination of microfinance and administration in Nigeria reveal pertinent factors militating against the effectiveness of institutions established for this purpose. Prominent among these factors are the inability of microfinance to get to the poor, disinterestedness of commercial banks and the fact that potential beneficiaries are largely unorganized. Others include lack of an enabling environment for small businesses to thrive and the erroneous impression that microfinance is a public sector responsibility. We have made appropriate recommendations to address these issues.

We have also looked at critical factors responsible for the success recorded by microfinance schemes in other countries highlighting the lessons we can learn from their experiences. We have no reasons to believe that the success recorded by microfinance in other countries cannot be replicated in Nigeria if we address the lapses in our microfinance policies and practices squarely.

Microfinance Supply and Administration: Schedule of Recommendations, Implementation and Regulatory Bodies

S/No	Recommendation	Implementation body	Regulatory Body
1.	Establishment of more Community and Mortgage Banks.	Central Bank	Central Bank
2.	Commercial Banks should play the role of whole-sellers of microfinance.	Various Commercial Banks, international organizations and donors.	Central Bank
3.	Establishment of Zonal Enterprise Development Agency.	All the State Governments in the six geopolitical Zones of Nigeria	Central Regulatory Body
4.	Establishment of Enterprise Training Institute.	State Governments	State Regulatory Body
5.	Town Unions and Traditional Councils should be actively involved in microfinance administration.	State Government	State Regulatory Body i.e. Relevant ministry.
6.	The platform provided by the Church should be mobilized for microfinance administration.	Church Administration	
7.	Adult Education schemes should be setup by Town unions and churches.	Town Unions and Churches	State Regulatory Body i.e Relevant ministry
8.	An apex Microfinance Development Fund should be created.	The Presidency (Federal Ministry of Finance, National Assembly, and State Assemblies)	Central Regulatory Body
9.	An enabling environment for small businesses to thrive should be created.	National and State Assembly, and the Nigerian People	
10.	NGOs and Civil Organisations should be involved in microfinance administration.	Central Regulatory Agency for NGOs	Central Agency.
11.	Registration of lands to enable the rural poor use them as collaterals for loans.	Local Government	State Regulatory Body i.e Relevant ministry

References

1. Baumann, T. *Pro-Poor Finance for Sustainable Livelihoods*
2. Carpenter, C. *SME Financing in Nigeria*. A paper presented for the Round Table on "Making Small Business finance Profitable in Nigeria".
3. Centre for Financial Assistance to African Countries. "Inter linking the formal and informal Financial Sectors in Developing countries." *Savings and Development Quarterly Review* No. 1, Milan (1990).
4. Federal Ministry of Industry. *Report of the 13th Meeting of the National Council of Industry (NCI-13)*. Makurdi, 2001.
5. Ilapenu, C. and Zeller, M. "Distribution, Growth and Performance of Microfinance Institutions in Africa, Asia and Latin America." *FCND discussion Paper* No. 114.
6. Inang, E. E., Ukpong, G. E. *A Review of Small Scale Enterprises delivery Strategies in Nigeria*. CBN Occasional Paper 1993.
7. Kasimu, S.Y. "Banking on Micro-Enterpreneurs: Innovative lending and Credit Programme." *NIDB Newsletter* October, 1997.
8. Mabogunje, AL. (1997): "Alleviating Poverty through Microcredit." Paper delivered at the Microcredit symposium organized by Obafemi Awolowo Foundation; Lagos, Nigeria.
9. Meade, J. *An Examination of the Microcredit Movement*, 2001.
10. Osa-Afiana, L. "Funding Industrial Growth: Strategic Options for funding of Enterprises in Nigeria." Paper presented at the Nnewi Economic Summit, 1st April, 2004.
11. Rudjito, P. "Strategies for Developing Micro, small and Medium Enterprises." Paper presented at the Non-aligned Movement's Business forum on South-South co-operation, Indonesia.
12. Ruomei, S. *The Development of Microfinance in China*, Chinese Academy of Social Sciences.
13. Vincent, G. *Sustainable Microentrepreneaurship: The Roles of Microfinance Entrepreneuarship and Sustainability in Reducing Poverty in Developing Countries*.

PAPER 2: Policy Needs in the Microfinance Sector: The Missing Angle

By
Dr. Kalu O. Oji

Conceptual Issues

What is Microfinance?

Microfinance is the provision of very small loans that are repayable within short periods of time. Their clients are basically low-income individuals and households with minimal assets that can be used as collateral. Conceptually, microfinance also includes financial products and services targeted at the poor (Mirero, 2004). This target is the differentiating factor that distinguishes microfinance from other financial services. At present microfinance includes such services as microcredit provision, microsavings and other deposit instruments, micro-insurance, microleasing, money transfer, and payments services.

Microfinance adopts the “credit-plus” approach. Its focus is not only on the provision of credit to the poor. It includes the additional feature of integrating credit with other developmental activities such as community organizing and development, leadership training, skills and entrepreneurship development, financial management, social mobilization, health education, etc.

What is Microcredit?

Microcredit is credit targeted at the poor and is designed to enable them have access to production capital (Rogally, 1999). It does not include other financial services such as those encompassed by microfinance.

The difference between microcredit and microfinance can be likened to the difference between “credit” and “credit plus”.

Why Microfinance?

The need for microfinance stems from the fact that the poor lack access to conventional financial institutions. This is so for obvious reasons, namely:

a) Demand Side

1. A lack of conventional collateral to secure loans. In most cases their labour is their only asset.
2. Their failure to meet minimum terms and conditions required for opening and operating different bank accounts.
3. Physical and/or economic inaccessibility of banks relative to the rural poor due to their location in distant urban centres.
4. Inappropriate services provision, documentation and tools for micro-enterprise operators.

b) Supply Side

1. The cost of serving the poor scattered over several settlements and rural areas is high.
2. Administering small loans has a high unit cost.

3. High risk covariance among the enterprises of the poor—only a small proportion of them thrive. This is due to the fact that they are usually primary sector activities subject to high risks such as the dependence of agriculture on weather conditions.

It also should be kept in mind that the real targets of microfinance are the enterprising poor who need finance for several reasons, notably:

1. Evidence from studies of traditional savings and credit institutions (e.g. Clubs, Moneylenders, etc.) show that the poor can borrow and repay, are good credit risks, and can pay interest rates often above market clearing rates.
2. The poor don't just need credit. If their enterprise is to succeed they need credit plus. The complementary services that enable their business plans to thrive should form an integral part of the financial services offered.
3. The poor need to be helped to grow. By increasing cycles of borrowing, spending and repayment they can be helped to move out of poverty. However dependence on these financial services should be avoided.

Who Provides Microfinance?

These services are usually provided by Microfinance Institutions (MFIs). Microfinance institutions are generally regarded as institutions whose major business is the provision of microfinance services. Three types are recognized namely:

a) **Formal MFIs:** These are the commercial, community, and development Banks. They are usually fully regulated by the Central bank.
b) **Semi-formal MFIs:** These include microfinance Non Governmental Organisations. They are not-for-profit legal entities that are limited by guarantees. They are usually registered with, but not under, the regulation of the Central Bank.
c) **Informal MFIs:** Under this broad group we can find Traditional Credit & Saving Clubs, *Esusu*, *Ajao*, etc). They are mainly traditional self-help groups (SHGs) or associations.

Conventional Policy in Finance Industry

The prevailing policy world-wide is usually regulatory, deriving largely from the pervasive market failures in the system such as asymmetric information, moral hazards, and covariate risk, and infrastructural inadequacies (especially in developing countries). As a result, the Central Bank undertakes the following kinds of regulation—deposit insurance, bank capitalisation recapitalisation and reserve requirements, chartering, and regular bank examinations/ supervision—in order to safeguard the trust and confidence of depositors, which is the greatest asset in the banking system.

An important issue to address is the question of the satisfactoriness of this type of microfinancial policy to actual microfinancial needs. Microfinance encloses peculiarities that renders conventional financial policy insufficient.

Peculiarities of Microfinance: Why microfinance is different.

Microfinance is different from ordinary financial activities and may not need conventional regulatory financial policy for the following reasons:

1. Microfinance is not simply provision of credit. It is *credit plus*. Regulation of additional services like skills enhancement and social mobilisation is relatively difficult to concretise.
2. Microfinance is a development tool to uplift the poor. To work in tandem with this end, policy has to take the same shape.
3. The primary targets of microfinance are the poor who are usually excluded from conventional services and regulation. This regulation should be cultivated by growth and development and not imposed.

4. A less imposing policy structure is to be encouraged as enterprises set up by the poor are usually informal (i.e. not registered).
5. Institutions that assist the poor usually are not profit-oriented (e.g. Microfinance NGOs). Rigid regulation may induce profit-mindedness so as to meet up with standards which may have adverse effects.
6. Due to the situation of the majority of clients, microfinance usually has the characteristic of non-collateral lending.

Nigeria as a whole presents certain features: the MFI clients are mostly women. The effective interest rate lies somewhere between 30 and 40 percent and the loans offered tend to be small, in the region of ₦2,000-10,000. They are often offered for a short duration, usually between 3 and 12 months with a weekly repayment schedule. Usually there is no moratorium and, as we have remarked earlier, no security. Considered from the client side there is a noticeable tendency for them to engage in trading activities.

The following consequences can be drawn from these features:

1. Excessive regulatory requirements may increase MFI costs which are passed on to poor borrowers thus defeating the objectives of microfinancing.
2. There is need to adopt a development orientation in drafting microfinance policy. The focus should be on determining what policies will help the micro-enterprises to grow, raising the living standards of the poor.
3. Policy should put greater emphasis on encouraging the growth of the capabilities and capacity of MFIs and their clients.

The key features of a policy that is tailored to the specific circumstances of microfinance in a Nigerian context will be sensitive to the needs of the primary stakeholders and their objectives. The MFIs, their clients and donors all aim at growth and development. The Central bank also wishes to regulate these activities.

We will attempt to sketch out these features based on the evidence acquired from a specific case study.

Evidence from a Case Study: UNESCO Study of Micro-Institutions and their Clients in Nigeria

The study was entitled "Impact of Policies on the Technological Capabilities of Clients of Microfinance Institutions in Nigeria" and its context takes into account the poverty of MFIs and their clients.

The clients of MFIs are usually small-scale operators functioning in the informal sector. They tend to be poor and are engaged in a variety of artisan workmanship, petty-trading, food-processing, agriculture, etc.

Usually they are characterised by the use of simple tools and technology. Their operations tend to flexible, one-man businesses with a corresponding small capital base and few employees who generally are household members. The operator normally possesses a low educational level, acquiring and accumulating skills mostly by the traditional apprenticeship system. All these characteristics indicate that they are businesses that yield a limited volume of output. Understandably their major objectives don't go beyond the securing of subsistence and saving of any surpluses for future needs.

Three key consequences from above are:

1. The prospect of expanding production and investment from owner-generated resources is almost secondary/ limited.
2. However, these enterprises can respond to incentives and opportunities to improve their capital base and technology.
3. The major means of injecting capital and technology into micro-enterprises is through microcredit.

The following conclusions are possible:

1. Micro-enterprises represent a source of subsistence, employment, and income for their owner.
2. Poverty is a major problem among micro-operators.
3. Poverty and the limited income imply that they lack capital to expand their operations.
4. Thus the provision of microfinance services represents a major strategy for poverty alleviation among the enterprising poor.

Research Problem

The research problems can be narrowed down to two scenes:

Scene 1: Poverty

Poverty is a major problem in developing countries including Nigeria. Nigeria's case is relatively serious. By 2001, about 70% of the Nigerians were living in poverty. In addition to this, according to a UNDP report, Nigeria ranks among the 25 poorest countries in the world while its poverty has proven to be deep and widespread. A majority of these poor individuals are engaged in small-scale enterprises in the informal sector and agriculture.

Scene 2: Small Scale Enterprises

Small-scale enterprises form an important sector in Nigeria. As a result, financial support for them has become a major component of the strategy for poverty alleviation. Several microfinance schemes provide loans to enable potential entrepreneurs start small-scale enterprises. These schemes only provide subsistence living for the proprietor or beneficiary with no possibility of providing jobs for others in the community.

To provide jobs for others as well as improve the living conditions of the operators, microfinance schemes should be able to upgrade the activities of the operators technologically. It is a fact that technology plays a vital role in the transformation of the activities of micro-operators. In spite of this, there are currently no documented studies to guide the injection of technology through microfinanced schemes. As a result a number of research questions were formulated:

1. What factors determine the technological capability of small-scale firms?
2. What strategy aids small-scale firms in enhancing their technological accumulation?
3. Which feature of the microfinance institutions enhances the accumulation of technological capability amongst small-scale operators?
4. Which macro-level and sectoral policies enhance the technological capability of microfinanced activities?

These key questions constitute the problem set for this study.

Research Objectives

Overall: To determine the impact of policies on the technological capability of clients of microfinance institutions.

Aim: To isolate the best practices and policies for the technological upgrading of microfinanced micro-firms.

Specific objectives:

1. Examine the enterprise characteristics of microfinance borrowers related to technological accumulation.
2. Assess the technological capability of small-scale firms.
3. Identify the determinants of the technological capability of micro-borrowers.
4. Assess the impact of firm's own policies on its accumulation of technological capability.
5. Determine the effect of the policies of microfinance institutions on the accumulation of technological capability by small-scale operator-clients.

6. Determine the effect of macro-level and sectoral policies on the technological capability of microfinanced firms.

Findings

a) Firms Technological capacity

1. There is low leasing capability among the firms, but design, manufacturing, and investment capabilities lie in the medium range. Their low capabilities for investment may be due to their low capital base and lack of knowledge about business management and skills.
2. In the last five years, the value of output per firm grew by an average of 15% per annum while the estimated profitability grew by an average of 22% per annum. These positive growth rates of both output and profitability suggest considerable production and profit capabilities among the surveyed firms.
3. On average the firms have attained high levels on innovation capability in their growth in output and competitiveness, and medium capabilities in hardware increases and technology adoption and adaptation. There is low reverse engineering capability among the firms.
4. Almost half of the respondents have introduced new products and penetrated new markets, while about two-thirds (62%) of them have learned new skills and techniques as well. This clearly suggests that training and skills development could be a more acceptable method of developing the innovative capability of the respondent firms. It is possible that most of the new skills were acquired in the process of interaction with their microfinance institution

b) **Determinants of micro-borrowers' technological capability**

1. The regression results showed that the technological capability of the micro-borrowers is positively and significantly explained by the number of employees or workers, the duration of client's loan, the age of major machinery/equipment of the enterprise, and the degrees of appropriateness of the machinery/equipment to workers' skills and available infrastructure.
2. The negatively significant determinants of technological capability are the amount of the operator's experience and the interest rate on the loan received from the MFI.

Table 1: Regression Estimates (Based on OLS) of the Determinants of the Technological Capability of Micro-Borrowers in Nigeria

Explanatory Variables	Coefficients	Std. Error	t	Sig.
Age of Owner	-.005	.005	-1.045	.298
Number of Employees/ Workers	.017	.008	2.040	.043
Length Experience in Business in Years	-.015	.006	-2.471	.015
Loan Amount (₦)	-2.839E-07	.000	-.825	.411
Loan Duration in months	.121	.033	3.645	.000
Loan Interest Rate (%)	-.023	.007	-3.375	.001
Years of Schooling	.007	.006	1.168	.245
Scale of production per Annum (₦)	-1.441E-08	.000	-1.101	.273
Age of machinery (years)	.038	.012	3.266	.001
Appropriateness of Equipment/ Machinery to production needs	-.019	.052	-.355	.723
Appropriateness of Equipment/ Machinery Workers Skill level	.377	.054	6.981	.000
Appropriateness of Equipment/ Machinery to Available Infrastructure	.126	.040	3.161	.002
Current value of firm's investment in Machinery/ Equip(N)	6.479E-08	.000	1.327	.187
(Constant)	1.069	.359	2.975	.003

Statistics: F-ratio=14.070; R-square=0.59; R-Square (adj)=0.54; S.E= 0.5812

c) **Good practices and Policies Identified**:

1. Duration of clients' loan: use of longer term loan.
2. Appropriateness & access: Use of equipment loan and equipment leasing.
3. Reduced rate of interest on clients' loans.
4. Training as an essential component of the packages MFIs offer to their clients.
5. Assisting clients to prepare business plans.

d) **Good Practices in the Policy Environment** (Macro & Sectoral)

1. Small and Medium Enterprises Development Agency of Nigeria (SMEDAN): SME Development & Promotion.
2. Strategy and Technology (S & T) Policy.
3. Poverty Reduction Policy: Poverty Reduction Strategy Papers (PRSP), the National Economic Empowerment and Development Scheme (NEEDS).
4. Small and Medium Enterprises Equity Investments Scheme (SMEEIS) in relation to the banking industry
5. Credit Guarantee for Small and Medium Enterprises

e) **Equity Investment Policy**: The Small and Medium Enterprises Equity Investment Scheme (SMEEIS)

1. 10% of Banks' profit after tax (PAT) for equity investments in small and medium enterprises.
2. Real sector and services.
3. Beneficiaries reduce their interest and other financial charges.
4. Receive financial advisory, technical, and managerial support from the banking industry.

Conclusion

1. Microfinance has development as its fundamental aim. A good microfinance policy should therefore aim at enabling the poor to increasingly move out of poverty through cycles of loans and repayment.
2. Minimal regulation should be exercised. Policy should focus instead on increasing the capabilities and capacities of MFIs and their clients—the SMEs.
3. Policy should incorporate good practices and policies based on Regional (Africa-wide) studies (examples can be obtained from the UNESCO Website).

PAPER 3: Situational Status of Microfinance Institutions

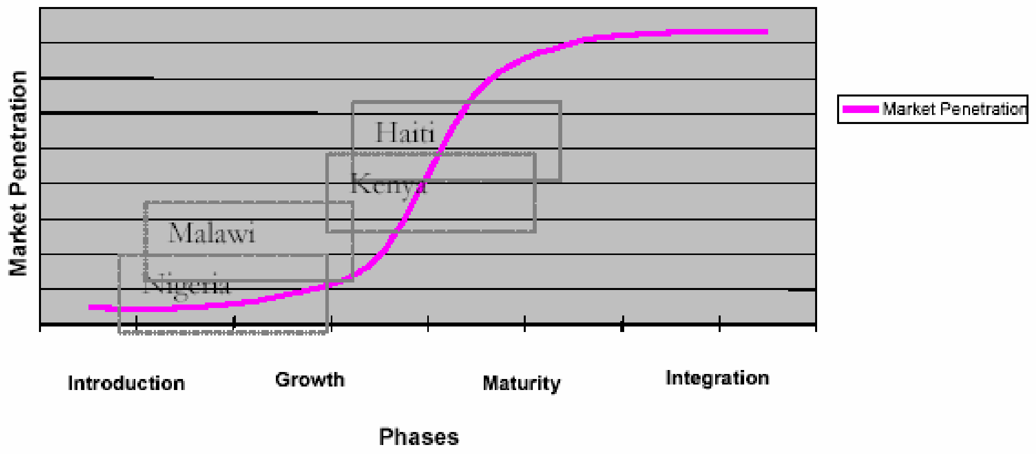
By
Dr. C. U. Okoye

Introduction

A microfinance institution (MFI) is a semi-formal, non-governmental and community development organization involved in rural development (Marx, 2001). In recent decades, microfinance, of which microcredit is a component, is a sub-set of flexible structures and systems by which a wide range of financial and enterprise development services are offered to micro enterprise owners in an affordable and convenient manner. It has become one of the buzzwords of contemporary development initiatives all over the world. This is particularly contextual to the developing countries, where top-down formal financial institutions have failed to address the credit needs of the real sector of the economy, thereby constraining the processes of investing for livelihood enhancement among the poor, the small-scale farmers and micro-level entrepreneurs.

Today a huge but underdeveloped market in Nigeria for poverty lending exists. As the depth of poverty in Nigeria continues to increase, it becomes imperative to ponder ways to strengthen, among other things, available institutions to fight it. Nigeria's MFI sector, in comparison to those of countries like Kenya, Malawi and Haiti, has not even started growing (see figure 1), suggesting that a lot of work still needs to be done, and that the industry may still be flexible enough to be nurtured upright with relative ease.

Figure 1: Microfinance Sector Development



Source: United Nations (2004) 'Microfinance Programme Impact Assessment 2003, UNCDF– MAIN REPORT. P 14. United Nations Capital Development Fund' Enterprising Solutions Global Consulting, LLC

Since the successes of the Grameen Bank of Bangladesh and several others, thinking about the composition of national financial systems has continued to shift towards the inclusion of non-bank financial institutions. At the centre of this change is the abandonment of the long-standing separation of microfinance programs from financial sector development and including it within a 'project' context for social welfare and poverty alleviation services.

The above trend reflects in the Federal Governments current reform effort in the financial sector of the economy. It has become expedient to denominate development efforts in Nigeria on the provisions of the National Economic

Empowerment and Development Strategy (NEEDS), the State Economic Empowerment and Development Strategy (SEEDS), and the nascent Local Economic Empowerment and Development Strategy (LEEDS). Naturally, they all derive policy directions from the Millennium Development Goals (MDGs). A look at the MDGs shows that goal number one is the lynchpin of the seven goals, and that has to do with the enhancement of peoples' income levels, for which microfinance initiatives have been adjudged fundamental. In fact, access to a reasonable income, affordable credit and associated services will go a long way in achieving the MDGs. There are abundant accounts of the potency of microcredit in pushing people away from extreme poverty. It is therefore a welcome idea to build and strengthen the MFI sub-sector. In doing that, three fundamental and basic objectives of microfinance must be kept in view. They are the strengthening of the self-help capacity of the poor and complementing the existing networks of mutual obligations; helping the poor accumulate savings in local MFIs—which form the basis for self-financing, enterprise development and household risk management; and weaning poor people from external subsidies and interference.

A crucial area of focus for assessing these issues is on the establishment of efficient financial systems, institutions and practices of which the importance of MFIs as catalyst for growth cannot be over-emphasised. Not least amongst these are the links between it and the real grass roots economy where the majority of the population is active.

In this paper, we focus on the macro-policy imperatives of building institutions meant to provide microfinancial services to the poor.

Institutions: The Software of Development Intervention

No development initiative can operate within an institutional vacuum. The market mechanism, on which reforms rely so much, operates not in a vacuum but on institutional "wheels," the appropriateness and health status of which could make or mar those reforms. The term "institutions" has been defined in different ways. Broadly they may be defined as organizations (see van Rennin and Waisfisz, 1988), or as a set of rules, compliance procedures, and moral and ethical behaviour norms (North, 1981). They are the formal and informal rules governing human interactions, the norms, processes and systems embedded in community, town, state and federal establishments. We may also speak of the degree to which laws and regulations are fairly applied, the regulatory frameworks, procedural devices for doing things, etc. Nevertheless, institutions also include agencies, organisations set up and working according to agreed principles to achieve set goals.

Strong institutional assumptions are often implicit in the design of programs and projects (Arkadie, 1989). To Nellis (1980) therefore, it is not surprising that early efforts to create a general theory of development administration failed. Institutional choice should be presented not as a dichotomy of state or market, but as a pluralism of possible contractual relationships, both explicit and implicit (Ostrum, Fenny, and Pitch, 1988). We must bear this in mind as we discuss the building of MFIs to serve the poor. It is important for policy makers to realise that MFIs, being grassroots embedded, often encapsulate the whole range of local social, economic, political and cultural norms and sensitivities and also transmit same in their operations. While formal upstream financial institutions can operate in a value-neutral manner, the same may not be said about community-based or even regional MFIs that target the poor.

In spite of the fact that for a long time microcredit institutions and MFIs in Nigeria have been crucial institutions for the distribution of incentives and resources for investment particularly in rural areas and among the urban poor, most Nigerians still do not have reasonable access to financial resources for investment. Inadequate access to financial institutions that would enable the poor to save in good times and borrow in bad, leaves them more vulnerable to economic downturns (World Bank, 2002). Building effective financial intermediaries and other market institutions should therefore be the central challenge for all levels of organisation in Nigeria: communities, state governments, local government councils, city councils, etc. Some of the pertinent questions we should be asking include: How were the efficient and effective systems among the many existing more or less traditional financial institutions built? What should these institutions be doing to remain sustainable in this modern era and in the context of on-going reforms? What can be done to develop new modern MFIs? In that regard, what the Central Bank of Nigeria (CBN) has started doing to mainstream microfinance is a significant move towards altering the financial architecture of Nigeria and will go a long way to eliminate distorting and discriminatory financial policies and practices, change institutions, adding new ones, and generally establishing the basis for greater efficiency in both mobilisation and the allocation of scarce financial resources in the economy.

Microfinance and Microcredit Institutions in Nigeria: A Profile

Types of Microfinance Institutions

The Nigerian microfinance industry has come a long way and boasts of all the four well-known models in the industry. A CBN study identified, as at 2001, 160 registered MFIs in Nigeria with aggregate savings worth ₦99.4 million and outstanding credit of ₦649.6 million, indicating huge business transactions in the sector (Anyanwu, 2004). Institutional structures for the provision of microcredit vary and may be government or public sector-oriented, NGO-supported, traditional or a mixture of two or more of these. There are those that exist along the lines of the Informal Model and involve revolving credit and savings associations (and isusu), which are based on traditional experience. Microfinance is also extended to clients through formal financial institutions in what is called the Formal Model. Examples include the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB) and the Nigerian Industrial Development Bank (NIDB). Such institutions usually know very little about the poor who need microcredit but have to maintain such a unit in order to fulfil statutory requirements by the political and financial authorities. There is the Linkage Model in which informal savings collectors are linked to the formal financial institutions. A good example is the defunct Village Adoption Scheme of the Centre for Rural Development and Cooperatives, University of Nigeria, Nsukka, which linked commercial banks to village cooperative societies and other groups for financial support. Finally, there is the Donor Model in which mainly international donors—such as UNDP—provide funds to MFIs for on-lending to their members and clients who enjoyed microfinance services.

The MFIs in Nigeria, most of which are non-regulated, include NGOs. More prominent among which are Nalt-United Self-Help Organisation (NUSHO) in Nsukka; OUTREACH Foundation (OF) situated in Lagos; the Country Women Association of Nigeria (COWAN) in Ondo State; the Farmers Development Union (FADU), which can be found Oyo State; the Development Education Centre (DEC) in Enugu, the Lift Above Poverty Organisation (LAPO) in Benin and the Save and Produce (SAP), Jos. Regulated sources of microcredit include the 282 community banks that were licensed by 2003, credit unions and cooperative societies.

Design Impulses, Characteristics and Pitfalls

Nigeria's experience in formal regulated microcredit financing shows the establishment over time of a number of multi-sectoral and sector-specific programmes and institutions with microfinancing components. Some of them are the Rural Banking Scheme, National Economic Reconstruction Fund (NERFUND), Peoples Bank, FEAP, Directorate of Food Roads and Rural Infrastructure (DFRRI), Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB), Nigerian Bank for Commerce and Industry (NBCI—for those who cannot borrow from the Nigerian Industrial Development Bank), National Agricultural Insurance Corporation (NAIC). NGOs and Community-Based organizations (CBOs) have also operated microcredit schemes. By special directives to banks to dedicate certain proportions of their lending portfolios, government had sought to address the credit problems of farmers and small-scale industrialists in response to episodes of economic difficulties since the early 1980s. Thus, the over-bearing influence of the state had ensured that these institutions were designed to fit into governments' strategic political objectives.

The historical development of Nigeria's formal MFIs contrasts with that of Indonesia (Bank Rakyat Indonesia, BRI-UD), Pakistan, Bangladesh and Thailand (Bank for Agriculture and Agric. Cooperatives) where the establishment of their versions of microcredit institutions pre-dated adjustment. In Nigeria, government-sponsored programs and institutions as well as the NGO-MFIs mentioned above are for the greater part excessively donor-dependent, which is a strong risk element that puts their future sustainability in question. Nevertheless, some have endured and diversified to deliver integrated services to their clients. For example, the Diocesan Development Services (DDS) launched its financial services operations in the 1970s, based originally on *oja*, the indigenous farmer council based on the indigenous MFI. (McNamara and Morse, 1998). DDS is involved in other services including on-farm research, primary health care, nutrition and water supply. It maintains an organic link between all these activities, using the microcredit component to 'lubricate' the others.

The key problems identified in the operations of the defunct Peoples Bank of Nigeria also apply to other public sector MFIs. These include the overdependence on government subsidies, extremely high overhead costs resulting from its extensive national networks, below market interest charges as well as the exposure of depositors to risk given the Bank's non-coverage by the National Deposit Insurance Corporation of Nigeria (see Babalola, 1991; Anaeto, 1994). The community banks on the other hand had a macroeconomic aim to integrate the entire financial system through emphasis on grass roots and rural resource mobilisation (National Board for Community Banks, 1992). By their emphasis on rural areas, they inherited the functions of the defunct Rural Banking Programme that was launched by the Federal Government in 1977. Also, by their emphasis on community infrastructure, they inherited the functions of the defunct DFRRI, itself a SAP relief programme.

Key Evolutionary Signposts

Institutional evolution is taking place in the Nigerian microfinance sector, but the pace is slow. Sources of change sweeping the microfinance sector at present in Nigeria include the Central Bank, MFIs themselves and the external donors who initiated these processes. We note that the mode in which they are occurring suggests recognition and prioritization of the needed basic interventions to foster the sector's growth. Signposts, which we believe will lead to more beneficial changes in the sector, include the following:

1. NEEDS and SEEDS, by recognizing the place of microfinance in poverty reduction, linking with MDGs and now catalyzing current initiatives at CBN assures us of an understanding of ongoing processes of change and the motives and capabilities of the 'active' and 'passive' stakeholders involved in that process. Government is beginning to see MFIs less as mere self-help organisations, and more as serious formal institutions whose activities could affect the nation's financial aggregates.
2. The United Nations Capital Development Fund (UNCDF) is one of the most important donors in the Nigerian Microfinance sector. Through its MICRSTAT project, it has recognised the need and has made significant efforts to strengthen the institutional, organisational, and technical capacity of MFIs. It has also sought to contribute to the development of knowledge and expertise in microfinance in Nigeria as well as participate in the coordination and collaboration of the different actors in the microfinance sector.
3. Since 1999, UNCDF and other donors have been emphasizing eradication of poverty through local governance and microfinance programmes.
4. A UNCDF project impact assessment report emphasizes moving away from the assumption that the main constraint for MFIs was access to capital, but upholds the supporting of microfinance with a clear focus on institution building, creating sustainable MFIs and capacity to select and support reputable MFIs that are confronting the challenge of bringing sustainable microfinance services to rural areas.
5. Financial sustainability will remain a core objective for UNCDF projects.
6. Donors are now supporting mostly 'retailer' MFIs as opposed to 'wholesale' institutions.
7. Donors are expressing strong support for MFI partners that have set up accurate and reliable management information systems (MIS).

Why Building Microfinance Institutions in Nigeria is Difficult

The following are very important constraints in the development of MFIs in Nigeria.

1. There is a general lack of awareness about opportunities in modern microfinance among Nigerians
2. Widespread poverty makes it difficult for promoters to muster the level of capital that will sustain the MFI through shocks and not put shareholders money at risk;
3. The registration processes for formal MFIs are often slow, tortuous, expensive, and fraught with uncertainties
4. There is a marked absence of dedicated public sector policies and institutions for the development and extension of microcredit in line with international best practice in the field. The policy environment for microcredit delivery is fragmented and thin and not sufficiently enabling
5. Lack of standards in the field is a problem, although the Community Development and Microfinance Roundtable (CDMR), a voluntary rally of purely private sector microcredit providers in Nigeria, has been making some efforts to provide that. Nevertheless, membership is low and highly dependent on external donor funds. So the extent to which the initiative is locally driven is suspect and its sustainability remains questionable
6. There is inadequate co-ordination between agencies that supply microcredit in Nigeria, whether in the public or private sector
7. There is insufficient effort aimed at promoting the interests of women in the distribution of microfinance services
8. The low level of documentation and dissemination of information on microcredit is a constraint
9. There is a lack of an autonomous re-financing outfit to meet the long-term credit requirements of the microfinance industry
10. There is a low-level of professionalism in the microcredit field, and inadequate capacity of managers and members
11. There is a general aversion of a majority of the population—particularly among the low income groups—for credit.

Elements of Good MFI Policy Design and Practice

The overall test of good MFI design is sustainable poverty reduction through increasing outreach, resource mobilization, cost coverage, profitability and dynamic growth. In Nigeria we need to be wary of the problems that bedevilled past microfinance operations of development institutions such as Peoples Bank. Many of them were ineffective on account of incompatibility with existing traditional savings and loans schemes operated by local communities, over-politicised, lacking in adequate professional staff, had tortuous lending procedures, were poorly funded, suffered high administrative costs, and had inappropriate expectations from poor, uninformed and illiterate clients. Building effective and sustainable microfinance institutions in Nigeria will require a lot of innovation on the part of the promoters, the government, NGOs and donors.

Governments, donors and promoters of MFIs should from the beginning take some decisions that are not necessarily of structure but have to do with social choice and ideology, and may have implications for the ultimate structure and functional approaches of the MFIs in specific local contexts. For instance, should it be savings first or credit first? The savings first mantra is appropriate in low return subsistent activities like agriculture, while credit first is suitable for high return activities such as certain aspects of trading. What do the people want, access to credit and other services or interest rate subsidy? Targeted public sector credit tends to benefit the non-poor far more than the poor. How much government involvement in the development microfinancing system of Nigeria is desirable? For instance should we create an apex microfinance agency and sub-apexes at zonal and state levels or allow their emergence from private initiatives?

Some general guidelines can be put forward for designing effective MFIs according to stakeholder roles. While we cannot, given the scope of this paper, deal with all the fine details of good MFI design, we can put forward some necessary generic considerations and guidelines.

1. Provide initial conditions (policy guidance and legal framework as the CBN is currently doing) to guide incorporation and upgrading of MFIs. The framework should deal with issues concerning all stakeholders: commercial banks, mortgage institutions, National Board for Community Banks, NACRDB, traders associations, farmers associations, the Commodity Companies recently established by the Federal Government, and other institutions that may have interest in microfinancing and enterprise development at all levels. In doing this, donors should be approached to give technical assistance to national financial authorities (CBN, Ministry of finance, National Planning Commission and the Legislature) to help design appropriate policy and regulatory frameworks.
2. Guarantee supply and access to loanable funds (savings, etc) for MFIs including provisions to foster linkages with upstream financial institutions with larger capital base.
3. Ensure participation, local commitment and sustainability by promoting projects based on the needs, culture, values and aspirations of groups and communities as well as priorities for enterprise development.
4. Make provisions for capacity building support for NGOs and CBOs that offer microfinance services.
5. Make provisions to encourage the savings and the banking habit for the attainment of financial self-sufficiency and sustainability.
6. Include aspects to provide financing, policy research and advice, as well as technical support in many areas including small and medium enterprises (SMEs) to encourage downstream enterprise development.
7. Consultants, both local and international, including multilateral donors, should be signed on to give technical support, capacity building and back-up funding to starters and existing MFIs.
8. Avoid excessive aid giving so as not to weaken self-help capacities and institutional viability.
9. Provisions to increase outreach capability of MFIs to the poor.
10. Recognise the multidimensional nature of poverty and bring on board all relevant institutions and agencies dealing with livelihood provisioning in the planning and coordination of microfinance development including development partners (bilateral, multilateral and non-governmental).
11. Provide for demonstration models and encourage replicability of successful MFI approaches in line with best practice but with clear sensitivity to local contexts.
12. Provide for exposure and exchange visits and training in innovative programmes and institutions locally and internationally.
13. Give systematic consideration to the specific needs of women (in terms of outreach, products and services, etc.).
14. Provisions to encourage competition in such a way as to push MFIs to become more market-driven and client-oriented.
15. Give incentives to drive the market at a faster pace.
16. An autonomous fund of the type to which CDMR is complementary should be established to fund the development of young MFIs and give financial support for established ones to attain larger outreach. Something similar to the planned Agriculture Development Fund (ADF) that is now before the National Assembly.
17. Provide for the establishment of networks and apex organizations for guidance, training, consultancy, services, self-regulation and supervision, liquidity exchange and refinancing.
18. The regulations and legal framework and institutional environment should support a range of institutional types, including non-profit entities, building societies, NGOs, and savings and loan cooperatives so as to foster diversity in terms of leadership, human resource capacity, systems and internal controls. Subsidiarity should be the key in order to accommodate all types and grades of microfinance institutions, including formal MFIs

regulated by the CBN or other agencies and semi-formal MFIs controlled by non-financial authorities like Registrar of cooperative societies as well as Informal MFIs controlled by customary law and societal norms. National-level imperatives for design of MFI systems are different from state-level and Local Council-level requirements. The Federal authorities must recognize this and accordingly give only broad guidelines and allow other tiers of government to address peculiar contextual issues.

19. Provide clear guidelines for weaning dependent MFIs from financial dependency as soon as possible as part of legislation guiding the operations of MFIs in Nigeria
20. Mount campaigns to enlighten people on the usefulness of microcredit and MFIs and disabuse their minds about their unhelpful perceptions regarding the serious difficulties of nurturing institutions since there is now greater transparency and due process in relevant government agencies.
21. Design MFIs to complement what already exists in terms of other supporting institutions, traditional institutions and practices (isusu, etc) human capabilities, and available technologies.
22. MFIs that finance manufacturing and technology-intensive activities should receive more incentives in the policy. This is because evidence shows that loans disbursed by major MFIs in Nigeria up to 2003 were mainly to trade and commercial activities (78%), leaving manufacturing (3.5%), agriculture (14.1%), multi-purpose (4.0%), services (0.7%) and others trailing behind (Anyanwu, 2004); and,
23. Some educational institutions abroad are already offering up to MBA course levels in microfinance institution building. Nigerian educational institutions should be advised and encouraged to come up with such even at diploma level.

Who Builds Microfinance Institutions?

This is a pertinent question, and it cannot be answered easily because as we would learn from political economy, there is no natural gravitation towards good institutions. The general public often perceives microcredit as something for the poor only. This has a way of discouraging many educated and relatively well-to-do people from being involved either directly of by way of indirect support. But everybody should have a role in the building of MFIs in a democratic society: government, business people, community actors, and existing institutions. MFIs may be said to evolve as financial systems grow. However, MFI need macro rules, frameworks and regulations to exist and succeed, which can only be provided by the state. Citizens on the other hand should need no specific permission to set up MFIs to help themselves. But, of course, getting registered with the regulatory authorities requires that the applicant conforms with statutory stipulations.

Most of the time the ruling elites, be they the past colonialists or the present Nigerian politicians hardly set up institutions to primarily benefit society at large but to help themselves. A plethora of microcredit initiatives in Nigeria in the past (Peoples Bank, FEAP, FSP, SME, NERFUND, etc) would, on the surface, appear to be good attempts but were largely politically motivated. Otherwise, by now Nigeria would have had comprehensive laws and legal frameworks for supporting the development of broad based participation in its microfinance sector. It is wise to leave some leeway for informal, and perhaps even innovative forms of MFIs to thrive. This is because public sector or large private commercial institutions do not always serve the interests of the poor and the vulnerable. Private monopolies, which often corner bilateral government-donor projects with a microcredit component still charge high prices. Interventions by active and passive stakeholders alike in various communities are necessary. People and corporate organizations need to be enlightened to understand that their philanthropy could support the development of microcredit and microfinance institutions, structures and groups that such investments could be profitable both in cash and otherwise.

In every sector of the economy there are usually some key drivers of growth and innovation. The issue of key drivers is very crucial. These are people who are ready to sacrifice their time and money to nurture the MFI. They are able to chart a positive direction for the institution, take risks, kick-start new ideas and practices that can advance the institution, and liaise between it and other 'remote' institutions such as governments and higher level networks. They may be found in various communities and may be engaged in vocations other than financial management. The challenge is to identify and fish out such individuals for encouragement.

Conclusions

The Nigerian scenery is marked by overly donor-directed structural arrangements and agenda for microfinance activities. This is expected since much of the funding for microfinance institutions come from donors, and reflects the relative paucity of governance and policy direction for poverty reduction programmes in Nigeria. Failures in governance cannot, however be remedied by donor support only. Governments at the local level are assumed to know best how to structure their MFI environments to create dynamic strategic linkages between the grassroots and national level coordinating instruments in order to seamlessly link the financial system with local level economic activities. Interventions are needed at various points in form of initiatives taken to introduce change that can deepen the finance sector beyond the orthodox and upstream sectors (the capital market, mortgage institutions, commercial banks, community banks), whether through policies, programmes or projects.

NEEDS and SEEDS provide impetus for policy interventions at national and state levels and define the broader policy frameworks. Safeguards need to be provided to ensure that these initiatives would not eventually suffer the usual abandonment that has in the past bedevilled national development programmes in Nigeria. The Local Economic Empowerment and Development Strategy (LEEDS) is yet to be evolve fully at the local government levels, at which the critical mass of innovation is most desirable in MFI systems development. Without viable and independent microfinance institutions at local levels the dream of funnelling thousands of microcredit groups into the larger MFIs and banks for financial intermediation may never come true.

Having recognized that microfinance could be used for poverty reduction, the formation of MFIs at all levels should be encouraged. An assessment of the activities of microfinance institutions in Nigeria has shown that the poor are good credit risks. The increasing access of the poor to credit and their unmatchable repayment rates suggests that microfinancing should be a viable enterprise. But government must create the enabling environment by, among other things, easing regulations and giving incentives to quicken the creation of MFIs. Incentives need to be given to people, groups and institutions that already operate microcredit institutions to strengthen and upgrade their operations.

References

1. Anaeto, E. 91994). "Community Banks Seek Peoples Bank Branches", *Business Times*, February 7.
2. Anyanwu C. M. (2004) "Microfinance Institutions in Nigeria: Policy, Practice and Potentials", Paper Presented at the G24 Workshop on *Constraints to Growth in Sub Saharan Africa,* Pretoria, South Africa, November 29-30, 2004.
3. Babalola, J. A. (1991). "Financial Institutions and Agricultural Finance", *Bullion*, Vol. 7, No. 2.
4. *Bank Annual Conference on Development Economics*, 1989, Washington, D. C., The World Bank.
5. Charistonenko, S (2004): "Policy Issues in Licencing Microfinance Institutions that Accept Deposits from the Public." Speech presented on March 18, at the International Validation Summit on Microfinance Policy and Regulatory Guidelines at the Central Bank of Nigeria, Abuja, Nigeria. P11.
6. International Fund for Agricultural Development (2001) *Rural finance for the poor: From sustainable projects to sustainable institutions*. Rome, pp.10.
7. Marx, M. T. (2001) "Nigeria's rural and microfinance: rural microfinance options", *Report on Formulation Mission* by IFAD/World Bank/CBN, Abuja, CBN: pp 4-22.
8. Nellis, John R (1980). "Maladministration: Cause or Result of Underdevelopment? An African Example". *Canadian Journal of Algerian Studies*, 13, no. 3: 413.

9. North, Douglas (1981). *Structure and Change in Economic History*. New York: Norton.

10. Ostrum, V., D. Feeny, and H. Pitch, (1988) (eds.) *Rethinking Institutional Analysis and Development.* San Francisco: International Centre for Economic Growth.

DISCUSSION NOTES

By
John Okoye
Investment Banker

SMEs are playing an important role in the emerging business models in the international supply chains as evident in the following statistics:

- ❖ In the EU, 40% of over 4 million firms that exported goods in 2001-2 were SMEs.
- ❖ In the US, SMEs having fewer than 20 employees constituted over 65% of the exporting firms in 1999.
- ❖ In Australia, nearly 70% of exporting firms and 60% of importing firms were SMEs in 2001.

For obvious reasons, local statistics on the role of SMEs in Nigerian economy is not readily available, but we cannot deny their role in local employment and wealth creation. Afterall, agriculture still contributes the lion's share of our GDP and remains the largest employer, even with limited number of mechanized/commercial farms.

SMEs are an indispensable and dominant part of any economy—completing the value chains of giant corporations, where they exist or playing more critical roles as in the developing economies. Financing SMEs, or micro financing is therefore a fundamental challenge due to their socio-economic importance and scarcity of seed money or capital in Nigeria.

The challenges to micro financing are varied and demanding on the different stakeholder groups:

1. Government/Donor Agencies
2. Microfinance Institutions (MFIs)
3. Beneficiaries (SMEs)

Successful completion of the ongoing Economic and Financial Sector Reforms under the NEEDS blueprint would create extensive industrial structures/business opportunities in Oil & Gas, Power, Telecoms, Aviation, etc. It would also generate pools of cheap funds for macro and micro economic agents, including SMEs to harness—from the Pension Reform Act 2004, Banking Sector Consolidation, Small & Medium Enterprises Equity Investment Scheme (SMEEIS) etc.

There are some pertinent questions here: Are our SMEs capable of exploiting the business opportunities available in the emerging industrial/business structures post privatization/sector reforms? Can our financial system boast of sustainable MFIs capable of filling the finance gaps with effective intermediation?

The challenges for our MFIs are also made more complex by the growing poverty in the land. A recent study by the United Nations ranked the oilrich Nigeria as one of the 20 Poorest Nations in the world even as the present administration battles to delete the country's name from its unenviable second place position on the TI Corruption Index. With their genuine struggles for socio-economic upliftment through quasi-economic endeavours, social groups and NGOs, the country's poor masses are also laying claims on all available micro or development funds in the system.

The dichotomy of value chain oriented microenterprises and poverty alleviation schemes make proper definition and targeting a natural starting point for microfinance design and practice in Nigeria. In his paper, "Policy Needs in the Microfinance Sector of Nigeria: The Missing Angle" delivered at Enugu Forum organized by African Institute of Applied Economics, Dr Kalu Oji of Dept of Agric Economics, University of Nigeria, Nsukka recognized three types of MFIs in the definition of Microfinance:

1. Formal MFIs (e.g. Commercial, Community and Development banks), usually regulated by the Central Bank.
2. Semi-formal MFIs (e.g. Cooperative Societies, NGOs), usually non-profit legal entities… but are not under the regulation of the Central Bank.
3. Informal MFIs (e.g. Traditional Credit & Savings Club, Esusu, Ajao, etc), mainly traditional self-help groups (SHGs) or associations.

As a group, the Nigerian MFI is a failure. An anatomy of the relics of the country's MFIs would reveal some inherent strengths (and weaknesses) both public- and private- sector led MFIs, which would guide the institutional design process.

Development banks - NACB, NBCI, etc enjoyed government backing and eligibility for donor funds from UN, ADB, DFID, USAID, etc. This finance window, which narrowed with declining public treasury, proliferation of parallel agencies (NDE, etc) and pariah country risk rating under the military is fast rejuvenating due to fast reversal of the aberrations.

Microbanking Institutions - Community banks, etc are marred by limited financial capacity, residual management scope and loose supervisory framework. Their successful adaptation to the customers/players in the informal or microeconomy who are also stakeholders in the MFIs make them, or the variants indispensable in the microfinance design process.

Rural Banking Initiatives were overwhelmed by the upscale capitalist orientation of their sponsors (i.e. commercial banks), who are tuned to viable businesses that meet highrisk acceptance criteria – management pedigree, turnover and property collateral.

Ironically, the positioning of our commercial banks above the vicissitude of our microfinance environment and insistence on the best practices have earned the Nigerian banking industry, etc world-class rating. Just this last week, Zenith Bank PLC won Bank of the Year 2005 Award conferred by The Banker Magazine, a subsidiary of the Financial Times of London. No doubt, the industry's good management capacity and scope for corporate venturing and innovation, especially after the banking industry consolidation commend them for active roles in the emerging microfinance scheme.

While the development banks and the microbanking institutions will naturally key into any emerging microfinance scheme, the commercial banks will typically play along unless the new MFI schemes promises goal congruence, in terms of return for their competitive funds and risk management. The pertinent question here is: how do we sweeten the emerging MFIs schemes to appeal the interests and attract the need synergies of all the relevant stakeholders? Sustainable MFIs must draw from the strengths in the (1) Development banks/FGN/donor agencies, for their deep purse (2) Microbanks, for their adaptation and local knowledge, and (3) Commercial banks, for their tested managerial capacity.

The truth is that our SMEs are either too small for relevance in any industrial value chain or crowded out by the avalanche of poverty alleviation schemes competing for microfinance. As expected, the MFIs operating in the muddled MFI environment are already contaminated by the poverty syndrome and have remained largely informal, fragile and disconnected from the larger financial system. Such mismatch weakens policy transmission and efficacy of financing schemes rolled out by the CBN/donor agencies from time to time.

For our SMEs and their financiers to be relevant and sustainable in the emerging post-reform Nigeria, we must adopt categorize and target the beneficiaries appropriately and also key in the new MFIs into the existing financial system via Multi-level Institutional Framework with at least three tiers:

Tier 1: Sectoral Venture capital Institutions to be registered by CBN with funding from SMEEIS/donors agencies.

Tier 2: Sustainable Community/Rural Banks Affiliated to Commercial Via SMEEIS Desks/donor agencies and sweetened with Tax Benefits.

Tier 3: State Sponsored Poverty Alleviation Schemes operating through NGOs, Cooperatives, Self-Help Groups with back up Credit Guarantees.

Such a multi-level approach to microfinance reform will introduce sanity in the residual sector and ensure sustained benefits for the entire spectrum of microfinance candidates, ranging for the rural poors through cottage industries to outsourcing agencies in the corporate value chains.

2ND PLENARY SESSION

Moderator: Kanayo Ogjiuba

Contributors noted that there are insufficient funds for financing microcredits, a fact that runs contrary to popular beliefs. It therefore falls on the government and donors agencies to provide more funds. More importantly it is vital to go to the core of the matter which is the fostering of real growth and development which will raise the vast majority of citizens that currently lie in poverty. Besides, microfinance for enterprise growth can only survive where there is adequate reward and incentive for genuine effort.

The problem of microfinance in the country does not reside on the beneficiaries but on the providers and administrators who ought to seek the right models to achieve their desired aims. The models currently being implemented are not well thought out. Imported models are applied without due regard to the peculiarities of the operating environment. For microfinance to succeed in Nigeria, the government should be reformed to ensure that policies are focused to the real needs of the poor, and are implemented in a sustainable basis.

Guest Speakers' Summaries

Engr Chris Okoye

The challenge is how to reach the 65 million poor people who need microfinance in Nigeria especially those resident in rural areas. This requires:

1. Setting up the regulatory and institutional framework for the delivery of microcredits. Microfinance should not be seen from a loan perspective only and should instead be developmental in approach. This approach will guarantee the changes in our environmental that is required to ensure ability to repay loans that have been granted.
2. Creating the enabling environment for micro-enterprises to succeed. Since microfinance is strongly related to micro-enterprises, it is imperative that the necessary infrastructure that supports micro-enterprises is put in place to ensure their success, especially the decentralization of microfinance institutions and services to the localities where these services are needed.
3. The Government of Nigeria to make deliberate policies that would leverage the growth of microfinance institutions. The CBN Microfinance policy being drafted could do this by liberating the microfinance institutions within the prudential guidelines to adequately and effectively serve the microenterprises without necessarily compromising profitability.
4. Capacity building for the micro-entrepreneurs. The micro-entrepreneurs are to be properly educated and trained to become active participants in wealth creation. Also there should be capacity building for the microfinance institutions to enable them deliver on the provision of microfinance services to the poor. This could be done by creating wholesaler MFIs in post consolidation era in collaboration with international donor agencies that are seeking for channels to get money to the enterprising poor.
5. Education—especially adult education for the beneficiaries of microfinance—is critical to the success of microfinance development. Education should include basic accounting, budgeting, business management and entrepreneurship development.
6. The structure of government must be changed to build synergy for all the constituent parts of the country to deliver services that will uplift the poor.

Dr Kalu Oji

What is needed are development policies that will improve the capacity and growth of micro-enterprises as well as the microfinance institutions. They include:

1. Those kinds of policies that would inject technology into the activities of micro-enterprises, and MFIs
2. The MFIs should develop financial products that can inject technology into the activities of the micro-enterprises.

3. Policy and regulatory environment should be able to support micro-enterprises and microfinance development. Sectoral policies—such as science and technology policy—that are sensitive to the needs of micro-enterprise sector are necessary for the success of the microfinance/micro-enterprise sector.
4. Change in the habit of the SME to accommodate the acquisition of banking habits in order to access banking facilities. This could be done through education and training.
5. Banks should also change their orientation towards micro enterprises—the banks should reach out to the micro-enterprises and not wait for the micro-enterprises to come to them. Bankers should identify the needs of their clients, assist them to build their business plans, administer the appropriate credit or service, and follow through to ensure the success of the venture. They should apply the new technology in lending such as group approach, cycle of loan-trial loan, first loan, second loan, etc. to ensure that their clients succeed to achieve the repayment rate of above 90% as has been proved.
6. Credit Extension Services are necessary for the growth of microfinance. Microfinance institutions that are successful have Credit Extension structures that enable them to reach their clients and deliver the services to them.

Conclusions

Microfinance for Nigeria should be the menu of financial and related services offered to the poor to enable them attain sustainable livelihoods and eventually exit from poverty. These services should include microcredit, micro-saving, micro-leasing, micro-insurance, credit guarantee scheme, etc. In other words, microfinance in Nigeria should be Credit Plus and development-oriented.

Problems and Bottlenecks

1. The major problem identified as militating against microfinance development is high default rate of the borrowers' repayment of microcredits has been put at about 30%.
2. Inadequate supply of microfinance services to the poor who are the target group. The existing financial institutions (banks) are microfinance shy thereby limiting the availability of both credits and other related services to the poor. This has been attributed to high cost of administering microcredits and financial services to the numerous poor scattered in various remote locations.
3. The regulatory requirements to access conventional banking and finance service are too high for the poor to meet thus excluding them from mainstream financial services. For example 10% of SMIEIS fund which ought to be targeted to the micro-enterprises has largely not been accessed because their requirements are difficult for the poor to meet.
4. Inadequate funding of State microfinance institutions. Government has not encouraged microfinance development by not funding the MFIs it set up, and by the general failure of governance to provide the right can of environment that sustains the growth of micro-enterprises in the country.
5. There is a low level of private sector participation in the MF sector because microfinance is seen as a social activity, hence profit making organizations are shying away from the sector though there is profit to make if the mechanism is properly worked out.
6. Too many people compete in one particular venture which drives down profitability and increase the inability to repay loans.

Suggested Policy Interventions

1. The Microfinance provider should have a proper assessment of type and scope of ventures for their beneficiaries to ensure that there is no over-competition that drives down prices and profits thereby jeopardizing the ability to

repay credits. Though competition is a genuine economic practice, microfinance providers and administrators should encourage diversification of ventures for their clients (micro-enterprises) to make them more viable and sustainable.

2. The Group or Cooperative model should be encouraged in micro-lending. The Group method encourages collective responsibility for repayment of loans thereby reducing tendency for default. Community leaders and the clergy could be tied into the repayment arrangement to strengthen this method.
3. The regulation of MFI should be such that would allow niche playing. The FG or CBN regulation should not be such that could stifle the emergence of niche players in the system. States could be given the scope to legislate or guide the establishment and operation of MFIs. For instance, the planned re-engineering and regulation of Community banks by the CBN should be done in such a way as not to exclude the poor from accessing funding from the community banks. It should actually be restructured to fill the gap in rural enterprise lending.
4. There is need for infrastructure development that enhances the operation and growth of micro-enterprises and microfinance institutions especially electricity, water, and access roads to remote locations.
5. The major policy thrust for microfinance in Nigeria should be developmental i.e. it should seek to lift the poor from poverty to sustainable livelihood and prosperity. This requires an integrated approach that offers credit plus other incentives or services to the poor. This is otherwise called the Credit-Plus Approach to Micro-financing.
6. Government intervention is critical to the growth of micro-enterprises especially in removing bottlenecks that discourage investment in microcredit financing e.g. difficulty in contract enforcement. Besides, government could provide Credit Guarantee for Micro-enterprises to ensure confidence in the microfinance providers.
7. Commercial financial institutions are not willing to lend to the micro-enterprises because of the high cost of administering the tiny loans to this class of borrowers scattered in mainly the rural communities. However, there should be deployment of technology in such a way that it could reduce the cost of managing credits and other microfinance services to the poor. Besides, banks could be given tax breaks in order to encourage them to venture into microfinancing in the post recapitalization era when investible funds would be readily available in the Nigerian financial market.
8. Banks could consider channelling their social responsibility funds into micro financing.
9. Insurance for microcredit is desirable to ensure stability in the system.
10. There is need to integrate informal systems of lending into the formal through what is referred to as the poverty lending approach. This would involve categorizing those requiring microfinance into two groups—the core poor and not-so-poor. Poverty lending approach should be used for the core poor, while the financial service approach should be used for the not-so poor group. In other words, financial services should be tailored to the needs of the various classes of the poor The formal MFIs could apply the methods used by the informal MFIs e.g. NALT NUSHO, the Esusu system, etc, that have achieved above 90% repayment rate for their loans.
11. There should be greater equity into the system of lending in terms of the identification of methods and channels through which the funds meant for the poor would actually get to them. Experience in the past has shown that funds released either by government or donor agencies were hijacked by highly placed individuals or organizations leaving out the poor.
12. There should be training and orientation for micro-enterprises to inculcate in them the sense of entrepreneurship and productivity. This could be done using the churches and other faith-based institutions, NGOs, and town unions for effectiveness. .
13. Information about the sources of microfinance e.g. SMIEIS, etc should be made more readily available to the SMEs and micro-enterprises. This could be done through seminars at local levels through churches and NGOs.
14. Conditions for accessing the SMEEIS fund should be reviewed to make it more easily accessible to micro-enterprises. For instance, the five years minimum age for companies applying to the SMIEIS fund discourages start-up firms.

15. Land registration at the rural areas could be done at the Local Government Councils; arbitration for microcredits could be administered at the rural areas through the town unions or other organized customary institutions that function as arbitrators. This is necessary because most micro-entrepreneurs depend on land for their livelihood. However, any far reaching intervention on land acquisition, registration and securitisation would require the review of the Land Use Act 1978 which poses a major set back to property rights in Nigeria.
16. There should be an orientation away from the system that encourages easy-wealth for those who do not produce, to a system that rewards hard work and entrepreneurship for the development of micro-enterprises.
17. These recommendations should be made available to the policy makers in government, industry, development and donor community, CSOs, and researchers for inclusion in their policy menu and programming for the micro-enterprises and microfinance sectors in Nigeria.