Microfinance
in a Disrupted World

SUMMARY

The microfinance sector has grown dramatically over the past 50 years and is one in the main sources of financial support for the poor worldwide. Today, the lending portfolios of microfinance institutions (MFIs) are worth a combined $124 billion, and 140 million customers. In Asia, more than 65% of adults have financial access, while in Africa it is over 40%. However, 1.7 billion adults worldwide still lack access to a bank account.

Christians have been at the forefront of micro-finance. VisionFund, Opportunity International, Hope International, and Partners Worldwide, collectively serve almost 9 million customers with over US$3 billion. They each have a slightly different focus ranging from loans as small as $50 lent to the poorest of the poor to business loans of >$10,000 awarded to entrepreneurs to tailored products for specific needs like education or agriculture.

Christian MFIs are uniquely positioned to serve the poorest of the poor and have the potential to influence and disciple millions of people worldwide.

But the industry is in trouble and faces significant short- and long-term threats. These include:

1. COVID-19 and its impact on the ability of the poor to repay loans
2. The limited impact of micro-finance in lifting people out of poverty
3. The rise of fintech and mobile money
4. Shifting priorities of private- and public-sector donors

The Christian MFIs spoken with are fully aware of these new realities and are in the process of adapting. They have deep relationships with the poorest of the poor, an impressive track record, and a global footprint to build upon. However, if they are to continue to effectively serve the poor, it will require them to work more

closely with local churches, overcome legacy systems and culture, adopt innovative technology, and develop new models and partnerships.

This short note outlines some potential opportunities for the future of Christian microfinance.

TRENDS

COVID-19

COVID-19 is straining its finances. Repayments, usually executed in cash and in person, have plummeted; yet the banks and investors which provide the MFIs with funds still expect money. A crunch looms. More than two-thirds of MFIs have cut lending, often by at least half, according to CGAP, a think-tank in Washington. Nearly one-third do not have enough cash to meet outflows this quarter. (MSC/ micro-save consulting has great info on the impact of COVID-19 on MSMEs specifically in Kenya)

Impacting Poverty

Randomized control trials (RCTs) across a variety of countries and settings have not shown evidence that microfinance loans have lifted families out of poverty on average. The initial hope was that it would be utilised by entrepreneurial individuals to enable them to grow enterprises. However, it has been found to primarily help families deal with emergencies, make critical purchases they couldn't otherwise afford, and put food on the table in times of scarcity. In other words, it has mostly provided a vital safety net but not a trampoline out of poverty.

While RCTs haven't found that microcredit raises incomes for average borrowers, there is a small group of people who do achieve higher business profitability when they receive loans. Sometimes these returns are impressive, far exceeding interest rates. These are true entrepreneurs as opposed to necessity entrepreneurs. The open question is whether it is possible to better target and support true entrepreneurs when offering loans for business, or whether tweaking the terms of the loans might improve business profits.

Christian MFIs are unique in that they seek to influence and disciple their clients. Although there are many challenges in achieving this, there is a strong evidence base that worldview/discipleship programs can be extremely effective. The largest randomised control trial of this type of intervention is with ICM in the Philippines, where it demonstrated a 9.2% increased income for households which participated in their worldview training. However, there are few examples of MFIs supporting local churches, who have credibility and broad networks, to provide entrepreneurial discipleship.

Technology Disruption

The past decade has seen a massive shift in the access of the poor to technology. For example; in Africa, 84% of the population are expected to have access to a mobile phone by 2025. Smartphone ownership ranges from 14% in Tanzania to 51% in South Africa. By 2021, 75% of Africans will have access to television and up to 90% to radio. In Kenya, pioneer of M-Pesa, over 30% of the economic activity is via mobile money.

MFIs have been slow to adapt to new technology. All of Christian MFIs spoken to in this study primarily deliver their services through in-person formats. As a result, fintech companies are rapidly gaining market share in financial services to the poor as they can reduce the transaction costs and gain economies of scale. However, fintechs face problems of customer acquisition, support, and also capital raising. There are significant opportunities for mutually beneficial partnerships between fintech and MFIs.

Shifting Priorities of Private and Public Donors

As a result of the previously discussed factors, microfinance is no longer 'de rigueur'. Most microfinance still requires some form of subsidy, which has been estimated at $25 per customer. However, confidence of private and public donors has been waning for some time and MFIs are struggling to secure this support. COVID-19 will exacerbate this trend and has already led to significant declines in private investment.

Opportunities

There is a short window of opportunity for MFIs to adapt to these new realities, and they should seek to;

1. Target true entrepreneurs and engage the local church
2. Utilise technology to provide tailored, low-cost discipleship, training and tools to support entrepreneurs
3. Build new partnerships to increase access, reduce costs and expand products and services to specific customer segments

1. Target true entrepreneurs and engage the local church

Christian MFIs provide broad financial services to the poor, but most do not actively target 'true entrepreneurs'. The potential benefits of targeting this group include:

- their ability to lift themselves and others out of poverty
- their substantial cultural influence in their communities
- better financial returns for the MFIs.

Part of the challenge is how to identify this group where there is limited access to financial data such as credit history. Field-based loan officers are trained to reduce risk in their portfolio and an entrepreneur may possess a higher risk appetite and thus exclude them. Fintech companies are pioneering the use of alternative methods including algorithm based lending utilising big data and AI and psycho-metric profiling. Harvard's Entrepreneurial Finance Lab has led much of the research behind this and spun out a fintech company, LenddoEFL. Kiva has experimented with trawling social media profiles to assess an individual's relationships, character, and thus likelihood of repayment. These alternative methods are still in early stages of development and have some challenges, such as individuals 'gaming' the process. However, if used to complement rather than replace traditional methods of selection, they could enable more effective targeting of true entrepreneurs who could then be assessed and supported in ways which suit their needs.

Local churches have deep trust-based relationships with their communities and extensive networks. If trained and supported, they could provide coaching and discipleship to entrepreneurs and create business networks of mutual support. In addition, their church buildings could provide low-cost office space for start-ups. This would help reduce many of the barriers entrepreneurs face and would enable MFI to more effectively target entrepreneurs and reduce loan default risk.

2. Discipleship, training and support goes digital

All of the Christian MFIs have a desire to influence and disciple their clients in their faith and provide practical training and support to their customers. However, most struggle to do this effectively at scale. There are a variety of reasons for this. Clients are unable to take much time away from their livelihood activities - training needs to be bit-sized rather than multi-day. Loan officers have limited expertise, time or incentive to provide training and support. Their primary role is to ensure that the client doesn't default on their loan, they have a sizable caseload to manage, and they are unlikely to have an entrepreneurial mindset and capabilities. None of the Christian MFIs are yet utilising technology to deliver training and support at scale. COVID-19 has forced them to begin to experiment.

It is recognised that this is a significant untapped opportunity to increase both impact and market share. WorldVision engages its rural agricultural clients in a program called Empowered Worldview and is looking at how this might be integrated into their microfinance work. Hope International, Partners Worldwide, and Chalmers Centre have developed a microenterprise curriculum. This is currently delivered in-person, although they are beginning to move it online.

Infotainment, which utilises new and old forms of media to both entertain and inform, could be an effective way to expand support and reach. For example, Mediae, a social enterprise in East Africa, uses TV, radio and SMS to provide education to over 9 million smallholder farmers. This also helps them access inputs, finance, and markets. (TedX talk here). Its methodology and technology could easily be adapted to support entrepreneurs.

3. Build new partnerships

In an increasingly competitive and challenging market, there will be pressure on MFIs and a need for them to expand into new areas or pioneer new models. MFIs need to maintain focus on their core mission. They should realistically assess their core competencies, knowing what they have to offer and when they need to partner with others.

Many MFIs (including Hope International, VisionFund, and Partners Worldwide) are moving upmarket and providing small business loans. The logic is that MFIs can follow their customers' development and thus increase their margins in this large and potentially attractive market. However, the evidence of MFIs who have pursued this strategy is that profitability fell in the medium-term (owing to lower margins and a higher risk of default). In hindsight, MFIs overestimated their capacities to serve the small business segment. Evaluating a small business loan requires a broader understanding of their business, the balance sheet, and their debt capacity. These micro-entrepreneurs require specific support to enable their businesses to grow. The risk profile of a micro-entrepreneur is different from a regular micro-credit client. The typical MFI loan officer is not equipped or able to address these issues. Partnerships with capacity-building organizations, small business focussed financial institutions and fintechs will be required if they are to succeed.

MFIs are unlikely to be able to make the leap to digital alone and need to prepare to work with fintechs. Their IT departments will need to develop a culture of experimentation and collaboration, in contrast to an organizational identity wedded to traditional methods. And they need to recognize that fintechs, with limited financial resources, need to get to market quickly, or they need financial support from prospective partners. To take advantage of what fintechs have to offer, MFIs must not only ask what they need from fintechs, but also be prepared to offer what fintechs need from them.

CONCLUSION

Micro-finance plays a vital role in sustaining the poor and can be particularly important in enabling entrepreneurs to grow their businesses and lift them out of poverty. In this post-Covid era, Christian MFIs are needed more than ever to provide practical support and influence millions of people for the Gospel. A relatively straightforward, low-cost, high-impact strategy would be better targeting of true entrepreneurs through the local church and utilise new technologies to provide them with discipleship and training at scale. To succeed MFIs will need to be agile, innovative and willing to work collaboratively for the sake of the Kingdom.

Articles

Microfinance, what happened?, Vox, 2019
Microfinance in a digital world, Centre for Financial Inclusion, 2019
Covid 19 micro-credit crunch, The Economist, 2020
A partial marvel, The Economist, 2009
The Miracle of Microfinance? Evidence from a Randomised Evaluation, Abhijit Banerjee, Esther Duflo, Rachel Glennerster and Cynthia Kinnan, May 2009
Randomizing Religion: the influence of Protestant Evangelism on economic outcomes, Dean Karlan, James Choi, Gharad Bryan, Harvard, 2020
Psychometric credit scoring, Next Billion, 2019
Shifting from MFI to SME financing, FinDev Gateway, 2017
State of the Market Report, Responsibility 2018
Financial Inclusion Database, World Bank

Main Christian MFIs

Details below are taken from the most recent annual reports. Figures are not directly comparable as each organisation has different definitions.

Vision Fund 2019 annual report

Provides micro-loans to the poor. Strong focus on rural and agriculture. Moving to provide larger small business loans.

- 28 partners organisations
- 1.1 million customers worldwide
- $694m loans disbursed

Opportunity International 2018 annual report

Focussed on micro-savings and loans to the poorest of the poor. Particular emphasis on educational loans to households and schools.

- 24 countries
- 6.6 million saving and loans
- $2 billion loans disbursed

Hope International 2019 annual report

Provides micro-loans to the poor. Strong focus on rural and agriculture. Moving to provide larger small business loans.

- 16 countries
- 1 million customers worldwide
- $1.48 billion loans disbursed

Partners Worldwide 2019 annual report

Focus on the upper end of micro-enterprises. Provides business mentoring and support.

- 84 local community institutions
- 105,000 customers worldwide
- 700 business mentors
- $16m loans disbursed

The Chalmers Centre

Provides research and tools to equip local churches worldwide to tackle poverty.