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Central African Policy Makers Convene: Forum shines spotlight on microfinance

Over the course of two-and-a-half days in March, regional leaders from 10 countries in sub-Saharan Africa—Burundi, Cameroon, Central African Republic, Congo, Chad, the Democratic Republic of Congo, Equatorial Guinea, Gabon, Madagascar, and Rwanda—gathered in Yaoundé, Cameroon, to discuss how policy measures can help improve access to financial services for low-income people in the region.

Bringing decision makers together at a crucial time

Forty central bank governors, ministers of finance, and other high-level officials from across the region met at the Central Africa Policy Forum to discuss issues such as regulating and supervising cooperatives, reducing costs of financial services, using new banking technologies to reach unbanked people, and ensuring poor people's money is protected while offering increased access to services.

The forum comes at a time of growing concern about regulatory environments for microfinance. In a recent CGAP/Citi industry opinion survey, inappropriate regulation ranked as the third highest risk the industry faces. However, in Africa, "there has been considerable progress: a number of countries in the region have recently passed microfinance laws," says Jennifer Isern, who leads CGAP's work in Africa. "Now it's up to policy makers to ensure these laws are put into practice through adequate supervision and other measures to enable greater access to finance."

Why focus on policy?

This increasing awareness of regulatory environments for microfinance among regional governments offers the opportunity to create consensus and standardize approaches to microfinance. François Kanimva, governor of the National Bank of Rwanda, describes the meeting as a useful opportunity "to exchange ideas with other countries in the region on these issues."

Where just one in five households has access to formal financial services, sub-Saharan Africa suffers from one of the lowest rates of financial access in the world. "But there are huge opportunities," says Isern. "With the right policy direction, Africa is poised for massive expansion in financial services, building on robust economic growth, donor

commitment, a strong savings culture, and a very diverse landscape of providers."

"At the end of the day, it is the central bank's role to not only protect against systemic risks," says Princess Maxima of the Netherlands, who champions microfinance as part of the United Nations Advisors Group, "but also to allow people to access a range of services, such as secure deposit accounts and reliable payments services."

Policy challenges

Interest rate caps

One obstacle to increasing access to finance highlighted by Princess Maxima during the forum was interest rate caps: "We are convinced that the best approach for governments is not to impose artificial interest rates," she says. "Instead, they should improve efforts in consumer education and create a level playing field."

Accountant shortage

Policy makers also discussed the critical shortage of accountants in the region and the need for better enforcement of financial standards. "On the positive side," says Djibril Mbengue, CGAP Africa microfinance specialist, "regional accounting bodies, such as the Fédération des réviseurs et experts comptables d'Afrique Centrale, are driving improved harmonization, and countries in the region are recognizing international financial reporting standards."

Technology innovations

Innovations, such as the use of mobile phones and other new technologies to deliver financial services, offer great promise for reducing transaction costs of financial services and were a hot topic at the forum. However, new technologies also pose fresh challenges for policy makers and regulators, says Tim Lyman, CGAP senior policy adviser. "Being too restrictive can mean fewer people in the formal financial system and higher costs to access services. But policy makers also need to be aware of potential protection gaps."

Transparency and consumer protection

Policy makers will have a critical influence in shaping the future of access to finance on the continent, says Isern. "Financial institutions need a policy environment that encourages competition and creative new services under transparent conditions. Above all, services must be financially and operationally viable. But policy makers must also take into account the impact on low-income people and ensure they are protected."

The Central Africa Policy Forum set the stage for on-going policy consultations, but the work is only beginning.

** The Central Africa Policy Forum was organized by CGAP in partnership with the Central African Central Bank and Banking Commission, the European Union, the*

French Ministry of Foreign Affairs, the French Development Agency, the FIRST Initiative, the United Nations Advisors Group on Inclusive Financial Sectors, and Making Finance Work for Africa.

BEHIND THE HEADLINES: Policy Change in Africa

An interview with Jennifer Isern, CGAP lead microfinance specialist

According to recent headlines, things in Africa are looking up. In January, the Economist, called it "Booming Africa," saying that growth on the continent may hit a record 6.4 percent in 2008 and poverty rates are dropping.

A recent CGAP survey found that funders continue to enthusiastically support access to finance as a strategy to contribute to improving the lives of Africa's poor--and that a major focus of their funding is policy work. The importance of policy change is clearly not lost on microfinance practitioners and clients on the ground: the Uganda Monitor thought a European Commission delegation's recommendation to regulate savings and credit cooperative organizations (SACCOs) was news the general public would want to hear.¹

In this context, we asked Jennifer Isern how policy can help support these positive trends.

1. What are current challenges in the regulation and supervision of access to finance in Africa?

We've seen considerable progress in Africa in developing laws and regulations that include microfinance institutions (MFIs). However, actual implementation of these laws remains a daunting challenge, especially for effective reporting and supervision of MFIs. Countries like Cameroon, Benin, Senegal, Uganda, and others have hundreds of small MFIs; but the decentralized operations of many MFIs often make it hard for supervisors to monitor their activities.

It's also a real challenge for authorities to keep up with the rapid pace of development, with new institutions and business models growing up--new "greenfield" banks and finance companies, mobile phone banking, and banking operations outsourced to retail agents.

In at least 10 countries in sub-Saharan Africa, member-owned financial cooperatives

are still supervised by generic cooperative departments outside the central bank, banking commission, or ministry of finance, which raises concern. In fact, supervising financial cooperatives was one of the major themes of CGAP's recent Central Africa Policy Forum in Yaoundé.

Overall, the first priority for regulators should be supervising large institutions that mobilize public deposits. Regular reporting on key financial indicators may be sufficient for credit-only institutions. (See CGAP's guiding principles on regulation and supervision of microfinance.)

2. But few African MFIs share their financial information publicly. How is this being addressed?

Banking commissions or other specialized bodies are developing accounting frameworks and reporting standards for MFIs to provide regular disclosure on financial and operational information in places like the West Africa Monetary Union (eight countries), the Central African Economic and Monetary Union (six countries), the Democratic Republic of Congo, and Madagascar. This transparency in reporting on pricing, financial results, and operations can be an effective way to promote consumer protection and overall market discipline. But there's always a cost-benefit to consider, because any reporting costs will be added to the overall cost of financial services paid by clients.

MFI professional associations have a useful role to play in analyzing the financial and operational results of their members, and global databases, such as the MIX Market, provide benchmarking of results by country, region, institutional type, and so on.

3. High interest rates in microfinance have been receiving a lot of attention lately. What are the issues in Africa?

With all the debate over the perception of high microcredit interest rates, it's worth noting that these rates have been dropping fairly fast. From 2003 to 2006 global rates dropped 2.3 percentage points per year² because of better institutional efficiency and increasing competition. While it's certainly the case that there are a few MFIs out there charging unreasonable rates, we think that most microcredit borrowers are paying rates that are basically fair in light of the loan sizes and early stage of the industry in most countries. The rates offered by most MFIs compare favorably to informal finance, supplier credit, and the few other alternatives that would be available to MFI clients.

Many countries try to address the interest rate question by imposing interest rate caps. However, in developed countries, studies seem to show that interest rate caps restrict the supply of credit to higher risk and lower income borrowers. The question of caps remains controversial in many developing countries.

In sub-Saharan Africa, interest rates also dropped at a rate of 1.4 percentage points from 2003 to 2006, but 19 out of 48 countries have imposed some type of interest rate cap (though several countries have lifted restrictions in recent years).³ But putting legal limits on the interest that MFIs can charge is tricky business. In theory, it would be possible to set a cap at an appropriate level--one that allows enough room for the unavoidably high costs of making tiny loans. But as a matter of practical politics, governments are unlikely to set caps that high, because even appropriate microcredit rates sound excessive to most people because they don't understand the reasons for them.

4. So what are some other ways African governments can address the interest rate issue?

Instead of interest rate caps, we recommend focusing on transparent pricing and promoting competition in the microfinance market, even though we recognize that neither of these is guaranteed to lower interest rates to an optimal level in every country market. CGAP is working with African policy makers and practitioners to help develop clear pricing, benchmark performance at national and international levels (MIX Market), and use new, more efficient banking technologies. We're also supporting stronger MFI operations through MFI training, information system support, financial statement audits, and external ratings.

5. What about consumer protection? As financial sectors around the world become more competitive, with more players and a broader range of services, governments are starting to consider consumer protection laws. So far in Africa, only four countries have enacted such laws for financial services. How does this affect clients?

At the moment, awareness of consumer protection is in its early days in the microfinance industry, but this awareness is definitely growing. Ensuring transparency and fair treatment of clients is key for good lending practices. And new services, like deposits, insurance, remittances, and lease financing, each raise its own distinct protection concerns, as do rapid advances in branchless banking.

In Africa, very little information on consumer protection is readily available, but a recent CGAP policy survey found that only South Africa, Malawi, Kenya, and Mauritius have enacted consumer protection laws for financial services; while Uganda has a draft under consideration. However, 20 countries have legislation requiring financial institutions to disclose certain information on pricing and contractual terms of services. Overall, these measures for greater transparency and disclosure of the fees and contract terms are a positive step that will help protect clients.

Some microfinance associations and international organizations are also advocating

codes of conduct in disclosing information and overall fair treatment of clients. National microfinance associations in Uganda, Benin, and Ghana have been working on different aspects of this for several years. As you probably know, the SEEP Network and ACCION are also advocating codes of conduct. We would like to see these adapted to other countries throughout Africa so that the microfinance industry itself is more active in promoting client protection.

For more information, refer to:

Microfinance Consensus Guidelines: Guiding principles on regulation and supervision of microfinance, CGAP 2003.

Regulation and Supervision of Microfinance, CGAP Donor Brief No. 12, May 2003.

Working with Savings and Credit Cooperatives, CGAP Donor Brief No. 25, August 2005.

Are Microcredit Interest Rates Exploitative? An interview with CGAP microfinance expert Rich Rosenberg, CGAP Portfolio, February 2008.

CGAP Reflections on the Compartamos Initial Public Offering: A Case Study on Microfinance Interest Rates and Profits, CGAP Focus Note 42, June 2007.

Competition and Microcredit Interest Rates, CGAP Focus Note 33, February 2006.

Protecting Microfinance Borrowers, CGAP Focus Note 27, May 2005.

Interest Rate Ceilings and Microfinance: The Story So Far, CGAP Occasional Paper 9, September 2004.

Microcredit Interest Rates, CGAP Occasional Paper 1, revised December 2002.

¹EU Delegation Chief Calls for Saccos Law, The Monitor (Kampala), 28 January 2008.

²Based on 175 MFIs for which MIX has data for the relevant years, weighted by gross loan portfolio. Note that these rate drops differ from the estimate in Are Microcredit Interest Rates Exploitative? An interview with CGAP microfinance expert Rich Rosenberg because they are updated, cover a shorter period, and are weighted differently.

³Thirteen countries have interest rate caps that are specifically for MFIs: the eight countries in the West African Monetary Union, Namibia, South

Africa, Mauritania, Nigeria, and Guinea. The six countries in the Central Africa Monetary Union have an interest cap for banks only. The caps range widely from 4 percent above the discount rate (Nigeria) to 20 percent plus 2.2 times the repurchase rate (South Africa). A few countries have restricted interest rates or profit margins for specific services, such as agricultural loans (Nigeria) or Islamic lending (Sudan) or institution type (cooperatives in Ghana).

FRONTIERS AND INNOVATIONS

Access to Finance in Malawi:

Could branchless banking transform the financial sector?

In Malawi, approximately 90 percent of the population is unbanked. But there may well be a solution at hand. Over four million Malawians—60 percent of the population—are already prime candidates to receive financial services via branchless banking.

Obstacles to outreach

As of June 2006, Malawi's nascent microfinance industry had at least 192,000 loans outstanding (US\$21 million) and 244,000 depositors (US\$23 million).¹ While the country boasts a healthy variety of microfinance providers, large government-owned programs dominate the sector and inadvertently distort the market. Almost all of Malawi's microfinance institutions (MFIs) are constrained by limited financial resources, outreach, and sustainability. Demand may be as much as five times the level of supply.²

The rural challenge

Microfinance providers have a good presence in Malawi's rural areas, where 86 percent of its population lives. However, Malawi's rural economy faces tough obstacles to increasing access to finance—mostly because of poor physical infrastructure (electricity, roads, and telecommunications) and dependence on rain-fed agriculture, which is highly vulnerable to variations in the weather.

Pioneers already experimenting with branchless banking

The good news is Malawi is in an excellent position to dramatically increase outreach via technology. "Such innovation is already happening at the lower end of the market, which puts Malawi among a unique group of countries where branchless banking has the potential to 'transform' the financial sector, rather than simply provide an additional method of access," says Mark Pickens, CGAP technology expert.

Branchless banking pioneer First Merchant Bank (FMB) gives tobacco farmers a debit card for payments and withdrawals via point-of-service (POS) terminals at 60 locations of retailer Farmer's World, while Opportunity International Bank of Malawi (OIBM) provides microfinance services via smartcard to 70,000 clients. OIBM also joined forces with Concern Worldwide for a short-term program delivering emergency cash transfers to food-insecure households.

Financial infrastructure constraints

Yet, for branchless banking to flourish in Malawi, "there's still work to be done," says Pickens. To start, Malawi's main provider of smartcards, Malswitch, has not yet been able to implement them in "off-grid" areas. Meanwhile, some banks are pursuing Visa-certified platforms and magnetic stripe cards instead of smartcards, putting Malawi on a path to developing parallel payments infrastructures.

Regulatory concerns

Nor is the necessary regulation currently in place.³ It's unclear if using agents outside of bank branches is permitted and for what services. Malawi's Money Laundering Act may hamper access to finance by increasing client information requirements, though it does appear to allow agents to perform critical know-your-customer (KYC) functions. Malawi's Banking Act also appears to forbid nonbank participation in banking business; however, a new draft Payments System bill could change that.

Fortunately, Malawi's policy makers and regulators have a good grasp of these issues and are actively reviewing the situation.

Branchless banking: Big business for Malawi?

At present, Malawi Savings Bank is exploring servicing very poor markets using smartcards, but it is the only other mainstream commercial bank, beyond FMB and OIBM, considering using technology to go down market. This is likely because of the very healthy profits already enjoyed by the commercial banking sector in Malawi. Mobile operators TNM and Celtel have so far reached only 6 percent of the market for voice customers alone, providing little incentive for launching a mobile-based payment or banking platform.

Strong revenue potential

Malawi's banks may well change their tune on using technology to go after low-income clients if one of the early pioneers realizes the potential of its early success. What's more, the Government of Malawi is responsible for a huge volume of regular payments, which could encourage innovation.⁴ Some 16 million transactions are completed every year between agricultural subsidy payments and disbursement and repayment of microfinance loans. If a bank captured just one-quarter of these at a reasonable fee,⁵ they would yield US\$4.2 million in fee income—adding 23 percent to gross revenue for a typical medium-sized bank in Malawi.

Donors are game

Malawi's donors are also keen to support more experiments to advance the potential of branchless banking. DFID, USAID, the World Bank, and UNICEF are all looking at how to do more with smartcards.

Ultimately, more than 100,000 low-income Malawians already use one of the new electronic payment and savings instruments—a strong sign, considering customers of Malawi's commercial banks number just 275,000. While branchless banking in Malawi is in its early days, the possibilities are very promising.

For more information, refer to:

Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance, CGAP Focus Note 43, January 2008.

CGAP Technology Program Web site

Use of Agents in Branchless Banking for the Poor: Rewards, Risks, and Regulation, CGAP Focus Note 38, October 2006.

1 If including voluntary deposits, the number of savings accounts rises to over one million.

2 *Expanding Financial Services in Malawi*, UNCDF, 2007.

3 For more information on regulating branchless banking, refer to Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance, CGAP Focus Note 43, January 2008.

4 These regular payments include salaries and pensions for current and past workers, annual delivery of agricultural subsidies to more than two million households, and agricultural and microfinance loans via MFRC and Malawi Savings Bank. The agricultural subsidy program alone is budgeted at MK 10.7 billion (US\$77 million) for payments and administration to deliver an estimated 4.2 million individual subsidy payments.

5 This projection assumes a low-income friendly transaction fee of MK125 (US 89 cents), which is less than what Malswitch and VISA charge.

DATA DOWNLOAD: 2007 CGAP Regional Funder Survey: Sub-Saharan Africa

40%*

* In sub-Saharan Africa, amount of funding concentrated in top six funded countries (2007).

In 2005, CGAP began surveying funders working in Africa to increase access to finance. In 2007, despite an expected slight decline in global official development assistance, CGAP's survey found that sub-Saharan Africa still draws attention from funders and aid to increase access to finance continues to rise.

In 2007, the 39 respondents to the survey had total commitments of US\$4.2 billion, covering 730 projects in all 48 countries in sub-Saharan Africa. Between 2006 and 2007, committed funding increased by 6 percent, and the number of projects increased by 61 percent. This number includes funding from a wide variety of funders, though most are noncommercial using public monies.

In contrast, a CGAP survey of microfinance investment vehicles (MIVs)--private funds that typically have a more commercial orientation--reports that MIVs invested only US \$69 million in sub-Saharan Africa out of US\$2.7 billion globally in 2006.

Funding Amounts per Country

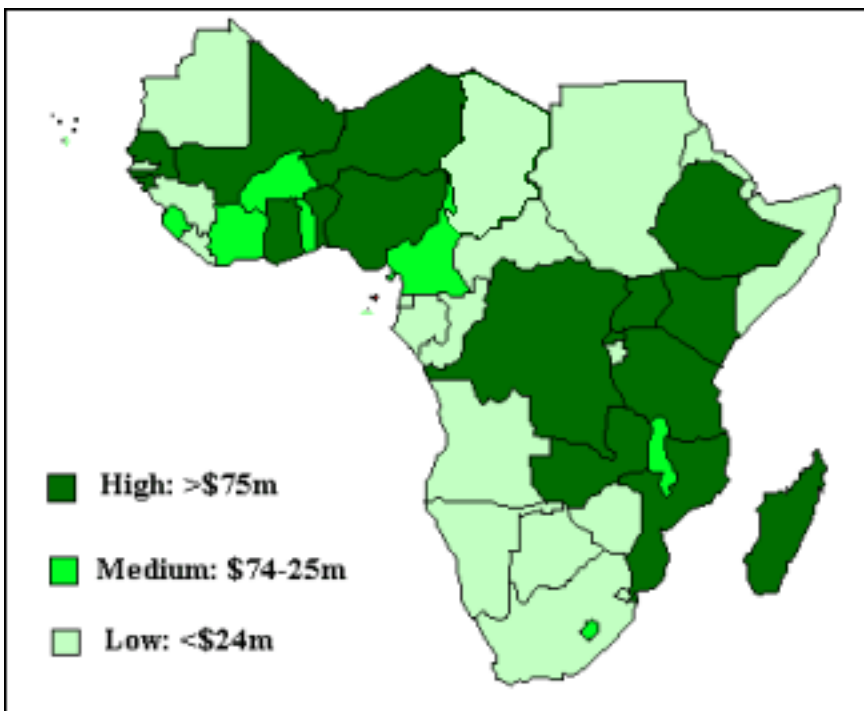
Funding is heavily concentrated in East Africa and certain countries in West Africa (Figure 1), with Uganda having the largest number (62) of financial access programs.

Figure 1: Funding Amounts per Country (US\$)

Funding is least concentrated in Central and Southern Africa. However, funders are increasingly investing in regional projects rather than country-specific ones.

Six countries (Ghana, Tanzania,

Madagascar, Uganda, Nigeria, Mali) account for over 30 percent of total committed funding; the 20 least funded countries account for only 2 percent.



For country-specific information in sub-Saharan Africa consult the [2007 CGAP Regional Funder Survey interactive map](#).

Figure 2: Funding Amounts per Country

High funding amount (≥ \$75 million)	GNI per capita <i>Atlas method</i> (current US\$)	Medium funding amount (\$25 – 74 million)	GNI per capita <i>Atlas method</i> (current US\$)	Low funding amount (≤ \$24 million)	GNI per capita <i>Atlas method</i> (current US\$)
Ghana	380	Togo *	310	South Africa ●	3630
Tanzania	320	Burkina Faso *	350	Chad *	340
Madagascar *	290	Cote d'Ivoire	760	Cape Verde *, ●	1630
Uganda *	250	Cameroon *, ●	880	Angola ●	940
Nigeria	400	Lesotho *, ●	720	Guinea *	440
Mali *	330	Malawi *	160	Sudan *	520
DRC *	110	Sierra Leone *	210	Mauritania *	510
Kenya	470			Burundi *	90
Senegal *	600			Gambia *	270
Benin *	450			Comoros *	550
Ethiopia *	130			Congo ●	750
Mozambique *	270			Zimbabwe	570
Niger *	210			Central African Republic *	310
Rwanda *	210			Somalia *	N/A
Guinea Bissau *	160			Namibia ●	2380
Zambia *	400			Gabon ●	3920
				Equatorial Guinea *, ●	3200
				Djibouti ●	1060
				Eritrea *	160
				Liberia *	110
				Mauritius ●	4670
				Swaziland ●	1670
				Sao Tome and Principe *	N/A
				Seychelles ●	8130
				Botswana ●	4430

* Least developed countries as defined by the United Nations (see methodology section, page 8)
● Lower and upper middle income countries as defined by the World Bank (see methodology section, page 8)

Funding by Activity Levels of the Financial System

Access to finance projects are distributed among three types of activities:

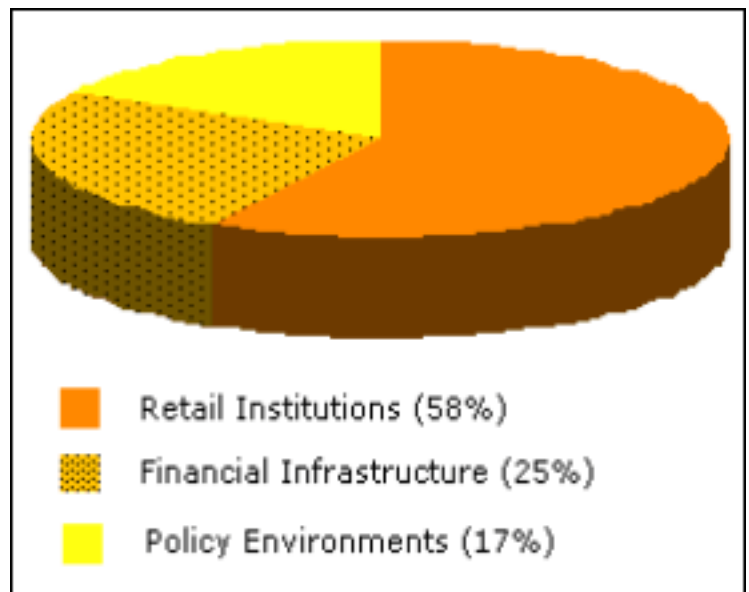
- **Retail institution projects** (58%) support a wide range of financial and nonfinancial institutions.
- **Financial infrastructure projects** (25%) support locally available market infrastructure and services, including auditors, rating agencies, networks and associations, credit bureaus, transfer and payment

Figure 3: Projects by Activity Level

% based on the number of projects

systems, information technology, and technical service providers.

- **Policy environment projects** (17%) support government policies and systems, including laws and regulations and enforcement bodies, such as banking supervision.



Retail Institution Projects*

- Capital for MFIs: 64%
- Technical assistance: 31%
- Other: 5%

Financial Infrastructure Projects*

- Capacity building: 55%
- Infrastructure: 21%
- Refinancing: 14%
- Other: 9%

Policy Environment Projects*

- Regulation/Supervision: 45%
- Broader policy support: 45%
- Other: 10%

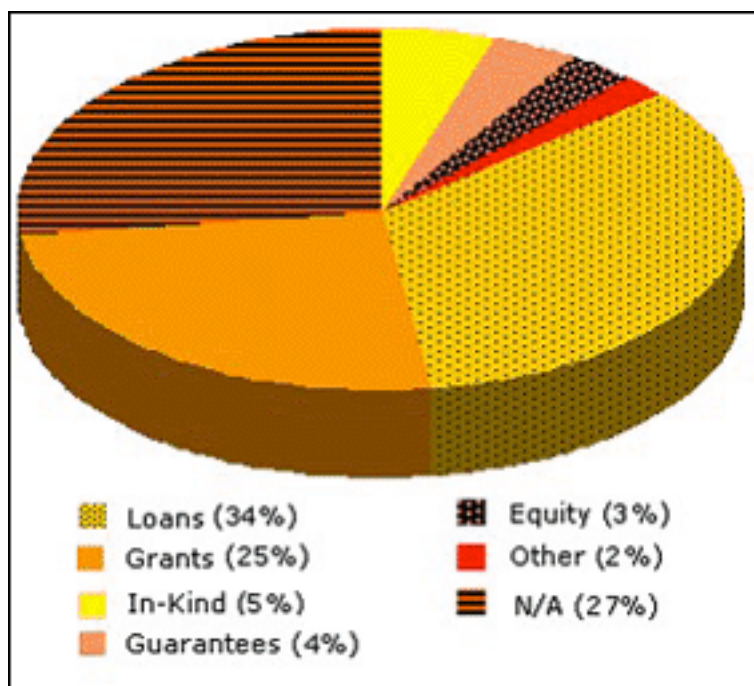
** (% based on the number of projects)*

Funding by Funding Instruments

Funders use a range of instruments, but they favor grants (46%) and loans (24%). Bilateral and multilateral funders and international NGOs are the main providers of grants; loans are funded primarily by DFIs, MIVs, foundations, and international NGOs. In-kind funding (4%) is typically coupled with either a loan or a grant. Guarantees (3%) and equity funding (2%) comes largely from development finance institutions.

Figure 4: Funding Instruments

% based on funding amounts



Maximizing Funders' Effectiveness in Supporting Access to Finance in Sub-Saharan Africa

Funding is increasing in sub-Saharan Africa, and projects are becoming increasingly complex and interdependent (multiple donors and multiple countries). Before launching a new program, funders should talk to others who are already active in the country to determine priority needs and where they can best add value.

2007 Respondents

AECI, AfDB, AFD, CIDA, DFID, the Dutch Platform (MoFA Netherlands, FMO, DOEN Foundation, Rabobank Foundation, Triodos DOEN Foundation, Oikocredit, Triodos Fair Share Fund, Cordaid, ICCO, Oxfam Novib, HIVOS, Hivos Triodos Fund), EIB, EC, FCSS (Fonds de contrepartie Sénégal-Suisse), FIRST, Gates Foundation, GTZ, IFAD, IFC, ILO, IMF, JBIC, KfW, Luxembourg Development Cooperation, MCC, MoFA Finland, MoFA France, NORAD, SDC, SIDA, UNCDF, USAID, the World Bank (IBRD, IDA).

For more information, refer to:

Elements of Donor Effectiveness in Microfinance: Policy Implications, CGAP, 2004.

Good Practice Guidelines for Funders of Microfinance, CGAP, 2006.

The CGAP STAR tool: a user-friendly, self-assessment mechanism for funding agencies.

¹ *Finance & Development*, December 2007, "Changing Aid Landscape," p. 20-21.

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