Microfinance in Mozambique
Achievements, Prospects & Challenges


A report of the Mozambique Microfinance Facility

Prepared by Fion de Vletter • June 2006

MICROFINANCE IN MOZAMBIQUE
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ABREVIATIONS AND ACRONYNMS

Names of microfinance operators are listed in Portuguese

ADB	African Development Bank
ADCR	Associação para o Desenvolvimento de Comunitárias Rurais
ADEM	Agencia de Desenvolvimento Economico da Provincia de Manica
ADEMO	Associação dos Deficientes Moçambicanos
AFD	Agence Française de Développement
AJAM	Associacao dos Jovens Agricultores de Mocambique
AKSM	Associaçao Kwaedza Simukai Manica
AMF	Actividades de Mico-finanças
ADF-AMINA	African Development Fund Microfinance Initiative for Africa
AMODER	Associação Moçambicana Para o Desenvolvimento Rural
AMODESE	Acção Moçambicana Para o Desenvolvimento
APROPEC	Associação para a Promoção de Pequenos Empresários de Cuamba
ASCA	Accumulative Savings and Credit Association
AusAid	Australian Agency for International Development
BCI	Banco Comercial e de Investimentos
BCM	Banco Comercial de Moçambique
DevPar	Development Partnerships
BIM	Banco Internacional de Moçambique
BOM	Banco Oportunidade de Moçambique
BoM	Bank of Mozambique
BPD	Banco Popular de Desenvolvimento
CCC	Caixa Cooperativa de Crédito
CCCP	Caixas Comunitárias de Crédito e Poupança
CCM	Conselhos Cristão de Moçambique
CCOM	Caixas Comunitárias de Operadores de Microfinanças
CFD	Caisse Française de Développement
CGAP	Consultative Group to Assist the Poor
CIDA	Canadian International Development Agency
CLUSA	Cooperative League of the USA
CMMEA	Cooperativa de Crédito dos Micro-Empresários de Angónia
CMN	Caixa das Mulheres de Nampula
COCAMO	Cooperation Canada-Mozambique
CPC	Cooperativa de Poupança e Crédito SCRL
CPSFR	Center for the Promotion of Rural Financial Services
CRER	Crédito para Empresarios Rurais
CRESCE	Crédito Sustentável para o Crescimento de Empresários
DANIDA	Danish International Development Agency
DED	German NGO
DM	German mark
DNCI	Direcção Nacional de Comércio Interno
DNDPR	Direcção Nacional de Promoção Desenvolvimento Rural
ECI	Ebony Consulting International
EU	European Union
FAO	Food and Agriculture Organization
FARE	Fundo de Reabilitação Económica
FCC	Fundo de Crédito Comunitário
FDC	Fundo de Desenvolvimento Comunitário
FDM	Fundo do Desenvolvimento da Mulher
FEF	Frederich Ebert Foundation
FFP	Fundo de Fomento da Pesca
FFPI	Fundo de Fomento de Pequena Indústria
FISH	Financial Services for Households
FSTAP	Financial Services Technical Assistance Project
FOS	Belgian NGO

GAPI	Sociedade de Promoção de Pequena Industria
GGLS	Group Guarantee Loans and Savings
GITMIF	Informal Working Group on Microfinance
GPE	Gabinete de Promoção de Emprego
GPIMF	Group of International Partners for Microfinance
GPPE	Gabinete de Promoção de Pequenas Empresas
GTZ	Gesellschaft fuer Technische Zusammenarbeit
IA	Impact Assessment
ICC	International Capital Corporation
IDIL	Instituto Nacional de Desenvolvimento da Indústria Local
IDPPE	Instituto Nacional de Desenvolvimento da Pesca de Pequena Escala
IFAD	International Fund for Agricultural Development
IFB	Training Institute for Banking
ILO	International Labour Office
ILRP	Inhambane Livelihoods Rehabiliation Project
INDER	Instituto Nacional para o Desenvolvimento Rural
IOM	International Organization for Migration
IPC	Internationale Projekt Consult
IRAM	Institut de Recherche et d'Application des Méthodes de Développement
ISCOS	Italian NGO
ITER	Italian NGO
KfW	Kreditanstalt fuer Wiederaufbau
LFS	Luso Financial Services
LWF	Lutheran World Federation
MEDA	Mennonite Economic Development Associates
MFI	Microfinance Institution
MIC	Ministério da Indistria e Comércio
MMF	Mozambique Microfinance Facility
MOLISV	Italian NGO
MPD	Ministério da Planificação e Desenvolvimento
MT	Metical (national currency)
NGO	Non Governmental Organization
NORAD	Norwegian Agency for Development
OJDR	Organização da Juventude para o Desenvolvimento Rural
OMM	Organisação das Mulheres Moçambicanas
OPMAD	Organização de Apoio a Proteção do Meio Ambiente e os Desprotegidos
ORF	Open Reintegration Fund
PAPIR	Projecto de Apoio às Pequenas Indústrias Rurais
PAR	Porfolio at risk
PARPA	Plano Para Redução da Pobreza Absoluta
PCR	Poupança e Crédito Rotativo
PDPME	Project for the Development of Small and Medium Enterprises
PRE	Programme for Economic and Social Rehabilitation
PREI	Industrial Enterprise Rehabilitation Programme
PROMIZA	Projecto de Microfinanças de Zambézia
PRU	Urban Rehabilitation Programme
RFSP	Rural Finance Support Programme
ROSCA	Revolving savings and credit associations
SDC	Swiss Agency for Development and Cooperation
SIDA	Swedish International Development Agency
SNV	Dutch NGO
SOCREMO	Sociedade de Crédito de Moçambique
UEM	Universidade Eduardo Mondlane
UGC-CCP	União Geral de Cooperativas - Cooperativa de Poupança e Crédito SCRL
UNCDF/SUM	United Nations Capital Development Fund/Special Unit for Microfinance
UNDP	United Nations Development Programme
UNICEF	United Nations International Children and Education Fund
USAID	United Sates Agency for International Development

USD	United States Dollars
VSL	Village Savings and Loans
WOCCU	World Council of Credit Unions
WRI	World Relief International

Currency Reference: Where dollar ($) figures are used in the text it is US dollars that is meant unless otherwise indicated. The exchange rate used is $1.00 = 25,000 Meticais (MT), the approximate average rate over the period 2004-2005.

FOREWORD

Ending extreme poverty, the aspiration of the Millennium Development Goals, is the overriding development objective of the 21st century. Despite great progress, one fifth of the people on Earth live on less than USD $1 a day. It is against this background that the UN General Assembly designated 2005 as the International Year of Microcredit, requesting a special occasion for supporting microfinance programs and initiatives throughout the world.

The Secretary General Kofi Annan, during his opening speech of the International Year of Microcredit, urged that if we are to reach the **Millennium Development Goals**, more effective use needs to be made of tools such as microfinance. He reinforced the fact that microfinance is **not charity** but a way to extend the same rights and services to low-income households that are available to everyone else.

The International Year of Microcredit itself had three main objectives. Its first objective was to increase *awareness* of microfinance and the conditions in which it can flourish. Second, to fill the *information gaps* about who has access to what financial services, at what cost, what impact this access has, and finally why access is currently limited. Third, to engage governments to ensure that their fiscal, macroeconomic, regulatory and supervisory policies support rather than stunt the availability of microfinance, and for multilaterals, donors, NGOs and private-sector institutions to treat microfinance as a serious *part of the financial sector and as a business concern.*

In order to ensure follow-up on the different initiatives in microfinance the “United Nations Forum to Build Inclusive Financial Sectors” was organized in November 2005. Participants were satisfied with the results but highlighted the ***lack of reliable data on financial services available for microfinance clients, and data on what services are actually used and needed*** by them.

In Mozambique, important activities have been initiated since the launch of the year. Participation in the Global Micro Entrepreneurship Awards was assured and an enabling legal framework was approved and is now being implemented. Furthermore, the National Microfinance Policy and Strategy under formulation was finalized and disseminated to different stakeholders, and an important ADB - IFAD Rural Finance Support Programme was launched.

Nevertheless, the ***information gap on different services and experiences available in Mozambique*** remains evident. Taking also into account the worldwide recognition of microfinance as an important poverty alleviation tool, the need for a comprehensive analysis of different experiences on microfinance in Mozambique was felt. Therefore, a partnership was established between Mozambique Microfinance Facility (MMF) and the United Nations Development Programme (UNDP) for the elaboration of this document, analyzing the lessons learned during the past ten years of microfinance in Mozambique.

This report offers an extensive overview of the development of microfinance in Mozambique, to enable a better understanding of which programmes and methodologies have been successful. By elaborating this report, UNDP aims to contribute to a more efficient use of this important poverty alleviation tool.

Finally, the report shows that it is highly probable that the Government’s 2005 target of 100,000 microfinance clients in Mozambique has been reached. Not withstanding, a major challenge lies ahead for all actors involved, namely making microfinance available in the rural areas of Mozambique.

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CANADIAN INTERNATIONAL DEVELOPMENT AGENCY

UNITED NATIONS DEVELOPMENT PROGRAMME

Preface

The Mozambique Microfinance Facility (MMF) is pleased to share the information contained in this report with the microfinance community in Mozambique and beyond. The nature and scope of microfinance activity in Mozambique has undergone significant change since the first microfinance summit in Mozambique in 1998. This account traces that development and assesses the status of microfinance activity in Mozambique today.

During the past six years the MMF has provided support to the microfinance sector through its partnership with a number of emerging microfinance institutions (MFIs). Its main contribution has been the provision of technical assistance to MFIs and support of the Bank of Mozambique in its efforts to develop legislation and regulations to govern this sector.

During its tenure, the MMF has worked closely with the Government of Mozambique through the Direcção Nacional da Promoção do Desenvolvimento Rural (DNPDR) and the Ministério da Planificação e Desenvolvimento (MPD) with the financial support of the Canadian International Development Agency (CIDA).

This survey of the microfinance scene in Mozambique brings together information that has previously been scattered and undocumented while also providing a current picture. Though it may not be comprehensive in every detail it will serve as a valuable historical record and resource for practitioners and those wanting to become better acquainted with the sector.

The MMF is grateful for the cooperation, partnership and financial contribution of the United Nations Development Programme (UNDP) in this venture. The United Nations Year of Microcredit 2005 was a significant motivator for this project. As well, thanks are offered to those in the microfinance sector who provided information through the surveys and interviews.

Appreciation is extended to Fion de Vletter who used his extensive experience in the microfinance sector, his considerable network and a personal tenacity to gather and compile the information for this survey. A significant contribution to the material in this document came from work done in the sector by Gabrielle Athmer and Katia Ribeiro Daude whose contributions have enhanced the value of this report.

This report should provide an opportunity for reflection and stimulate dialogue that can contribute to the further growth and development of microfinance in Mozambique. In the end, that kind of thoughtful review will, it is hoped, result in even more extensive and effective access, by those on the economic margins, to credit on reasonable terms and an opportunity to invest their savings with confidence.

Allan Sauder, President
Mennonite Economic Development Associates (MEDA)
on behalf of the joint venture partners in MMF
Development Partnerships Inc. (DevPar) and MEDA

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MEDA

DevPar Group

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This study has been given considerable extra value by the decision of the Dutch Microfinance Platform to allow the results of the Poverty Assessment and Impact Study of three urban MFIs to be presented (see Section 3.1). These findings are the culmination of some two years of research on urban microfinance clients in Maputo. I would like to thank all those involved in that study for the opportunity to disseminate this important information, especially Gabrielle Athmer, the team leader, who co-authored Section 3.1.

I would like to thank Katia Ribeiro Daude for volunteering to write a brief summary of her initial doctoral research on the rural clients of the Caixas Comunitárias de Operadores de Microfinanças (CCOM) project, previously known as the Caixas Comunitárias de Crédito e Poupança (CCCP) project (see Section 3.2).

In particular I would like to thank Pierre Martin of the Mozambique Microfinance Facility (MMF) who originally conceived this study and invited me to undertake it. I would also like to thank Lizbeth Martell of the MMF for her support and for providing me with her earlier research on microfinance operators.

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1.0 COMING OF AGE: A REVIEW OF THE PAST DECADE

1.1 Introduction

This study is in part a symbolic tribute celebrating the United Nations International Year of Microcredit 2005 – but it goes well beyond that intent. The report spans more than a decade of microfinance activity in Mozambique and, evolving from what some felt to be an "experimental curiosity", it seemed that this global celebration of microfinance provided a good opportunity for a "stocktaking" of an industry coming of age. Moreover, with the Government of Mozambique having set itself the objective of serving 100,000 microfinance clients[1] by the year 2005[2], it was an appropriate time to see how close the industry came to achieving that target.

This report should also be seen in the context of the Statement of the Advisors Group to the United Nations International Year of Microcredit 2005[3] (see Annex 5). The statement indicated that the year would be a success if it achieved the following three goals:

- If it increased awareness of microfinance and the conditions in which it can flourish.
- If it contributed to filling the information gaps about who has access to what financial services, at what cost, what impact this access has, and why access is currently limited.
- If it secured the commitment of governments to ensure that their fiscal, macroeconomic, regulatory and supervisory policies support rather than stunt the availability of microfinance, and of multilaterals, donors, NGOs and private-sector institutions to treat microfinance as a serious part of the financial sector and as a business concern, not an act of charity.

It was decided by the Mozambique Microfinance Facility (MMF) that the best way to increase the awareness of microfinance and to fill the information gaps would be to conduct a survey of all the known microfinance operators[4] in the country. As such, 32 active operators[5] were identified[6], allowing a comprehensive assessment of the microfinance sector based on a full set of data from all but one operator[7]. The information obtained from the survey allows the reader to know what products are being offered by which operators and by specific area. Moreover, the information obtained from the survey allowed comparisons with earlier surveys in order to assess the level of progress made within the sector.

[1] Microfinance clients include borrowers with loans of less than $1,000 and savers with current or term deposits with entities considered to be microfinance operators (see definition of microfinance operators in footnote 5).
[2] See the text box on page 2 for details.
[3] United Nations Forum to Build Inclusive Financial Sectors, United Nations Headquarters, New York, 8 November 2005.
[4] This study uses the same definition for microfinance operators as used by the 1998 Mozambique Microfinance Study, that is, "Microfinance institutions in Mozambique are defined as non-governmental organizations (NGOs) and/or private institutions providing i) financial services including both credit and/or savings targeted at the poor; ii) financial services delivered by multipurpose NGOs intending to separate this activity from others; iii) loans or average deposits of less than $1,000 and iv) financial services in monetary form". Some exceptions were made which are explained in the survey methodology in Chapter 2.
[5] The term microfinance *operators* is used in this study rather than microfinance *institutions* because the Mozambican financial legislation considers only a few categories of microfinance operators (commercial banks, microbanks and credit cooperatives) as "institutions". The term "operator" is the generic term in the legislation for all entities providing microfinance.
[6] It is commonly asserted (including in the National Microfinance Policy and Strategy paper) that the number of microfinance operators in the country is 45. This is based on entities registered with the Bank of Mozambique. This is a misleading figure as a large number of those registered are associations of solidarity groups belonging to the IRAM-CCCP (now CCOM and henceforth referred to CCCP-CCOM) project that should be treated as one operator. In its 2004 annual report, 10 of the 12 entities registered to perform credit operations under Decree 47/98 were associations operating under the CCCP-CCOM project.
[7] It is likely that there are other small operators, scattered in more remote parts of the country and that there are private operators located in some of the urban areas.

The publication of this report was postponed beyond the UN Year of Microcredit 2005 in order to seize the opportunity of presenting the results of a poverty assessment and impact study of the Maputo-based clients of three major microfinance institutions (MFIs). These results, arising from comprehensive research funded by the Dutch Microfinance Platform, as well as preliminary results obtained from research among rural credit clients, contribute significantly towards achieving the second aforementioned goal in respect to the issue of impact.

A detailed chronology of events, presented as Annex 4, based largely on documents collected by the author over 16 years, helps the reader to follow the evolution of the microfinance sector and to assess progress in terms of the third objective of the UN **International Year of Microcredit** relating to the roles played by the Government of Mozambique, the multilaterals, donors, NGOs and the private sector.

The rest of this chapter will briefly review the main changes that have occurred within the microfinance sector of Mozambique, looking at the historical evolution, quantitative changes (summarizing some of the main findings of the survey) as well as qualitative transitions occurring within the regulatory environment and stakeholder involvement. It also outlines some of the more recent works on microfinance in Mozambique.

Chapter 2 analyses the results of the 2005 microfinance operator survey and compares these findings with the results of earlier studies.

Chapter 3 summarizes the results of the two impact studies. Section 3.1 reviews the findings relating to the urban (Maputo) clients while Chapter 3.2 looks at the impact of microcredit on small holders in a remote area of Cabo Delgado. The urban impact study is one of the most comprehensive studies of this nature undertaken in Africa. It was therefore decided that a considerable portion of this book be devoted to it.

Chapter 4 examines what could be considered the prevailing challenge of microfinance in Mozambique and of great concern to the UN Advisors Group. The second Poverty Reduction Strategy Paper (PARPA II) gives prominence to rural development and recognizes the importance of rural finance and microfinance to promote it. Although microfinance in Mozambique has made some impressive strides in meeting the needs of the rural poor, its impact has so far been very limited. The chapter reviews what is likely to be the next take-off phase of microfinance.

Achieving the Government of Mozambique Objective of 100,000 Microfinance Beneficiaries by 2005

In 1997, at the Washington World Micro Credit Summit, the former Prime Minister Pascoal Mocumbi announced that Mozambique would set itself the target of reaching 100,000 microfinance beneficiaries. In 1998 resolution 3/98 of the Council of Ministers was passed which aimed to serve 50,000 clients through microfinance by the year 2000 and 100,000 by 2005. When the 1997 declaration was made there were barely 20,000 microfinance beneficiaries and few believed that the goal was realizable. Two developments allowed for faster growth than thought possible. One was the success of the Accumulative Savings and Credit Association (ASCA) methodology through the Revolving Savings and Credit (PCR) groups. PCR members account for almost a quarter of the total number of beneficiaries in 2005. The second has been the very rapid response to the introduction of deposit accounts by the main providers, notably NovoBanco, SOCREMO and Tchuma. By June 2005, these institutions had some 37,000 savers, substantially more than the number of borrowers. Table 1demonstrates that there are now about as many borrowers as there are savers with an estimated total of 130,814 microfinance beneficiaries who either benefit from one or both loans and savings products. The net number of beneficiaries is calculated by deducting all those clients who had been double counted. This result was achieved by deducting from the gross total of 130,814 the number of clients double counted (i.e. 27,343)[8] giving a net total of **103,471 by June 30, 2005**.

Evidence obtained from some of the major operators in early 2006 suggests that by the end of 2005, the net number of microfinance beneficiaries was likely in excess of 120,000.

[8] The number of double counted clients was obtained as follows: CMN (212 borrowers), SOCREMO (1,600 savers), Tchuma (4,803 savers), NovoBanco (12,108 savers), ADEM (318 borrowers), Ophavela (2,534 borrowers), AKSM (736 borrowers), CARE VSL (758 borrowers), Kukula (4,200 borrowers), CPC (58 savers), CCC (16 borrowers).

Finally, chapter 5 critically assesses the progress made, especially against priority concerns of the UN Advisory Group and then looks at main challenges facing the microfinance sector.

Apart from obtaining quantitative information from the microfinance operators, a major objective of this study was to be able to present descriptions and details of each of the operators identified. Annex 1 presents detailed information (as supplied by each operator) in terms of location, target groups, types financial products offered, contact persons, etc.

1.2 A Brief Historical Overview[9]

1.2.1 The Beginnings

The earliest linkage to microfinance in Mozambique can probably be traced back to the creation in 1989 of the Urban Enterprise Credit Fund established as one of the components of the World Bank's Urban Rehabilitation Programme (PRU) and executed by the Office of Employment Promotion (GPE) in the Ministry of Labour. This programme provided small loans for a variety of urban activities, including restaurants, bars, beauty salons, carpenters, fishermen, etc. This was the first attempt to establish a non-bank fund (although loans were disbursed through the state bank Banco Popular de Desenvolvimento (BPD)) and charge commercial interest rates.[10]

In 1992, with German unification, some 18,000 Mozambican contract workers were repatriated. The German Government through its technical assistance agency Gesellschaft für Technische Zusammenarbeit (GTZ) established a training and credit programme to assist the *regressados*[11] and housed the programme with the GPE. This programme soon split the training and credit activities. The credit programme then opened its doors to all existing micro-entrepreneurs in Maputo and Beira and established the seeds of what eventually became the commercial bank SOCREMO.

The signing of the Peace Accord of 1992 marked a new era for Mozambique and sparked considerable debate about the role of microfinance in the reintegration process of demobilized soldiers. The process of demobilization[12] started when microfinance was still in its nascent period and involved a myriad of organizations with a variety of views on how to approach reintegration. Much discussion was centered on whether the demobilized were to receive credits or grants. Many suggested that the GTZ-GPE *regressado* model was the path to follow but providing vocational kits (see footnote 12) as credit instead of cash, following prerequisite training. Reality showed that the demobilized soldiers had no intention of repaying, considering the training and kits as part of their rightful compensation for years at war.[13]

In 1993, World Relief announced plans to establish "village banks" for poor market women in the Chokwe area of Gaza Province. Because the scheme was so ambitious and the methodology unconventional (at the time), this initiative has generally been hailed as the first microfinance initiative in the country. Impressive results were reached, including repayment rates approaching 100%, consequently attracting various high-powered government delegations to visit the programme. These first impressions were lasting and were probably instrumental in the positive support that the financial sector has enjoyed from the government. In 1993 the French consultancy company Institut de Recherche et d'Application des Méthodes de Développement (IRAM)[14] started to undertake a comprehensive series of studies in preparation for its Caixas Comunitárias de Crédito e Poupança (CCCP) project.

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[9] For a detailed chronology of events affecting the microfinance sector, see Annex 4.
[10] At that stage a variety of sectoral government funds were established to promote activities through highly subsidized rates of interest (see Annex 4).
[11] Today they are referred to as *Madgermanes* ("those of Germany").
[12] The demobilization of former Frelimo and Renamo soldiers was complicated, involving inter alia a process of providing them with a technical skill, usually through training and appropriate equipment (kits), to reintegrate into the economy. Generally the training was hasty and inadequate and the kits were sold to obtain cash. Many ex-soldiers just returned home to their rural areas or started informal sector activities.
[13] See S. Fraser and R. Candido (2001). *Research Study of Post-Conflict Microfinance in Mozambique,* Concern World Wide; and The Springfield Center for Business Development. Also, F. de Vletter (1999), *The Evolution of Microfinance in a Successful Post-Conflict Transition: The Case Study of Mozambique* paper presented to the Joint ILO/UNHCR Workshop: Microfinance in Post-Conflict Countries, ILO, Geneva.
[14] Institut de Recherche et d'Application des Méthodes de Développement

1.2.2 Dominance by International NGOs in Rural Areas

With the exception of the GTZ-GPE programme in Maputo and Beira, microfinance in the mid-1990s was largely driven by international NGOs with experience in microfinance. These microfinance operations did not immediately target the more accessible and concentrated market of Maputo-Matola with an estimated 70-80,000 market traders. In 1995, CARE International approved their first loans (based on the solidarity group methodology), through its programme Crédito Sustentável para o Crescimento de Empresários (CRESCE)[15] with mainly market traders in Chimoio and Gondola (Manica Province). World Vision was at about the same time looking for microfinance opportunities in Tete, Nampula and Zambézia (later focusing on the latter province).

The earlier years of microfinance were dominated by the presence of small (mainly rural) international NGO initiatives introducing microfinance as one of several components for their integrated (usually rural) programmes. "Microfinance" was very much the development buzzword of this time and there was a prevailing assumption that it could be managed with much greater facility than was eventually experienced.

1.2.3 Shifting the Focus towards Urban Areas

The natural magnet for microfinance activities was Maputo and, to a lesser degree, other cities. In 1995/6 the Banco Internacional de Moçambique (BCI) and the Fundo de Desenvolvimento Comunitário (FDC) started a pilot project with Swiss funding that was the precursor of the first cooperative exclusively devoted to microfinance, named Tchuma. Tchuma significantly expanded its lending activities in 1999. In 1997 Mennonite Economic Development Associates (MEDA) was the first international NGO to establish itself in Mozambique with the primary purpose of setting up an exclusive or, as the Consultative Group to Assist the Poor (GCAP)-inspired expression put it, a "minimalist"[16] microfinance programme in Maputo. This programme, called "Kulane ka Ntwananu", started its credit operations in 1999. In 1997, IRAM launched its CCCP programme in Maputo and Chokwe on behalf of the Bank of Mozambique (BoM) using a village bank type methodology of associations of solidarity groups called *caixas comunitárias*. In 1998, SOCREMO was the first microfinance programme to become a registered financial institution, with the Government of Mozambique owning 94% of its shares. In 2000, NovoBanco, managed by the German consultancy firm Internationale Projekt Consult (IPC), started in the form of the newly created institutional category of *microbanco*. NovoBanco forms part of the worldwide ProCrédito network: 30% of the shares belonged to the Banco Internacional de Moçambique (BIM) with the rest belonging to several other international investors.[17] In Nampula, the exclusively female targeted Caixa das Mulheres de Nampula (CMN) was established in 1994 with subsequent support by Cooperation Canada-Mozambique (COCAMO).

Much of the microfinance debate during the latter half of the nineties focused on financial sustainability. Rural microfinance was considered to have little prospect of attaining financial sustainability within the commonly accepted "norm" of about five years.

1.2.4 Community Based Initiatives

While microfinance activities especially *credit* transactions were being concentrated in Maputo, CARE introduced a new methodology for remote rural communities that it developed with great success in Niger. The methodology known today as Accumulative Savings and Credit Associations (ASCAs) and in Mozambique as PCRs (*poupança e crédito rotativo)* was introduced in 1999 as part of its Crédito para Empresarios Rurais (CRER)[18] programme in Nampula. At around the same time, the methodology was also introduced to Inhambane Province through the Inhambane Livelihoods Rehabilitation Project (ILRP). In 2000, IRAM extended its CCCP programme to a remote area of Cabo Delgado Province proving that, despite the prevailing arguments about the difficulty of rural finance of

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[15] Sustainable credit for the growth of entrepreneurs.
[16] The term "minimalist" was used to describe programmes that only undertook microfinance operations vs. maximalist, the term used to describe microfinance operations at the time that commonly had supplementary components such as training, health, education, etc. attached to them.
[17] ProCredit Holding AG (25%), IFC (10.4%), Doen Foundation (20.3%), The Netherlands Development Finance Company (FMO) (10.4%) and Fundo para Fomento da Habitaçao (FFH) (3.9%).
[18] Credit for rural entrepreneurs.

reaching sustainability, it could lend to rural farmers and attain recovery rates almost equal to its urban operations[19] (see section 3.2).

1.2.5 Eclipse of the International NGOs

During the first years of the new millennium some unexpected transformations have taken place. First of all, the programmes of the pioneering international NGOs such as World Relief, CARE, World Vision and MEDA started showing declining portfolio performance, which can be partly attributed to increased competition and changing priorities at management levels since most of the NGOs were polyvalent institutions. These NGOs played the key role of opening the microfinance market at a critical time, however growth in the local industry and market changes led them to different paths. The portfolios of the CARE, World Vision and MEDA programmes were merged into the newly established Banco de Oportunidade de Moçambique (BOM) in 2005, acknowledging the changing environment and the strength of private operators in keeping sustainability a priority.

1.2.6 Growth of National NGOs

An important development within the sector has been the survival and growth of several smaller Mozambican NGOs, associations and cooperatives. Four initiatives are particularly noteworthy: the Associação Hluvuku – Male Yeru, Associaçao Kwaedza Simukai Manica (AKSM) (originally promoting village banks, but recently switching to promoting PCRs)[20], CMN and the União Geral de Cooperativas (UGC). [21] The emergence of the recently (2004) established Fundo do Desenvolvimento da Mulher Sarl (FDM) arising from the Group Guarantee Loan and Savings project (GGLS) of Save the Children (US) is also encouraging. These operators, with the exception of the UGC, have received technical assistance (mainly in the form of courses and small grants) from the MicroStart Programme and the MMF. The emergence of the five operators promoting PCR groups[22] has had a dramatic change on the nature and location of the microfinance especially in terms of savings (see sub-section 1.2.8). Of particular interest is Ophavela, an offshoot of the CRER programme. As PCR groups cannot render the promoting institution sustainable, Ophavela's success lies in the fact that PCR methodology is an attractive concept and donors are willing to pay NGOs such as Ophavela management fees to promote them in selected areas (see Chapter 4).

Some debate has arisen regarding the appropriate level of technical assistance to be offered to institutions, given the varying prospects of sustainability for some of these operators. Although management performance of such operations has been encouraging, concern has been raised about whether sufficient volumes could be generated to ensure sustainability. An important development that might guarantee the future of smaller operators has been an increasing demand by development "organizations" programmes to contract the services of microfinance providers, thus adding management fees to the sustainability equation (see Chapter 4).

In 1999, GAPI SARL, a financial institution specializing in rural credit, started a second-tier (wholesale) microfinance lending facility, until now the only local MFI-targeted source of funds. Clients to date include Tchuma, SOCREMO, UGC, FCC, as well as trader and farmers associations.

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[19] IRAM's modular approach to the CCCP model assumed the creation of 40 associations and a union per module. For the rural environment, sustainability was projected after eight years.

[20] Village banks normally depend on externally sourced credit funds, while PCRs lend money to borrowing members from savings mobilized internally.

[21] The UGC's input credit programme for chicken breeders was not considered to be part of the 1st or 2nd National Microfinance studies because of the credit in-kind factor. The UGC operation was, however, included in this study because UCG has established the microfinance cooperative *Cooperativa de Poupança e Crédito* which will lend in cash and is currently contemplating how to transfer the in-kind credit clients to the cooperative. The in-kind credit programme is worth mentioning for two reasons. First it has, despite various problems in the chicken breeding business due to cheap imports from Brazil, survived for about 15 years and continues to provide credit to almost 1,000 clients. No interest is charged on the inputs provided but half the profits derived from the inputs are given to the UGC.

[22] CARE has recently (2004) established a new PCR programme, CARE Village Savings and Loans (VSL) in Zambézia with UNDP funding. Ophavela (Nampula) and Kukula (Inhambane) were both created out of the CARE programmes CRER and ILRP respectively. The other NGOs are ADEM and AKSM (both based in Manica Province).

1.2.7 Legal Reforms[23]

Microfinance provision was regulated by Law 28/91 that did not provide for the institutional forms felt necessary for the development of the sector. Pressures exerted by the operators encouraged the BoM to issue decree 47/98 to regulate microcredit activities. Although an important step forward, these regulations did not allow operators to capture deposits and allowed the BoM to establish limits to credit (two policy options against which the Advisors Group take a strong position). The emergence of large operators and NGOs promoting PCRs which were essentially savings institutions, made it necessary for the government to introduce some alterations to the Credit Institutions and Finance Companies Law 15/99 through Law 9/2004 and the accompanying decree 57/2004 (replacing decree 47/98).

The alterations allowed for four categories of microfinance provision. Category A introduces the new category of "micro bank" which in turn is divided into 4 sub-categories (of which 3 are entitled to accept deposits from the public). Category B covers local savings and credit organizations, in particular credit cooperatives. Those entities registering as either category A or B are considered to be microfinance *institutions* and therefore subject to prudential supervision (microfinance prudential ratios are being finalized). Entities falling within categories C and D[24] are defined as microfinance *operators* and are required to register with the BoM while being subject to monitoring.

In 2005 the sub-category "microfinance bank" which allowed a minimum capital requirement of 25 billion MT vs. 70 billion MT for other commercial banks was abolished. This has led to the recent creation of three commercial banks dedicated to the provision of microfinance (despite higher capital requirements). NovoBanco registered as a commercial bank in 2004. SOCREMO switched its status from microfinance bank to commercial bank in 2005. BOM has also registered as a commercial bank. Most other institutions, apart from credit cooperatives, were still contemplating which of the four categories of operator giving the status of micro bank was the most advantageous for them.

Commercial banks, micro banks and credit cooperatives are also obliged to provide information on their credit operations to the Central Credit Registry, previously known as the Risk Centre and accessed by all contributing institutions. Because of the very different nature of the clients and institutions, the MMF, in collaboration with GITMIF, proposed to the BoM in 2004 the creation of a Risk Centre for Micro-Debtors (MICRODEV), which would also serve all categories of microfinance operators.

1.2.8 The Emergence of Savings as a Microfinance Product

Perhaps because the impact of deposit facilities for micro banks has only just started to be felt, savings (often referred to as the "forgotten half of microfinance" but necessary to obtain sustainability) have often been neglected in discussions of microfinance in Mozambique. The 2005 operator survey found that almost half the microfinance clients in the country are, in fact, savers.

While credit has largely taken off in urban areas, savings were initially the main microfinance product in rural areas initiated through PCR groups which accounted for about 25,000 rural savers in June 2005, or 40% of all microfinance savers. The number of savers in urban areas has recently surpassed those in rural areas. In 2000 Tchuma started with a stamp-based savings pilot scheme in collaboration with CARE and then introduced passbook savings in 2003. NovoBanco introduced current accounts and term deposits in 2001. SOCREMO followed suit in 2005. The major advantage that these savings products have over other commercial banks is the very low minimum deposits.[25]

[23] Readers wishing to obtain more information on legislative reform within the sector should consult the chronology in annex 4 which provides details of changes occurring by year as well as referring to the comprehensive coverage of this subject in the research paper by Marie-Charlotte Buisson (see section 1.5 for reference).
[24] Category C is comprised of microfinance operators that only provide credit while category D is comprised of microfinance operators that act as intermediaries in obtaining deposits.
[25] NovoBanco, for example, requires a minimum deposit the equivalent of $4.00 vs. and average of $218.00 for other commercial banks (see Athmer and Hunguana (2005), section 1.5 for full reference).

The case of the CMN deserves special mention. Although not yet legally registered as a cooperative, for all intents and purposes it functions as one and is one of only two cooperatives[26] in Mozambique that depends entirely on member savings for its loan capital and is approaching sustainability.[27]

1.3 Operator Achievements

The 2005 microfinance operator survey (details of which are provided in Chapter 2) allows us to measure or estimate some of the major achievements over the past decade or so. Most notable has been the growth in the number of active microfinance clients (i.e. those clients either with an outstanding loan or engaged in some form of savings at the time of the survey) that surpassed the objectives set by government for 2005, reaching approximately a total of 103,471 by mid-2005. The total value of outstanding loans[28] (active loan portfolio) of the operators covered in 2005 stood at $16.4 million (June 2005). There has been almost no change in the *number* of operators between 1997and 2005, decreasing slightly from the 35 identified microfinance operators in 1997 to the currently identified 32. However, a process of consolidation, acquisition and attrition (especially of component microfinance schemes) has resulted in what appears now to be a much more stable industry with the emergence of a large majority of operators that are devoted solely to the provision of financial services. A significant increase in the proportion of national NGOs was registered while international NGOs involved directly in microfinance provision decreased substantially. By 2005, the industry was increasingly in the hands of three commercial banks (NovoBanco, SOCREMO, and BOM). By 2005, 43% of the respondent operators had portfolios at risk (PAR)[29] of less than 3% and more than half the operators had more than 1,000 clients (two had more than 10,000). By the end of 2005 three large operators had reached operational sustainability.[30] The survey results show that the gender distribution of all microfinance clients (borrowers and savers) is remarkably balanced, given that socio-economic, cultural and religious influences have resulted in strongly skewed regional patterns.

1.4 Stakeholder Interests and Impact

As a case study, microfinance in Mozambique will not be remembered for any particularly dazzling programme or methodology but rather for the synergetic way in which all stakeholder levels – operators, government and donors – collaborated to stimulate the sector.

On the **government** side, some public institutions continue to undermine sustainable commercial credit through the provision of highly subsidized loans. This approach is against the advice of the Advisors Group which recommends that *"governments and others are restrained in their provision of subsidized capital to microfinance, and aim to deploy it in ways that encourage, not discourage, commercially-driven capital into the sector"*. This notwithstanding, there is clearly an overall pro-microfinance shift within government spearheaded by committed individuals who have played a critical role in the evolution of the industry. In particular, the efforts of the Bank of Mozambique and INDER (later the National Directorate of Rural Development and Promotion (DNDPR)) should be highlighted. The BoM has for many years sought to create an enabling legal environment for these sectors (see sub-section 1.2.7) and is currently establishing its supervisory capacity. Legislative change was generally done on a consultative basis with operator and donor involvement. With these changes, the BoM respects the good practice of combining savings and loans to ensure the long-term financial sustainability of the institutions. The role of the DNDPR has been critical, being instrumental in the production of the 1998 and 2000 microfinance studies, organizing the three national microfinance conferences, producing the National Microfinance Strategy, and heading or participating in the

[26] The other cooperative dependent on member savings is the Caixa Cooperativa de Crédito, SCRL which has only about 300 savers and 16 borrowers. The other Cooperativa de Poupança e Crédito, SCRL only has 58 savers and 1,200 borrowers (of which 640 were considered to be microfinance borrowers).
[27] Stephen Gudz, a consultant working with the CMN, states that its financial sustainability was 75% in November 2005, having increased from about 35% in the previous year.
[28] Total value of loans outstanding is defined as the value of the balance of all loans owing to a financial institution.
[29] PAR is defined as the value of outstanding balance of loans in arrears/value of loans outstanding > 30 days.
[30] The operational sustainability or operational self-sufficiency ratio is defined as financial income divided by the combined total of financial costs + operating costs + loan loss provision. The three MFIs were NovoBanco, SOCREMO and Tchuma who claim that technical assistance has been included in their calculation of sustainability.

steering committees of the country's major microfinance programmes.[31] Of significant importance has been the government's non-interventionist role in letting the microfinance sector evolve, much along the ways advocated by the Statement of the Advisors Group *"that government ownership of the financial sector is inversely correlated with access"* and that *"governments have a crucial enabling role to play in increasing access to financial services"*.

At the **donor level**, the early development of the sector was greatly assisted by the World Bank and the UNDP, in establishing the Microfinance Informal Working Group (GITMIF) and the Action Research Programme. Apart from donor promotion of microfinance at the operator level, three sector-wide initiatives have had significant impact. The UNCDF's MicroStart Programme assisted various operators through grants and technical assistance with the primary objective of building up institutional capacity.[32] The Canadian Government funded the Mozambique Microfinance Facility (MMF) which has provided technical assistance to the BoM, was the principle organizer of the 3rd National Microfinance Conference, provided technical assistance to six operators, offered financial courses, organized various workshops and maintained a quarterly database.[33] The UNDP, in conjunction with AusAid and the African Development Bank (ADB) Microfinance Initiative for Africa (AMINA) funded the Upstream Microfinance Capacity Building Project with the objective of building up the capacity of the state in terms of policy making, supervision and teaching. Research by Marie-Chalotte Buisson (2005) (see section 1.5) indicates that donors have contributed about $30 million to the sector of which 82% went directly or indirectly to individual operators and 18% to the sector as a whole[34]. Details of donor contributions to the microfinance sector presented to the Group of International Partners for Rural and Micro Finance (IPRMF) in February 2006 are presented in Annex 6.

On a different dimension, donors are playing an increasingly important role in stimulating the activities of microfinance operators through large integrated development projects, many of which include a financial component – usually microfinance. Instead of establishing in-project delivery mechanisms, donors/government tend to contract financial service providers. A good example of this is the ADB's project to support fishing communities in northern Mozambique. In terms of microfinance, the project will contract an NGO or agency to promote ASCAs as well as making available some $12 million to financial service providers (mainly microfinance) through an arrangement with the Fishing Support Fund (FFP) that would allow it to wholesale loan funds to participating operators.

In 2005 like-minded donors, at the initiative Agence Française de Développement (AFD), established the Group of International Partners for Microfinance (GPIMF), later renamed the International Partners for Rural and Micro Finance (IPRMF). This group will attempt to ensure that donors involved in microfinance support do so according to accepted best practice guidelines.[35] In the terms of reference of the IPRMF of April 2006, the general objective is to participate "*in the reduction of poverty through the support of the development of the microfinance and rural finance sectors in Mozambique, in the context of the PARPA".*

Operator interests have, until late 2005, been largely represented by GITMIF. Despite some attempts to establish better regional representation, their interests have largely been channeled through the Maputo-based informal working group that has always been open to all stakeholders. Having met regularly since 1997, the group has had an important influence over the evolution of microfinance. However, with growing sophistication of the industry and increasing specificity of stakeholder interests, GITMIF has outlived its usefulness. Although the Government has had its own Reference Group since 1999, two important developments in 2005 made GITMIF redundant. One was the creation of the

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[31] These included the MicroStart Programme and the MMF the CCCP-CCOM project and the Upstream Programme.

[32] The partner institutions were Tchuma, SOCREMO and GGLS, in the category of "organisations with potential for growth and sustainability", and Kwaedza Simukai Manica (KSM) and the Women's Savings Bank of Nampula (CMN), due to the fact that they showed opportunities for developing models for community-based financial services, which are appropriate to Mozambique's rural areas.

[33] The purpose of MMF is to strengthen the capacity of microfinance institutions in Mozambique, supplying credit to a growing number of poor people. This programme, in the amount of $4.4 million, is financed by CIDA and began at the beginning of 2000, and has its operational termination foreseen as September 2006. The partner institutions are CRESCE (now taken over by BOM), FCC, GGLS (now FDM), Karela (now taken over by BOM), Assoc. Hluvuku- Male Yeru and SOCREMO.

[34] Of the amount going to operators, 59% was in the form of loans, 21% grants, 5% equity participation and 5% others/not known.

[35] These are elaborated in: Committee of Donor Agencies for Small Enterprise Development (1995). *Micro and Small Enterprise Finance: Guiding Principles for Selecting and Supporting Intermediaries* (also known as the "Pink Book"), Donors' Working Group on Financial Sector Development, World Bank, Washington DC. Also, Committee of Donor Agencies for Small Enterprise Development (2001). *Guiding Principles for Donor Intervention*, The World Bank, Washington DC.

donors' group (IPRMF) and the second was the creation of an informal group of microfinance operators, which originally started as a working group of the largest operators, with the objective of looking at the possibility of establishing an association of microfinance operators. This group is now open to all operators in the country and by mid-May 2006 had 13 operators who had signed a protocol. The group now meets on a monthly basis. One problem that they will face is that with a widening disparity of operator types, methodologies and target groups, there is decreasing commonality of interests. There has been considerable pressure, especially from the donors and the Rural Finance Support Project (RFSP) for an association of MFIs to be established. More recently there are signs among the operators themselves that, despite their heterogeneity, such an association is likely to be formed as common interests are identified (see chapter 5 for further discussion on this topic).

1.5 Recent Studies on the State of the Microfinance Sector

In 2005 three important studies were produced reviewing certain aspects of the microfinance sector. The first, *Characteristics of the Microfinance Sector and of the Three Institutions involved in the Impact Assessment*[36] summarized the findings of phase A of the study *Poverty Outreach and Impact Assessment in Mozambique with Three Partner Institutions of Members of the Dutch Microfinance Platform* (see Chapter 3 for more details). This study provides a detailed analysis of the three largest MFIs (by portfolio) in the country, namely NovoBanco, SOCREMO and Tchuma.

The second, *A Comparative Analysis of Microfinance Institutions in the New Institutional Environment of Mozambique*[37] is a Masters thesis supported by the AFD. This study is probably the most comprehensive study available on the sector, looking at it from a wide perspective. A large majority of the microfinance operators were studied in detail, analyzing growth, location, loan sizes, etc. with the objective of showing the breadth of coverage both geographically as well as in terms of client income levels (depth of outreach). The report also provides a detailed analysis of donor involvement and contributions, the role of government and the changing legislative environment.

The third, *The Potential for Mobilizing Savings in Rural Areas*[38] was commissioned by the National Directorate for Rural Development (DNDR) through the Upstream project. The study highlights the importance of informal financial systems that are practised in the country.

[36] By Gabrielle Athmer (team leader) and Henriqueta Hunguana (ICC Mozambique).
[37] By Marie-Charlotte Buisson , First Year Masters Research Report for the Department of Faculty of Economic Analysis and International Development, Faculty of Economic Sciences Université d'Auvergne Clermont-Ferrand 1 C.E.R.D.I.
[38] By Felisberto Navalha and Sophie Teyssier.

2.0 FINDINGS OF THE 2005 SURVEY OF MICROFINANCE OPERATORS[39]

2.1 Methodology

This chapter analyzes the results of the 2005 survey of microfinance operators. The survey consisted of two questionnaires: section A requested general information about the operator including some quantitative measures such as the number of clients, gender division and value of loans outstanding. The results of that section are fully transcribed in Annex 1. The second questionnaire (section B) examined more sensitive financial data for the purposes of aggregative analysis. For reasons of confidentiality, the individual institutional responses have not been published (see Annex 2 for section B of the survey questionnaire). A total of 32 institutions were identified as offering microfinance products. In the case of the Cooperativa de Poupanca e Crédito SCRL (CPC), which has a considerable portfolio of loans exceeding $1,000, these loans and respective clients have been excluded from the analysis. In the case of AMODER, which also has a significant number of clients with loans exceeding $1,000, it was not possible to factor out non-microfinance transactions and clients due to technical problems prevailing at the time of the survey. Only one institution did not fill in the questionnaire, nevertheless useful information was obtained by requesting loan conditions. Some 22 responses were received for the second questionnaire relating to portfolio performance indicators.

It should be noted that private Mozambican operators have recently become engaged in microfinance activities. Some are conforming to conventional microfinance best practices. Others are likely to operate along similar lines to the “finance companies” (loan sharks) in South Africa. It is likely that not all of the smaller private operators have been covered by this survey.[40]

2.2 Previous Operator Surveys/Directories of the Sector

Prior to the 2005 study, there had been six initiatives to review the activities of the microfinance operators in Mozambique. The first, undertaken in 1996 was an *Inventory of Microcredit Schemes in Mozambique,* with a focus on Nampula;[41] the second was the *Survey of Microfinance Programmes in Mozambique*, undertaken in 1997 by MEDA with financial assistance from the World Bank and published in 1998[42]; the third, *The Mozambique Microfinance Study*[43] was undertaken in 1997 and published in 1998 as part of a sector overview commissioned by the Government of Mozambique[44] for presentation to the First National Microfinance Conference. The fourth report, *Study of the Microfinance Sector in Mozambique,*[45] was presented to the Second National Microfinance Conference. The Mozambique Microfinance Facility, in preparation for the Third National Microfinance Conference, undertook the fifth initiative, the *Directory of Microfinance Operators in Mozambique 2004*. This study provided details of 34 operators but was never published. The latter formed the basis of the 2005 survey (providing useful background data and contacts), although 12 of the listed operators in 2004 were either not operational, acquired by another operator or were not considered to be a microfinance operator for the purposes of the survey. Finally, in 2005, the Ministry of Planning and Development, through the Upstream Project, published the *Directory of Microfinance Operators in Mozambique* that provides details of 13 providers and their operations.

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[39] The analyses presented in this paper are drawn from the questionnaires filled out by the operators covered in the survey. No responsibility is taken for any incorrect data or information that may have been provided by employees acting on behalf of the operators. It is assumed for the purposes of the analysis that the information provided is reliable. In the case of one operator who did not wish to fill out the questionnaire, some basic information regarding loan product, eligibility and conditions were obtained from brochures and employees.
[40] Attempts were made to locate the financial operators registered with the Bank of Mozambique, namely the Crédito Popular, Policrédito, Cedi-Crédito and CBA Crédito. All had Maputo addresses but could not be found at indicated addresses.
[41] Gabrielle Athmer, SNV. This survey focused mainly on operators based in Nampula Province but also described the main operators found in the rest of the country.
[42] Prepared by Fion de Vletter and Marcelino Raimundo. This survey was undertaken on a similar basis to that of the 2005 survey. All known microfinance operators plus other non-bank financial institutions were requested to fill in a detailed questionnaire similar to the one used during 2005. Considerable data was collected but never analyzed until this study.
[43] Prepared by Anne-Marie Chidzero, Christine Frolich-Lassimo, Henriqueta Hunguana and Carlos Cuevas. The survey of microfinance operators was based on that of the 1997 MEDA survey, adding two operators that existed in 1997 but not covered by the MEDA survey.
[44] INDER, Bank of Mozambique and Ministry of Planning and Finance.
[45] Prepared by ICC, financed by MICRONET and UNDP, coordinated by CARE, in collaboration with the National Directorate of Rural Development (DNDR) of the Ministry of Agriculture and Rural Development.

Two previous surveys were used in this study, as they had the most useful data for comparative purposes: the 1997 MEDA study[46] and the ICC study of 2000.[47] Unfortunately, the methodology and information requested for the three surveys were not always consistent to allow comparisons between the surveys.

2.3 Results of the 2005 Survey and Comparisons with Earlier Surveys

Table 1 lists all the institutions that, at one stage or other, were included in the three selected surveys. Grey areas indicate that operators were not included in a survey for two reasons: they were no longer operational, or they were not considered eligible by the survey methodology. Some programmes chose a new institutional path, most notable was the 2005 merger of the CRESCE, KARELA and the MEDA (Kulane) programmes into the Banco de Oportunidade de Moçambique. The table below clearly shows the high rate of dropout or institutional transition over the period 1997-2005. Although GAPI plays a very important role in the microfinance sector it has been excluded from the survey as it is considered to be a wholesaler to MFIs and associations which, due to their small size and polyvalent activities, have not been considered microfinance operators for the purposes of this study.[48]

Table 1: Summary of Three Selected MFI Surveys by Active Borrowers and Savers

Note: Non active operators are shaded.

MEDA Study 1997		ICC/CARE 2000	MMF/UNDP 2005	
	Active Borrowers	Active Borrowers/ Savers	Active Borrowers	Active Savers
ACTION AID**	18			
ADCR	100 (est.)			
ADEMO	Not started	60		
AMODER	186	296	950	-
AMRU	50 (est.)	50		
ASSOC. PROGRESSO	170		100	-
BPD/BAD*	100 (est., state bank, special project)			
CARE (CRER)	106	499 *(footnote 55 demonstrates that there were 3,237 clients by September 2000)*		
CARE (CRESCE) →BOM (see below)	412	2,020		
CMN	50	750 (savers) + unspecified number of borrowers	212	1,702
CONCERN	Not provided			
ECOTEC	100 (est.)			
FARE*	65 (SME loans)	* not considered MFI		
FFPI*	26 (SME loans)	176	*not considered MFI	
FOS**	150	953	1,500	
GAPI	200 (SME loans)	*not considered MFI		
GPE	8 (SME loans)	32	* not considered MFI	
GPE-GTZ → SOCREMO	835	1,517	5,801	1,600 (est.)
GPPE	Not provided	Included (no info)		
GTZ ORF*	100(grants to demobs)			

[46] The MEDA study formed the basis of the operator survey for the 1998 *Mozambique Microfinance Study.* The former is used since details are provided for each operator that have been extracted and recently analyzed in order to allow for quantitative comparisons with the 2005 data. The study covered 33 microfinance institutions but for the purposes of making comparisons in this study, two further institutions Action Aid and FOS, identified by the 1998 study were included.
[47] The 2000 study presents an "inventory of microfinance institutions" that lists 29 operators of which quantitative data was provided for 24. In addition to the 29, the inventory also provided information on AMODER and the FFPI that were not considered to fall within the study's definition of a microfinance operator. Quantitative data from that study was restricted to active loan clients and credit portfolio, savers and value of deposits. The 2000 study focused mainly on case studies of six operators: CCCP (IRAM/BoM), CRESCE (CARE), CRER (CARE), FCC (World Relief), SOCREMO and Tchuma.
[48] GAPI provides loan capital to a variety of associations representing mainly agricultural producers as well as traders and some vocational skill groups. It is estimated that the associations provide microcredit to approximately 2,000 borrowers.

	MEDA Study 1997	ICC/CARE 2000	MMF/UNDP 2005	
	Active Borrowers	Active Borrowers/ Savers	Active Borrowers	Active Savers
HELP AGE	60			
HELVETAS	448			
HELVETAS Moç	180			
INTERMON/OSM →Hluvuku- Male Yeru	340	406	1,205	
CCCP→CCOM) Maputo & CD	Not started	2,173	14,205	0
ISCOS	102			
ISCOS LIGURA	Not started			
ITER	Not started			
KULIMA	10	40	60	0
LWF	66			
MBEU	50 (est.)	0		
MEDA (Kulane) →BOM	105	620		
OJDR	90	59		
OXFAMUK/I	30			
PAPIR	300 (est.)			
SNV	Not provided			
TCHUMA	Not started	1,378	8,387	4,803
UGC/CPC	130 cooperatives (est. 1,500 borrowers)	210	115 (CPC) & 973 input credit (UGC)	0
World Vision (AMF)	10			
WRI (FCC)	180 groups (est. 3,000 members)	4,422	3,884	0
MEDA 1997 STUDY TOTAL	**+/- 9,000**	↓		
Operators Added to ICC Study 2000				
AMODESE		0	120	0
CARE – ILRP → KUKULA (PCR promoter)		Included (no info)	4,200 (est.)	6,000 (est.)
CCM		0		
CMMEA		0	51	0
GGLS→FDM		631	1,239	0
KARIBU		24		
NOVOBANCO		0	12,108	30,813
Poupanças Communitarias		59 (savers)		
World Vision PROMIZA→KARLELA→BOM		676		
ESTIMATED TOTAL FROM THE ICC SURVEY		**16,649*** **	↓	↓
Operators Added to MMF/UNDP Study 2005				
ADEM (PCR promoter)			318 (est.)	1,586
AJAM (PCR promoter)			12	0
AKSM			736	1,789
ASM Credito			312	0
BOM			2,718	0
CARE VSL Zambezia (PCR promoter)			758	6,050
CCC			16	300 (est.)
CPC			640 (micro loans only)	58
First Microfinance Programme			1,111	0
IRAM- RCRN			Not yet started	0
Malanga Micro Credito			868	0
MultCredito			Not provided	0
Ophavela (PCR promoter)			2,534	9,122
Project Hope			822	0
Projecto Lhuwuka			525	0
The Hunger Project			511	0
ESTIMATED TOTAL OF THE MMF/UNDP STUDY (2005)			**66,991**	**63,823**

*not considered to be microfinance operators for the purposes of comparative analysis in this study
** existing at the time of the survey but not included (information obtained from the *Mozambique Microfinance Study*)
***excludes UGC poultry input credits and CRER ASCA groups

2.3.1 Client Growth (Outreach)

The data shows that over a period of eight years the microfinance sector has undergone considerable transformation. The most notable change has been in terms of microfinance beneficiaries. In 1998 it was estimated that there were approximately 9,000 loan beneficiaries of which about half received services from only two providers (World Relief's FCC programme and the UGC's poultry input credit programme). By 2000 the ICC study presents a total of 16,649 clients but this figure is considered to be underestimated. By adjusting for the correct number of clients for the listed operators, it is probably more realistic to say that there were about 23,000 active microfinance clients in 2000 (including PCR group members and savers with the CMN).[49]

By 2005, the picture changed considerably, with operators reaching 66,000 borrowers and 63,000 savers. This increase can be attributed primarily to the rapid growth in numbers of savers. The introduction of savings products since 2001[50] and the success of the ASCA/PCR methodology led to a very rapid growth in deposit accounts, to the extent that the number of savers almost matched the number of borrowers in 2005. PCR members promoted by Ophavela, ADEM, AKSM, Kukula, CARE-VSL Zambezia and the IDPPE (not included in the survey as it is a government pilot programme) accounted for about 40% of savers. Other savers were accounted for by depositors holding accounts with NovoBanco and to a much smaller extent Tchuma. With SOCREMO introducing savings accounts in 2005 and BOM opening accounts in late 2005, one can expect further rapid increases.

High client turnover registered among the larger operators suggests that, in addition to the current clients, it is estimated that there have been at least an additional 100,000 clients who have had access to microfinance *loans* over the past ten years.[51] From this perspective one can argue that more than 200,000 Mozambicans have had access to microfinance services over the past decade.[52]

2.3.2 Portfolio Growth

The total value of outstanding loans[53] (active loan portfolio) seems to have grown proportionately much more than active client volume. The 2000 study presented an active portfolio of 33 billion MT or $2.2 million.[54] By 2005 the active loan portfolio covered by the survey increased to $16.4 million, a considerable increase, reflecting growth in average loan values (accounted for mainly by NovoBanco, SOCREMO and Tchuma). Data collected from the main microfinance operators[55] shows that active portfolio increased by more than 50% annually from 2001-2004[56]. The increase from 2004-2005 was smaller due to the consolidation process of the portfolios acquired by BOM and the closure of the FCC operations in the North.

2.3.3 Average Loan Size

Although no calculations were made of average loan sizes in previous studies, an examination of average loan values[57] and lending conditions, suggests that a much broader range of clients are now being served. In the earlier years loans provided by the larger operators and most of the small

[49] Data obtained from Gabrielle Athmer (2000) *Case Study: Rural Microfinance Pilot Project* shows that by September 2000, CRER had 3,237 clients of which 1,913 belonged to savings stamp groups, 694 to PCR groups, 270 to solidarity groups and 360 to farmers' associations. The CARE's Inhambane Livelihood Rehabilitation Project started PCR groups just before CRER so it can be assumed that there were about 1,000 clients. It is estimated that there were about 2,000 UGC input credit clients in 2000. Adjusting for other programmes for which no information was obtained (approximately 700), we would then get a total of about 23,000 microfinance clients.

[50] The CMN introduced savings accounts for its members in 1994. These accounts were technically illegal but continued with the tacit knowledge and acceptance of the BoM.

[51] NovoBanco estimates that it has served a total of some 50,000 loan clients since inception; Tchuma has served 20,000 while SOCREMO says it has had about 20,000 clients since 1999. IRAM CCCOM calculates that they have had about 27,000 loan clients. Because of clients switching from one operator to another, an allowance has to be made for double counting. This figure excludes other operators such as FCC, CRESCE and all the smaller operators.

[52] Information obtained from client interviews of the impact assessment study showed that relatively few clients leave one institution for another, especially in the lower loan categories where most of the dropout rates occur.

[53] Total value of loans outstanding is defined as the value of the balance of all loans owing to a financial institution.

[54] This amount includes AMODER's portfolio. An exchange rate of 1USD = 16,000 MT was used by that study.

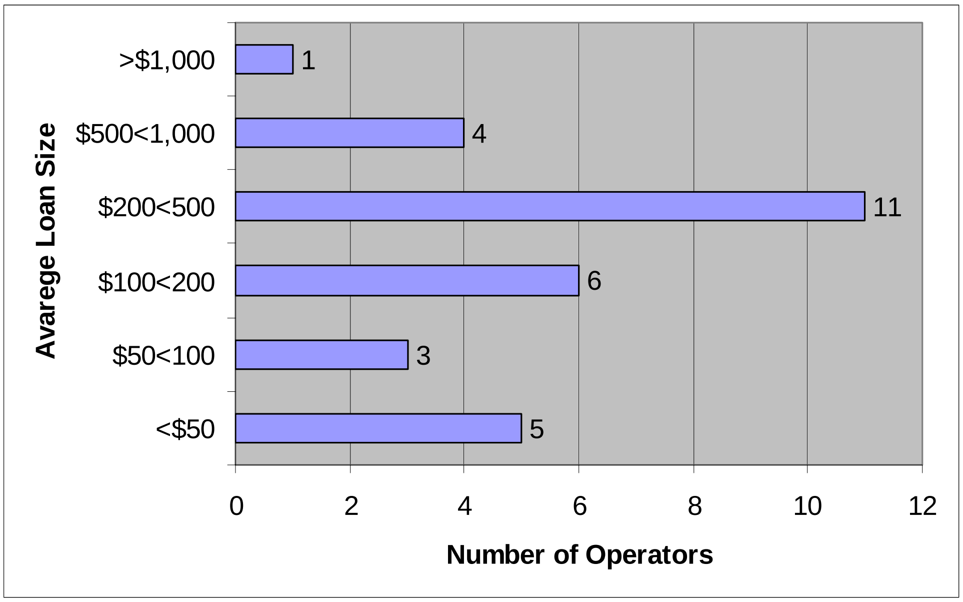
[55] Since 2002 MMF has collected information from selected operators: CMN, CCCP-CCOM, CRESCE (until taken over by BOM) FCC, FDM, Male Yeru, NovoBanco (more recently), Ophavela, SOCREMO and Tchuma.

[56] Research by Marie-Charlotte Buisson (2005) shows that active portfolio increased by 52% between 2001-2002, 50% from 2002-2003 and 73.5% from 2003-2004.

[57] Average loan sizes were calculated by: total value of loans disbursed in 2004 divided by the total number of loans.

"component" programmes would rarely exceed $200 with an average that probably hovered between $100 - $150. In 2005 the modal cohort of loans provided by *lending institutions* (i.e. all operators excluding those promoting PCRs), was $200 - $500 (Figure 1), but the overall average probably exceeds $400. Four operators had average loans between $500 and $1,000. Of these, NovoBanco ($827) and SOCREMO ($624) collectively accounted for 17,907 (27%) of the total active loan clients in mid-2005. Due to the deposit constraints (prevailing poverty), loans obtained from PCR groups average considerably less than $50. Of the larger operators, the CCOM project, with an average loan size of $108, is the only one that can be said to reach a lower income group of beneficiaries (especially in Cabo Delgado where average loans are about $60 - $70).

Figure 1. Average Loan Size (2004)



Higher average loans have been the result of various factors such as client progression to larger loans, and inflation and exchange rate movements, however the primary factor has been the decision by some MFIs to move up-market.

2.3.4 Depth of Outreach

The UN Advisors Group put considerable emphasis on the potential role for microfinance in reducing poverty. A measure that is often used as an indicator of whether an MFI is targeting the poor is "depth of outreach" (the ratio of average loan balance to GNP per capita). In 2004 the GNP per capita was $250.[58] According to the MicroBanking Bulletin, depth of outreach is defined as targeting "low-end" clients if average loan balance is less than 20% of the per capita GNP ($50); "broad" with an average loan balance of between 20% and 149%; or "high-end" if average loan balance is between 150% and 249% (i.e. above $375). Average loan balances are generally much easier to obtain than average loan sizes. Figure 1 shows the average loan sizes for 2004: roughly we can say that the threshold for "high" could be about $500 while the low end about $100. Using the average loan size as reference, it can be concluded that five (16%) of the operators were serving high-end clients and eight (25%) of the operators could be considered to be serving the low-end clients, of which most are ASCA programmes. The large majority (59%) of operators offer loans for the "broad" range of clients.

Using average loan balance is a simple abstraction of a complicated reality. Some MFIs offer a variety of products that target different segments of the market, a technique that helps reduce risks and is recommended as a best practice by CGAP. In the case of NovoBanco, SME loans target the higher end client and this consequently has an impact on the overall average. More relevant indicators would be median values and minimum loan amounts. As demonstrated in section 3.1, loan methodology is

[58] See *Characteristics of the Microfinance Sector and of the Three Institutions involved in the Impact Assessment* by Gabrielle Athmer (team leader) and Henriqueta Hunguana (ICC Mozambique).

important. The results of the urban client impact study shows that most active borrowers access credit only with asset guarantees, automatically disqualifying the poorer end of the market. Operators offering solidarity-group loans and ASCA programmes are able to provide smaller loans as group methodology helps in diminishing operational costs. With this methodology the lower segments of the market can be served.

2.4 Number of Service Providers

It is interesting to observe that the number of microfinance operators has hardly changed over the years. The 1997/98 surveys covered 42 institutions but seven of these were not considered to be microfinance providers (BPD/BAD, DED, CRS, GAPI, FARE, FFPI, GTZ ORF). In 2000, 29 institutions were surveyed and in 2005, 32 operators were located. Although the numbers remained virtually the same, a comparison of the operators covered by the surveys shows that there has been a rapid turnover. Of the 35 operators surveyed in 1997/1998, only 15 were still operational two years later in 2000 and only eight were operational in 2005. Of the 29 microfinance operators studied in 2000, just over half (15) still existed during the 2005 survey.

2.5 Institutional Transition

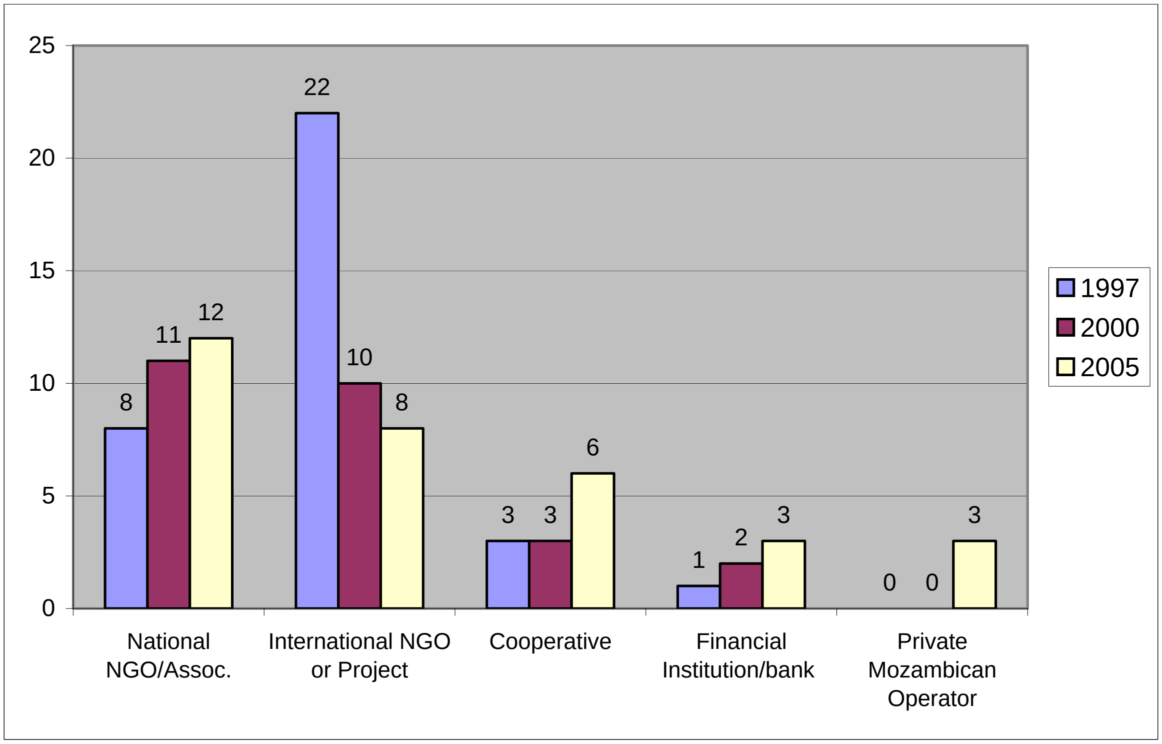
As indicated above, there has been a high turnover rate for microfinance operators. Most of those that have disappeared were small programmes launched by international NGOs, often components of an integrated programme that were never intended to have a prolonged life or pretense of sustainability. A fair number of national initiatives have gone a similar route.

Not only has there been a large turnover in operators but, as Figure 2 clearly shows, there has been a significant evolution of the types of operators providing microfinance. In 1997, only three years after the inception of World Relief's village banking programme, about two-thirds of the operators were international NGOs or donor agencies. Less than a quarter of the operators were national NGOs or associations. Over the next eight years international NGOs initiatives in microfinance provision decreased significantly, accounting for less than a quarter of the operators while national NGOs/associations (i.e. registered and only operating in Mozambique) increased their presence to 42%. Three other important developments also significantly altered the structure of the microfinance sector. With the growing commercialization of the sector, one could expect to see more financial institutions and banks as well as small private operators. By 2005, the market was dominated by three commercial banks (NovoBanco, SOCREMO, and BOM). Tchuma, being a cooperative, is considering conversion to a commercial bank. The second significant development has been the establishment of registered private Mozambican money lending companies in recent years.[59] The three encountered appeared to be not only well managed but already covering their costs with relatively small amounts of private capital.[60] Finally, the number of savings and credit cooperatives, representing special interest groups such as the CCC, CPC and imminently, the CMN has increased.

[59] Private credit companies are registered directly with the Bank of Mozambique. According to the owners the process is simple and takes approximately one month.

[60] The three Mozambican operators encountered had very different backgrounds. One operator previously managed state-owned enterprises. Having successfully sued the state for outstanding salaries owing, he invested virtually all the proceeds into developing his lending business, having in the meantime obtained an MBA in South Africa. Another operator learned about microfinance through his brother-in-law who managed the credit operations of a large programme. He is currently employed full-time at Mozal and has invested his own earnings into establishing his enterprise. The third operator is a well-established businessman who has also invested his own funds into his lending operations.

Figure 2. Institutional Transition (1997-2005)



The 1997 survey revealed that, of the 35 operators, only 15 (43%) demonstrated[61] either a commitment or performance indicators that offered reasonable long-term operational prospects. Of these 15, only three: CRER, ECOTEC-MICRED and Programme to Promote Small Rural Industry (PAPIR) stopped operating. Seven institutions continue today. These are AMODER, CMN, FOS (now FOS-Chitima), Tchuma, FCC, CCCP (now Caixas Comunitárias de Operadores de Microfinanças and subsequently referred to in this report as CCCP-CCOM) and GTZ-GPE (SOCREMO). Five operators were acquired or transformed: the activities of Helvetas-Mozambique and Intermon were transformed into the association Hluvuku-Male Yeru, while the portfolios of CRESCE, KARELA and MEDA were, as mentioned previously, acquired by BOM.

In 2005, the picture is quite different. Of the 32 operators surveyed, 24 (75%) could be considered to have reasonable long-term survival prospects. Although a few of these have not yet achieved desirable performance indicators, it is expected that they will improve, taking into account their early stages of operations, the technical backstopping available and their stated objectives. The remaining eight operators are generally small and have not yet reached the scale or performance levels that suggest that they will be long-term players.

[61] Based on author's opinion which was formed according to the information provided by the operators themselves.

Table 2: Quantitative Profiles of Surveyed Operators

Note: All figures as at 30 June 2005, unless otherwise stated.

Name of Institution and Year of Establishing Financial Activities	Active Portfolio	Average Loan Size 2004*	Active Male Clients	Active Female Clients	Credit Officers/ salaried ASCA promoters
ADEM (2002)	693m MT ($27,720) (est.)	1.5m MT ($60) (est.)	377 (savers only)	1,209 (savers only)	5
AJAM (1998)	190m MT ($7,600)	$650 (est.)	6	6	1
AKSM (2001)	780m MT ($31,200)	1.6m MT ($63)	537 (savers only)	1,252 (savers only)	3
AMODER (1994)	44.1bn MT ($1.76m)	46.4m MT ($1,856) (2005)	760 (est.)	190 (est.)	12
AMODESE (1999)	613m MT ($25,000)	6m MT ($240)	46	74	2
ASM (2005)	382m MT ($15.300)	$100 (est.) (2005)	37	275	3
Assoc. Progresso (1997)	75m MT ($3,000)	1m MT ($40)	50	50	2
BOM (2005)	$386,000	7.5m ($300) (est.)	1,413	1,305	25
Care VSL Zambezia (2004)	$11,370	$15 (approx)	3,449 (savers only)	2,601 (savers only)	6
CCC (2003)	235m MT ($ 9,400)	15m MT ($ 600) (est.)	9 (credits only)	7 (credits only)	1
CMMEA (2002)	851m MT ($34,000)	10m MT ($400) (est.)	44	7	1
CMN (1994)	1.2bn MT ($48,000)	4.7m MT ($188)	0	1,702 (savers only)	1
CPC (2000)	5.6bn MT($225,000) (micro loans only)	$352 (micro loans only)	418 (credits only)	222 (credits only)	1
FCC (1994)	$511,730	$239	1,556	2,328	47
FDM (1997)	$94,669	$123	62	1,177	8
First Microfinance Project (2003)	4.3bn MT ($172,000)	$170	800	311	12
FOS (1998)	100m MT ($4,000)	500,000 MT ($20) (est.)	800	700	2
Hluvuku- Male Yeru (2001)	11.3bn MT ($452,000)	11.5 m MT ($460)	711	494	5
IRAM-CCOM (1997 M; 2000 CD)	23.3bn MT ($932,000	2.7m MT ($108) (M&CD)	6,118	8077	12
Kukula (registered NGO 2004, started ASCAs in 1999)	$126,000	$30	0	6,000 (savers only)	2
KULIMA (2001)	$10,000 (est.)	$300 (est.)	18	42	1
Malanga (2004)	$185,000	$213	356	512	3
Multcredito (2005)	No information				
NovoBanco (2000)	$5.5m	$827	6,954 (credits only) 12,159 (savers w/o credits)	5,153 (credits only) 6,547 (savers without credits)	78
Ophavela (1997, registered NG0 2004)	43.3m MT ($1,720)	252,000 MT ($10)	4,996	4,126	8
Project Hope (2004)	997m MT ($39,880)	3m MT ($120) (approx)	0	822	4
Projecto Lhuwuka (2003)	751m MT ($30,000)	2m MT ($80)	173	352	3
SOCREMO (1999)	94bn MT ($3.78m)	15.6m MT ($624)	2,900 (credits only)	2,900 (credits only)	45
TCHUMA (1999)	46bn MT ($1.86m)	8m MT ($326)	3,231 (credits only)	5,156 (credits only)	40
The Hunger Project (2001)	1.7bn MT ($ 68,000)	8.6m MT ($344)	0	511	1
UGC/CPC (2002 CPC, 1990 UGC)	894.5m MT ($ 36,000)	6.25m MT ($250)	65 292 (input credit, est.)	49 681 (input credit, est.)	3
TOTALS	**$ 16,386,589**		**48,337**	**53,629**	

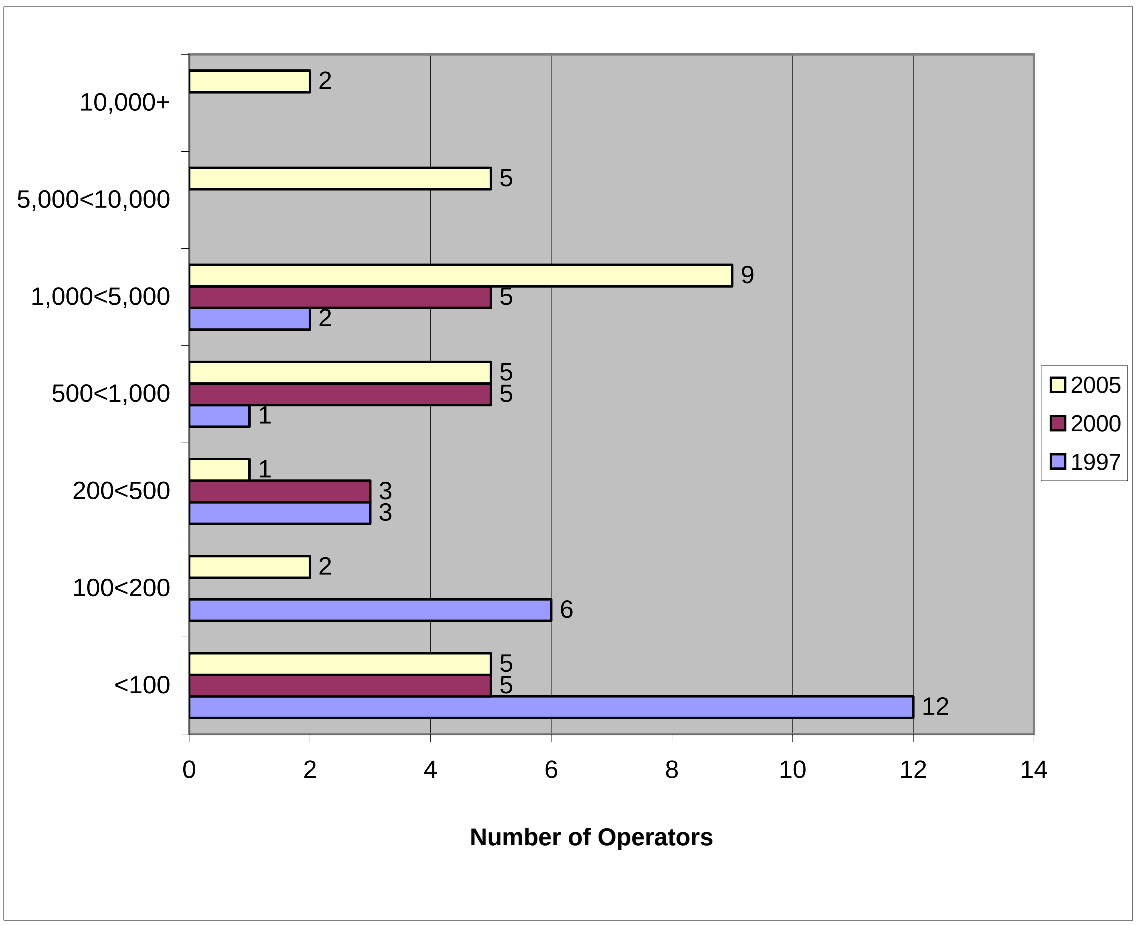
* total value of loans in 2004 divided by number of loans in 2004

2.5.1 *Institutional Growth*

Comparative data from the three surveys presented in Figure 3 shows how the number of operators with higher client numbers has grown. In 1998 there were only two operators with more than 1,000 clients. By 2005 half (16) of the operators had more than 1,000 clients and two (NovoBanco and IRAM-CCOM) had more than 10,000 clients. In 1997 half of the operators (12) were serving less than 100 clients. In 2005 it could be concluded that there exists a general trend for operators to scale-up but that there are still a few operators with small numbers of clients, often components of integrated rural projects, which are unlikely to grow substantially.

One of the most visible trends in the microfinance industry is the growing dominance of a limited number of operators. NovoBanco, SOCREMO and Tchuma control more than two-thirds (68%) of the active portfolio. One operator, NovoBanco, controls one third of the total active portfolio. Although there is no comparative data, there has been a significant growth in active portfolios with four operators holding portfolios exceeding $1.0 million and almost half of all operators with more than $100,000 each. By the end of 2005 three MFIs claimed to be financially sustainable (including technical assistance).[62]

Figure 3. Size of Operator by Number of Active Clients (1997-2005)



On the other hand, Figure 4 shows that almost half (15) the operators have small active portfolios (i.e. less than $50,000). This can be partly explained by the fact that five of these operators were promoting ASCAs with small amounts of savings mobilized for on-lending.

[62] NovoBanco, SOCREMO and Tchuma.

Figure 4. Size of Active Portfolio (June 30, 2005)

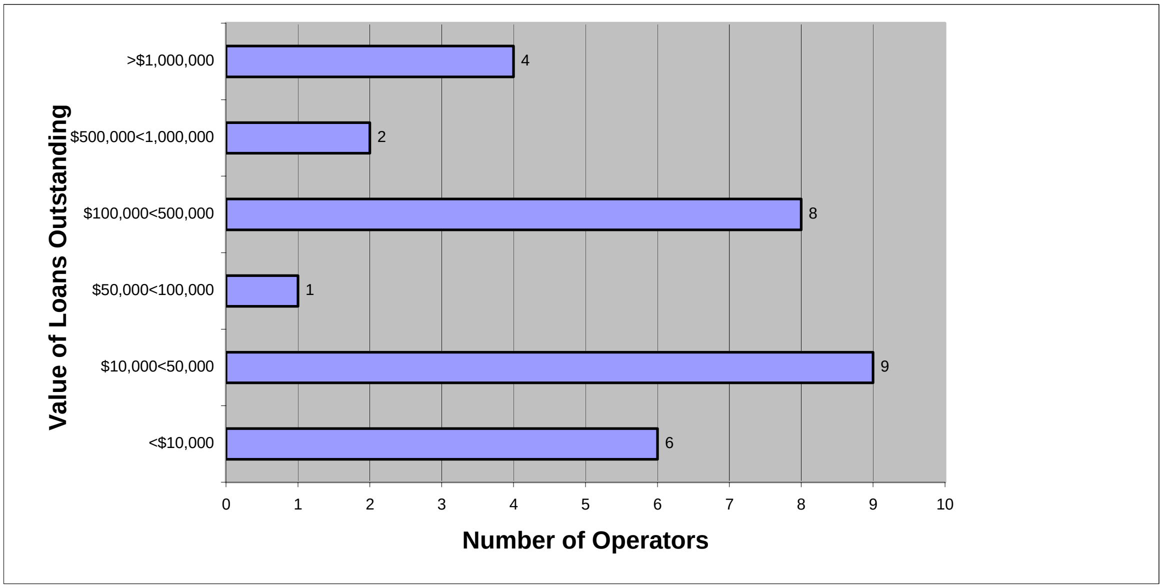
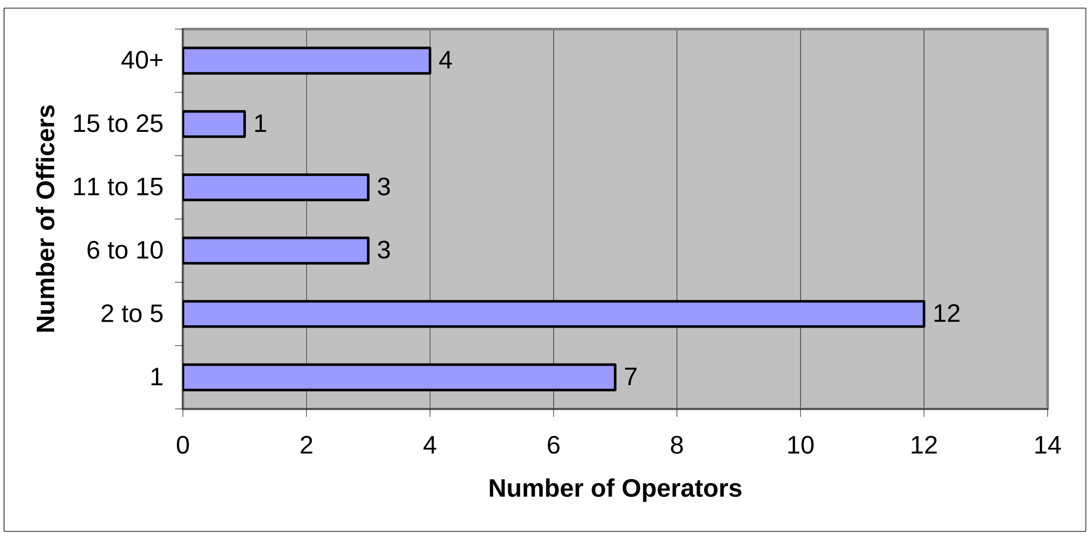


Figure 5 demonstrates that, by using loan officers or salaried promoters as proxies for staff numbers, the majority of operators are still very small in terms of personnel. Of the 30 operators providing information on staff, almost two-thirds (63.3%) had less than five officers/promoters. Only four (13.3%) could be considered large institutions with more than 40 officers/promoters.

Figure 5. Number of Loan Officers/Salaried ASCA Promoters per Operator



2.5.2 Institutional Performance

One of the most encouraging indicators has been a substantial improvement in operator portfolio quality. The 1997 MEDA survey obtained information on loan recovery rates from 25 operators. Figure 6 indicates that only four (16%) had recovery rates that approached levels considered acceptable from a best practice perspective (exceeding 90%). Almost half (12) had rates below 70% and 20% of operators had levels below 50%. Figure 7 shows a dramatic change by 2005. Of the 21 operators providing information, more than half (57%) had portfolios at risk (PARs)[63] of less than 5% (>30 days). There are, however, still a large number of operators (one-third) that have PARs in excess of 20%. Given the number of non-responses to this question (34%), it can be assumed that many of those are also likely to have poor portfolio performance.

[63] PAR is defined as: value of outstanding balance of loans in arrears/value of loans outstanding > 30 days.

Figure 6. Loan Recovery Rates (1997)

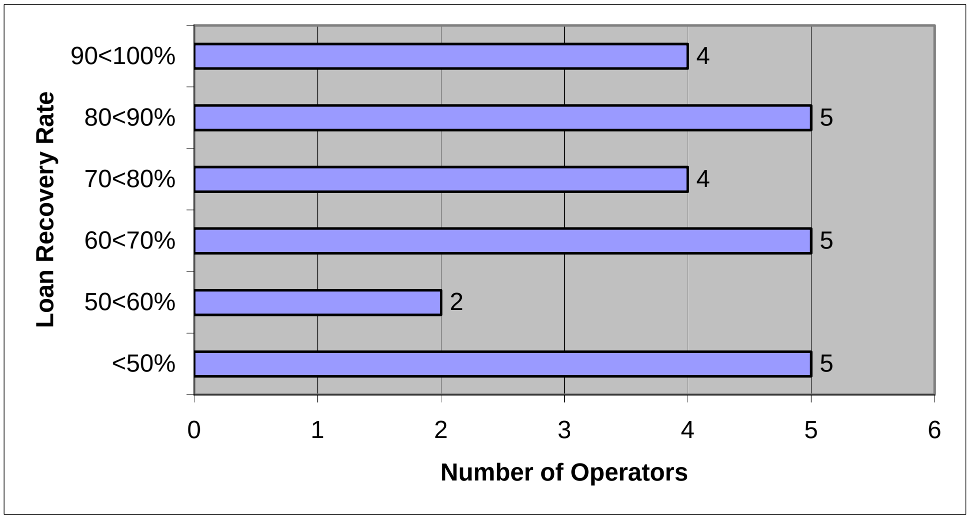
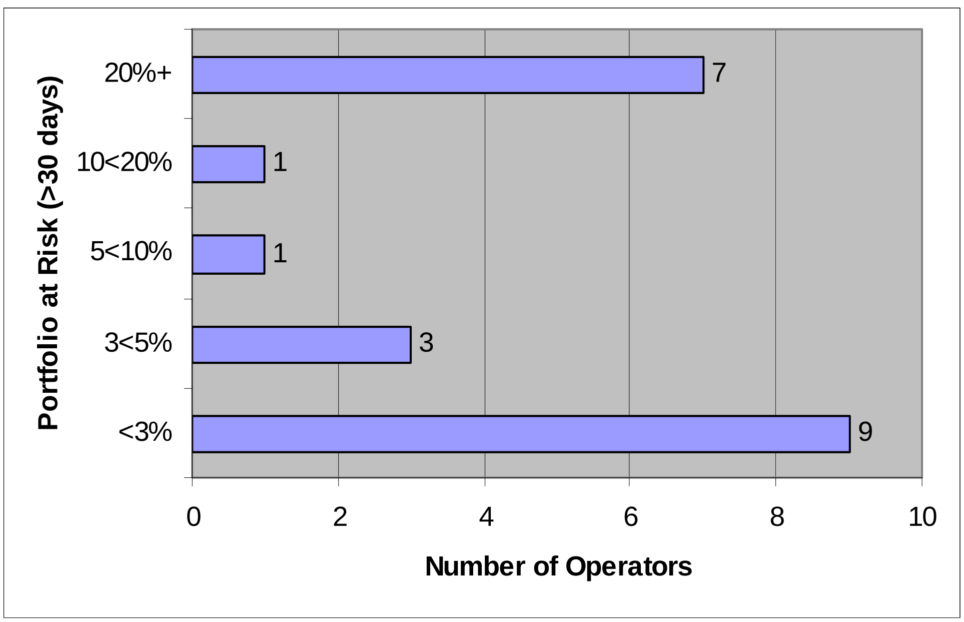


Figure 7. Portfolio Quality (PAR) (2005)



2.5.3 Financial Products and Methodologies

Figure 8 indicates that a minority of operators provide loan products strictly to individuals. In 1997 just under a quarter did so but by 2005 just over a third provided loans *only* to individuals. The 2005 survey shows that there has been a significant decline in the proportionate number of operators lending to groups or to *both* individuals and groups. Although there appears to be a decline in operators working with solidarity groups or village banks, there has been a rapid growth of the number of PCR programmes with strong prospects for much greater expansion of this methodology. The largest operators (by portfolio - NovoBanco, SOCREMO) are only providing individual loans. Tchuma has decided to target poorer clients through smaller loan sizes and has revived its solidarity group portfolio (see next paragraph). The CCOM project mainly offers loans to solidarity groups via registered associations but is increasing the number of individual loans as the credit needs of their older clients continue to grow. BOM is using a mixture of individual, solidarity group and village banking methodology.

Although the number of operators offering credit *only* to individuals is still comparatively small, the value of loans provided to individuals by *all* operators overwhelmingly dominates credit provision in the country, with more than 90% of the active loan portfolio being channeled to individuals. The provision of individual loans allows for more rapid portfolio growth and usually a faster path to sustainability. Solidarity or group loans limit the individual growth capacity of beneficiaries, as they depend on the repayment capacity of the other members in the group. The group methodology is often used by MFIs to limit operating costs (following up on different loans at the same time) and therefore allows an MFI to provide smaller loan amounts in a sustainable manner. Solidarity group lending through associations has been successfully undertaken by CCCP-CCOM in both peri-urban and rural areas and in irrigation schemes by GAPI (providing wholesale loans to associations). Chapter 3 demonstrates that, with the increasing saturation of the individual loan market in the Maputo-Matola urban axis, some operators such as Tchuma are targeting poorer clients organized in solidarity groups as they do not have sufficient asset guarantees needed for individual loans. As demonstrated by the CCCP-CCOM experience, the solidarity group methodology much more effectively targets poorer households (see chapter 3 for a more detailed discussion poverty reduction and the impact of individual and group loans).

Figure 8. Loan Methodologies (1997-2005)

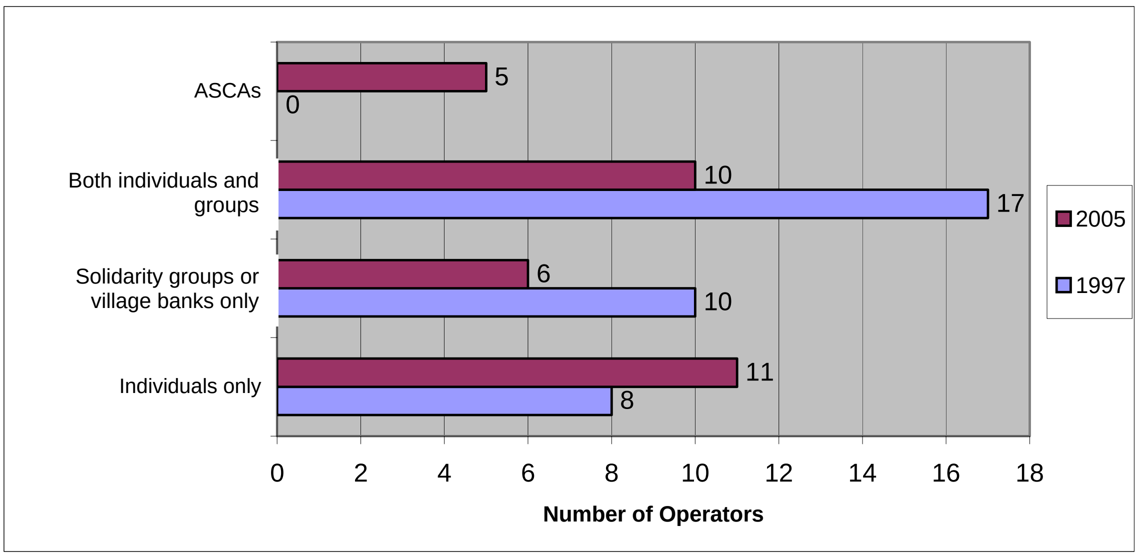


Table 3 shows a shift from a primary focus on microenterprise loans to a combination of microenterprise and agriculture loans. In 1997, only 18% of the operators provided both microenterprise and agricultural loans while, in 2005, 44% did. However, in the majority of cases, agricultural loans only accounted for a small fraction of the total loan portfolio. Only CCOM and the association Hluvuku-Male Yeru can be said to have provided agricultural loans in relatively large volumes. In 1997, more than two thirds of the operators (68%) gave the majority of their loans to microenterprises. By 2005, this was reduced to less than half, partly explained by the fact that microfinance loans proved inappropriate (or at least difficult to administer) for *productive* microenterprises[64] and five operators, focusing exclusively on productive enterprises, ceased operations. Another notable trend has been a shift away from in-kind credit. Only the UGC continues to provide this facility but the future of this form of credit is uncertain as plans are made to pass these clients to the UGC's more conventional microfinance operations under its new programme the CPC (not to be confused with the CPC associated with the BoM).

In terms of newly introduced financial products, the most important development since 1997 has been the growth of PCRs and more recently the deposit facilities offered by the commercial banks NovoBanco, SOCREMO and BOM. The CMN, though not legally a cooperative, has allowed members to open current accounts since 1994. Tchuma has offered savings facilities since 2000 and

[64] Productive activities such as carpentry, welding and milling require some durable capital investment which take much longer than merchandise stock to realize a return. Also, the amounts needed are usually considerably higher than the small stocks needed by market vendors.

NovoBanco since 2001. The introduction of the new legal entity “micro bank” is expected to cause a big increase in the number of operators offering savings facilities with the imminent introduction of interest-bearing savings accounts.

Increasing competition in the Maputo-Matola area amongst NovoBanco, SOCREMO and Tchuma, all targeting similar beneficiaries, has led to three developments. The first has been noticeable improvements in the quality of the loan products offered, in particular the swiftness of loan approval and renewal. The second relates to client oriented services such as modern offices and more efficient customer service. The third has manifested itself in the introduction of new financial products such as housing loans (NovoBanco), salary-based loans (NovoBanco and Tchuma) and small and medium enterprise loans (starting at about $4,000 for NovoBanco and $6,000 for SOCREMO). BOM will soon introduce a compulsory credit life insurance (see footnote 65). It is important to note that, even though loans are meant to be channeled for specific purposes, beneficiaries often allocate them for other purposes, frequently for construction and the purchase of household goods.

Table 3: Types of Products Offered

Description	Number of Operators Offering Product			
	1997		2005	
	#	%	#	%
Mainly/exclusively microenterprises	18	53	15	47%
Productive microenterprise only	5	15	-	
Mainly/exclusively agricultural production	5	15	3	9
Both microenterprises and agriculture	6	18	14	44
In-kind credit (seed/livestock)	5	15	1	3.1
Fishing Activities	-		4	12.5
Small/medium enterprises	1	3	3	9
Housing	2	5.9	2	6
Salaried Workers-(employer guarantees)			2	6
Credit Life Insurance[65]	-		1	3.1
Deposit facilities (bank type)	1	3	5	16
Community based savings			5	16

2.5.4 The Cost of Credit

Commercial bank interest rates were more or less the same as those of microfinance institutions in the mid-1990s; they have now decreased to half those levels, and are currently around 21-23% p.a. In contrast, interest rates charged by microfinance operators appear to have increased. Although it was often difficult to gauge from the responses whether rates were charged on a declining or a flat rate (suggesting the need for a more rigorous analysis in terms of *effective* rates), the two sets of information point to an upward trend (see Figures 9 & 10). This trend is strongly influenced by two factors. One is that ASCA groups are charging 10% per month (flat) for lending their internally raised funds. The other is that at least some of the private operators are charging relatively high rates, 10% per month declining in one case and 16.7% flat in another. Figure 9 shows that in 1997 the modal interest range was between 30-40% per annum (mostly flat) while currently (Figure 10), the modal monthly rate is between 4-5% (mainly declining) that would give roughly similar *effective* rates. Operators justify higher interest rates based on higher operational costs. Although BoM advisory notice 1GGBM/99 allows microfinance operators to set their interest rates at whatever level they want,

[65] This product is to be introduced by BOM in February 2006. It covers the full outstanding amount of the loan on the death of a client (0.024% of loan per month)

it would be prudent for them to provide convincing evidence that the higher rates are warranted.[66] In South Africa, where microfinance is often given a bad name by extortionate interest rates applied by loan shark companies, there are counter initiatives by companies such as the Small Enterprise Foundation, modeled on the Grameen Bank and operating since 1991, that aim to provide loans at the prevailing prime interest rate. [67]

Figure 9. Annual Interest Rates (1997)

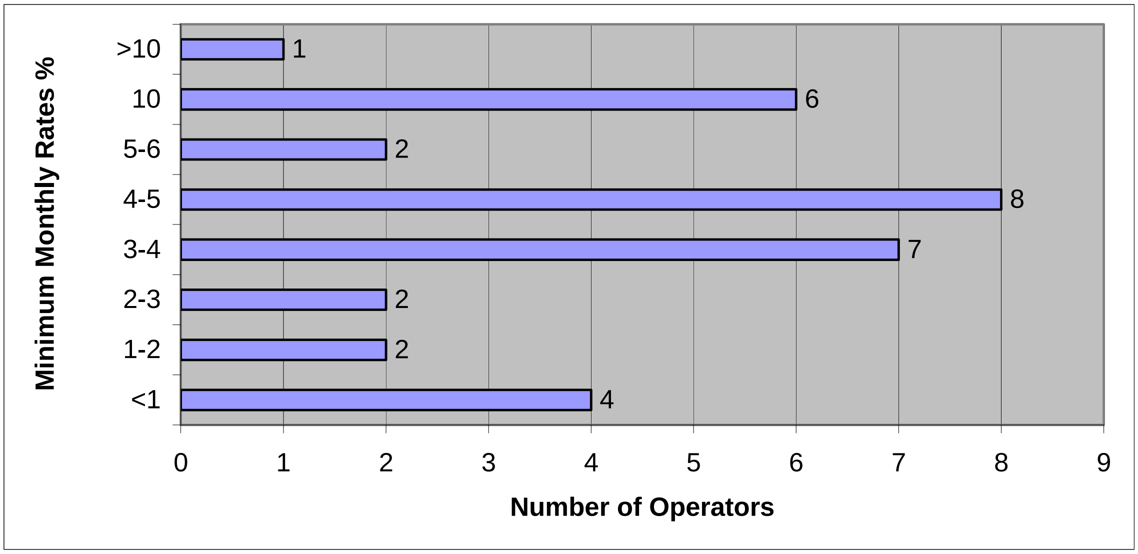
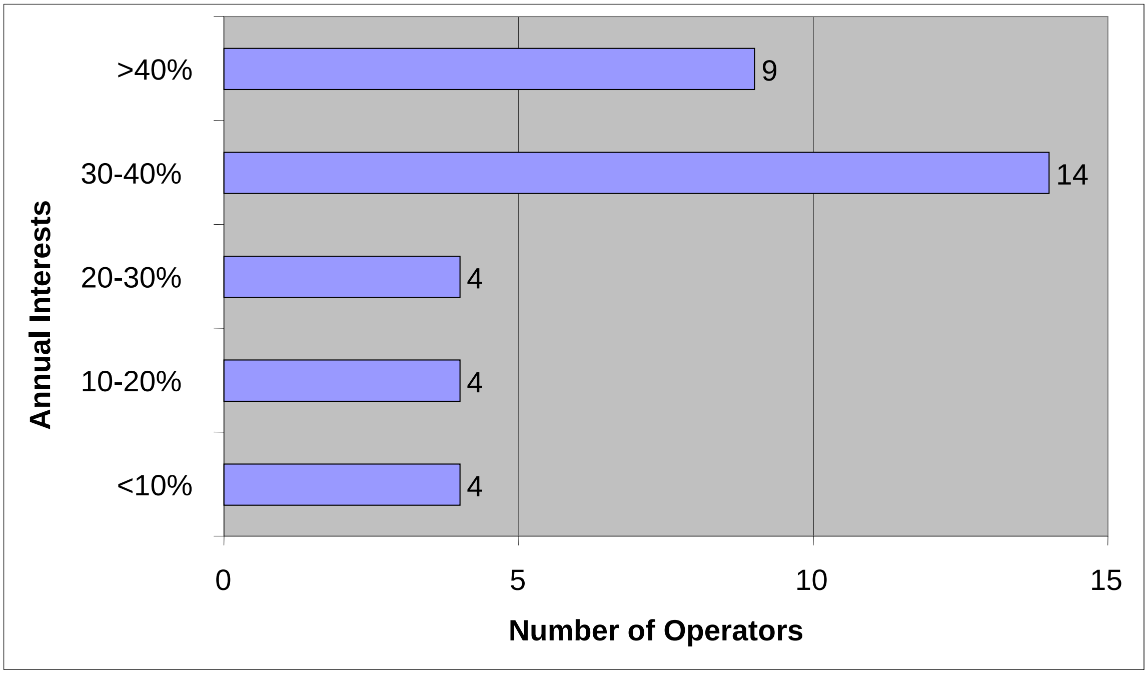


Figure 10. Monthly Interest Rate (2005)



One major MFI presented the following justifications for maintaining higher interest rates:

[66] In its 2004 Annual Report, NovoBanco stated: "In contrast to the banking sector, institutions that focus on micro-lending, including NovoBanco, did not follow this significant downward trend in lending rates, but rather kept their interest rates at a constant level during the period covered by this report" (p.18). Nowhere in the report does it justify why the higher rates are maintained.

[67] Financial Mail, December 23, 2005, p. 28.

- Interest rates are fixed to cover not just cost of funds but administrative costs. Principal costs are personnel, and these are not decreasing. Other important costs include office supplies, communications and security.
- It is likely that for most MFIs the cost of funds is actually increasing because, at least for the formalized institutions, there is limited access now to donated funds. MFIs' cost for financial resources is closer to retail rates of interest and not wholesale and, when borrowing from foreign organizations, MFIs usually bear the exchange rate risk.
- It is not fair to compare MFI rates with commercial bank rates. MFIs as a rule avoid charging commissions, preferring to make the charges to customers as predictable and as transparent as possible. A large part of their profits come from bank charges and not from interest rates.
- Although MFIs charge higher interest rates, they also pay considerably higher interest rates on savings (term deposits).
- Clients do not consider the interest rates to be a problem. Whilst this cannot be used to justify charging higher rates than necessary to cover costs and ensure the sustainability of the organization, the fact is that for the relatively low value of the loans and the relatively short terms, the benefit to the individual client of a cut of 10% in the annual interest rate translates into a relatively small saving, whereas it would be the death knell for an MFI.

2.5.5 Gender Issues

The survey found an almost even distribution between women (52.6%) and men (47.4%) in terms of microfinance beneficiaries across the country (see Table 2). It is likely, however, that without a conscientious effort on the part of donors to promote female participation, the present situation could have been considerably different. The survey shows that there are four programmes (CMN, Kukula, Project Hope and The Hunger Project) that exclusively target women, collectively accounting for 9,035 clients. Other programmes such as Ophavela (PCRs) operating in Nampula Province, were initially heavily dominated by male members but, following considerable promotion, there is now almost equal gender participation.

Despite such successes, gender disparities remain and obvious in programmes serving the South and North. This disparity was clearly demonstrated when the FCC programme was extended to the North. In the South female clients outnumbered men by a factor of two to one. In the North, using the same methodology, FCC struggled to attain 15% female participation. Larger credit programmes in the North such as the First Microfinance Programme and CCCP-CCOM (Cabo Delgado) continue to show that, despite concerted efforts to promote greater female participation, the former has managed 28% female participation while the latter, operating in rural areas, only achieved 12.6%. In contrast, CCOM (Maputo) operating in suburbs of Maputo-Matola has almost three quarters (73.5%) female participation. Regional variations have usually been attributed to socio-economic, cultural and religious differences.

Given that savings deposits have only been recently introduced by microfinance operators, it is too early to comment on gender patterns, although there are early indications that men are much more likely to open up savings accounts than women. In December, 2005 NovoBanco had 41,689 deposit accounts (the vast majority being current) of which only about a third belong to women.

2.5.6 Distribution of Microfinance Operators and Outreach

Table 4 and Map 1 demonstrate the extent of regional disparity in microfinance provision (see Annex 3 for details by operator). The Maputo-Matola axis alone is served by 14 operators who supply credit to more than half (50.8%) of nation's active micro-borrowers. Because of the higher average loan size in the Maputo area (in particular from NovoBanco and SOCREMO) these borrowers receive a proportionately higher percentage (58%) of the active portfolio. Because of the significant impact of PCR programmes and the recent introduction of savings products, the Maputo area is only responsible for 39.1% of the active savers. However, with the rapid growth of new savings accounts at NovoBanco and the recent introduction of savings products by SOCREMO, it can be predicted that the number of savers will increase rapidly, especially in the Maputo-Matola area.

The Beira Corridor (traversing Sofala and Manica provinces) has received comparatively large investments by the three commercial microfinance banks (NovoBanco, SOCREMO and BOM) and the

PCR programmes (AKSM and ADEM). The corridor now accounts for 11.7% of the nation's MFI borrowers and almost 18% of the savers.

The disparity of microfinance provision may at first seem to be unreasonably skewed. However, an analysis of the distribution of non-agricultural informal activities at least partially explains the apparent distortion. The preliminary data published by the *Instituto Nacional de Estatistíca* (INE) of its informal sector survey[68] show that of the non-agricultural informal sector activities, 42% of those involved in trading and 48% of those involved in services (excluding transport) are located in the province of Maputo or Maputo City.

Table 4: Geographic Distribution of Active Clients and Active Portfolio[69]

Data as at 30 June 2005

Area	Active Borrowers		Active Savers		Active Portfolio ($)	
	#	%	#	%	#	%
Maputo/Matola	34,164	50.8%	24,927	39.1%	9,555,700	58%
Maputo Province	3,478	5.2%	-		859,303	5.2%
Gaza	2,624	3.9%			266,519	1.6%
Inhambane	6,050	9%	6,000	9.4%	616,977	3.7%
Beira	3,554	5.3%	6,172	9.7%	1,750,000	10.6%
Sofala Province	129	0.2%	645	1%	5,160	0.03%
Chimoio	3,207	4.8%	1,873	2.9%	748,000	4.5%
Manica Province	924	1.4%	2,730	4.3%	53,760	0.3%
Tete	1,631	2.4%	-		238,000	1.4%
Zambezia	1,888	2.8%	6,050	9.5%	240,370	1.5%
Nampula City	1,433	2.1%	6,274	9.8%	548,000	3.3%
Nampula Province	2,684	4%	9,122	14.3%	441,720	2.7%
Cabo Delgado	5,246	7.8%	-		887,000	5.4%
Niassa	300	0.4%	-		200,000	1.2%
TOTALS	**67,312**		**63,793**		**$16,410,509**	

Table 5 shows the operators serving different regions in 1997 and in 2005. Map 2 shows the distribution of operators for these years. The number of operators in the Maputo-Matola area has increased considerably. Inhambane, without microfinance operators in 1997, now hosts three programmes, while provision in Niassa has decreased. Although the number of providers in the other regions has remained about the same, most of the operators from 1997 no longer exist, having been replaced by other programmes, often in different areas.

[68] INE (2006). *Infor 2004 Inquérito ao Sector Informal,* Preliminary Results, Maputo.
[69] Breakdowns by operators are provided in Annex 3.

Table 5: Operators by Province (1997/98-2005)

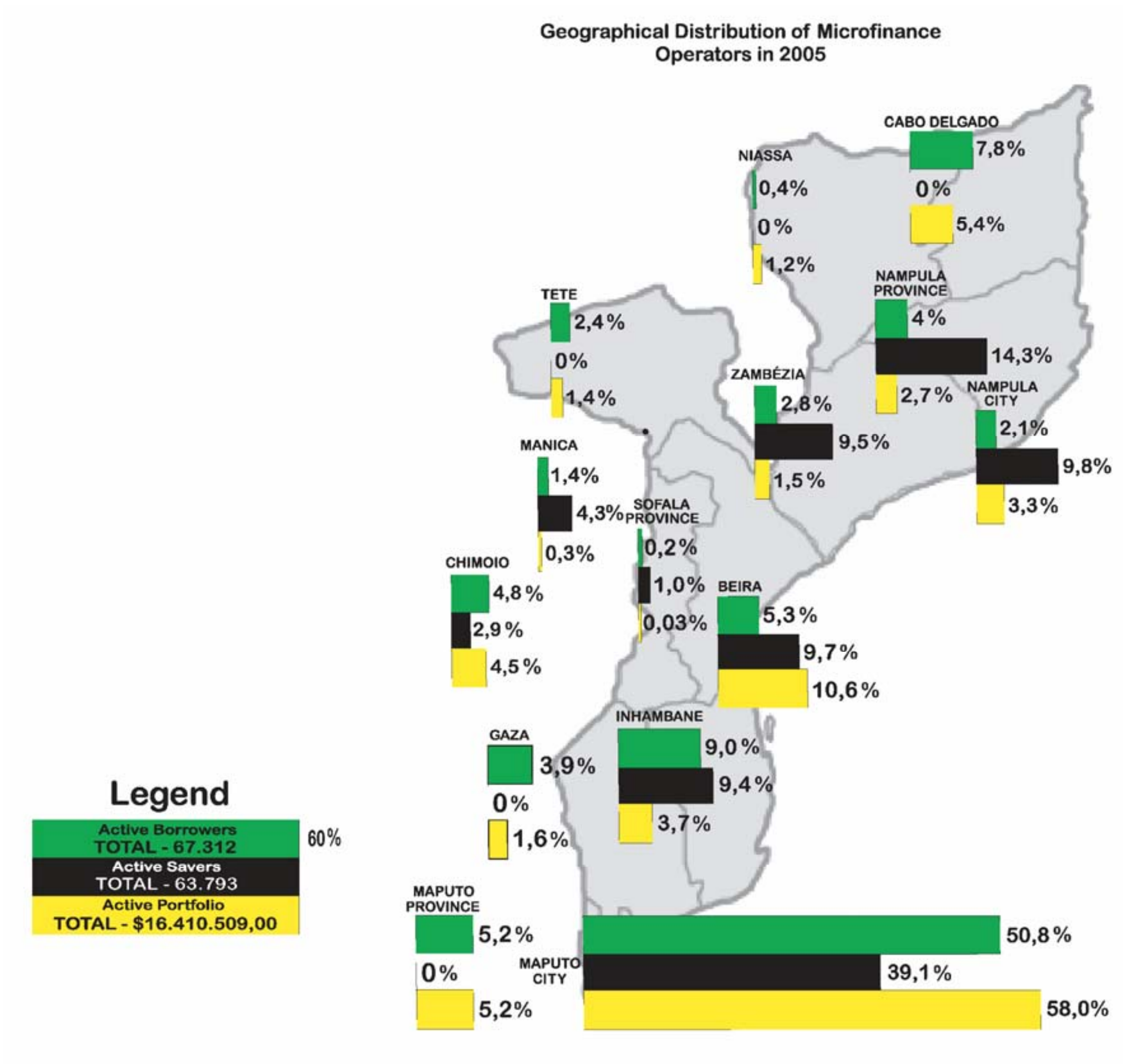
Area	1997/1998	2005
Maputo/Matola	GPE-GTZ (SOCREMO) CCCP ISCOS ITER LWF Tchuma MEDA	NovoBanco SOCREMO Tchuma BOM Assoc. Lhuwuka UGC-CPC CCCP-CCOM AMODESE KULIMA ASM Creditp Multcredito Malanga Micro Credito CPC CCC
Maputo Province	ADEMO AMODER AMRU MBEU Helvetas Helvetas-Mozambique Intermon KULIMA	Male Yeru Tchuma FDM, FCC AJAM The Hunger Project CCCP-CCOM Malanga Micro Credito
Gaza	ADCR AMODER AMRU LWF World Relief International	FDM FCC Tchuma Project Hope AMODER The Hunger Project
Inhambane		FCC AMODER Kukula
Beira	ISCOS ISCOS-Liguria PAPIR	NovoBanco SOCREMO BOM
Sofala Province	ECOTEC-MICRED LWF PAPIR	ADEM
Chimoio	CARE-CRESCE ISCOS	BOM SOCREMO NovoBanco
Manica Province	AMRU CARE-CRESCE OPMAD	ADEM AKSM BOM
Tete	AMODER HELPAGE LWF FOS	FOS-Chitima CMMEA AMODER
Zambezia	AMODER World Vision (AMF) Action Aid	BOM AMODER Project Hope Care VSL
Nampula City	CONCERN-CAWANA Caixa das Mulheres Rurais GPE	CMN NovoBanco
Nampula Province	CARE- FISH OJDR SNV	AMODER Ophavela IRAM RCRN
Cabo Delgado	AMODER GPPE CCCP	AMODER First Microfin. Prog CCCP-CCOM Assoc Progresso
Niassa	AMODER Assoc. Progresso OXFAM-UK	AMODER

2.5.7 Rural-Urban Disparity

Of the 32 operators in existence, apart from the five PCR promoters (Ophavela, Kukula, CARE-VSL Zambezia, ADEM and AKSM), only three lending programmes (CMMEA, FOS-Chitima and Assoc. Progresso) can be described as operating *exclusively* in rural areas[70] and four (CCCP-CCOM, Assoc. Hluvuku-Male Yeru, AJAM and the First Microfinance Programme), operate in *mainly* rural areas.

The five ASCA providers reach 24,547 savers in six provinces (the IDPPE established a PCR pilot scheme along the Cabo Delgado coast in early 2005). Due to the very limited capacity of PCR groups to generate lending capital, the combined active portfolio of the five operations adds up to less than $200,000, barely 1.0% of the total active portfolio in mid-2005.

Of the seven lending programmes operating in *either* exclusively or mainly rural areas, a total of 7,532 clients were reached or only 11.8% of all borrowers in mid-2005. Because of the relatively small loans, these clients received only 5.0% of the total active portfolio.



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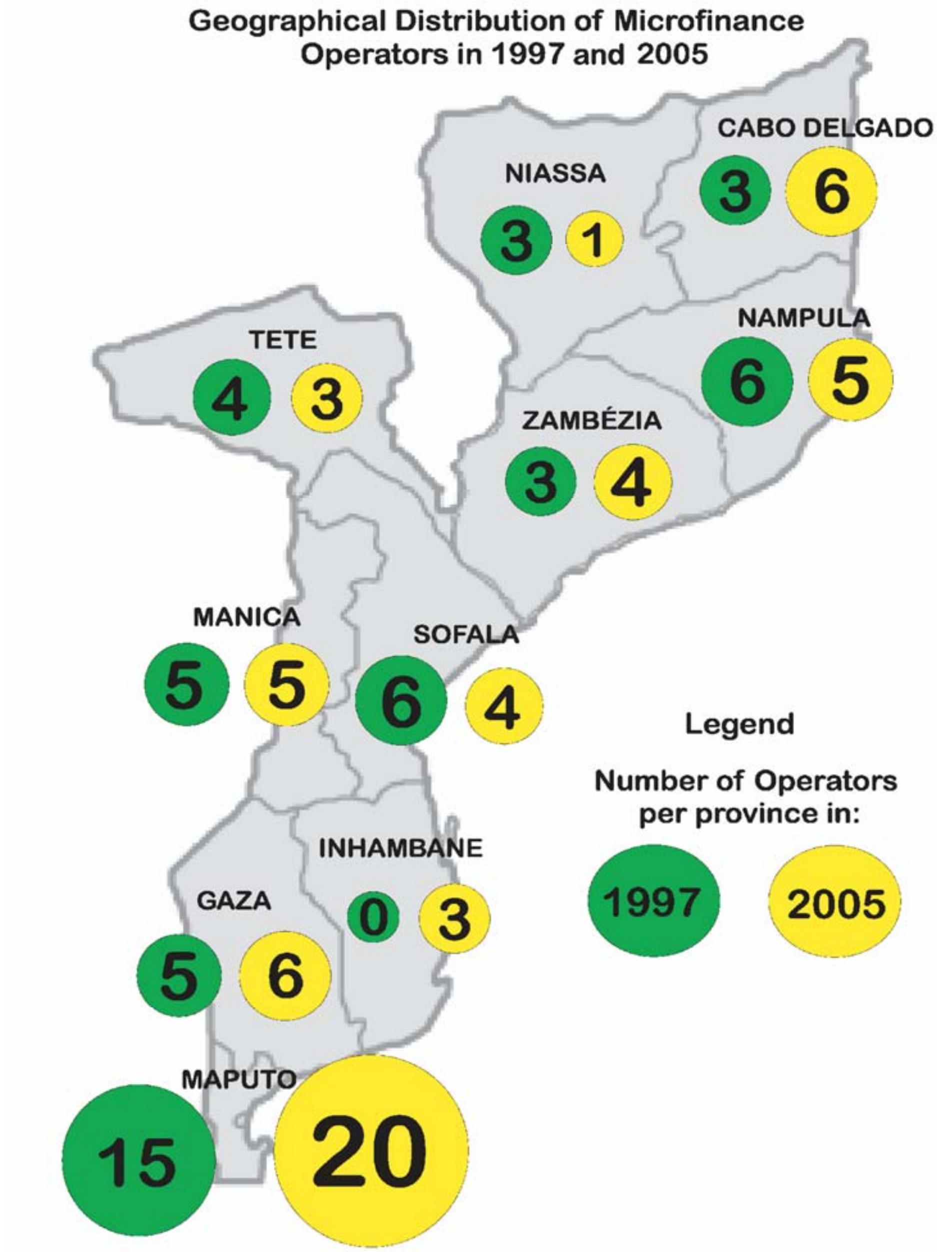
70 Rural areas are defined here as any area not considered "urban" by INE for census purposes.


Geographical Distribution of Microfinance
Operators in 1997 and 2005
CABO DELGADO
3 6
NIASSA
3 1
NAMPULA
6 5
TETE
4 3
ZAMBÉZIA
3 4
MANICA
5 5
SOFALA
6 4
Legend
Number of Operators
per province in:
1997
2005
INHAMBANE
0 3
GAZA
5 6
MAPUTO
15 20

3.0 THE IMPACT OF MICROFINANCE ON URBAN AND RURAL CLIENTS: FINDINGS FROM TWO RECENT STUDIES

Microfinance is hailed by some as one of the more successful development tools of the past decade[71]; however, focus on institutional aspects such as portfolio quality, sustainability ratios, etc., has resulted in little public knowledge about the socio-economic characteristics of the clients and how microfinance has affected them. The continued provision of microfinance without knowing much about its effect on its clients is usually justified on the basis that, if there is a growing demand for a product, the net benefits of that product should be positive.[72] Fortunately, in the case of Mozambique, two comprehensive studies were recently launched: one, a study of urban clients was finalized in early 2006 and the other, a doctoral investigation focusing on rural beneficiaries, has just reached the stage where some preliminary findings can be released.

The first study, *The Poverty Outreach and Impact Assessment of 3 MFIs in Maputo, Mozambique*[73], was undertaken on behalf of "The Netherlands Microfinance Platform" [74] and funded by some of its members.[75] It is a study of the Maputo-based microcredit clients and depositors of three large operators which together accounted for 58% of the microfinance borrowers in Maputo, almost all the deposit account holders and 86% of the value of loan portfolio. The assessment took place over the period June 2004 to February 2006.

This study represents one of the most comprehensive of this nature in Africa and is an important step towards a better understanding of urban microfinance institutions and their clients. Of particular interest is that differences in the impact of microfinancial services on smaller and larger micro-entrepreneurs have been analyzed. Section 3.1 of this chapter summarizes the main findings and their implications.

The second study is being undertaken by Katia Ribeiro, a Mozambican doctoral student at the University of Manchester. She has just completed her fieldwork among rural farming households benefiting from loans provided by the CCCP-CCOM project in Cabo Delgado Province and has kindly provided a synthesis of her initial results to demonstrate the impact of these loans on rural clients. Through this research, we have a study which complements that of the Dutch Microfinance Platform, in particular for small-holder households who have applied credit toward increasing the production of their crops. This comes at a crucial juncture for microfinance in Mozambique, with hopes being pinned on microfinance to reduce the poverty of rural Mozambicans (see next chapter). Section 3.2 of this chapter briefly reviews the major findings that have so far emerged from this study.

3.1 Urban Clients: The Results of the Poverty Outreach and Impact Assessment in Mozambique

By Gabrielle Athmer and Fion de Vletter[76]

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[71] "Microfinance has become one of the key driving mechanisms towards meeting the MDG's, specifically the overarching target of halving extreme poverty and hunger by 2015"; from the speech to launch the International Year of Microcredit by Mark Malloch Brown, Chef de Cabinet, Office of the Secretary General to the United Nations (18 November, 2004).

[72] Some such as T. Dichter in his controversial article *Hype and Hope: The Worrisome State of the Microcredit Movement* (2005) (see www.microfinancegateway.org for an abridged version; a full version of this paper is available on www.omidyar.net) argue that the positive effects of microfinance have been over-exaggerated and need to be more closely monitored.

[73] The study was carried under the supervision of Gabrielle Athmer (lead researcher). The rest of the research team consisted of Hans Bekkers, Henriqueta Hunguana (ICC), Benedito Murambire (ICC) and Fion de Vletter.

[74] Members of the Dutch Microfinance Platform include: Hivos, Novib, FMO, ASN Bank ,ABN Amro, Cordaid, DOEN Foundation, Icco, ING, Interpolis, Ministry of Foreign Affairs, Oikocredit , Rabobank Foundation ,SNV, Triodos Bank (see: www.microfinance.nl).

[75] Hivos, Novib, FMO, Doen Foundation and the Netherlands Platform of Microfinance with the support of the Ministry of Foreign Affairs.

[76] This summary is extracted from the overall synthesis report of the Impact Assessment entitled *The Microfinance Market in Maputo, Mozambique – Supply Demand and Impact: A Case Study of Novo Banco, SOCREMO and Tchuma.* The full report will be available at www.microfinance.nl.

3.1.1 Objectives

The multi-phase impact assessment study *Poverty Outreach and Impact Assessment in Maputo, Mozambique* was undertaken with two principal goals:

External goal: *to provide reliable evidence of the diverse impacts of micro-financial services on different categories of clients, in order to be able to justify the use of public funds.*

Internal goal: *to provide reliable evidence of the diverse impacts of micro-financial services on different categories of clients, to inform strategic planning of MFIs.*

3.1.2 Methodology

The MFIs chosen for the study were those in which various members of the Dutch Microfinance Platform had different interests. These MFIs, henceforth referred to as MFI A, B and C, happened to be the three largest MFIs by portfolio, each providing individual loans but having very different institutional histories.[77] The three MFIs are financially sustainable and are each others' main competitors in Maputo City.

It was not a choice to focus on individual loans but the number of solidarity group members served by MFI A was too insignificant to be analyzed.[78] Clients receiving individual loans, usually backed by asset guarantees are, by implication, from the higher end of microfinance clients.

The research was implemented in a participatory way with the management of the MFIs having a considerable input in each stage of the study including: the definition of hypotheses, the choice of indicators and the design of the questionnaires, while commenting on the reports emerging from the different phases of the study.

An important feature of the assessment was the division of clients into categories, premised on the understanding that the impact of microfinance varies for different types of clients. The participant MFIs chose loan size as the criterion for the stratification of the clients. Loan sizes were divided by three categories: the low loan category includes loans up to 7,499, 999 MT (around $327); the middle loan category includes loans from 7.5 million MT– 19,999,999 MT (from $328 – 868); the high category includes loans of 20 million MT and more ($869).[79]

It was assumed that impact would more fully manifest itself after a period of at least two years. For that reason the assessment focuses on the more-than-two-year-old microcredit clients of the three MFIs and depositors from two MFIs.[80] To a limited extent ex-clients (dropouts) were studied. They are defined, for the purposes of the assessment, as clients who did not return to the institution within a period of six months after the repayment of the previous loan. To be able to compare the interviewed dropouts with the interviewed active clients, "dropouts" must also have been with the institution for more than two years prior to leaving. However, MFIs B and C also provided general information on the number of all dropouts per loan category.

Assessing impact on the client level is a methodological challenge mainly because of attribution, as many factors influence impact such as macro economic conditions, client characteristics and product features. Moreover, loan fungibility makes it difficult to trace the application of the loans. In the ideal world, if a client applies credit to increase merchandise stocks and business performance increases,

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[77] MFIs B and C are registered as commercial banks, MFI A as a cooperative. Both MFI A and B started as pilot projects in the early and mid 1990s; MFI C started off as microfinance bank ("micro bank") in 2000. MFI A is the only institution that was not launched by an external agency. The support and ownership structure (investors, funding agencies and TA) of MFI B and C is more extensive and solid than for MFI A which is currently considering transforming into a bank to attract more investors.
MFI A strives for striking the balance between sustainability and reduction of poverty through reaching poorer clients; MFI B and C have a more commercial approach and aim for increasing breadth of outreach including also SME (Small and Medium Enterprise) lending. MFI A is the only MFI with a specific poverty focus and with the objective to reach further down the market. Despite its poverty focus and strong portfolio performance, it has difficulties to attract sufficient funding.

[78] MFI A started by providing solidarity group lending but later switched to individual lending. Lately, in an attempt to reach poorer clients, it has decided to re-introduce solidarity group loans.

[79] Exchange rate: 23,000 meticais = USD $1(June 2004).

[80] MFI B had only introduced deposit facilities at about the time of the in-depth interviews.

the *impact chain* is clear and the impact is obvious. Unfortunately, reality is more complicated and is it better to speak of an *impact web* made up of many factors influencing each other, making it much more difficult to disentangle the causes and their effects.

This study dealt with this challenge by using a mix of research methodologies, thus enhancing the reliability of its findings by examining similar issues from different perspectives. The following methodologies were applied by the study:

- Analysis of **historical loan portfolio data** for each MFI, divided by loan categories, to obtain an understanding of characteristics of the MFIs and the borrowing and repayment patterns of each loan category.
- Analysis of **loan appraisal data** of at least two-year-old clients of two branches in Maputo for each MFI.[81] In total, the loan appraisal information for 1,287 clients and 78 ex-clients (having left after a period of at least 2 years) was analysed, providing an insight into client characteristics and possible impact per loan category.
- A **sample survey to assess the poverty level of MFI A's Maputo clients** by category in comparison with the Maputo population.[82]
- **In-depth interviews with a large number of clients and ex-clients** of each MFI, providing the clients' perspective on use, impact and quality of services of MFIs. Moreover, the interviews gave an insight into clients' use of other financial services, including informal and the clients' perspective on their business environment.[83]

3.1.3 The Urban Socio-Economic Environment

Before examining the results of the impact study, a brief overview is made of both the informal economy where almost all the activities of urban microcredit clients are located as well as the informal financial systems prevailing in the environs of Maputo.

The Informal Economy

Our knowledge of the informal sector in Maputo has been largely based on a series of small sample studies starting from the late 1980s. However, in 2004/2005 the first systematic nation-wide survey of the informal sector was undertaken by the *Instituto Nacional de Estatística* (INE).[84]

The size of the informal sector has been subject to some debate but all estimates indicate a substantial contribution.[85] In Maputo it was found to be the largest source of employment (mainly self-

[81] MFI C retrieved the loan appraisal information of all (807) more than two-year-old active clients from two branches in Maputo City. From MFI A and MFI B, a sample was randomly selected consisting of respectively 291 and 189 active clients. The data has been weighted and corrected for inflation of Maputo. A sample of 78 dropouts who had been clients for more than 2 years was selected from MFI B. However, MFI A and MFI C did not provide information on dropouts due to time constraints, combined with, in MFI A's case, limitations of its MIS.
[82] For the assessment of MFI A's clients' poverty level, a quantitative survey has been conducted among 164 (ex) clients of MFI A, who had been credit clients for more than 2 years (April - May 2005). This sample was drawn from the sample used for the analysis of loan appraisal information. Results were weighted in order to be representative for all more-than-two-year-old (ex) clients of MFI A. The poverty assessment included both dropouts and active clients. The assessment compares the poverty level of MFI A's clients in Maputo City with the poverty level of the overall population in Maputo City. On the basis of the findings of the national household budget survey (Instituto Nacional de Estatística (INE) (2004*). Inquérito aos Agregados Familiares Sobre Orçamento Familiar. Relatório Final*, Maputo, Mozambique), the most powerful indicators for poverty levels defined as household expenditure levels were identified. These indicators proved to be housing characteristics and availability of consumer durables.
[83] In-depth interviews were conducted during the period June – September 2005 with a total of 140 clients, stratified as follows: 10 active clients per loan category per MFI; 10 dropouts per MFI; 10 clients who had (exclusively) deposit accounts of MFI C as well as MFI A. The credit (ex) clients were selected randomly from the sample for the loan information analyses. Dropouts were chosen from the sample of 2-year-old clients active by June 2004 but who had voluntary dropped out afterwards and had not taken a loan 6 months prior to the time of the interview. To ensure rigour of the data obtained from the interviews, the so-called 'Qualitative Impact Protocol', or *QUIP*, developed by *Imp-Act* was used. Statistical analysis requires a critical sample size, while this is not the case with qualitative research: the more interviews held, the more benefits in terms of useful data. However, to be able to understand the main problems of clients of a specific category, the minimum number of interviews held per category should be 10 (*Imp-Act* Practice Notes 2004).
[84] INE (2006). *Infor 2004 Inquérito ao Sector Informal Preliminary Results*, Maputo.
[85] Direcção Nacional de Estatística (DNE) (1993). *Relatorio sobre os resultados finais do inquerito às famílias na Cidade de Maputo (Vol 1,)* National Planning Commission, Maputo. This survey of families in Maputo estimated that the urban informal sector provided about 43% of Maputo's income. Pinto de Abreu, using a monetarist approach, estimated the informal sector contribution to be about 33% of GNP. (Pinto de Abreu, A. (1996). *Sector Informal em Moçambique: uma abordagem monetarista.*) Navia and Kaufmann estimated that the informal sector in Beira accounted for 60% of the city's income (Navia, E. and F. Kaufmann (1999). *Abordagem sobre Pequenas Empresas em Sofala*, UCM-GEA Consult Paper 1, Beira).

employment) for women.[86] Preliminary data from the INE informal sector study found that the agricultural sector overwhelmingly dominates both the informal sector and the participation of a large majority of the population aged over 6 years. Disaggregating the data shows that non-agricultural informal sector activities absorb almost 600,000 individuals vs. just over 1 million individuals absorbed by the formal sector (including agriculture). Trading and services (excluding transport) account for just over three-quarters of the non-agricultural informal sector participants. Of particular significance to the microfinance operators is that 42% of all those involved in trading and 48% of those providing services are located either in Maputo Province or Maputo City.[87]

Often called the "sector of last resort", this may be true for many, but data collected in the mid-1990s found that a large proportion of informal sector operators were earning substantially more than lower-level wage earners.[88] Given the diversity of the sector and the economic backgrounds of those operating in it, studies, not surprisingly, demonstrated a very wide variation of earnings from the sector.[89]

The poorer elements of the informal sector were often found to work seven days a week with only a short break to worship on Sundays. One survey of female traders found that they worked on average 10 hours per day and almost no one took leave; most did not stop their activities during national holidays and almost two-thirds claimed that they were not free over weekends.[90]

Most households involved in informal activities have at least two sources of income, usually pursued by different household members[91], though individual members with two or more income-earning activities are not uncommon. Many households will have at least one member earning wages but, despite minimum wage legislation, lower wage levels normally cannot support the basic needs of an average family.

In 1996, a study of informal and formal sector workers in Maputo and Beira found that those involved in informal activities tended to be young, with the vast majority being less than 35 years old. Most can be considered literate, with about 70% having achieved at least 4th *classe*. By comparison, unskilled factory workers tended to be older (the majority being over 35 years with lower levels of education).[92]

The same study found that start-up capital needs averaged around $40 and came mainly from personal savings. Few borrowed money and if they did, they did so through family or friends. Average net monthly income was very low (about $50) with less than 10% earning more than $100. Most activities were done on a self-employment basis, with less than 20% employing someone. Wage rates for informal sector employees were considerably below minimum wage levels, which over the years have hovered between $40-50 per month.[93] They were also subject to exploitative conditions[94] that appear to continue.[95]

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[86] The UNDP (2001). *Mozambique: Gender Women and Human Development – An Agenda for the Future,* National Human Development Report cites that 77.9% of economically active urban women and 50.3% of men are engaged in the informal sector.

[87] The situation is less skewed for formal sector participation, with less than a third (31.5%) being located in Maputo Province or Maputo City.

[88] See F. de Vletter (1996). *Study of the Informal Sector in Mozambique (Maputo and Sofala),* Poverty Reduction Unit, Ministry of Planning and Finance. This study, in addition to targeting informal sector operators, also interviewed unskilled factory workers. The study found that despite relatively long service records, wages of the factory workers were still shockingly low and many who claimed to have worked for about 20 years were *still* earning the minimum wage. About two-thirds depended on incomes earned by other family members (usually from the informal sector).

[89] See P.D. Little, P.D. and I.B.L. de Coloane (1992). *Petty Trade and Household Survival Strategies: A Case Study of Food and Vegetable Traders in the Peri-Urban area of Maputo, Mozambique,* USAID, Maputo. Although the traders' average earnings of about $40 per month were about twice that of average formal sector wage earnings, 70% earned considerably less than this, with about half earning about the same as formal sector wage earners. De Vletter's 1996 study found a modal monthly income of $50-100 in Maputo vs $20-50 in Beira.

[90] See S.R de Abreu (1994). *A Mulher e o Sector Informal p*aper presented at the seminar "Mulher e o Sector Informal" organized by Frederich Ebert Stiftung and Muleide, Maputo.

[91] See D.E. Sahn (1993). *Living Standards in Maputo: a Descriptive Report,* Food and Nutrition Policy Program, Cornell University, Washington. The study found that in Maputo one-third of the households earned an income from only one activity, 40% had two sources and 27% had three or more.

[92] See de Vletter (1996) op. cit.

[93] Ibid.

[94] Abreu (1994) op. cit. found that 89% of the informal sector employers interviewed did not allow leave, 72% did not permit officially recognized holidays and 72% did not give off week-ends. The majority are paid in kind (principally food and lodging). Less than one-tenth claimed to pay wages (usually at very low levels - $5-10 per month).

[95] In 2005, enquiries made during the in-depth interviews of the impact assessment revealed that the standard rate earned by informal sector assistants for shoe sellers was about $20 per month.

A study commissioned by MMF in 2004 attempted to evaluate demand for credit of small market vendors in the markets of the City of Maputo.[96] The study found that the greater part of the vendors' businesses have been getting weaker. Only about a tenth of the vendors had a loan, and a large majority of those had borrowed from an MFI. Of those who did not borrow, a little more than a third said that they would be interested.[97] The study also found that many vendors use advances from their suppliers, and think that these advances involve fewer risks than loans.[98]

Most informal sector traders work within an economic environment prone to seasonal fluctuations (normally linked to *festas* such as at year-end, Easter, other holidays, especially long weekends) and more regularly at each month-end (pay days).

An important aspect of the informal sector is that the majority of vendors and service providers pursue what can be considered to be survival activities because of the lack of economic alternatives. Such activities require little more than the most fundamental basics of selling and, due to very limited entrepreneurial aspirations do not change or grow much. A relatively small percentage can be considered much more entrepreneurial with inherent skills that could (given appropriate stimulus such as credit) elevate them to more sophisticated levels of business, normally manifested through diversification, capital investment and rapid growth.

The high number of respondents claiming to have suffered from weakening businesses, as found by the MMF study cited above, may be at least partly explained by four important negative influences recently affecting Maputo's urban economy. The first is that, following the economic growth and employment creation associated with the "mega project" Mozal (aluminum refinery), the labour-absorbing capacity of the Maputo-Matola economy has slowed, resulting in more of the economically active population seeking survival in the informal sector. This has led to increasing competition especially among those activities requiring minimal start-up capital. The second problem has been the significant revaluation of the rand (associated with the devaluation of the dollar)[99] resulting in higher import prices (most goods sold in the market are imported from South Africa). The third problem has been the increased price of fuel (increasing by about 100% over 2005)[100] which has affected transport prices as well as general purchasing power. Finally, much stricter controls at the border resulted in reduced profit margins and the frequent confiscation of under-declared merchandise.[101]

Informal Financial Practices

Although a comprehensive study on informal microfinance has never been conducted in Maputo, there is no doubt that more people are served by informal microfinance systems than by MFIs. The impact assessment interviewed clients about the use of informal financial services and found that most clients with low and mid-level loans are involved with informal financial practices (see discussion in section 3.1.4). In Maputo, two systems stand out, both forcing members to save. The rotating savings and credit association (ROSCA) popular in many parts in the world, is common in Mozambique (particularly in urban areas) and is called *xitique*. The second is a system of daily savings deposited with collectors operating at the markets, called *xitique geral* and is limited to the Maputo-Matola area. Informal funeral associations are popular among the slightly better off. Less prevalent, but still significant, are the commercial moneylenders.

[96] See K.Murdoch (2004). *Study of the Demand for Credit in Markets in Maputo, Mozambique*, Mozambique Microfinance Facility.
[97] Of the 62% that stated they were not interested, 44% stated they didn't want to take on a loan (fear of assuming such a responsibility, fear of goods being confiscated, very complicated and expensive to request a loan), 39% stated that they were unable to take on a loan (lack of guarantees or the business was very new) and11% stated they did not need a loan.
[98] The role of commercial credit in Mozambique has not been adequately researched but recent evidence from other countries (e.g. Nicaragua) suggest that commercial credit (e.g. wholesale advances) is increasingly important in relation to cash loans (see A. Legovini (2002). *The Distributional Impact of Loans in Nicaragua*, World Bank).
[99] Since the end of 2001 when the rand hit its lowest point of approximately 14 per US dollar, the rand has gradually strengthened, though erratically, to stabilize at approximately 6 per dollar in early 2006.
[100] During the period February-November 2005 prices of petrol and diesel approximately doubled, having increased from 14,000 to 29,350 MT/lt for gasoline and from 13,900 to 26,050 MT/lt for diesel.
[101] In prior years informal sector traders could quite easily smuggle goods through the border. The government has since clamped down and traders now accept that they are playing a form of roulette with the customs officers. The general modus operandi appears to be to not declare 100% of the goods as traders say that would make it impossible to make any profits. It seems that most declare about 30% of their goods at the border. However, the minibus taxis in which they usually travel are randomly searched along the highway to Maputo, often resulting in the confiscation of all their merchandise due to inadequate disclosure.

Apart from the impact study and a few previous studies with smallish samples, there is little empirical evidence on how extensive these practices are. The studies that did look at *xitique* and *xitique geral* membership found quite varying percentages, influenced by the sample group and the location of the survey. [102]

Xitique is a form of forced savings in a group with peer pressure being important to increase self-control on spending. The system is especially popular among women but men also participate. Typically, the group consists of 4 to 10 people, friends or family members. On a periodic basis, (daily, weekly or monthly) a certain amount of money is saved. The money is paid out in rotation to each one of the members who are part of the group. There is a wide variation in xitique arrangements. For example, sometimes the kitty is in kind, e.g. in pots and pans, which prevents the participants from using the money for other reasons than they planned for. The amounts deposited vary considerable, but can constitute a large portion of the income - up to one third or more.

Xitique geral is said to have been introduced in Maputo in the nineties and continues to operate exclusively in Maputo. This system of money collectors exists in West and Central Africa and in parts of India, but not in other parts of Southern Africa. It has probably been introduced in Maputo by immigrants. The system is mainly used by market vendors in Maputo and has as its objective to facilitate access to savings services. The savings are made based on monthly contracts, which establish the daily amounts to be deposited with a collector's fee of one day's deposit. The market vendors consider the monthly lump sum as their 'salary', which they use for paying their monthly bills including their loan instalments.

Funeral associations operate generally in groups of 20 to 30 persons, often from the same family. Each one of the members pays a monthly amount. In the event of a death, the members of the fund and their direct relatives—spouse, parents and children—are entitled to a coffin. Sometimes, other expenses, such as hospital costs in the case of serious illness are also covered by the fund. Similar broader arrangements were encountered between related families (family funds), with each family required to contribute a monthly amount into a common account that could be accessed for a commonly agreed purpose, ranging from sickness to university fees.

To date there are relatively few money-lenders, making individual loans in amounts that range from the equivalent of a few hundred to a few thousand dollars. The most commonly used guarantees are the good reputation of the borrower, post-dated cheques and personal possessions. Generally the interest rate is 20% per month or more (up to 50% monthly). Mostly, interest is paid monthly and many moneylenders do not accept partial reimbursements. This can result in a longer-term dependency of the moneylender, when the person is unable to accumulate the entire lump sum at once. Mozambique has so far been spared the *micro-lender* (loan shark) industry that has rapidly spread throughout Southern Africa.[103] In the recent past, Maputo in particular has witnessed the registration of several credit providers lending at about 10% per month (declining balance) mainly to salaried workers who guarantee their loans with post-dated cheques.
The emphasis of informal systems like the money collectors is on "saving-up", which requires gradual deposits to be built up to reach a certain target amount. Interest-bearing microfinance loans do the opposite ("saving down") by allowing clients to receive funds bulked at the beginning of a time period and repaid through subsequent installments.

3.1.4 Characteristics of the Assessed Clients

Client characteristics, as determined from loan appraisal data and the in-depth interviews, showed very close similarities across the three MFIs studied, probably accounted for by the fact that the

[102] Abreu (1994) op. cit. found that 36% of her sample were members of *xitiques* while de Vletter (1995) (*Urban Poverty and Employment in Mozambique: An Analysis of a Deepening Crisis and its Policy Iimplications*, Poverty Alleviation Unit, Ministry of Planning and Finance) found 14% of those involved in informal sector vending or services to be members. D.H.Graham (1991) (*Peri-Urban Baseline Research Results: Maputo,Mozambique* USAID/Ohio State University), found that 18% of household heads or spouses were members. The average size was found to be 5 members meeting on an average of every 20 days with an average contribution of about $4 per meeting . A MEDA study of Xikelene market in 1997 (unpublished) found that 78% of the 200 respondents deposited daily with a mobile banker *(xitique geral)* and 15% of the respondents were members of group *xitiques*. It is quite likely that in some markets the prevalence of *xitique geral* is much higher than in others. Xikelene market in particular had a pervasive presence of mobile bankers. Murdoch (1994) op. cit. found 27% of her sample belonging to a group *xitique.*
[103] In Botswana for example, micro-lenders have become prevalent, commonly charging an effective annual interest rate of 250% per annum, and an important factor behind the an average debt of $500 per person (BBC report on consumerism in Botswana, 20 February 2006).

business loan products of the three MFIs are similar in terms of their loan conditions. The reader is reminded that the characteristics described here apply to clients with activities in Maputo and who have borrowed over a period of at least two years from one of the institutions observed.

One of the more surprising findings is the relatively older age of the clients. Despite the youthfulness of the informal sector, the average age of the more-than-two-year old client was over 40 for all three MFIs. There was no obvious explanation for the scarcity of younger clients, though lack of asset guarantees (exacerbated by the fact that many young people continue living with their parents due to a lack of affordable housing), perceived higher risk because of behavioral traits, and residential instability were indicated as possible factors.

Females dominated the three loan categories, though in diminishing proportions, as loan categories increased (except in the case of MFI A which specifically targets women). Data from the interviewed MFI B clients also suggested that a high proportion of the clients are likely to be single parent (mainly female) households. Qualitative interviews found that a large majority of clients had at least two sources of income. MFI C´s clients were relatively well educated: more than half (58%) of their clients had reached secondary school, while more than a quarter (27%) of MFI A's had. Very few clients had no education at all.[104] Data collected by the Maputo household expenditure survey found that of the population age group 25-65, more than one-quarter (26%) had no education at all and that only 20% had secondary education.[105]

The majority of MFI B's and MFI C's clients have fixed business assets while a minority of MFI A's do. Fewer women own business assets than men, the difference being rather large in the case of MFI A. A majority, albeit a small one, of clients operated their activities on their own. Between a third to a half of the clients had employees, with men having a slightly higher propensity to employ workers than women.

Only a small minority of the two-year-old clients had a current account at their MFI: 13% of MFI C's clients[106] and 28% of MFI A's. Only 1 % of MFI C's two-year-old clients had a term deposit. Interviews showed that most of the middle and high loan category borrowers had previous experience with commercial banks in terms of holding accounts but little in terms of previous loans. Many low loan clients still have no deposit accounts despite the introduction of accounts by MFI C and MFI A, for some time at the time of the in-depth interviews. MFI C currently has more than three times more depositors than borrowers, attracting many clients who are not interested in credit. The assessment findings indicate deposit accounts have considerable potential for deep outreach. During the interviews it became clear that the low average value of deposits with the observed MFIs does not reflect the savings capacity of the clients as most deposit clients also hold other bank accounts and/or belong to informal savings systems.

Although there was considerable variation between the MFIs, the in-depth interviews revealed a pattern suggesting that the majority of low and middle-level loan clients, and a significant minority of those with high loans, belonged to x*itique* groups or saved through daily deposits (*xitique geral*). Despite the common assumption that people transit from informal systems to formal banking services when they have the opportunity, the evidence from the assessment suggests that a there is a tendency to transit, but not a strong one: clients with higher loans were more inclined to have deposit accounts and showed less inclination to participate in informal financial arrangement. Interviews with deposit holders (see section 3.1.11); however, found that wealthier clients tended to engage in a broad mix of formal and informal financial arrangements, suggesting that the importance and usage patterns of informal financial systems requires further study.

Very few clients applied any vocational skill to their activity. Although most clients were found to have considerable experience in their particular activity, there are virtually no barriers (apart from minimum merchandise costs) to potential competitors for most types of vending activities. According to the interviewed clients, the main threat to the performance of their businesses was increasing competition.

[104] MFI C is the only MFI collecting information on client education for loan appraisal. Education levels of MFI A's clients are known through the poverty outreach assessment.
[105] Calculation made by impact research team on the basis of data for Maputo from the household survey of INE (2004).
[106] From the beginning of 2005, all clients of MFI C have deposit accounts, as opening of the account is one of the requirements to qualify for a loan.

For market vendors, this came mainly in the form of vendors selling along the open streets. This is particularly relevant to low loan clients who have minimal capital and entrepreneurial skills to give them an advantage over new market entrants.

Although some clients had developed a variety of imaginative activities, most were engaged in activities that could be segmented into the following types:

- Vending from fixed spaces in markets, streets and home, usually from a table or box, requiring minimum capital investment apart from, in some instances, scales and/or a calculator/cell phone (depending on the product).
- Vending from a closed stall in a market, a shop on the street or a shop located on the plot of the owner's residence. These activities require substantially more capital investment and are usually undertaken by clients with high-level loans.
- Itinerant cross-border traders who regularly travel to Swaziland or South Africa to buy goods for wholesaling to traders, typically those mentioned above. Costs are largely restricted to merchandise, transport, lodging, customs and storage of merchandise not sold on return. The biggest risk faced by these traders is full discovery of merchandise by customs officials. Usually only about a third of the merchandise is declared, otherwise such trade is said not be lucrative. Discovery through random checks (usually on the main road to Maputo) will result in severe financial penalties.
- The most common form of services found were bars and/or restaurants usually referred to as *barracas* and *quiosques.* Other common services include beauty salons and public cell phones. The capital investment costs of these activities are similar to those of setting up small shops if not higher and usually require 1-2 employees.

3.1.5 Client Borrowing Patterns

Reasons for Borrowing

The clients assessed were obtaining loans meant for business application, and in most cases contractually stipulated for working capital loans. Increasing merchandise stock is not only done in anticipation of higher demand, but also for increasing efficiency (less travel time), reducing costs through bulk purchases, and to create demand (more articles are said to attract more customers). However, as will be seen later, many clients apply their "business loans" to non-business purposes, in particular for residential construction or rehabilitation[107] or for the purchase of household durables. Loans are also applied to covering unexpected expenses arising from crisis or for expenditure smoothing for households that typically suffer from unpredictable income fluctuations.

Client Retention Rates

Although the three MFIs studied are relatively young, by far the greatest number of clients served by these institutions is no longer with them. The assessment study took a longitudinal perspective on retention, taking into consideration all new clients registered between July 2001 and June 2002, and then assessed the records of all those clients who remained active by end-June 2004. Although the results could be somewhat distorted by active clients who happened to be resting at end-June 2004, the findings showed that only about a quarter of clients remained after two years.[108] Looking at the phenomenon from a different perspective, information collected for the 2005 microfinance survey showed that the three MFIs collectively had just over 26,000 active borrowers in mid-2005. However, the same operators stated that, from about the same time (1999 for MFI A and MFI B and 2000 for MFI C), they together served a total of 90,000 individual clients, giving a ratio of almost 3.5 of total clients to active clients (a little lower if taking into consideration double-counting of the relatively few clients who change MFIs).

[107] It should be noted that MFI C does in fact offer housing loans which it prefers to call "renovation loans" as they are usually used for small projects with flexible terms and flexible amounts.
[108] Twenty-three percent of MFI C's clients remained and approximately 15% of MFI B's. The very low rate for MFI B is largely explained by the restructuring process it underwent, which resulted in a significant reduction of its low category clients. Moreover, the percentage could be higher because some inconsistencies were found in the provided data due to the transference of clients to newly opened branches. MFI A undertook its own analysis which found that in March 2006 about 25% of its clients who registered in or before June 2002 were still active.

Concerned with the high dropout rates, MFI A commissioned a study to examine the extent and causes of client dropout. Client retention is important because longer-term clients increase average loan balance and reduce loan delivery costs. MFI C estimated that clients only start becoming profitable to them after about three loans (close to two years). Moreover, higher client retention rates become critical in the increasingly competitive and saturating microfinance market of Maputo City.

Annual dropout rates for over the period July 2002-July 2004 showed that in the case of MFIs B and C, the rates exceeded 40% while for MFI A the rate was just below 30%.[109] Consistently, a disproportionate part of the dropouts (voluntary and involuntary[110]) belonged to the low loan category. In the case of MFI B, on average 75% of all dropouts were from the low loan category (probably the poorer clients) and, in the case of MFI C, 64%. According to MFI B, almost half of the dropouts did not have repayment problems. The assessment did not look at impact on the majority of dropouts who leave within two years of being a client. This still leaves an important area for further research as it is possible that, apart from the clients who satisfy their credit needs or were expelled, other clients leave because they did not benefit from the loans. The in-depth interviews suggest that the effect of crises might be an important influence in forcing clients to quit: while just over half (52%) of the still active clients faced a crisis, 70% of the clients who dropped out (after two years) did.

The in-depth interviews suggested that few clients switch to other MFIs in search of better conditions. Most clients were found to remain committed to their original MFI with little interest in finding better conditions from alternative MFIs. Interviews showed that only very few of the clients who left their MFI for reasons linked to their MFI would try to find better conditions with an alternative MFI, possibly because the products offered were so similar. Overall, few clients have parallel loans with other MFIs, though a significant minority of high loan clients did.

Clients Divided By Loan Categories

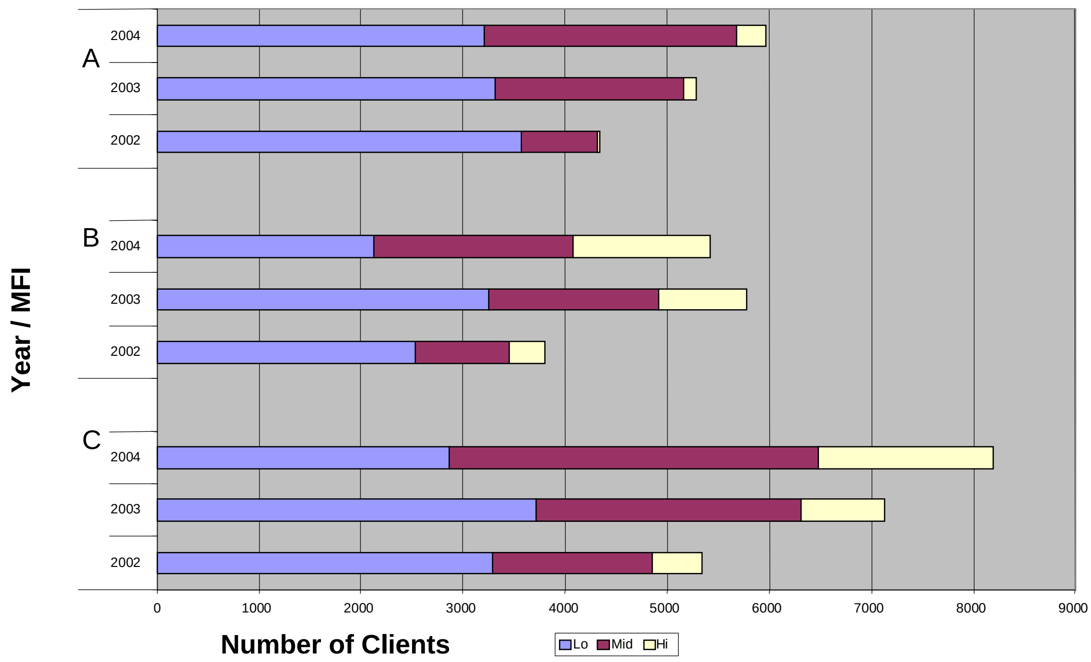
Figure 11 demonstrates that the largest portion of all clients for MFI A and MFI B is in the low loan category and in the middle category in the case of MFI C. The absolute number of low loan category clients of (poverty oriented) MFI A and of C is almost the same by June 2004. The relatively slow growth of higher category loans in MFI A is largely attributable to its regulation that all clients must start with a minimum loan size and increase them by fixed increments. The sharp decrease of Socremo's low loan category clients in 2004 is due to its policy of portfolio consolidation as part of its restructuring, which included an increase in the minimum loan amount and resulted in a reduction of the number of low category clients.

In terms of volume of outstanding portfolio, the middle loan category is the most important for MFI A: 53% of the volume of its loans belongs to this category. The high loan category is the most important for both MFIs B and C: around 60% of the volume of their business loans is from this category.

While women were the majority in all loan categories, the difference decreased with each progressive loan category.

[109] Dropout rates differ significantly according to the formula used. The calculation made for all three MFIs used the formula of Mark Schreiner as mentioned in MicroBanking Bulletin April 2001, i.e. retention rate= active clients at the end of the period/(active clients at the beginning of the period+ new clients). Dropout rate =1- retention rate.
[110] Voluntary: clients who do not reapply. Involuntary: clients who reapply and were rejected.

Figure 11. Changes Over Time In Number of Clients by Loan Category



The loan appraisal data was collected over a period during which there was strong growth in loan size (June 2002 - June 2004). The qualitative interviews, however, indicated that the following year was seen as a difficult one with many clients facing hard times economically. This seems to be reflected in the considerable slowing of loan size growth for all loan categories but especially for the lowest loan categories. The results of the interviews suggest that the highest category loans, and to some extent the middle category loan clients, are much more resistant (or even unaffected) by macro economic difficulties as their average loan sizes tended to increase in comparison to the low loan category clients, who either stabilised or reduced their loan amounts.

Arrears

Data on arrears per loan cycle of two-year-old clients showed very low averages for MFI C (just over two days), five days for MFI B to just over eight days for MFI A . The higher number of days in arrears (and lower dropout rates as discussed before) for the latter is probably explained by a more tolerant policy towards late payments as well as a more explicit poverty focus. Clients from the lowest loan category have the most repayment problems, which might reflect the vulnerability of these clients to crises and shocks. Interestingly, the more-than-two-year-old female clients of MFI B and C have more short-term repayment problems than men, especially in the age group of 30 – 39. However, most women resolve their repayment problems within 30 days. Consequently, portfolio at risk (>30 days) with regard to female clients is generally better in all categories. MFI A's portfolio at risk (>30 days) is 4%, of MFI B 0.86% and MFI C 1.96%.[111]

Resting Periods

A considerable number of more-than-two-year-old clients rest more than 30 days in between loans: around one third of MFI B and C's clients[112], and 40 % of MFI A's clients. Only a few more-than-two-year-old clients rest longer than 180 days.[113] A major influence affecting many vendors is the seasonality of their credit needs, particularly over the Christmas and Easter periods as well as over long-weekend holidays. This suggests that clients tend to borrow according their needs and

[111] June 30, 2004.
[112] The calculation of resting periods for MFI B and C's clients include loan processing time (estimated at approximately 2 – 3 days). This was not the case for the resting days of MFI A's clients.
[113] In the case of MFI C, 68% of those taking resting periods rested for less than 30 days and 16% for more than 180 days.

investment possibilities. There are indications that clients who faced a crisis took a resting period to recover from it.

3.1.6 Depth of Outreach

The UN Year of Microcredit called for increasing the outreach of MFIs as a tool to reduce poverty. MFI A was the only MFI studied with a specific poverty focus and with the objective to reach further down the market. MFI B and MFI C have a more commercial approach and aim to increase breadth of outreach, by including small and medium enterprise (SME) lending. For this reason a poverty outreach study was limited to MFI A,[114] which anticipated that the results could help it develop a strategy of expanding its services to poorer clients.[115] Because low loan clients tend to be higher risk, MFI A applies loan ceilings in order to ensure that poorer clients get sufficient attention from the loan officers, who otherwise would tend to go for the less problematic clients with larger businesses.

This study compared welfare indicators applied to MFI A's more-than-two-year-old clients with the results of the National Household Survey[116] and found that 43% of these clients had attributes similar to the top 20% (by expenditure levels) of Maputo households.[117] A small but still significant minority - 13,6 % - live below the poverty line determined for Maputo City, while this is the case for 53.6% of the Maputo population in general. The poverty line[118] for Maputo is set at 19,515 Meticais per person per day, which is $3.90 when using the dollar exchange rate at Purchasing Power Prices.[119] At the same time, it is important to recognize that many, if not the majority, of clients belonging to the upper expenditure quintile are not rich. Mozambique has a very small wealthy upper class. Though most clients live in cement houses and have electricity, interviews revealed that, with the exception of a notable few, the majority of these clients could be considered to be at the low end of an emerging middle class.

The average daily expenditure of the households of MFI A clients is $9.94 (at Purchasing Power Prices) per person per day against $8.93 per person per day spent by the households of the Maputo population. Location of agencies was important in reaching poorer households. Households of the clients of a branch located near a large market in one of the poorer suburbs were found to spend $7.42 per person per day, against $11.92 spent by households of clients from a branch in the city centre. No household was found to be under the international USD $1(at PPP prices) poverty line.

Classified by loan category (defined by last loan) we see most poor clients in the lowest loan category and least in the highest category. It can therefore be concluded that loan size of more-than-two-year-old clients is a good proxy for their wealth level. This is much less the case for the size of the first loan of these clients, which is logical, given the fact that MFI A applies a loan ceiling for the first loans.

The division of the portfolio by categories makes the trade-off between poverty outreach and sustainability more obvious: clients of the lowest loan category, who are likely to be the poorer clients, are more costly per unit of currency loaned. The lowest loan category clients cause a higher portfolio at risk, drop out more often and fewer clients of the lowest category clients take sequential loans. The middle and high loan categories are more important in terms of portfolio volumes, have shorter resting periods and show better repayment records (i.e. they are better clients in terms of institutional sustainability).

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[114] For the assessment of MFI A's clients' poverty level, a quantitative survey has been conducted among 164 (ex) clients of MFI A, who had been credit clients for more than two years. This sample was based on the sample used for the analysis of loan appraisal information. Results were weighted in order to be representative for all more-than two-year-old (ex) clients of MFI A.
[115] As part of its strategy, MFI A has reinvigorated its solidarity group lending initiative, the methodology it originally adopted.
[116] INE (2004) op. cit.
[117] The average daily expense per person is 49,708 MT against 44,637 MT for Maputo City. The average expense of clients of one branch mainly serving a large informal market is significantly lower: 37,121 MT per day against 59,614 MT for the branch located in the centre of the city.
[118] The poverty line is based on the findings of the second National Household Consumption Survey (2002- 2003). Region specific poverty lines were constructed on the basis of the Cost of Basic Needs methodology.
[119] One dollar PPP equaled 22 US cents or 5 thousand Meticais in 2004. Since the exchange rate Metical-US dollar did not change much and inflation was limited, the values in 2002/03 will not be much different. It is important to note that PPP rates were designed for comparing aggregates from national accounts and not for making international poverty comparisons. As a result there is no certainty that an international poverty line measures the same degree of need or deprivation across countries. It will be better though than the exchange rate at the banks, since it takes account of non-international traded goods and services.

As MFI A, with a clear poverty focus, has 43% of its more-than-two-year-old clients in the top 20% highest expenditure level, it can be assumed that MFI B and C would have more of its retained clients in this group. This is backed by the fact that the more-than-two-year-old clients constitute a group of whom the majority are relatively old business people, relatively well educated and with considerable business experience (see discussion on household welfare 3.1.8).

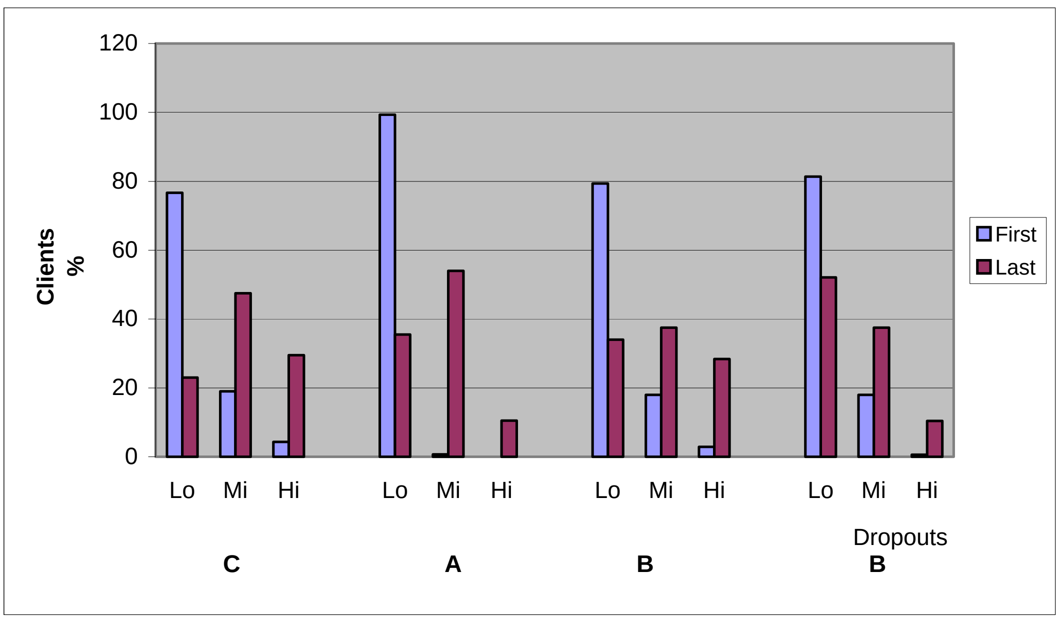
The INE household survey found that 24% of Maputo's economically active population is self-employed of which the majority could be considered to be potential beneficiaries of microfinance. The self-employed are almost equally distributed among the quintiles, with the exception of the lowest quintile where the self-employed represent only a small percentage of the population. The fact that MFI A's clients are predominantly concentrated in the two highest quintiles suggests considerable potential to reach the self-employed further down market through MFI A's solidarity group loans and savings products.

3.1.7 Impact of Credit on Economic Activities

Transition Between Loan Categories

Figure 12 shows how the loan categories have shifted over the period June 2002-June 2004[120], demonstrating that clients for all the MFIs mostly started with low loans but that the majority (of those continuing to borrow) two years later had either middle or high level loans. As indicated earlier, most clients in fact drop out while still in the low loan category.

Figure 12. More-Than-Two-Year Old Clients by MFI, Loan Category and Time of Appraisal



The majority of the clients started in the lowest category: virtually all clients of MFI A and 80% of the clients of MFI B and MFI C. Most of these clients succeeded in moving to another loan category. Due to its policy on loan growth, comparatively few of MFI A's clients moved to the third category. The percentage of MFI B and C's clients in the high loan category at the time of the last loan was almost identical. Although a similar percentage of the dropouts and active clients started in the first category, more than half of those clients who dropped out after a period of around two years had remained in this category. Results from the interviewed clients showed that for the period 2002-2004, loans grew significantly for all categories, but particularly for the high and middle category clients (all of whom graduated from lower loan categories).

[120] The amount of the information derived from the most recent loan appraisals are corrected on the basis of monthly inflation rates from Maputo City, to make them comparable with the information at the time of the first loan.

Monthly Sales (Size of Activity)

Figure 13 shows the percentages of clients who experienced growth in the size of their loans, value of monthly sales (proxy for business size) and repayment capacity, calculated on the basis of aggregated household assets. It demonstrates similar trends among the three MFIs and shows that a large majority of clients had increased their loan sizes over the period. However, the percentages of clients experiencing increased value of sales and repayment capacity were considerably smaller, albeit majorities.

The loan appraisal data showed that, in the case of MFI A, all clients in the high category (based on the last loan) experienced considerable growth of loan size and started from the low loan category. Similarly, the majority of clients in high loan categories for MFI B and C started with low loans. At the time of the first loan, the volume of sales was around seven times higher than the loan in the case of MFI B and C and five times in the case of MFI A.[121] At the time of the last loan, the similarity between the MFIs is striking with an average value of monthly sales of all clients of around 3.7 times the size of the loans. Faster increasing average loan size could be due to cautiousness of both client and MFI at the time of the first loan. It could also be due to a lack of business opportunities, of business skills, or application of loans for non-productive purposes. Significantly, the majority of clients who remained in the low loan category over two years also succeeded in increasing the value of their monthly sales. As pointed out earlier, the year following the period covered by the loan appraisal data was economically difficult, causing most low category loan clients to reduce or maintain their loan amounts, while monthly sales values for many also decreased. Many clients who did not succeed in increasing their value of sales said that their situation would have been worse without a loan.

The pattern that clearly emerged from the two MFIs without a loan ceiling was that the higher the loan category of the first loan, the lower the increase in sales.[122] For MFI C, 66% of clients who started in the lowest loan category increased the value of their sales versus 60% of those who started in the middle and 44% of those who started in the highest loan category.

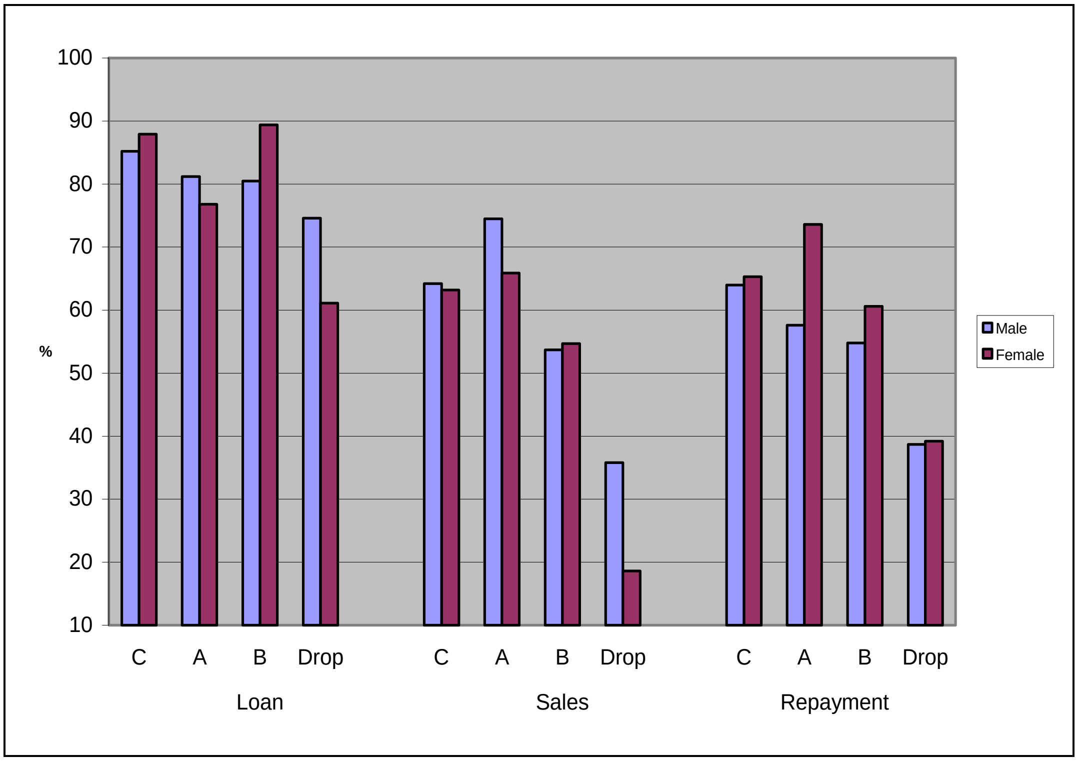
A more detailed analysis of data for MFI C's clients showed that the lowest decile, with monthly sales volume of less than $500 at the time of the first loan (approximately), showed increases of almost 185% over a two to three year period. This is compared to negative rates of growth (-11%) registered by 20% of the largest businesses, with a monthly volume of sales of more than $2,000 (approximately) at the time of the first loan.[123]

The data suggests that by the time the low loan category clients reach the high loan category, their businesses would have registered substantial growth. On the other hand, the larger micro enterprises, starting with high category loans, are unlikely to grow further without undergoing substantial structural changes. We should keep in mind that these are working capital loans with conditions not usually favourable for longer-term investments.

There is little difference between the percentage of active male and female clients whose business increased. From MFI B's dropouts, only a minority experienced growth of value of sales (36% of the male dropouts and only 19% of the female).

[121] This difference could be due to the fact that MFI A collected fewer details in relation to the value of sales at the time of the first loan.
[122] This is confirmed by regression analysis of MFI B and MFI C. Because almost all MFI A's clients started in the first category, this trend can not be analysed with regard to MFI A's clients.
[123] For MFIA and MFI B, these analyses could not be made because of limitations of the sample size.

Figure 13. Percentage of Clients with Increased Loans, Sales and Repayment Capacity



Client Responses in Relation to Loans and Business Performance

Almost all more-than-two-year-old clients felt that their loans were important for their businesses. A majority showed increased value of sales and of those who did not, many said that their business would be worse if they had not have had a loan.

Loan data of the interviewed clients showed that all the highest category loan clients for MFI A started in the lowest category (as per regulation) as did the majority (60%) of MFI B clients and 70% of MFI C's clients. Confirming the patterns observed in the previous section, loan growth patterns derived from the high loan clients *who started from lower loan categories* leave no doubt that these were the most dynamic clients, registering (on average) by far the highest growth rates from the first loan to the last loan (as at the time of the interview). Lowest growth rates were registered among those clients who remained in the lowest loan group.

When asked about the performance of their businesses, responses reinforced what had been found through the loan appraisal data which revealed that just over half had recorded increased sales. The interviews showed that just under half (48%) of the respondents felt that their activities "grew" while 43% felt that their businesses fared worse since first receiving loans.[124] The highest percentages of clients who felt they grew were in the highest loan category.[125] It should be noted that none of the interviewed clients started in the high category. The reasons for downturns in their business performance (according to respondents from MFI B) were split into three categories: i) those affected by economic influences (46.1%), ii) those affected temporarily by a crisis or unexpected event (30.7%) and iii) those who could be considered to have brought about the problems themselves - basically mismanagement (23.1%).

Interviewed high category loan clients demonstrated business strategies typically associated with entrepreneurs such as diversification, expansion and employment creation. Low category loan clients

[124] Interviews were conducted after what was considered to be a difficult year in comparison to the previous years covered by the loan appraisal data.
[125] This was the situation witnessed with MFI A and MFI B but not for MFI C, where most of the highest loan clients claimed to have weaker performance (although average loan growth for MFI C's highest loan clients was more than 300% from mid-2000 to mid-2005).

indicated that they mainly increased stock (although a significant percentage had lowered their stock recently in response to economic difficulties).

The loan appraisal data found that a minority of the clients who already have fixed business assets managed to increase their asset base. For example, in the case of MFI B and C, 48% and 36% of the clients who own fixed business assets had increased their asset values.[126]

Loan appraisal data also demonstrated that generally, clients used loans for increasing stock. Furthermore, stock values increased on average much more than sales levels. Qualitative results, on the other hand, showed that many lower loan clients felt that their stock had been reduced during the past year due to worsening economic conditions. Much less frequently, loans are used for investment in business assets and loan appraisal data showed that the number of clients with business assets did not increase. The qualitative results suggest that the interest rate is an impediment for high loan category clients and as such microfinance might be limited in its capacity to provide larger businesses funds for expanding their activities through the purchase of fixed business assets.

The total number of employees remained more or less the same over the time period studied.[127] Therefore, the findings do not support the widespread assumption that microfinance contributes to job creation. Given that the vast majority of clients invest their loans in buying more stock, the subsequent spillover effects of business expansion during a two to three year period may not have been significant enough to manifest themselves in terms of increased fixed investments or employment creation. However, the in-depth interviews show that a relatively small percentage of clients have grown considerably faster than most of their fellow borrowers and were able to diversify, expand and increase employment.

3.1.8 Impact of Credit on the Level of Household Welfare

The impact study made an attempt to code the level of well-being of the interviewed clients, based on the information gathered and observations at their home or enterprise. The "norm" consisted of a cement block house, electricity and what was considered to be a standard array of household assets.[128] Very few households were encountered that could be considered significantly below the norm. The poverty assessment study found that more than 90% of MFI A's at-least-two-year-old clients had electricity vs. less than half of the Maputo citizens and that twice the proportion owned cars (about one-quarter vs. an eighth). Interviews revealed that many clients applied at least part (and often a significant part) of their "business" loans to what was referred to as *"futuro"*-related expenditures i.e. the construction or rehabilitation of their residences or acquiring household goods.

The qualitative interviews showed that the majority of clients from all client categories felt that their overall level of household welfare had increased since starting to borrow and the vast majority of clients across all categories felt that credit had a positive role on the level of household welfare. Increased household welfare, however, came in two forms: indirectly through increased income attributed to improved business resulting from the business loan or, more conspicuously, from the direct application of the business loan to either the construction or rehabilitation of their household residence or the purchase of household goods. Given the difficult economic environment and the limited ability of many clients to apply their loans to positively beneficial business purposes, the benefits derived by these clients was greater when channeled directly towards increasing the level of household welfare. Some of the interviewed clients indicated that they simply did not want to expand

[126] No information was obtained from MFI A on fixed assets at first loan appraisal.
[127] The number of MFI C's clients with employees decreased over time by 3%. The largest proportion of clients employs 1 or 2 workers (33% of all clients at the time of the last loan). In the case of MFI A, there was little data available on employees at the time of the first loan. In the case of MFI B, costs of employees did not change over time.
[128] An attempt was made to assess a client's level of household welfare by attributing a level between 1-3. Level 1 signified a considerably lower standard in relation to the "norm" and 3 was considerably higher than the norm (e.g. those with cars or any other indicator that would set them clearly above the norm). This was a subjective exercise based on impressions gained during the interview. The "norm" of the clients interviewed consisted of the following: a house made of cement blocks with electricity, a dining table with 6-8 chairs, a fridge, stove, television, sofa and lounge chairs and beds. Of the 90 active clients interviewed, only 10 (11%) were classified at the lowest level 1; the majority (58%) were attributed with a 2, and about a third (31%) were at the highest level 3. The distributions for both MFI C and MFI B clients are almost identical while, given the nature of MFI A's mission to target comparatively poorer households, proportionately more of the poorer households were found to be MFI A's clients.

their businesses, probably because income earned was considered adequate and the scale of operations manageable, given their available resources.

3.1.9 Influence of Crises

The qualitative interviews showed that 55% of the 120 credit clients (active and dropouts[129]) interviewed, and 80% of the clients which only held an account, faced one or more crises in the past three years. This percentage was considerably higher for credit clients that had dropped out (70%) than for clients that were still active (52%). A minority (30%) of the dropouts, indicated that they stopped borrowing as a result of crises they faced, sometimes linked with perceived unduly harsh and inflexible behaviour from loan officers. The real percentage of clients an MFI loses due to crises is likely higher, since clients who dropout before being two years with the MFI and clients that were expelled after two years due to late repayments and defaults were not included in the calculations.

Most of the crises clients faced were related to health problems (either the client them self or within the family) and deaths of family members: 50% for credit (ex) clients and 67% of clients with exclusively an account. Due to the high prevalence rate of HIV/AIDS (16.2%) in Mozambique, it is likely that some of the health problems and deaths in the family were HIV/AIDS related, as some clients revealed spontaneously during the interviews (questions were not HIV & AIDS specific).

3.1.10 Reasons That More-than-Two-Year-Old Clients Drop Out

The loan appraisal data showed that the majority of clients drop out within the first two years of borrowing. The Impact Assessment study focused on an atypical group of dropouts (i.e. those who leave after having had at least two years of loans) because we wanted to compare performance of these clients to those that remained with the MFI. An assessment of loan appraisal data was undertaken for 78 dropouts from MFI B and interviews were conducted with dropouts from all three MFIs. The loan appraisal data show that drop-outs had lower increases in loan size and that significantly fewer increased their monthly sales values and repayment capacity (figure 3).

The more-than-two-year-old clients normally have good repayment records, have usually benefited from credit and, moreover, represent – especially at the higher loan levels – the commercially most important client group for the MFIs.

Although loan appraisal data for MFI B's drop outs showed that their business performance was significantly worse than other more-than-two-year-old clients, interviews with small samples of dropouts (ten per institution, and therefore subject to caution) suggest that many clients who voluntarily leave the institution operate (according to the information provided during the interviews) successful businesses and, according to repayment histories, have normally been good credit risks.

The main reasons for dropouts deciding to leave were associated with events such as crises. The data above suggests that this could apply to about a third of the dropouts. Although clients often said that their MFIs can be sympathetic to the effect of crisis on some clients, many clients with temporary repayment difficulties felt that, despite long and good credit histories, zero-tolerance arrears policy is being over-zealously applied by loan officers. This provoked ill will and often led to a decision on the part of the client to stop further borrowing. Only some sought loans from another MFI.

3.1.11 Use and Impact of Current Accounts

Interviews were conducted with clients that exclusively held deposit accounts (i.e. from MFI A and C only as MFI B introduced accounts in mid 2005).[130] The interviews showed that security against theft and fire and self-control to prevent unnecessary spending were the most mentioned motivations to open an account. The favourable conditions such as a low opening balance and low or no minimum subsequent deposit, and the vicinity of the branches were important incentives to open an account at the MFI.

[129] Breakdown: 90 active clients and 30 dropouts.
[130] Sample included10 clients from MFI A and 10 from MFI C. MFI A has only a few dozen clients with current account, while MFI C has more than three times more depositors than borrowers.

As is described in microfinance literature,[131] poor people often use an amazing diversity of savings tools, including non-liquid services (whereby savings cannot be withdrawn at any time), to build up lump sums and liquid savings services for emergencies. Each savings tool has its own specific purpose. The interviews showed that this strategy of 'targeted savings' was used by the poorer as well as by the better off clients. The trend was the wealthier the client, the more diversified the package of formal and informal services used. The combination of services used by wealthier clients included, for example, current accounts at the MFI and another bank (liquid services), x*itiques,* funeral associations and term deposits (illiquid services).

The majority of the interviewed clients used the current account at the MFI for longer-term savings. They chose a current account because they wanted to accumulate money gradually and to be able to access money in case of emergencies. A small minority of clients of MFI C used a term deposit. The MFIs do not yet offer a more flexible interest bearing savings product (current accounts do not bear interest).

Most of the clients used the MFI current account to save for 'opportunities', such as starting or running a business and acquiring business or household assets. However, less than half of these clients succeeded in using their savings for this purpose. The most common reason for savings withdrawal was emergencies like theft and illness. Clients running a business in the markets near the branches used the current accounts on a daily basis for business management. The use of the account by those clients who had also credit from the MFI was generally related to credit: saving for reimbursement and facilitation of credit transactions.

The majority of the interviewed clients were involved in one or more informal financial systems; the *xitique* groups, *xitique geral* and funeral associations*. Xitique* groups were most popular among women of all wealth levels. The better-off are probably more attracted by the social aspect of the *xitique* groups, and the poorer by the peer pressure to save. Clients mentioned the easy access and security as comparative advantages of the current accounts in relation to the informal products. However, most of the clients did not stop using informal systems after opening a bank account. As comparative advantages of the popular *xitique* groups, the peer pressure to save and the social contacts were mentioned. Although almost all interviewed clients mentioned the security of the money collector in the markets (*xitique geral*) as a concern, it was mentioned only once that the vicinity of the MFIs' branches compensate for the ease of the money collector operating in the markets.

Contrary to expectations, clients with deposit accounts[132] did not show a significantly better repayment record. Interviews revealed that *xitique* groups or *xitique geral* was in many cases an important tool to save for the reimbursement of loans. Moreover, many clients appeared to have accounts in other banks. Most clients who had accounts in other banks said that they use those accounts more frequently than the MFI account, mainly because of the ease of the ATM services for daily expenses.

Men used the accounts generally more frequently than women. This can be explained by women's priority placed on contributions to *xitique* groups. Most of the clients involved in *xitique* groups saved more frequently and saved higher amounts per month in the groups than they had as a balance on their bank accounts. There were some examples of women saving even one third of their income with the *xitique* groups. According to clients, *xitque* groups are mostly used by women because men would not trust each other sufficiently or they would not have the patience to attend group meetings. The fact that forced savings remain beyond control of family members and friends likely contributes to the popularity of *xitique* among women.

Impact has been estimated by considering what would have happened differently in the client's socio-economic lives if the MFIs had not offered savings accounts. It appeared that the majority of interviewed clients who had exclusively a deposit account would be worse off if the MFIs had not existed. All these clients had a low income or were classified as poor. They would have had more difficulties to cope with crises; they would have been exposed to considerably more risk of theft and would have spent more time and money on transport to deposit money in another bank (in the case of

[131] See for example: G. Wright (1999). *A critical review of savings services in Africa and Elsewhere*, MicroSave, Kenya.
[132] These findings only apply to MFI C as MFI B did not have yet clients with deposit accounts during the period of analysis.

those who had another account). For the minority of clients, it would not have made a lot of difference if the MFI had not existed as they had easy access to other banks.

3.1.12 Client Satisfaction

Clients responded positively to all the issues raised in relation to loan products and related services. However, lesser degrees of enthusiasm were evidenced in relation to guarantor policies, guarantee requirements and valuations/depreciation rates, and high interest rates, felt particularly by high loan categories. Although the MFIs were seen in a very similar light, there were some features that distinguished one MFI from another such as arrears tolerance, rapidity of loan processing, interest rates, etc. Some clients reported that loan officers recommend that they increase their collateral (sometimes urging the replacement of functioning household appliances that ware older and therefore written off) in order to increase their borrowing capacity.

Most clients with exclusively deposit accounts were satisfied with the MFIs products and services. Clients were most positive about the treatment, the proximity of the branch to the house or market and the low costs to open an account. Many clients would appreciate the introduction of ATMs and payment of interest on accessible savings. Interestingly, the clients of MFI A did not complain about the monthly maintenance fee on their current accounts, while the clients of MFI C did, even though most of them were wealthier than the MFI A clients.

A product feature valued by clients of MFI A was the minimum deposit amount of 10 000 Meticais ($0.40) as it made them feel that even very little money was welcome, though bank statements proved that none of the interviewed clients had ever deposited such a small amount. The other MFIs do not have a minimum deposit.

Another positive feature was the fact that MFI A asks the client to nominate the person who is entitled to the money in the event of death. It was reported that, in banks other than those studied, it can take months for the spouse to get access to the deceased's money, if at all.

3.1.13 Summary and Implications

The main findings and implications of the study are summarized as follows:

- In-depth interviews with clients of different loan categories, as well as dropouts, showed an overall positive impact on both the supported economic activities as well as household welfare.
- Microcredit, though contractually stipulated for business purposes, also plays an important role in improving living standards through direct application into housing construction or renovation and acquisition of household durables. Households prefer small, sporadic injections into housing, reflecting their often volatile financial situation.
- The profile of the more-than-two-year-old clients surveyed under this assessment study shows that they are better educated than the average Maputo citizen, middle-aged, economically active people with considerable business experience.
- A small part of the more-than-two-year-old clients of the poverty focused MFI A could be considered to be poor, as defined by living under the poverty line. Individual guarantee-based microfinance requires the ownership of assets, most of which operate with electricity.
- Almost half of the clients of the poverty focused MFI A (43%) and assumingly a larger portion of the clients of the other MFIs belong to the top 20% income group of the Maputo. These clients are not wealthy, but belong to the low end of an emerging middle class.
- Credit provided by the MFIs proved to have most impact on those borrowers who tend to have basic entrepreneurial skills and who started with small loans. Evidence also showed that even those remaining with low loans seemed to benefit during normal economic conditions. Even during times of economic difficulties, clients who had climbed to higher loan categories continued to increase their loans, suggesting that loans were also important tools to confront such difficulties. Borrowers of lesser entrepreneurial capacity or those encountering multiple crises in households or businesses were unable to use their loans as effectively.
- Although instrumental in promoting the growth of small enterprises into larger ones, loans have not been very successful in promoting the growth of the existing relatively larger clients. This

suggests that the available loan products are good at stimulating growth from small to larger firms but are limited beyond that.

- On average, the value of stock of the clients increased. Only a minority of clients succeed in increasing their fixed asset base while the overall effect on employment numbers is negligible.
- Clients who drop out after a period of two years perform worse during these two years than the clients who continue with an MFI. Many dropouts claim they had well-performing businesses and were good loan clients but decided to leave for reasons often associated with crises. For the MFIs this could mean that they lose long-term good clients due to short-term financial problems. Some dropouts claim that the treatment by loan officers, as a result of minor repayment problems resulting from a crisis, stopped them from further borrowing.
- A large majority of clients did not continue to take loans after two years. The majority of dropouts leaving within the first two years of borrowing were from the lowest loan category.
- Client growth rates for the three MFIs have so far been maintained because new clients exceed dropouts. Unless MFIs make greater efforts to retain their clients they may well find it difficult to maintain past growth rates (having, indeed, recently shown significant slowing).
- MFI B and C experienced up-market growth and now compete with each other for a specific segment of the loan market, limited at the lower end by the need for collateral/ or individual guarantees and at the upper end by what are essentially working capital loans with interest rates considerably higher than the commercial banks. MFI A has recognised the limitations of up-market growth and decided to improve its solidarity group lending in a bid to service the lower end of the market.
- Current accounts reduced the vulnerability of clients towards emergencies and helped them to manage their businesses. The rapid growth in the number of current accounts with NovoBanco, exceeding the number of borrowers by almost three times,[133] demonstrates the enormous demand for this product.
- Informal financial systems still play a very prominent role in helping urban households cope with their erratic fund flows. Rather than substituting, microfinance products, whether credit or savings, seem to complement these arrangements.

3.2 Microcredit and Rural Livelihoods: The CCCP-CCOM Project

By Katia Daude[134]

3.2.1 Background

The CCCP-CCOM began as a project in 1997 under the supervision of the Bank of Mozambique and financed by the AFD, offering microcredit loans to entrepreneurs in Maputo. In 2000, activities were developed in Montepuez, a district in the Cabo Delgado province. By the end of 2004 there were 32 active associations with a total of 4100 members and a portfolio of over 4 billion MT. The products offered were of two types: i) commercial loans of a conventional microcredit format usually aimed at small traders, with monthly payments and a maximum length of six months and ii) agricultural loans, aimed at peasant farmers who require longer duration loans with no interim repayments as their cash flow is limited during the crop growing season, and who are only able to make repayments in the sale period after the harvest.

With respect to the agricultural loans, the CCCP-CCOM project has an innovative loan provision system; it draws on conventional microcredit methods (small loan amounts and personal household goods used as guarantee) and combines them with rural finance techniques (i.e. targeted credit of longer duration normally payable with the income from harvest). This approach allows CCCP-CCOM to reach the smallholder farmer who has no access to commercial financial services and whose access to credit is limited. In some villages, producer associations have been created providing access to credit mostly in the form of inputs such as seed and pesticides.

CCCP-CCOM operates along the lines of the ‘village banking model’ where it creates local associations who have “ownership” of their activities. The associations are empowered to decide on the concession of the credits and are at the same time responsible for their repayment. Loans are

[133] Figure as of June 2004.
[134] This section is based on data gathered as part of a doctoral research project, which continues as a work in progress.

made available for a specific productive activity, usually commerce or agriculture but the specific use of the credit is left up to the individual. Individuals are organized in solidarity groups that help the association in managing the number of individuals as well as in enforcing repayment.

CCCP-CCOM has consistently maintained high repayment rates (between 98% – 100% in the first four years of operation) on a portfolio that is growing exponentially, both in loan amounts and numbers of members. Its Montepuez operation serves the rural population in one of the poorest provinces in the country, making it an interesting subject for an impact study. Impact analysis can take various approaches; the study from which this paper was written (refer to footnote 135) briefly looks at direct impact on member household livelihoods and comments particularly on the impacts of having a CCCP-CCOM loan as reported by association members; namely increased ability to pay for labour in the fields, increased agricultural production and increased number of household income generating activities.

3.2.2 An Overview of CCCP Impact on Member's Livelihoods

Altogether over 300 members of CCCP-CCOM associations were interviewed (7.3% of membership) and over 150 non-members, with members reporting various types of impact.[135] More than 90% of the members surveyed ranked CCCP-CCOM's impact as noticeable (ranked three out of five) or more. The three most frequently mentioned results, by descending order of importance are discussed below:

Ability to Pay for Labour

The ability to pay for labour to help in the fields is indicated as the most obvious and direct result of having access to a CCCP-CCOM agriculture loan. The loans are specifically designed for this purpose and are usually disbursed around the time when farmers begin clearing their fields for planting and therefore need more help. Over 80% of the members surveyed declared having paid someone to help them in their fields, with more than 50% indicating having paid as much as or more than the loan amount received. Of the non-members, less than 10% reported having hired someone to help in their fields.

There are at least four obvious reasons why some members may not have used their loans to pay for labour. Firstly, in the last loan cycle, loans were disbursed a little late, thus requiring that members advance money from their savings to pay for labour. This situation was further aggravated by the intensive rains during the year which resulted in fast weed growth; the fields consequently needed weeding even before the loan was disbursed. Secondly – and this applies mostly to new members – the limited loan amount combined with the delay in the disbursement results in members investing in other activities or using it for household consumption, knowing that they have sufficient income from crops to allow them to repay the loan. Thirdly, members sometimes request agricultural loans but then use them for other activities, as other loans do not give the same repayment flexibility. Fourth, association committees – in particular those outside the district capital where trade is restricted – tend to feel that commercial loans are not profitable and are progressively steering away from them and favoring agricultural lending, further encouraging members to borrow under the agricultural loan but then using the loan for other purposes.

Ability to Increase/Expand Crop Area

One of the direct benefits of being able to pay for labour to help in the fields, according to the members, is that it allows them to expand their crop areas. This is a predictable result of being able to pay for labour and is further supported by a comparison of average member and non-member crop areas (in hectares) as shown in the following table:

[135] The survey covered 12 associations randomly chosen from the 32 CCCP-CCOM associations that have been in activity for over one year. Within those associations, a weighted number of members were randomly chosen to be interviewed. Non-members were chosen using a geographically matched method to be the control group.

Table 6: Average Crop Areas by Membership Status

	Average Crop Area 2003/04	Average Crop Area 2004/05
Non-Member	2.5	2.4
Member	3.1	3.2
Overall average	2.9	3.0

The table shows that non-members on average have lower crop areas than CCCP-CCOM members; this would support member's claim that being a member does help expand crop area. A further analysis of average crop areas between members lends further support, as follows:

Table 7: Average Crop Areas by Duration of Membership

Years as a member	Average Crop Area 2003/04	Average Crop Area 2004/05
About 1 year	2.3	2.5
About 2 years	2.9	2.6
About 3 years	3.2	3.4
Total	3.1	3.2

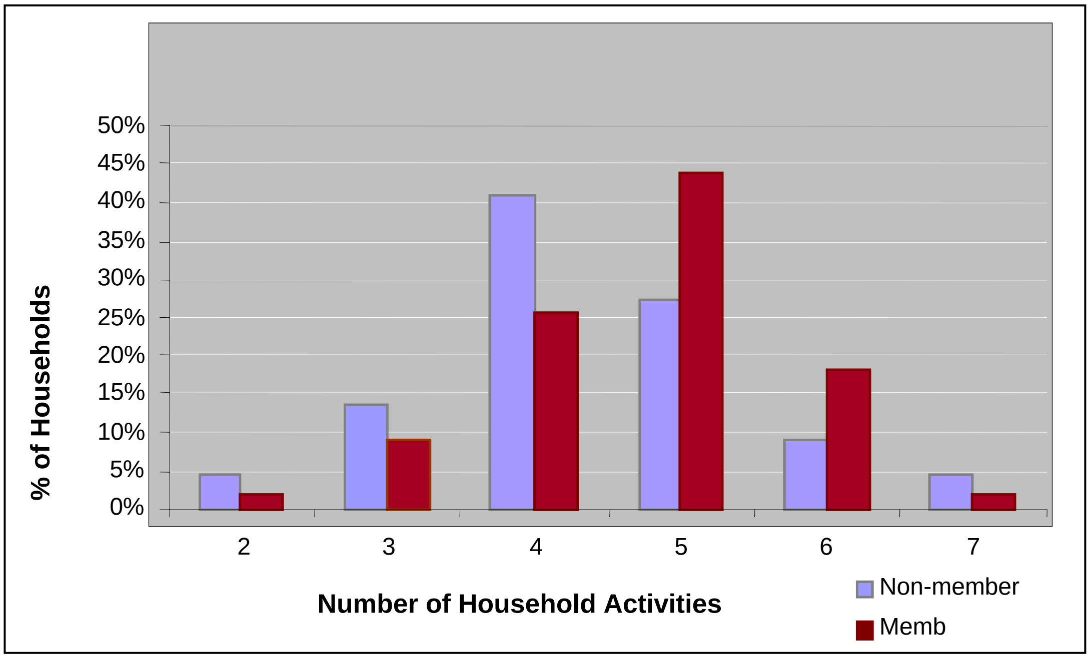
The results shown on this table may further support members arguments that having loans does help them expand their crop areas, since the longer they have been members of the CCCP-CCOM the larger their average areas. Furthermore, members who have only had one loan cycle do not show greater average areas than non-members, which is understandable as the initial loan amounts are small (1.0 million MT or about $40) and at best only enough to help clear one hectare of land.

Statistically, the relationship between being a member of the CCCP-CCOM and average crop area is significant indicating that there is some correlation between them; however, the direction of this correlation is not explained by the tests. One other interpretation could be that generally people with larger field areas are the ones that tend to become members, although this is not supported by the second table, presented above, on years as a client and average crop area.

Diversification in Household Activities

Most members also report being able to pursue new activities or expand existing ones, helping them better cope with the "hunger period" and to a certain extent smooth cash flow over the dry season. Looking at the reported number of household income generating activities of clients and non clients we obtain the following graph:

Figure 14. Distribution of Number of Household Activities



Member households do tend to have a slightly more diversified portfolio with 64% of member households undertaking five or more activities as opposed to only 41% of non-member households. The correlation between these however is not statistically supported by tests therefore suggesting that there may be other reasons for this difference. One of the most obvious options is that members may be people who are less risk averse and thus more likely to be entrepreneurial – a lot of non-members declared no desire to join the CCCP-CCOM for fear of loosing assets or being unable to meet repayment obligations.

3.2.3 Conclusion

CCCP-CCOM has managed to implement a microcredit service to peasant farmers that allows them access to credit both for agricultural and commercial activities, while simultaneously educating them on credit management with a focus on ownership of the associations. The impact on livelihoods is important as it allows a deeper understanding of rural finance methodologies and can help to make a difference in particular in the light of the current focus on poverty reduction through agricultural development.

This paper addressed the three most reported aspects of the impact of CCCP-CCOM loans as perceived by the farmers themselves and used the data collected to analyze the objective facts to support the previous indications. It does seem that members are indeed more able to hire labour to work on their fields which in turn enables them to work on greater crop areas. This is particularly true when we look at the duration of members' participation in the programme - the correlation between being a member of the CCCP-CCOM and average crop area is significant but is also subject to other interpretations. The number of activities undertaken by the households also seems to indicate that members are more active; however this could be for other external reasons.

4.0 THE POTENTIAL ROLE OF MICROFINANCE IN RURAL AREAS

Worldwide experience indicates that microfinance has largely been an urban phenomenon. The main reasons for this are the higher transactions costs and risks associated with rural activities, primarily due to remoteness of clients, poor access, lack of communication, non-existent banking facilities, and lack of qualified personnel, etc. Chapter 2 has demonstrated that in terms of financial service provision and loan capital, Mozambique's experience confirms similar distortions. However, a closer look shows that the evolution of microfinance in the rural areas of Mozambique has been diverse and the rapidly changing reality of the rural economy is likely to stimulate a take-off similar to that witnessed in urban areas. As argued below, both the demand for and supply of microfinance are very favourable, supported by a significant donor-government driven emphasis to promote rural finance and a stimulating legal environment. PARPA II, in which considerable weight is placed on rural development, emphasizes the importance of rural finance and microfinance in stimulating rural development.

4.1 The Changing Rural Economy

The rural economy in Mozambique has been undergoing major transformation. Structural adjustment, price liberalization and the effective privatization of agricultural marketing has led to a positive response from small-holder farmers to sell surplus "subsistence" crops such as maize, groundnuts and beans to traders often operating through remotely located *postos de venda.* [136] NGOs such as CARE and World Vision have successfully introduced new cash crops including sesame, paprika, sunflower and soybean. The Cooperative League of the USA (CLUSA), CARE and ACDI-VOCA have also significantly enhanced the production and marketing of crops through the promotion of farmer associations and umbrella groups. Finance for the promotion of small-holder cash crop production arose in different forms, either through direct input credits or trader advances. Input credits have been mainly provided by the large agro-processing companies known as *empresas de fomento*, in particular those producing cotton in Nampula, Cabo Delgado and Niassa provinces. With the liberalization of agricultural commodity marketing, the main source of small scale trader financing came from the large traders such as V&M Grain Company and Export Marketing which provided advances to smaller traders as well as farmers' associations on condition that they would supply agreed volumes of specific crops to the traders' warehouses.[137] Donors, in particular the EU, provided loan capital funds to AMODER and GAPI to stimulate trader activities.[138] Microfinance for small informal traders was provided mainly by the World Relief's FCC (N) programme (now terminated). With the exception of input credit from the *empresas de fomento*, there was virtually no credit being provided for agricultural producers until the pioneering initiatives of the CCCP-CCOM project in southern Cabo Delgado.

The movement of Zimbabwean farmers into Manica Province over the past few years stimulated an agricultural boom.[139] In other provinces, particularly Tete, Zambezia, Nampula, Niassa and Cabo Delgado, significantly increased production of cash crops, especially tobacco, has stimulated hundreds of thousands of smallholders to supply the growing number of *empresas de fomento*. In the case of Mozambique Leaf Tobacco (MLT) in Tete Province, 89,000 small holders are growing and supplying tobacco. Some $20 million worth of inputs are advanced every year to the farmers by MLT while approximately $90 million is paid for the tobacco sold. Difficulties in administering input credits has made the larger companies look for financial intermediaries to manage the loans. GAPI has provided production loans to smallholders supplying Dunavant in Zambezia. Plexus in Cabo Delgado is negotiating with CCCP-CCOM to provide credit to cotton growers and MLT is currently looking for a suitable provider.

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[136] *Postos de venda* are village based collection points operated by small traders themselves until such time that they have accumulated sufficient volumes to hire transport to the destination market. The *postos* can also be manned by employees of larger traders who periodically send trucks/tractors to collect the accumulated stock.

[137] See F. de Vletter (2003). *A Review of Three Successful Cases of Rural Finance in Northern Mozambique,* commissioned by the World Bank/CGAP.

[138] See MIC/CE Credit Facility Monetary and Evaluation Committee (2004). *Mid-Term Evaluation of the Credit Facility to Finance Agricultural Marketing,* DNC Research Note No. 23, National Directorate of Trade, Ministry of Industry and Trade.

[139] In early 2006 Joe Hanlon and Teresa Smart in their article "*The Manica Miracle is Over"* claimed that due to the lack of technical support and finance many agricultural initiatives in Manica had failed. At around the same time the tobacco company Alliance One announced that it would stop the activities of its companies DIMON and STANCOM, large producers of tobacco in northern Mozambique, because of disagreements with the government over land concessions in Tete Province (*Savana* 19 May, 2005).

4.2 Rural Non-Microfinance Finance Experiences in Mozambique

In the early post-independence years, the FRELIMO government recognized the importance of agriculture and channeled the majority of the loan capital provided by the state to agriculture (through the state bank BPD).[140] However, very poor recovery rates led to a retraction and since then limited commercial bank lending has reached the rural areas with the exception of loans to large traders and *empresas de fomento*. This situation has been exacerbated by very low levels of commercial bank lending for the country as a whole, in particular to rural areas, due to high Treasury bill rates and low rates of loan recovery.[141]

Donors, NGOs and government have pursued a variety of approaches to stimulate rural finance. Some progress has been made in bringing the commercial banks back into the rural arena. Though this has been done through donor supported guarantee funds which reduces considerably the risk of the banks, it is felt that these initiatives (USAID funded Center for the Promotion of Rural Financial Services (CPSFR) and the Italian Cooperation funded Programme for Relaunching the Private Sector (PRESP) being managed on behalf of Government by the Ministry of Industry and Commerce and Ministry of Agriculture respectively) are expected to stimulate a more commercial approach to the financing of farmers and to agro-processing[142] of local crops such as cashews. The influx of experienced commercial farmers from Zimbabwe and South Africa should stimulate this change of attitude.[143]

Another approach to stimulate value-chain activities has gained support from donors. The "Rural Enterprise Innovation Grants" experience of TechnoServe proved an effective way of stimulating innovative business initiatives. Incentive grants averaged about $30,000 and were generally successfully applied. In one case, an activity that started with a $25,000 grant has now grown to the extent that it has just received $2.5 million in risk capital. Though this is not a form of commercial finance, it uses the same principle as the "Trickle Up (TU)" approach of stimulating enterprise with an initial start-up grant with the objective of creating viable activities that later benefit from microfinance.[144]

Risk capital programmes and joint-venture funds are increasingly important. Recent initiatives include the Swedish supported Malonda Foundation (contractual joint ventures), IFC and Aquafer (Gatsby Fund) The Government, through the Center for the Promotion of Agriculture (CEPAGRI) created in 2006, is also planning to engage itself directly in equity financing.[145]

GAPI, in partnership with Rabo Bank and NOVIB, is about to launch a rural bank. GAPI itself will focus on the provision of business development services with the objective of promoting the bankability of rural enterprises.

One other form of rural finance, usually ignored, but having a significant impact on the development of southern Mozambique, has arisen from the very large numbers of migrant workers employed in South Africa. TEBA Bank, serving largely miners, allows them to transfer money to their wives who hold local accounts with the bank. Furthermore, a similar effect (income transfer) has been facilitated by the company Kawena, which allows any Mozambican to "transfer" goods to their families by paying in South Africa and having the recipient obtain the goods in one of many warehouses, scattered throughout southern Mozambique.

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[140] In 1987 51% of bank loans were directed to agriculture but by 1992 this had dropped to 35% while 54% of all credit was disbursed in Maputo alone (Abreu and Hallam, BoM Staff Paper No. 1).

[141] A banking sector study by KPMG in 1993 showed that total loans from the commercial banks were the equivalent of only 37.5% of deposits.

[142] The cashew producers Miranda and Africaju in Nampula Province originally received financing from GAPI but are now receiving substantially higher loans from BCI-Fomento backed by USAID-MIC guarantee funds.

[143] In response to the increasing demand for agricultural loans, especially by Zimbabweans farming in Manica Province, the Standard Bank has placed a Zimbabwean banker with agricultural lending experience in Chimoio.

[144] The organization Trickle Up (TU) started its activities in Mozambique in 1993 in collaboration with the ACDR, MBEU and KULIMA. $50 grants were provided to potential entrepreneurs of the poorest 5-10% of the population - the "credit adverse". After a three month rigorous training programme an additional $50 credit could be made available, if certain conditions were fulfilled.

[145] The government also amalgamated the *Fundo Fomento Agrário* and the *Fundo de Desenvolvimento da Hidráulica* to create the *Fundo de Desenvolvimento Agrario (FDA).*

Recently the viability of providing savings services through the Post Office network has been examined (undertaken by KPMG and commissioned by the Malonda Foundation).[146]

4.3 Developing Appropriate Microfinance Products for Rural Client Needs

In the mid-1990s, the FAO spent considerable effort designing a "Rural Finance Master Plan" intended to be incorporated within the sector-wide agricultural programme, PROAGRI. For various reasons, the plan was shelved and was in many ways reincarnated through the Rural Finance Support Programme launched in 2005. In the Master Plan, the chosen methodology, then referred to as *caixas locais* was based on the model developed by IRAM/BoM's CCCP project, even before it had been implemented. In 2000, the CCCP project commenced its Cabo Delgado operations through its office in Montepuez. The programme initially started lending to small informal traders, similar to those targeted by the FCC (N) programme in the Montepuez area, but gradually broadened its outreach to cover four remote districts and now focuses on lending to farmers to help them pay for agriculture inputs (usually labour for weeding purposes). Not only has the impact been positive (see section 3.2) but very high rates of repayment have been maintained. The programme is based on a decentralized system of associations of solidarity groups called *caixas comuntárias* that borrow money from the project at 12% annually and then on-lend to their member groups at 3% per month. The success of the programme can be partly attributed to a considerable amount of preparatory research (starting in 1993) that carefully assessed the needs of its target groups including the adjustment of repayment schedules according to the production patterns of the beneficiaries.

CARE experimented with a different methodological approach. In 1997 it started its Financial Services for Households programme (FISH) in Angoche. This was later transformed into the larger CRER programme in Nampula, which experimented with four financial products: solidarity group loans for traders, loans to farmers' associations, savings stamp groups, and ASCAs. CARE had successfully introduced the ASCA methodology to 80,000 rural women in Niger through its *Mata Masu Dubara* (MMD) programme and felt that, given the widespread participation of Mozambicans in *xitique* groups, ASCAs would be easily understood and attractive. In 1999 ASCA groups were piloted with the IDPPE among fishing communities. In 2001 CARE decided to terminate its CRER programme but created an NGO, Ophavela, to continue to promote ASCAs. CARE also started an ASCA programme in Inhambane (1999) exclusively for women (now the NGO Kukula) and more recently the CARE VSL Zambezia programme funded by the UNDP. Two other ASCA programmes have also been established in Manica province (AKSM and ADEM). ADEM and, more recently KULIMA, have been contracted by the IDPPE to promote ASCAs in fishing communities along the coast of Sofala and Zambezia provinces. The ASCA concept has been well-received in a variety of rural environments, notably fishing communities, predominantly agricultural communities and small town traders. All operators promoting ASCA groups claim that their initiatives have been very positive with the main weakness being that, for many groups, especially the informal traders, the collected savings are insufficient to meet the members' credit needs.

The RFSP has now chosen both rural microfinance methodologies (*caixas comunitárias* or Rural Finance Associations (RFAs) and ASCAs) as the priority models to be promoted, while also offering possibilities for other innovations through the Outreach and Innovation Facility. Despite being generically called the *Rural Finance* Support Programme, it focuses almost exclusively on the promotion of *microfinance* in rural areas.

The ASCA and *caixa comunitária* models were developed with substantial resources, previous international experience and foreign expertise. The success of the Mozambican NGO Hluvuku-Male Yeru based in southern Maputo Province deserves to be mentioned as well. Having inherited projects initiated by Intermon and Helvetas, Hluvuku-Male Yeru has been managed entirely by Mozambicans for four years. The institution provides loans for a variety of activities through different methodologies and loan terms and its target groups are farmers and fishermen.[147] Despite the difficulties of reaching these target groups, Hluvuku-Male Yeru manages to achieve good performance indicators.[148]

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[146] See Buisson (2005) for a fuller discussion on this issue.
[147] Currently there are about 100 fishermen getting loans averaging about $250 and 100 farmers with an average loan size of about $100.
[148] Information for November 2005 (provided by MMF) showed that PAR>30 days was less than 5%; operational sustainability 152% and financial sustainability 94%.

In terms of providing credit to farmers associations, one of the most interesting and innovative initiatives was conceived by CLUSA in collaboration with GAPI whereby groups of farmers' associations (fora) borrow money for trading purposes. In this scheme some 20 fora in Nampula Province signed a joint agreement applying the solidarity group approach (whereby a defaulting forum would be guaranteed by other signatory fora).[149] GAPI also experimented with loans to the association of small entrepreneurs in Cuamba (APROPEC) whereby members (informal agricultural commodity traders) could obtain a loan from the association through creating solidarity groups. The experience gained from this has led GAPI to manage more than $2.0 million of funds, from the ADB, for microcredit provision (both individuals and groups) to approximately 10,000 families involved in smallholder irrigation farming in the provinces of Maputo, Gaza, Sofala and Zambezia. Although still in its early stages, the GAPI experience has been very positive. In some ways similar to the CCCP-CCOM methodology, GAPI provides credit on a wholesale basis to associations that are given training in both management and microfinance. Associations then effectively become financial intermediaries and choose whether to on-lend to their clients as individuals or in solidarity groups. By early 2006, some 2,000 members of associations were receiving credit.[150]

With growing emphasis on value-chain linkages, donors and government are looking for ways to promote product transformation/added value activities. Limited rural microfinance and virtually no urban microfinance have been successfully channeled towards added-value/productive activities. The 1997 survey showed that four programmes were specifically targeting productive activities. The best known of these was the PAPIR project in Sofala Province that supported artisans and their associations, which eventually all collapsed. Currently, the only known microfinance initiative targeting productive activities is the SNV CASCA programme which provides credit through AMODER to small satellite cashew processors supplying processed cashew to the larger producers such as Miranda Cajú for export.

4.4 Current Issues and Future Challenges

Although notable progress has been made in the last few years in terms of mobilizing rural savings and providing loan capital to rural small holders and traders, the previous sections show that rural microfinance is still relatively insignificant in terms of market opportunities and rural microfinance needs.

Recent developments and announcements, however, indicate that rural clients will be given much greater attention by some of the larger operators in the country. IRAM is currently replicating its Cabo Delgado model (called the Rede de Caixas Rurais de Nampula –RCRN) to serve three districts in Nampula province (financed by SDC) and there are indications that other donors intend to establish similar schemes in other provinces, while other large operators are preparing to enter into the rural arena. NovoBanco engaged an agricultural credit expert to look at the potential for applying products developed elsewhere by sister ProCredito banks and has publicly stated that they will soon start providing individual loans to farmers with adequate guarantees. BOM is currently collaborating with ACDI-VOCA in Manica Province to develop appropriate loan products for farmers associations with the hope that this experience can also be introduced to Sofala and Zambezia provinces. In addition, BOM is considering introducing a system of mobile banking that would enable rural clients to save and borrow. Tchuma has spent considerable time researching the agricultural scene in Manica province, examining possibilities for financial intermediation between *empresas de fomento* and outgrowers.[151] As indicated in the previous section, GAPI's approach of providing wholesale credit to associations for further on-lending to their members has had positive results and is likely to see very rapid growth in the near future.

[149] See F. de Vletter (2003). *A Review of Three Successful Cases of Rural Finance in Northern Mozambique*, commissioned by the World Bank/Consultative Group to Assist the Poor (CGAP).
[150] GAPI lends to MFIs and the associations at the same rate. In early 2006, the wholesale rate was 18% per annum. Associations usually provided credit to their members at 3% higher than the rate provided by GAPI.
[151] Tchuma has indicated that, with appropriate funds, it would start providing microfinance in rural areas.

4.4.1 A Changing Paradigm: Outsourcing Financial Services

At the time of conceiving the RFSP, it was felt that rural microfinance needed to be stimulated from the supply side (i.e. by providing the appropriate incentives for MFIs to provide financial services). There are, however, recent indications that quite independently of the RFSP, donors have created a demand for rural finance provision that has already surpassed the capacity of the existing MFIs. Moreover, as indicated earlier, there is a strong possibility that the private sector, especially the *empresas de fomento,* will be seeking to contract the services of financial institutions to manage input credits.

In the early stages of microfinance development in Mozambique, microfinance was often designed as an integrated component of an NGO's rural development programme (e.g. Concern, Action Aid, World Vision, LWF, etc.). Now rural development programmes such as those being promoted by the ADB, IFAD, UNDP, the World Bank and bilaterals such as DANIDA and SDC identify the financial provision needs and then tender for appropriate financial service providers. A good example of this was the IFAD-funded Nampula Artisanal Fisheries Project that engaged the services of the Fund for the Promotion of Small Industry (FFPI) to provide individual credit for fishermen, traders and processors and to Ophavela to establish PCRs among coastal communities. The programme has now expanded south to Beira and has contracted the services of ADEM, and recently KULIMA to establish ASCAs in Sofala and Zambezia. The ADB has recently started a similar project for northern Mozambique with a credit line of $12 million to be managed by the Fisheries Support Fund (FFP) for on-lending to financial service providers (including those promoting PCRs and providing loans for small and medium enterprises). The model is slightly different than the IFAD programme as it does not subsidize operational costs; rather it offers wholesale interest rates in the hope that retail rates would attract suitable service providers. At the time of writing, the World Bank and FAO were designing a project targeting the Zambezia Valley which is expected to contract the services of private sector financial service providers to promote community based savings and credit groups and for the provision of more conventional forms of credit.

The recent trends in donor procurement of rural service provision and the anticipated demands from the private sector will substantially change the roadmap towards sustainability as seen from the conventional financial institution model. This model basically foresees financial sustainability once the right mix of portfolio quality, client volumes and loan values have been attained. What we are witnessing in Mozambique is the emergence of a two-tier demand system whereby a donor demands the services of an institution or a private company in order to satisfy the credit and/or savings demands of a project target group or a company's out-growers. This is another best practice strategy, as it is commonly known that the credit components of integral programmes are not very successful and the provision of financial resources will allow capacity building of existing programmes. These types of arrangements will result in a substantial proportion of institutional income being derived from service provision fees, thereby reducing the need to reach sustainability solely through interest income.

4.4.2 The Need for Complementary Non-financial Services

The transformation of GAPI into a business development service provider to accompany the imminent creation of a rural bank is a good example of the underlying need to provide complementary services to most rural finance. Urban microfinance is rarely complemented by additional non-financial services such as business training or technical counseling. In rural areas clients usually require additional support before receiving loans either in terms of group organization (farmers associations, credit management committees, trader associations, etc.) or technical assistance for improved crop production and/or basic business practices.

In some cases the financial service providers themselves offer organizational skills. This was first done by *empresas de fomento* but more recently by microfinance operators as in the case of CCOM's *caixas comunitárias* and FCC's village banks as well as the NGOs promoting ASCAs. In these cases capacity building of the management committees is an essential part of ensuring that the financial services operate efficiently and therefore provided by the MFI itself. Trader finance benefiting poor rural households also depends on group training, mainly in the form of building up the management capacity of farmer associations and their umbrella groups. A good example was the experience of

CLUSA and GAPI with the former providing the training and the latter the credit. Larger loans coming from GAPI for agricultural processing have often been administered in partnership with technical assistance providers such as TechnoServe (cashew processing being a particularly good example). International experience has demonstrated that it is best to separate the non-financial service component from the provision of financial services. GAPI provides both management and microfinance training to associations before providing them with credit, but these two functions are carried out by two distinct accounting entities within GAPI. When the anticipated Development Bank is created with Rabo Bank and other partners, GAPI will operate a separate company providing business development services, mainly to the beneficiaries of credit.

There is, however, a general absence of non-financial services aimed at improving farming capacity and complementing agricultural credit. The CCOM experience has shown that farmers without technical assistance have successfully applied credit to increase yields simply by increasing labour inputs. It can be assumed that in those areas with NGO interventions to improve farming systems (through better input technology and the introduction of cash crops), credit provision could be expected to have even higher impact.

5.0 CURRENT ISSUES AND FUTURE CHALLENGES

5.1 A Review of Current Policy Objectives and Prior Recommendations

To reach the goal of 100,000 microfinance clients by 2005 was considered daunting when announced in 1997. Retrospectively, it will have seemed a small hurdle. Now, the government has set itself the much more ambitious challenge of fighting poverty with the help of microfinance, particularly in rural areas.[152]

The proposed National Policy and Strategy for Microfinance (2005) has the following objectives:

- To encourage the development of a viable and sustainable sector which, in combination with other measures, contributes to the reduction of poverty;
- To make financial services available to low income groups;
- To use microfinance as a means for income generation, thereby contributing to solving the socio-economic problems of the target group such as health, nutrition and education;
- To present microfinance as a business opportunity for investors.

To better understand the process of evolution of the microfinance sector, a brief review is made of the recommendations arising from the three national microfinance seminars occurring between 1998-2004 and to what extent these recommendations evolved and were fulfilled.

The issues and recommendations arising from the National Framework and National Action Plan for Microfinance Development in Mozambique elaborated during the first national workshop on microfinance (1998) were as follows:

- To establish a common vision and define stakeholder roles; this was to be done by reviewing the efforts of the three existing task forces (Reference Group, Informal Working Group and Action Research Project);
- To develop a vibrant and diverse microfinance industry with an ultimate view to its sustainability; this was to be done through donor and government support to operators felt to be pursuing good practices and recognized performance standards;
- To develop a cadre of well-trained and professional MFI staff and to support the institutional capacity building of MFIs;
- To define a legal framework that would ensure a favourable environment without heavy regulation and supervision;
- To strengthen local MFI networks in the South, Centre and North of the country;
- To gradually move the MFI community to more rigorous application of financial and operational performance standards and monitoring.

The second National Microfinance Seminar (2000) did not produce recommendations, but the ICC presentation of its Second Study of the Microfinance Sector in Mozambique listed what it felt to be the “main challenges to operators and donors” which were as follows:

- To develop a favourable atmosphere for the development of the sector;
- To develop skilled personnel at government and MFI levels;
- To increase competition and outreach in rural areas;
- To confront the problem of HIV/AIDS;
- To achieve sustainability;
- To acquire finance;
- To improve the administrative and informative areas;
- To develop microfinance career courses;

[152] At the time of finalizing this study the final draft of PARPA II was approved but the indicators in the strategic matrix were still under review. The version circulating in early June placed emphasis on approving and implementing a national policy and strategy on rural and microfinance. The number of number of beneficiary “*low income clients*” was projected at 175,000 by 2009.

- To promote a greater exchange of information between operators.

The Third National Microfinance Seminar (2004) made the following principle recommendations:

- To create a Task Force to elaborate the regulations to accompany the newly altered law on credit institutions (law 9/2004);
- To promote access to financial services, in particular rural areas;
- To create conditions of continuity for financial services provided by projects coming to an end;
- To study the possibility of constituting a coordinating body for microfinance;
- To examine the country experiences such as Uganda in terms of diseases such as HIV/AIDS and malaria;
- To prioritize savings in a gradual, prudent and secure manner.

5.2 Progress to Date

With the exception of recognizing the importance of savings in the last seminar, the recommendations essentially focused on the following recurring observations:

- Microfinance is not adequately serving the rural areas;
- Coordination and information exchange needs to be improved between stakeholders;
- Microfinance should be used as a poverty reduction tool;
- There is an urgent need for institutional capacity building with focus on personnel training;
- There is a need for an improved enabling environment, in particular through legislative reform;
- Microfinance should be provided by increasingly sustainable operators;
- Microfinance provision needs to be adapted to the prevalence of HIV/AIDS.

Some of these issues have elicited encouraging response but others remain as pressing, if not more so.

- In terms of **rural outreach**, this study has demonstrated that microfinance continues to be largely an urban phenomenon but that community based groups have made it possible to quickly reach and serve large numbers of the rural poor (with the major constraint being that loans are limited to members' savings). The recent launching of the Rural Finance Support Programme is directing considerable resources to promote a greater coverage of the RFA (*caixas comunitárias*) and ASCA methodologies while encouraging the development of innovative ways to promote rural finance.
- The issue of **coordination** remains a very relevant matter, especially with signs that the Microfinance Informal Working Group is no longer serving the interests of an increasingly heterogeneous and competitive sector and that stakeholders are creating more focused groups of the donor community, government representatives, RFSP partners and MFIs.
- The issue of microfinance being a **poverty reduction tool** is particularly important, given the recent inception of PARPA II and the government's current priority focus on poverty reduction, although it is important to recognize that there may be poor people to whom it will never be commercially viable to provide financial services.
- Significant strides have been made in terms of **institutional capacity building** through bilateral assistance and sector-wide projects. However, the need for more intensive institutional capacity building has probably never been greater due to the likely increases in the supply of financial resources from donor programmes and the private sector for microfinance services in rural areas.
- It is probably in the area of creating an **enabling environment** where most progress has been made, through appropriate legislation drafted on a consultative basis. Operators have made it clear, however, that, although the legal environment has changed significantly, there are still worrying obstacles to overcome (see Section 5.5.5).
- Equally impressive has been the move towards reaching higher levels of **operator sustainability** through dramatic improvements in management capacity and performance indicators. Several of the largest operators have now reached financial sustainability and others are likely to follow soon.
- In relation to the question of **HIV/AIDS**, a recent workshop on HIV/AIDS and microfinance was organized and resources have been provided for assisting MFIs for coping with the problem.

- The results of the impact study suggests that a **better understanding of clients' financial needs**, in particular urban ones, could improve the quality of financial products offered. Such improvements could lead to decreases in dropout rates and improved impact.

5.3 Assessing the Case of Mozambique Based on the Statement of the Advisors Group

Before contemplating the challenges facing the microfinance sector in Mozambique, it would be appropriate to consider the Statement of the Advisors Group (see Annex 5 for the full text) which, at the end of the UN International Year of Microcredit 2005, also looked back at past achievements while identifying the challenges ahead from a global perspective.

The Statement placed much emphasis on microfinance as an effective tool for fighting poverty. Despite being encouraged by the numerous examples of how microfinance can transform the lives of poor people, the Statement declared that, "*it is clear that the biggest challenge for the next few years is to provide microfinance on a significantly greater scale than anything we see in poor countries today. A particular challenge is in rural areas that can be especially costly to reach."* However, it raised concerns about the level of awareness of the relationship between financial access, poverty and economic growth, therefore stressing the importance of data collection, particularly in regard to the type of financial services that are relevant, who has access to these services, and what might be their level of impact. The Statement also devoted considerable attention on the importance of governments' roles in stimulating the environment for microfinance, specifically calling for governments not to control interest rates and to allow MFIs to take deposits. It also calls on government to introduce adequate measures to protect depositors (e.g. through deposit insurance and promotion of a credit bureau). The Statement recognized the need for all stakeholders to promote or deliver microfinance on a commercial basis. Although it concedes that the issue of subsidizing the provision of financial services to poor people is not clear, the Advisors Group recommends that: "*governments and others are restrained in their provision of subsidized capital to microfinance, and aim to deploy it in ways that encourage, not discourage, commercially-driven capital into the sector."* Furthermore it recommends: "*that multilateral institutions and other donors give serious thought to how they can use their resources more effectively to develop commercially sustainable microfinance*." While recognizing that microfinance should evolve as a commercial product, the downside would be to steer microfinance away from the poorer potential clients as the depth of outreach of many MFIs might be going progressively up-market. Furthermore, most investments into commercial MFIs will be foreign-sourced and therefore entail significant exchange rate risk. The Statement also calls for a greater recognition of the importance of new technology in microfinance service provision and the diversification of products. Finally, and perhaps most importantly, the Statement calls for a greater recognition of the importance of understanding client needs and to actively involve them in the design of more appropriate financial products.

Against the issues raised by the Statement, Mozambique's achievements rate fairly well. Although, not in the same league as several other African countries in terms of outreach and innovation, the case of Mozambique may eventually be recognized as a good example of an emerging sector, much of which is commercialized and growing according to market forces in an environment that has benefited from a government committed to a stimulating regulatory environment.

Government, led in particular by the BoM and the DNDR, has approached the microfinance sector in a responsible and consultative manner along the ways suggested by the Advisors Group, though attention is still required in terms of deposit protection and subsidized government credit funds. Considerable progress has also been made in terms of commercializing the delivery of microfinance; the bulk of microfinance loans are now being provided by commercial banks. Microfinance provided by commercial banks has also benefited from technological innovation such as ATMs and on-line services. The poorest clients have been more effectively served by ASCAs, and the solidarity group associations. Although sustainability is still an issue with the delivery of these latter products, there are encouraging signs that a variety of important rural-based projects are turning to these methodologies as the most effective way to reach the poor.

Mozambique has also come a long way in meeting the Advisors Group's concerns about information gaps and better understanding the needs of clients. In the past few years important research has been undertaken that has provided useful insights about the sector, its impact and client perceptions. The information gap, however, is still of concern and more investment is needed for better understanding clients' needs, and for impact assessments and relevant information dissemination.

5.4 Approaching Maturity: Lessons Learned and Adapting to New Paradigms

With the eclipse of the UN International Year of Microcredit, it is likely that other introspective national exercises such as this one have been undertaken. There is little doubt that, as we gain more experience and better understand microfinance, a much more objectively critical approach to it is imminent. The benefits of microfinance have been accepted for many years in circles internationally dominating the sector as virtually sacrosanct and microfinance has remained largely unchallenged in its objective of providing finance to the poor. The writings of critics such as Tom Dichter and surveys such as one recently done in Nicaragua[153] are making us more aware of the shortcomings of microfinance and augur a growing debate. Microfinance is no longer a development fad; it has proven to be a commercially sustainable financial intervention and the widespread creation of commercial banks devoted to microfinance provision indicates that it is here to stay. Its evolution in Mozambique is a reflection of what has occurred in many other countries.[154] As part of the maturation process, we can expect the industry to be less experimental and to be more retrospectively analytical with time. The comprehensive impact study reviewed in section 3.1 is indicative of how the sector can be expected to evolve based on longitudinal data and client experiences.

A look back over the past decade or so of microfinance development in Mozambique has revealed some important lessons which are likely to be similar to the experiences of many other countries. These are summarized as follows:

- The GTZ-GPE project to assist *regressados* from the former German Democratic Republic demonstrated that the simultaneous provision of credit and business courses from the same institute is not only difficult but unsustainable.
- Providing credit as a component of integrated development programmes only works if credit is meant to target a small group of beneficiaries leading to their own individual economic sustainability but not as a mechanism for continued provision.
- International NGOs involved in direct provision of microfinance services can play an important role in opening microfinance markets and sprurring competition. The experience of CARE, MEDA and World Vision in Mozambique confirms this, and demonstrates that such NGOs have the foresight to exit when local commercial interests have scaled up and begin to adequately serve the market.
- National NGOs managed by dedicated and competent personnel have shown that relatively small operations have promising prospects to reach sustainability.
- Some national NGOs, particularly those promoting PCRs, have demonstrated that sustainability is not only related to clients and interest payments but can be attained through fees charged to donors interested in hiring the services of such NGOs.
- Good management, not interest rate levels, is the key to high repayment rates. Highly subsidized government credit funds are not only generally badly managed with poor loan recovery but negatively affect the growth of commercial credit.
- Microfinance offered to poor rural farmers is possible with high rates of loan recovery.
- Recent growth rates of urban current deposit accounts and the rapid expansion of PCRs has demonstrated that the demand for savings products is likely to be much higher than for credit.

Not only has the maturity of the sector provided us with important lessons on which to continue its positive evolution, it has also made us more aware of its shortcomings and issues that remain to be tackled. Some of the issues that we can expect to be on the agenda for stakeholder consideration include:

[153] See: A. Legovini (2002). *The Distributional Impact of Loans in Nicaragua*, World Bank.
[154] For a good global overview of microfinance refer to The Economist's "*Microfinance Survey*", November 7th 2005.

- Improving our understanding of why client dropout rates are so high and designing credit products tailored to the needs and capacities of the target beneficiaries.
- Increasing microfinance provision to the poorer households participating in the Mozambican economy, whether urban or rural. This would include greater emphasis on solidarity group loans. The issue of the distributional impact of microfinance promises to be an important theme internationally.
- More effectively targeting young entrepreneurs who, according to the impact study, have not benefited greatly from microfinance.
- Improving the impact of microfinance on enterprise growth and development with complementary inputs (provided by other entities) such as business development services.
- Developing financial products that are better tailored to the changing needs of the more entrepreneurial clients who, according to the impact assessment, grow comparatively rapidly, often reaching enterprise dimensions that no longer can derive benefits from the products available.

5.5 Recommendations for Meeting the Challenges of the Next Decade

5.5.1 Microfinance and Rural Poverty

Increasing competition and dwindling client growth potential in urban areas has resulted in a shift of strategy by some of the larger commercial operators to develop rural products, however it is unlikely that they will be catering to the needs of the rural poor. Rather, they will be targeting traders and farmers with sufficient guarantees and/or belonging to out-grower schemes.

Targeting the poor with microfinance, for the foreseeable future, is only realistic through direct donor intervention or indirectly through the subsidization of operational costs. The experience of the CCCP-CCOM project, GAPI and the ASCA-promoting NGOs are good examples. Even though the methodology of the *caixas comunitárias* of CCCP-CCOM is modeled on sustainability, the eight-year horizon is not attractive for commercial initiatives and its spread will depend on the intervention of donors such as AFD, SDC and programmes such as the RFSP.[155] This is even more pronounced in the case with ASCAs which will only yield sustainability for the NGOs promoting them as long as there is external demand from the donor community or the government for their promotional services.

At a national meeting of district administrators in Vilanculos (October 2005), the concept of microfinance was introduced as one of the government's instruments to combat poverty.[156] The idea of having microfinance operations in their areas was welcomed with much enthusiasm. Unfortunately most are unlikely to see microfinance come to their areas for a long time. The reality is that their chances are more akin to a lottery as "winning" will be dependent on exogenous donor/programme decisions.

There are, however, promising signs that donor-driven microfinance will grow rapidly for two reasons. The first is that much more development aid is targeting the rural areas as agriculture and value-chains are attracting more attention. Secondly, the need for effective financial services is usually recognized as essential for the success of these programmes. Unlike previous "component" experiences, the provision of financial services will be contracted out to operators with proven track records.

5.5.2 Capacity Building to Meet Projected Expansion in Rural Areas

With the anticipated increase in contracted financial service provision, there will be a need to expand the capacity of financial service providers. Until now, training of microfinance technicians has been through on-the-job experience, courses or exchange visits organized through MicroStart, the MMF and Upstream and courses offered through local training institutions.

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[155] At the time of writing, the CCOM programme was revising its strategy for the second phase of the project, contemplating the centralization of the *caixas*, to the extent that all 32 of the existing *caixas* in the Montepuez area of Cabo Delgado would be served by one *caixa*. This new approach assumes that clients would be prepared to travel up to 200 km to receive and repay loans.

[156] Ester dos Santos (2005). *As Microfinances em Moçambique*, DNDR, Ministry of Planning and Development, paper presented to National Meeting of District Administrators.

The RFSP has allocated considerable resources for contracting agencies to promote *caixas comunitárias* and ASCAs. However, the issue of building up the capacity of human resources to meet the RFSP plans as well as the rapidly growing demands from donors such as the ADB, World Bank and bilateral agencies does not appear to have received adequate attention. On-the-job training has serious drawbacks because of its lagged effects, thus slowing down the spread and impact of the programmes. To overcome this constraint, greater commitment is needed by both government and the donors to establish appropriate facilities for developing the requisite training modules for the various skill levels needed to ensure the unimpaired growth of these and other financial services. An important but relatively small step in this direction has been taken by the Financial Services Technical Assistance Programme (FSTAP) to finance microfinance courses for six months through the Bank Training Institute.

5.5.3 Developing Financial Products to Better Suit Client Needs

Although many MFIs claim to undertake regular market surveys of client needs, there are indications that there is considerable room for improving the array of financial products to better suit client needs. The urban client impact assessment showed that more than two-thirds of any group of clients who started borrowing two years ago would have dropped out. Although some of the dropouts are likely to have satisfied their borrowing needs, it is expected that many would have continued to borrow if the benefits derived from the loans were greater or if the methodology would have made repayments easier (clients often found the repayment of a comparatively large amount on a monthly basis difficult within their financial system, combining informal forced savings arrangements, informal sector activities and often salaries). The study also showed that younger urban clients were not benefiting from microfinance.

In the rural areas, ASCAs have been found to be imbalanced in terms of overall client needs. More remote village groups tend to save but do not fully use the accumulated savings for credit, while in towns, ASCA groups were found to have credit needs greatly exceeding the member savings. Such imbalances suggest that there is scope for transferring accumulated savings from rural areas to meet the credit needs of the more urbanized groups. Recent experimentation with *caixas comunitárias* suggests that there is great demand for savings products by the solidarity groups but, until now, only credit products have been available.

The urban impact study also found that microcredit has had a very positive impact on those clients demonstrating entrepreneurial abilities. It appears that many clients are unable to benefit from small loans for the simple reason that their only strategy is to increase their stock in the hope of selling more – a difficult proposition in the informal market where there are virtually no barriers for competitors. Although requiring more investigation, there seems to be a strong argument for providing basic business skills to microfinance clients, though not provided by the MFIs themselves.

The urban impact study also found that a considerable amount of microcredit was being channeled into non-business expenditures, in particular for the expansion or rehabilitation of housing and buying consumer durables.

5.5.4 Stakeholder Participation in the Evolution of Microfinance

The evolution of microfinance in Mozambique owes much to a synergetic interchange between its stakeholders. It is important that such an ambience continues but there are signs that, with the growing sophistication and commercialization of the industry, stakeholders are becoming more insular by creating groups that represent the specific interests of their members. The Informal Working Group, having played a significant role in developing the industry, is now in serious need of transforming itself into another body that continues to ensure stakeholder interchange.

The national strategy contemplates the creation of a commission made up of various stakeholder representatives. The Third National Seminar also recommended establishing some form of coordinating body. While the donors and government have created their own working groups, the operators are more difficult to mobilize under an umbrella group for two reasons: disparity of interests and geographic dispersion. The idea of creating an association for microfinance operators has been debated for some time and features as a committed component of the RFSP. With some justification, operators have resisted pressures to create such an association claiming it is a body that is desired more by the donors than by the operators themselves. In late 2005, the large operators in Maputo initiated monthly meetings to consider common interests and the feasibility of establishing an operator association. Although these meetings are now open to all MFIs, one problem that will need to be addressed is how the interests of smaller operators throughout the country will be represented. The recent RFSP initiative to ask the operators to formalize a representative structure has been initially received with some reluctance but the importance of such representation (assumed to include a broad range of institutions) is being given a high priority by representatives of the RFSP, government and donors. At the time of writing, there appeared to be a general recognition of the importance of establishing an association of MFIs, but little consensus on how such a body would be structured or operate.

The creation of the IPRMF in 2005 was a significant development towards achieving a coordinated approach by donors to rural and microfinance. In 2006 it set an indicative plan of activities which included: *"contributing to the definition and implementation of the 'Microfinance National Policy and Strategy'; being recognized as a subgroup of the Financial Sector Working Group; to establish a link with the PROAGRI Group; establishing a strong dialogue with the microfinance operators; supporting the creation of the Commission of coordination of the microfinance sector; and identifying a governmental counterpart and establishing a regular mechanism of dialogue with it."*

One of the features of the Microfinance Informal Working Group that accounted for much of its success was the fact that it was open to anyone wishing to attend. It is important that this opportunity continues and that microfinance not become a behind-closed-doors industry. Even if a formal coordinating commission is established, all stakeholders should be allowed the opportunity to present their ideas/concerns and to have open debates on issues on a regular basis through a highly inclusive type of forum that would allow observers to participate.[157] Although such an arrangement may not overcome the problem of geographic dispersion, it would at least allow more remote operators to participate directly in meetings.

An effective way of overcoming the lack of information exchange, especially outside of Maputo, would be to establish a website (probably managed by the MFI association or the forum) with information relevant to operators throughout the country such as the quarterly statistics compiled by the MMF, chronology of relevant events, tenders for financial service provision, the posting of important research studies such as those mentioned in the introductory chapter. A chatroom allowing electronic exchanges between operators and experts in the field could also be of great benefit.

5.5.5 Continued Improvement of the Operating Environment

In a recent presentation on behalf of the operators, policy issues that still needed attention were highlighted.[158] Despite significant progress in terms of legislative reform, it was felt important that the beneficiaries of the Upstream Project in the BoM and the Ministry of Planning and Development be encouraged to transmit what they learned to their colleagues and to lobby for changes in various aspects of policy and legislation. Examples of issues that still needed attention included the following:

- The government introduced a new way of calculating the stamp tax to be paid on every contract which is even more complicated and very time-consuming, resulting in some operators having to hire a full-time person just to deal with the calculations. Operators feel that this tax renders little income for the government and impedes institutional efficiency.
- Clients signing contracts are required to have their identity document (BI) that can take 6-12 months to obtain and chits indicating that the BI is in process are not acceptable as substitutes.
- All contracts require notarial stamps, a time consuming process, which is felt to be unnecessary as contractual breaches are very unlikely to ever find their way to the courts.

[157] The idea of creating a more encompassing stakeholder forum is presented in the study by Buisson (2005) but is of a more formal nature than the one suggested above.
[158] Presentation by Kathryn Larcombe at the Closing Seminar of the Upstream Project June 2005.

- Donations for operational costs are treated as income and are therefore taxable. Most operators rely initially on some donor contribution for operational costs and much of the support from the Rural Finance Support Project is expected to be in this manner.
- In calculating capital adequacy, the BoM does not recognize donations for fixed assets and the loan fund as part of shareholder funds, despite the fact that the regulation could be interpreted in this way. Some operators claim that despite waiting for more than two years for clarifications, they have received numerous warnings of being in contravention of the regulation.
- BoM inspectors criticized the use of domestic goods as collateral – a commonplace practice amongst operators. In this and in other aspects, some inspectors demonstrate a lack of understanding of microfinance.
- During the Upstream Project, beneficiaries apparently did not visit local institutions to gain a better understanding of microfinance in Mozambique. While other countries were visited, operators were concerned that such visits were not very helpful unless put into the national context.
- With the deadline for operators to choose one of the legal options stipulated by decree 57/2004, there is some concern that the legislation has not sufficiently addressed the issue of PCRs. Establishing cooperatives is still complex and the other forms of local savings/credit organizations need to be more clearly defined by the BoM.

5.5.6 Confronting HIV/AIDS

Mozambique is a country that is deeply affected by the HIV/AIDS epidemic. Already one of the ten most infected countries in the world, Mozambique is also bordered by five countries with some of the highest national prevalence rates: South Africa, Swaziland, Zimbabwe, Zambia and Malawi (Tanzania has a relatively low rate). Mozambique's national HIV prevalence rate was projected to grow to 16.2% by the end of 2004, with the Sofala, Manica and Maputo provinces each having provincial infection rates above the national average. The microfinance industry in Mozambique cannot afford to ignore the reality of HIV/AIDS in their working environment and must therefore take a proactive, yet cost effective, stance against HIV/AIDS in order to reduce the impacts of the disease.

While there is considerable funding available for HIV/AIDS health and social programming, there is comparatively little assistance for HIV/AIDS mitigation in microfinance.[159] HIV/AIDS has demonstrated its ability to attack all components of society, from the household to the marketplace. Microfinance can play an important role in mitigating the impacts of HIV/AIDS by providing a means for individuals and communities affected by the disease to continue to develop their businesses, store up financial assets and enhance their overall quality of life.

MFIs need to better understand the impacts of HIV/AIDS on their clients and appropriately modify their microfinance products and services.[160] MFIs can look to partner with established insurance providers in order to offer microinsurance to their clients in addition to loans and savings. MFIs need to consider the impacts of HIV on their human resources and develop appropriate employment policies. MFIs should also establish partnerships with specialized organizations to offer seminars and educational materials to clients to better educate them on the facts about HIV/AIDS prevention and treatment.

5.6 Concluding Remarks

This study has attempted to deal with several of the concerns raised in the Statement of the Advisors Group to the United Nations International Year of Microcredit 2005, in particular their concern about information gaps and the lack of understanding of client needs. By comparing the data obtained from all known microfinance operators in the country with earlier studies, this study has demonstrated the significant progress made over the past decade. It also provides the reader with detailed information about each operator participating in the survey. The report has been richly enhanced by the results

[159] Uganda has pioneered work in this field. One example is the Uganda Women's Effort to Save Orphans (Uweso) that provides credit to women who look after children, most orphaned by HIV/AIDS.
[160] Some of these modifications could include: i) flexible loan repayment terms allowing clients a longer period of time before their initial payment; ii) low interest, emergency loans with negotiable repayment rates to assist clients with immediate capital needs; iii) establishment of a voluntary emergency fund in which clients can make contributions and apply for withdrawals in times of need; iv) allowing loan accounts to transfer to other non-infected members of the family; v) allowing family members to attend group meetings in place of the sick client; vi) increasing the clients'contributions to a loan insurance fund that could be used to underwrite outstanding loans.

from the urban and rural client impact studies, providing the first rigorously researched insights into client behaviour and perceptions. Furthermore, a detailed chronology of events that contributed to the overall evolution of the microfinance industry has been presented in order to help future researchers better understand the role of the various stakeholders in this process. Finally, it will serve as a useful guide for the microfinance technical assistants who come to Mozambique with little understanding of the wider context of the sector in which they are engaged.

"Microfinance" is a generic term applied to a diverse and complex array of stakeholders, products, methodologies, institutional forms, target clients, target activities and locations. Studies such as this are expensive and time-consuming undertakings, based on periodic surveys that depend on the sporadic interests of donors. With intervals of several years and different sponsor objectives, inter-survey comparisons will always be difficult. Given that the Bank of Mozambique should be monitoring registered microfinance operators, it is recommended that in the future the BoM, perhaps in collaboration with a representative body of the MFI operators, conduct regular analysis of the operators, using a standard questionnaire from which information for key indicators could be taken and published in its annual report and website. In this way the evolution of this crucial sector can be much more effectively monitored.