Microfinance in Africa: Is it Either the Problem or the Solution?

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Summary. — This article is based on research undertaken on microenterprises in the informal sector in Kenya, Malawi and Ghana. It seeks to provoke critical reflection on the uncritical enthusiasm that lies behind much proselytizing of microfinance for informal sector microenterprise. It questions whether the extensive donor interest in microenterprise finance really addresses the problems of microentrepreneurs or whether it offers the illusion of a quick fix. It suggests that the real problems are more profound and cannot be tackled solely by capital injections but require fundamental structural changes of the socioeconomic conditions that define informal sector activity and a fuller understanding of the "psyche" of informal sector entrepreneurs. © 1997 Elsevier Science Ltd

1. INTRODUCTION

In the 1990s the field of microenterprise finance has expanded enormously. There have been some striking experiments mostly from outside Africa which have allegedly produced impressive results, usually measured in terms of outreach and repayment rates, and which have been driven largely by the perceived demand for credit. Some have alleged that this "new world of microenterprise finance" has the "potential to do in finance what the green revolution has done in agriculture — provide access on a massive scale to the poor" (Otero and Rhynes, 1994p1). To date, institutional innovation and experimentation appears to have raced ahead of serious analyses of client impact, the evidence for which often appears quite anecdotal or inconclusive. In addition, it is clear that the whole momentum has been sustained by substantial donor finance. Although various moves are afoot to move toward institutional sustainability and hardly a single credit program appears to be without its sustainability projections, the actual evidence appears thin on the ground. The question of sustainability without either substantial donor subsidies or a shift toward less poor clients (i.e. from microenterprises to small businesses) has not been answered (at least in Africa). This article suggests that the current fascination with microfinance may be just as optimistically misplaced as an earlier fascination with smallholder, rural and cooperative finance in the 1960s and 1970s. The mechanisms for delivering credit, such as in the tendency to avoid direct subsidies, may have changed but the objectives remain similar (Adams and Von Pischke, 1992). This paper is based on original research undertaken in Kenya, Malawi and Ghana over a three year period and forms part of a wider investigation into the respective informal sectors of these countries.

2. SOURCES OF ENTERPRISE FINANCE

Although institutional finance for microentrepreneurs in the informal sector is fairly new, informal sources are not. Informal finance is multifarious and ubiquitous to informal sector economies in Africa and most entrepreneurs make use of informal sector financial intermediation. Like the informal sector itself, informal finance can be viewed as lying somewhere along a continuum that separates complete formality and complete informality, in this sense, ranging from casual loans and gifts from family and friends to formal sector commercial bank loans. The most common source of enterprise finance is from family or friends but institutionalized forms, such as rotating savings and credit associations (ROSCAs) were also common in some of the survey locations, as were arrangements with merchants and traders but moneylender use was much

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less prevalent. There were also many respondents who had a relationship with the formal financial sector but this was nearly always in terms of savings deposits and not lines of credit. There were five broad avenues of financial intermediation identified by the fieldwork: formal institutions (including commercial banks, the post office, credit unions, government and nongovernmental organization (NGO) credit/savings projects; moneylenders; merchants and traders; friends and relatives; and ROSCAs/savings clubs. Without denying that other forms of finance exist in each of the case study countries, the fieldwork did not reveal significant direct or indirect information on other practices such as money transfers from landlords (known to be common among cocoa farmers in Ghana) or of pawnbroking (which was referred to by only one or two respondents in each country).

The major sources of enterprise start-up funds (Table 1) gives a very good indication of the type of financial resources available to microentrepreneurs. The principal source is usually the entrepreneur herself — over half of all enterprises were started largely with self generated funds. In most cases these came from either savings made from sales of agricultural produce or from employment. Usually, self-generated funds are supplemented by either gifts or flexible loans from friends and/or relatives but in Malawi and Ghana a third of respondents actually identified this as the major source of finance when they set up in business. The comparatively lower figure for the Kenya Regional sample (and correspondingly higher number of enterprises started principally from personal savings) is probably a reflection of the fact that these entrepreneurs were more likely than those in any of the other samples to have been both male heads of household and with income from farming activities and, therefore, likely to be in a better position to self finance business activity. Loans from an organization or someone else refers to formalized credit, including commercial bank loans, NGO credit projects and government credit programs, together with moneylenders and merchants or suppliers. As the figures indicate, these sources of finance were relatively uncommon at the enterprise formation stage. Similarly, although many respondents were found to be in savings groups or ROSCAs, they were not significant sources of start-up capital.

It is clear, therefore, that microentrepreneurs set up in business principally with finance from themselves and their families/friends. Given the levels of operations characteristic of this sector it would be tempting fate to suppose that the “typical” informal sector microentrepreneur would benefit from larger volumes of funding at the start up stage. Nor would it be judicious to assume that those who have not set up in business would make the best use of any prospective funding, as already it would appear that they have distinguished themselves as being less entrepreneurial than those who have already embarked on an enterprise (taking on risk, opportunity seeking, delaying gratification etc.) and therefore, perhaps less likely to “succeed” in business. Thus, putting together one’s finance informally can be construed as an appropriate screening device. It can be argued that if a person cannot save and attract funds for an enterprise activity from those people who know him/her best, it can be doubted that a loan from a microenterprise credit program would be the most appropriate method of overcoming the problems faced by this person.

Once established and with a measure of credibility, entrepreneurs appeared to become more integrated with formal and informal financial intermediaries (Table 2), although self-generated funds and those from friends and/or relatives remained predominant. Aside from these, the most prevalent source of finance was from suppliers. In some cases these suppliers or merchants brokered credit in cash as a subsidiary to their trading activities but more usually this type of credit was linked to the sale of an entrepreneur’s products or his purchase of commodities (usually inputs to the business). In many ways, in the minds of microentrepreneurs, the supplier/merchant seemed to stand midway between the moneylender and friends/relatives: loans were usually short term, flexible and dependent on a close relationship between the borrower and lender. Often

<table>
<thead>
<tr>
<th>Table 1: Major sources of enterprise start-up funds (percentage distribution)</th>
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<tr>
<td></td>
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<tr>
<td>-----------------------</td>
</tr>
<tr>
<td>Personal savings</td>
</tr>
<tr>
<td>Loan or gift from friend or relative</td>
</tr>
<tr>
<td>Loan from an organization or someone else</td>
</tr>
<tr>
<td>Don’t know/cannot remember/ etc.</td>
</tr>
</tbody>
</table>

Source: Author’s fieldwork
Table 2. Credit and savings experiences (percentage distribution)

<table>
<thead>
<tr>
<th></th>
<th>Kenya Kibera (n=160)</th>
<th>Kenya Regional (n=140)</th>
<th>Malawi (n=160)</th>
<th>Ghana (n=150)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit given to customers</td>
<td>70</td>
<td>68</td>
<td>66</td>
<td>77</td>
</tr>
<tr>
<td>(% saying yes)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit received from suppliers, i.e. merchants (% saying yes)</td>
<td>26</td>
<td>25</td>
<td>18</td>
<td>45</td>
</tr>
<tr>
<td>Those who have obtained formalized credit (%)</td>
<td>3</td>
<td>13</td>
<td>20</td>
<td>5</td>
</tr>
<tr>
<td>Those who have used a moneymailer (%)</td>
<td>&lt;1</td>
<td>3</td>
<td>9</td>
<td>10</td>
</tr>
<tr>
<td>With a formal sector bank account (%)</td>
<td>56</td>
<td>88</td>
<td>15</td>
<td>53</td>
</tr>
<tr>
<td>Members of a ROSCA or similar informal sector savings entity (%)</td>
<td>61</td>
<td>54</td>
<td>59</td>
<td>48</td>
</tr>
</tbody>
</table>

Source: Author's fieldwork

there was no explicit interest charge, rather the price of what was supplied or purchased was adjusted to give the lender his margin. For the lenders, this type of credit was likely to widen and deepen their customer base (getting more customers and selling more to them). There were broadly two types of entrepreneur likely to use this type of financing. Those with a trusted record and relationship with the lender who were likely to get this type of credit on reasonably advantageous terms and, probably a greater number, who obtained such credit on the basis of their weak and vulnerable position. They needed such lines of credit simply for their enterprises to survive and this was exploited by the supplier. Sometimes, for example, the supplier would provide inputs such as cloth on credit and purchase the borrower's output, a garment in this case, at a price minus the cost of the selling price of the original cloth plus a "fee" for providing the credit. The result, of course, is a cheap garment for the supplier to retail at a further mark up.

On average between two-thirds and just over three quarters of respondents from each subsample gave credit to their customers. This was usually done to either get new customers or to encourage existing customer loyalty. Interest rates were applied only in exceptional cases and the terms and conditions of customer credit were often the mirror image of the entrepreneur's relationship to suppliers. Often customers would pay by ad hoc installments after making an initial downpayment, thereby initially supplying credit to the entrepreneur before becoming indebted to her. Sometimes the entrepreneur would build in a cover charge to the total cost to the customer but often was unable to do even this because the high levels of competition and poverty of customers were likely to give the entrepreneur little room for maneuver. For some types of enterprise activities, such as fitters/mechanics and tailors, the initial "down payment" given by customers was often in the form of inputs rather than cash. For example, a dressmaker would receive cloth from a customer to make a particular garment, do the work, provide the finished article to the customer and wait for payment to come, typically at month end when formal sector employees were paid or after a harvest. Another type of credit arrangement common to some types of enterprise activities, such as the provision of "fast food," involved regular customers accumulating debts and settling up after a particular number of items had been taken or consumed, or at week or month ends. For those types of activities that made use of apprentices (tailors, metalworkers, carpenters etc.) there may well exist the possibility of generating funds from fee paying apprentices, a type of bonded labor. Sometimes it was found that entrepreneurs deliberately took on apprentices not just as a cheap form of labor (often for the business and the household) but also as a source of income from the regular fees paid by apprentices or their sponsors (Velenchik, 1995).

In contrast to credit brokered between customers and suppliers, the incidence of formalized or institutionalized credit was very low. Generally, commercial banks rarely take much interest in the informal sector and microentrepreneurs are aware of this. Among the Kibera subsample, for example, 96% of respondents had never applied for a loan from a bank usually because they had neither the skills or collateral to be taken seriously. Six respondents had, in fact, applied for a bank loan, three were turned down and three were successful (all of whom were women with husbands in formal sector employment). The respondents in the Kenya Regional sample tended to own more sophisticated businesses with larger amounts of fixed capital and hence security (many of them also had land titles) so it was not surprising to find that a far greater number had obtained formal sector finance. A number had also received credit from either government or NGO-
funded projects. The exposure of the respondents in Ghana to formal sector credit falls between that of the two Kenya samples, although all but one of the seven respondents who had obtained formal finance were located within the Kumasi subsample (two of them had got loans from a special fund for small scale entrepreneurs set up by the Government under the country’s structural adjustment program). In Malawi there was evidence of a surprisingly high number of respondents having used formalized finance. In fact, none of the respondents had obtained commercial bank loans and the very few who had obtained enterprise finance had done so from an NGO project. Nearly all of those who had obtained formal finance had actually got agricultural credit in kind from a government parastatal concerned with financing maize production and not for their microenterprise activity.

3. MONEYLENDER FINANCE

Moneylenders have a prominent place in the literature on informal sector finance and are considered to be significant sources of finance for low income groups (Adams and Fitchett, 1992) but in some places during this research it was difficult to find them. Moneylenders are defined as those individuals who spend a significant part of their time lending money, usually for short periods and sometimes unsecured by collateral. Interest rates are usually relatively high but borrower transaction costs are low and disbursement is normally quick. Moneylenders tend to operate in highly localized markets and have close relationships to their debtors, which limits the numbers of loans they are likely to extend at any one time. Among the Kenya samples, the reported use of moneylenders was very low which appeared to be a reflection of the stigmatized nature of moneylending and the absence of moneylenders in particular areas (the sensitive nature of moneylending may well imply that more people had actually used this form of finance than were willing to admit to it). For the Kibera sample, the poverty and transient nature of much of the population were also factors that mitigated against moneylender activity. Those respondents in the Regional sample who had used a moneylender had, in each case, obtained money from Asians.

In Malawi a greater number of respondents admitted to having obtained loans from moneylenders. In all cases the loan was for consumption/distress purposes and involved relatively small loans with short maturities. Respondents, whether they had used a moneylender or not, were unanimously of the opinion that their behavior was exploitative and that they should be avoided (people did not consider moneylender charges in terms of opportunity cost, inflation, risk, or any other factor that can be argued to place moneylenders in a less negative context). Most believed that moneylenders generally got a 100% return on their loans irrespective of the time-frame. Whether the loan was to be repaid in a week, a month or a season, the standard cost was a doubling of the original amount lent (see Chipeta and Mkandawire, 1992 for information on the origins of moneylending in Malawi).

Most respondents knew that moneylenders were unlikely to give relatively long term loans (for seasonal inputs, for example) and were usually most likely to make loans for consumption purposes, for distress consumption, such as for funeral or medical expenses, and at certain times of the year for the payment of school fees. There was a general feeling that moneylenders would not lend to the poorer members of a community but only to those who could offer some form of surety such as a member of the family with a waged income or a particular asset (moneylenders often insisted on loans being guaranteed by an mboni, a trusted or respected man or relative of the debtor, who would testify as to the borrower’s honesty and ultimately underwrite the loan). For those who had used a moneylender, the process of getting a loan had not been as quick as is sometimes assumed, although still much quicker than institutionalized methods of getting credit. First time borrowers were likely to incur a significant transaction cost measured in time consumed traveling to meet the moneylender, negotiating with him and then waiting for his response. Once one loan had been paid back and a record established the procedure was quick, provided the moneylender had liquidity. Among those respondents who admitted to using a moneylender, the average time taken between first approaching the lender and getting the cash was 2.28 days. Some reported having to make repeated visits to the moneylender to persuade him of their credit worthiness. Although the latter can foreclose on a borrower’s assets, this is a course of action which carries a number of costs for the lender as well as the borrower and the general feeling was that moneylenders preferred to avoid seizing assets as much as possible so were careful to undertake a thorough screening of potential borrowers. Nevertheless, asset seizure remained their principal sanction on default.

A similar picture emerged from the Ghana fieldwork but there appeared to be greater variety in the interest rates levied by moneylenders depending on the nature of the loan and, perhaps more importantly, the relationship between the lender and borrower. Indeed, this ability to craft loan contracts that are idiosyncratic is one of the major advantages that moneylender finance has over formal finance. Examples included a charge of 50% per month for a loan of 20,000 currency units; a flat rate 50%
payable on a loan of 500,000 currency units with a six month maturity; and an interest rate of 40% per year charged on a year long loan of 40,000 currency units. There was one unusual case of a respondent (a weaver) having set up his business with a moneylender loan. As in Kenya and Malawi, however, the general impression of moneylenders was a negative one. The most common reason for viewing moneylenders negatively was the interest rate charged (37%) followed by reasons associated with the behavior of moneylenders — “they are cheats...I’m afraid of them... I don’t like them”, etc.— (21%) and those who said they simply did not want or need them (15%). Other responses included moneylenders not known to be available in a given area (8 percent); not thought about it (8%) and other (11%) which included two respondents who screened themselves out on the basis of not having collateral or the type of security needed by a moneylender.

4. THE SAVINGS SIDE OF THE FINANCIAL SERVICES COIN

The other side of the financial services coin that appears in Table 2 is savings, which constitute the basis for achieving financial independence and the path toward microenterprise self-sufficiency. It is, of course, not credit itself that lever the poor out of poverty but their ability to save from income generated from the use made of credit. It is this side of the financial intermediation equation that sometimes appears to be undervalued in some quarters but not by commercial banks which seem much more predisposed to offer savings (deposit) facilities to poor microentrepreneurs than to offer them credit. By implication, microfinance programs that stress only lending are likely to be missing opportunities to assist the many poor people who may wish to save but do not necessarily wish to borrow.

The numbers with bank accounts (no differentiation was made between savings or current accounts) in Kenya is surprisingly high. Among the Regional sample 88% of respondents had an account (15% had two accounts) and even in the slum of Kibera over half of all respondents possessed an account. A similar percentage of Ghanaian respondents also had accounts and only in Malawi was there a low incidence of account holders, where virtually all of those with accounts were located around Blantyre. An explanation for the high number with accounts in both Ghana and especially Kenya, is hard to find although it appeared to be relatively easy to open an account and because of the status associated with having a bank account there appeared to be a strong demand for them. Although it was not possible to get systematic data concerning the amounts held in these accounts, the impression was that many accounts were dormant or with negligible sums in them, suggesting that the actual use of these accounts was low. Nevertheless, one conclusion that can be drawn on the issue of formal banking is that although formal banking institutions are averse to extending credit to the type of informal microentrepreneurs surveyed, they do not appear to have difficulties extending deposit facilities.

The ubiquity of rotating savings and credit associations (ROSCAs) and to a lesser extent similar entities such as savings clubs (non rotating community savings groups) throughout Africa is well documented (Fuglesang and Chandler, 1991) and the evidence from this research confirms that they are very common. On average over half of all respondents were members of these types of organization (called merry-go-rounds in Kenya, susu in Ghana and chiperengani in Malawi). Although ROSCAs vary in size and particular practices, the principles that define them remain fairly constant in each of the study areas. To begin with, members usually know each other and are bound by a common bond such as by location, ethnic group, approximate income level or type of enterprise activity. Members agree to contribute a fixed sum of money periodically (typically weekly or monthly) into a collective pool which is sequentially allocated to each member in rotation. Sometimes members will contribute odd amounts at different times to bring their total weekly or monthly obligation up to the required level. At the end of each collection period or at meetings, the pool of collected money is given to one member, at the next occasion to the next member, and so on. At any time during a full cycle of dealings, members who are waiting their turn are creditors to the ROSCA (net savers) and those who have received a pool of money are debtors (net borrowers). As the ROSCA moves through a cycle these positions are rotated.

ROSCAs are popular among microentrepreneurs, offering them a self sufficient, voluntary-based organizational framework through which to save and borrow. It is also significant that members are not accountable to their ROSCA for the use of the funds they get and are therefore free to use the money for whatever they wish, which is not the case for most other types of finance. But ROSCAs are not only popular, they are also highly efficient. They constitute an arrangement whereby group solidarity (which forms the basis for risk management) is nurtured around a closed circular flow of money where savings match credits without the need for interest rates or tangible collateral and where transaction costs are kept very low. In the words of one eminent commentator: “the ROSCA is intricate, yet fundamentally simple and elegant. It is state of the art intermediation, as well designed to finance as a Bach fugue is to classical European music” (Von Pischke, 1992, p.330).
In Ghana, a common method of saving was in the form of savings groups organized by an itinerant collector (susuman). The collector would act as the intermediary, collecting daily deposits of an amount determined by individual savers, which were usually then placed on deposit in a commercial bank, and distributing each member’s savings at the end of a given month minus one day’s contributions which he kept as his fee. He would keep records and distribute savings cards to members for them to keep a record of their contributions. Although he charged a fee, he reduced the transaction costs of members, as they did not have to meet up to pool and disburse funds or to chase after members who delayed on payment of their contributions as in ROSCAs, and his presence seemed to encourage savings discipline. These savings groups are voluntary arrangements but it is obviously in the susuman’s interests to mobilize as many clients as he can and encourage them to save as much as they can because this increases his profits, which often seemed to be quite considerable (it was not uncommon for a susuman to have over 100 clients).

In Kenya, conventional small group ROSCAs, with a greater social purpose and led by ROSCA organizers or committees were more commonplace, rather than the type of savings groups maintained by a susuman in Ghana. ROSCAs were also common in Malawi but so too were community funds (sometimes known as ASCRAs: accumulating savings and credit associations). These groups were usually based on membership of a religious or social organization and comprised anywhere between 20 and more than 100 individuals. Members typically contributed into a savings fund to meet a target for a particular community project but individuals could also borrow funds for which interest was usually (but not always) payable. Such community funds have their equivalents in Kenya (harumbee) and Ghana but, among those surveyed, appeared to be much less common.

5. THE DEMAND FOR CREDIT (OR DEBT)

It is generally believed that a lack of credit is a major problem for microenterprises in Africa and this study confirmed this. But, few entrepreneurs anywhere in the world are likely to answer the simple question: “Do you need credit now?” with a categoric “no,” so it would be surprising if informal sector entrepreneurs were any different. More illuminating questions concern the demand for different types of credit, the loaded question: “Do you want to have debts?” (which is, of course, another way of asking the first question) and the terms on which the credit would seem acceptable. The latter issue is very difficult to appraise given the difficulty of acquiring reliable information from respondents: one can assume that the spectrum in monetary terms is bounded by moneylenders at one end and gifts at the other. Table 3 gives some answers to the first question. First, between 4 and 14% of respondents in each location did not feel they wanted any credit. This was usually because of an aversion to being in debt sometimes as a result of a bad experience (one Ghanaian respondent had actually ended up in court when he got into difficulties repaying a government funded loan). A number of respondents said they were too old to receive credit and a few felt happy with the level at which their businesses were operating and did not want to take on an extra burden implied by taking credit.

Although it was not always easy to separate credit into fixed and working capital elements, it was found that most respondents wanted credit for working capital either exclusively or in combination with a particular fixed capital item. This was expected, as the majority of respondents operated enterprises with very low fixed capital requirements and in Kenya Kibera and Malawi, in particular, there were large numbers of traders.

<table>
<thead>
<tr>
<th>Table 3. The demand for credit (percentage distribution)</th>
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<tr>
<td>Credit not currently needed (%)</td>
</tr>
<tr>
<td>(%) wanting credit for working capital only</td>
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<tr>
<td>(%) wanting credit for fixed capital only</td>
</tr>
<tr>
<td>(%) wanting credit for a mixture of fixed and</td>
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<tr>
<td>(%) wanting credit for diversification of</td>
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<tr>
<td>(%) wanting credit for non enterprise purpose</td>
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<tr>
<td>Kenya Kibera (n=160)</td>
</tr>
<tr>
<td>Kenya Regional (n=140)</td>
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<tr>
<td>Malawi (n=160)</td>
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<tr>
<td>Ghana (n=150)</td>
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<td>Source: Author’s fieldwork</td>
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who invariably wanted credit to increase their stocks of goods for sale. Together with those respondents who used relatively large amounts of a particular raw material input such as tailors or carpenters, there was a common desire to get credit to purchase either in bulk at a discounted unit price or to juggle supply and demand by purchasing at times of relatively high supply and low price and thereby increasing the value added or resale margin for the microentrepreneur (sometimes this strategy was combined with a desire to cut out or reduce dependence on middlemen). For some types of activities such as tailoring, there was a desire to obtain working capital so that entrepreneurs could produce for stock rather than to customer orders and thereby reduce down-time or slack periods.

Where fixed capital was wanted it was often for a particular piece of equipment that the respondent felt would give her a competitive advantage (rarely was it for direct replacement of broken or old equipment). Many carpenters wanted circular saws so that they could cut their own planks rather than rely on a sawmill; tailors repeatedly suggested the need for an overlocking machine to do particular types of stitching; and metalworkers of various sorts wanted particular types of welding equipment. It was not always clear however, whether such needs had been clearly thought through or whether particular respondents had simply seen or heard of a new piece of equipment that was available and they imagined that it would give them an advantage. Such problems as repaying the loan and the effects on cash flow of what would most likely be a fairly highly leveraged investment were seemingly not fully anticipated, nor was the possible need for training to use the new equipment properly; whether it was really compatible with existing levels of operations and the types of markets currently serviced; or of the potential difficulties of servicing or repairing the equipment.

A few responses were somewhat grandiose, such as that given by a respondent from the Kenya Regional sample, whose mattress business was barely in existence, yet he suggested he needed a loan to purchase a pick-up truck to deliver the mattresses he made. Those wanting credit for general expansion included a number of respondents who wanted credit but were unable to specify a particular purpose (this was particularly common in the two Kenya samples). Almost a quarter of Malawian respondents wanted credit to set up a different type of enterprise (diversification) which appeared to be primarily a reflection of the low margins currently obtained by many respondents (they wanted to move into something perceived as being more profitable) but in some cases appeared to indicate a sometimes erroneous impression that other people with other types of enterprise were doing much better than the respondent. In many cases there were likely to be other mitigating circumstances that resulted in these perceived inequalities and, in any case, the levels of competition in the activities perceived to be profitable — such as fish selling — were usually very high.

A relatively small number of respondents decided they would prefer credit for non-enterprise purposes. In reality, the figures given are probably an underestimate. Given the economic condition in which many respondents live, it would not be unreasonable to believe that with the cash (credit) in their hands, respondents would have found many more pressing household and personal consumption needs that they would have prioritized above credit for business needs. Nevertheless, among those citing the need for non enterprise credit the greatest number wanted to purchase agricultural inputs or livestock, followed by improvements to houses. One person (Kenya Kibera) wanted a loan for his wife so that she could train to become a dressmaker and another admitted to needing a loan to pay off an existing loan.

Another group of respondents all of whom had received one or more loans from specialist microenterprise lending institutions (i.e. formal credit) were also asked about their credit needs. The majority were currently servicing a loan. The results obtained (Table 4) were very similar to those obtained from the those microentrepreneurs included in the samples above (Table 2) — the inference being that despite having received credit, the demand for it appeared to remain fairly constant. There did not appear to be any movement toward self-sufficiency or graduation away from microfinance programs even for those who had received four or more credits. In fact, among those respondents from the Kenya Kibera sample there was a slightly greater number who needed more credit than among the random group where 97% of respondents had never received any type of formal credit. Furthermore, the impact of these credits on operations — measured in terms of increased sales, profitability or employment — was negligible and little different to the same set of variables recorded for those similar microenterprises which had not received credit.

As mentioned above, the demand for credit means the same as the demand for debt, the difference being whether one takes the creditor's or the debtor's viewpoint. Thus, as a caveat to the line of questioning above, the respondents in Ghana were asked how they felt about being in debt (the actual question was separate from those on credit so as to reduce the potential for biased responses). Over a third of respondents in Ghana said that they never wanted to be in debt (but only 13% said they did not want credit) and 41% said that they did not like the idea of being in debt but acknowledged that it was sometimes necessary to be (Table 5). This question, then, tends to confirm the confusion of the terms debt and credit that exists in people's minds, whereby they tend to
Table 4. The demand for credit among those with a formal credit history (percentage distribution)

<table>
<thead>
<tr>
<th></th>
<th>Kenya Kibera (n=100)</th>
<th>Kenya Regional (n=100)</th>
<th>Malawi (n=80)</th>
</tr>
</thead>
<tbody>
<tr>
<td>More credit/or a follow on credit not currently needed (%)</td>
<td>10</td>
<td>7</td>
<td>14</td>
</tr>
<tr>
<td>(% ) wanting credit for working capital only</td>
<td>31</td>
<td>20</td>
<td>37</td>
</tr>
<tr>
<td>(% ) wanting credit for fixed capital only (including repairs to fixed capital items)</td>
<td>7</td>
<td>30</td>
<td>12</td>
</tr>
<tr>
<td>(% ) wanting credit for a mixture of fixed and working capital or general expansion</td>
<td>22</td>
<td>26</td>
<td>25</td>
</tr>
</tbody>
</table>

Source: Author’s fieldwork

view credit as something positive and debt as something negative. There is, of course, nothing wrong with these perceptions as long as the terms are not confused.

The debt/credit issue is one of semantics and centers on one’s perspective on this aspect of finance. It also suggests that savings and credit concepts may not be as clear cut as some would like to think. For example, a large amount of savings in Africa are held in non-monetary form (livestock, land, jewelry etc.) and therefore savings are often difficult to distinguish from investment or even consumption. It is the same case with credit, which can take any number of forms where an obligation or expectation of future compensation is involved. Undoubtedly, the vast majority of “credit” in Africa takes a non-monetary form including the lending of labor and tools. It is also important to recognize that not all African languages contain discreet and accurate translations for terms such as credit, debt, interest rates, repayment cycles, collateral and so forth, so meanings may change or at least differ in translation. Finally, cultural differences can also add different dimensions to the savings and credit conundrum. Interest charges, for example, are often perceived in a different context in Africa than in the North. The convention of separating usury from fair lending in terms of interest ratios (interest to principle, as the amounts are finally repaid) with the amount of time elapsed being of less importance (Shipton, 1992). Such differences in interpretation of interest charges can also be found on the basis of religion (Islamic conceptions of interest charges being a classic example).

Another factor influencing the demand for credit is the perceived nature of credit, not so much in terms of its conceptual meaning but in terms of its practical value. It has already been mentioned that it is not surprising to find a high demand for credit among informal sector entrepreneurs. But this demand is clearly conditioned by what people perceive as credit and what people perceive as their problems. Many respondents in the Kenya Regional sample, for example, were located in areas where donor and/or government credit programs had operated. Many people had had soft loans and many had defaulted. The lenders had seemingly given up trying to get the money back, so for many people, credit from outsiders (the government, donors, whites etc.) was not greatly dissimilar to a gift. This was vividly captured by the respondents who said they “would like an unconditional loan.” Similarly, many respondents believed that the key to increased sales was increased stocks and, therefore credit was the key to achieving this. This is obviously true but only up to a point and the assumption, which often seemed to exist, that sales would rise with stock ad infinitum showed a sharp neglect for other limiting factors, such as local liquidity. In other words, credit may be neither the real problem nor the answer to the constraints experienced by many microentrepreneurs.

Table 5. The demand for debt in Ghana (percentage distribution)

<table>
<thead>
<tr>
<th>(%) responses to the question: How do you feel about being in debt?</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>never want to be in debt</td>
<td>35</td>
</tr>
<tr>
<td>don’t like it but sometimes it is necessary</td>
<td>41</td>
</tr>
<tr>
<td>don’t mind as long as I can pay it off or the terms are not too severe</td>
<td>14</td>
</tr>
<tr>
<td>don’t know/other response</td>
<td>10</td>
</tr>
</tbody>
</table>

Source: Author’s fieldwork

6. WHY CREDIT OFTEN DOES NOT YIELD THE RESULTS EXPECTED

An important dimension to enterprise and entrepreneurship development is the issue of access to credit and particular markets but any attempts to
facilitate access to credit and markets runs the risk of being ineffective or even detrimental if they are not accompanied by changes in the undertakings themselves aimed at improving the use currently made of the factors of production (i.e. changes in techniques - ways of doing things - and/or technology - the equipment, machines, tools used). Less than 10% of all respondents who had received formal credit, including credit from NGOs, were able to demonstrate any type of change in technique or technology since they had received their first loan. It is erroneous to assume that credit inputs, for example, can yield results while assuming that internal decision making within enterprises is analogous to the neoclassical economists’ black box (i.e. unexplained). Furthermore, the emphasis placed by microentrepreneurs on finance as a constraint may reflect liquidity problems for reasons other than unsatisfied demand for credit. As suggested previously, apparent problems of capital shortages may be the result rather than a cause of managerial shortcomings, as partly confirmed by underutilization of capacity problems.

The following are posited as limiting the impact of microenterprise finance and in defense of the argument that warns of significant limitations to what credit alone can do for the “typical” microentrepreneur in the African informal sector. None of them individually necessitates the denegation of credit as a tool, nor is it assumed that these factors are unique to Africa (they are likely to exist to varying degrees in many other parts of the world) but taken as a whole, they imply the need to at least reappraise the existing tendency in some quarters to eulogize over the potential of microfinance to transform microenterprise and the economic condition of the microentrepreneur.

(a) Enterprise as an impermanent portfolio of activities

Often there is no specific, permanent enterprise activity but rather a variety of different activities that coexist or follow one another depending on such factors as input availability and agricultural seasons. This is typically the case for vending activities, although usually an entrepreneur will have a dominant or main activity that he or she tends to concentrate on, other things being equal. In addition, within the household there is often a blurring of responsibilities concerning domestic work tasks and roles and those of income generating or, where relevant, agricultural based activities. Thus, it is not always easy to delimit a specific business activity to which the entrepreneur is fully dedicated, which is an essential assumption of most credit projects.

(b) The lure of rural links and real estate (opportunity costs)

Enterprise is often seen as ephemeral, being tied into the life of its creator unlike land and real estate which may be perceived as a more secure if, sometimes, less profitable form of investment. Both these latter forms of investment act as insurance in the absence of state provision for retirement or ill health and their ownership is likely to bestow more kudos or status than the ownership of enterprises. Land and real estate do not normally perish and can be worked by kin to produce for consumption and income generation. The purchase and use of land and property, therefore, is likely to be a major attraction for surplus funds and a clamp on enterprise growth, although the flow of funds can work in both directions with surpluses from agriculture, for example, being diverted into enterprise capital especially at the enterprise start up stage. Once again, however, the effect is to increase the difficulty of delimiting enterprise activities and the flow of funds within them.

(c) The role of the extended family and kinship networks

The importance of the extended family can imply both positive and negative factors and is largely determined by the individual’s position or status in the community or society (Ake, 1990; Ayittey, 1990 and Dia, 1991). The extended family and kinship networks create entitlements and the practice of eleemosynary within extended families is endemic. Employment for kin, for example, is a type of insurance and fits into life cycle planning strategies or cycles of reciprocal obligations and can imply a drain on an entrepreneur’s resources or a source of cheap labor depending on the circumstances. Similarly, the prestige and power afforded to a successful entrepreneur by members of his extended family may act as an incentive to entreprenurial endeavor which may at least partially offset the disincentive effects of sharing income and wealth. The same networks can aid the aspiring entrepreneur with start-up capital and funds for enterprise expansion on favorable terms or act as a drain on financial resources if the entrepreneur is called on to fund funerals, school fees, etc.

(d) Particular role expectations, social sanctions and cultural standards

Many factors are relevant in this regard. For example, the social perception of the qualities pertinent to enterprising activity are very important
in molding the receptivity to opportunity seeking. In societies that place low status on economic individualism, for example, this is likely to limit entrepreneurial endeavor. The fieldwork accompanying this study uncovered numerous examples where entrepreneurs had appeared to increase their status by methods which effectively reduced the profitability of their businesses, such as by employing people with little regard for productivity. The proximity of social roles to those of strictly business management may mean that the entrepreneur has to balance his time between a variety of competing interests. Different groups (by tribe, gender or educational status, for example) may be expected to operate certain types of enterprise and not others, so encouraging the adoption of particular enterprise activities on the basis of reasons other than strictly economic ones. The manner in which wealth is managed can take particular forms dependent partly on such factors as the supernatural, superstition and social appearances (see Buckley, 1996).

Additional limits to growth may be determined by the desire to avoid “growing into formality” and the administrative and financial burdens this may imply. In addition, the very nature of operations may place limits on expansion. For example, if one operates at capacity (such as the volume that can be carried or stored) and all is sold at a particular price, there may be little incentive to cut price to sell more, especially if the entrepreneur is disinclined to delegate or enter into formal partnerships.

(h) The nature of the labor input

Few informal sector enterprises genuinely employ many people on a consistent, full-time basis. When they do, the labor is usually apprenticeship and/or family labor and there is often a high element of underemployment and low productivity which is accepted and tolerated by entrepreneurs, whereas, in other socioeconomic settings this may not be the case. The employment of kin over non-kin, close kin over distant kin or fellow ethnics over outsiders can be construed as rational if it implies that the entrepreneur is choosing closer people because the greater the degree of social cohesion, the greater the degree of trust, and the lower the transaction costs of protecting contracts. Thus, this employment practice becomes an alternative to formal contract law and to the vertically integrated firm. The prevailing economic conditions — abundant and cheap labor — infer that the labor input constitutes the main element in most enterprise activities. The importance of the labor input is also increased by breaking bulk into very small quantities, with such activities being particularly adaptable to the low purchasing power of most consumers. Thus, although labor productivity may not be a high priority for many entrepreneurs of the type interviewed, labor inputs are normally the fulcrum on which enterprise activity exists.

(i) Historical precedent

The importance and nature of prior contact with outside forces, especially the colonialists and the prior existence of physical markets contribute significantly to configuring the opportunity structure facing entrepreneurs. These factors have, of course, varied between countries but some commentators have attempted to demarcate generalized differences between Eastern/Southern Africa and Western Africa (Iliffe, 1983 and Geiger and Armstrong, 1964).
(j) Weakness of factor markets

Markets may not exist or be poorly defined in purely economic terms. The market for enterprise finance being a good example. From the surveys, it was shown that a major factor in obtaining finance rested on family and kinship networks and not necessarily on purely economic criteria. Often, prices are not applied to certain goods and services because of the costs of doing so. Family and apprenticeship labor is a good illustration of this with allocations usually made principally on the basis of kinship networks rather than market prices and often involving the exchange of gifts or the expectation of some future reciprocal obligation rather than a direct factor reward in the form of a wage payment. It was also found that these same kinship networks, rather than market based alternatives, formed the basis of many problem solving strategies.

(k) Scarcity and economic survival

Enterprise success is largely determined by how entrepreneurs cope with their environment. The informal sector environment may imply that entrepreneurs place an “invisible ceiling” on their enterprise growth defined by an inhibitory or interfering regulatory environment, poor infrastructure, a lack of access to capital, and so on. The paucity of economic opportunities and severe demand constraints often imply the need to surmount survival barriers which may limit the potential for entrepreneurial behavior. It may be that the closer one is to the margin of basic survival the harder it is to be entrepreneurial because risk of failure increases.

7. CONCLUSION

It is these non-finance problems that are likely to mitigate against the success of microcredit interventions and, furthermore, it is suggested that those unidimensional approaches postulated as far-reaching panaceas such as the microfinance perspective (Otero and Rhyne, 1994) may well be as optimistically driven as the donor community’s fascination with rural credit and cooperative finance in the 1970s. Despite the incredible growth over the last decade in microenterprise credit programs throughout Africa, there appears to be little evidence to suggest significant and sustained positive impacts for the supposed beneficiaries (in terms of, for example, microentrepreneurs “graduating” to higher or more sophisticated levels of operations, increasing income flows or levels of employment). The most commonly touted indicator of the success of microenterprise credit programs is the loan repayment rate but this, of course, indicates only that borrowers are able and willing to repay, it says virtually nothing about impact on enterprise operations. Clearly, microenterprise credit cannot be assumed to improve microenterprise performance (however it may be measured) just because it is characterized by high repayment rates or levels of outreach. Furthermore, there remains a paucity of time series data indicating that consistently good repayment rates have been achieved from institutionalized microcredit programs in Africa or that such microcredit (as distinct from small business finance) is sustainable without donor support (see Hulme and Mosley, 1996 for an excellent comparative study on enterprise credit programs in a number of different locations). Any conclusions, therefore, must await further investigation.

Clearly, there is no single development model for the informal sector, as problems and possible solutions will vary depending on such factors as location, subsector, levels of economic development and so forth and this article has not digressed into possible alternatives but only seeks to highlight the danger of stepping into blueprint or vending machine approaches to development. It cannot be discounted that in some cases credit can stimulate sustained enterprise growth but given the type of barriers faced by microentrepreneurs and the prevalence of restrictive or impeding policies, its impact is likely to be very muted, at least in the short run. Therefore, it is suggested that the informal sector in Africa has survived and grown without interventions and that direct interventions of credit may not necessarily be a prerequisite for its further development, which is almost certainly the case if credit is not also combined with accessible savings facilities. Instead, attention is drawn to the availability and suitability of existing sources of finance, which may, paradoxically, be undermined by microfinance institutions (Rogaly, 1996), and the need to eliminate the discriminatory regulatory environment. Perhaps, above all, it is important to recognize that rather than being a panacea to the problems of development (low incomes, low employment levels etc.), the starting point for viewing the informal sector is as a symptom of unjust development, the result of the systematic denial of basic rights (to education, to health services, to partake in civic society etc.). One can argue that at best, microcredit may serve to ameliorate this injustice, at worst, it may serve to perpetuate it and detract from other necessary and perhaps more appropriate interventions. The danger is that the hard selling of microfinance as a new anti-poverty blueprint by microfinance evangelists will lose sight of this and overlook the fundamental limitations to the institutional sustainability of microfinance organisations: constraints to client impact.
NOTES

1. It is important to stress that this paper is concerned with credit for informal sector microenterprises and not with credit for small or medium enterprises which is considered a separate issue dependent on a different set of parameters. It is believed that studies which take the trouble to distinguish between micro, small and medium enterprises are likely to yield more insightful and accurate results than those that do not.

2. The research undertaken in Kenya (1992), Malawi (1993) and Ghana (1994) made use of a variety of research instruments including a detailed questionnaire which forms the basis of the data sets presented here. There were four sampling frames. The Kenya Kibera sample (160 entrepreneur interviews) comprised microenterprises located in the Kenya Kibera slum in Nairobi, the majority of whom were traders of one sort or another. The Kenya Regional sample (140) comprised a cross section of predominantly service and manufacturing microenterprises located in four regional towns: Kakamega, Muranga, Bungoma and Nakuru. The Ghana sample (150) was drawn from three towns: Accra, Kumasi and Cape Coast and was made up of a variety of service, manufacturing and trading activities. In Malawi, the sample (160) was almost exclusively made up of traders or food preparation activities which were located in the outskirts of Blantyre, in Mangochi or Chiradzulu (all in the Southern Region). The respondents were chosen at random from these areas and would be classified as operators of microenterprises by most quantitative or qualitative criteria. For example, using the employment criteria, over a third employed nobody on a full time, consistent basis and overall, the average number of employees per enterprise was roughly two, the majority of whom were apprentices or family employees.

3. These sources of enterprise funding were found to be ubiquitous throughout all sampling locations and are therefore not enumerated in Table 2. The giving and receiving of credit within networks of friends and relatives was a regular experience for nearly all respondents. There is great variety and flexibility to this type of finance and any terms or conditions are likely to be unstated (some degree of reciprocity or obligation being assumed, for example) and variable (repayment when conditions are favorable for the borrower or loans rolled over into gifts etc.).

4. Credit is debt. As has been pointed out elsewhere (von Pischke, 1991 and Shipton, 1992), the choice of usage is determined by whether one takes the lender’s or the borrower’s perspective. It is a curiosity (and not just of the English language) that one word implies a positive connotation whilst the other does not.

5. The question was: “Do you need credit now?...if yes, specify for what purpose”. It did not directly lead the respondent, so they were free to suggest they wanted the credit for any purpose (such as for school fees or household consumption) but presumably because of the nature of the questionnaire most respondents thought primarily about their business needs.

6. For further details see Buckley (1996a), and Buckley (1996b) in Hulme and Mosley, “Finance Against Poverty” (Vol.2).

7. Consider the numerous references in the literature on enterprise development that suggest the need for entrepreneurs to have access to credit. Why don’t they suggest that a major problem for such entrepreneurs is a lack of debt?

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