



## IN BRIEF...

# Microfinance – small loans pay

With the aid of microfinance it has been possible to give poor people access to financial services.

### What is microfinance?

Microfinance is the term used for various methods of giving poor people access to financial services. More than 20 years' experience of microfinance around the world shows that poor people with little education are reliable borrowers who, if they are given the opportunity, invest wisely and are prepared to save. Experience also shows that women are usually the best borrowers since they are better than men at repaying loans and in investing to meet the needs of their families and children.

### Background

There are several reasons why poor people are outside the formal financial sector. Traditional banks do not consider poor people as creditworthy since it is often the case that they do not own anything that can be provided as security for loans. Another reason is that the cost of administering small amounts is considered to be too high. A further reason is that bank offices are usually to be found in towns while poor people, and particu-

larly women, live in rural areas and have neither the time nor the money to travel to town.

The risk involved in lending money without security is met by giving customers good reasons to repay their loans. One reason of this type can be the possibility of obtaining further loans. Repayments are normally made in small and frequent intervals. This is a method that is suitable for the borrowers and their income flows and it gives the "micro-banks" an opportunity to create good contacts with their borrowers. The result is that repayment levels often exceed 95 per cent.

Since the micro-banks are located in the same places as their customers, their administrative expenses are lower and their routines can be simplified. Moreover, in the microfinance business the interest charged on loans is at market rates. However, poor customers are willing to accept these interest rates since the possibility of borrowing money for their micro-businesses and for the schooling of their children means a lot more to

them than the cost of the loan.

The interest rate makes it possible for the micro-banks to cover their expenses over time and to be completely independent of development cooperation funds.

### What is the situation today?

Microfinance is a worldwide movement and today there are many successful micro-banks. One of the most successful is Grameen bank, or "village bank" (Grameen means village) in Bangladesh, which has more than two million customers today, mostly women. Earlier Sida was one of the largest contributors to Grameen Bank but now it can manage without contributions and instead borrows directly on the private capital market. Examples of other successful micro-banks are BancoSol in Bolivia and Bank Rakyat-Unit Desa in Indonesia. These examples show that it is possible to be financially self-supporting by offering professional banking services to poor people.

Sida is supporting a number of different microfinance projects, for example in Bolivia, Zimbabwe, Tanzania, Nicaragua, Mozambique and Bangladesh. Support is provided at different levels. The projects at the institutional level can, for example, have the aim of improving the institutions' administrative capacity or increasing access to capital for on-lending. The projects at the national level can, for example, have the aim,

in cooperation with the central bank, of drawing up laws and rules to facilitate the work of the microfinance institutions and to guarantee the quality of their services.

### **The future**

Sida is participating internationally in the development of microfinance methods and techniques and is spreading this knowledge to organisations and banks working with microfinance in Sweden and developing countries. Sida's vision is that the

microfinance sector should be gradually integrated with the formal finance sector and be made subject to the supervision of financial supervisory agencies. This will make it possible for poor people to gain access to other banking services, for example savings and payment services, and for micro-banks to gain access to the private capital market.

Sida's support for microfinance is administered at the Department for Infrastructure and Economic Cooperation, INEC.

*Halving poverty by 2015 is one of the greatest challenges of our time, requiring cooperation and sustainability. The partner countries are responsible for their own development. Sida provides resources and develops knowledge and expertise, making the world a richer place.*



SWEDISH INTERNATIONAL  
DEVELOPMENT COOPERATION AGENCY

SE-105 25 Stockholm Sweden  
Phone: +46 (0)8 698 50 00  
Fax: +46 (0)8 698 56 15  
sida@sida.se, [www.sida.se](http://www.sida.se)