Microfinance as a suitable instrument of the European and Czech development co-operation

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Abstract: European countries use microfinance as an instrument of development cooperation in three separate forms, which differ in the financial flow. In the first type, the government transfers grant money to their non-government organizations (NGOs), which then distribute the funds directly to the local microfinance institutions (MFIs) (e.g., Finland). In the second form, the funds are sent through to the branch-offices of the NGOs located in the developed country to developing countries (e.g., Norway, Sweden). The third type allows for a direct relationship between a donor country development co-operation agency and a local microfinance institution in a developing country without intermediation of the developed country NGOs (e.g., Great Britain, Germany). The Czech Republic currently does not support microfinance by the direct/indirect transfer of funds, but it promotes the awareness of the Czech NGOs and the public of microfinance as a tool for the economic development.

Key words: microfinance, development cooperation, microfinance institutions, NGOs

The concept of microfinance gives the poorest people in developing countries the chance to access financial services outside the traditional banking system (Romero and Albino 2006)

The traditional financial institutions are not interested in financial transactions with poor people, because they are unable to offset the lack of information about a client through various types of security arrangements to ensure the proper loan repayment. If there is no collateral, guarantee or guarantor available, the bank does not provide the loan. This issue of asymmetric information was theoretically elaborated by Joseph Stiglitz – the Nobel Prize in Economics winner for 2001, along with George Akerlof and A. Michael Spence (Nobel Prize 2010). The concept of microfinance was popularized in 2006 by awarding the Nobel Peace Prize to Muhammad Yunus and the Grameen Bank (Bangladesh) highlighting their contribution to the economic and social development (Nobel Prize 2010). Microfinance overcame the information asymmetry problems through lending very small amounts of money, with a frequent collection and the use of cross-guarantees. The principle of a collective guarantee is the basis of the economic viability of microfinance, in contrast with the formal requirements of the conventional banks on the individual client (Nobel Prize 2010).

The research published by this article was elaborated on two levels. The first level describes the bilateral development co-operation based on the utilization of microfinance in various European countries and it formulates the generally used models. The second level presents the current support of the Czech government in the microfinance field.

MATERIAL AND METHODS

Secondary data were obtained by desk research in annual reports and other documents of the researched institutions. Primary data collection was done by the qualitative research methods, interviews and structured surveys with the microfinance representatives. The status of development co-operation utilizing microfinance in different European countries were consulted with Miroslav Zámečník, an economist and a member of the Board of the Microfinance Foundation (a Czech NGO) and a member of the Government National Economic Council, and confirmed at the web-pages of the organizations quoted. The ways how the Czech development co-operation could support microfinance was discussed in two interviews with representatives of the Ministry for Foreign Affairs of the Czech Republic and the Czech Development Agency.

From June to December 2010, a structured survey was carried out in the co-operation with the representatives of the Czech non-governmental organiza-
tions using microfinance for the aim of collecting the relevant data.

RESULTS AND DISCUSSION

European microfinance strategies

The concept of microfinance as a development assistance is pursued by many European countries. The European Commission supports microfinance in a number of ways, through the National Indicative Programmes, the non-governmental organizations budgetary line, etc. (Malhotra 2004). They carry out their microfinance activities in three different ways which differ in the level of the NGOs participation. As one of the results of the research, three different structures were formulated according to the financial flows.

The Finnish Abilis Foundation (FAF) is an example of the first structure which provides financial resources in the form of direct grants to its NGO partners in Africa and Asia. No Finnish NGO is therefore directly participating in the implementation and coordination of projects. One of the important aspects of this model is that the local NGO in a developing country is fully responsible for the project and financial management (Figure 1) (Annual report – FAF 2009).

Over the years, there were thousands of financed projects in more than 70 countries. Many of them achieved financial sustainability (e.g. were able to carry on the operations after the financial support from Abilis Foundation was discontinued). The Foundation has been established by the Unit for NGOs, Department for Development Policy, Ministry of Foreign Affairs of Finland.

The second structure is represented by large organizations such as the Swedish Diakonia (Annual report – Diakonia 2009), the Norwegian Stromme Foundation (Annual reports – Stromme Foundation 2008) and the British Microloan Foundation (Annual reports – British Department 2009). The implementation and coordination of projects in different countries is done in co-operation with local organizations, but through their own branches (Figure 2).

The Diakonia is the joint international development Christian aid organization. The work takes place in partnership with approximately 400 local organizations, religious communities and popular movement groups in around 30 countries in Asia, the Middle East, Africa and Latin America. Diakonia’s operations are financed on the basis of grants received from the Swedish International Development Cooperation Agency – SIDA, the EU and other sources, as well as donations from the congregations and individual donors.

The third possibility is the direct funding to foreign organizations by the government development agencies of various countries. The examples include the UK Department for International Development (DFID) supporting microfinance institutions in Pakistan, Nigeria and many other countries, and the German Deutsche Gesellschaft für Technische Zusammenarbeit (Annual reports 2009 – GTZ) as well (Figure 3).

Figure 1. Structure of financial flows of development assistance utilizing microfinance without the participation of developed NGOs.

Source: elaborated by Svitáková

Figure 2. Structure of financial flows of development co-operation utilizing microfinance carried out with the NGOs from developed countries co-operating through their branches in developing countries.

Source: elaborated by Svitáková
Figure 3. Structure of financial flows of development co-operation utilizing microfinance as a direct funding realized by a government agency in a developed country to organizations in developing countries.

Source: elaborated by Svitáková

Czech Republic and microfinance

There is a concept very similar to microfinance well known from the Czech history. The so-called “kampeličky”– credit cooperatives named after their main Czech promoter František Cyril Kampelík (1805–1870) – were self-help institutions established in the second half of the 19th century which greatly contributed to the accumulation of capital in the Czech countryside. The reason for carrying out this work is a proposal to include microfinance as a valuable instrument to enhance both the scope and effectiveness of the Czech official development assistance.

The Czech Republic development assistance (a relatively new, the post 1989 phenomenon) would thus follow the path that has proved quite popular in a number of other more traditional and experienced donor countries within the EU. As a main reason for including microfinance as a form of development assistance, there was recognized the lasting impact of this type of intervention through sustainable development of small local enterprises or microenterprises. The access to working capital facilities on a continuous basis is a prerequisite for the healthy development of any business, because a single injection even in the form of a grant does not ensure the sustainability of a small business and it can create the culture of dependence on the development assistance, which is completely contrary to the business mentality. Support for productive small enterprises is a virtue in itself (“learning to fish”), but it is almost a precondition for the long-term economic sustainability of a business venture after the departure of the Czech partner who provided the initial support and capital. Microfinance, as a repaid financial assistance, implies a larger and direct participation and involvement of communities in development projects (groups of microentrepreneurs, usually women, are jointly liable through cross guarantees) and so increases not only business viability but also empowerment of women in rural underdeveloped areas.

The possibilities of using microfinance by Czech NGOs pursuing their development projects are still quite limited. In many examples, microfinance plays only a secondary role in the overall design of development projects.

In May 2010, the government presented the official development assistance concept of the Czech Republic for the 2010–2017 period which directly refers to microfinance as one of the possible instruments of the international development co-operation. The Czech government does not provide funds to the NGOs or MFIs (microfinance institutions) directly as some of the European governments do. However, the Czech Ministry for Foreign Affairs and the Czech Development Agency have provided support through two grants extended to the Microfinance Foundation (NFMF), thus facilitating the launch of the web-based development portal to promote microfinance among the Czech NGOs in 2011. The first grant is focused on dissemination of knowledge about microfinance among high-school teachers and students. The second grant is dedicated to the dissemination of knowledge among the Czech NGOs, the design and launch of the web-based portal and the incorporation of the microfinance – based components into the project portfolio of Czech NGOs.

The main objective of these projects is to strengthen the awareness of the term “microfinance” and its potential developmental impacts on a sustainable basis among the Czech development assistance community and the public at large and to create an information base upon which microfinance could become an integral part of the Czech development cooperation. The preparation and start-up of a development portal is an important part of one of the NFMF projects mentioned. The main function of the portal is to support the integration of microfinance into the project portfolio of Czech NGOs.

The support provided by the development web-portal to Czech NGOs is realized in three different ways depending on the situation of the individual NGO.

(1) The first type is an NGO with its own back-office and administrators for all microfinance activities. Usually such NGO has its own pool of small entrepreneurs or partners among the local MFIs. In this case, the main activity of the NFMF is the promotion of microfinance activities on the portal and during the events to the investors and public.

(2) The second type is an NGO with a strong local MFI partner in a developing country, but the
NGO itself does not have personal and technical capacities to realize all the administrative or the back-office work related to the processing of loans extended by the Czech to the MFI. In this case, the NFMF provides the back-office works for all investments. For example, the NFMF has a collection bank account and sends the money to the partner MFIs account. The NFMF also controls the schedules of payments for all investments, develops contracts and communicates with the investors and the MFIs representatives, provides marketing for the NGO. The main function of the NGO is to control the work of the MFI who receives investments in the field to ensure that all the contract covenants are observed.

(3) The third type is an NGO which does not cooperate with any local MFI, but which has its own pool of small local entrepreneurs who are interested in receiving loans for the expansion of their business. This type of NGO does not possess the technical capacity for the realization of microfinance. In this case, the NFMF provides to the NGO the back-office works for all investments, i.e. the NFMF has its own collection bank account and sends money to the NGO account, controls the schedules of the payments for all investments, communicates with the investors, provides marketing of the NGO and its individual entrepreneurs to the investors and the public.

The promotion and propagation of the NGOs activities and the MFI at one web portal is a very popular type of support in the developed world. An example is the “KIVA portal” (kiva.org) which was elected as the most useful web-based portal for year 2009. The Microfinance Foundation development portal will provide a set of comprehensive information about the current state of microfinance in the Czech Republic, the actual professional activities of the Czech experts in this area and about the specific microfinance projects.

CONCLUSIONS

Although the principles of microfinance and its use as a tool in the fight against the poverty are a relatively new phenomenon, it has been adopted quite rapidly as a part of the development assistance by some Western European governments. The approach adopted by the individual governments considerably varies. No direct financial support by the Czech government to microfinance or specific micro-project currently exists. Czech government supports the activities to strengthen the awareness of the Czech public and donor community about microfinance and also considers microfinance as a new option for the future development co-operation, as evidenced by the “Concept of international development cooperation of the Czech Republic for the 2010-2017 period” published in May 2010. Despite some recent controversies, most of economists believe that non-profit institutions that transform themselves into regulated microfinance institutions will be central players in the effort to scale up microfinance and to address poverty at the global level. (Ledgerwood 2006) Microfinance is one of attractive, useful, and promising tools for a more effective development co-operation both at the European and the Czech level.

REFERENCES


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