

Leah Oldham- Senior Thesis/Baker Scholars Project- “The Role of Nonprofit Microfinance Institutions in Alleviating Poverty: From Theory to Practice”

When deciding what I would like to do for my Senior Thesis and Baker Scholars project, the only thing I was sure of was that I wanted to do something that had an action component to the project. I knew that I wanted to have a project that would allow me to involve the student body of the university. I knew that I wanted to raise awareness about an issue that could invite students to have a role in making a positive difference. I started narrowing down ideas for my project during the fall semester of my senior year.

I was fortunate to be enrolled in a 481 special topics course that allowed me to explore global economics and engage in the study of the markets, power, and politics in world trade. Dr. Bill Park mentored me and introduced me to Pietra Rivoli’s book *The Travels of a T-shirt in the Global Economy*. Rivoli’s book served as the main resource of my study. Prior to reading the book, I had not had the opportunity to engage in a focused study of global economics. The topics covered in my reading detailed how the economic system in the U.S. is structured and how economic actions by the U.S. government greatly affect other countries. Rivoli provides a journey of discovery that shows both the positive and negative effects of globalization and free trade for many countries. From the greater understanding I developed in the 481 course, I became curious about the economic effects of trade agreements between the U.S. and many nations and the particular economic and financial struggles that many people face in developing countries. This curiosity led me to explore an organization that I had learned about in a global studies course I had taken my junior year. From what I could remember, the Kiva organization allowed individuals from around the world to lend any amount of money over \$25 to individuals that were in great need of loans. After thinking about the unique opportunity the Kiva provides, I

knew that I had decided what my project would involve: nonprofit microfinance institutions and how an institution can help alleviate people living in poverty.

I knew I would have to encompass my own personal experience seeing the need for such institutions. I kept thinking about my experiences visiting Vietnam and Cambodia while studying abroad during May 2011. I saw people working tirelessly each day to make a living and earn just enough to survive. Cambodia was much less developed than Vietnam, and I saw a great need for people to be given an opportunity to be entrepreneurs in their communities. At this point, I knew that I had found my action component of the project. My project came together when I decided on both the theory I wanted to explore and the action that I felt must be taken. With guidance from Dr. Park, I decided the title for my project: “The Role of Nonprofit MicroFinance Institutions in Alleviating Poverty: From Theory to Practice”.

For the theory portion of my project, I researched the role of microfinance institutions to gain a greater understanding of microfinance as a concept and the different types of microfinance institutions that exist. I learned about the rationale, scale and scope, evaluation, and success of the microfinance lending process. In addition, I learned about various issues associated with the process. For the practice portion of my project, I introduced the microfinance lending process to the student body at the University of Tennessee. My hope was to implement a new initiative in an organization I’m involved with on UT’s campus. I am currently a member of the T.A.S.C. Force which is a new organization on UT’s campus this year. As a part of the service component of the organization, I have introduced Kiva, a nonprofit microfinance institution. I wanted to share how the Kiva program seeks to help people around the world create opportunity for themselves and others. The organization allows volunteers as well as microfinance institutions (field partners) to give loans to people and families in countries that need financial support. The

system works by the donor choosing a borrower, making a loan, getting repaid, and then repeating the process if desired. The implementation portion of my project was put into practice when I planned a fundraising event with T.A.S.C. Force to raise money to send through the Kiva organization to the field partner so a loan can be given to an individual in need. My goal with this project is to become more educated about the current state of microfinance institutions in countries and to raise awareness about KIVA and the role of nonprofit microfinance in alleviating poverty. I want to increase awareness on UT's campus and beyond about the need and benefits of microfinance lending organizations.

To better understand my project, it's important to know how the Kiva organization works and how the T.A.S.C Force organization on campus will be involved in lending to Kiva. First, I will provide more information about Kiva and what distinguishes Kiva from other microfinance lending organizations. Matt Flannery, Kiva CEO and Co-Founder, best describes the role and outlook of Kiva when he explains, "Kiva doesn't believe that lending is a silver-bullet, poverty alleviating mechanism." He adds, "We do believe, though, that lending is one meaningful tool in a larger set of tools that the development community can use to alleviate poverty" (Flannery). Flannery sees Kiva as a public property "owned" by three main constituents—the entrepreneurs, the lenders and the MFI partners, all of whom are served by Kiva. There has been criticism that one constituent has to benefit at the expense of the others, but in reality each constituent must rely on the other (Flannery). The relationship between the three constituents is vitally important for this reason. An understanding of the challenges and needs of each constituent is imperative in order for each constituent to be the most successful in loaning, borrowing, or repaying.

Specifically in the cases of most lenders that use Kiva, the majority of people have little knowledge of microfinance before they decide to contribute. Kiva's website provides the most

basic information about how Kiva works in an effort to be clear to lenders. Kiva's loans are disbursed before they are funded on the Kiva site which might surprise some people. However, the pre-disbursal does not make the loan any less effective; it is just simply a part of the process. When Kiva started in 2005, there was no other source of funding for loans so it was necessary to wait for the Kiva funds before handing out loans (Flannery). As Kiva grew though, MFI's (microfinance institutions) started to expect and depend on the loans being funded so the MFI's disbursed the loans in advance to give the best service possible to clients. The pre-disbursal method has been the norm since that time.

What distinguishes Kiva from other NGO's and microfinance institutions is the ease of access and ability to contribute. Kiva provides pictures and stories from each of the borrowers and keeps track of the financial data so people all around the world have the opportunity to invest money in a cause that can continuously have positive results. Matt Flannery's personal story shows the positive impact from the lending process. Flannery shared in an online post the following: "Last year, I spent a few weeks in Cambodia and witnessed dozens of women who were given a savings account for the first time, thanks to our MFI partners there. Rather than save under the mattress, they were creating accounts with an MFI. In a dangerous place like Cambodia, this is an incredible service" (Flannery).

Kiva has made the practice component of my project possible because it has given me and T.A.S.C. Force the opportunity to participate in the lending process. By working with Kiva, the mission to connect people through lending to alleviate poverty has been achieved. The mission of T.A.S.C. Force has also been recognized through this project. The mission of the T.A.S.C. Force is to raise awareness about human and social issues in today's world in hopes of spreading selfless acts for those in desperate need. By educating individuals, T.A.S.C. Force

members strive to transcend physical acts of altruistic behavior and set an positive example for others. All members of T.A.S.C. Force are actively involved in philanthropic tasks, and my project is one more task that can provide service to others. I introduced my project to the members of T.A.S.C. Force. They chose to support my project, and we raised \$25 from holding a bake sale on campus. The purpose of holding a small fundraiser was to show that every dollar counts to help someone in need. Just the \$25 that we raised was able to help someone in need in Cambodia, and the Morng family was who we ended up helping. The mother, Heng Morng, had applied for a loan of \$700 to buy seeds and pesticide to maintain her farm. She is 47 years old and lives in a village near the Mekong River about 20 kilometers from Phnom Penh City with her husband and six children. Heng's husband is a construction worker, and Heng is a weaver. However, when farming season arrives Heng and her husband are rice, sesame, and sugarcane farmers. The loan was disbursed to the family on March 14, 2012, and there is an expected 22 month repayment schedule. My hope is that we created greater awareness of the positive impact people can make just by investing a small amount of money.

The whole concept of microfinance is based on investing and loaning a small amount of money. Microfinance is the term used to describe "small-scale financial services-primarily credit and savings- provided to people who farm or fish or herd; who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages or commissions; who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban" (Robinson 9). Microfinance has been more of a recent development in the world. A microfinance revolution developed in the 1980's and came of age in the 1990's as a means to provide borrowers with more diverse economic

opportunity and as a result, greater income and self-confidence (Robinson introduction xxx). Microfinance lending has ultimately been a way to provide individuals with self-sustaining opportunity. Marguerite S. Robinson explains in *The Microfinance Revolution* that “overall, microfinance services can help low-income people reduce risk, improve management, raise productivity, obtain higher returns on investments, increase their incomes, and improve the quality of their lives and those of their dependents” (Robinson 9). Bangladesh’s Grameen Bank was the first main institution to raise awareness that the poor population can establish credit when given the opportunity under certain circumstances.

There is a great rationale and the need for microfinance institutions. The rationale for microfinance is to provide opportunity for those that have been neglected by the formal banking sector. The need for microfinance is related to the magnitude of global poverty. Eighty percent of the world’s 4.5 billion people living in low and lower middle income economies don’t have access to formal sector services (Robinson 10). It’s sobering to know that more than 3 billion of the world’s people now live on less than \$2 per day (“Global Poverty and Microfinance”). It’s estimated that the number of poor entrepreneurs who use microfinance today range from 30 million to 50 million worldwide and some believe it might be as high as 100 million (“Global Poverty and Microfinance”). Ninety percent of the financially underserved live in Asia, Africa, the Middle East, and Latin America, and most people in demand for microfinance are involved in the unregulated, informal sector of the economy (Robinson 11). Global data indicates that countries can substantially improve levels of financial inclusion by creating effective policy and regulatory environments.

If individuals had local access to appropriate institutional savings and credit services, economic productivity could be greatly increased (Robinson 10). Lucia Wegner discusses the

direction microfinance should have moving forward in "Microfinance: How Bankers Could Buy Back Their Souls." Wegner explains that "in order for microfinance institutions to reach more poor people they should become an integral part of the financial sector, and develop as sound domestic intermediaries [and] should go commercial, broadening their client basis and scaling up their loans to small enterprises." Marguerite S. Robinson echoes Wegner's sentiment because Robinson argues that the demand for microfinance "cannot be met by government or donor funded programs or institutions...this demand can be met on a global scale only through the provision of financial services by self-sufficient institutions" (Robinson 11). There is no doubt that nonprofit lenders in particular have an integral role in microfinance by experimenting with new methods, mitigating risk, and overall providing services that the private sector does not offer ("Global Poverty and Microfinance"). However, mounting evidence shows that the private sector can establish a greater role in microfinance lending by capitalizing investment funds and establishing a beneficial infrastructure. The opportunity for the private sector could transform nonprofit microfinance institutions into regulated financial institutions that can adopt the best practices to move towards greater success. Ultimately, in an effort to alleviate poverty, collaboration between both private and public institutions will be necessary ("Global Poverty and Microfinance").

The measure of success for a MFI is to both serve the poor and be financially sustainable. There have been many lessons and aspects to evaluate over the years to reach greater success. The MFI experience in the 1970's taught a valuable lesson about self-help from financial services. The early generation learned how to approach microfinance and prevent loans from being misconstrued as gifts (Terberger 189). There was a mix of public and private sector involvement in the 1980's and 1990's. Indonesia has been a positive example of success from the

microfinance revolution. Indonesia developed a loan methodology and savings services on a national scale as well as staff training and incentives that encourage knowledge of the microfinance market. Those two aspects combined with a high loan repayment rate showed measurable success. However as a whole, microfinance in the 1990's was mainly a debate between the financial systems approach and the poverty lending approach (Robinson 22).

The debate still continues today, but what we do know is how microfinance institutions have given great hope and opportunity to many people around the world. Michael Chu, a former Wall Street financial specialist in the use of capital markets for company acquisitions, became a leader of the financial systems approach while president of ACCION International (financial systems approach institution): "this is nothing short of changing *the very nature of banking* from servicing the top 23 or 30 percent (at the most) of the population of the developing world to meeting the demand of the rest. It is the reclaiming of finance for society at large- the true democratization of capital (Robinson 25).

My goal of this project is to educate people on the reality of living conditions for many people around the world. I hope that this project will be eye opening and informative. I want to support hardworking individuals here in the U.S. and around the world. Personally, I hope to gain greater understanding of the economic impacts of microfinance and to find ways to financially and efficiently fund individuals that need it the most to become self-sustainable.

"I am only one, but I am one. I cannot do everything, but I can do something. And I will not let what I cannot do interfere with what I can do." ~Edward Everett Hale

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