

**UNDP MICROFINANCE  
ASSESSMENT REPORT  
FOR  
Pacific Islands**

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## A. Regional Situation

The three sub-regions within the Pacific: Melanesia, Micronesia and Polynesia are characterised by different cultures, environmental conditions and histories.

All of the Pacific Island Countries (PICs) have experienced significant fluctuations in economic growth, reflecting the small size of their economies, their reliance on agriculture and, in the case of the larger countries, one or two key industries. Cyclones and other natural disasters are frequent as most countries are situated wholly or partially in the cyclone belt. Overall, their macro-economic performance since around 1980 has generally been poor, with little or no growth in real per capita incomes in most countries. The World Bank has described this as the “Pacific paradox”, noting that it has occurred despite a favourable natural and human resource endowment and high levels of aid. In recent years there has been a deterioration in macro-economic management in a number of countries: Papua New Guinea, Cook Islands, Tonga, Vanuatu and the Solomon Islands.

The lack of growth in the PICs and the ineffectiveness of government policies in ensuring sustainable growth, have focused attention on the need for accelerated private sector development. This increasingly includes recognition of the role of the informal sector. In 1991, there were only around 370,000 formal sector jobs throughout the region, compared with an economically active population of 1.8 million. Most of the remaining labour force was engaged primarily in subsistence agriculture, with a small number working in the urban informal sector. In virtually all the PICs, the labour force is growing much more rapidly than the number of jobs available in the formal sector. Donor assistance to the sector has changed markedly over the last decade from Government budget support and untied grants, to tied technical assistance. There is an increasing, albeit reluctant, realisation in both Government and civil sectors of the need for self help measures and longer term planning horizons. The Pacific comprises fifteen separately governed countries. Papua New Guinea, the largest of the Pacific countries has a population of 3.75m.

Much of the country is unconnected by ground transport due to the extreme ruggedness of the terrain and the widely dispersed location of villages. Solomon Islands and Vanuatu have population densities of about 13 people per square kilometre. Pitcairn Island (a separate country and British protectorate) has a total population of 47 people. Inter and intra country transportation poses the greatest single difficulty to economic development and market access. Kiribati highlights this problem, with 28 main islands and many smaller islands spread over 3,550,000 square kilometres and with a total population of 78,000. Throughout the Pacific, most of the land mass (in excess of 75%) is given over to subsistence or semi-subsistence agriculture. The high cost and infrequency of transportation, the lack of opportunities for market diversification, the ruggedness of the terrain (as in Melanesia) comprise the context within which microcredit must be provided, particularly in rural areas. Annex IV provides more detail on country-specific contexts.

## B. Finance and Banking

As in many developing countries, the financial structure in almost all Pacific Island Countries comprises both formal and informal financial institutions. The formal financial institutions are mainly based in urban areas and include central banks, commercial banks, development banks, offshore banks, housing finance and other finance companies, national provident funds and insurance companies. The informal financial institutions such as credit/savings cooperatives and credit unions usually provide credit and savings services to people in rural areas and outer islands.

In the bigger Pacific countries such as Papua New Guinea, Fiji, Vanuatu, Solomon Islands, Tonga and Kiribati, financial systems are well developed compared to small nations like Niue, Tokelau, Marshall Islands, Palau, Federated States of Micronesia and Cook Islands. These bigger countries above have each established a central banking institution (central / reserve bank) which is primarily responsible for managing the country's international reserves, administering the currency and foreign exchange, and supervising the banking system. Development banks as well as commercial banks exist in fourteen countries, excluding Tokelau. Most countries in the Pacific have more than one commercial bank with the highest number (six) in Palau and Papua New Guinea.

Countries in Micronesia like Palau and Marshall Islands also have access to banking institutions in Guam, Hawaii and mainland U.S. By the and large, commercial banks are not in a position to effectively reach out to rural areas and few commercial banks are located outside the main centre, except in Papua New Guinea and Fiji, hence, most PICs rely on credit/ savings cooperatives and credit unions, many of which have long been providing savings and credit facilities to people in rural areas. Some PICs also utilise their post offices and postal agents to provide savings facilities to rural people. National provident Funds have been established in countries like Fiji, Kiribati, Palau, Solomon Islands, Vanuatu and Western Samoa. Offshore banking services, including Trust Fund Management, are also being provided by some countries (Vanuatu, Western Samoa, Cook Islands, Niue and Palau).

The table below shows formal banking facilities by country. In some cases the actual number of establishments in a given category is unclear, particularly with organisations located in the outer islands. Where the number of establishments is large relative to the rest of the region, this has been shown.

### C. UNDP Suva Country Office

The United Nations Development Programme (UNDP) is committed to achieving sustainable human development (SHD). To advance SHD, UNDP's Executive Board has determined that UNDP's Sixth Development Cycle should be focused on: (i.) eradicating poverty; (ii.) creating jobs and sustainable livelihoods; (iii.) advancing women; (iv.) protecting and regenerating the environment; and (v.) promoting sound governance.

Based on its global programme framework, past programme experiences, and the views expressed collectively and individually by Pacific Island Governments, the UNDP has proposed for Governments' approval the "Employment and Sustainable Livelihoods" theme for its Sixth Cycle Sub-Regional Programme. Supporting this theme will be four programmes: (1) Development Management; (2) Private Sector and Sustainable Livelihoods; (3) Environment and Natural Resources; and (4) Human Resource. Each of these four programmes will pursue common objectives of private (formal) sector job creation, enhanced non-formal livelihood options, enhanced productivity and remuneration, and reduced unemployment. The theme of the sub-regional programme for the Pacific and its four components was endorsed by the Governments of the Pacific Island countries on 25 October 1996 in Saipan.

#### Programme Overview

As one of the four programmes under the Sub-Regional Programme, the private sector and sustainable livelihoods programme (PSSLP), has as its goal the creation and/or promotion of employment and livelihood opportunities, and will be linked closely to the other three programme components of the sub-regional programme. It also takes the two-pronged approach to addressing the priorities of the Governments:

(i.) focus on Trade and Investment; and (ii.) support for Small Entrepreneurs. With regard to the first prong or the Trade and Investment Component, the Governments, while aware of the poor track record in trade and investment, continue to regard outward-looking strategies as the best option for generating employment and other income opportunities in the formal wage sector. Thus their continuing push for greater and more beneficial links with the high economic growth centers of the global economy such as the APEC region.

At the same time, the region is having to deal with the fact that the formal wage sector may never be in a position to accommodate more than 30 percent of the labour force unless there are dramatic changes in the patterns of investment flows and population growth. For the majority (approximately 80 per cent) of the labour force, the only realistic source of livelihood including informal employment is the non formal sector including in urban areas where an increasing number of households are now making a living. In order to support the expansion of employment and sustainable livelihoods at this level, the Governments have indicated the desire to direct resources at supporting the small entrepreneurs through the Small Entrepreneur Support Component of the PSSLP.

## Trade and Investment Component

The trade and investment performance of the PICs over the last two decades has not been encouraging. Papua New Guinea and Nauru are the only Pacific Island economies which have surplus balance of trade and goods. The Solomon Islands and Fiji have been improving steadily although the former case, involving significant log exports, may not be sustainable. Nauru's situation is also deteriorating as exports of phosphate are declining. The remainder of Pacific Island economies have relatively large deficit balances of trade in goods, and in many countries, balance of trade figures are progressively worsening.

The underlying problems in the Trade and Investment area are commonly known. They include restrictive policies and administrative procedures; lack of access to secure land and other resources; high labour costs due to inflation and inappropriate labour policies; lack of access to finance and technology; and low skills levels.<sup>1</sup>

The goal of the Trade and Investment Component is to increase employment and livelihood opportunities through increased trade and foreign investment. Given the need to focus activities and the growing importance of APEC to the future of the Pacific Island region, the Investment and Trade component includes APEC-related objectives particularly in relation to trade/marketing and investment/technology flows.

The objectives include:

Objective 1 To create an enabling legislative and policy environment for trade and investment by:

Assisting in the review and streamlining of license approval procedures;

Assisting in the development of appropriate macro-economic policies for improving conditions for FDI and export production (financing, tax incentives, labour skills and costs, infrastructure, technology); and

Supporting initiatives aimed at forging strategic alliance between the private sector and the governments of PICs to establish proactive consultative process for formulation of policies and strategies for development.

Objective 2 Exploit the opportunities emerging from APEC for trade promotion, economic and technical cooperation and maximise the benefits of economic integration by:

Improving access to and understanding of timely market intelligence in APEC region (including quarantine, health and safety requirements);

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<sup>1</sup> For a comprehensive discussion by country representatives of constraints and priorities in trade and investment, see "Report of the Logical Framework Project Planning Workshop on Development of Trade in the Pacific Region", Forum Secretariat, 1995.

Supporting the identification and development of new markets in APEC;

Supporting trade and investment promotion and the advertisement of products and services in APEC;

Identifying and promoting new ideas for export products to the APEC region;

Supporting effort aimed at lowering export production costs;

Reviewing the feasibility of establishing an APEC Center in PNG.

The Trade and Investment Component will have two sub-components, covering the following: 1) APEC Centre; and 2) Trade and Investment Policies and Practices.

#### Small Entrepreneurs Support Component

It is estimated that the people of working age in the Pacific Islands region are four to nine times the number of formal sector jobs and the gap is widening. This means that in some Melanesian countries, for example, the non formal subsistence sub-sector will have to somehow accommodate up to 85 per cent of the labour force which the formal job market can not absorb.

At the same time, the ability of the non formal subsistence sector to provide gainful employment and livelihoods is being seriously eroded due to cumulative impact of modernisation and neglect by governments and their development partners. There is also a serious contraction in migration opportunities (“safety valve”) which some of the Polynesian and Micronesian countries had been relying on to ease the pressure on local resources.

Given the significance of the small non formal subsistence sector as a source of employment and livelihoods, it is surprising that it has received very little support from governments and their development partners.

Constraints to the development of this sector include the lack of an enabling policy environment; a weak or non-existent entrepreneurial culture; limited access to advice and practical information including business or employment opportunities; limited access to finance and technology/innovations; poor and scarce land resources; limited access to markets and market information; and low and inappropriate skills levels.

The goal of the Small Entrepreneurs Support Component is to increase income and livelihood opportunities in the small non formal sector by developing an enabling environment or sustainable livelihoods at the community level, and providing support to the small entrepreneurs. The following vulnerable groups are targeted, namely: the rural/urban poor and women, youth, and redundant civil servants.

The objectives include:

Objective 1 The creation of an enabling legislative and policy environment for small entrepreneurs by:

Assisting in the reviewing and streamlining of procedures to minimise time and costs for the approval, starting-up and operating of business;

Seeking the removal of unnecessary regulations and administrative procedures constraining vendors in operating business in the non-formal sector; and

Supporting (indirectly) through other UNDP Programmes and Donors the initiatives related to basic education with emphasis on life skills; and vocational training with emphasis on employable skills.

Objective 2 Facilitate access to markets by:

Improving the distribution of market information including on the local/national scene through new and existing networks; and

Supporting efforts to improve access of rural producers to markets.

Objective 3 Promote business and entrepreneurial skills and opportunities by:

Establishing and supporting “Small Business Centers” or “Small Enterprises Support Agencies” focusing on providing business skills training and practical advice on business opportunities, technology and financing. Target groups will include the redundant public servants who need re-skilling and the disadvantaged groups including the rural poor, youth and women; and

Supporting (indirectly) through other UNDP Programmes and Donors in related activities including vocational training with emphasis on agro-fishery processing, eco-tourism and small manufacturing.

Objective 4 Improve access to finance, land and lagoon resources by:

Promoting and establishing special integrated credit and group guarantee schemes to meet the special needs of the micro-enterprises; and

Supporting (indirectly) through other UNDP Programmes and Donors, the related tasks including the audit of land and lagoon/ocean resources and the streamlining of procedures; and applying techniques for settlement of, or avoiding, disputes on ownership of resources. The latter could be incorporated into business training materials (refer 3.1).

Objective 5 Strengthening subsistence and rural-based production systems and social organisations by:

Careful adaptation and application of appropriate technology, support of action research to improve the livelihood-providing capacity of the subsistence sector, improving the targeting and

delivery of rural extension services and strengthening of community organisations and local planning.

The Small Enterprise Development Programme will strengthen national capacities to support indigenous small entrepreneurs by: assisting in identifying gaps in policies, incentives and access to finance; and, recommending measures to create a more enabling environment for indigenous enterprises. It will also work with small enterprises to develop management skills by providing business and technical training and follow-up advisory support.

The Social Mobilisation for Sustainable Livelihoods for Poor and Disadvantaged Groups will work at community level to: widen the opportunities and ease of entry of the poor into the informal income generating sector; strengthen support mechanisms for income generation for this target group; and, improve social mobilisation empowerment through participatory based assistance.

Timely, accessible access to credit is fundamental to the success of both the above sub-programmes. At present the lack of access to credit will limit development of income generating activities even where appropriate income opportunities, training and support are available. The very high transaction cost of microcredit provision in the Pacific, due to low density communities and small populations, has discouraged the formal finance sector from providing this service.

#### D. Donor Interventions in Microfinance Sector

According to the Pacific Island Yearbook (17<sup>th</sup> Edition), the South Pacific is one of the most heavily aid assisted regions in the world, with an estimated A\$1,637 million (1990), or A\$256 per capita, flowing into the region by way of official development assistance, both bilateral and multilateral. This aid plays a crucial role in meeting government development programmes and, in many cases, budgetary requirements.

Over the years, bilateral donors and multilateral donors, including regional development organisations and non-government organisations (NGOs) have been providing financial assistance to microfinance projects targeting disadvantaged groups in the Pacific. Both Seed funds and technical assistance have been provided, particularly through the New Zealand Government (NZODA) which is the major bilateral donor in this sector. Other bilateral donors include Australia (AusAID), the United States (USAID), European Union and Canada. Multilateral donors to the microfinance sector include the UNDP, the ILO and IFAD. UNDP mainly provides technical assistance and rarely provides financial assistance, whereas IFAD provides significant financial assistance. Regional development organisations like the South Pacific Commission (SPC) and the Forum Secretariat are also significant contributors to the sector, particularly through the funding and co-ordination of regional activities.

Most donors target exclusively disadvantaged groups, particularly women, and in some cases youth and Outer Island (rural) groups. Projects funded by NZODA are usually administered by development banks or by the Ministry/ Department of Womens Affairs. New Zealand has a very proactive policy toward womens' development, particularly income generation. IFAD funds are also administered by formal lending institutions such as development banks in Tonga and Western Samoa and by the Central Bank in Solomon Islands. By and large, financial assistance does not exceed US\$100,000 except for the NZODA funded womens' credit scheme administered by Fiji Development Bank amounting to approx. US\$474,054 and the AusAID funded project administered by the Central Bank of Solomon Islands for a total of SI\$1.5 million (US\$420,000). In some cases, projects are funded by several donor agencies both local and foreign. Countries in Melanesia and Polynesia receive substantial aid from donors compared to countries in Micronesia such as Palau, FSM and Marshall Islands.

The table overleaf identifies the biggest microcredit schemes in the Pacific. The Terms of Reference for this feasibility study and programme document preparation did not allow for in-country field reviews. The information in the table is therefore based on the combined knowledge of the Consultants and the UNDP Suva Country Office, together with a document review. There are inevitably gaps in the table where information was not available. Interest rates are generally simple, per annum, although in some cases the basis for calculation was not available.

#### Local NGOs' Intervention in Microfinance Section

In the Pacific as in many parts of the developing world, NGOs have been increasingly recognised as effective in delivering community-based development programmes. Most donor agencies are providing some financial assistance to NGOs for the implementation of development programmes including microfinance schemes and community based support for income generating projects.

International NGOs involved in microfinance programmes in the Pacific Nations include the Save the Children Foundation for the small revolving fund in Solomon Islands, the Foundation for Peoples of the South Pacific (FSP) for the AMAK Revolving Fund in Kiribati, and Peace Corps providing technical assistance to WOSED in Fiji, Small Business Finance Scheme in Solomon Islands and Borrower Training for the Tonga Development Bank.

Some local NGOs, particularly the credit unions, are actively providing micro-credit services in almost all nations in the Pacific. Some NGOs are specifically established for the purpose of implementing a microfinance project, as in the case of the Trust for the Liklik Dinau Project in PNG. Other local NGOs implement programmes providing small loans to women such as the Business Foundation in Western Samoa.

It is recognised, however, that these NGOs, especially local NGOs, are dependent on external funding and technical assistance. Many are organisationally weak and many are poorly equipped to execute microfinance. Most, however, are enthusiastic and have a role in community support.

## E. Case Studies on Microcredit Schemes

Evaluation of previously established microcredit schemes is sporadic. Some schemes appear to have been subject to more evaluation reports than access to technical assistance; other schemes are remembered by name only, with establishment details and factors contributing to failure long forgotten.

<p>Successful Microcredit Projects</p> <p>Case Study 1 Papua New Zealand - Liklik Dinau Abirote Trust</p> <p>Case Study 2 Cook Islands - Nukuroa Revolving Fund, Mitiaro Island</p> <p>Case Study 3 Fiji - The Women's Social and Economic Development Programme</p>
<p>Unsuccessful Microcredit Projects</p> <p>Case Study 4 Papua New Guinea - Woman's Credit Scheme, Simbu Province</p> <p>Case Study 5 Tonga - National Youth Credit Scheme</p>

### Case Study 1: Liklik Dinau Abirote Trust (Successful Microfinance Scheme)

Location: PNG, with pilot project operating in villages close to Goroka town

Target group: Exclusively for disadvantaged women

Life Span of the Project: 5 years (1994 to 1999)

Access to Funding: Grants for seed capital or operational expenses from Department of Village Services and Provincial Government for K100,000 (US\$77,900) and from the Foundation for Law, Order and Justice for K29,461 (US\$22,900); technical assistance from UNDP (including the salary of the technical advisor) and K18,200 (US\$14,180) for purchase of a vehicle; additional seed capital pledged by AusAID amounting to K195,000 (US\$151,900) with the first tranche of K100,000 (US\$77,900) received in May 1996.

**Fund Management:** Fund administered by Trust (an NGO specifically established to implement the Project) and is governed by a seven member Board of Trustees, chaired by a representative from the PNG Banking Corporation, and with representatives from UNDP, the Department of the Prime Minister, the Department of Village Services and Provincial Affairs, the Department of Home Affairs, the Foundation for Law, Order and Justice, and the National Council of Women. The manager of the Trust is a United Nations Volunteer (UNV) technical advisor. Loans are disbursed to groups adopting the 2-2-1 approach of the Grameen Bank.

#### Technical Assistance

**Provision:** TA provided by the UNV technical advisor, field staff consisting of nine men and seven women, and livelihood training by Department of Primary Industry.

#### Critical Success

**Factors:** Exclusive targeting of borrowers through means testing, rigid training before loan releases, peer pressure and group accountability, strict credit discipline and close monitoring.

**Summary:** Liklik Dinau Abitore Trust

The Liklik Dinau Abitore Trust is a microfinance programme initiated by the UNDP. It was established in September 1995 and was pilot tested in villages close to Goroka town. It is envisioned to be self-sustaining after five years. The maximum loan is K300 payable in twelve months at 15% interest per annum, equating to an effective interest of around 29% per annum. Though the loans are given to individuals, the groups are collectively responsible for the repayment of the loan. Peer pressure coupled with weekly payments during weekly meetings ensures high repayment.

As of June 1996, there were 334 borrowers with a cumulative repayment rate of 91.4%. The Liklik Dinau Abitore Trust has achieved much in the two years that the programme has been operating. It has shown that with a professional and disciplined approach in lending, it is possible for microfinance programmes to achieve high repayment rates in PNG.

**Sources:** 1. Microfinance in the Pacific Island Countries by Paul McGuire, December 1996, pp.39, 61-70

2. Small Business Development in Papua New Guinea: Lessons by Sally Brookes, 1996, pp.30-31

#### Case Study 2: The Nukuroa Revolving Fund (Successful Microfinance Scheme)

**Location:** Mitiaro Island, Cook Islands

**Target Group:** All people in the island of Mitiaro

**Life Span of the**

**Project:** Three years

Access to Funding: SPC (NZ\$10,000) for seed capital

Technical Assistance: SPC

#### Critical Success

Factor: Cooperation and support of the people; community pressure, which ensures loan repayment; and development of the skills and capability of the people to manage the project.

Summary: The Nukuroa Revolving Fund (NRF) was established in Mitiaro, in the Cook Islands in September 1988 through the South Pacific Commission's Mitiaro Integrated Rural Development Project (MIRDP). It aimed to reduce the difficulties experienced by local people in obtaining credit for small loans through existing financial institutions, and gives people the means to acquire the tools and equipment to participate in project activities on the island. A fund of NZ\$10,000 is managed by a committee elected by the community which includes a representative of traditional chiefly leaders, each of the churches, the youth and women's organisations, the Island Council and the MIRDP committee. As members of the community, the committee is able to judge amongst themselves the creditworthiness of applicants, thus overcoming the need for collateral.

The establishment of the fund was accompanied by a participatory training workshop on the principles of banking for the community and the fund's management committee. Initially the fund was restricted to loans for agricultural equipment, but in 1990 the community decided to remove restrictions, enabling people to borrow for home improvement and non-agricultural income-generating activities. It also raised the upper limit of loans from NZ\$500 to NZ\$1,000. In 1992 the fund had grown to over \$42,000. Of 126 loans granted, 50% were made to women who proved to be the most creditworthy in terms of making their repayment within the 12-month repayment period. On-time repayment rates averaged 94% over the period. This confirmed loan recipients' concern to retain their eligibility and access to further loans from the NRF. The social pressures within the Mitiaro community influenced the repayment habits of clients.

Source: 1. ADB Report  
2. From Words to Wheelbarrows, the Nukuroa Revolving Fund by Vaine Wichman, 1993

#### Case Study 3 The Women's Social and Economic Development Programme (WOSED) (Successful Microfinance Scheme)

Location: Fiji covering urban and rural areas

Target Group: Disadvantaged women

Life Span of the  
Project: 1993 / ongoing

Access to Funding: SPC (F\$8,794) for pilot phase and NZODA (F\$86,216) for expansion

Technical Assistance: TA provided by Peace Corps Volunteers (small business advisors); WOSED supervisors and WOSED facilitators

#### Critical Success

Factor: Close monitoring and supervision, peer pressure, intensive training for both borrowers and staff, credit discipline, sound management

Summary: WOSED is a microcredit programme, which was patterned after the successful Grameen Bank (GB), of Bangladesh. Though modifications were made to suit the conditions and culture in Fiji, the GB principles of Unity, Discipline, Courage and Hard Work were strictly adhered to by the WOSED implementors and the beneficiaries alike. In the implementation of WOSED, some of the essential features of the GB have been adopted such as: formation of women's groups, small loans and weekly repayments, loans for income-generating projects only, compulsory savings, rigorous staff and clientele training, group accountability and responsibility, and the 2-2-1 mode of loan disbursement to members.

Loans are for eighteen months, with an interest rate of 8% flat charged over the eighteen months. In other words, the total amount of interest payable is calculated as 8% of the original principal, and this is charged evenly over the eighteen months. This is equivalent to an effective interest rate of 10.3%. Groups may elect to repay their loans weekly or fortnightly, but most groups have opted for weekly repayments. The first loan is for a maximum of F\$500 (US\$355), and the second loan is for a maximum of F\$1,000 (US\$709).

The programme was pilot-tested in April 1993 involving two women's groups in Rakiraki, two groups in Savusavu and two groups in Suva for a total twenty-seven women. As of June 1996, there were 137 borrowers and the programme registered a cumulative repayment rate of 71.6%. A further 47 borrowers had been trained and were waiting to receive their loans.

Source: 1. A Study of Credit Programmes and Schemes Benefiting Disadvantaged Groups in Fiji, September 1995, ESHDP/UNDP  
2. Microfinance in the Pacific Island Countries by Paul B McGuire.

Case Study 4 Women's Credit Scheme in Papua New Guinea - Simbu Province, Pilot Project (Unsuccessful Microfinance Project)

Location: Papua New Guinea (Simbu Province)

Target Group: Women from low-income families

Life Span of the Project: Three years

**Access to Funding:** Funds from the Simbu Province Government, a Member of Parliament's "discretionary fund", and APDC grant totaling K23,300

**Fund Management:** Grant given in trust to a committee of public servants to administer

#### Technical Assistance

**Provision:** Business Development Officer (BDO) from the Simbu Department's Commerce Division for business advice, and PWRD/SPC for advisory assistance on administration of scheme and ILO for training.

#### Critical Failure

**Factors:** Lack of training and technical support to management and beneficiaries, poor record keeping, lack of participation and commitment of beneficiaries as scheme was managed by a committee of public servants and was never turned over to the women's association as originally intended.

Lack of population density in such a large area also meant poor productivity of loan management.

**Summary:** In 1988 a credit scheme exclusively for women was piloted in the East Sepik and Simbu Provinces of Papua New Guinea. Simbu Province was the most ambitious of the two pilot sites in terms of gearing the credit scheme for access by all the seven districts of the province covering a land area of 6,181 sq.km and a population of over 170,000.

A fully operational, well-managed scheme has not been established in Simbu. The fund was provided a total of K23,300 in 1988, but by October 1993 the amount remaining in the account was K2,271.81, and there had been no deposits to the fund since March 1992. The standard bookkeeping made it difficult to determine the repayment rates of individual borrowers. However, the letters to defaulters indicated a considerable number had failed to fully repay their loan, although the amounts outstanding were often small (K30-40), relative to loan sizes (K100-500). The SPC review found out that the scheme faltered from the beginning due to inadequate coverage by technical visits. Moreover, training for management and beneficiaries were lacking. The project was suspended in 1992.

**Source:** Review of the SPC Women's Credit Scheme in Melanesia (Papua New Guinea, Solomon Islands, Vanuatu): Report, by Jane O'Donohue & Vaine Wichman, 1995, pp8-13.

#### Case Study 5 The Tonga National Youth Credit Scheme (Unsuccessful Microfinance Scheme)

**Location:** Tonga, covering two island-groups of Tongatapu and Ha'apai

**Target Group:** Youth groups

**Access of Funding:** SPC (AU\$20,000 or T\$18,000 for seed capital)

Fund Management: Tonga National Youth Council through a credit committee

#### Technical Assistance

Provision: International Labour Organisation (ILO), Regional Equitable and Sustainable Human Development Programme (ESHDP/UNDP), Ministry of Education

#### Critical Failure

Factors: Poor management, poor monitoring, lack of credit discipline and responsibility, beneficiaries lack business orientation, leniency in loan collection, absence of well-defined policies.

Summary: The Tonga National Youth Credit Scheme was launched in September 1993 with training to provide business orientation and skills to interested youth groups. Loans were released in December 1993 to eligible youth groups to finance the establishment of income-generating projects. The maximum amount that a group can borrow is T\$1,000 payable within a year at 10% interest rate per annum. Collateral and other forms of securities are not required. An applicant youth group however is required to get an endorsement from the umbrella organisation to which the group belongs.

The scheme is managed by the Tonga National Youth Congress (TNCY) and is overseen by its Director with the support of the Executive Committee. A credit committee was created to appraise and approve project proposals. The Project Officer is responsible for the day-to-day operation of the credit scheme.

As of April 1996, a total of 15 projects were funded of which 10 are operational and 3 are non-operational. Repayment is low and a UNDP review in May 1996 cited some factors that contributed to low repayment performance, namely: unprofitable operation, lack of business orientation, disintegration of the groups, lack of credit discipline and responsibility, and leniency in loan collection.

Source: Evaluation of the Tonga National Youth Credit Scheme: A Report prepared by ESHDP/UNDP, May 1996

## F. Demand for Microfinance

Economic growth throughout the Pacific has been low during the last decade. Fiji, Kiribati, Vanuatu and the Solomon Islands recorded negative growth in per capita incomes during the 1980s and early 1990s. Tonga, Federated States of Micronesia and the Marshall Islands display stagnant growth rates.

The combination of low overall economic growth, and generally high population growth, in environments unable to generate adequate increases in wage earning employment places pressure on the subsistence and informal income generating sectors.

In this context support to the informal and subsistence sectors becomes a significant factor in improving quality of life and contributing to economic growth. Two Sub Components of the Small Entrepreneurs Support Component of the Private Sector and Sustainable Livelihood Programme: Social Mobilisation for Sustainable Livelihoods for Poor and Disadvantaged Groups; and, Small Enterprise Development Programme focus on this sector. However, without adequate access to finance, achievements in market access, business and technical skill improvement, or in creation of an enabling legislative and policy environment, key objectives of these two sub components are of limited value.

There is very little data on poverty for the Pacific Islands. Recent published socioeconomic data is mainly confined to Fiji and shows that urban poverty has grown significantly in recent decades from 6% of Fijians in 1997 to 25% in 1992. Few if any economic studies of poverty have been conducted in other countries of the region. The governments of Pacific Islands take pride in established beliefs that countries of the region are “poverty-free” due to customary institutions such as the extended family. However, as noted earlier, population growth in the Pacific far exceeds economic growth. This situation will inevitably contribute to poverty, whether measured, acknowledged or not, particularly in urban areas.

The tables overleaf identify the degree of urbanisation by country and estimate the urban poor.

## G. Pacific Urban Populations and Estimated Urban Poor

## Sub-Region: Melanesia

Country	Population	Urban Percentage	Urban Population	Est. "poor" Population
Fiji	800,500	39	312,000	78,000
New Caledonia	196,800	71	140,000	42,000
Papua New Guinea	4,141,800	15	621,000	186,000
Solomon Islands	395,200	13	51,000	15,000
Vanuatu	173,900	18	31,000	9,000
Total	5,708,200	20	1,155,000	330,000

## Sub-Region: Micronesia

Country	Population	Urban Percentage	Urban Population	Est. "poor" Population
Federated States of Micronesia	109,200	N/A	N/A	N/A
Guam	153,700	38	58,000	17,000
Republic of Marshall Islands	57,400	65	37,000	11,000
Nauru	11,200	100	11,000	3,000
Northern Mariana Islands	62,700	N/A	N/A	
Palau	17,700	N/A	N/A	
Total	411,900	26	106,000	31,000

## Sub-Region: Polynesia

Country	Population	Urban Percentage	Urban Population	Est. "poor" Population
American Samoa	58,900	48	28,000	8,000
Cook Islands	19,900	58	12,000	4,000
French Polynesia	220,000	57	125,000	38,000
Niue	2,300	30	700	200
Pitcairn Island	47	0	0	
Tokelau	1,500	0	0	
Tonga	90,000	31	28,000	8,000
Tuvalu	9,600	42	4,000	1,000
Wallis & Futuna	14,800	0	0	
Western Samoa	165,100	21	35,000	11,000
Kiribati	78,400	37	29,000	9,000

Total	660,547	40	261,700	79,200
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Source: South Pacific Commission, Mid Year Population estimates 1996. Urbanisation ratios not available where noted. NB Estimated “poor” calculated as part of this feasibility study.

Several features of interest emerge from this data:

The total urban population within the Pacific amounts to approximately 1.5 million. However, rates of urbanisation vary markedly between sub-regions. The total urban population is spread over 22 different countries and territories with an average urban population of 68,000 per territory.

This measure of urbanisation, of course, is only a first step to gauging demand. Given the paucity of data concerning poverty in the Pacific, it is not possible to accurately estimate the number of “poor”, let alone those who are economically active. Present best estimates, which are very much “rule of thumb”, based on the combined experience of UNDP Suva and the Consultants, indicate a poverty ratio of 25% for Fiji and 30% in most other territories. If accurate, these suggest a total potential population of 438,000 across the region, or an average of 20,000 per territory.

Most Pacific countries have only one urban centre. The two exceptions are Papua New Guinea and Fiji. Whilst intuitively this suggests that density of poor populations is therefore relatively high, it should be borne in mind that all Pacific urban centres are very small. The largest (Port Moresby National Capital District) has a total population of 223,000, and the smallest (Funafuti, Tuvalu) a population of 4,000. Rural areas in the Pacific consist of outlying islands. Some examples are given below. In some of the small countries and territories the population is too small to comprise an urban centre.

Country	Population	Rural Population	Number of Islands	Rural Population Density/Island
Tonga	90,000	62,000	36	1,700
Kiribati	78,400	49,000	33	1,500
Vanuatu	173,900	142,900	70	2,000
Republic of Marshall Islands	57,400	20,000	34	588

These rural island communities are often the focus of bilateral donors’ efforts to introduce microfinance programmes, many of which have failed.

Lending patterns in the Pacific also tend to confirm the presence of micro-entrepreneurs in the region. The average size of loan made by Development Banks in the Pacific is US\$1,200, across all sectors.

## H. Finance, Banking and Informal Credit Institutions

### Development Banks

Fourteen countries within the region have a Development Bank. All Pacific Development Banks are currently wholly or partially Government owned. In some countries (such as Tonga and the Solomon Islands) a commercial bank also holds shares. Clearly, once the Development Bank moves significantly towards self-sufficiency, this places the two banks in direct competition and the Development Bank may negotiate sale of commercially owned shares. One Development Bank which has demonstrated consistent performance improvement (Cook Islands) is currently open to tender as part of a wider asset sale.

Most Development Banks have a history of poor performance, arising from: inadequate financial and management accounting systems; high cost structures; government policy restrictions; low interest rates and very low collection rates. All Development Banks have received significant financial and technical assistance from Donors. The Tonga Development Bank is considered to be one of the best performing in the region.

Most Development Banks have attempted to provide microfinance but few have continued to do so because of the very high cost. In some cases, bilateral donor funds are used to subsidise the cost of small loans. Similarly it is very costly to maintain branch offices outside the main centre(s). Where this is done (for example, Cook Islands, Tonga, Kiribati) office set up costs and/or equity has been provided wholly or partially by Donors.

Six Development Banks provide targeted services to disadvantaged groups - generally considered as Women, Outer Islands and Youth. These are: Tonga, Cook Islands, Western Samoa, Solomon Islands, Kiribati and Fiji. The total number of microfinance borrowers reached through these schemes is less than 5,000. About 80% of the total portfolio for all Development Banks was for loans of less than \$10,000 in 1995, and about 90% for loans of less than \$2,000. Interest rates range from 8% flat to 16%.

### Credit Unions

Most Pacific Island Nations have a range of credit unions. These are often church or interest-group based, generally in the main centre(s) and generally accessed by wage and salary earners. They provide microcredit in the range of US\$5.00 to 1,000.

Formal credit unions have flourished largely due to the activities of the Hans Seidel Foundation (German NGO). Credit unions established by HSF are provided with ongoing institutional strengthening and training and operate through a National League of Credit Unions apex. This has proved successful in Papua New Guinea, the Solomon Islands, Vanuatu, Tonga, and Kiribati. They are particularly successful where there are few other formal options for savings available.

## Revolving Funds

Revolving funds are the most widespread source of formal microfinance, particularly in the Outer Islands. Our survey identified eighteen such schemes currently in operation throughout the Pacific. It is likely, in fact, that the number of revolving funds established but not necessarily operating is between 80-100.

Many of the revolving funds were established under conditions which precluded their effective use: criteria too rigid; community unclear how to dispense/account for funds; lack of accounting and quality control. There are many examples of funds which “revolved once only”; there are also many examples of funds long forgotten by Donors, still sitting largely untouched in needy island communities because criteria for use were inappropriate and/or the procedures for use were unclear.

All schemes appraised had been established by Donors. These schemes are most prevalent in Papua New Guinea, Cook Islands, Western Samoa, Kiribati and Tuvalu. Successful revolving funds require careful attention to accounting and collection. The isolation of most islands means this task must be undertaken within the community, usually using an established Island Council.

Three factors mitigate against long term success of these schemes: lack of accounting and management skills; dwindling motivation; lack of real business opportunities. A key success factor with such schemes is the monitoring of fund use by an external agent and the availability of pre and post borrowing training and skill development.

Unfortunately the presence in the Outer Islands of large numbers of poorly functioning or non-sustainable schemes based on low interest rates mitigates the success of schemes which operate on a cost-recovery basis. Two exceptions are Outer Islands revolving funds in Tonga and the Cook Islands which are managed by the Development Banks and charge standard Bank interest rates (8% - 12%). This, however, is still insufficient to meet operational costs without Donor assistance.

## Grameen Derivatives

There are several successful examples of Grameen models in the Pacific. The two most visible are the Fijian Womans Social and Economic Development Programme and the Papua New Guinea Liklik Dinau Abitore Trust. In total about 500 borrowers have been reached with these two projects, over a three year period. There are some serious limitations to the application of the Grameen model in the Pacific. These include: no centres of population density commensurate with successful Asian and Latin American examples; limited opportunities for market diversification; geographic distance precludes regular supervision.

A study by ESCAP (1993) for example, investigated the feasibility of a Grameen Bank for Kiribati but concluded it would not work effectively due to: lack of appropriately skilled staff in the Outer Islands; high administrative and transport costs; difficulties in providing sufficient support to

borrowers, and difficulty convincing borrowers that the loan was not a gift. The study concluded that multiple, localised credit unions would be more effective.

### Informal Savings and Credit Schemes

The Pacific has a reputation for consumption according to production, rather than accumulation and savings. This is largely correct, especially in remote island communities, and is a function of both the semi-subsistence life style and the fecundity of the land, which ensures a continual, adequate food supply, albeit of limited variety in remote islands.

However, there are many examples of informal credit schemes developed locally. Most of these are amongst groups of women who contribute to, and borrow from, group funds. Many of these groups require interest payments or a contribution in kind.

A large number of Outer Islands still have no, or minimal, access to formal banking and savings schemes but are well used to donor-funded grants. Considerable groundwork is required to bring about attitude changes which would support the introduction of microfinance on a cost recovery basis.

### Microcredit for Women Borrowers

#### Formal Microcredit Schemes

(Historically) Womens' limited access to finance in their own right has been a major constraint to womens' ability to develop microenterprises. Over the last five years, Pacific womens' access to microcredit has improved substantially and in fact over 60% of microcredit schemes analysed were targeted specifically at women borrowers.

Reviews indicate severe, consistent difficulties with womens' microfinance schemes:

Administering groups have not established adequate systems for loan delivery and management;

Loan management systems or income generating activities conflict with traditional systems of resource allocation;

The absence of consistent, knowledgeable back-up support (access to credit) has led to loan defaulting and business failure;

Many products originally intended for sale and later kept (tapa, mats, food), leading to repayment difficulties;

There are numerous examples of men obstructing either schemes or production. This is sometimes based on traditional role conflict but more often due to perceived lack of “fairness” particularly when access to finance for men is more limited;

It is too often assumed that attendance at a short training course will provide sufficient business skill. This is often incorrect and many women say they have not understood but were afraid to ask (in both mixed and single sex groupings).

### Informal Microcredit Schemes

Most womens’ committee credit schemes include savings schemes. At least some component of the savings is usually compulsory with the capacity to voluntarily contribute more and to withdraw the voluntary component if required. Compulsory savings components range from about US\$0.50c per week to US\$5.00 per week. Some schemes separate fund components into those which can only be used for income generating activities and those which can be used for emergencies, funerals, weddings and other special occasions, with priority given to borrowers according to the above order.

The number of such savings and credit schemes operating without donor assistance is huge. For example, in Western Samoa there are over 330 villages, each of which has one or more scheme.

Access to microfinance by the economically active urban poor is very limited. Most microfinance schemes have been set up in the Outer Islands and/or are directed at special disadvantaged groups. The greatest need for microfinance is in urban centres which have moved from subsistence to cash economies but where existing formal financial institutions cannot, or will not, service loans below US\$500.00. Even so, the lack of volume and density of population in urban areas requires that financial intermediaries must operate with even more rigour than microfinance institutions in Asia or Latin America to approach operational sustainability. Options for selection of financial intermediaries which satisfy the Committee of Donor Agencies - Guiding Principles of Selecting and Supporting Intermediaries - are few. Section 2.0 raised three questions to determine whether further feasibility analysis should be undertaken. Results are summarised below.

### Potential Locations of Microfinance Organisations and Clients

Through a series of meetings and seminars with UNDP staff and the Resident Representative of Western Samoa and Fiji the following Locations have been identified:

#### Locations

Year 1	Three sites: Fiji Lautoka on the island of Viti Levu Suva, on the island of Viti Levu, and Labasa, on the island of Vanua Levu
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In each case, the site radius will extend 50km from the city centre.

- Year 2            Three sites:  
Western Samoa  
Vanuatu  
One Micronesian Country  
The Vanuatu site will encompass the urban squatter centres in Port Vila which are currently being assisted under the UNDP Social Mobilisation programme.
- Year 3            Three sites: to be decided by the end of Year 1 on the basis of country interest as demonstrated at Regional Microfinance Workshops, and availability of suitable and interested financial intermediaries in urban centres.

Justification:

Fiji provides three sites with differing urban characteristics within one country. Activities operating under other projects provide target groups with community networks and other sources of community support identified and active. There is a strong local UNDP office capable of providing both the necessary direct and indirect inputs and undertaking baseline and evaluation studies to allow trialing of framework and processes.

Western Samoa Regional Office has expressed keen interest in participating and can provide access to urban communities with existing community networks.

UNDP has been working for a year to improve the income generating capacity of formed groups of women through the UNDP: Vanuatu Women Development Scheme (VANWODS). A UNDP project network under VANWODS can provide support. The target group is a squatter settlement in Port Vila where up to 40% of the Vila population live. The majority of people in these settlements are from outer islands or rural areas who do not have the right to land in the urban capital. Selection criteria based upon per capita income, assets and lack of current employment are currently being trialed, together with group membership criteria.

## I. Risks and Special Considerations

The lack of borrower density in the Pacific makes both provision of borrower support and lending services difficult and expensive. Most successful models elsewhere have an outreach that exceeds the entire population of many Pacific Island Countries. Grameen in Bangladesh, and BankoSol in Bolivia, for example, each have clientele in excess of 2 million.

It is difficult to form Solidarity Groups without inherent conflict of interest amongst members, given the limited depth and range of market opportunities, particularly in smaller island communities.

The requirement for Solidarity Groups to contain only one member per household will be inappropriate in many communities, particularly within Polynesia, where Solidarity Groups based around the extended family may be the only acceptable composition for group guarantees. Similarly the concept of “household” will require redefinition generally within the Pacific. This is generally accepted as a family which “eats and sleeps together”. Appropriate means tests will require development on a country by country basis.

There is very limited scope for transferability of schemes designed for urban poor to rural poor. Criteria will have to be more specifically tailored to individual target groups than is the case in other regions.

The high management and administration cost associated with low volume lending in dispersed populations will result in very high interest rates to achieve self sufficiency.

The historical widespread distribution of aid with minimal (if any) accountability requirements has generated a jaundiced view toward interest, and indeed repayment, particularly in the Outer Islands.

Overall the key risks are:

- Very high cost structures;
- Limited range of institutions meeting selection criteria;
- Low volumes of borrowers in contiguous geographic areas;
- Need for very high levels of technical assistance to both borrowers and institutions.

There are already many programmes addressing these issues in the Pacific. The ITSP should undertake detailed appraisal of existing or previous projects and incorporate “lessons learned”.

## J. Critical Success Factors for Microfinance in the Pacific

- ♦ Concentrate resources on organisations with the greatest potential for operational and financial self-sufficiency;
- ♦ As a component of the start up phase, build plans for long term sustainability including how diminishing reliance on external assistance can be achieved; set achievable milestones and publicise progress against targets widely;
- ♦ Focus resources jointly on community strengthening and institutional strengthening, and assess readiness against defined minimum “preconditions” for start up before lending commences;
- ♦ Reduce layers of management and communication between the potential borrower and the lending officer to the absolute minimum;
- ♦ Start where the community is, not where you want them to be, especially with project size and type;
- ♦ Simplify application procedures and paperwork;
- ♦ Make sure appraisal and mean testing procedures do not cause potential borrowers to lose face or confidence;
- ♦ Extend credit quickly;

### Other Central Success Factors

Insist on some form of business plan for start up or business extension to help borrowers establish a frame of reference for “how it will work”.

Set collateral substitute requirements consistent with community capacity;

Understand market limitations and discourage unworkable and oversaturated projects at an early stage;

Provide larger loans based on successful repayment;

Get clients promoting the scheme, not just community workers.

Do not mix income generating loans with loans for social purposes. Where this is unavoidable, establish clear priorities for lending.