The Impact of microfinance on poverty reduction in Rwanda from 2005-2014 : Case of vison Hope

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CHAPTER ONE

INTRODUCTION

1.0 General Introduction to the Study

For more than 30 years microfinance has been portrayed as a key policy and program intervention for poverty reduction and 'bottom-up' local economic and social development.
Microfinance is the provision of tiny loans to the poor to help them establish or expand an income-generating activity, and thereby escape from poverty, it began with the work of Dr Muhammad Yunus in Bangladesh in the late 1970s, spreading rapidly to other developing countries.
Most early microfinance institutions (MFIs), including Yunus's own iconic Grameen Bank, relied on funding from government and international donors, justified by MFI claims that they were reducing poverty, unemployment and deprivation (Milford Bateman March 2011).

The microfinance sector in Rwanda is relatively young. Although small self-help peasant organizations (such as tontines-ROSCA or ibimina) have existed for some time, the sector growth accelerated with the creation of the Rwanda Banques Populaires or Union des Banques Populaires du Rwanda (UBPR) in 1975 whose network dominates the microfinance industry today.
The history of MFIs is better described trough the following time line:

- 1965 : Probable date of appearance of the first ROSCA or IBIMINA;
- 1975 : Establishment of the first Banque Populaire (BP), the Banque Populaire of NKAMBA, on August 4, 1975;
- 1986 : Banques Populaires create a Union called Union of the Banques Populaires (UBPR);
- 1994 : all MFIS stopped their activities and lost their assets during the 1994 war and genocide;
- 1995: Launching of the financial sector reform. After 1995, the Government started reforms of the financial sector aiming at creating an efficient financial system. The principal objectives of these reforms include the reinforcement of the Central Bank (BNR) legal powers of coordination and supervision of the banking structure, the introduction of new financial instruments, the liberalization of interest rates and the opening of the banking structure to foreign banks. These reforms had a considerable impact on the development of the Rwanda's financial sector.
- 1996 : Reopening of the Banques Populaires;
- 1999: Promulgation of the banking law n° 08/99 dated June 18, 1999 assigning the responsibility for the MFIs' supervision to BNR ;
- 2002 : Creation within the Rwanda Development Bank (BRD) of the Fund for Refinancing and Development of Microfinance (FOREDEM);
- 2002/2003: Adoption by BNR of two instructions regulating the activities of microfinance in general (Instruction n° 06/2002) and the instruction specific to COOPECS (Instruction n° 05/2003);

- 2004 : First microfinance conference evaluating the level of achievement of the objectives of year 2005, declared international year of microcredit;
- 2005: a “microfinance best practices sensitization tour” was organized around the country by the Secretary of State for Planning (in the Ministry of Finance) and the

Governor of the National Bank of Rwanda explaining the risks of an illegal proliferation of Coopecs and other MFIs. Were invited to these meetings all MFIs, local authorities at various levels; the National police force and all the other actors of the field.

In 2008, the sector counted 125 MFIS including 111 COOPECs, 11 SA and 3 limited liability companies. These numbers confirms the attractiveness of the COOPECS model within the entire microfinance sector. Indeed the user-owned financial cooperatives that offer savings, credit and other financial services to their members are easy to establish (low minimum capital) and are based on a common bond, a linkage shared by savers and borrowers that can be based on a community, organizational, religious or employee affiliation. They provide members the chance to own their own financial institution and help them create opportunities such as starting small businesses, building family homes and educating their children in a democratic manner.

Globally, the number of people in absolute poverty has been in decline for around 25years (Poverty Reduction in Africa by Paul Collier 2007), yet in Africa it is still increasing. The challenge of poverty reduction in Africa is of a different order from that elsewhere and will require different strategies.

Poverty remains a matter of growing concern in many developing countries of the world. Today, as other continents continue to register sustainable economic growth and development, Africa is not only lagging behind but is trapped in a vicious circle of borrowing and donor dependency syndrome which some critics point out as one of the causes practically sabotaging real development. Africa has perpetually failed to focus its development efforts on the optimum utilization of the immense natural resources that many countries are endowed with to turn it into wealth to propel their economies and people towards a high level of economic and social development and as a consequence eliminate pervasive poverty.

Poverty is a complex phenomenon influenced by a large number of factors and which can be studied from many different perspectives. The study and interpretation of poverty isn't a simple task, as there are as many ways of measuring poverty as there are ways of defining it.

According to (Ghalib, Asad K. (2007), Poverty is a condition in which a person of community is deprived of the basic essentials and necessities for a minimum standard of living.

1.1 Background

Rwanda's Economic Development and Poverty Reduction Strategy (EDPRS) is both a document and a process. As a document, the EDPRS sets out the country's objectives, priorities and major policies for the next five years. It provides a road map for government, development partners, the Private Sector and civil society and indicates where Rwanda wants to go, what it needs to do to get there, how it is going to do it, what the journey is going to cost and how it will be financed. The strategy provides a medium term framework for achieving the country's long term development goals and aspirations as embodied in Rwanda Vision 2020, the seven year Government of Rwanda program, and the Millennium Development Goals.

The EDPRS breaks with the past in two ways. Firstly, the strategy redefines the country's priorities. Rwanda's first Poverty Reduction Strategy Paper (PRSP) covered the period 2002-2005. It was elaborated in a post-conflict environment where the primary emphasis was on managing a transitional period of rehabilitation and reconstruction.

The EDPRS assigns the highest priority to accelerating growth to create employment and generate exports. It will achieve this through an ambitious, high quality public investment program aimed at reducing the operational costs of business. This big push will create strong incentives for the Private Sector to increase its investment rate in subsequent years. With two thirds of the population aged less than twenty-five years, particular emphasis will be placed on creating jobs for young people. Vision 2020 *Umurenge* is a highly decentralized integrated rural development programme designed to accelerate extreme poverty reduction in Rwanda. It is currently being piloted in thirty of the poorest sectors (*imirenge*) of the country.

Governance seeks to build on Rwanda's reputation as a country with a low incidence of, and zero toleration for corruption and that has initiated innovative home-grown mechanisms for conflict resolution, unity and reconciliation. In the next five years, Rwanda plans to develop a regional comparative advantage in 'soft infrastructure', that is, those aspects of governance, such as well-defined property rights, efficient public administration, transparency and accountability in fiscal and regulatory matters.

1.1.0The current global Perception of microfinance

In the global arena there is already the impression that microfinance is successful in reducing poverty. Many policy makers are therefore engaged on how to make microfinance sustainable and available to many poor households in the future. Many stake holders in the microfinance industry especially donors and investors argue that, "Microfinance can pay for itself, and must do so if it is to reach very large numbers of poor households" (CGAP).

The overall message in this argument is that unless microfinance providers charge enough to cover their costs, they will always be limited by the scarce and uncertain supply of subsidies from governments and donors. The main underlying assumption in this argument is that microfinance is already good for the clients, and therefore what is really urgent is to make the financial service available to as many poor people as possible. Morduch (2000) correctly points out that this kind of enthusiasm for microfinance rests on an enticing win-win proposition that: Microfinance institutions that follow the principles of good banking will also be the ones that alleviate the most poverty. The assumption being that with good banking practices it is possible to cover costs and operate in a sustainable manner to continue serving clients and alleviating poverty (Morduch 2000).

1.1.1 The microfinance hype

The 1997 Microfinance Summit called for the mobilization 0f $20 billion over a 10 year period to support microfinance. The United Nations proclaimed 2005 as the "Year of Micro-credit" while 2006 went a score higher to award a Nobel Peace Prize to the largely acclaimed founder of modern microfinance: Prof. Muhamad Yunus and the Bank he founded in the 1970s: the Grameen Bank. The recent publicity accorded microfinance potentially creates an image of an institution that is all success, thus lacking critique. To justify such significant hype and investment in the name of poverty reduction compared to other alternative investments for the same cause in other programs; it is important that the proposition that "microfinance reaches and helps the poor most" be proven and not just assumed.

As though to counter the negative arguments against the impact of microfinance on poverty reduction, other studies have found that microfinance is relevant to poverty reduction not just for the beneficiaries but also there are positive spillover effects to the rest of the community (Khandker 2006). In his study Khandker (2006) uses a panel household survey from Bangladesh and observes that access to microfinance contributes to poverty reduction, especially for female participants, and to the overall poverty reduction at the village level

1.2 Problem Statement

There are about three billion people, half of the world's population, living on the income of less than two dollars a day. Among these poor communities, one child in five does not live to see his or her fifth birthday *(Barr, Michael S. (2005).*

One study in 2006 showed that the ratio of the income between the 5% richest and 5% poorest of the population is 74 to 1 as compared to the ratio in 1960, which was 30 to 1, *(Microfinance/Facts and Figures).*

To enhance international development, the United Nations Organization (UNO) announced the millennium development goals, aimed to eradicate poverty by 2015, *(Barr, Michael S. (2005).*

In this regard according to *(Ibid, 2005, p.273),* microfinance is the form of financial development that has its primary aim to alleviate the poverty.

Governments, donors and NGOs around the world responded enthusiastically with plans and promised to work together towards the realization of these goals. In the recognition of microfinance, the UNO celebrated the year 2005 as a year of micro-credit, (Mia, Md. B. *"ICT in Microfinance: A Bangladesh Perspective"*, p. 1).

As a result this financing instrument is perceived worldwide as a very effective mean against hunger and poverty, mainly in developing countries. Microfinance is a credit methodology, which employs effective collateral substitute for short-term and working capital loans to micro-entrepreneurs (Hubka, A.; Zaidi, R. (2005).

Thus, the level of a country's poverty has long been linked with measures of its economic development. Little consideration was given to the social reorganization of the natural resources (e.g. empowerment vs. alienation of people, sustainable use vs. depletion of the environment). Fallavier, P. (1998).

As a matter of fact, most promoters of microfinance do not wholly disagree that microfinance alone cannot do the job. For example, Sam Daley-Harris, Director of the Microcredit Summit Campaign, writes, “Microfinance is not the solution to global poverty, but neither is health, or education, or economic growth. There is no one single solution to global poverty. The solution must include a broad array of empowering interventions and microfinance, when targeted to the very poor and effectively run, is one powerful tool.” (2007: 1).

In the words of Professor Yunus (2003: 171; emphasis added), “Micro-credit is not a miracle cure that can eliminate poverty in one fell swoop. But it can end poverty for many and reduce its severity for others. Combined with other innovative programs that unleash people’s potential, micro-credit is an essential tool in our search for a poverty-free world”.

1.3 General Objective

The General Objective of the study is to evaluate the Impact of microfinance on Poverty reduction in Rwanda

1.3.1 Specific Objectives

1- To Investigate if the standards of living of the People in Rwanda has increased due to Microfinance
2- Has the socio-economic life improved due to Microfinance support
3- To evaluate the difference between Microfinance users and non-microfinance users

1.4 Research Question

In the light of the general objective of this research proposal and its specific objectives, the following are the research questions

1- Has the standards of living of the people in Rwanda increased due to Microfinance Institutions?
2- How has the socio-economic life of the people in Rwanda improved due to Microfinance support?

3- What are the lifestyle differences between the Microfinance and non- Microfinance users?

1.5 Hypothesis

The hypothesis of the study is

Ho: Microfinance scheme can improve the socio-economic standards of the people in Rwanda

Ha: Microfinance scheme cannot improve the socio-economic standards of the people in Rwanda

1.6 Methodology

The principle purpose of this section is to deal data collection and analysis, which also represents the choices I have made in order to make the right option of my thesis, the questionnaire design and sample selection. It concludes with the information about the secondary sources.

1.6.1 Sources of Data

The research will use both primary and secondary Data

1.6.2 Primary Data

The collection of primary Data involve carrying out interviews in selected company, provision of questionnaires.

1.6.3 Secondary Data

Data collected form Kigali library. The research will also be conduct from annual reports containing detail of financing companies, internal records kept by organizations.

1.6.4 Sampling design and the procedures

The researcher will use simple random sampling where by all element equals chances of being selected and purposive sampling to select people who are expected to give right information.

1.6.5 Scope of the study

The scope will be limited to an investigation of Vision finance LDT targeted to find out about microfinance impact on the socio-economic standards life of the clients of Vision finance LDT. Rwanda being a case of less develop country with less economic development, microfinance need to be studied to judge how they have impacted the socio economic.

CHAPTER TWO

2.0 Literature Review

Microfinance, according to Otero (1999, p.8) is “the provision of financial services to low-income poor and very poor self-employed people”. These financial services according to Ledgerwood (1999) generally include savings and credit but can also include other financial services such as insurance and payment services. Schreiner and Colombet (2001, p.339) define microfinance as “the attempt to improve access to small deposits and small loans for poor households neglected by banks.” Therefore, microfinance involves the provision of financial services such as savings, loans and insurance to poor people living in both urban and rural settings who are unable to obtain such services from the formal financial sector.

2.1 Microfinance and microcredit.

In the literature, the terms microcredit and microfinance are often used interchangeably, but it is important to highlight the difference between them because both terms are often confused. Sinha (1998, p.2) states “microcredit refers to small loans, whereas microfinance is appropriate where NGOs and MFIs supplement the loans with other financial services (savings, insurance, etc)”. Therefore microcredit is a component of microfinance in that it involves providing credit to the poor, but microfinance also involves additional non-credit financial services such as savings, insurance, pensions and payment services (Okiocredit, 2005).

2.2 The History of Microfinance

Microcredit and microfinance are relatively new terms in the field of development, first coming to prominence in the 1970s, according to Robinson (2001) and Otero (1999). Prior to then, from the 1950s through to the 1970s, the provision of financial services by donors or governments was mainly in the form of subsidised rural credit programmes. These often resulted in high loan defaults, high loses and an inability to reach poor rural households (Robinson, 2001).

Robinson states that the 1980s represented a turning point in the history of microfinance in that MFIs such as Grameen Bank and Bank Raykat Indonesia began to show that they could provide small loans and savings services profitably on a large scale. They received no continuing subsidies, were commercially funded and fully sustainable, and could attain wide outreach to clients (Robinson, 2001). It was also at this time that the term “microcredit” came to prominence in development (Microfinance Information Exchange, 2005). The difference between microcredit and the subsidised rural credit programmes of the 1950s and 1960s was that microcredit insisted on repayment, on charging interest rates that covered the cost of credit delivery and by focusing on clients who were dependent on the informal sector for credit (ibid.). It was now clear for the first time that microcredit could provide large-scale outreach profitably.

The 1990s “saw accelerated growth in the number of microfinance institutions created and an increased emphasis on reaching scale” (Robinson, 2001, p.54). Dichter (1999, p.12) refers to the 1990s as “the microfinance decade”. Microfinance had now turned into an industry according to

Robinson (2001). Along with the growth in microcredit institutions, attention changed from just the provision of credit to the poor (microcredit), to the provision of other financial services such as savings and pensions (microfinance) when it became clear that the poor had a demand for these other services (Microfinance Institution Exchange, 2005).

The importance of microfinance in the field of development was reinforced with the launch of the Microcredit Summit in 1997. The Summit aims to reach 175 million of the world's poorest families, especially the women of those families, with credit for the self-employed and other financial and business services, by the end of 2015 (Microcredit Summit, 2005). More recently, the UN, as previously stated, declared 2005 as the International Year of Microcredit.

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