Creating Value Beyond Microfinance Through Entrepreneurship Development in Kenya

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As microfinance providers and supporters continue promoting the importance of improving access to financial services amongst micro and small business owners, they will need to augment their microfinance services with promoting basic entrepreneurial training.

The scene at open-air markets in Kenya, especially in the rural areas, can sometimes be troubling. As you enter the marketplace, you will see lines of merchants selling similar products all vying to get your attention. While this competition is good from a consumer's point of view, given that it often leads to bargain prices, the same cannot be said from the merchant's point of view. Most of the merchants at the marketplace have loans from a microfinance institution (MFIs) or a savings and corporative society (SACCOs) and make regular repayments, usually bi-weekly or monthly. They are involved in the same lending groups and are familiar with each other's business prowess. Yet at the marketplace, their competition is intense, undercutting each other and driving profit margins to breakeven or negative margins, which ultimately impacts their timely loan repayments and further indebtedness from charges incurred due to late payments. At the end of the day, these institutions see significant improvements to their bottom line, while the merchants struggle to stay afloat – borrowing more from a second lender to pay the first one.

This kind of experience is common for businesses at the bottom of the pyramid that depend on making enough daily sales to pay for the products they purchased on credit from wholesalers. Over the course of the loan period, the regular repayments become more difficult for the merchants and they start falling behind schedule – missing payments here and there, and incurring late fees. Indeed, in a recent study, Dean Karlan and Martin Valdivia found that basic entrepreneurship training could lead to improved managerial decisions and ultimately higher profits. Unfortunately, according to the study, the majority of financial institutions that provide microfinance services prefer to focus on the "infusion of financial capital, not development of human capital."[1] When destructive competition threatens the very livelihood that MFIs and SACCO are trying to improve, it's often because these institutions are experiencing mission drift and little to no emphasis is put on human development for both loan officers (LOs) and their clients. Further, these institutions rely heavily on overwhelmed LOs who do not always have time to provide entrepreneurial training nor do they always have good business acumen in understanding the needs of the merchants in order to help them be financially productive. Specialized trainers who have a good understanding of how to help these merchants improve their profits and managerial decision-making should be the ones providing basic entrepreneurial training and not the LOs.

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[1] Karlan, D. and Valdivia, M. (2009). Teaching Entrepreneurship: Impact of Business Training on Microfinance Clients and Institutions

For the majority of microfinance clients, the group based lending meetings follow a typical development path. LOs or "teacher" as they are commonly referred to facilitate these meetings mainly focused on collecting the loan repayments and the loan portfolio management. In some cases, many meetings are devoted to pressuring group members to make repayments on behalf of those not able to meet their scheduled repayment amounts or for those defaulting members who have disappeared.

At the maturity of the loan, these same MFIs and SACCOs report near perfect repayments rates without mention of the clients who moved into the ranks of indebtedness nor do they mention those that were pressured to subsidize the entire process.[2] Finally, the LO provides a stamp of approval for the next loan cycle.

Many including myself find it hard to comprehend and find it unacceptable that after all the work being done to provide affordable access to basic financial services to micro and small businesses, there is still so little to show by way of productivity improvements and better profits margins. Clearly, something has to be done to create value for these merchants beyond simply giving them microfinance.

To address these issues, the microfinance sector needs to first commit themselves to the original missions of complementing financial services with non-financial services such as basic entrepreneurial training. This would require MFIs and SACCOs to augment their microfinance services with the strengths of complementary services that have proven to enhance their core products.[3] To do so, they will have to gain a clear understanding of the expected improvement of offering entrepreneurial training.

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[2] Duffy-Tumasz, A. (2009). Paying Back Comes First: Why Repayment Means More than Business in Rural Senegal

[3] Henry, S. (2006). Good Practice in Business Development Services: How Do We Enhance Entrepreneurial Skills in MFI Clients?