

DPRN PHASE II – REPORT NO. 12

Stimulating business
development: another role
for microfinance?

Synthesis

Triodos  Facet

INHOLLAND

Development Policy  Review Network

Colophon

This document reports on the seminar entitled 'The future of Microfinance and Business Development Services in developing countries' organised as part of the process entitled 'Stimulating Business Development: Another side of microfinance?'. This process was carried out within the framework of the Development Policy Review Network (DPRN) and was organised by Triodos Facet and Hogeschool INHolland. With a view to stimulating informed debate and discussion of issues related to the formulation and implementation of (Dutch) development policies, DPRN creates opportunities to promote an open exchange and dialogue between scientists, policymakers, development practitioners and the business sector in the Netherlands. For more information see www.DPRN.nl and www.global-connections.nl .

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Synthesis report on 'Microfinance Institutions and Business Development Services in developing countries'

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Responsible organisations: Triodos Facet and INHolland

Introduction

Currently we are witnessing an unprecedented revolution in development cooperation which is referred to as microfinance. A lot of people maintain that microfinance has improved the lives of millions of people by combating social exclusion. Microfinance is also said to stimulate enterprise development.

However, capital alone may not be enough to stimulate enterprise development. Entrepreneurs also need access to markets and advisory services. Research and experience indicate that providing business development services (BDS) can enhance entrepreneurial performance considerably. Yet, entrepreneurs' access to these services is still limited. The question we therefore have to ask ourselves is *whether microfinance institutions (MFIs) can play a role in improving the access of entrepreneurs to non-financial services?*

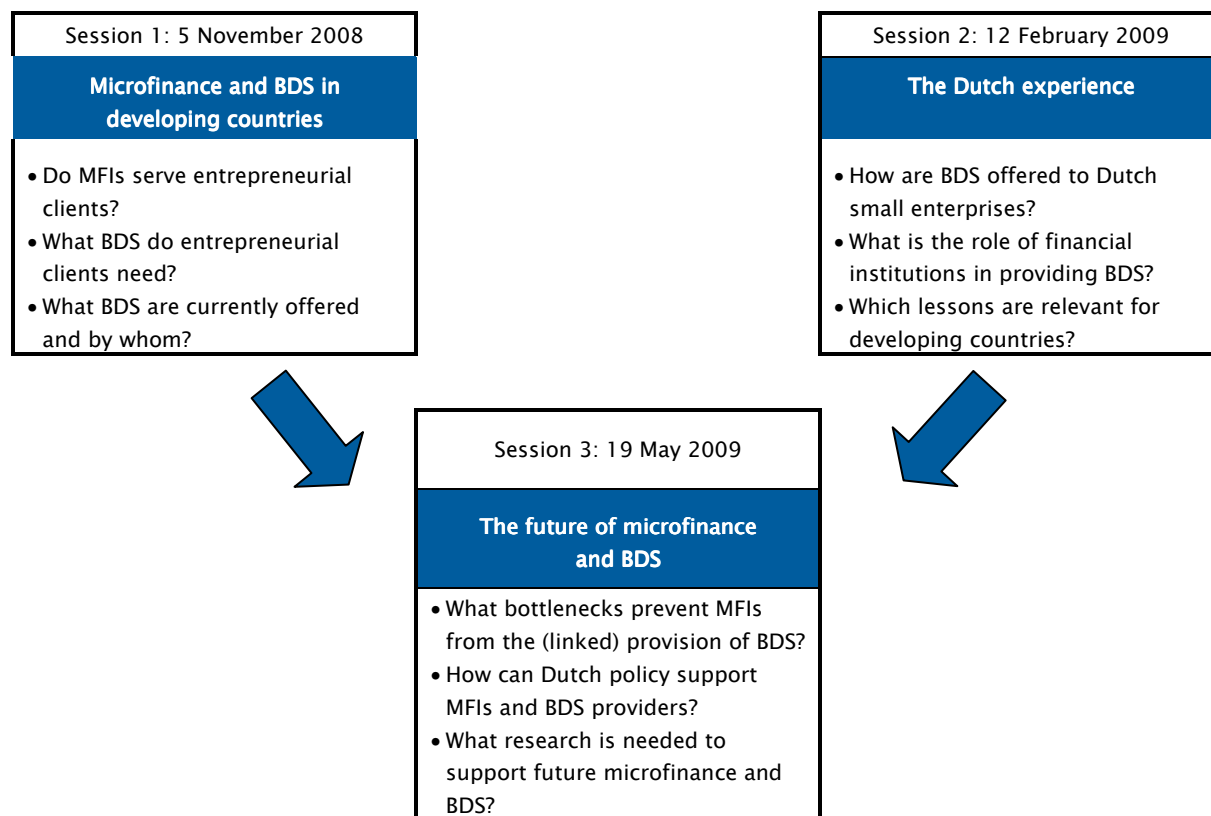
Triodos Facet and INHolland took up this question and organised a one-year process within the framework of the Development Policy Review Network (DPRN), from August 2008 to June 2009. The objectives of this process were:

- To enhance the understanding of the role of microfinance institutions (MFIs) in providing non-financial services or business development services (BDS) to small entrepreneurs;
- To share information, perceptions and experiences between interested researchers, policymakers and development practitioners concerning (i) the needs of small entrepreneurs for non-financial business services and (ii) the potential role (micro)finance institutions can play in providing these non-financial business services; and
- To use the practical experiences in drafting inputs for the Dutch development policy.

The process included a relay system encompassing a series of three seminars and an ongoing web-based discussion. The first and the second seminar focused on the current state of affairs in developing countries and the Netherlands. Experiences from these seminars formed the building blocks for the development of concrete policy recommendations and avenues for further academic research that were discussed in the third seminar.

This report summarises the outcomes of the process as a whole. The three seminar reports on which this synthesis is based can be found on the Microfinance and DPRN websites (<http://microfinance.global-connections.nl>; <http://www.dprn.nl/phase-ii-publications>).

Figure 1 – Overview of the process



Main insights from the process

During the process, the main conclusion that we reached is that we are still talking about small enterprises, microfinance and BDS as if they were homogenous entities. There are various types of small enterprises, with their own particular need for financial and non-financial services. Research should study these differences and policymakers should adapt their policy and activities accordingly. In addition, the following conclusions were formulated:

1. Let's be realistic about microfinance

MFIs offer financial services to a wide variety of clients, with their own particular needs. We should not expect all microfinance clients to develop into successful small- and medium-sized businesses. In most developing countries, the majority of micro-enterprises do not move beyond the survival mode. Just a small group of MFI clients (estimated at about 5 – 10%) have the potential to develop their business into a small or medium-sized enterprise.

2. Linking MFIs with non-financial services

MFIs could provide an interesting distribution channel for non-financial services to clients, as it would help to improve the success of their clients. Yet, MFIs should not be delivering these services themselves because:

- MFIs are financial institutions and generally do not have the capacity to provide non-financial services;
- Financial Institutions should start providing services for which they are held morally responsible (e.g. financial literacy);

- The preferred approach is for financial institutions to establish cooperation networks with BDS providers and – when deemed necessary – refer clients to such service providers;
- The design of the non-financial services should be based on client needs, rather than donor log frames;
- The costs of providing non-financial services should not be included in the costs for financial services.

The example of Grupo ACP, presented at the second seminar, shows that it is possible to offer both financial and non-financial services within a clustered organisation in a commercially viable way.

3. Different types of BDS for different types of clients

We need to define the term ‘BDS’. We can identify three broad categories of BDS, each with their own relevance for a particular type of enterprise.

Client development services	Raising awareness among clients of their basic business or personal (financial) situations. Generally aimed at preventing harmful situations (e.g. over-indebtedness, unhealthy environments). Clients are in survival mode and generally not willing to pay for these services.
Entrepreneurship development services	Helping individuals to start their own business and raising awareness on entrepreneurship as a career choice, plus basic business skills training. Clients are aspiring to set up a business from a positive choice, not so much out of necessity.
Business development services	Supporting existing small businesses to improve their operations, with the services ranging from business advice to technical skills training and linking entrepreneurs to markets.

This categorisation of business development services results in the following differentiation:

		Non-Financial Services		
		Client development Services	Entrepreneurship Development Services	Business Development Services
Microfinance Institution Clients	Small enterprises		<ul style="list-style-type: none"> • Enterprise Education (at vocational training and polytechnic level) • Business Creation programmes 	Management training <ul style="list-style-type: none"> • Business Advice • Technical skills training • Supply chain / market access • Innovation programmes • Sector / market studies • Business associations • Health, safety and environmental advice
	Micro enterprises	Financial Literacy programmes Health, safety and environmental awareness programmes	<ul style="list-style-type: none"> • Enterprise Education (at vocational training level) 	<ul style="list-style-type: none"> • General business skills
	Self employed	Financial Literacy programmes		<ul style="list-style-type: none"> • Adjusted advice • Informal training
	Income Generating for Survival	Financial Literacy programmes		

4. Build capacity for both MFIs and BDS providers

Linking financial and non-financial services to enhance the growth of the small enterprise sector requires interventions at the level of both MFI and BDS providers. Bottlenecks that these institutions face and possible interventions are described in the table below.

Bottlenecks relating to BDS providers	Interventions
BDS providers are limited in number	Train existing entrepreneurs to deliver BDS: entrepreneurs train entrepreneurs
BDS providers often lack quality and do not always understand client needs	Set quality standards and create industry organisations
BDS may not be cost effective; clients may not be willing to pay	Set up a system in which entrepreneurs pay BDS through vouchers

Bottlenecks relating to MFIs	Interventions
MFIs do not have capacity to deliver services other than financial services	Create a referring model in which loan officers link high potential clients to BDS-providers
MFIs can be blamed if BDS leads to business failure; need to avoid conflicts of interest.	Create an institution that assists MFIs in delivering non-financial services
MFIs are constrained by rules and regulations	Provide additional funding to MFIs which are engaged in non-financial services
MFIs have difficulties selecting the high-potential clients who might need BDS	Support MFIs with obtaining a client-focus and help them measure and manage non-financial performance.
MFIs lack good linkages to BDS providers	

5. Conduct applied research on microfinance and BDS

While popular opinions are easy to form, it is quite difficult to make substantial and well-founded statements with regard to microfinance and BDS. There are so many basic questions that still need answers. The table below presents some research avenues for the future.

Research avenues
<ul style="list-style-type: none"> • The impact of BDS on the performance (success rate) of small businesses. • The identification of the most successful type of BDS. E.g. basic skills trainings targeting large numbers versus the more sophisticated tailor-made business advice. • The systematisation of best practices in mixing BDS and microfinance. • The design of a BDS client pre-selection tool with proven selection variables. • The identification of which type of MFI clients really need BDS. • The cost-effectiveness of BDS. • The cost-effective implementation of BDS provision in fragile environments.

Conclusions

Together, the three seminars culminated in a better understanding of the needs of entrepreneurs for non-financial services and the bottlenecks facing both MFIs and BDS providers as regards providing these services in both the Netherlands and in developing countries. In addition to the policy recommendations and listing of future research needs, the process has resulted in a website with a well-documented library-page containing articles on microfinance, business development services and the linkages among them (<http://microfinance.global-connections.nl/content/library>). In order to sustain the outcomes of this seminar series the following suggestions for follow-up can be made:

Firstly, a session could be organised in cooperation with the other institutions organising DPRN processes so that the outcomes of the various DPRN processes can be shared with the Minister of Development Cooperation.

Secondly, academic institutions, such as the INHolland Center for Microfinance, could take up the challenge of dealing with the research suggestions expressed by the seminar participants.

Thirdly, and in relation to the previous point, regular meetings could be organised at which researchers could present the studies which followed from the suggestions raised during the seminars. In the event of such meetings being organised, the seminar series participants should be sent invitations. This will help to sustain the newly established networks and possibilities for cooperation.

Finally, a formal platform could be created at which the collected materials on microfinance and business development services are maintained and updated. The INHolland Center for Microfinance and the Netherlands Platform for Microfinance could play a role in the maintenance of these materials.

