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Performance of microfinance institutions in Burkina Faso

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Performance of Microfinance Institutions in Burkina Faso

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Abstract

This study tests the performance of microfinance institutions (MFIs) in Burkina Faso using indicators such as the sustainable interest rate and the subsidy dependence index. The results indicate that MFIs outreach performance remains very low compared with potential demand, and the factors responsible appear to be both the refusal of most MFIs to mobilize local savings and the high costs of supply of microfinancial services. The results also show that MFIs are not viable and sustainable. Their interest rates are kept low and do not allow them to cover all the costs. In addition, the results indicate that MFIs are dependent on subsidies. However, the oldest MFIs and/or institutions providing deposit services have the lowest subsidy dependence index. It is suggested that more attention should be placed on savings mobilization and ceilings on interest rates should be removed in order to allow MFIs to charge sustainable interest rates.

Keywords: microfinance, performance indicators, Burkina Faso

JEL classification: E21, E43, G10, G20

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1 Introduction

In francophone West African countries, particularly West African Economic and Monetary Union (WAEMU) countries,¹ macroeconomic stabilization and structural adjustment policies have been implemented since the end of the 1980s. The liberalization of financial markets—including the restructuring of the banking sector, interest rate deregulation, etc.—is an important component of these policies. It is widely presumed that the liberalization of financial markets may not only lead to a better allocation of financial resources but also to the elimination of inefficient institutions. Indeed, in WAEMU countries, the liberalization of financial markets led to the failure of many commercial banks² and most development banks³ or agricultural banks.⁴ Unfortunately, this was not accompanied by the creation of high-performance financial institutions, particularly in rural and peri-urban areas, that would have taken over after their failure. In any case, there was a low probability that it could be otherwise, see the constant decline of the role of the state within the framework of economic reforms.

The commercial banks are established in towns where the country's wealth is concentrated. Actually, they are mainly interested in medium and large enterprises or in rich households. On the other hand, they avoid doing business with the rural and urban poor, because the costs of supply of microfinancial services are high. In addition, many credit projects were set up. The results of these projects—often excessively dependent on subsidies—are disappointing most of the time.⁵ This led donors to suspend their support to these projects, thus causing bankruptcy for most of them. In addition, there are very dynamic and diversified informal financial institutions, which adapt relatively well to the mainly limited savings and credit needs of poor populations. But, they are generally ill equipped to finance medium- and long-term investments on a substantial scale.

The lack of access to formal financial services in rural and peri-urban areas and the inability of the informal sector to provide sustainable financial services to the poor led to the emergence of innovative financial institutions. These innovative financial institutions, usually labelled under the term 'microfinance institutions', have emerged with the support of government, civil institutions, and donor organizations. Microfinance institutions (MFIs) include member-based savings and credit cooperatives, solidarity credit groups, small credit projects, and credit NGOs. Contrary to banks, which serve exclusively urban elites, MFIs focus on rural and urban poor households and their demand for financial services. Therefore, one understands the increased interest of public authorities in West African countries—particularly

¹ The West African Economic and Monetary Union currently comprises eight countries: Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger and Togo. The common currency of WAEMU countries, the franc de la Communauté Financière Africaine (CFA franc), is issued by a single central bank, the Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO). \$US1 = 700 CFAF.

² A total of 18 commercial banks went bankrupt.

³ Development banks went bankrupt in all these countries, except in Mali.

⁴ Agricultural banks have been liquidated in Benin, Côte d'Ivoire, Niger, and Togo.

⁵ The lack of efficiency of these projects is mainly caused, among others, by weak repayment rates, mismanagement, etc.

WAEMU countries—and various actors (donors, civil organizations, private sector, etc.) that emerged in the recent years for investing in microfinance.

If top priority was given until the mid-1990s to the increase of the number of MFIs in order to provide financial services to the poor on a large scale, a twofold widespread consensus has been reached since the last few years. First, the financial needs of poor populations are structural needs and institutions that target at the poor have to be viable and sustainable. Second, MFIs cannot be successful without the appropriate legal and regulatory framework. In recognition of these premises, in 1994 WAEMU political and monetary authorities set up a legal and regulatory framework.

On the one hand, it was hoped that the liberalization of financial markets and the regulatory measures, by eliminating gross distortions and reducing the cost of service delivery would lead to viable and sustainable MFIs. Indeed, research and studies on financial reforms and regulatory policies have been pointing to the substantial positive effects of such reforms and policies on the microfinance sector in Asia (Gurgand *et al.* 1996; Larrivière and Martin 1998, etc.) and in Latin America (Gonzalez-Vega *et al.* 1997; Ramirez 1998, etc.). On the other hand, it was hoped that these measures, by eliminating faulty or fraudulent microbanking practices, would contribute significantly to institutional sustainability. Some studies (CGAP 1996; Zeller and Sharma 1998; European Commission 1998, etc.) have shown that the liberalization of the financial market as well as the creation of an appropriate legal and regulatory framework led to a healthy microfinancial sector.

However, one can note that in WAEMU countries, the number of MFIs has been growing since the implementation of financial reforms and the creation of the legal and regulatory framework. But it is doubtful whether this implies that they are performing well. For example, the Consultative Group to Assist the Poorest (CGAP) estimates that only about 3-5 per cent of MFIs worldwide are at present financially sustainable. Another 7-10 per cent are expected to become financially sustainable within ten years. The other 90 per cent of MFIs will either fold or continue requiring subsidies (Gurgand *et al.* 1996).

Furthermore, it can be pointed out that since then no evaluation has been undertaken about the performance of MFIs in WAEMU countries. According to various opinions expressed within WAEMU financial and monetary policy and research circles, the liberalization of financial markets and the creation of the regulatory framework have had or should have significant impact on the performance of the microfinancial sector.

To address the above hypotheses and examine the empirical foundations of the above doubts, this study addresses the following questions. Does the fast development of the microfinancial sector in WAEMU countries show that MFIs are performing well? In other words, do MFIs play a significant and increasing role in financial intermediation? Do they succeed in providing the target populations with sustainable financial services on a large scale? To answer these questions, the study confronts data from Burkina Faso, a country whose geographical situation encompasses both the advantages of WAEMU coastal countries and the disadvantages of WAEMU arid countries.

The study includes five sections. Section 1 presents the discussions concerning the evaluation of the performance of MFIs, followed by a description of the methodological approach in section 2. Section 3 and section 4 highlight major findings with regard to

outreach performance and sustainability, respectively. Section 5 provides a summary of conclusions and recommendations that emerged from the study.

2 ‘Welfare studies’ versus ‘institutional studies’

In developing countries, the lack of access to savings, credit and insurance services is among the main constraints facing low-income households and the poorest. This lack of financial services contributes to limiting the ability of the poor to finance their activities, improve their incomes, and have access to basic services such as food, education, medical services, clothing, housing, etc. (Zeller and Sharma 1998). Because commercial banks neglect to provide savings and credit services to them, the poor, at least until the 1950’s, almost exclusively borrowed from informal lenders (Adams and Vogel 1986; Germidis *et al.* 1991; Adams and Delbert 1994, etc.).

In order to mitigate the imperfections of financial markets, microcredit projects were established after the Second World War, thanks to support from governments and donors. The objective was both to reach the greatest number of poor people and to provide them with financial services at a low cost. Since it was widely believed that the key determinant of the poor demand for credit was its costs, these microcredit programmes were largely subsidized. Governments and donors then designed microcredit as part of an integrated programme of poverty alleviation and welfare improvement in favour populations. Their approach was considered to be ‘welfarist approach’ or ‘directed credit approach’. Based on logic of subsidization, this approach led to high unpaid rates and transaction costs, resulting in the failure of many microcredit programmes (Von Pischke *et al.* 1983; World Bank 1989; Yaron 1994, etc.).

Economists from Ohio State University—such as Adams, Cuevas, Graham, Von Pischke, Adams and Donald, etc., experts in rural finance—were among the first to show that most of these credit programmes launched in developing countries have failed. They blame this failure on the fact that these programmes are based on faulty conceptions: (i) the poor are neither creditworthy nor able to save; (ii) credit should be cheap in order to allow small farms and urban microactivities to be profitable enough; (iii) subsidized microcredit may decrease the role of informal lenders which charge high interest rates; (iv) financial transactions on informal financial markets would not be significant, and (v) commercial banks would not operate in rural areas because transaction costs are higher.

According to rural finance experts, each of these assumptions led to ‘worst practices’ which resulted in inefficient and costly policies: (i) low interest rates had often led to gross distortions and mistargeting in services; (ii) subsidized credit constantly encouraged borrowers to engage in less productive activities, and contributed to significantly increased loan losses; (iii) cheap formal credit benefited only rich households, i.e. a tiny proportion of the population; (iv) finally, low interest rates prevented full recovery of transaction costs, and severely affected the performance of financial institutions.

These findings led to a new approach characterized by the will to liberalize financial markets. This new approach strongly influenced financial reforms implemented in

developing countries. Considered as an ‘institutionalist approach’ or ‘financial market approach’, it, above all, focuses on the fact that subsidies led to a worse allocation of financial resources, and to unsustainable institutions. The defenders of this approach (Adams 1985, 1992; World Bank 1989; Gurgand *et al.* 1994, etc.) are seeking to establish first of all institutions, which offer savings and credit services on sustainable and commercial bases. MFIs designed in this way emphasize financial self-reliance and viability. They charge high interest rates, because of high lending costs. The objective is not only to reach large numbers of the poor, but also to do it in a sustainable manner (Gurgand *et al.* 1996; Yaron and Charitonenko 1998; Gibbons and Meehan 1999, etc.).

These two approaches, i.e. the ‘welfarist approach’ and the ‘institutional approach’ still exist. Many MFIs are caught, on the one hand, by their determination to find new sources of external funding to increase their loan portfolio in order ensure their financial viability, and, on the other hand, by their concern to provide service to low-income and poor people, and reconcile their economic and social objectives. This contrasted opposition between two the trends of thought constitutes what is commonly known as ‘microfinance schism’.

This schism is also characterized by the methods to evaluate the performance of MFIs. The ‘welfarists’ measure the performance of MFIs on the basis of ‘welfare studies’ or ‘household studies’. They are interested in MFIs’ impact on the living conditions of the beneficiaries. Welfare studies are strongly criticized by the ‘institutionalists’ because of their subjectivity, their cost and the methodological difficulties they introduce. They would rather deal with ‘institutionalist studies’. They are interested in market variables, such as the repayment rate, transaction costs, the degree of financial self-reliance, etc. The welfarists, in turn, object to the institutionalists because of their failure to take into account the outreach performance as well as MFIs effects on the poor. Therefore, they propose other performance criteria: the number of savings accounts or the number of loans, the improvements in productivity, incomes, capital accumulation, food expenditures, and social services (education, health, housing, etc.).

Today, there is neither an agreed upon nor a widespread definition of a well-performing MFI. The performance criteria and indicators used vary significantly from one author to the next, or from one organization to another, since they depend on the methodological approach, which, in turn, depends on the determination to give priority to the supply side or to the demand side of the financial intermediation.⁶

3 Analytical framework

Since no definition of a well-performing MFI has been able to rally support unanimously, we adopt an approach based on both performance criteria introduced by Yaron (1992b, 1997) and those proposed by CGAP (1996). These authors suggest two key criteria to evaluate the performance of MFIs: outreach and sustainability. It is

⁶ Many authors and organizations have published evaluation methods. For example, PEARLS by the World Council of Credit Unions, the ‘Micro-Rate’ by the Private Sector Initiative Corporation and by UNCTAD, CAMELS developed by ACCION International, performance criteria designed by the Consultative Group to Assist the Poor (CGAP)/World Bank, USAID’s Microenterprise Innovation Project, etc.

important to mention that a great majority of studies are based on these criteria (Gurgand *et al.* 1996; Larrivière and Martin 1998; Gibbons and Meehan 1999).

Outreach is defined as the ability of a MFI to provide high quality financial services to a large number of clients. The indicators of outreach performance are changes in the number of clients, percentage of female clients, the amount of savings deposits, the value of the outstanding loan portfolio, the average amount of savings deposits, the average value of loans, etc.⁷

Sustainability requires MFIs to cover all transaction costs (loan losses, financial costs, administrative costs, etc.) with the return on equity (net of any subsidy received), and consequently to function without subsidies. It is measured by indicators such as the sustainable interest rate,⁸ the quality of loan portfolio, administrative efficiency, staff productivity, and the degree of dependence to subsidies.

In this study, MFIs sustainable interest rate is estimated on basis the model suggested by CGAP (1996).⁹

$$R = [(AE + LL + CF + K)/(1 - LL)] - II$$

R = the annualized effective (or viable) interest rate

AE = administrative costs

LL = loan losses

CF = financial costs

K = the desired capitalization rate

II = investment income.

Dependence to subsidies is measured by the subsidy dependence index (SDI) developed by Yaron (1992b, 1997). The SDI is defined by Yaron (1997) as the ratio which measures the percentage increase in the average on-lending interest rate required to compensate an MFI for the elimination of subsidies in a given year while keeping the return on equity equal to the approximate nonconcessional borrowing cost. SDI is calculated on basis the following formula:

$$IDS = \frac{S}{LP * i} = \frac{A(m - c) + [(E * m) - P] + K}{LP * i}$$

S = total subsidy

A = subsidy on concessional rate borrowing

⁷ Other indicators such as changes in the number of branches or units established, the number of savings accounts, the number of loans, the value of assets, etc. are also used.

⁸ The viable interest rate that an MFI will need to realize on its loans.

⁹ Each variable in this equation is divided by the average outstanding loans, and is therefore expressed as a decimal fraction. For further details, see CGAP (1996).

- m = market (reference) interest rate
 c = concessional interest rate
 E = annual average equity
 P = profit (losses)
 K = miscellaneous grants and benefits
 LP = annual average loan portfolio
 i = lending interest rate.

This analytical framework is confronted with data from a random sample of six Burkinabe MFIs¹⁰ (two member-managed savings and credit cooperatives,¹¹ two group credit institutions,¹² and two credit project and NGOs)¹³ considered as representative of the microfinancial (the different philosophies, approaches and institutional models, localization of institutions, etc.). The sample includes the Federation des Caisses Populaires (FCPB), the Union des Coopératives d'Épargne et de Crédit du Bam (URC-Bam), Promotion du Développement Industriel et Agricole (PRODIA), the Fonds d'Appui aux Activités des Femmes (FAARF), the Association pour le Développement de la Région de Kaya (ADRK) and the Association 'Être comme les Autres' (ECLA). A brief overview of the main characteristics of these institutions is presented in Table 1.

Table 1
Characteristics of selected microfinance institutions

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FARRF	ADRK	ECLA
Date of creation	1972	1989	1981	1991	1969	1991
Geographical coverage (%)	69	02	04	82	07	04
No of branches	102	09	02	45	290	03
Target population	Rural urban	Rural	Peri-urban	Women	Rural	Rural
% women	24	49	58	100	31	35
Average savings (US\$)	72	70	–	–	22	16
Average credit (US\$)	547	548	485	614	75	224

Source: BCEAO/BIT (2001).

¹⁰ The microfinancial sector comprises between 50 and 60 institutions.

¹¹ Savings and credit cooperatives operate on the cooperative principles. They offer both mandatory savings deposits and credit services. Cooperatives also give ownership and control to members.

¹² Group credit institutions focus on women. Most institutions provide credit facilities only. They grant loans, thanks to donor funds.

¹³ The third group of MFIs comprises credit projects and NGOs.

4 Outreach performance

Outreach performance requires microfinance institutions to reach a large public, and to have a significant and increasing volume of activities (savings, credit, insurance, etc.).

4.1 Clientele

MFIs clientele is very heterogeneous, since they target both rural households and urban low-income populations. Urban clients are mainly small traders, micro-entrepreneurs, groups, and associations. Rural clients are small farmers, animal breeders, women, craftspeople, groups, and associations. According to PNUD (2000), poverty in Burkina Faso hits mainly these categories of the population. This makes it possible to assert that MFIs reach the poor populations, and even the poorest.

Women¹⁴ are under-represented in MFIs clientele (see Table 1). They are relatively less represented in the savings and cooperative systems and in the credit projects/NGOs than in the group credit systems. This result can be easily explained. While savings and credit cooperatives, and credit projects or NGOs target all categories of poor people, solidarity credit systems serve almost exclusively women.

As Table 2 shows, MFIs have been characterized by significant growth in the number of their clientele (an average annual growth rate of about 24 per cent). This finding, however, reveals an uneven progress. For example, the number of female clients increased less rapidly (average annual growth rate of about 9 per cent). The number of members of savings and credit cooperatives grew at an average annual growth rate of nearly 20 per cent, against 14 per cent for the clientele of group credit institutions and 7 per cent for the number of clients of other institutions (projects and NGOs). In 2000, the total number of MFIs clients stood at 497,000, representing 8.3 per cent of the target populations.¹⁵ Despite the rapid growth of MFIs clientele, their outreach remains small compared with the potential demand.

Table 2
Number of MFI clients

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs		Total MFIs
	FCPB	CEC/Z	PRODIA	FARRF	ADRK	ECLA	
1994	68,175	318	537	36,115	8,579	2,500	110,350
1995	82,769	2,862	730	55,256	8,033	2,216	155,951
1996	92,702	7,155	947	69,070	9,965	2,800	170,180
1997	120,000	12,972	1,207	74,706	12,428	2,935	257,944
1998	162,789	15,438	1,028	78,442	13,049	2,955	344,557
1999	196,892	18,801	994	84,717	14,466	2,750	468,446
2000	238,067	22,516	1,092	94,494	15,479	3,328	497,446

Source: BCEAO/BIT (1996, 1998, 2001).

¹⁴ According to UNDP (1999) women are among the poorest.

¹⁵ The number of the target poor clients in Burkina Faso is estimated at around 6 million (BCEAO/BIT 2001).

The largest institution, caisses populaires, accounted for around 48 per cent of all clients. Other small MFIs each served around 2,300 clients (0.01 per cent of all clients). In some areas, there is no intense competition amongst MFIs. However, it is worth revisiting these figures. Most MFIs are still relatively young—the average age nearly 9 years—and in full expansion. It is true that most MFIs cover a small fraction of all target clientele. But if one considers some small areas, one notices that their outreach performance is much more significant. Indeed, there are pockets of the country, where coverage is very high. It may range from 30 per cent in some villages of member-managed village banks to an average of 40 per cent for caisses populaires, and even 60 per cent for some projects and NGOs.

4.2 Financial services provided by MFIs

MFIs offer a very limited range of savings and credit products. Savings products comprise short-term savings (the small amounts the population saves for emergencies and unexpected expenditures) and long-term savings (money the population saves for specific expenses, particularly medium or long-term investments). The average duration of short-term savings is one month. Most MFIs do not pay interest on short-term savings. For long-term savings, the interest rates range between 3 per cent and 5 per cent per year.

MFIs offer mainly two types of microcredit products: short-term individual or group credit, and medium and long-term individual credit. The first type of loan is characterized by (i) the average loan size being between CFAF 5,000 (US\$ 7.14) and CFAF 300,000 (US\$ 428.57); (ii) terms are from six to twelve months; (iii) the interest rates range between 10 per cent and 17 per cent per year in nominal terms). For medium and long-term credit (terms exceed 12 months), borrowers are primarily individual micro-entrepreneurs. The average loan size ranges between CFAF 300,000 (US\$ 428.57) and CFAF 3 million (US\$ 4,285.71). Here also, interest rates, average loan terms as well as loan guarantee systems vary from one MFI to another. In general, savings and credit cooperatives use traditional loan guarantee schemes (physical assets, prize durable goods, etc.), whereas group credit institutions lay emphasis on group-based liability. As far as projects and NGOs are concerned, they have been divided between the two systems.

Table 3
Financial services of the MFIs

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FARRF	ADRK	ECLA
% short-term savings	80	85	–	100	82	85
Savings interest rate	0-4%	3-5%	–	0%	5%	0%
% short-term loans	90	69	73	100	40	82
Lending interest rate	10%	11-17%	17%	10%	10-12%	15%
Average loan duration (month)	12	6 to 12	12	6 to 12	12	6 to 12

Source: BCEAO/BIT (2001).

Savings and credit cooperatives, projects, and NGOs grant loans for productive as well as consumption purposes. Group credit institutions finance exclusively productive and commercial activities. However, on average, more than 70 per cent of loans are given for less than one year which cannot allow the borrowers to use them for long-term investments. Savings deposits are mainly short-term savings (Table 2) that cannot be used to support long-term lending.

4.2.1 Savings and credit

MFIs savings activity is strongly influenced by their philosophical approach and particularly by the choice to focus on the mobilization of local savings or on lending activity. The rapid growth in the number of MFIs clients has led to high levels of savings deposits (Table 4). In effect, deposits significantly increased throughout the years, rising to CFAF 14.9 billion (US\$ 21.28 million) in 2000, compared CFAF 3.8 billion (US\$ 5.43 million) in 1994 (average annual growth rate of 23.7 per cent in nominal terms). The growth of savings deposits was particularly the work of savings and credit cooperatives (average annual growth of 27 per cent). Cooperatives accounted for almost 89 per cent of total amount of savings deposits in 2000. Cooperatives, it must be remembered, give priority to savings in comparison with credit. The increase in savings was very low for group credit systems (average annual growth rate of less than 10 per cent). Group credit institutions as well as projects and NGOs have concentrated mostly on providing credit facilities.

Similarly, FMIs loan portfolio grew significantly (see Table 5). By the end of December 2000, MFIs had granted loans for a total amount of CFAF 17.6 billion (US\$ 25.18 million). The average nominal growth rate was 35.3 per cent per year. Group credit institutions hold the highest record of growth, with a nominal growth of 50 per cent per year, followed by savings and credit cooperatives (average nominal growth of 36 per cent per year), and projects and NGOs (average nominal growth of 20 per cent per year).

Table 4
Value of savings (in CFAF million)

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs		Total MFIs
	FCPB	CEC/Z	PRODIA	FARRF	ADRK	ADRK	
1994	2,564	75	–	51	74	12	3,358
1995	3,861	143	–	47	89	25	5,072
1996	4,687	238	–	58	134	25	6,106
1997	6,529	374	–	343	175	28	8,434
1998	8,394	449	–	412	210	31	11,370
1999	9,889	308	–	421	213	32	12,850
2000	11,259	370	–	434	287	35	14,900

Source: BCEAO/BIT (1996, 1998, 2001).

Table 5
Value of loans (in CFAF million)

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs		Total MFIs
	FCPB	CEC/Z	PRODIA	FARRF	ADRK	ADRK	
1994	961	212	112	33	228	6	2,122
1995	2,048	398	204	296	312	10	3,988
1996	3,959	496	317	719	487	6	6,085
1997	4,862	712	354	1,103	488	15	9,732
1998	6,063	883	361	1,247	498	36	11,229
1999	8,099	546	420	1,624	611	82	15,091
2000	10,228	573	504	1,721	641	172	17,625

Source: BCEAO/BIT (1996, 1998, 2001).

One important observation that can be made from Tables 4 and 5 is that the largest MFI, caisses populaires (FCPB), represents 75 per cent of the total amount of savings mobilized by MFIs and 58 per cent of the total amount of loans granted by all the MFIs. Besides, MFIs represent 4 per cent of the total amount of local savings mobilized by all the financial institutions (MFIs, commercial banks, and other formal institutions) and 2 per cent of the total value of loans granted by all the financial institutions.

5 Sustainability

The sustainability of MFIs depends, among others, on elements such as the structure of interest rates, quality of loan portfolio, staff productivity, financial and administrative costs. We analyse these different elements and the resulting degree of financial and operational self-sustainability.

5.1 Interest rates

The viability of MFIs, and consequently their sustainability, is closely linked to their financial spread. MFIs lending interest rates (12 per cent to 24 per cent per year) are obviously higher than the formal market rate (14 per cent), except for some rare institutions, such as caisses populaires or FAARF. In effect, most MFIs mainly operate in rural and peri-urban areas, often in remote areas, where risks and transaction costs are very high.

Table 5 indicates that MFIs interest rates on loans, although usually higher than bank rates, are not viable. Most MFIs should double, even triple their lending interest rate to cover all the costs. The difference between sustainable lending interest rate and the present lending interest rate is particularly high as far as PRODIA and ECLA are concerned. It must be said that these two institutions do not offer savings services.

Are low-income people and the poorest able to pay for financial services at high interest rates (25 per cent to 44 per cent per year)? From this viewpoint, it can be noticed that a great number of empirical studies have shown that what is most valuable to the poor is

the access to financial services. They are often willing to pay for services at full costs. Besides, one knows that in Burkina Faso, the poor borrow from informal lenders despite their high interest rates. Lending interest rates on the informal financial market can reach 50 per cent, or even more, for a few of months (Tapsoba 1982; Ellsasser 1992; Nguyen *et al.* 1998).

Table 6
Interest rates (%)

	Savings and credit cooperatives		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FAARF	ADRK	ECLA
Lending interest rate	10	15	17	10	12	15
Sustainable interest rate	11.85	31.25	42.34	25.12	23.76	44.19

5.2 Quality of loan portfolio

In order to supply their services on a sustainable basis, it is imperative that MFIs maintain high repayment rates. Failing to maintain the quality of their loan portfolio can affect their efficiency.

Table 6 shows that all the MFIs studied have quite high repayment rates. Usually, they add up to more than 91 per cent, even 99 per cent to 100 per cent for some. For group credit institutions such as PRODIA and FAARF, these high repayment rates appear to be closely linked to group loans and to the use of group-based liability.¹⁶ These mechanisms are particularly adapted to small borrowers, especially women who generally lack traditional collateral-suitable assets.

Table 7
Rate of loan recovery (%)

	Savings and credit cooperative		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FAARF	ADRK	ECLA
1994	93	96	97	98	95	100
1995	98	97	95	97	99	100
1996	99	97	95	93	91	100
1997	97	96	96	95	97	100
1998	94	91	94	94	96	99
1999	99	90	92	95	97	100
2000	98	95	94	96	96	100

Source: BCEAO/BIT (1996, 1998, 2001).

¹⁶ Through the mechanism of solidarity guarantee (or 'peer monitoring'), in case of failure to repay, every member of the group is responsible for the debt contracted by one of them. With this mechanism, pressure within the group can be high and constitutes an efficient means of encouraging the repayment of loans (Hoff and Stiglitz 1993).

Savings and credit cooperatives (FCPB and CEC/Z) as well as projects and NGOs (ADRK and ECLA) also experience very high repayment rates. Repayment rates are higher in savings and credit cooperatives because a strong sense of ownership is maintained. The performance of projects and NGOs is due to the fact that they intervene on a small scale and they can, in this way, follow-up and monitor borrowers who might encounter difficulties in repaying their loans.

5.3 Administrative expenses

The sustainability of MFIs also depends on their capacity to minimize transactions costs, especially administrative expenses. According to Christen (1997), the norms of 'optimal practices' assume that well-managed MFIs should be able to maintain the ratio of administrative expenses to transaction costs between 15 per cent and 25 per cent.

Table 8 indicates that none of the case studies is administratively efficient. According to BCEAO/BIT (2001), the average administrative expenses of the cooperative systems, solidarity credit systems and projects in 2000 were respectively 33.1 per cent, 48.4 per cent and 39.4 per cent, respectively. Savings and credit cooperatives are more efficient than the other microfinancial systems. One may assume that this difference comes from the fact cooperatives massively use voluntary staffs (cashiers, elected leaders, etc.).

In addition, it can be noticed that the ratio of personnel expenses rather developed in a jigsaw fashion. The creation of new branches usually leads to a high increase of administrative costs. However, let us note that the rate of administrative costs for FAARF, 61 per cent, is very high. FAARF justifies this high rate through its large geographical coverage, which requires initial important investments in infrastructure and human resources.

Table 8
Ratio of personnel expenditures to transaction costs (%)

	Savings and credit cooperative		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FAARF	ADRK	ECLA
1994	51	35	56	40	43	45
1995	30	34	47	43	40	42
1996	26	37	41	49	39	41
1997	28	33	43	58	34	48
1998	32	26	51	63	36	45
1999	38	29	52	61	36	48
2000	41	20	48	61	32	47

Source: BCEAO/BIT (1996, 1998, 2001).

5.4 Staff efficiency

The most important part of administrative costs is attributed to personnel expenditures. They range between 50 per cent and 70 per cent of the total amount of MFI administrative expenses (Gibbons and Meehan 1999). Therefore, it is essential that

MFIs control their staff efficiency. Staff efficiency¹⁷ is measured through ratios such as the average number of savings accounts or the average amount of savings deposits per employee, the average number of loans per employee or the average value of loan portfolio per employee. Since some MFIs in our sample do not offer savings services, we use the last two ratios.

As far as the average number of loans per employee is concerned, the optimum for MFIs is between 300 and 500 clients (Christen 1997; Gibbons and Meehan 1999). On the other hand, there is no optimal range for the average amount of the loan portfolio per employee, since it depends on the loan methodology used, the level of the clientele's poverty, the economic environment, etc.

Table 9 shows that staff productivity is low. For example, if one considers the average number of loans per employee in 2000, one clearly sees that only one MFI, ADRK, has a ratio that is higher than 300 (i.e., 669 clients). It also has the highest average amount of portfolio per employee. The other MFIs are far from the norm of 300 clients per employee.

Among the main explanations for this low productivity of MFI staff, one can mention the fact that most MFIs are ill equipped in computers and do not have an efficient management information system.

Table 9
Staff productivity

	Savings and credit cooperative		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FAARF	ADRK	ECLA
No of loans per employee	86	110	68	51	669	25
Value of loan/employee	17,000	42,000	23,300	21,600	87,200	3,900

Source: BCEAO/BIT (1996, 1998, 2001).

5.5 Dependence on subsidies

The analysis of the subsidy dependence index for all of the six selected institutions shows a high dependence of MFIs, even the older ones,¹⁸ on subsidies (see Table 10). In 2000, the two savings and credit cooperatives, (i.e., FCPB and CEC/Z) had to raise their lending interest rate by 29 per cent and 136 per cent, respectively, in order to ensure their self-sustainability. To compensate for full elimination of subsidies, the two group credit institutions, PRODIA and FAARF, had to more than double their interest rate on loans. Finally, the SDI of ADRK and ECLA shows that they had to increase respectively their lending interest rate by 185 per cent and 236 per cent to be self-sustainable.

¹⁷ This concerns the 'productive' staff, i.e. field staff (credit officials, cashiers, etc.).

¹⁸ FCPB and ADRK have more 25 years of experience.

These results are consistent with the finding from the analysis of MFIs sustainable interest rates (see section 4.1). It is necessary to raise the lending interest rate in hopes of covering all transaction costs, and even more, to suppress the subsidies.

However, it is important to point out that in the year 2000 the two oldest MFIs, i.e. FCPB and ADRK, had the lowest SDI. Conversely, the youngest MFIs, i.e. FAARF and ECLA, had the highest SDI. From the results, it is evident that there is a correlation between SDI and the age of the institution. It supports the theory that MFIs must be allowed time to become self-sustainable. On the other hand, it appears that savings and credit cooperatives, i.e. FCPB and CEC/Z, which offer obligatory savings have the lowest SDI. This suggests that the mobilization of local savings may help MFIs to ensure their viability and sustainability.

Table 10
Subsidy dependence index (2000)

	Savings & credit cooperatives		Group credit institutions		Projects and NGOs	
	FCPB	CEC/Z	PRODIA	FAARF	ADRK	ECLA
1 Market interest rate = m (%)	14	14	14	14	14	14
2 Subsidies on concessional borrowing	00	00	17	313	52	33
3 Annual average equity = E (millions CFAF)	1801	487	495	1328	263	45
4 Subsidy on equity = $E*m$ (millions CFAF)	252	68	69	186	37	06
5 Miscellaneous grants (millions CFAF)	375	33	73	99	30	14
6 Profit (losses) = P (millions CFAF)	496	-05	09	323	71	01
7 Total subsidy = $(2)+(4)+(5)-(6)$	131	106	150	275	48	52
8 Interest income = $LP*i$ (millions CFAF)	457	78	72	126	56	22
9 Subsidy dependence index = $(7)/(8)$	29%	136%	208%	218%	86%	236%

6 Conclusions, recommendations, and research questions

Among the key findings that emerge from the study, we can point out the following:

- *Reaching the poor on a large scale remains a challenge for FMIs:* Despite the rapid growth of MFIs in recent years, their outreach remains very small compared to the potential demand. About 92 per cent of the 6.5 million of poor households in Burkina Faso have not been reached. One also notes that, with few exceptions (savings and credit cooperatives and some NGOs), MFIs have focused mainly on providing short-term credit services. In addition, MFIs do not offer other financial services such as micro-insurance and money transfers.
- *Savings mobilization leads to better self-sustainability:* savings and credit cooperatives succeeded in mobilizing an important volume of savings deposits. They have the lowest subsidy dependence index because the mobilization of savings provides them with inexpensive and sustainable source of funds for lending. The other microfinance systems, and particularly group credit institutions which do not provide deposit services, have the highest subsidy dependence rates. Savings mobilization, therefore, is an indispensable element for a well-performing MFI.

- *MFIs have a high quality loan portfolio*: All the microfinance institutions have high repayment rates. This constitutes proof that the low-income populations and the poorest are a good credit risk when loan guarantee schemes are well adapted.
- *MFIs are not self-sustainable*: All the MFIs in Burkina Faso, including the largest and the oldest institutions, depend on subsidies. MFIs interest rates are kept low and do not allow them to cover all the transactions costs (administrative cost, financial costs, loan losses, etc.). They are administratively inefficient. As the subsidy dependence index indicates, MFIs, even the oldest, rely from subsidies from donor organizations. This result indicates that building a sustainable MFI requires a long-term effort, some patience, and outside support. Outside support is particularly needed for institution building (training, information and sensitizing, etc.) as well as for the creation of new branches or the development of innovative products.

In view of these findings, the approach to improve the performance of MFIs calls for:

- *More attention should be placed on savings mobilization*: The potential demand for microfinance is large. Demand concerns credit facilities, savings services, insurance services, etc. To reach a large number of the poor, MFIs need to concentrate on providing all these financial services. Savings mobilization particularly must receive an adequate attention because it provides MFIs with a sustainable source of funds for lending. In addition, MFIs should establish strong partnerships with commercial banks in order to attract additional financial resources for lending. They should also negotiate funds for long-term lending with local and external partners.
- *MFIs should adopt efficient management information systems*: MFIs, even the smallest, have reached a level of operation that requires adequate management information systems (MIS). Using efficient management information software as well as other innovative banking technologies (credit scoring technology, smart card operations, Internet, etc.) can contribute to a reduction in administrative costs, an increase in staff productivity, and improvement in the reliability of accounts. While using new technology can be strongly beneficial for MFIs, it is equally true that it introduces additional costs, which can handicap their performance. Furthermore, using technology requires some capabilities. Thus it is the MFIs' responsibility to identify the best practices as well as cost-effective ways to use new technology to improve outreach, efficiency, and client satisfaction, which are becoming requirements of viability and sustainability in an increasing competitive micro-finance sector.
- *Ceilings on interest rates should be removed*: The legal and regulatory framework should be more flexible. Ceilings on interest rates should be removed and MFIs should be allowed to charge competitive interest rates.
- *Subsidies should be degressive*: For recent experiences or the creation of new branches, it is not abnormal for operating costs to be subsidized. This being said, viability objective necessarily implies that these subsidies must be decreasing and cover only a percentage of administrative costs (for example, 80 per cent the first year and 60 per cent the second year and so on and so forth). In effect, it is important that subsidies benefit to MFIs which make gradual efforts to attain financial and operational self-sufficiency.

- Finally, experience indicates that, apart from the level of outreach and the degree of self-sustainability, the performance of MFIs depends, among others, on the managerial efficiency, the social and economic environment, the linkages between MFIs and the other various development actors, and the impact of MFIs on the livelihood for the poor. It is important to consider these issues that need further research.

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