Microfinance and Poverty Reduction in Nigeria: A Case Study of LAPO Microfinance Bank

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The candidate confirms that the work submitted is her own and that appropriate credit has been given where reference has been made to the work of others.

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Oluwatomi Ehagbor Owolabi

To my adorable parents – Augustine and Febisola Owolabi

and my darling husband - Emmanuel

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Abstract

From a contextual and service users' perspective, this thesis investigates the poverty reducing effect of microfinance including the implementation processes and features of microfinance. Poverty is in this study conceptualised as 'capability deprivation' so that poverty reduction is achieved through improved capabilities for the poor. The literature review on microfinance begins with an attempt to locate the reasons for microfinance within the context of the finance-development and credit rationing literature. It also recognises the institutional-based approach to understanding the exclusion of the poor; and recognizes the role of lending group and social relations within the group in shaping individual and social capabilities of the poor. Next, it reviews some of the recent discourses in the microfinance literature. It uncovers a call in the literature for studies that look beyond impact to evaluate the features and characteristics of microfinance delivery and use from the clients' perspective. The central arguments of this thesis include: (i) the utility or disutility of microfinance stems from the features of microfinance and its implementation strategies, as well as clients' practices. (ii) The microfinance literature has not paid enough attention to the perspectives of service users, which can adversely affect microfinance assessments and its potential for poverty reduction. The study examines LAPO microfinance intervention in semi-urban and urban areas in Edo State, Nigeria. Given the research objective, design and methods, data collection and analysis were guided by the Interpretive, Capability and Poverty Participatory Assessment approaches. The mixed methods approach is selected as the most appropriate for addressing the research questions. Secondary data as well as primary data sourced from 35 interviews and 62 questionnaires were employed. Data analysis was conducted using qualitative, frequency distributions, cross-tabulations, Logit and OLS regression analysis. This study finds that service user perceptions of poverty place value on a stable source of livelihood, and the ability to meet basic material household needs. Hence, poverty reduction is measured as increased household capabilities as well as the increased ability to achieve successful business outcomes. The findings show that service users' perceptions affirm the poverty reducing effect of microfinance. It also confirms the proposition that the various implementation processes and features of microfinance have unique effects on service users with differing potential for good or harm. The use of trust and personal relations as criteria for selecting group members, as well as the use of an individual guarantee to insure against risk due to imperfect information, suggests the possibility of exclusion. Heterogeneity in groups as well as low *monitoring levels leave service users exposed to greater risk of moral hazard. Peer support enables service users to share ideas and build social networks vital to the success of their businesses and for raising social capital important for combating poverty. Despite the potency of the threat of social sanctions in enforcing repayment, the actual implementation of social sanctions and peer pressure comes at a cost to service users, including damaging social relations. While the targeting of women fosters their empowerment, the labelling of microfinance as a pro-women initiative has the potential to reinforce rather than challenge the prevailing gender bias in the Nigerian society. As regards loans, high repayment burden arising from the use of dynamic incentive creates the potential for harm. The use of savings as loan guarantee against peer defaults also has a similar effect. Although service users affirm the role of savings and non-financial services in the expansion of capabilities, the obscurity surrounding the access to some of the more criteria-determined non-financial services, is found to be damaging to service users' experience. Hence, this study argues that while there are some links between poverty reduction and microfinance, these two are complexly related.*

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List of Abbreviations

APR	Annual Percentage Rate
BRAC	Bangladesh Rural Advancement Committee
CA	Capability Approach
CBN	Central Bank of Nigeria
CGAP	Consultative Group to Assist the Poor
CSO	Client Support Officer
EFInA	Enhancing Financial Innovation and Access
EIR	Effective Interest Rate
FINCA	Foundation for International Community Assistance
FSS	Financial Systems Strategy
GDP	Gross Domestic Product
HDI	Human Development Index
ILO	International Labour Organisation
LAPO	Lift Above Poverty Organisation
MDGs	Millennium Development Goals
MFIs	Microfinance Institutions
NACB	Nigerian Agricultural Cooperative Bank
NBS	National Bureau of Statistics
NGN	Nigerian Naira
NGOs	Non-Governmental Organisations
OLR	Ordered Logit Regression
PCA	Principal Component Analysis
PPA	Participatory Poverty Assessment
PPP	Purchasing Power Parity
RCT	Randomised Control Trial
RESP	Respondent
ROSCA	Rotating Savings and Credit Association
SAP	Structural Adjustment Programme
SE	Social Exclusion
SHG	Self Help Group
SME	Small and Medium Enterprise
SSA	Sub-Saharan Africa
THPCE	Total Household per Capita Expenditure

UN	United Nations
UNDP	United Nations Development Programme

CHAPTER ONE

GENERAL INTRODUCTION

1.1 INTRODUCTION AND STATEMENT OF THE RESEARCH PROBLEM

For many developing countries, microfinance continues to be considered as a very important instrument for poverty reduction. The widely held assumption is that providing financial services to poor households enables them to become micro entrepreneurs, accumulate savings, improve their income, smooth consumption, manage risks and eventually escape the vicious cycle of poverty. Yet, there is great controversy as regards the poverty reducing effect of microfinance. Critics argue that microfinance has not improved incomes, but has led to increased indebtedness of the poor, even leading to suicide in some cases (Reed, 2013). It is safe to say that the discourse in the literature has moved beyond the criticism that the reality is at odds with the ‘purist approach to microfinance’, as it is now widely accepted that microfinance is not the ‘miracle’ it was claimed to be. However, the international development community remains optimistic about propagating microfinance as an effective tool for poverty reduction, and it appears that it is here to stay as a proclaimed sustainable instrument for poverty alleviation. This relies on the claim that microfinance has shown huge success in effectively and efficiently providing sustainable financial services to the poor who are otherwise excluded from mainstream financial services (Johnson and Rogaly, 1997; Armendariz de Aghion and Morduch, 2005; Copestake et al., 2005). With these different viewpoints, a sober reflection would be to ask the question: does microfinance actually reduce poverty?

Moving forward, the body of literature to which this study is designed to contribute towards is the recent call to approach the delivery and evaluation of microfinance from the clients’ perspective and vantage point. Particularly, this body of work surrounds three recent debates which the researcher identifies to be very relevant for advancing the discourse on microfinance and poverty reduction. These include: (i) the literature on the recent client indebtedness that plagued the microfinance industry; (ii) increasing empirical evidence that the perceived positive impact of microfinance on poverty reduction is not been realized; and (iii) the call for a wider focus on inclusive finance. As introduced briefly in this chapter and explored more deeply in chapter 3, this body of work has led to an increasing call for studies that look beyond impact to evaluate the features and characteristics of microfinance that have the potential for poverty reduction from the clients perspective.

There are different components or features of microfinance that affect clients experience as regards the poverty reducing effect of microfinance. Some of these features may be client-related, supply-related, product-related and context-related. Hence, while this study evaluates the potential of microfinance to reduce poverty, it particularly explores the poverty reducing effects of the various features of microfinance delivery and use, from the clients' perspective. This chapter presents a general introduction to the poverty and microfinance discourse as adopted in this study, as well as to the study's justification, objectives, methodology, and conceptual framework. It also sheds light on the scope and limitations of the methodology applied therein, regarding a comprehensive understanding of poverty and microfinance in Nigeria.

1.2 DEFINITION OF KEY TERMS

Poverty is generally seen as a state of lack or deprivation. This includes lack of monetary and non-monetary resources to meet basic needs (World Bank, 2012); deprivation in choices, opportunities and the capability to better one's life (Sen, 1985, 1997, 1999); and deprivation in the capacity to participate effectively in society (Townsend, 1999; Chambers, 1994). For contextual and relevance purposes, this study applies Amartya Sen's capability approach to the analysis of poverty[1]. Here, poverty is conceptualised as 'capability deprivation' so that poverty reduction is achieved through improved capabilities for the poor. The capability approach to poverty emphasises the reduction of capability deprivation through the expansion of valuable 'freedoms' and 'ability' to live valued lives in terms of realizing human potential. It therefore places emphasis on identifying and prioritizing the freedoms that people value.

Turning attention to the subject of microfinance, it is important to begin by distinguishing the focus of this study – 'microfinance', from the original root word 'microcredit' – which refers to small loans. In recognising this departure from microcredit, Armendariz and Morduch (2005, 2010) define microfinance as additional efforts beyond microcredit to 'collect savings from low-income households (LIHs), and in some places to help in distributing and marketing clients outputs'. Particularly,

[1] See Chapter 2 for a detailed discussion on the justification for this conceptualising of poverty as capability deprivations.

they base this distinction on three key factors – the service (s) provided; the focus in terms of clients and objective; and the providers of these services.

> 'Microcredit was coined initially to refer to institutions like the Grameen Bank that were focusing on getting loans to the very poor. The focus was explicitly on poverty reduction and social change, and the key players were NGOs. The push to microfinance came with recognition that households can benefit from access to financial services more broadly defined and not just credit for microenterprises. With this came an orientation towards the less poor households and toward the establishment of commercially oriented, fully regulated financial entities (Armendáriz de Aghion and Morduch, 2010:15).

Microfinance is defined as the 'provision of financial services to low-income people' or more generally referred to as 'a broad set of financial services tailored to fit the needs of poor individuals' (CGAP, 2013). Similarly, microfinance has been defined as

> 'small-scale financial services—primarily credit and savings—provided to people who farm or fish or herd; who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages or commissions; who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban (Robinson, 2001: 9)

An additional literature that has also shaped the definition of microfinance in this study is the work of Ledgerwood (1999: 1) where she defines microfinance as 'the provision of financial services to low-income clients'. According to her, these financial services generally include credit and savings but may also include insurance, payment services, social intermediation such as development of self-confidence, training in management capabilities and financial literacy among group members. As she notes, 'the definition of microfinance often includes both financial and social intermediation'. Based on these definitions, microfinance for the purpose of this study is defined as the provision of small units of financial (e.g. credit, insurance, remittances, savings) and non-financial services (e.g. financial education, health education, skill acquisition etc.) to the economically active poor who lack access to mainstream financial institutions, with the use of innovative techniques (e.g. dynamic incentives, group lending, pre-loan savings, frequent repayments)[2].

[2] See Chapter 3 for a detailed discussion on the justification for this conceptualising of microfinance.

Drawing on the seminal work of Lancaster (1966: 133) who rejected the 'traditional approach that goods are the direct objects of utility and, instead supposing that it is the properties or characteristics of the goods from which utility is derived', this study emphasizes the need to examine the properties and characteristics of microfinance and their contribution to poverty reduction. Hence, the goal is to evaluate the effectiveness of microfinance in increasing the capabilities of the poor in Nigeria, paying close attention to the effect of the different features and implementation processes of microfinance from the clients' perspective. Given this objective and the specified definition of microfinance in this study, any commercially oriented and fully regulated financial entity, that provides small-scale financial (beyond credit) and non-financial services to low-income clients will meet the criteria for the selection of the case-study microfinance institution (MFI)

1.3 JUSTIFICATION OF THE STUDY

The increasing number of the extreme poor in Nigeria has led to a widespread use of microfinance; as it is increasingly prescribed to have huge potential for poverty reduction (Cons and Paprocki, 2008; World Bank, 2012). Nigeria is a typical example of a country that mirrors the situation in Sub-Saharan Africa (SSA) in terms of high population growth, high poverty rates, dominant and growing presence of microenterprises, and expanding microfinance industry (Bateman and Chang, 2012). With the current widespread use of microfinance in SSA, and an increasing focus on how best to financially serve the poor, it becomes imperative to ask whether microfinance is beneficial or harmful to the poor. While research on providing financial services to the poor in Asia has been vital to the microfinance literature, the poverty reducing effect of microfinance in SSA is less documented. And while microfinance interventions in Kenya and Uganda have been well documented, evaluation of microfinance in Nigeria is far less well documented. While there exists a lot of anecdotes providing evidence on how microfinance has transformed the lives of the poor in Nigeria, evidence from rigorous contextual studies has been scare. Whilst celebrating the increased access to finance recorded in Nigeria over the last 5 years[3], it is important to investigate microfinance interventions and their potential for poverty reduction.

This concern becomes more valid when we consider three of the most recent debates in the microfinance literature. The first is the call for a shift to a client-focussed

[3] See chapter 4 for a detailed discussion on access to finance in Nigeria

approach to microfinance following a number of devastating sub-prime microfinance meltdown and the recent client over-indebtedness that rocked the sector (Bateman and Chang, 2012; Sinclair, 2012; Harper 2011 and Klas, 2011). Reviewing the state of microfinance following these happenings and in a bid to determine the way forward, various stakeholders during the 2012 and 2013 microcredit summit campaign called for a refocus on product design and delivery approach which appropriately takes account of client needs and characteristics. This includes the need to understand the contextual factors that influence the financial behaviour of the poor; and which financial services they need and which benefit them the most, why and for what purposes (Reed, 2013; Maes and Reed, 2012).

The second is the growing concern that the perceived positive impact of microfinance has not been realised. This includes increasing evidence from more rigorous randomised control trials (RCTs) that questions the much anticipated positive impact of microfinance on poverty (Banerjee et al., 2009; Karlan and Zinman, 2009). A review of some of the more recent systematic reviews (Pande et al., 2012; Stewart et al., 2010, 2012; and Duvendack et al., 2011) of the impact studies on microfinance shows a call for a look beyond the impact of microfinance. Particularly, based on findings from a systematic review of 15 impact studies in SSA, Stewart et al., (2010) call for more empirical studies to investigate the features and characteristics of microfinance that have the potential for both good and harm; and that this should be taken into account when promoting the use of microfinance in SSA. In a later study, Stewart et al., (2012) recommends that future research can gain more value by identifying how, and under what circumstances do microfinance interventions benefit the poor.

The third is the call for a wider focus on inclusive finance. This body of work highlights the diverse financial service needs of the poor, and the diverse situations in which they work and live. It also raises awareness about the immense diversity of financial institutions that serve the poor in developing countries. While informal financial service providers are known for their convenience and flexibility (Ledgerwood et al., 2013), they can however be highly unreliable and insecure. On the other hand, regulated and supervised formal financial institutions such as commercial banks, state banks, microfinance banks, agricultural development banks, and non-bank formal financial institutions, offer a broader range of financial services. However, they have showed reluctance in adopting social missions, and due to high operation costs, often cannot deliver services to the poorest of the poor.

Alongside this institutional dimension of the discourse is the idea that the poor need a wide variety of financial services as borrowers have different sets of characteristics and needs (Bauchet et al. 2011). This dimension of the discourse sits well with the earlier debates presented and is relevant to the call for a client-focused approach to the evaluation and delivery of microfinance. This is one that accounts for the diverse needs of the poor and recognises that not all products/features will be beneficial to all clients all the time. Additionally, in order to generate improved products and services that flexibly and reliably serve the poor, we need to understand their experiences with the products they are currently exposed to and identify the features and characteristics of microfinance that have the potential for both good and harm. It ultimately argues that financial products and institutions need to mature in ways that accounts for this diversity; and that this requires that financial institutions be leveraged in a consolidated way to increase the financial inclusion of the poor.

The above review exposes a gap in the literature. This is the need for studies that look beyond impact to investigate the poverty-reducing potential of the features and characteristics of microfinance delivery and use from the clients perspective. Most studies that attempt to investigate the features of microfinance intervention focus on individual components like loan structure, loan repayment frequency, dynamic incentive, interest rate, savings and group lending technique (Stiglitz, 1990; Aghion, 1999; Ghatak and Guinnane, 1999; Marr, 2002; Ahlin and Townsend, 2007; Fischer and Ghatak, 2010). These studies often assess microfinance interventions from the viewpoint of MFIs rather than microfinance users. Particularly, the focus is usually on the innovative lending techniques and implementation strategies that enable MFIs to profitably provide microfinance to the poor and achieve high repayment rates. This has led to a disjointed understanding of how MFIs operate and the resulting effect on poverty. Overall, there is a dearth of studies that evaluate microfinance as a whole from the perspective of service users.

In all, there is an overall dearth of studies investigating the link between microfinance and poverty reduction in Africa, and Nigeria particularly. While there exists a lot of anecdotes providing evidence on how microfinance has transformed the lives of the poor in Nigeria, evidence from rigorous contextual studies has been scare. Whilst celebrating the increased access to finance recorded in Nigeria over the last 5 years[4], it is important to investigate microfinance interventions and their potential for poverty reduction. Nevertheless, poverty is a multidimensional concept and so is its reduction. Hence, in line with other studies, this study recognizes that microfinance is not a panacea to lift the poor out of poverty. Rather, it is only one of many factors that can contribute to poverty alleviation.

1.4 AIMS AND OBJECTIVES OF THE STUDY

The overall aim of this thesis is to examine the potential of microfinance for poverty reduction from the clients' perspective. The specific objectives of this study include:

- To identify the capabilities that microfinance clients in the Nigerian context value and have reason to value
- To evaluate the implementation processes and features of microfinance interventions, and their effects from the viewpoint of service users
- To evaluate the effectiveness of microfinance as a tool for poverty reduction.
- To investigate clients microfinance practices and their effect on the expansion of capabilities

In order to achieve these objectives, this study defines and addresses certain key questions:

- How do microfinance clients perceive poverty, and what capabilities do they value and have reason to value?
- What are the experiences of clients with microfinance (features and their implementation processes)?
- How do the poor assess the ability of microfinance to spur the expansion of capabilities for the poor?
- What borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor?

1.5 RESEARCH METHODOLOGY

Research methods tend to be defined along the qualitative /quantitative divide. This study applies a mixed method approach (Robson, 2002) that is not limited to a single method of social enquiry, but rather a combination of the qualitative and quantitative method in understanding social reality (Hentschel, 1999; Bamberger, 2000; Creswell,

[4] See chapter 4 for a detailed discussion on access to finance in Nigeria

2003). The idea is to prioritize the research objectives and to apply appropriate methodological techniques to achieve the objective regardless of what side of the divide the method belongs (Patton 1990; Creswell, 2003). In achieving research objectives 1 and 2, qualitative research methods in the form of semi-structured interviews and participant observation are used to collect survey data reflecting clients' experience with microfinance, as well as their perception of poverty including what capability dimensions they value and have reason to value. Systematic content analysis is employed in identifying and coding recurring themes, analysing existing links, and finally interpreting what the findings means as regards achieving the research objective.

On the other hand, quantitative research method is employed to achieve objectives 3 and 4. This includes the construction of a questionnaire to generate data reflecting clients' evaluation of the poverty reducing effects of microfinance as well as clients microfinance practices. Empirical analyses including frequency distribution and contingency tables, logit and OLS regressions, and multivariate data reduction econometric techniques are employed in analysing the quantitative data. This enables us to evaluate what capabilities have increased, for whom; and what borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor. The qualitative and quantitative findings will be used to provide reliability checks and complement each other.

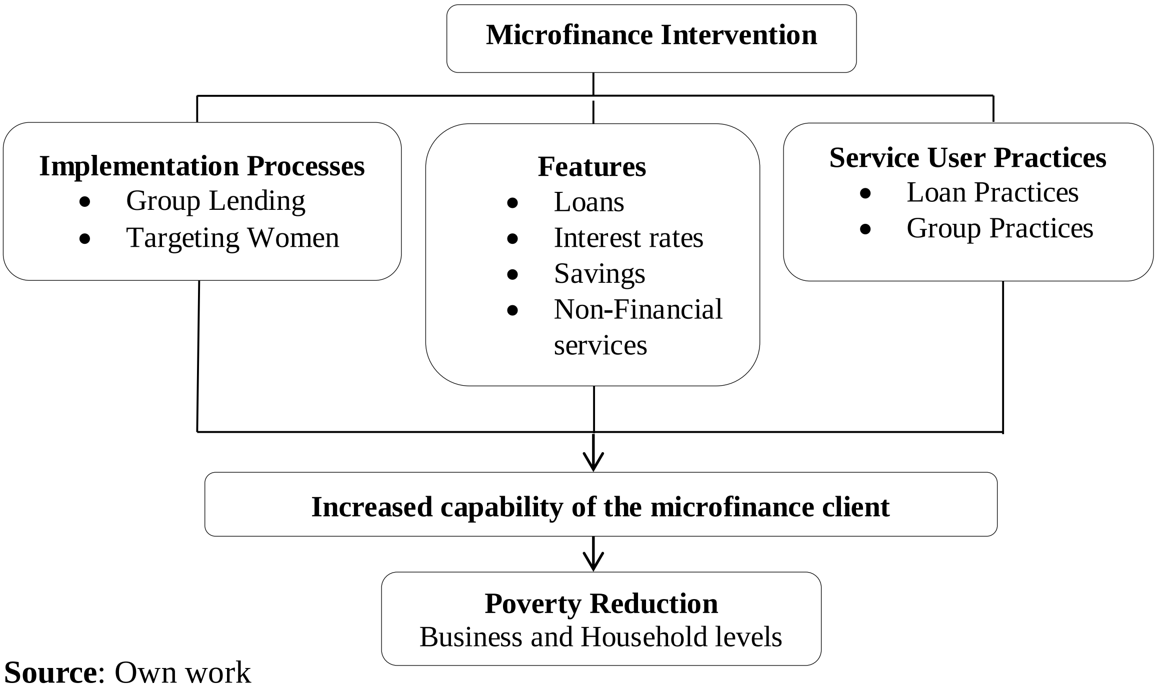
1.6 SCOPE AND LIMITATIONS

While the emphasis on the context of the research may constitute strength to the study, this, as well as its restriction to a single MFI, limits the generalizability of the results. A more comprehensive nation-wide study is thus required to validate the findings. The researcher is also limited by time and resource constraints, as well as the perception of respondents about the major concepts inquired and their willingness to provide reliable information. It is important to mention that this study covers microfinance clients who are served through the group practice with an implicit or explicit sense of joint liability. It does not cover the experience of clients who are able to do without this social collateral as they are considered to be less poor.

1.7 CONCEPTUAL FRAMEWORK

Given the conceptualisation of poverty and microfinance in this study, Figure 1 presents a diagrammatic representation of the framework that depicts the proposed relationships and intermediating factors studied in this thesis.

Figure 1.1: Conceptual Framework



Source: Own work

1.8 STRUCTURE OF THE THESIS

In order to achieve the set out objectives, this thesis consists of seven other chapters.

- Chapter two presents a review of the literature on poverty. It reviews the various approaches to poverty as well as the unresolved issues in the existing literature. It concludes with a presentation of the conceptualization of poverty applied in this study.

- Chapter three begins with a review of related microfinance theories that point to the imperfection of financial markets and the implication for the poor. This is followed by a review of the changes in the conceptualisation and implementation of microfinance. It reviews the transition from the early focus on microfinance as a poverty reduction tool to the new focus on a commercialised microfinance and discusses the key features of this new microfinance model. Next, it presents a review of the literature on key components of microfinance interventions and their effect on poverty with supporting empirical evidence. Finally, it presents the conceptualization of microfinance used in this study.

- Chapter four introduces the discussion of poverty and microfinance in Nigeria. It highlights how the different approaches to poverty manifest in Nigeria, the increasing size of the growing poor population as well as the financial exclusion of the Nigerian poor. This is followed by a look into the practice of microfinance in Nigeria and an introduction to the case study for this analysis, Lift above Poverty Organisation (LAPO) MfB.

- Chapter five presents the analytical framework and research methodology that guides the rest part of the thesis. It begins with discussing the research approach and the theoretical frameworks that guide their implementation. Next, it discusses mixed methods as an appropriate methodological framework consistent with the research approaches selected. This is followed by a description of the fieldwork exercise beginning from the selection of the study area to the collection of the required data. Finally, the techniques for analysing the research data are presented.
- Chapter six answers the questions: How do microfinance clients perceive poverty – what capabilities do they value? What is their evaluation of the implementation processes and features of microfinance; with particular attention to their potential for harm or good? In general, what role does microfinance play in the lives of the poor? It investigates clients' experience with group lending and women targeting as implementation processes on the one hand and then loans, interest rates, savings and non-financial services as features of microfinance on the other. The final section consists of an analysis of clients' perception of poverty and the capabilities that they value.
- Chapter seven evaluates the effectiveness of microfinance, as well as clients' microfinance practices in the expansion of capabilities. In order to achieve these objectives, this chapter addresses the questions: how effective is microfinance in enabling the expansion of capabilities? What borrower-related microfinance practices are better associated with higher expansion of capabilities? It evaluates the effectiveness of microfinance in poverty reduction at the business and household levels using frequency tables and cross-tabulations to explore variations across clients' demographics. This is followed by a regression analysis of clients' group and loan practices on one hand and poverty reduction on the other.

- Chapter eight contains the concluding section of this thesis. It draws together the implication of the study, specifically how the findings throws light on the role of microfinance in poverty reduction, what policy implications can be drawn as well as areas of further research.

CHAPTER TWO
POVERTY

2.1 INTRODUCTION
Poverty remains a perpetual challenge for all societies, and has regularly been followed by widespread efforts to provide inclusive financial systems to cater for the poor. Although an income based poverty line is generally used in measuring poverty, one important component of these attempts both at national and international levels is the continuous debate over what poverty means. A more recent understanding of poverty is the idea that poverty is multidimensional in nature. This calls for a shift from a one-dimensional income based measure to a multidimensional understanding and approach to tackling poverty. Although this idea is widely accepted, its application or implementation in estimating poverty is rather implicit, as there are no universally specified poverty dimensions. Different conceptualization of and approaches to poverty influence the choice of indicators for measurement, the classification of who is regarded as poor and who is not and also the policies adopted for tackling poverty. This chapter presents a theoretical and empirical review of the three prominent approaches to poverty identified in the literature. They include the monetary approach, the capability approach, and the social exclusion approach. It is important to mention that each approach comes with certain strengths and drawbacks. Nevertheless, the capability approach is employed in this study[5] and hence a greater portion of the discussion focuses on this approach. This is followed with a review of the unresolved issues in the existing literature. Drawing on the review of the poverty approaches as well as the contending issues, the concluding section presents the conceptualization of poverty applied in this study.

2.2 DEFINITIONS OF POVERTY
The concept of poverty is highly contested: there is no single clear-cut definition (Alcock, 2006). Traditionally, poverty is expressed in terms of 'distributional issues: the lack of resources at the disposal of an individual or household to ensure a suitable standard of subsistence or living' (Barnes, 2005:9). Beyond an individual's ability to satisfy minimum living standards of food, clothing, shelter and fuel, it is also about 'having what you need in order to have the opportunities and choices necessary to participate in society' (Bradshaw et al., 2008:1). Poverty reduction is a major goal for

[5] The argument for adopting the capability approach is presented in the methodology chapter of this thesis.

both national governments and international development agencies such as the United Nations and the World Bank. Two broad definitions of poverty include:

> 'Fundamentally, poverty is a denial of *choices and opportunities*, a violation of human dignity. It means lack of *basic capacity* to participate effectively in society. It means not having enough to feed and clothe a family, not having a school or clinic to go to; not having the land on which to grow one's food or a job to earn one's living, not having access to credit. It means insecurity, powerlessness and exclusion of individuals, households and communities. It means susceptibility to violence, and it often implies living in marginal or fragile environments, without access to clean water or sanitation' (United Nations, 1998 cited in Gordon, 2005:4).

> 'Poverty is pronounced deprivation in well-being, and comprises many dimensions. It includes *low incomes* and the inability to acquire the basic goods and services necessary for survival with dignity. Poverty also encompasses low levels of health and education, poor access to clean water and sanitation, inadequate physical security, lack of voice, and *insufficient capacity and opportunity* to better one's life' (World Bank, 2011).

These definitions encompass different dimensions of poverty. Poverty is seen to entail deprivation in income or monetary resources (monetary approach); deprivation in choices, opportunities and the capacity to better one's life (capability approach); and deprivation in the capacity to participate effectively in society (social exclusion approach). These approaches to poverty, as discussed in section 2.4 capture and place emphasis on different dimensions of poverty.

2.3 APPROACHES TO POVERTY

Following the work of Laderchi et al (2003), this section presents a review of the three main approaches to poverty: the monetary, capability, and social exclusion approach. It explores the theoretical underpinnings, criticisms and strengths as well as the challenges associated with operationalizing these approaches.

2.3.1 THE MONETARY APPROACH

This is the most commonly used approach in the identifying and measuring poverty. Welfare is measured by total consumption, proxied by either income or expenditure data, and poverty is described as a 'shortfall below some minimum level of resources', termed the poverty line. (Laderchi et al, 2003:248). Besides the utility maximizing behaviour assumption, one main argument for the monetary approach is the minimum rights approach which considers it a human right to earn a certain basic income because of the freedom of choice this brings (Atkinson, 1989; van Parijs, 1992). Another is the assumption that beyond its ability to measure utility, monetary indicators may also be able to proxy other aspects of poverty and welfare. It is argued that beyond the lack of resources, monetary indicators represent a convenient short-cut method for identifying individuals who are poor in other fundamental dimensions, such as health, nutrition etc. The assumption is that with appropriately devised measuring tools, uniform monetary metrics can be used to capture all possible inherent heterogeneity among individuals and their situations. One underlining problem with this approach is: how do we define the level of basic income. The validity of the utilitarian approach also depends partly on how well utility can measure well-being; how satisfactory monetary expenditure is as a measure of poverty; how well a shortfall in utility sufficiently captures all aspects of poverty; as well as the justification for any given poverty line (Laderchi et al, 2003).

The poverty line can either be set as an *absolute* or a *relative* measure of poverty. Absolute poverty measures poverty in terms of minimum standards of living which everyone should have in spite of the country they live in (Lister, 2004; Spicker, 2007). Although this approach to measuring poverty allows for easier comparison of poverty rates in different countries across the globe, it is disadvantaged to the extent in which it becomes arbitrary in its application in different societies. However, for the purpose of cross country comparisons and for consistent poverty indicators, the World Bank uses the absolute measure of poverty. First introduced by the World Bank in 1990, the $1 a day poverty line has been recently revised to $1.25 and $2 a day, to measure extreme and moderate poverty respectively and are adjusted for application to local currencies using the 2005 purchasing power parities (PPPs). Global poverty rates measured as the number of people living below $1.25 a day has declined significantly since the 1980s. The total number of extremely poor people fell from about 1.94 billion in 1981 to about 1.2 billion in 2010. This substantial reduction in poverty over the past three decades, however, disguises huge regional differences. The figures show a decline in the number of the extremely poor across all regions, but SSA where the population growth rate exceeded the rate of poverty reduction, thus doubling the number of extremely poor people in the region over this period (World Bank, 2012). As mentioned earlier, these absolute poverty lines are controversial in their relevance to different societies. Most countries therefore apply national poverty rates which are relative and believed to better reflect the equality of opportunities in a given time and space.

Relative poverty is measured using a poverty line which is derived in money terms based on some 'basket of goods' which is recognized as being set relative to the society to which it relates. Here,

> ‘Individuals, families and groups in the population can be said to be in poverty when they lack the resources to obtain the types of diet, participate in the activities and have the living conditions and amenities which are customary, or at least widely encouraged or approved, in the societies to which they belong. Their resources are so seriously below those commanded by the average individual or family that they are, in effect, excluded from ordinary living patterns, customs and activities’ (Townsend, 1979:31).

This approach to measuring poverty based on a standard of living or level of income sufficient to satisfy basic needs (like food, water, clothing, basic health care, and housing), relative to what prevails in the society under consideration is often referred to as a measure of ‘moderate poverty’. Particularly in the 1970s, this emphasis on relative poverty, inspired greater attention to a much wider conceptualisation of poverty beyond just income or expenditure. This period also saw a move from a narrow concept of ‘income poverty’ to a wider focus on ‘unmet basic needs’ including, the need for social relations and participation within the society.

Relative poverty can also be measured using a poverty line set as a percent of average income. For example, the European Union classifies as poor ‘those individuals who are employed and whose household equivalised disposable income is below 60% of national medium equivalised income’ (Laderchi et al, 2003). The Nigerian National Bureau of Statistics (NBS) also adopts a relative measure of poverty set at two-thirds of the total household per capita expenditure (THPCE). With the above definition, if real income increases for everyone in the society, but income distribution remains the same, relative poverty will also remain unchanged. This relative measurement of poverty can sometimes produce strange results. For instance, if the median annual household income in a wealthy society is £1 million, then a household with annual income of £100,000 would be considered relatively poor, even if such a household can meet all of its basic needs. Further, if the median annual household income in a poor society is only 50 percent of what is needed to meet basic needs, then households with the median income would not be labelled poor, even though they are clearly poor on an absolute scale. Here, relative poverty decreases only with a more equal distribution of income regardless of how this is achieved. For instance, if income levels changed in a way that hurt high earners more than low ones, relative poverty would decrease even though everyone is worse off.

However, these monetary poverty indicators almost always consist of only private resources, and overlook social resources (i.e. a variety of resources and benefits provided publicly, e.g. public health care, schools, the environment etc.). This is likely to create an 'implicit bias in policy choices in favour of the generation of private income as against public goods provision, and similarly, a bias in the identification of the poor for targeting purposes towards those lacking private income' (Laderchi et al, 2003: 249-250). Additionally, nutritional requirements appear dominant in the justification for defining the monetary poverty line. Yet, differences in metabolic rates, age, gender and size implies varying adequate nutritional requirements (Payne, 1993). Food prices and availability, as well as differing tastes also affect how much money is needed to achieve any given level of nutrition. Furthermore, poverty lines are typically drawn up at the household level even though the distribution of resources within the household may differ, resulting in differing individual nutritional levels. This suggests an inherent problem in drawing a unique poverty line based purely on nutritional requirements. A better approach would be to draw up a range of income levels, from a minimum poverty line below which everyone is poor, to a maximum poverty line above which no one is poor, in nutritional terms. A practical example of this is the common approach of setting the 'poverty' line and the 'extreme poverty' line.

Furthermore, economists approach welfare from the level of the individual; hence, poverty defined as a shortfall in welfare is individualistic. Consumption and income data are however collected at the household level. This implies that some level of adjustment is necessary for estimating individual poverty from any given level of household resources; including how income and expenditure is allocated within the household. Estimating individual poverty involves both practical and theoretical problems. For instance, if we adopt a minimum rights perspective and assume equal rights for all individuals, then assigning different weights to individual needs would be inconsistent with the definition. Nevertheless, if these rights are perceived as relating to outcomes rather than resources, or, if a utility-based perspective is adopted, adjustments that take into account different individual needs are justified (Laderchi et al, 2003).

Overall, beyond the challenges discussed above, the approach is daunted by some weaknesses. For example, the welfarist assumption that all relevant heterogeneity applicable to humans can be controlled for, requires fairly strong assumptions. Moreover, this approach addresses individual achievements, but fails to take into account social resources – social interactions and interdependencies at the household and community level - that may significantly influence individual achievements. Despite significant methodological developments and the apparent 'scientificity' of poverty estimates under this approach, these estimates still require numerous value judgements and are therefore open to debates (Reddy & Pogge, 2002; Ravallion, 2002). These value judgements on what constitutes a necessity and hence qualifies to be part of the essential consumption basket are generally performed 'externally', i.e. without the involvement of poor people themselves.

Although many of the methodological elements applied in estimating monetary poverty are borrowed from economic theories (e.g. equivalisation techniques), recent debates in the development literature have argued that poverty is in itself not only an economic category. It is argued that non-monetary indicators can be as good as and sometimes better than monetary poverty measures; as income and consumption capture only certain dimensions of poverty (Addison et al, 2009; Harris, 2002). This calls for the need to move beyond consumption and income measures of poverty to adopt other multidisciplinary measures and concepts that capture wider wellbeing dimensions. This is supported by growing consensus that an in-depth understanding of poverty requires the use of interdisciplinary approaches that bridge the gap between disciplines and combines quantitative and qualitative methods in the measurement and analysis of poverty. This is expected to bridge the divide between other social scientists (anthropology, sociology and politics) and economists. This chapter therefore turns to other poverty approaches that allows for a multidimensional and interdisciplinary approach to poverty. Next, we explore the Capability Approach which applies a human development approach to measuring and analysing poverty.

2.3.2 THE CAPABILITY APPROACH (CA)

This approach advocates that poverty be measured in terms of human development i.e. the expansion of individual capabilities and not the maximization of income or utility (Sen, 1985, 1997, 1999). Here, the 'freedom of individuals to live valued lives' is considered to be a better measure of well-being than monetary resources. Poverty therefore refers to deprivation in terms of failure to achieve certain basic or minimal capabilities. ‘Basic capabilities refer to the ability to satisfy certain crucially important functionings (valuable achievements) up to certain minimally adequate levels’ (Sen, 1993:41). Well-being is therefore perceived as the freedom to live valued lives in terms of realizing human potential (referred to as individual capability).

This emphasis on characterizing the quality of human life by the ability to achieve ‘potential outcomes’, denotes a shift from monetary indicators to a focus on non-monetary measures for evaluating deprivation or well-being. Income is treated only as a means to increased well-being, and not the outcome of interest. In other words, monetary resources are only considered as a means to an end, and not an end in itself. It is argued that, monetary resources do not represent a reliable measure of capability outcomes because individuals face differences in transforming available resources into valuable attainments (*functionings*). These differences depend on individual characteristics such as: physical abilities, mental/intellectual abilities, differences in metabolic rates, as well as contextual differences in individual living conditions (e.g. access to public services).

Based on these differences, an emphasis on final outcomes requires that poverty assessments consider the fact that certain individuals require more resources than others to achieve the same outcome. The emphasis is therefore on the *adequacy* of a combination of monetary and non-monetary resources to achieve certain capabilities rather than the *sufficiency* of these resources. It is important to note that contrary to certain criticisms, the CA considers the role of social goods and externalities in influencing an individual’s capabilities. It is the utilization of commodities (physical and intellectual) acquired by income as well as those publicly provided that enables individuals to attain certain functionings. Besides private monetary resources and public goods and services, individual characteristics (including age, gender, and physical capacities) and the general societal context influence an individual’s capability set and the use to which it is put, or the individual’s functionings that can be achieved. Therefore, although monetary resources remain instrumental in the achievement of poverty reduction (or enhanced well-being), it is just one of the several factors that contribute to the different dimensions of well-being. While the above discourse represents the foundational tenets of the CA, three critical debates remain central to its application as an approach for poverty assessment. These debates are discussed below

2.3.2.1 Operationalizing the Capabilities Approach

Key questions within the capabilities approach over which there remain certain uncertainties include: what are the relevant dimensions and by what process should they be decided. Sen generally characterises dimensions as 'beings and doings' and his stance with regards to this challenge is that: often only an incomplete measurement of multidimensional poverty is feasible, yet he holds that this incompleteness is by no means an embarrassment. He notes that capabilities can vary 'from such elementary physical ones as being well nourished, being adequately clothed and sheltered, avoiding preventable morbidity, and so forth, to more complex social achievements such as taking part in the life of the community, being able to appear in public without shame, and so on' (Sen, 1995: 15). Yet, he neither defines a universal list of basic capabilities nor provides guidelines for developing such a list.

However, several attempts have been made to define such a universal list (see table 2.1 below). The most influential attempt to draw such a list by Nussbaum (2000) encompasses ten capability measures of wellbeing. Although Nussbaum recognises that this list is open-ended and open for revision to suit different locations, she strongly supports and points to the benefit of drawing up a list of central capabilities. Inherent in this list of capabilities is an overwhelming importance on the quality of life an individual is 'capable' of achieving or has the 'freedom' to achieve. She argues that across different societies, there is an 'overlapping consensus' on what is needed to achieve a full human life. She therefore defends these capabilities as the moral entitlements of all humans and argues that in the absence of any of these ten capabilities, the human life becomes impoverished such that 'it is not worthy of the dignity of a human being' (Nussbaum, 2000:72).

In addition to the Nussbaum's list, Sabina Alkire launched the Oxford Poverty and Human Development Initiative (OPHI) dedicated to research about those poverty dimensions (see table 2.1) not yet sufficiently assessed in previous studies and data sources(Alkire and Foster, 2007). Additionally, the UNDP human development index (HDI) was derived from the CA. Here, poverty is measured as '… deprivation in three essential elements of human life…longevity, knowledge and decent standard of living … (UNDP, 1997:18). The indicators of deprivation for developing countries include: life expectancy below 40 at birth; adult illiteracy; and an average of under-five mortality and lack of access to improved water sources. Here, poverty is measured as '… deprivation in three essential elements of human life…longevity, knowledge and decent standard of living … (UNDP, 1997:18). The indicators of deprivation for developing countries include: life expectancy below 40 at birth; adult illiteracy; and an average of under-five mortality and lack of access to improved water sources. Indicators for developed countries include: life expectancy below 60 at birth; lack of functional adult literacy; population with income below 50% of the national median disposable household income and the long-term unemployment rate. This implies that the choice of dimensions and benchmarks are arbitrary and likely to be revised with changing poverty levels in the country or region where poverty assessment is being made, as well as changes in global poverty rates (Laderchi et al, 2003).

Table 2.1: Capability Dimensions

Alkire and Foster (2007) Oxford Poverty Human Development Initiative (OPHI)	Informal employment, empowerment/agency, physical safety, ability to go out without shame, psychological and subjective well-being
The Millennium Development Goals	Extreme hunger & poverty, universal primary, education, gender equality & empower women, child mortality, maternal health, HIV/AIDS, malaria, & other diseases, environmental sustainability, global partnership for development.
World Bank Living Standards Measurement Survey (LSMS)	*Household:* Household Composition, Food Expenditures, Non-Food Expenditures, Housing, Durable Goods, Non-farm self-employment, Agro-pastoral activities, Economic Activities, Other income, Savings and Credit, Education, Health, Migration, Fertility, Anthropometrics *Community:* Demographics, Economy & Infrastructure, Education, Health
Voices of the Poor Narayan et al (1999)	*Material Wellbeing:* Having Enough Food, Assets, Work *Bodily Wellbeing:* Being and appearing well, Health Appearances, Physical Environment *Social Wellbeing:* Being able to care for, bring up, marry and settle children, Self-respect & dignity, Peace, harmony, good family/ community relations *Security:* Civil peace, physically safe and secure environment, Personal physical security, Lawfulness & access to justice, Security in Old Age, Confidence in the Future *Psychological Wellbeing:* Peace of Mind, Happiness, Harmony (including a spiritual life and religious observance), Freedom of Choice and Action
Hamilton (2003): Needs categories	*Vital needs:* Adequate shelter, Sufficient clothing, Required daily caloric intake, Periodic rest, Exercise, Social entertainment *Particular social needs:* Bald need-claims - the need for an efficient train service, Provision - the need for a television, Consumption and production, i.e. the need for a car *Agency Needs:* Autonomy, Intersubjective recognition, Active and creative expression
Nussbaum (2000) Central Human Capabilities	*Life*: normal length of life, *Health*: good health, adequate nutrition and shelter *Bodily integrity*: movement, choice in reproduction *Senses*: imagination and thought, informed by education *Emotions*: attachments *Practical reason*: critical reflection and planning life *Affiliation*: social interaction, protection against discrimination *Other species*: respect and living with other species *Play*, *Control* over one's environment, politically (choice) and materially (property)

Source: Author's Compilation (2014)

Although these lists have been widely used, the importance placed on international comparability goes contrary to the context sensitivity of the CA, which emphasizes inquiring about context specific dimensions for any particular country. In all, not much attention has been given to the possibility of a universal measure of capability poverty as most studies identify with the contextual relevance of this approach. A critical look at these lists also shows that no one of them is exhaustive of the various dimensions of poverty. This confirms Sen's point that only an incomplete measurement of multidimensional poverty is feasible. Sen also recommends that in dealing with poverty in developing economies, certain basic capabilities (e.g. 'the freedom to be well nourished, well sheltered, and in good general health, the capability of escaping avoidable morbidity and premature mortality, the ability to move about freely', and so forth) which are central to important functionings should be included (Sen, 1996). However, he also mentions that this depends on the domains or dimensions of interest as the selected capabilities cannot be independent of what we intend to study. Additionally, the emphasis is placed on identifying and prioritizing freedoms in the domains that people value and have reason to value. These value judgements should also be determined by the subjects of interest and not externally imposed.

Sen has continued to argue against a universal list, claiming that the lack of specification ensures the relevance of the CA to different persons and cultures. He argues that the evaluative exercises (poverty, human rights, human development etc.) for which capability sets are selected, vary greatly in practice, and so should be the capabilities (Alkire, 2002, Sen 2004). In his response to the call for a universal capability set, Sen replies,

> 'The problem is not with listing important capabilities, but with insisting on one predetermined canonical list of capabilities, chosen by theorists without any general social discussion or public reasoning…... pure theory cannot "freeze" a list of capabilities for all societies for all time to come, irrespective of what the citizens come to understand and value. That would not only be a denial of the reach of democracy, but also a misunderstanding of what pure theory can do….To insist on a fixed forever list of capabilities would deny the possibility of progress in social understanding and also go against the productive role of public discussion, social agitation, and open debates…What we focus on cannot be independent of what we are doing and why (e.g., whether we are evaluating poverty, specifying certain basic human rights, getting a rough and ready measure of human development, and so on)' (Sen 2004a: 77-80).

He argues that an appropriate application of the CA as an evaluation technique must not only meet the relevance criterion (i.e. be context-specific with a focus on what people value and relevant for the intended objective), but also the usability criterion (i.e. be usable for empirical analysis). However, he does not provide specific guidelines on how the CA can be implemented. Hence, researchers who attempt to operationalize the CA are faced with certain complexities. Some of these have been concisely clustered below.

Figure 2.1: Complexities in Operationalising the CA

1. a plurality of evaluative spaces ranging from agency-autonomy-empowerment and capabilities to material standard of living and achieved functionings;
2. a plurality of dimensions and a multiplicity of indicators and scales, of a quantitative or qualitative nature, and objectively or subjectively measured;
3. a plurality of units of analysis (individuals, households, subgroups of population) and personal heterogeneities that can affect the conversion process of resources into capabilities, such as gender, age, or racial and religious differences;
4. a plurality of environmental contexts, including socio-economic, geographical, cultural and institutional variables.

Source: Chiappero-Martinetti and Manuel Roche (2009: p162)

This raises several issues about operationalizing the CA for empirical purposes. This includes the choice of dimensions, the unit of analysis, the availability of appropriate datasets for capturing the different dimensions, and the need for conducting primary surveys that can satisfy the research and statistical requirements. For instance, even when the relevance and usability criterion is met, there is still the question of what constitutes legitimate grounds for selecting any given dimension. In an analytical review of the different processes used for selecting capability dimensions in existing studies, Alkire (2008a) identifies five methods for selecting dimensions (see Table 2.3 below). It is immediately obvious that these methods overlap and can be used jointly. We will briefly review some of these methods and how they have been used to select some of the prominent capability lists mentioned in table 2.1. This is important to set the stage and guide the selection of capabilities that will be used in this study.

For example, the selection of the HDI dimensions were partly influenced by the availability of existing cross-country comparable data and their ability to meet the relevance and usability criterion, as regards relating to human development and their usefulness in empirical analysis. We can also identify some form of normative assumptions inherent in the selection of the HDI dimensions. Here, the assumption is that people across regions, cultures, gender, societies etc. value income, basic education and survival. These assumptions may be drawn from the researchers' own views, social theory, psychological views, or popular conventions within the literature. The logic, assumptions and claims behind the use of these dimensions are also made explicit and transparent. This adds tremendous value to the selection process as it enables critical review of the underlying assumptions, allowing for criticisms, support and suggestions for improvement. Nussbaum's list can also be argued to involve some normative assumptions. In spite of her argument that her list constitutes an 'overlapping consensus' on what is needed to achieve a full human life across different societies, it is yet to undergo any public deliberative process.

Figure 2.2: Existing methods for choosing capability dimensions

Existing Data or Convention – to select dimensions (or capabilities) mostly because of convenience or a convention that is taken to be authoritative, or because these are the only data available that have the required characteristics

Assumptions – to select dimensions based on implicit or explicit assumptions about what people do value or should value. These are commonly the informed guesses of the researcher; they may also draw on convention, social or psychological theory, philosophy, religion, and so on.

Public 'consensus' – to select dimensions that relate to a list that has achieved a degree of legitimacy due to public consensus. Examples of such lists at the international level are universal human rights, the MDGs, and the Sphere project; these will vary at the national and local levels.

Ongoing Deliberative Participatory Processes – to select dimensions on the basis of ongoing purposive participatory exercises that periodically elicit the values and perspectives of stakeholders.

Empirical Evidence regarding people's values – to select dimensions on the basis of expert analyses of people's values based on empirical data on values, or data on consumer preferences and behaviors, or studies of which values are most conducive to mental health or social benefit.

Source: Alkire (2008a)

Take the Millennium Development Goals for example; they represent a set of dimensions generated by a public deliberative process that is said to have led to a legitimate consensus. Formed by heads of states from 189 United Nation member states, this list has received widespread political support around the world. However, it has been criticised on the basis that it does not represent an actual full consensus; and that the consensus was not reached by the general public but by heads of states. Regardless of the debate about who is included in the deliberation process, the strength of dimensions selected using this process lies in the authority and claim to legitimacy of the capabilities selected. The ability to overtime generate data useful for comparable evaluations across communities is also an added advantage. Yet, the fact that the poor whose well-being is the subject of interest is likely to be excluded from the public debate and their values not represented in the public consensus is a disadvantage.

Capabilities can also be selected from an ongoing deliberative process. Here, the goal is to extract information on the dimensions of poverty the poor value, using participatory approaches and group discussions. The attraction to this process is that ‘value judgements are made and revised directly by the community concerned’. Some drawbacks include the possibility that the process may be hijacked by the elite in the community. Additionally, in the absence of trust; discussions on ‘values’ may be misleading and superficial. It is also expensive and may be particularly unfeasible at a large scale. Nevertheless, Alkire (2008a) argues that this approach is a preferred option when the researcher (i) intends to capture value issues in a reflective way, (ii) can ensure that conflicting views are expressed safely, and (iii) can capture the views of all relevant groups without excluding certain people due to power balance.

Finally, capability dimensions can be selected and drawn from empirical analysis. For example, based on empirical evidence, some normative values required for a healthy human well-being have been articulated by a number of psychologists (Biswas-Diener and Diener, 2001; Inglehart and Baker, 2000). Drawing from 78 empirical Participatory Poverty Assessment (PPA) reports, surveys such as the ‘voices of the poor’ applied this method by gathering and synthesizing findings regarding the poverty dimensions the poor value (Narayan et al, 1999). Although this method may be disadvantageous for side-lining the perspectives of the poor currently studied, combining this with a deliberative or participatory method will ensure that the capabilities selected are relevant to the context. In all, there is no universally accepted capability set and the validity of the selected capabilities is likely to be improved when a combination of two or more selection techniques are applied, and when the process of selection is clearly made known. Beyond the challenge of selecting capabilities, another difficult task in operationalizing the CA is the translation of capabilities (i.e. all potential achievements an individual may have) into something measurable.

2.3.2.2 Empirical analysis

One of the main challenges with analyzing poverty under the CA is data availability. Particularly, one has to decide whether to use an existing dataset or collect an original dataset suitable for the purpose of the analysis. As mentioned earlier, selecting poverty dimensions using secondary analysis - an existing dataset – side-lines the perspectives of the poor currently studied, and only combining this with a deliberative or participatory method will ensure that the capabilities selected are relevant to the context. In tackling these issue, primary analysis have come in very useful, and is sometimes the only opportunity for addressing issues such as how to know what people have reason to value. Primary analysis generally involves fieldwork activity designed to collect the required data for addressing a specific research question. Such analyses are usually conducted through face-to-face or phone interviews, questionnaire-based surveys, field observations or ethnographic research. In recent years, participatory poverty methods have been widely used to investigate the perceptions, conditions, and preferences of people, and also to get them involved more directly. It allows the researcher to collect data that is appropriately tailored to satisfy the research objectives.

Primary analysis offers some undeniable merits. First of all, it may be the most suitable and sometimes the only solution when working on context-specific or, relatively new empirical research that requires exploratory fieldwork. Secondly, it allows for in-depth investigation into context-specific topics, people or situations. It also allows the researcher to collect quantitative and qualitative subjective information on the subject matter. Third, it allows respondents to express their opinions and values, and play a more active role. It is obvious that these features are fitting to the operationalization of the CA. However, some disadvantages related with primary analysis include one; it is generally time-consuming, and expensive. Second, the reliability and validity of the analysis is usually difficult to validate. Also, since the analysis is often conducted with a relatively small sample size, the sampling design and the response rates strongly impact the statistical significance of the analysis.

The theoretical shift from the monetary approach to the CA involves key challenges at the methodological level. Operationalization the CA requires the use of a different set of analytical techniques and research strategies. A diverse and broad range of statistical techniques have been employed both separately and jointly in empirical applications based on the CA. A broad classification of the widely employed techniques include: ‘scaling and ranking solutions, fuzzy set theory, multivariate data reduction techniques, and the regression approach’ (Chappero-Martinetti and Manuel Roche, 2009: p 171). Scaling techniques are generally used at the macro level and are more suitable for aggregating indicators that a single multidimensional measure for regional or country comparisons. Typical examples include the HDI, the Gender

Empowerment Measure (GEM), and the Gender-related Development Index (GDI). Fuzzy sets techniques are commonly used in the CA for micro-level analysis and they handle ordinal and continuous variables simultaneously (Addabbo et al. 2004; Chiappero-Martinetti, 2006; Qizilbash and Clark, 2005; Roche, 2008). In measuring multidimensional poverty, fuzzy set theory holds that while there are cases where functionings have either been fully achieved or not achieved at all, oftentimes, there is only a partial degree of achievement. In this case, the cut-off point between those 'poor' and the 'non-poor' is quite complex and vague. Hence, by measuring variables based on a degree of membership, the fuzzy set theory attempts to tackle this challenge with measuring and aggregating functionings.

Multivariate data reduction techniques are particularly appropriate when dealing with a large list of poverty indicators, as they facilitate the aggregation of variables (Di Tommaso, 2007; Klasen, 2000; Kuklys, 2005; Roche, 2008). Some of the predominantly used data reduction methods include: factor analysis, principal component analysis, cluster analysis and multiple correspondence analysis. Lastly, the regression approach which includes a broad range of technique, including OLS regression, ordered logit, probit models, and structural equation modeling has been employed in modeling capability, functionings and subjective well-being (Anand et al., 2005; Anand and van Hees, 2006; Burchardt, 2005; Krishnakumar, 2007). Here, the models are usually constructed to predict a multidimensional aggregated measure of poverty using a theoretically or contextually determined set of predictors. Nevertheless, regardless of the technique employed, empirical analysis of poverty using the CA is plagued with certain limitations. For an in-depth comparison of the main statistical techniques applied or an in-depth review of some of the empirical studies based on the CA, see Chiappero-Martinetti and Manuel Roche (2009).

The challenge is that capabilities represent a set of *possible achievements* and as such are difficult to measure empirically. In practice, some studies tend to measure functionings (i.e. realized achievements) rather than capabilities. Even after legitimate dimensions have been selected, further issues requiring consideration include: choosing relevant output indicators for the capability dimensions, modelling the relationship between indicators and dimensions, assigning relative weights and addressing the issue of endogeneity. Particularly, the multidimensional emphasis of this approach creates problem of aggregation. One argument is that each capability is intrinsically valuable and hence, no trade-offs should be introduced. This restricts the sort of aggregative approaches that can be employed. Yet, aggregation is important for reducing large amounts of information into manageable sizes and fully aggregative strategies are likely to be relatively more useful for policy making. It is obvious that these pluralities with operationalising the CA and in the empirical techniques employed have led to inherent complexities in implementing the CA as an approach to poverty. This in turn, has led to some criticisms of the CA as discussed below.

2.3.2.3 Critiques of the CA

One major criticism of the CA is the supposed individualism of Sen's approach. The critics (Evans 2002; Stewart and Deneulin 2002; Stewart 2005; Deneulin 2004, 2006, 2008 among others) forcefully argue that an evaluative framework whose fundamental elements are individual capabilities is misleading. They therefore argue that even when the application of the CA is evaluative, the wider goal of any evaluation is to guide prospective recommendations. They argue that any analyses that fails to carefully account for the role of collective actions, social structures, and other institutions in creating individual capabilities, is bound to be deeply flawed.

In responding to these criticisms, Robeyns (2008:90) argues that this criticism of the CA based on its individual focus is often misleading as it is based on a misunderstanding of the CA. She argues that although the CA embraces ethical individualism, it does not defend ontological or methodological individualism. She makes the distinction that ethical individualism "postulates that individuals, and only individuals, are the ultimate units of moral concern. … This, of course, does not imply that we should not evaluate social structures and societal properties, but ethical individualism implies that these structures and institutions will be evaluated in virtue of the causal importance that they have for individuals' well-being." Ontological individualism holds that "society is built up from only individuals and nothing than individuals, and hence is nothing more than the sum of individuals and their properties." Methodological individualism postulates "that all social phenomena can be explained in terms of individuals and their properties."

Robeyns advocates for the support of ethical individualism – arguing that any framework that adopts an alternative unit of concern such as the group, the family, or the community, will overlook any potential or existing inequalities within these units. For instance, analyses that focus on the household tend to overlook the deprivations of women and children. An important contribution is her observation that "a commitment to ethical individualism is not incompatible with an account of personhood that recognises the connections between people, their social relations, and their social embedment.” Therefore, criticisms that the CA is methodologically or ontologically individualist are misconstrued. Engaging ethical individualism in operationalising the CA as an evaluative framework recognises the social structures and institutions that shape capabilities. However, it does not commit to the task of investigating how these capabilities are created or shaped. Most criticisms of the ethical individualism of the CA focus on this latter task.

Deneulin (2004, 2008) criticizes the CA for focusing too much on the expansion of individual capabilities in a way that it pays too little attention to the conditions of capability expansion. She argues that without studying the institutions, structures or policies that in part create and sustain these capabilities, the CA will be unable to generate the sort of recommendations required to promote capabilities. Thus, it is unable to advance its own goal of expanding capabilities. “In the light of the Costa Rican development path, assessing development on the basis of individual capabilities, or irreducibly social goods that are of intrinsic value to individual lives…would miss out …certain structures of living together that make the whole process of development and expansion of individual capabilities possible”. She argues that if the CA was always used purely to evaluate states of affairs, then this oversight would not be particularly significant, but that this is not the case. In practice, it is increasingly been used as ‘a guiding theory for development practice’ as the empirical evaluation feeds into policy advice. Thus, Deneulin further claims that it ‘directs attention away from the examination of the structures of living together and historical explications of these structures, which are responsible not only for the conditions of life of individuals today but have also affected past generations and will affect future ones (2004:76)’.

As Alkire (2008b) noted, Deneulin’s criticisms of the CA does not challenge ethical individualism – as her approach “still ultimately judges development by individuals’ lives.” Rather, it challenges the assumption that in operationalizing the CA, evaluation can be detached from prescription. The debate here is whether the required informational set for an evaluative assessment should be chosen because it best identifies the objectives of ultimate value? Or because it affords sufficient information on which further recommendations can be based? Robeyn’s and Sen’s defense of the informational space set by the CA has focused on the former; while Deneulin’s criticism stems from her focus on the latter.

Stewart (2005) also advocates that research work based on the CA should pay more attention to 'collective or group capabilities.' She defines groups as "ways of categorising people in ways that represent common affiliations or identities." She mentions three ways in which group membership shape individual capabilities. First, the intrinsic benefit of participating in a group can lead to an expansion of individual well-being – by increasing self-esteem, providing positive human relationships etc. Additionally, individual capabilities may be affected directly by "how well the group they identify with is doing." (p 187) Second, "groups are important instrumentally in determining efficiency and resource shares." For example, collective group actions can enable the poor to expand quite different capabilities (189). Third, "groups influence values and choices. Groups could also exert negative influences on capabilities through these same three mechanisms. Given these three critical roles, analysis of what makes for 'good' groups and what makes for 'bad' groups becomes a critical part of any research agenda, and of policies towards the promotion of capabilities and human well-being." (190). She argues that these capabilities are intrinsic by nature, and that individuals are only able to enjoy them because of their participation in the group. Here, the key focus is the recognition that the enjoyment of these capabilities by the individual is currently and perhaps also in the future, dependent on their participation in the group, such that changes to the entire group are very much likely to affect individual capabilities.

As mentioned earlier, criticisms that the CA does not recognise the influence of groups on individual values are misconstrued. It can be observed that Stewart's and Deneulin's criticism of the CA stems from their attempt to apply it in a "prospective" sense - to make recommendations as to 'the promotion of capabilities.' Hence, this is not necessarily a criticism of the individualism of the CA but, rather, criticisms that the focus on evaluative analysis leaves the techniques of prospective analysis unspecified. Particularly, it does not stipulate the significance of including groups and social relations, in prospective analyses. They therefore suggest that more attention be given to the creation of capabilities by groups and that the vocabulary be modified to recognise group or collective capabilities. Deneulin claims that the emphasis on information on the expansion of capabilities shifts attention away from the more important structures that shape these capabilities.

On the other hand, group capabilities, could also be used to imply that every member of the group enjoy or value these capabilities. It is this type of assertion that Sen and

Robeyns, are wary about, and for this reason are reluctant to approve the term or assign "intrinsic" significance to social structures. Their argument is that any approach that ascribes intrinsic significance to group capabilities without consulting all the related parties, forfeits the ability to offer a more differentiated and nuanced account of how any particular social structure (group, family, tradition), affects diverse members at any point in time. Robeyns therefore urges feminists to endorse ethical individualism, arguing that the CA must ultimately focus on individuals. By doing so, we can accurately evaluate the capabilities that individuals value and have reason to value, allowing us to progress the border of groups which, unfortunately, can be considerably unfavourable towards some members.

In conclusion, the CA provides a coherent framework for conceptualizing poverty in terms of the freedom or opportunities individuals have and the lives they live. In contrast with the monetary approach, it embraces a much wider approach to the causes of poverty. The shift from the narrow focus on the private monetary resources individuals have to the sort of life they can lead; creates room for social goods, individual differences and other externalities which are often neglected in the monetary approach. However, like the monetary approach, it suffers from methodological challenges in selecting operational measures. Both approaches are individualistic since both capability failure and utility deprivation are individual characteristics, even though, in reality, their achievements depend on household and community characteristics, particularly for children and the elderly. Although the monetary approach adopts an external assessment of deprivation, the review above shows that the CA can be designed to allow for value judgements by the poor themselves. Yet, both approaches pay little attention to the causes or dynamics of poverty, although some studies go beyond measurements to investigate the processes leading to or the causes of, capability and/or monetary poverty (Dhatt & Ravallion, 1998; Baker, 1997).

2.3.3 SOCIAL EXCLUSION (SE)

The concept of social exclusion (SE) was developed in developed countries to refer to the processes of deprivation and marginalization that can arise even in countries with comprehensive welfare packages. It has been applied to developing countries through the activities of the Social Summit and various UN agencies (Clert, 1999). The SE is defined as a 'process through which individuals or groups are wholly or partially excluded from full participation in the society in which they live (European

Foundation, 1995)'. This approach stems from the early work of Townsend who relatively defined the poor as those who 'are in effect excluded from ordinary living patterns, customs and activities (Townsend, 1979: 31)'. Hence, SE is socially defined; pertaining to groups (gender, age, racial or ethnic categories) rather than individuals. SE therefore involves a *relative* approach – exclusion from 'normal' activities - to the estimation and definition of poverty.

In contrast with the previous approaches, SE pays more attention to the processes and dynamics that engender deprivation as well as the outcome of exclusion. SE is also expressed as '… a dynamic process, best described as descending levels: some disadvantages lead to some exclusion, which in turn leads to more disadvantages and more exclusion and ends up with persistent multiple (deprivation) disadvantages (Eurostat Taskforce, 1998:25)'. Hence, multidimensionality – being subject to more than one and possibly multiple deprivations – is an essential feature of SE. This raises issues of aggregation as in the case of CA. Empirical studies also points to causal links between different dimensions of SE, e.g. between income and employment; housing and employment; insurance and formal sector employment. SE has also been linked with monetary poverty as lack of income is both a cause of SE (exclusion from social relations) and an outcome (exclusion from productive opportunities).

Indicators of SE in developed countries normally include unemployment, minimal income and social relations, access to housing, and democratic rights. For instance, Townsend (1979) introduced the use of social indicators in establishing poverty thresholds. In the Townsend approach and other studies based on his approach, even when measures which could be seen as related to income such as the nutritional value of diet and participation (e.g. holding birthday parties for children) were included, they were mainly included as reflections of particular social customs. Applying these indicators to developing countries however raises difficult issues as the features of SE in these countries are likely to differ from those in developed countries. While these indicators remain highly relevant, it is difficult to find appropriate norms that can serve as benchmarks for SE in developing countries. In these countries, although high level of communality encourages and deepens social interactions, it however does not eradicate the very dominant 'social class' structures. Unemployment, poor living conditions, lack of social insurance etc. are characteristic of the majority of the population and do not indicate exclusion from normal social activities.

‘To the extent that the normal may not be desirable, what is “normal” may not be satisfactory in defining the benchmarks of exclusion’ (Laderchi, et al, 2003:259). One suggested solution is to adopt standards from outside the society, in this case developed countries (Room, 1999). However, in this case, one might ask: if external standards are adopted; then what is it that the poor are excluded from? Another suggestion is to derive context-specific indicators through consultation as suggested in participatory approaches. Still, it is empirically possible based on individual characteristics such as gender, race, caste etc., to identify which groups are correlated with multiple deprivations in other poverty approaches. This therefore suggests the failure of the SE in this case. For instance, this is the case in Nigeria where over 60% are relatively poor; living with a dearth of social amenities and basic infrastructure. In this case, the norm is not desirable. It is obvious from the above review that the SE approach ‘defies clear definition and measurement’ and is therefore the most problematic to interpret and the least well-defined conceptualization of deprivation (Micklewright, 2002:7). It is particularly difficult to apply the concept to developing societies because despite the possible conflict between what is desirable and what is normal, it is difficult to define ‘normality’ in these societies as well. The society-specific requirement also raises issues of possible discontinuities in the SE approach.

However, one issue which arises is often the suggestion with the social exclusion approach that the poor may be excluded on a long term basis, and sometimes leading into notions of a social underclass. Another issue that arises is which society individuals are being excluded from. In a divided society, a person may be included so far as own group (e.g. ethnic) is concerned but excluded from other groups. Social exclusion can occur (a) at the family level in terms of discrimination from access to and use of resources available in the family; (b) at societal level in terms of discrimination on the basis of caste, descent, ethnicity, gender, HIV status, religion, race, migrant status, sexual orientation or where they live; and (c) at the state and policy level in terms of employment, welfare schemes, social security policies and their implementation (Media for Rights, 2011).

Nevertheless, advocates of the SE approach take pride in its emphasis on the processes and dynamics that engender deprivation; as well as its contribution to analysing structural characteristics within societies in terms of group deprivation. SE also encourages an emphasis on distributional issues - redistribution of opportunities and achievements - and points to the failure of the state to improve the situation of the excluded and incorporate all social groups. In contrast, the monetary and capability approaches are individualistic and do not place emphasis on distributional issues.

2.4 UNRESOLVED ISSUES

With these different approaches, it is obvious that there are some unresolved issues in the literature on poverty. First, what is the scope in which poverty or deprivation is defined and how is that scope captured by chosen indicators? Should poverty be restricted to the material aspects of life, or comprise of social, political and cultural aspects? Should poverty be measured in terms of resources/utility or in terms of the freedom to live ‘valued’ lives? What indicators would be considered appropriate for the different approaches? For instance, should indicators measure what individuals can achieve i.e. the capacity to be and do a range of things, or what they actually achieve? Secondly, should we adopt universal definitions and measures of poverty that are applicable across different societies without serious adjustments? The CA approach is conceived with an initial focus on developing countries. As described earlier, this raises problems with their application to developed countries. In contrast, the monetary and SE approaches were conceived with an initial focus on developed countries, and the same problem applies. To some extent some approaches are more appropriate for certain contexts, and may need to be adjusted for better implementation and relevance in particular societies. This creates problems with comparisons across different contexts.

Third is the question of the objectivity or subjectivity of poverty measures. Poverty statistics and remarks about poverty are often presented in a way that suggests objectivity, i.e. the idea that poverty statistics capture a certain reality which is “out there”. However, as far as poverty measures are influenced by individual value judgements, they are subjective. This raises the question: who makes these value judgements? Is it done implicitly by statisticians or researchers who specialize in measuring poverty? Are these value judgements explicit so that they are readily available and subject to sensitivity analysis for evaluation? Are they made through a participatory poverty assessment process involving stakeholders and the poor themselves? Table 2.3 below contains an overview of the comparison of these approaches as presented by Laderchi et al. (2003).

Table 2.2: A Comparison of Poverty Approaches

	Monetary poverty approach	Capability poverty approach	Social exclusion approach	Participatory approach
Unit of analysis	Ideally the individual, *de facto* the household	The individual	Individuals or groups relative to others in their community/society	Groups and individuals within them
Required or minimum standard identified by	Reference to 'external' information; central element is nutritional requirements	Reference to 'lists' of dimensions normally assumed to be objectively definable	Reference to those prevailing in society and state obligations	Local people's own perceptions of well-being
Sensitivity to social institutions	None, but assessments can be broken down by group	Emphasis on adequacy rather than sufficiency leaves space for (non-modelled) variations	Central element	Reflected in the way people analyse their own reality
Importance of processes	Not essential Increasing emphasis	Not clear	One of the main thrusts of the approach	Critical for achievement of satisfactory methods
Major weaknesses conceptually	Utility is not an adequate measure of well-being, and poverty is not an economic category	Arbitrary elements in choice of basic capabilities, problems of aggregation	Broad framework, susceptible to many interpretations, difficult to compare across countries	Whose perceptions are being elicited, and how representative are they? How does one deal with disagreements?
Problems for cross-country comparisons	Comparability of surveys, of price indices, of drawing poverty lines	Fewer problems if basic capabilities are defined externally, but the difficulties and inconsistency in aggregation makes comparisons tough	Lines of social exclusion essentially society-specific; also an aggregation problem	Cultural difference can make appropriate processes differ across societies, making results incomparable
Data availability	Household surveys regularly conducted; omitted observations can be important. Use of national income date-but requires assumptions on distribution	Data less regularly collected, but could easily be improved	Currently have to rely on data collected for other purposes. If agreed on basic dimensions, data could be regularly collected	Generally only small purposive samples. Never available nationally, would be difficult to extend method for regular national data collection
Major weaknesses for measurement	Needs to be anchored to external elements Arbitrary	Impossibility of set evaluation. Problems with multidimensionality	Problems with multidimensionality. Challenge of capturing process	How comparable? How representative?
Policy implication	Emphasis on economic growth and distribution of monetary income	Investments in extending basic capabilities via monetary incomes and public services	Foster processes of inclusion, inclusion in markets and social process, with particular emphasis on formal labour market	Empowerment of the poor

Source: Laderchi et al., 2003:28

Fourth, is how to determine the poverty line that separates the poor from the non-poor? Two related issues arise: firstly, what is the justification for adopting any such line; and secondly, to what extent is the poverty line defined as relative to a given context or is intended to reflect some absolute standards of deprivation. From a relative point of view, the poverty line is defined with reference to some summary measure of the overall distribution. At the other extreme, a poverty line is set in terms of minimal requirements in the dimension of interest identified in absolute terms, e.g. on the basis of some needs of the individual deemed as essential for survival. In reality it is difficult to identify such absolute needs irrespective of societal standards. None the less, the sense of deprivation or unhappiness caused by poverty is greatly influenced by average societal standards. In general, relative standards are mostly adopted in countries where it is assumed that all have access to the means to ensure survival, while where the availability of a survival minimum is felt as a pressing issue (i.e. generally in developing countries), absolute standards are more often adopted.

A fifth issue concerns the *unit* over which poverty is defined—at the individual or household level. While it is individuals who suffer or enjoy their lives, data, particularly of a monetary kind, normally pertain to households. Some resources (not only money income, but also sanitation, clean water) come via the household and it is difficult to ascertain the distribution of services they provide to the individual. Sixth, is the issue of *multidimensionality*. While the monetary approach argues that the monetary metrics either captures the essence of deprivation, or proxies all other deprivations, this depends on how well the relevant heterogeneity between individuals can be adjusted for, so that their monetary resources become comparable across individuals. On the other hand, Sen proposes the constitutive plurality of welfare assessments that do not present themselves in the form of a single index. However, in this case, how should each constituent dimension be measured and how should they be aggregated. By definition aggregation implies a loss of information, whose influence on the final results should be appropriately tested for (Laderchi et al, 2003).

In conclusion, although it is unanimously agreed that poverty is a problem that needs necessary action to address it, there still remains a lot of uncertainty about the concept of poverty. Some unresolved issues include: what constitutes poverty, the unit of focus - individual or household level, the relative importance of the different dimensions of poverty, the need to distinguish and pay attention to the depth of poverty, the vulnerability of different groups to poverty and the gender and ethical dimensions of poverty. There are also different opinions about the causes of poverty and the relative importance of these causes, which in turn, results in different recommendations on how best to address poverty. Despite the agreement on the need to address poverty, the degree of intervention is still not certain. For some advocates, the aim is poverty alleviation; for others it is poverty reduction; and for the very ambitious, it is poverty eradication.

2.5 CONCLUSION

This chapter reviews some of the approaches – monetary, capability, and social exclusion - to conceptualizing and measuring poverty. It is evident that there is no clear definition or universally agreed conceptualization to poverty. Each approach holds different perspective of what constitutes a just society and a good life. They each involve methodological assumptions that are often unclear; which results in different estimates and categorization of the 'poor' and therefore different policy implications. With regards to measuring poverty, national income data and household consumer surveys have become more available over the years for estimating monetary poverty. In contrast, indicators of capability poverty often depend on one-off surveys as data for most capabilities are unavailable on a regular basis. Similar data deficiencies apply to the SE approach as some dimensions of SE may not be measured at all or maybe measured with deficient indicators.

Yet, the multidimensionality of human life advocates that poverty be approached from a multidimensional point of view. This has also been universally accepted in the poverty literature. Of the three approaches discussed in section 2.2, Amartya Sen's capability approach provides a much wider human development approach to poverty. As Alkire (2008a) puts it

> 'The capability approach is a coherent framework that researchers can draw on in order to utilize diverse approaches to multidimensional well-being in a concerted and conceptually coherent fashion. It can be and, it is expected, will be applied differently depending on the place and situation, the level of analysis, the information available, and the kind of decision involved' (Alkire 2008a:2).

Due to its broader focus on the development of human welfare, an emphasis on the 'quality of life' and the lack of specification which allows it to be tailored to context-specific differences, this study adopts a capability approach to poverty.

Overall, the CA emphasises the reduction of capability poverty through the expansion of valuable freedoms and therefore places emphasis on identifying and prioritizing the freedoms that people value. Therefore 'the things that people value and have reason to value' are expected to be a primary concern in selecting appropriate dimensions. As this study evaluates the ability of microfinance to reduce poverty through improved capabilities for the poor, the research question derived from this analysis is: what capabilities do microfinance clients in the Nigerian context 'value and have reason to value'? Aware of the complexities associated with operationalizing the CA, this study selects capability dimensions based on the purpose of the study, what the subjects of interest 'value and have reason to value', as well as the contextual suitability of these dimensions. In doing this, we make sure to explicitly describe how and why a given dimension is selected in order to allow for constructive criticisms (Alkire, 2008a; Robeyns, 2005). In all, poverty is multidimensional and any attempt to measure, assess or evaluate poverty reduction will only capture certain dimensions. The key is to clearly state what dimensions are covered and how the selected capabilities or indicators are selected.

CHAPTER THREE

MICROFINANCE

3.1 INTRODUCTION

Microfinance is generally perceived as the provision[6] of financial services to the economically active poor who lack access to mainstream financial services [7] (Armendariz de Aghion and Morduch, 2010; (CGAP, 2013); Ledgerwood, 2013, 1999). It includes the provision of microcredit; and more recently has been expanded to include the provision of micro-savings, insurance and money transfer services. It has been welcomed by many as a golden bullet to poverty reduction, which is market-driven, enabling the poor to become micro entrepreneurs, improve their income, and eventually escape the vicious cycle of poverty. However, given the recent client over-indebtedness that plagued the sector and findings from rigorous impact studies suggesting that microfinance may not be the solution that many had hoped; there is a growing concern that these expectations are not being met. Recent debates have gone beyond this questionable positive impact to a call for studies that *listen to clients and approach the delivery and evaluation of microfinance from the 'clients' vantage point*. *A*sking what it is that they are looking for when they utilize financial services? What features of microfinance are beneficial and which are not? (Maes and Reed, 2012:1-2). This study falls within this more recent client-focused approach

One might ask: why do we need 'microfinance' for the poor or why do the 'poor' lack access to mainstream financial services, how is microfinance provided to the poor, and what are the poverty implications of microfinance? These are the questions to which this chapter attempts to provide answers. In answering the question of 'why' the exclusion of the poor from mainstream finance, this chapter turns to the theories on financial development as well as the financial exclusion literature. While the former argues for the emergence of financial institutions due to market imperfection and

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[6] As will be discussed later on in this chapter, it does matter who provides microfinance – formal/informal institutions, profit/non-profit organisations. This is because; the objectives as well as institutional nature of the providers have implications for the implementation processes and terms and conditions in which microfinance is provided. For instance, we can assume that because formal MFIs are more likely to be regulated, they are therefore less likely to offer extortionate rates and more likely to be safer than informal MFIs. Also, while non-profit providers may provide subsidies, profit oriented MFIs may not.

[7] Mainstream financial services refer to those services provided by mainstream financial institutions which are of interest to and readily available to the general public, as opposed to appealing to only a very specific subset of the public. However, depending on how microfinance is viewed, some, e.g. credit unions, may well be for those who could have access to 'mainstream' but for whom mainstream is expensive.

information asymmetry in credit markets (Alkerlof, 1970; Stiglitz, 1990 amongst others), the latter focuses on market imperfection, information asymmetry and the implications for the poor.

In answering the question of ‘how’, this chapter reviews the various transitions in the implementation mode of microfinance - from the early focus on microfinance as a poverty reduction tool to the new focus on a commercialised microfinance that emphasises profitability and financial sustainability of the MFIs. The question is: does this change in focus endanger the poverty reduction effects of microfinance? This question becomes more important when we consider three of the most recent debates in the microfinance literature. These include: (i) the recent claims that indebtedness plagues the microfinance industry, (ii) the growing concern that the perceived positive impact of microfinance has not been realised and (iii) the call for a wider focus on inclusive finance. Following the review of the recent debates in the literature, a gap in the literature is identified, and the research questions and objectives defined. Next, an attempt is made to present a conceptualization of microfinance that will allow for the research objectives to be achieved. This conceptualisation draws from the theory of consumer demand proposed by Lancaster (1966) which proposes that ‘the good, per se, does not give utility to the consumer; it possesses characteristics, and these characteristics give rise to utility …and only by moving to multiple characteristics can we incorporate many of the intrinsic qualities of individual goods (Lancaster, 1966:134)’. Given our focus on microfinance, we argue that the utility or disutility of microfinance stems from the effect of the different features (group lending, targeting women, microloans, savings, interest rate and non-financial services) of microfinance interventions. With this understanding, the discussion turns to investigate the contribution of these different features to the overall poverty reduction effect.

3.2 MICROFINANCE IN THE CONTEXT OF THEORIES OF FINANCIAL DEVELOPMENT AND INTERMEDIATION

There is no specific theory of microfinance yet. However, given that microfinance emerged from the initial focus on microcredit and that microcredit remains a key component of microfinance interventions, the theoretical argument for microfinance is located in the mainstream finance literature. This is particularly the financial development and financial intermediation theories. These theoretical models demonstrate that financial markets, institutions, and instruments may arise to mitigate the impact of information and transaction costs. ‘In emerging to ameliorate market frictions, financial arrangements change the incentives and constraints facing economic agents (Demirgüc-Kunt and Levine, 2008: p1)'. Despite the emergence of financial institutions, an additional literature on financial exclusion argues that certain people in the society, mainly the poor, are credit rationed and excluded from the mainstream financial system. In the light of this, it is argued that microfinance emerges to mitigate the information, enforcement and transaction costs involved in providing financial services to the poor and that in doing this; they lift the constraint facing the poor. This section reviews this theoretical literature and concludes with a discussion on how MFIs tackle these market frictions and provide financial services to the poor.

3.2.1 MARKET IMPERFECTIONS, INFORMATION ASYMMETRY AND IMPLICATIONS FOR THE POOR

In analysing the 'market for lemons', Alkerlof (1970) introduces the idea of the imperfection of markets with regards to information. He notes that for any market transaction, one party has more information about the transaction than the other party does. This notion is now known as the *theory of asymmetric information*. Applying this theory to credit markets, the borrower is more informed about the probability of success of his investment or the actual use of the loan than the lender. This raises major concerns for lending institutions as it creates problems of ***adverse selection*** and ***moral hazard*** (Stiglitz and Weiss, 1981).

The problem of adverse selection arises because the borrower is relatively more informed *prior* to the disbursement of the loan. Specifically, because the lender lacks sufficient information to determine the probability of success for each investment, it may approve loans to risky (low probability to repay loan) investments and yet reject safe (high probability to repay loan) investments. The problem of moral hazard arises because the lender relatively lacks sufficient information to monitor the actual use of the loan *after* it has been disbursed. The risk here arises because when a lender lends credit to a borrower, the lender's risk and therefore its expected return is tied to certain unobservable choices made by the borrower. Lenders cannot control the choices made by borrowers with regards to how much work to put into the project, which particular project to choose, or the decision to repay loan after the realization of project returns. While the former deals with selection, the latter deals with monitoring the loan to ensure repayment.

To identify low-default probability borrowers, lenders make use of different screening devices. One argument is that the lender can charge high interest rates sufficient to cover the risk of default. The assumption is that only borrowers with high profit projects will be able to afford high rates. However, individuals willing to borrow at high interest rates do so because they perceive their probability of default to be high. Hence, the average ‘riskiness’ of borrowers increases with high interest rates. This increases the possibility of defaulting loan repayment and hence lower bank profits (Stiglitz and Weiss, 1981). On the other hand, since the return on the project depends on the interest rate, the action of the borrower is likely to be affected by changes in the interest rate. For example, high interest rate means borrowers have to pay more for profitable projects, which decreases their return on successful projects. The borrower therefore uses the interest rate as a screening device for which project to invest in. Borrowers are induced to avoid low-yield investments in favour of high-risk high-yield investments in that on the upside returns are unlimited whereas on the downside losses are limited. Borrowers therefore undertake projects with high probabilities of default but higher returns when successful. This is the moral hazard effect – a trade-off between charging high interest rates and inducing borrowers to undertake projects with high probability of success (Stiglitz and Weiss, 1981). Although it is expected that higher interest rates should increase the return to the lender in a non-default state, the moral hazard effect may be strong enough to create sufficiently high loses to reduce the overall return to the lender. These adverse selection and moral hazard problems lead to ‘market imperfections’ – a situation where the market is unable to allocate resources efficiently.

Considering these market imperfections, the theories of financial development (Merton and Bodie, 2004; Demirgüc-Kunt and Levine, 2008) argue that financial institutions, markets and instruments may emerge to mitigate the effects of these information, enforcement, monitoring, and transaction costs. For example, the ability of banks to improve the acquisition and enhance the availability of information about managers or borrowers or borrowers and lenders will certainly improve resource allocation. Likewise, the presence of financial institutions that can monitor investments through various financial contracts and instruments will increase investors’ confidence and influence saving allocations. It is important to note that though financial intermediaries ameliorate the effects of these costs, they do not eliminate them. Hence, they also face the problems caused by information asymmetry and adopt different screening devices to tackle them. Recognising the potential increase in loan default and therefore lower profit that may arise from screening through interest rate, banks are more likely to prefer credit rationing and the use of collateral as screening techniques (Stiglitz and Weiss, 1981).

As regards the former, Jaffee and Russel (1976) present a credit market model consisting of two types of borrowers. They include: honest borrowers, who accept loans only if they perceive they will be able to make repayments, and dishonest borrowers, who as long as the cost of default is sufficiently low would default on their loans. They assume that honest borrowers prefer smaller loans relative to dishonest borrowers and that the bank is aware of the proportion of honest and dishonest borrowers in the market. Still faced with the problem of adverse selection, the bank is forced to place limits on the amount of loan granted in order to induce self-selection of borrowers and limit the probability of default. Hence, the bank is better off with rationing credit than with increased interest rates (Stiglitz and Weiss, 1981). Similarly, Williamson (1986, 1987, and 1988) presents a theoretical model that illustrates why in mitigating monitoring and verification costs banks are likely to ration credit by limiting the number of loans such that only investments requiring large credit will access credit. He argues that given the large equity required for these projects, the borrowers are more likely to be prudent with their investment and select projects with less probability of default. As regards the use of collateral to enforce loan repayments, the bank retains the right to the asset until the loan is completely paid and in the event of a default, can sell the asset to recover the money lent (Bernanke and Gertle, 1989, 1990).

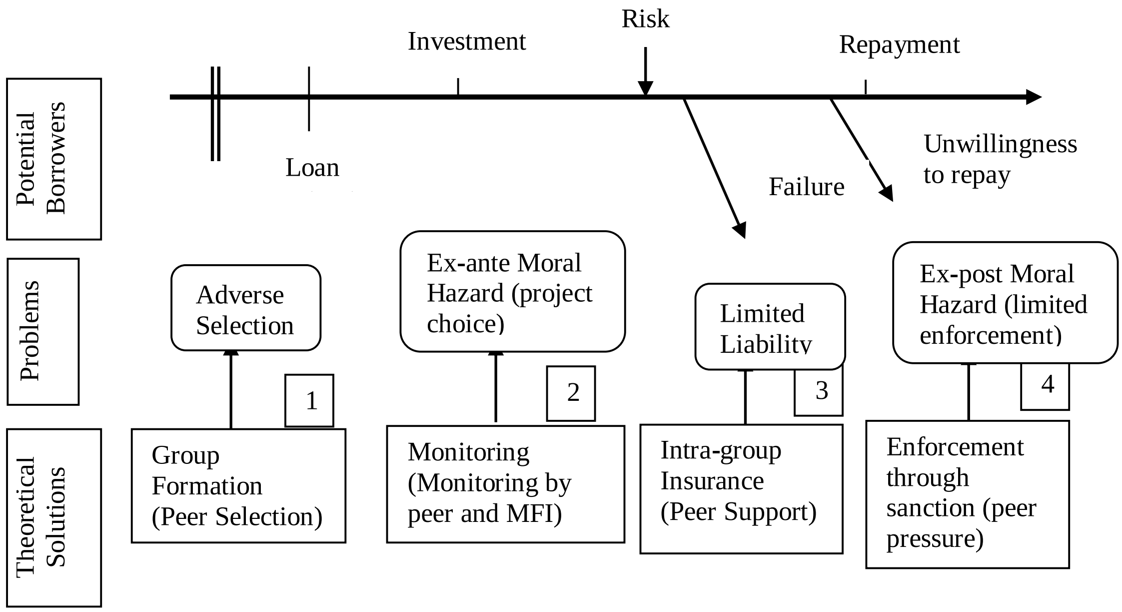
When we consider these screening techniques, the result is a situation where the poor and other disadvantaged groups often face difficulty or complete exclusion from access to and/or use of mainstream financial services appropriate for their cultural, socio-economic needs and status. This process is referred to as financial exclusion (Leyshon and Thrift, 1995). Although the reason for exclusion may differ over time and for different situations, the financial system has a natural tendency to cater for the socially powerful and exclude poor and disadvantaged groups. For instance, since information regarding the creditworthiness of the non-poor (e.g. governments, transnational corporations, and other rich and influential economic agents) is publicly available, they can borrow huge funds in the spot market at very short notice and at low interest rates. The presence of publicly available information ameliorates the cost of acquiring information to assess their creditworthiness. This acts as an incentive for potential lenders to supply credit to this class of borrowers; and also shifts power to the borrowers as they are in a position to choose from a variety of willing potential lenders. The opposite is the case with regard to lending to the poor due to the associated high information cost (Armendáriz de Aghion and Morduch, 2010). Additionally, with regard to credit rationing and the use of collateral as screening devices, these factors tend to favour the rich and powerful economic agents. For instance, with regard to the availability of collateral, the poor do not often own assets that pass for collateral.

While the high information cost associated with providing financial services to the poor is a little complex, the problem of high transaction cost is relatively straight forward. Providing financial services to low income households (LIHs) is characterised with relatively high transactions costs since handling several small transactions is more costly than servicing one large transaction for a wealthier borrower. From these debates, the evident implication for the poor is a shortfall in the supply of credit and a wider exclusion from financial services. This sets the stage for microfinance and presents a convincing argument for the provision of financial services to the poor. The question is: how do MFIs succeed in ameliorating the high information and transaction costs involved in providing financial services to the poor when the mainstream financial institutions fail to do so? In answering this question, this discussion turns to the group lending feature of microfinance.

3.2.1.1 Group lending as a Mechanism for tackling Market Imperfection and Information Asymmetry

Group lending refers to a lending technique where the ‘poor’ who often lack access to mainstream financial services are required to come together as a group for the purpose of accessing financial services (Ghatak, 1999; Armendariz de Aghion & Morduch, 2010). It is a key component of microfinance which enables MFIs to mitigate the information, transaction, monitoring and enforcement costs associated with lending to the poor. This is explicitly illustrated in the dynamic group lending model (see Figure 3.1 below) proposed by Simtowe and Zeller (2006).

Figure 3.1: Dynamic Group Lending Model



Source: Simtowe and Zeller (2006)

In ameliorating information costs, the group lending contract makes use of valuable resource that the individual-liability contract does not – being the information borrowers have about each other (Ghatak, 1999). This is the ability of potential borrowers to utilise local information about each other's project – 'risky' or 'safe' – in order to select the best partners (Ghatak, 2000; Armendariz de Aghion & Morduch, 2010). It has been argued that explicit or implicit joint liability (i.e members are jointly liable for loan repayments in the case of any defaults in the group) encourages self-selection in the form of assortative matching. This is known as ***peer selection.*** Implicit in this model is that during group formation, safe borrowers have keen preference for selecting perceived safe partners as a measure to checkmate and lessen joint liability payments. Here, risky or safe borrowers form lending groups with their kind (Ghatak, 2000).

As regards monitoring costs, given the joint liability feature of microfinance, service users also have an incentive to monitor loan usage by their group members. This is known as ***peer monitoring***. This involves scrutinizing their group members to ensure that loans are not used in a way that endangers loan repayment. This is likely to enhance repayment and avert strategic defaults as group members can verify the project returns of their peers, thus mitigating ex-post moral hazard (Aghion, 1999). Two other features of the group lending contracts expected to ameliorate enforcement costs include ***peer support*** and ***peer pressure***. Here, group members are required to willfully support or forcefully repay the loan repayment of a defaulting member. Where members are willing to contribute and make repayments, the group lending process continues and the enforcement cost is borne by the group members. However, if the non-defaulting members are unwilling to meet the obligation of the defaulting member, this might result in a total collapse of the lending contract. Here, the MFI bears the loss of the loan obligation as well as any enforcement costs; and group members bear the loss of future access to loans, and in some cases any savings contribution. Even when peer support comes through, group members may need to induce loan repayments through peer pressure and/or social sanctions. Particularly for groups where peer monitoring is low, sufficiently strong social sanctions may be capable of enforcing high repayment performance. It is considered as a tool for mitigating ex-post moral hazard (Besley and Coate, 1995). Additionally, the practice of group lending increases the size of financial transactions and ameliorates the transaction costs involved in providing financial services to the poor.

Unlike the more obvious mitigation of transaction costs by lending to groups compared to poor individuals, there is mixed empirical evidence on the ability of group lending to ameliorate the high information, monitoring and enforcement costs associated with providing financial services to the poor. In a critical analysis of evidence from Peru, Marr (2001) argued that the above theoretical frameworks which propose the ability of microfinance to achieve financial sustainability and poverty reduction through group lending are based on over-simplistic and unrealistic assumptions. Take for instance, positive assortative matching that is expected to result from peer selection; this is based on the assumption that group members have perfect information, or can raise the required information without costs Ghatak (1999, 2000). This underlying assumption weakens the strength of this argument. In accounting for this setback, Aghion and Gollier (2000) construct a model that assumes imperfect information. They argue that in the absence of assortative matching, group lending still improves market efficiency. However, this claim is based on their unrealistic assumptions that prospective group members have prior knowledge of the costs of auditing loan use and repaying for peer defaults. Since the actual value of costs can only be ascertained from group interactions, the assumption of perfect *ex-ante information* limits the strengths of their findings. Additionally, these models fail to account for the possibility of heterogeneous group formation.

Similar arguments can also be made as regards the assumption of peer monitoring. For example, theoretical models by Stiglitz (1990) and Varian (1990) are based on certain assumptions that are highly restrictive: (1) perfect and costless information amongst borrowers; (2) costless monitoring of peers; and (3) no alternative source of credit. Even when other studies (Aghion, 1999 and Conning, 2000) allow for costly monitoring, they assume that borrowers can impose costless social sanctions on defaulting clients to secure loan repayments. However, studies that investigate social sanctions allowing for perfect information (Besley and Coate, 1995) and imperfect information (Diagne, 1998) amongst borrowers, find that peer pressure only works because of the intolerance of potential defaulters' to *passive* social sanctions, signifying that *active* social sanctions inflict costs on service users that diminish the effectiveness of group lending.

Outside the unrealistic assumption of complete information and costless social sanctions, these models rely on certain incentives to induce individuals to screen, monitor their peers and enforce repayment; in order to checkmate and lessen joint liability payments and achieve high repayment rates (Ghatak, 2000). These incentives include: the cost of joint liability (paying for defaulters), and dynamic incentive (i.e. continuous access to increasing credit if prompt repayment is made); and are expected to be effective due to the assumption that all things being equal, people minimise costs. However, these models ignore the fact that regardless of the incentive, performing group duties might come as a cost to service users, thus, creating an additional incentive for them to find possible ways to reduce and/or transfer these costs to other group members. These complex social relationships that develop amongst joint liability group members are therefore vital in assessing the poverty-reducing potential of microfinance.

Yet, empirical impact studies almost exclusively focus on the end-use of microfinance when assessing poverty outcomes, largely overlooking the effect arising from group interactions, implying that the internal group dynamics is neutral in influencing ultimate poverty outcomes. While some studies (Painter and Mknelly, 1999; Wydick, 1999; Copestake et al., 1998; Montgomery, 1996) focus on single aspects of group dynamics, very few studies (Marr, 2001; Yeboah, 2007) explore the complete set of duties (i.e. peer screening, monitoring, and so on) that service users are compelled to carry out when participating in joint liability based group lending. This is an area in which this study intends to make a contribution.

In examining financial transactions amongst agricultural farmers in the Philippines, Floro and Yotopoulos (1991) find that personal kinship relationships played an important role in mitigating information cost and moral hazard problems. Similarly, findings from Northern Nigeria showed that group and credit transactions occurred between kinsmen. This makes information on default easily obtainable; thus, ameliorating the moral problem. However, field observation shows that this is not always the case. Empirical findings suggest that not all lending groups are formed through peer selection. For example, in the case of FINCA affiliates in Peru, potential borrowers are added to a list of other potential borrowers which then forms a group, disregarding the importance of an existing relationship between members (Karlan, 2003; Marr, 2002). Hence, members had limited and shallow information about the level of risks of their peers. Likewise, while homogeneity among members in terms of social class is expected to enhance cooperation and consensual decision-making, this can also be a downfall as this can be channelled negatively. Particularly with groups comprising of close relatives and members with strong social ties, it was often the case that when information of possible threat to repayment was obtained, it was often hidden or not disclosed to the group or the MFI officers (Marr, 2002).

Additionally, effective monitoring requires that group members maintain good knowledge of the use of loans by their peers. However, achieving perfect knowledge is a difficult and costly process. Even when this information is available, divulging such information may attract negative consequences as such a member may be labelled as an informant. Hence, service users weigh the net effect of monitoring before deciding to monitor their peers. With regards to the implementation, empirical evidence from Malawi and Peru find a partial and passive peer monitoring process (Simtowe and Zeller, 2006; Marr, 2002). Overall, the transfer of liabilities and responsibilities from MFIs to the service users also implies a shift of the responsibility for these costs (Armendariz de Aghion & Morduch 2010). The greater the information, monitoring, and enforcement costs, the lesser the effectiveness of group lending in ameliorating them. With this mixed result, it is important to explore how effective group lending is in ameliorating and transferring the information, monitoring and enforcement costs to the clients. Particularly for clients, how do they deal with these costs, how does the practice of group lending affect the utility or disutility they experience with using microfinance and in turn their potential for capability expansion? These are important questions that need to be addressed.

3.2.1.2 Summary

In conclusion, beyond this mainstream neo-classical institutional economics (NIE) approach which focuses on information and transaction costs as the reason for fragmentation of financial markets, there are other approaches to theorizing and investigating the exclusion of the poor from financial markets. First, Dymski (1998:2) argues that the NIE approach represents a thin and problematic explanation of the financial exclusion of the poor. He notes that it does not recognise that exclusion may be due to unequal power relations or social structural factors accumulated overtime. He particularly argues that 'agents, in turn, are often complexly constituted, not simple; and they are often embedded in thick social relations which mould their behaviour in markets'. As Hospes (1996:13) writes, financial systems can be viewed as 'social systems sustained by actors who are not only participants of these systems but also of other social systems, such as ethnic community, an extension program, an office, a neighbourhood, a religious society, a group of entrepreneurs, that affect or somehow embed financial systems'. This approach sits within the political economy literature which emphasises the ability of social structures and power relations to foster financial exclusion of the poor.

Similarly, Johnson (2005) presents an alternative institutional-based approach to understanding the exclusion of the poor from financial markets. By exploring the governance structures (contractual policies, enforcement and monitoring mechanisms) that guide the operations of financial intermediaries, she argues that these structures, as well as other price and non-price mechanisms of financial intermediaries (formal and informal) are influenced by and embedded in underlying cultural, social and political factors. For example, the difference between price (e.g. interest rates) and non-price features (e.g access to loans and enforcement of loan repayments) in banks versus rotating savings and credit associations (ROSCAs) can be tied to their organisational structure. Based on banking law, banks are obliged to protect the deposit of savers and to make profit for shareholders through the design of loan and savings services. In order to do this, shareholders appoint the management who monitor savings and enforce the repayment of loans, including the use of collateral-based lending and the use of contract law to claim collateral in case of default. In contrast, with mutual organisations, prices and repayment enforcement mechanisms are set by members in their own interest and with some flexibility. This implies that beyond information and transaction costs, fragmentation is caused by one, fundamental organizational differences and two, how norms, cultural and social relations influence the formation and functioning of various financial intermediaries.

In applying this line of thought to the financial inclusive literature, Johnson (2013:6) argues that in order for financial inclusion to be addressed, we have to identify and address the wider social relations that create poverty and exclusion. She argues that an increased understanding of the way social institutions influence markets is crucial for an effective analysis of how markets work. For example, social structures such as gender, class, ethnicity (caste) have been known to create or shape fragmentation in the credit market (Johnson, 2004), and labour market (Folbre, 1994; Rogaly, 1996, Copestake, 2006). These social institutions create social processes and differences through which exclusion and inclusion in the economy works; thereby playing a role in the creation of poverty. Therefore, she argues that investigation into the impact of microfinance on women empowerment should not just examine the outcome (i.e. whether women are empowered or not) but should rather explore the gender relations that women face both within and outside the household that foster the exclusion from markets. As she writes: ‘How then can institutional developments to promote an ‘enabling environment’ and supportive institutions be understood if what is ‘disabling’ with respect to inclusion has not been identified?’.

It is important to note that these new approaches do not challenge the NIE explanation for financial exclusion. Rather, they challenge the assumption that any approach which ignores the social context and cultural and social embedding of credit markets can offer a true or complete explanation for the fragmentation in financial markets. It also challenges the assumption that prescribing institutional developments for promoting inclusive markets can be detached from identifying and understanding the causes of exclusion. This focus on social institutions is more in line with the SE approach to poverty which pays more attention to the processes and dynamics that engender deprivation as well as the outcome of exclusion. In all, all of the above approaches are different strands of the same literature and can only explain certain dimensions or causes of exclusion. Hence, a richer understanding will be to integrate findings from the various strands or adopt approaches that are broad enough to identify all the disabling factors with respect to inclusion.

As regards this study, it is not our intention to analyse the factors that foster poverty or financial exclusion. Our emphasis is rather on evaluating the poverty reducing potential of microfinance from the clients’ perspective. The debate here is whether a meaningful evaluation of the poverty reducing effect of microfinance can be conducted without due consideration of the processes or structures that create poverty? The researcher argues that this is possible, but recognises that the analysis will have limited relevance for making recommendations as to the promotion of capabilities. Nevertheless, by operationalising the CA as an evaluative framework, we are able to recognise and account for some of the social structures and institutions that shape capabilities; without committing to the task of investigating the wider social relations that create poverty and foster exclusion.

In line with this notion, this study agrees that institutional relations are critical to comprehending how various social groups achieve expansion of their different capability sets. For instance, for microfinance clients, the lending group plays a crucial role in the extent to which microfinance clients can successfully take advantage of MFIs to access microfinance. Acceptance in a lending group offers the opportunity to obtain credit while the exclusion from a lending group restricts the access to resources. This implies that beyond ameliorating information and transaction costs, group lending increases the social capability of the poor. This is the recognition that access to microcredit for the poor is currently and perhaps also in the future, dependent on their participation in the group, such that changes to the entire group are very much likely to affect individual capabilities.

Particularly, beyond MFIs, other social institutions play an important role in perpetuating the conditions of poverty by enhancing or limiting the freedom of choice and opportunities of the poor. More importantly, beyond institutions outside of the household, access to opportunities is also influenced by relations within the household. The household plays a crucial role in the construction of gender identity and in shaping gender differences in access to opportunities and resources. Very importantly, social institutions can have positive or negative impacts. With the former, the poor gain access to resources; and in the latter, they may suffer from conflict, greater insecurity, and oppression. However, while this study recognizes the role of social structures in shaping individual and social capabilities, this study is limited to the role of the lending group and social relations within the group to increase the capability of the poor.

3.3 APPROACHES TO MICROFINANCE

Changing perceptions of poverty have over the years driven changes in the rationale for and the implementation mode of microfinance. With a meritocratic explanation to the causes of poverty in the 1950s, when the poor were assumed to be incapable of saving sufficient funds to accumulate assets and therefore could not afford collateral for credit, agricultural development banks (ADBs) were introduced and funded by international donors and national governments to provide microcredit, to the poor. By the 1980s, the realization that contrary to earlier beliefs, the poor were not ignorant; but rather they were potential entrepreneurs who lacked an institutional environment that would provide them with the opportunity to contribute their part to the development process (Chamlee-Wright, 2005). With this understanding came the claim that providing microcredit to poor households enables them to set up a microenterprise, improve their income, and eventually escape the vicious cycle of poverty. However, this had to be heavily subsidized to offset some of the high information and transaction costs associated with providing financial services to the poor.

Uncomfortable with this endless dependence on subsidies, the USAID and the World Bank, took decisive actions to phase in a new commercialized microcredit model[8] that is characterized by a profit-driven private-led business model (Bateman and Chang, 2012). The idea that lending to the poor can be a profitable venture with large profits[9] recorded by MFIs increased the spread of this new model across Asia, Africa and other continents. Although this new commercialised model includes the provision of other financial and non-financial services to the poor, which has led to a shift from 'microcredit' to 'microfinance', it has been argued that it also creates a double bottom line resulting in a struggle between the goal of financial sustainability and the goal of serving the poor. Based on this brief history, we can identify two separate approaches to providing financial services to the poor: (i) poverty reduction and (ii) profit. While the former employs microfinance as a development policy tool, the latter considers it to be a profitable business opportunity. This section reviews these two approaches, namely: the *poverty reduction* and the *financial systems approach*.

[8] Despite this commercialization of microfinance, it however remains very different from conventional banking. As will be discussed in section 3.6, certain distinguishing factors include its unique features such as the micro size of loans, gradual micro increases in loan size, group lending, joint liability, non-collateral lending etc.

[9] With regards to profit sharing, it varies across different institutions. For the Grameen bank, the borrowers own 95 percent of the total equity, while the Bangladesh government owns 5 percent. For LAPO Nigeria, 97 percent of the bank is owned by the LAPO NGO, while 13 percent is owned by the CEO.

3.3.1 POVERTY REDUCTION APPROACH

Microcredit is here perceived as a tool for poverty reduction and empowerment through subsidized credit. It places little emphasis on the financial sustainability or profitability of the MFI but rather focuses on the provision of subsidized credit to the poor and extreme poor to help them escape poverty. Other financial services such as savings and insurance are not normally core components of this approach; except for some microcredit interventions where mandatory savings is a requirement for receiving a loan (Gulli, 1998; Robinson, 2001). Particularly advocated by Yunus this approach rests on the idea that as much as productive opportunities exists, through access to microcredit, the poor are able to stabilize incomes and ameliorate vulnerability to risk (Zeller and Meyer, 2002); acquire human capital and physical assets, and escape poverty.

However, Bateman and Chang (2012) argue that this argument for a positive relationship between microcredit and poverty reduction is rather ambiguous. For instance, in the absence of productive opportunities, repayment capacity will typically be lost and repayment enforcement is more likely to impoverish borrowers. Hence, access and use of microcredit by the poor can decrease or increase poverty, depending on the availability of productive opportunities as well as other factors (Gonzalez Vega, 2003). It is also argued that while the economically active poor may be able to effectively use credit and make repayments, the extremely poor may not (Robinson, 2001). This may be due to lack of profitable self-employment (Hulme and Mosley, 1996), or lack of relevant skills needed to effectively use the loans, which creates greater risk (Charitonenko and Rahman, 2002).

Hence, this approach emphasises the inclusion of training programmes in financial initiatives targeted at the poor. This is based on the assumption that the poor need to develop the relevant business, financial, agricultural, literacy skills and training required to make effective use of financial services (Gonzalez Vega, 2003). However, two major drawbacks of this idea includes: first, the associated cost of providing these non-financial services may impede the MFIs financial sustainability; second, the relevance of the training provided by the MFIs to the trainees is in question. On the one hand, it is argued that the trainings are not often tailored to suit the unique business needs of the poor. On the other hand, it is argued that the service users are not intellectually able to grasp and thus properly value and use the training provided. The point to be learnt here is: it is not enough to integrate training; but the *right training* at the *right time* provided in the *right way* to enhance a profitable use of credit (Yeboah, 2010).

The ability of other development tools (e.g. education [10], housing, health, infrastructure) to be more effective in tackling poverty than credit, has also been raised. It is argued that beyond the access to and use of credit, the poor require basic needs of food, water, shelter, clothing, healthcare and presumably education to be able to make effective use of loans (Robinson, 2001; Charitonenko and Rahman, 2002). With regards to the narrow emphasis on credit, it is evident that credit is often not the major constraint faced by the poor – poor households demand a variety of services (Gulli, 1998; Gonzalez Vega, 2003). For instance, in the presence of binding constraints, which is often the case with the poor, access to credit does not guarantee the creation of profitable productive opportunities. Access to credit for the poor does not compensate for the absence of roads required to transport farm produce; lack of technological knowhow or other socio-cultural factors that may impede the profitable use of credit (Gonzalez Vega, 1994 and 1998a).

However, MFIs with a focus on poverty reduction have failed to satisfy the demand from the poor, in terms of both outreach and financial sustainability (Robinson, 2001). In an investigative study of rural finance, Gonzalez Vega (2003) explains that notwithstanding several efforts to expand the supply of subsidized credit for agriculture, using a considerable amount of public fund, a good number of the rural poor in developing countries do not have access to financial services. Additionally, with huge dependence upon a continuous inflow of subsidized credit, at least in the short run, it became evident that this approach cannot be sustainable. It is argued that even if a positive relationship between access to credit and poverty reduction is assumed, sustainable microfinance established on the basis of cost effectiveness is a better approach. Two adduced reasons for this include: (i) financially sustainable MFIs can leverage funds for their loan portfolios by accessing commercial debt, mobilizing public savings, or making profitable investments; and (ii) given the importance of financial services to the poor, a long-term access is required (Robinson, 2001;

[10] Although education is a major component of human capital development, its use here is different from the human capital formation mentioned above. Compared to a holistic education programme that can be designed to meet different dimensions of human capital development, the contribution of microfinance towards human capital development may be limited in terms of the services provided. Also, the argument is that if education is a better tool for human capital development, the transference of resources to microfinance interventions would mean that these resources are employed below their optimal use.

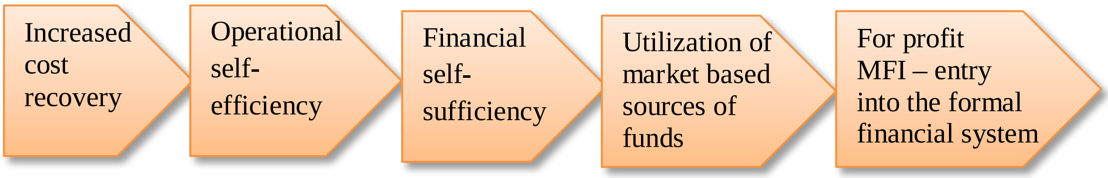
Gonzalez Vega, 2003). These arguments therefore support the call for a rather more financially sustainable approach – the financial systems approach.

3.3.2 FINANCIAL SYSTEMS APPROACH

Under this approach, microfinance is purely perceived as the business of providing financial intermediation to the poor and low-income households. Unlike the poverty reduction approach which emphasises the provision of credit and other non-financial services, this approach emphasizes other core components of financial services such as savings, insurance and remittance services (Gonzalez Vega, 2003; Adams, 1995). The main supposition with the financial system approach is that the innovative lending techniques employed by MFIs make the provision of financial services to the poor not only possible but also profitable (Robinson, 2001). Particularly, it is argued that there is no need to set poverty reduction as the goal of microfinance. The fact that the poor can borrow and make repayment is sufficient evidence that the services provided are of value and profitable for both the bank and the clients thus, subsidized credit is not needed (Gulli, 1998).

It is believed that with considerable supportive macroeconomic, political, legal and regulatory conditions, MFIs can be developed to provide financial services on a sustainable basis to the economically active poor and low-income households (Robinson, 2001). One implication of this goal of financial sustainability is that microfinance is directed towards low-income economic units who are able to make use of financial services, not necessarily the extreme poor (Rhyne, 1998; Gulli, 1998). It also requires that financial services to the poor be provided at interest rates that take account of all overheads – including risks – and generate profit. MFIs are expected to employ full cost recovery pricing approach and expand their loanable funds through savings mobilisation sourced domestically, commercial debt, profitable investment, and ploughed back profits (Robinson, 2001). This is expected to enhance large scale outreach with wider range of financial services. The emphasis on savings mobilization rather than reliance on government and/or donor funding is consistent with the goal of creating independent MFIs. This obligation to achieve financial self-sustainability has therefore driven the 'commercialization of microfinance'.

Figure 3.2: Paths to Microfinance Commercialization



Source: Charitonenko and Rahman (2002)

Commercialization of microfinance is an ideology that hints at the use of market-based theories with a steer or shift towards profitability of MFIs. The seeming sustainability of this approach is reliant on governments' commitments to the liberalisation of the financial markets with reduced targeting of loans; institutional governance and capacity of the MFIs, better pricing of financial products, and knowledge of the market (Von Pichske, 1991). It also requires the ability to adopt innovative lending techniques[11] that curtail costs and risks; appropriate products that meet the needs of the poor and attract low income borrowers and savers; innovative operating and information systems; specialized staff training; interest rates that guarantee institutional profits; and others (Quach, 2005). With these foundational requirements, the microfinance industry has called on national governments to introduce regulatory and supervisory framework policies for MFIs. For example, the Nigerian microfinance policy framework was introduced by the CBN in 2005 and revised in 2011. Also, existing donor funding is more likely targeted towards institutional development rather than financing of loans.

However, the goal of providing sustainable financial services implicitly implies that MFIs provide financial services to the poor, whenever they find it profitable to do so. The removal of subsidy and the absence of interest rate restrictions could make the market for the poor become even worse as the market occupiers may act in their own interest. A good example of this is the existing 'mission drift' which is increasingly becoming evident among MFIs. Mission drift arises when MFIs 'finds it profitable to reach out to unbanked wealthier clients while at the same time crowding out poor clients'. This includes the targeting of wealthier clients in an attempt to avoid monitoring costs and loan arrears. Simply put, unbanked wealthier clients cost less relative to poor clients. Take for instance the mission of poverty reduction and assume that a good proxy for outreach to the poor is the average loan size. Then, 'the smaller the average loan size, the greater the depth of outreach in the microfinance parlance'.

[11] Some of the innovative lending techniques used by MFIs such as joint liability, progressive lending, frequent repayment etc are discussed in the next section.

Hence, mission drift occurs when the average loan size of an MFI increases as it reaches out to wealthier clients neither for cross-subsidization nor for progressive lending reasons[12], but solely for profit (Armendáriz and Szafarz, 2009:2).

In conclusion, in addition to the differences between these two approaches highlighted in table 3.1 below, this study recognises the conflict between the social goal and the profitability goal. First, the poverty reduction approach falls short because it centres on a social objective without recourse to profitability which is important for financial sustainability. Second, the financial system approach centres on profitability without recourse to the impact on the poor.

Table 3.1: Poverty Reduction versus Financial System Approach to Microfinance

Features	Poverty Reduction Approach	Financial System Approach
Problem definition	Overcome market imperfection	Lower risk and transaction costs
Role of financial markets	Promote new technology Stimulate production Implement state plans Help the poor	Intermediate resources more efficiently
View of users	Borrowers as beneficiaries selected as targeting	Borrowers and depositors as clients choosing products
Subsidies	Large subsidies through interest rates and loan default Create subsidy independence	No or few subsidies Create independent institutions
Sources of funds	Governments and donors	Mostly voluntary deposits
Associated information systems	Designed for donors	Designed for management
Sustainability	Largely ignored	A major concern
Evaluations	Credit impact on beneficiaries	Performance of financial institutions

Source: Quach, 2005

Despite the significant support for the financial system approach, the conceptualization of poverty as capability deprivations in this study i.e. a multidimensional approach, requires a balance between the financial systems approach and the poverty reduction approach with due consideration of cost-effectiveness. This thesis therefore joins other studies (Charitonenko and Rahman, 2002; Gonzalez Vega, 2003; Quach, 2005) in the

[12] Cross–subsidization refers to the targeting of 'unbanked wealthier clients in order to finance a larger number of poor clients whose average loan size is relatively small'. Progressive lending on the other hand is a feature of microfinance and implies that existing clients can access higher loans upon satisfactory repayment of previous loan (Armendáriz and Szafarz, 2009).

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call for a mixed approach to microfinance. This approach would enable the achievement of both financial and social objectives. This mixed approach maintains a balance between the social and profitability goal through a combination of social intermediation (which is distinct and provided by government and donors) and financial intermediation. Here, while MFIs focus on financial intermediation under the regulation of the appropriate authorities, government and donor support would focus on social intermediation for the poor. Microfinance can therefore be approached as financial intermediation for the poor with government and donor support.

First, this support can be in terms of creating an enabling financial environment and sound informational intermediaries that aid financial intermediation for the poor. These actions should be targeted towards institutional development rather than direct subsidy to the cost of financial services. This could include (i) encouraging the adoption and development of financial technologies that would ensure reduced risk of financial transactions at reasonable cost; and (ii) enhancing the institutional infrastructure to support the application of these new technologies (Gonzalez Vega, 2003). Second, donor funding and government support should be directed towards the provision of non-financial services such as improvement of physical infrastructure, job creation, trainings on business skills, education and health care i.e. social intermediation to the poor. Three key consumer protection strategies identified by CGAP include: building consumer financial capability, establishing industry-wide codes of conduct and government regulation (McKee et al., 2011). Service users need to be empowered with the knowledge and understanding of competing products and the ability to choose what services is best suitable to their needs. Given the information asymmetry between the service users and providers, government support targeted at increasing the financial literacy, financial capability and financial education of the poor is expected to equip service users with basic information and skills to make informed financial decisions.

It is important to note that although the introduction of favourable economic policies is a necessary condition for expanding financial outreach in rural areas; this is not sufficient (Gonzalez Vega, 2003). The establishment of institutional and physical infrastructures that enables serene operation of financial agents is requisite for rural financial deepening. Although these forms of government and donor supports can be seen as a form of indirect subsidy, they are different and a preferred choice to the direct subsidy of the costs of financial services. Commercial MFIs can therefore provide additional benefits for their clients by partnering with these social intermediaries. With this detailed review of the literature on microfinance providing a good background for our understanding of microfinance, the next task is to construct a conceptualization of microfinance that will be applied in this study.

3.4 RECENT DEBATES IN THE LITERATURE

This section focuses on three main discourses which the researcher considers to constitute the recent debates in the microfinance literature. The first is the call for a shift to a client-focussed approach to microfinance following the recent client over-indebtedness that rocked the sector. The second is the growing concern that the perceived positive impact of microfinance is not been realised. This includes increasing evidence from more rigorous randomised control trials (RCTs) that questions the much anticipated positive impact. The third is the call for a wider focus on inclusive finance. The review of these recent debates is expected to enable the researcher identify a gap in the literature for which this study will be designed to fill, and then define research questions and objectives that will be relevant in the recent literature.

3.4.1 CLIENT OVER-INDEBTEDNESS

Beginning with the Initial Public Offering (IPO) by Compartamos a Mexican MFI in 2007, the carefully constructed edifice of modern microfinance began to crumble. It revealed how top executives of MFIs were able to privately enrich themselves by silently charging extortionate rates on microloans. This led to a widespread critique of the commercial microfinance model in general. Furthermore, by 2008, a number of devastating sub-prime microfinance meltdowns had begun in Morocco, Nicaragua and Pakistan. These meltdowns were marked by rapidly growing client defaults, huge client over-indebtedness, and massive client withdrawal. By 2009, the near-collapse of the microfinance sector in Bosnia was the centre of attention in the debate on microfinance (Bateman et al., 2012). The most devastating of all started in late 2010 in Andhra Pradesh, India (Arunachalam 2011). Owing to a high rate of over-indebtedness, huge recycling of loans to repay earlier microloans and high defaults, the Andhra Pradesh’s microfinance interventions effectively collapsed in late 2010.

At this point, long-standing supporters of microfinance openly expressed their concerns at the way the microfinance concept was being destroyed in the hands of neoliberals and hard-nosed investors (Harper 2011; Klas, 2011; Sinclair, 2012). The pursuit of financial sustainability meant that MFIs had to be profitable even at the expense of the poor.

> Commercialization of the microfinance sector has driven the growth (of the global microfinance industry) much faster than the sector could absorb. The growth was 200%, 300% growth, amazing. Then, there were lots of other pressures that came with growth and everybody's interest had to be taken care of. Maybe in the priority list, client interest became the least important one' (Vijayalakshmi Das cited in Reed, 2013:8).

Reviewing the state of microfinance following these happenings and in a bid to determine the way forward, various stakeholders during the 2012 microcredit summit campaign noted that:

> At a time like this, it is important that we *listen to clients and the people who work most closely with them* and know them best. We need to *approach the field from the clients' vantage point*-asking what it is that they are looking for when they utilize financial services-and redouble our efforts to ensure that the tools we provide will enable them to achieve what they most desire for themselves and their families….. When we use those standards as our measuring stick, when we design our financial services and other support systems so that our clients can achieve these objectives, then we will be providing a tool that our clients can use to help free themselves from the shackles of poverty' (Maes and Reed, 2012:1-2).

This therefore calls for a refocus on product design and delivery approach which appropriately takes account of client needs and characteristics. Here, an institutional response involving developing new products or making adjustments within the institutions cannot be the end game. We need to understand the contextual factors that influence the financial behaviour of the poor and which financial services they need and which benefit them the most, why and for what purposes. Understanding the 'how' and 'why' of consumer behaviour with regard to financial services requires an understanding of the heterogeneity of clients and how age, gender, life-cycle events, income level etc. influence their behaviour. This is because as people move through different cycles in life – from dependence on parents to independence; from school to work, to marriage, family responsibilities and possibly retirement, their financial needs changes. There is also the need to comprehend consumer behaviour and their use of financial services. Supporting finding from Schicks (2013) which draws from the field of economics, psychology and sociology and adopts a comprehensive framework in identifying the causes of over-indebtedness in microfinance shows that, beyond external and lender-related factors, client characteristics and practices are important causes of over-indebtedness. In 2011, Elizabeth Rhyne wrote in the Huffington Post: 'Like sex, microfinance can be safe if practiced responsibly' writes (Rhyne, 2011). There is though the question of what is regarded as safe and acting responsibly; and who is acting responsibly – that is the lender or the borrower? Investigating the features of microfinance interventions, their characteristics and implementation processes as well as the use to which microfinance is put will help us understand what 'safe and responsible' provision and use of microfinance entails.

3.4.2 EMPIRICAL LITERATURE

In spite of the apparent popularity and success of microfinance, there exists no clear evidence of positive impacts on poverty reduction (Stewart et al, 2010, 2012; Duvendack et al, 2011). There has been a recent drive in the international development community[13] towards encouraging more rigorous approaches to impact evaluations, particularly randomized control trials (RCTs). Impact evaluation is an objective and systematic assessment of the outcome/result achieved from a program. It entails the estimation of the average effects of a treatment or program on the outcome of interest. It begins with administering a treatment to a certain group called the 'treatment group' and setting aside another group called the 'control group' that does not receive the treatment. The goal here is to estimate the effect of the programme on the treatment group using the control group as a comparison. The biggest challenge of an impact evaluation study is to determine what would have happened to program participants in the absence of the program. A participant's outcome in the absence of the program (i.e what would have been) is referred to as the counterfactual.

The problem here is that while we can only truly assess program impact (independent of other factors) by comparing actual outcomes against counterfactual outcomes, we cannot observe the counterfactual. Hence, the main challenge is finding a control/comparison group that can appropriately substitute for the counterfactual (Khandker, et al., 2010). In addition, mainly comparing the mean differences of participant outcome after treatment with that of non-participants will result in biased results. For instance, if the assignment into a programme is not done randomly such

[13] See initiatives by 3ie (http://www.3ieimpact.org/) and the World Bank's Development Impact Evaluation (DIME) initiative (http://go.worldbank.org/1F1W42VYV0

that selection is based on certain characteristics[14] that make participants different from non-participants, then these studies are likely to suffer from selection bias thus, impeding the validity of the impact estimates (Caliendo 2006). It is argued that these problems can be ameliorated with the use of RCTs.

The application of RCTs to microfinance related studies has been propagated by the work of Banerjee et al. (2009), Karlan and Zinman (2009), and Duflo and Kremer (2005). It involves the random assignment of potential clients into ‘treatment’ and ‘control’ groups, such that both groups must consist of potential clients who are yet to be financially served, so that an evaluation of the impact of the programme can be done. Random assignment ensures that self-selection into treatment groups does not contaminate the potential outcomes. Proper randomisation also ensures that the treatment and control groups consist of individuals with similar observable and unobservable features, assuming no spill-over effects. Thus, the mean differences in individual outcomes are interpreted to be the treatment effect (Blundell and Costa Dias, 2002, 2008). This section presents a review of some of the recent RCT-based studies as well as prominent systematic reviews of the impact of microfinance.

The Banerjee et al. (2009) microfinance impact evaluation study evaluated the impact of microfinance on outcome variables such as business profits and revenues, consumption, asset acquisition, employment and empowerment. The endline survey was collected 15-18 months after the baseline. They concluded that ‘while microcredit succeeds in affecting household expenditure and creating and expanding business, it appears to have no discernible short-term effect on education, health, or women empowerment’ (p30). The study therefore concludes that microfinance may not be the ‘miracle’ it is sometimes claimed to be. For Karlan & Zinman (2009), the endline survey was collected 22 months after baseline. Sample consists of 1601 loan applicants, of which 1272 were randomly assigned to the treated group and 329 to the control. They find that the treated group did borrow more. Male borrowers tend to decrease employment outside the family, increase use of informal credit ‘to absorb shocks’, and experience a downsizing of the business with increased profit. No suggestion of further increases in well-being was found, but there was evidence of ‘a small decline in self-reported well-being’ (p18).

[14] Self-selection may be based on observable characteristics such as age, sex, gender, educational attainment, employment status and unobservable characteristics such as business skills, motivation, entrepreneurial ability etc. (Armendariz de Aghion and Morduch, 2010).

In a systematic review of the empirical evidence on the impact of microfinance (micro-credit and micro-savings) on the poor in sub-Saharan Africa, Stewart et al (2010:6) reviewed 35 studies which compared the impact of having microcredit or micro-savings with not having either. Of these, 15 studies including 4 RCTs, 2 non-RCTs and 9 case control studies were considered to be of good quality and thus included in the in-depth review. 11 of these study micro-credit interventions, 2 on micro-savings and 2 combined credit and savings. They find a positive impact of microfinance on savings, health, expenditure, asset accumulation, and housing. The impact of microcredit on education, nutrition, income, women empowerment, and job creation is found to be mixed. There is also mixed evidence suggesting that microfinance positions the poor to be more able to deal with shocks. They find that 'whilst both micro-credit and micro-savings have the potential to improve the lives of the poor, micro-credit in particular, also has potential for harm. Micro-savings may therefore be a safer investment for development agencies.' They argue that this is particularly so when microcredit clients spend credit on non-productive consumption or long-term future investment rather than immediate future investment; or whose long-term future investment or businesses fail to generate sufficient returns to cover the interest rates. Based on these findings, the authors call for more empirical studies to investigate the features and characteristics of microfinance that have the potential for both good and harm; and that this should be taken into account when promoting the use of microfinance in SSA.

Another systematic review of the empirical evidence on the impact of microfinance is conducted by Duvendack et al., (2011). Using certain criteria[15] such as the clarity of research question, random assignment of participants amongst others, the Duvendack et al. study screens the existing body of microfinance evaluation literature to identify the more rigorous and valid studies. 58 more rigorous studies were selected from an initial pool of 2643 studies, and reviewed based on the research design adopted. They show that a majority of the previous impact studies are seriously biased, incomplete or else very poorly designed to the point of being quite unusable. They reached an explosive conclusion, arguing that "[the] current enthusiasm [for microfinance] is built on [...] foundations of sand" (p. 75) and that the support for microcredit having been made not so much on the basis of the *economics* (of poverty reduction and development), but to the *politics* of the neoliberal economic ideology.

[15] See Duvendack et al., (2011) for a complete list of the criteria used in determining the validity of the impact evaluation.

Similarly, Pande et al (2012) conduct a systematic review of studies that examine the impact of formal banking services (credit, savings and transfers) on the incomes of the poor in low and middle-income countries. They focus on the impact on household income, assets, and consumption; small and micro-business investment, income, asset and output; and other poverty indicators. 12 studies reviewed include three RCTs, four quasi-experimental studies, and five observational studies which investigated the impact of formal finance or financial technology on poor people's income. They find convincing evidence that access to formal banking can raise the income of the poor. The pathways through which this occurs include: first, new savings products that break traditional barriers and address physical and behavioural barriers, increase savings and enable asset accumulation. Second, improving banking technology facilitates remittances, consumption smoothing and savings accumulation. Third, state-driven banking sector expansion in rural areas is associated with an increase in rural wages, agricultural investment and a reduction in rural poverty. Particularly in rural agricultural dominated areas, access to credit is related with increased agricultural incomes as it allows for increased investment in high-quality agricultural inputs and consumption smoothing.

Stewart et al (2012: p6) conduct a systematic review of the impact of micro-credit, micro-savings and micro-leasing on client engagement with economic opportunities; and the ensuing outcome on clients' income, savings, accumulation of non-financial assets and expenditure. Beginning with over 14000 citations, studies were excluded based on certain inclusion criteria such as not credit, savings or lease based, no comparison group, no focus on economic related outcomes amongst others. In all, 17 studies satisfied the inclusion criteria with good enough quality. With no rigorous evidence on the impact of micro-leasing, their findings focus on credit and savings. As regards micro-savings, they find no impact on client's engagement in economic opportunities, but mixed impact on the other four economic outcomes evaluated. Similarly, micro-credit is found to have mixed impact on all economic outcomes evaluated; this is the case even when combined with micro-savings. In suggesting that micro-savings might represent a safer intervention, they reach the conclusion that: 'it is important to consider whether there is potential for harm in offering either of these services, or indeed in not doing so. While the lack of financial services may limit the ability of the poor to withstand shocks or to increase their wealth, microcredit also brings the risk of increased debt and loss of collateral'.

However, even these methods of evaluation possess certain weakness: they do not effectively articulate and reflect the characteristics of microfinance users, the context in which microfinance interventions operate and the process of implementing these interventions in their evaluation of microfinance. This creates the impression that MFIs and service users are homogenous. Additionally, impact evaluation studies attempt to assess the impact on service users, but rarely explore why the observed impacts occur. In conclusion, these more recent and supposedly more accurate RCTs find mixed results of the impact of microfinance. Although savings look promising, microcredit appears not to be the golden bullet to poverty reduction that it has been made out to be. As Stewart et al (2012) recommends, beyond evaluating the impact of microfinance, future research can gain more value by identifying how, and under what circumstances do microfinance interventions benefit the poor.

3.4.3 INCLUSIVE FINANCE

This focus on building an inclusive financial systems to serve the poor (World Bank 2008; Ferrand, Gibson et al. 2004; Porteous 2004; DFID 2005) has been propagated using catchphrases such as ‘Finance for All’, ‘getting institutions right’, and ‘Making Markets Work for the Poor’. This body of work highlights the diverse financial service needs of the poor, and the diverse situations in which they work and live. It also raises awareness about the immense diversity of financial institutions that serve the poor in developing countries. However, it ultimately draws the point that the poor face various needs and limitations and therefore financial products and institutions need to mature in ways that accounts for this diversity; and that this requires that financial institutions be leveraged in a consolidated way to increase the financial inclusion of the poor.

Drawing from the book Portfolios of the Poor (Collins et al., 2009), which investigates the ‘financial diaries’ of 250 poor households across urban and rural areas in Bangladesh, India and South Africa, three dominant themes emerge with regard the financial needs of the poor: cash flow management and consumption smoothing, dealing with emergencies and risk management, and accumulating larger sums for life-cycle events. First, the authors conclude that the poor are active money managers who engage in intensive use of financial tools; constantly seeking to save or borrow little sums. This is contrary to popular thinking that with very small incomes, the poor are expected to consume their income as soon as it arrives. Rather, recognising the unreliability and irregularity of this small income, the poor tend to actively manage their income as there is a constant need to ensure that there is sufficient money to meet the daily need for food. Second, like everyone else, when emergencies arise, the poor need large amounts of capital. Third, even when regular, small incomes are insufficient to meet large-scale life cycle expenditures including children education, marriage, child birth and other emergencies such as expanding an existing business or establishing a new one (Ledgerwood et al., 2013).

Having identified the financial needs of the poor, the next question is: what financial tools do they currently use? What are the strengths and weaknesses of these tools and how does microfinance differ? The 'financial diaries' show that relative to formal financial instruments, poor households managed more of their money through informal tools geared towards handling small sums of money over short time periods. With regard to handling emergencies and managing risks, the poor pull whatever resource is at their disposal. Assets could be sold, landed properties mortgaged out and precious metals pawned. Social networks are also explored for gifts in cash or kind, and also for low-cost or interest-free loans. These informal tools are however not suitable for accumulating large sums because the greater the value and the longer the time scale, the greater the risk of theft or misuse. It is also difficult to get larger loans from the informal money lenders as this requires longer repayment period which holds greater risk of default. Therefore, informal money lenders are unwilling to issue such loans. Hence, it is often the case that these life-cycle needs are often met using a mix of loans, savings, gifts from family, and the receipts from the sale of assets.

From the most simple to the more complex, informal financial service providers (e.g. moneylenders, savings collectors etc.) and mutual organizations (e.g. self-help groups, ROSCAs, credit unions etc.) are known for their convenience and flexibility (Ledgerwood et al., 2013). This is because the members live in the same community and are very well knowledgeable about their peers including their financial circumstances. This is obviously well suited to the financial needs of the poor highlighted above. However, informal financial institutions can be exploitative with a limited choice of short-term financial products. On the other hand, because mutual organizations are owned and managed by the poor themselves, the cost of operation is generally low. Yet, the success of the organisation is limited to the financial skill of the poor; and unless they are effectively supervised and regulated, they can be 'captured' by the more influential leaders with the possibility of members losing their money. Hence, these informal tools are highly unreliable and insecure. The convenience and close proximity to savings can be a setback as it increases the possibility for dis-savings and the risk of loss of money. This implies that only the highly disciplined will be able to accumulate large sums.

Additionally, through pioneering innovative techniques such as group lending and mobile banking, non-governmental organisations (NGOs) have contributed towards mitigating the barriers to serving the poor. However, these institutions are oftentimes not profit oriented and can become excessively dependent on external donors. Similarly, regulated and supervised formal financial institutions such as commercial banks, state banks, microfinance banks, agricultural development banks, and non-bank formal financial institutions, offer a broader range of financial services. However, they have showed reluctance in adopting social missions, and due to high operation costs, often cannot deliver services to the poorest of the poor.

It becomes obvious that despite the strengths of these institutions, they all have certain limitations when it comes to financially serving the poor. Informal and mutual institutions may be convenient for the poor but they may not be able to provide long-term, large scale supply of financial services and also insurance from risks. Formal institutions may be able to provide a wider range of reliable and secure services; but may be unable to provide the convenience and flexibility which the poor require in their use of financial services. Hence, with appropriate supervision and regulation, each of these institutions can be leveraged in a consolidated way to increase the financial inclusion of the poor. This would require efforts to link self-help groups and credit unions to commercial banks, networking mutual organizations together to attain economies of scope and scale, supporting the downscaling of commercial banks through the integration of e-payment technologies and mobile banking into their branch networks.

This increased understanding of the financial needs and practices of the poor has led to a recent shift from a focus on microfinance to a broader concern for 'financial inclusion' with particular focus on the wider 'financial ecosystem' and making financial markets work for the poor.

> 'Different products present different risks and delivery challenges, and it is unlikely that a single class of service providers will effectively provide all the products that poor people need. A key challenge is how to create broader interconnected ecosystem of market actors and infrastructure needed for safe and efficient product delivery to the poor (Ehrbeck et al. 2012:1)'.

While this study agrees with the institutional dimension of this discourse, it draws more from the idea that the poor need a wide variety of financial services as borrowers have different sets of characteristics and needs.

> 'The overall message from this body of work is that poor people face various limits, and their ability to capitalize on opportunities varies greatly. …Not all borrowers want to grow a business. The variable results seen can be as much a function of borrower intent as borrower ability. A one-size-fits-all product will not bring benefit to the borrowers or profit to the providers. Instead, the microfinance industry needs to continue to mature in ways that allows it to view poor customers as individuals. Some of those individuals will leverage financial services to smooth consumption; some to manage risk; some to make investments they have the skill and resources to profit from; some will do all of the above. With a view of serving all of these needs, microfinance providers may evolve a new generation of improved services and products that reliably and flexibly help poor people (Bauchet et al. 2011:19)'.

This dimension of the discourse sits well with the earlier debates presented and is more relevant to the call for a client-focused approach to the evaluation and delivery of microfinance. This is one that accounts for the diverse needs of the poor and recognises that not all products/features will be beneficial to all clients all the time. Additionally, in order to generate improved products and services that flexibly and reliably serve the poor, we also need to understand their experiences with the products they are currently exposed to. In relation to the focus of this study, this is in line with the call for empirical studies to investigate the features and characteristics of microfinance that have the potential for both good and harm. Certain recurring themes emanating from these debates include:

- The need to approach the evaluation and delivery of microfinance from the clients' perspective and vantage point.
- The need to understand the contextual factors that influence the financial behaviour of the poor, what financial services they need and which benefit them the most, why and for what purposes.
- The need for more empirical studies to investigate the features and characteristics of microfinance delivery and use; and identify which of these have the potential for good and/or harm.
- The need to identifying how, and under what circumstances do microfinance interventions benefit the poor.

Thus, the above review exposes a gap in the literature. This is the need for studies that look beyond impact to investigate the features and characteristics of microfinance delivery and use from the clients perspective. In addition to the objective defined in the previous chapter, two more objectives are defined in this chapter. The objectives of this study therefore include:

- To identify the capabilities that microfinance clients in the Nigerian context value and have reason to value.
- To evaluate the implementation processes and different components of microfinance interventions and their effects from the viewpoint of service users.
- To evaluate the effectiveness of microfinance as a tool for poverty reduction.
- To investigate clients microfinance practices and their effect on the expansion of capabilities.

The overall aim of this thesis is to examine the potential of microfinance for poverty reduction from the clients' perspective. In order to achieve these objectives, this study defines and addresses certain key questions:

- How do microfinance clients define poverty, and what capabilities do they value and have reason to value?
- What are the experiences of clients with microfinance (features and their implementation processes), from the service users perspective?
- How do the poor assess the ability of microfinance to spur the expansion of capabilities for the poor?
- What borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor?

With the research objectives and questions clearly defined, we attempt to adopt a conceptualisation of microfinance that is appropriate for achieving these objectives and answering the questions.

3.5 CONCEPTUALIZING MICROFINANCE

In conceptualizing microfinance for the purpose of analysis, this study draws from the theory of consumer demand proposed by Lancaster (1966). In this seminal work, Lancaster rejected the 'traditional approach that goods are the direct objects of utility and, instead supposing that it is the properties or characteristics of the goods from which utility is derived ……. and only by moving to multiple characteristics can we incorporate many of the intrinsic qualities of individual goods' (Lancaster, 1966:133-134). The argument here is that consumer demand is not for goods themselves but for the characteristics or features they contain. Applying this proposition to the subject of interest in this chapter, we can infer that the demand for microfinance is not for microfinance itself but for the features and characteristics of microfinance. It would also mean that the utility or disutility of microfinance stems from these features of microfinance and their implementation strategies. With this understanding and drawing from the much wider definition of microfinance as the provision of financial services to the poor (Armendariz de Aghion and Morduch, 2010; CGAP, 2013), microfinance for the purpose of this study is defined as:

> The provision of small units of financial (credit, insurance, remittances, savings) and non-financial services (may include financial education, health education, skill acquisition and management training) to the economically active poor who lack access to mainstream financial institutions with the use of innovative techniques (dynamic incentives, group lending, targeting of women, pre-loan savings, frequent repayments).

This definition and conceptualisation of microfinance allows us to account for and address clients experience with the features and implementation processes of microfinance, which is emphasized in this study. The conceptual framework which guides the analysis in this study is graphically presented in Figure 1.1 (see Chapter 1). This definition includes a broad range of financial and non-financial features as well as their implementation strategies which based on our understanding of microfinance have the potential to affect the expansion of capabilities. Alongside group lending which has been discussed earlier in this chapter, other features and implementation processes of microfinance considered to affect poverty reduction include: the focus on women, credit, savings, and non-financial services.

As regards the ***focus on women***, this has been shown to have positive outcomes on gender equality (Cheston and Kuhn, 2002), women empowerment (Khandker, 2001; Pitt et al., 2006), as well as higher household benefits (Khandker, 2003). Here, empowerment can be seen as the process of taking ownership and control of one's life through the expansion of choices (Kabeer, 1999). Data from rural Bangladesh showed that the involvement of women in microfinance positively affected their decision making at the household level, access to economic and financial resources, social networks, freedom of movement and their bargaining power within the household (Pitt et al., 2003). There is also empirical evidence to support the claims that household benefits more when income accrues to women rather than men; as women are relatively more likely to spend their income on their household needs. Findings from a study of clients of the Grameen Bank in Bangladesh estimates an 18% average increase in household consumption when credit is granted to a female borrower and 11% for male borrowers (Khandker, 2003).

However, some studies argue that there is a limit to achieving the goal of gender equality as microfinance scarcely challenges the socially embedded structures that foster gender inequality (Swain and Wallentin, 2009; Gaiha and Nandhi, 2005). Supporting evidence from 2 MFI interventions in Bangladesh where only 37% of the women had considerable control over the use of loans, while 63% had limited or no control (Goetz and Gupta, 1996). Some have therefore argued that microfinance interventions need to pay more attention to improving the capabilities of women to enable them function in more productive roles as emphasizing access to microcredit alone is unlikely to challenge the existing gender roles (Hulme and Mosley, 1996). Similarly, findings from Ghana suggest that rather than facilitate women empowerment, microfinance may reinforce gender inequalities as increase in income is more likely associated with an increased share of household expenses for women while the husbands decreased theirs. These women became increasingly overburdened thus dampening their progression towards empowerment (Cheston and Kuhn, 2002). Given these variations, this study will explore the experiences of women with microfinance, how this has affected power relations within the household and the expansion of capabilities.

There is no doubt that ***microloans*** are core to the delivery of microfinance interventions and their characteristics - loan size, use, repayment frequency, and interest rate - influence the experience of the service users with microfinance. *Loan sizes* vary across different interventions, loan types and loan cycles. The typical practice of most MFIs is to begin with a microloan and, based on service users' repayment performance, progressively raise the loan size. This practice is referred to as progressive lending. The popular belief among practitioners is that the ability of service users to meet previous obligations shows their ability to effectively utilize and repay loans as well as the viability of the microenterprise. Besides its use for testing the creditworthiness of borrowers, this promise of higher loans creates an incentive for higher loan repayments. However, some have argued for an upper limit to be set for microloans based on the idea that service users' debt capacity is a better criterion for credit assessment instead of credit need[16] (Ledgerwood, 1999). The high level of indebtedness recorded in the previous section also points to the need to apply a cautious approach to the issue of loan size. While higher loan sizes might increase clients' ability to take advantage of bigger investment opportunities, it might also lead to an increasing use of loans for non-income generating activities.

As regards *loan use*, it has now been accepted that microloans are often spent on consumption and non-income generating purposes (Johnson and Rogaly, 1997; Hulme and Mosley, 1996) Bearing in mind the cost of loans, how does loan use affect a client's ability to repay loans on one hand and poverty reduction on the other? On the one hand, the use of loans for non-business purposes may positively affect poverty reduction at the household level. Findings by Hulme and Mosley (1996) show that microloans used for consumption purposes keep the poor from sinking further into poverty thereby covering their vulnerability. On the other hand, it might negatively affect repayment capacity therefore increasing client's vulnerability to indebtedness and poverty reduction. This study investigates this widely accepted use of loans for non-income generating purposes. The question is: does it led to increased capabilities at the household and business level or is there a trade-off?

Loan repayments are also often made in frequent and regular installments within short intervals such as weekly, bi-monthly and monthly. It is argued that frequent repayment patterns ensure high repayment rates and instill fiscal discipline into service users; although the former rather than the latter (MkNelly and Kevane, 2002). Take LAPO microfinance bank (MfB) in Nigeria for instance, clients are expected to make a weekly repayment of NGN 2,600 on a NGN 50,000 loan with loan duration of 30 weeks. However, this comes with a high repayment burden. As shown in chapter 5, about 60 percent of the Nigerian population lives below the USD1 a day poverty line. This suggests that the poor that MFIs serve live below NGN 1,050[17] per week (NBS, 2012). Given the characteristics of clients, it is important to examine what their experience is with making repayments.

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[16] The former refers to the amount of additional loan an individual can take-on without running the risk of default; while the latter captures 'needs' and relies on self-reported information that might not take into account the debt capacity.

[17] This is calculated based on USD1 = NGN150 as at January 24, 2014.

Additionally, *interest rates* represent the cost of lending and the higher they are, the lesser the net gains to service users. Given the empirical evidence that some microenterprises show high marginal returns (McKenzie and Woodruff, 2008; De Mel et al., 2008), and that the poor reportedly pay high interest rates to informal moneylenders, it is often argued that the poor are insensitive to interest rate changes. However, conclusions drawn based on these findings will most likely be flawed as these studies face certain limitations. For example, the studies do not capture how the opportunity cost for own labour is estimated. In countries with considerable unemployment and under-employment, it is easy to ascribe zero price for own labour. Returns to investment will be significantly reduced if the costs of own labour are taken into account. We therefore consider the loan size, use, repayment frequency, and interest rate to play a significant role in affecting the utility that clients derive from using microfinance; with a further effect on the expansion of capabilities.

Overall, given the failure of the state welfare system to operate effectively in developing countries, ***insurance*** and ***savings*** for the purpose of retirement is particularly important. Also, access to safe savings is important for asset accumulation as long as savings exceeds dis-savings. Especially for the poor, no matter how little the savings might be, over time the accumulated savings will be a catalyst in their freedom from the vicious cycle of poverty. Accumulated savings is required to meet certain lifecycle needs such as marriage, childbirth and education; emergency needs such as sickness, unemployment, death, famine, floods, war; and investment needs (Rutherford, 2000). Savings help to cushion financial shocks or unforeseen expenses without having to incur more debt. Without savings, the poor are adversely affected by the full impact of these shocks (Kempson et al., 2005).

Non-financial services (e.g. skill acquisition; social capital; health services/education, management and financial education) are argued to be crucial components of microfinance. With a multidimensional approach to poverty, these services can be designed to target different dimensions of capability deprivations. For instance, financial education and training directed towards increasing clients' knowledge of budgeting and money management can greatly improve the capability of clients to productively and profitably use credit and savings. Similarly, health and social empowerment programmes can greatly improve the capability of clients with positive social and empowerment outcomes. Findings from Bolivia and Sri Lanka which investigate the impact of financial education on financial behaviour outcomes show an increase in product knowledge, increased ability to evaluate loans and calculate own debt capacity (Gray et al., 2009). Beyond the direct effect on capability outcomes, the relevance of non-financial services with regards to being tailored to meet the dimensions that people value is the key to successful poverty reduction. There still remains much to be learnt about which sorts of non-financial services are needed by whom, which methodologies are most effective in providing them, and how they can be combined with other opportunities to achieve long-term sustainable poverty reduction. Despite these challenges, non-financial services remain key to the successful use of microfinance and constitute a significant tool for increasing individual capabilities. This study will investigate the non-financial services provided by the case-study MFI, the experience of clients with these services, and their contribution towards increased capabilities.

3.6 CONCLUSION

This chapter began with an introduction to the concept of microfinance; including a review of why we need microfinance and how microfinance services are provided. Next, it provided a review of the recent debates in the microfinance literature, specifically (i) the recent claims that indebtedness plagues the microfinance industry, (ii) the growing concern that the perceived positive impact of microfinance has not been realised and (iii) the call for a wider focus on inclusive finance. A review of these debates uncovered a call in the literature for studies that *listen to clients and approach the delivery and evaluation of microfinance from the 'clients' vantage point*. Asking: what it is that they are looking for when they utilize financial services? What features of microfinance are beneficial and which are not? (Maes and Reed, 2012:1-2). With this, a gap in the literature is identified, and the research questions and objectives defined. The research gap is particularly defined as: the need for studies that look beyond impact to investigate the features and characteristics of microfinance delivery and use from the clients perspective. Drawing from the theory of consumer demand proposed by Lancaster (1966), a conceptualization of microfinance which allows us to account for the features and implementation processes of microfinance; and thus enables the achievement of the research objective is employed. The final section reviewed existing evidence of the likelihood for the different features of microfinance and their implementation processes, to result in different poverty reduction effects for service users. Overall, given our focus on microfinance, we argue that the utility or disutility of microfinance stems from the effect of the different features (group lending, targeting women, microloans, savings, interest rate and non-financial services) of microfinance interventions. With this understanding, the analysis will investigate the contribution of these different features to the overall poverty reduction effect.

CHAPTER FOUR

POVERTY AND MICROFINANCE IN NIGERIA

4.1 INTRODUCTION

Poverty has remained a constant feature of the Nigerian society and presents itself in different dimensions. Despite relatively high economic growth rate, relative poverty[18] in Nigeria has increased over the last three decades (NBS, 2012). This has continuously been followed with several anti-poverty initiatives with the aim of providing inclusive systems to cater for the poor. Among these, there has been a long history of financial initiatives aimed at increasing access to finance for the poor in Nigeria. Early indigenous microfinance activities is said to date back to the 16th century in the form of indigenous thrift and credit groups. More recently, with the commercialisation of microfinance as well as the introduction of the Nigerian microfinance policy framework which provides a platform for MFIs to operate profitably, there has been a rapid rise in the operations of modern MFIs. From an initial licensing[19] of 8 MFBs by the CBN in 2006, the number of MFBs grew to 820 in 2010 (CBN, 2011). This chapter reviews the state of poverty and microfinance in Nigeria separately. It begins by exploring the economic background in Nigeria. It then goes on to address how the different approaches to poverty are manifested in Nigeria, highlight the increasing size of the growing poor population as well as the financial exclusion of the poor. This is followed by a look into the practice of microfinance in Nigeria and an introduction to the case study for this analysis, Lift Above Poverty Organisation (LAPO) MfB.

4.2 NIGERIA: SOCIO - ECONOMIC BACKGROUND

The Federal Republic of Nigeria is one of Africa's most resource rich countries. She has the highest population in Africa with over 160 million people, is Africa's largest crude oil producer and eight in the world, and her natural gas reserves is the seventh largest in the world. With the discovery of oil in 1956, independence in 1960, the Nigerian economy looked very promising at the time. However, beginning with the coup d'états in 1966, the civil war of the late 1960s, the neglect of the agricultural and manufacturing sector with greater dependence on crude oil, a series of unfavourable

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[18] See section 4.3.1 below for a discussion of poverty measures in Nigeria, and Table 4.4 for evidence of growing poverty rates

[19] The licensing of MfBs or MFIs by the CBN positions these institutions as formal financial institutions under the regulation of the CBN. Acquiring an MfB license involves higher minimum requirements including higher capitalization compared to MFIs. While all MfBs must be regulated, the majority of the MFIs in Nigeria still operate in the informal sector.

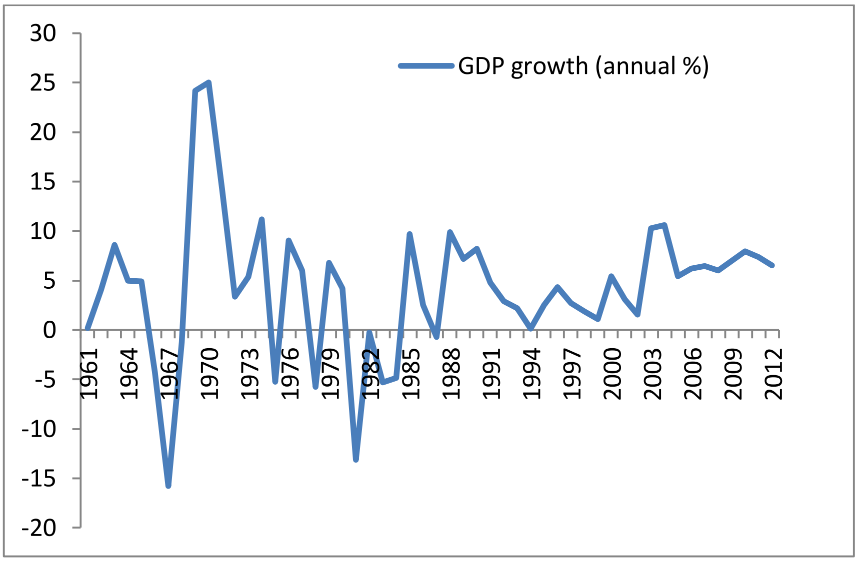
economic and political events have stalled her economic growth. Despite the oil boom in the 1970s which fuelled double digit growth rates on the average, Nigeria in the 1980s was characterized by sharp decline in crude oil prices, continued military rule, and economic mismanagement. Falling crude oil prices was accompanied by a 4.8 percent decline in GNP per capita per annum from 1980 to 1987 (Obadan, 2003).

By 1986, the IMF/World Bank prescribed structural adjustment programme (SAP) was adopted by the Nigerian government as part of the conditions for economic assistance and as a tool towards economic recovery. The SAP package was designed to restructure the economy by reducing the dependence on oil and the unproductive investments in the public sector, expanding the productive capacity of the private sector and thus, increasing the productive base and laying the foundation for non-inflationary growth (Ayadi et al., 2008). Key features of the programme include the commercialization, privatization of the public sector and removal of subsidies; adoption of market prices in all sectors; and trade liberalization with the commitment to pursue a realistic exchange rate. Although this opened the path for privatization and liberalisation of the Nigerian economy, SAP was heavily criticized for its perceived negative impact on welfare as it led to a collapse of social services and basic infrastructure, high inflation, drastic collapse in the exchange rate and was abandoned in the mid-1990s. Other factors that continue to stall economic development include corruption, poor implementation and continuation of development plans (Obadan, 2003; Okojie, 2002; and Olomola, 2000).

However, more recent economic and financial reforms in the past decade has placed the country back on track, with average economic growth rate of 7 per cent in the last decade as shown in figure 4.1 below. Some of these reforms include the privatisation of the telecommunications sector in 2000/01, consolidation of the banking sector in 2005 as well as the payment of the external debt achieved through 60 percent waver of the debt by the Paris club in 2005. These reforms among other factors strengthened the resilience of the Nigerian economy to economic shocks during the recent global financial crisis, allowing it to maintain economic growth rates above 6 percent per annum. With the recent rebased nominal GDP figures announced by the National Bureau of Statistics (NBS) in April 2014, the Nigerian economy is currently ranked the largest in Africa and 26th in the world. Yet the GDP per capita is only $2,700 which is less than half that of South Africa which currently ranks second in Africa; meaning that South Africans are 'more than twice as rich' (The Economist, 2014).

Hence, despite this high economic growth rates, 'living standards' and 'poverty rates' remain important issues of concern for the Nigerian government and its people.

Figure 4.1: Economic Growth measured by GDP Growth (1961-2012)



Data Source: World Bank (2012)

Additionally, key socio-economic indicators do not look very promising as discussed below. Unemployment[20] rate in Nigeria has remained relatively high as shown in Table 4.1 below. The high rate of unemployment and heavy bureaucracy in the formal sector has driven a large portion of the population to operate in the informal sector (Anyanwu, 2004). This is reflected in the large size of the Nigerian informal sector which comprises of over 17 million enterprises (NBS, 2014). This sector is largely dominated by microenterprises[21] constituting about 61.4 percent of the economy (Anyanwu, 2004). These businesses are mainly involved in retail and wholesale trading, hotels and restaurants; and are faced with limited access to finance (Udry, 1993). Due to the absence of safe facilities to place deposits and accumulate savings, enterprises in this sector are stricken by poor liquidity management (Osthoff, 2005 and Pagura, 2003). The growth of the Nigerian informal financial sector reflects the

[20] The unemployment rate in Nigeria is measured as 'the proportion of those who were looking for work but could not find work for at least 40 hours during the reference period to the total currently active (labour force) population' (Federal Ministry of Justice, 2014:36). The high number of unpaid family labour in Nigeria remains a potential cause for the underestimation of unemployment or underemployment in Nigeria. This constitutes a constraint to economic progress with possible more damaging effects than those of unemployment (Raheem, 1993). In all, underemployment remains particularly high and contributes considerably to the widening gap between the actual and reported unemployment rates in Nigeria.

[21] According to the Nigerian classification, 'Microenterprises are enterprises with less than 10 employees with a total asset of less than N5 million (excluding land and buildings) and operated by sole proprietor (NBS, 2010)'.

financial exclusion of a large proportion of the 'economically active' population. This large number of informal microenterprises sets the stage for microfinance to thrive.

Table 4.1: Socio-Economic Indicators of Nigeria (2005-2012)

Indicator Name	2005	2006	2007	2008	2009	2010	2011	2012
Unemployment	…	…	12.7	14.9	19.7	21.4	23.9	…
Labour force participation (% of total population ages 15-64)	54.9	55.0	55.2	55.4	55.5	55.7	55.9	56.0
Labour force, female (% of total labour force)	42.9	42.9	42.8	42.7	42.7	42.6	42.5	42.5
Domestic credit provided by banking sector (% of GDP)	8.6	4.9	16.6	24.9	37.8	30.0	35.8	35.6
Domestic credit to private sector (% of GDP)	13.2	13.2	25.2	33.8	38.5	24.8	20.9	20.9
Inflation, consumer prices (annual %)	17.9	8.2	5.4	11.6	11.5	13.7	10.8	12.2
Money and quasi money (M2) as % of GDP	17.7	19.0	28.0	36.4	40.8	32.8	33.7	36.5
Lending interest rate (%)	17.9	16.9	16.9	15.5	18.4	17.6	16.0	16.8
GDP growth (annual %)	3.4	8.2	6.8	6.3	6.9	7.8	6.8	6.5
GDP per capita growth (annual %)	0.8	5.4	4.0	3.4	4.1	4.9	3.9	3.6
Population (Total in millions)	139.6	143.3	147.2	151.2	155.4	159.7	164.2	168.8
Population growth (annual %)	2.6	2.6	2.7	2.7	2.7	2.7	2.8	2.8
Rural population (% of total population)	54.3	53.6	52.9	52.3	51.6	51.0	50.4	49.8
Urban population (% of total)	45.8	46.4	47.1	47.7	48.4	49.0	49.6	50.2
Life expectancy at birth, total (years)	48.7	49.2	49.8	50.3	50.8	51.3	51.7	…
Birth rate, crude (per 1,000 people)	42.5	42.4	42.3	42.2	42.1	41.9	41.8	…
Death rate, crude (per 1,000 people)	16.0	15.6	15.1	14.7	14.4	14.1	13.8	…
Mortality rate, infant (per 1,000 live births)	96.7	93.6	90.7	87.8	85.1	82.6	80.1	77.8
Fertility rate, total (births per woman)	6.0	6.0	6.0	6.0	6.0	6.0	6.0	…

Source: World Bank (2012)

The table also shows relatively low domestic credit to the private sector as well as high lending rates, which have curtailed private sector investment activities that could help to create employment and reduce poverty. Double digit inflation rates, with an annual average inflation rate of 11.4 percent between 2005 and 2012 are also capable of eroding the savings capability of households. Particularly, the growing population rate has been followed by rapid urban migration. This continues to exert a downward pressure on the deteriorating and fragile infrastructure (water, health facilities, light, road, etc.), social services, and bleak formal labour market in both urban and rural areas (Pagura, 2003). However, the socio-economic indicators of health show steady improvement over this period. One possible reason for this is the increasing allocation of official development assistance (ODA) to the health sector – 24.1 percent, 46.6 percent and 56.8 percent in 2007, 2008 and 2009 respectively (NBS, 2012). Nevertheless, the next section shows that poverty remains a major challenge for majority of the Nigerian population.

4.3 POVERTY IN NIGERIA

Poverty has remained a recurring factor in the Nigerian society. A look into the history of poverty in Nigeria suggests that the country might have experienced better days with lower poverty rates in the past. Particularly with gaining her independence in 1960 and the crude oil boom in the 1970s, this era up until 1980 is said to have been categorized as years of plenty with relatively low poverty rates[22] of less than 30 per cent of the population. However, with a growing dependence on crude oil revenue in the 1970s, the sudden decline in oil prices in 1982 led to a major collapse of the economy. The neglect of the manufacturing and agricultural industry created high levels of unemployment. By 1989, the World Bank ranked Nigeria as a low income country and poor enough to be eligible for concessional aid from the international development association (IDA) (NBS, 2012).

Although the country has made some progress over the years and is now ranked as a lower-middle income country with relatively high growth rates, poverty rates remain high at over 60 percent [23](NBS, 2012). The coexistence of abundance of natural resources with high poverty rates, often experienced in some developing countries depicts a situation of 'poverty in the midst of plenty'. Particularly, economists refer to the situation where the abundance of resources fuels or breeds corruption among government officials as a 'resource curse'. This is the case in Nigeria where the World Bank estimates that 80 percent of oil revenues accrue to just 1 percent of the population, due to corruption (Obadan, 2003).

As discussed in chapter 2, poverty is a multidimensional concept. It entails deprivation in income or monetary resources; deprivation in choices, opportunities and the capacity to better one's life; and deprivation in the capacity to participate effectively in society. These different dimensions of deprivation are captured by the monetary, capability, and social exclusion approaches to poverty respectively. This section looks at each of these forms of deprivation with regard to how they present themselves in the Nigerian context.

[22] An indication of how absolute and relative poverty are measure in Nigeria is presented later on in this section. See Table 4.4 below for relative poverty estimates.

[23] This is twice the poverty rate (30 percent) in the 1980s mentioned earlier. These rates are assumed to be comparable as they are both provided by the NBS (2012). It is expected that even if the poverty line might have been modifies in the last 30 years, the figures must have been adjusted to reflect any changes and to allow for consistent measures.

4.3.1 MONETARY POVERTY

From a monetary approach, the NBS employs three measures of poverty (see table 4.2 below). This consists of two absolute measures including an annual absolute poverty line[24] and the dollar per day poverty line; and a relative measure set at two-thirds of the total household per capita expenditure (THPCE).

Table 4.2: 2010 Poverty in Nigeria (%)

		Food Poverty	Absolute Poverty	Relative Poverty	Dollar per day based on adjusted 2005 PPP
Sector	Urban	26.7	52.0	61.8	52.4
	Rural	48.3	66.1	73.2	66.3
	National	41.0	60.9	69.0	61.2
Geo-political zones	North Central	38.6	59.5	67.5	59.7
	North East	51.5	69.0	76.3	69.1
	North West	51.8	70.0	77.7	70.4
	South East	41.0	58.7	67.0	59.2
	South South	35.5	55.9	63.8	56.1
	South West	25.4	49.8	59.1	50.1

Source: NBS, 2012

Based on these three measures, the percentage of the Nigerian population living in poverty increased from 54.7 percent, 51.6 percent and 54.4 percent in 2004 to 60.9 percent, 61.2 percent and 69 percent respectively in 2010 (NBS, 2012). These figures support the often reported high poverty rates in rural and northern Nigeria which can partly be explained by the low returns to rural businesses and predominantly agricultural economy in the North. However, the corresponding high poverty rate in urban and southern Nigeria confirms the increasing spread of poverty. Further segregation of relative poverty as reported in table 4.3 below, shows the high rate of inequality.

Table 4.3: Relative Poverty in Nigeria (%), 1980-2010

Year	Non-poor	Moderate-poor	Extreme-poor
1980	72.8	21.0	6.2
1985	53.7	34.2	12.1
1992	57.3	28.9	13.9
1996	34.4	36.3	29.3
2004	43.3	32.4	22.0
2010	31.0	30.3	38.7

Source: NBS, 2012

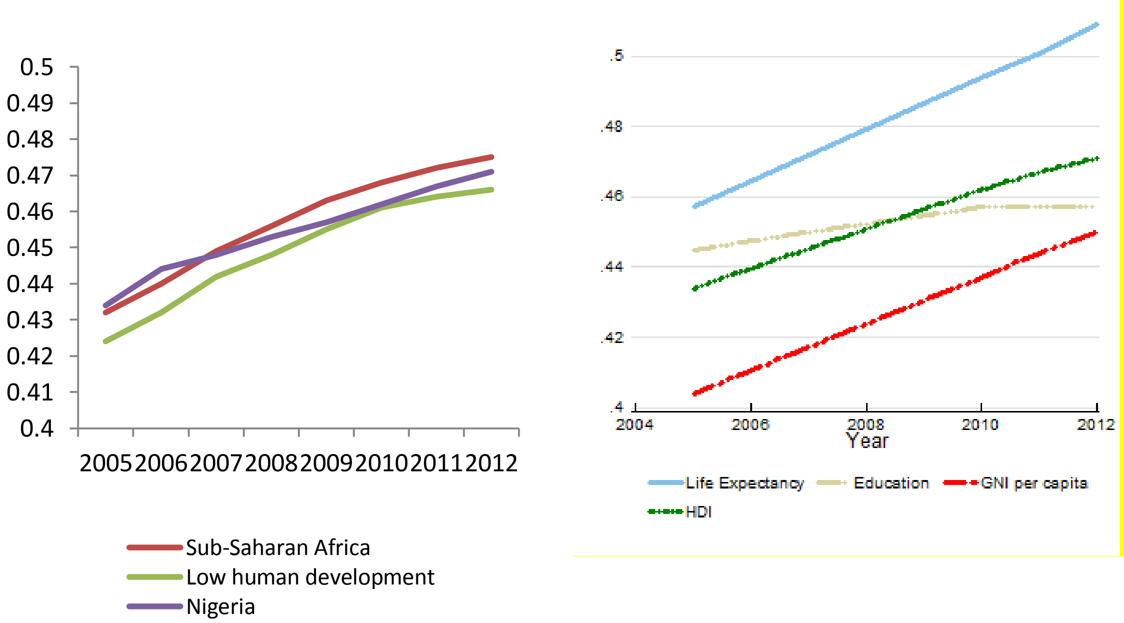
[24] This is based on 'minimal requirements necessary to afford minimal standards of food, clothing, healthcare and shelter. This method considers both food expenditure and non- food expenditure using the per capita expenditure approach. This method is otherwise known as Food Energy Intake measure of poverty. First you obtain the food basket of the poorest 40 percent of the population. Then compute the food expenditure that can give 3000 calorie per day based on the national food basket for the poorest 40 percent' (NBS, 2012).

Here, households with expenditure less than one-third of the total household per capita expenditure (THPCE) are classified as 'extremely poor' while households with expenditure greater than one-third but less than two-third of the THPCE are classified as 'moderate poor'. The proportion of non-poor Nigerians has decreased by more than half from a commendable rate of 72.8 per cent in 1980 to 31 per cent in 2010. Over the same period, the extreme poor have increased by more than six times, from a low rate of 6.2 per cent in 1980 to a disturbing rate of 38.7 per cent in 2010. The NBS estimates that poverty rates (absolute, relative and dollar-per-day) may have further risen to about 61.9 percent, 71.5 percent and 62.8 percent respectively in 2011 (NBS, 2012).

4.3.2 Capability Poverty

With the capability approach to poverty, the Human Development Index measures 'three basic measures of human development': a healthy and long life, a decent living standard and access to knowledge. As shown in figure 4.2 below, an HDI value of 0.471 in 2012 positions Nigeria in the low human development category, ranking at 153 of 187 countries in the survey. Although this represents a 9 percent increase from an initial HDI value of 0.434 in 2005, this HDI value remains relatively low and below the average HDI value of 0.475 for Sub-Saharan Africa. It is also a far cry from the HDI value reported for the USA and the world average which is 0.910 and 0.694 respectively. Much of this increase of HDI in Nigeria is owed to the rapid increase in life expectancy and also a slower increase in per capita income.

Figure 4.2: Trends in Nigeria's HDI Component Indices (2005-2012)



Source: UNDP Human Development Report, 2013

The HDI value is also considered to be an indicator of human capital development. This is an important factor for individual wellbeing or national wealth as it influences the productive capacity of labour. Hence, increased capabilities reflected in higher HDI value is of great importance if Nigeria is to increase the welfare of her citizens and remain competitive in the future.

4.3.3 SOCIAL EXCLUSION

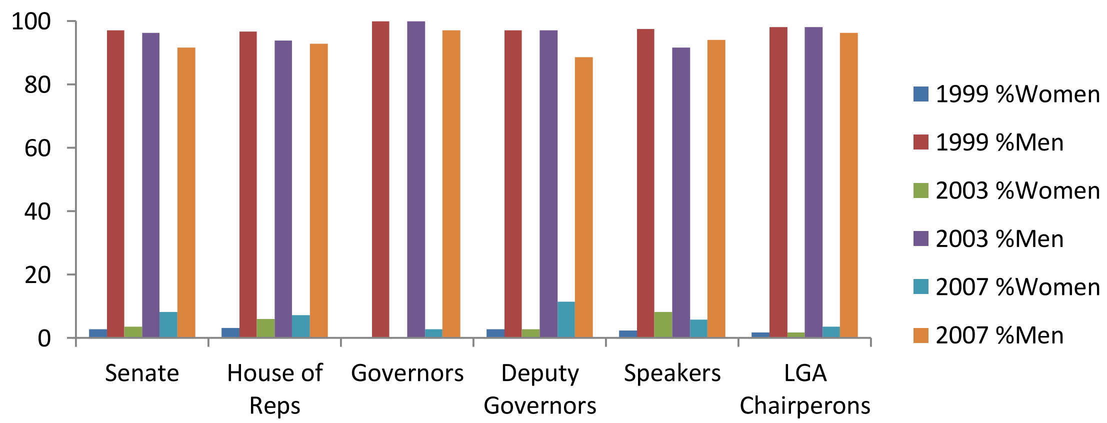
Poverty is seen in the social exclusion approach as 'non-participation' of individuals in activities considered as necessities in their society. A contextual approach to this analysis would suggest that this definition is more appropriate for developed countries where the socially excluded are often the marginalized minority. A more appropriate definition for a developing country such as Nigeria would be:

> 'The unique interplay of a number of factors, whose consequence is the denial of access, to an individual or group, to the opportunity to participate in the social and political life of the community, resulting not only in diminished material and non-material quality of life, but also in tempered life chances, choices and reduced citizenship' (Kenyon et al, 2002: 209).

The emphasis on material and non-material dimensions of poverty as well as the tempered quality of life chances and opportunities available to individuals is particularly relevant for the Nigerian poor. Talking about tempered life chances, the Nigerian 2008 social statistics report showed that majority of Nigerians lacked access to basic infrastructure and social amenities. For instance, just 7.7 percent of households had access to pipe-borne water in 2008. Bore holes appears to be the main source of water for 28.4 percent of households while 27.1 percent had to rely on streams/pond/river/rain. Only 10.3 percent of households had access to a flush or septic tank. This is particularly low in northern states where the 'Islamic toilet etiquette' is practiced. Particularly Borno, Taraba, Sokoto and Zamfara state recorded none on the average. 41.4 percent and 48 percent of households were without electricity supply in 2007 and 2008 respectively. In terms of cooking fuel, 79.6 percent of households made use of wood, 18.5 percent used kerosene and only 0.6 percent of households used gas (NBS, 2009b).

Access to a decent and adequate source of income is also important in addressing capability constraints. For instance, individuals can use income generated from gainful employment to improve their capabilities and quality of life chances, leading to an improved standard of living. However, in Nigeria, unemployment has been relatively high and on the increase. National unemployment[25] rate averaged 12 percent between 2003 and 2008 with a rapid increase from 11 percent in 2007 to 23.9 percent in 2008. Particularly interesting is the difference in unemployment rates across regions, industries and gender (NBS, 2009b). 'In Africa, it is often said that poverty wears a female face' (Ezekwesili, 2009) as exclusion is generally divided along gender lines (NBS, 2009a). This is apparent in the state of unemployment, low-representation in high wage non-agricultural employment, and high-representation in low wage and non-decision making employment positions. With regard to exclusion from adequate resources, in 2008, the percentage of wages earned by women in the non-agricultural sector was less than half (32.3 percent) the wages earned by men (67.7 percent). As regards ownership of resources measured by land ownership, only 7.2 percent of lands were owned by women compared to 38.1 percent owned by men. In terms of access to credit, men had greater access to credit as 11.6 percent of the adult male population had access to credit compared to 9.8 percent of women[26] (NBS, 2009a). As shown in Figure 4.3 below, very few women actively participate in decision making processes. Women representation has been repeatedly very low in the National Parliament (Senate and House of Representatives) as well as the State and Local Governments.

Figure 4.3: Gender Distribution of Political Positions in Nigeria



Source: NBS, 2011

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[25] In the Nigerian context, the unemployment rate measures the percentage of the labour force (15 – 65 years) excluding the medically unfit and students, available and willing to work but unable to find work (CBN, 1993). It does not account for the problem of underemployment i.e. the underutilization of the productive capacity of workers below their reasonable potential. Hence, the official Nigerian unemployment rate is biased downward.

[26] This includes microcredit provided by MFIs and non-MFIs. It confirms the presence of other sources of informal finance in the Nigerian financial system. It also shows that although MFIs focus on women, non-MFIs may be more patronised by men.

However, one major limitation of these figures is their focus on the public sector. The private sector houses a large number of women involved in high paid top management decision making positions. For instance, considering the telecommunication sector which has been privatized, women on the average accounted for 32.3 percent of the employment in this sector between 2001 and 2007 (NBS, 2009a). This wide gender disparity is also evident at top management levels. The NBS reports that in the public sector, the proportion of male permanent secretaries and judges is nearly five times the proportion of their female counterparts. In 2007, women accounted for only 20.7 percent and 20.1 percent of permanent secretaries and judges respectively (NBS, 2009b). Also, although more women are increasingly participating in politics and top positions of professional occupations, they are still obviously ‘outnumbered by their male counterparts’ (Every Culture, 2011). Amongst other things, this is influenced by underlying social institutions as well as cultural beliefs that ‘Men are the decision makers, and that a woman’s place is in the kitchen’. Some of these traditional social institutions which contribute to the marginalization and vulnerability of Nigerian women are discussed below.

4.3.3.1 Social Institutions and Women Exclusion in Nigeria

Social institutions include those attitudes, norms and values evident in the traditions and customs of a society. They reflect the normative value system of people and are especially pertinent in issues regarding gender equality. Social institutions such as customs, religions and traditions can be a starting place for discriminatory gender norms. Besides marginalization on the basis of health status, ethnicity, social status or geographical location, one group of people consistently marginalized in Nigeria is the female population.

Although the Nigerian constitution prohibits gender based discrimination, it does not sufficiently protect the rights and physical integrity of the Nigerian women. For example, the Panel Code (section 55(4)) applicable in the Northern states allows for chastisement of the wife by the husband (Nigeria CEDAW NGO Coalition, 2008). Only four out of the 36 states in Nigeria have enacted laws to legally prohibit domestic violence. In 2003, 64.5 percent of women in Nigeria considered being beaten by their husbands as normal. The birth of a male child is also celebrated and received with more delight than a female child (Eyinade, 2010). Also, the practice of Purdah in Muslim communities in some northern states of Nigeria limits the civil liberties of women. Although some women willingly practice ‘purdah’ in obedience to their religion, it restricts the ability of women to effectively participate in their society. Women in purdah can only leave their home with their husbands' permission and must always be accompanied by a man when in public. It also restricts their freedom of dressing as these women must be veiled in public. Some of these women are not allowed to trade in market places and therefore have to rely on their husbands or their sons for their source of livelihood (Afolabi, 2009).

With regards to ownership rights, although civil law recognizes the right of women to own land, certain customary laws confer this right on men alone. While the federal government of Nigeria has the right to assign land as it deems fit, land tenure is mainly a local issue as families in each community often apportion land within themselves. In most communities, customary laws only allow for land to be transferred from fathers to male children. Women mainly obtain access to land through marriage or purchase as inheritance is predominantly a male affair in many Nigerian ethnic societies. Although women legally have the right to inheritance, they often get nothing. This reinforces the economic dependence of the Nigerian women. Even in marriage, in the absence of a will that legally transfers the ownership to the wife, property and wealth of a late husband are often times transferred to his sons if they are of age, or taken over by other male relatives of the deceased if the sons are not of age. In the Fulani culture, the wife and properties of the deceased may be inherited by his brother (Every Culture, 2011).

As advocated by the participatory approach to poverty, the NBS also applies a subjective measure of poverty. Here, individuals are required to self-assess their wellbeing and provide their opinion on whether they consider themselves poor or not. The result shows that in 2010, 93.9 percent of Nigerians considered themselves to be poor as compared to 75.5 percent in 2004 (NBS, 2012). Overall, the above discussion points to the fact that poverty in Nigeria presents itself in different dimensions and that despite relatively high economic growth rate, poverty and income inequality have increased over the last three decades. This therefore justifies the decision to study poverty in Nigeria and the effectiveness of microfinance as a tool for poverty reduction. Having explored the scene of poverty in Nigeria, we turn towards financial access and microfinance in the Nigerian context.

4.4 MICROFINANCE IN NIGERIA

Nationally representative data on the access to finance in Nigeria reported by EFInA (Enhancing Financial Innovation and Access), shows that in 2012, 59.3 million adult

Nigerians (67.5 percent of the adult population) were unbanked (EFInA, 2012). As expected, savings accounts and debit cards are the most patronized products with 86.6 percent and 64 percent of the banked population respectively reporting their use. About 78.8 percent of the rural population is unbanked and more likely to save at home, with friends/family, informal savings society or village associations (EFInA, 2010a). Overall, the EFInA financial access strand[27] estimates that in 2012, about 39.7 percent of the adult Nigerians (34.9 million) were financially excluded. This represents a massive market not yet captured by the Nigerian financial system and increasingly been served by the microfinance sector.

The microfinance sector is becoming an increasing part of the Nigerian financial system and cuts across both the formal and informal financial system. Microfinance interventions in Nigeria are provided by indigenous informal institutions such as individual money lenders, credit unions, NGO-MFIs and friendly lending societies; and more formal institutions like financial cooperatives, building societies, state-owned agricultural banks, and MFBs. The discourse on microfinance in Nigeria presented in this section introduces the activities of these indigenous MFIs in Nigeria as well as the modern microfinance currently practiced in Nigeria. Modern microfinance which is a commercialized version of the Grameen Bank microfinance model proposed by Dr Yunus, is the focus of interest in this study.

4.4.1 INDIGENOUS MFIS

This includes both informal interventions as well as home-grown government initiatives aimed at providing financial services to the poor. The more informal member-led friendly lending societies exist in different forms and by different names across both rural and urban Nigeria. For example, they are called adashi in the North and esusu in the South. They are usually centred on a commonality such as age group, kinship, resident location etc. In urban areas, salaried workers or people who originate from the same village community are likely to patronize these informal financial

[27] The financial access strand comprises of four strands: the banked, formal other, informal only and the financially excluded. (i) **Banked**: consists of all those who have access to and use formal deposit money banks (DMBs), in addition to using a traditional banking product. (ii) **Formal Other**: refers to those who are financially served by non-bank formal financial institutions such as Insurance companies, microfinance banks, pension funds, finance companies, primary mortgage institutions etc. Together, the first two represents the formal included. (iii) **Informal only**: refers to those who only access and use informal financial products and services, but do not use banks and non-bank financial institutions. (iv) **Financially excluded**: consists of all adults who do not make use of banks; formal other or informal financial institutions. Also included here, are individuals who obtain loan from family/friends or from an employer and have no other contact with the financial system (EFInA, 2010a). See www.finscope.co.za

groups for the exclusive benefit of their members. Group members often make periodic contributions to a pool from which they individually access loans on a rotational basis. These indigenous microfinance groups provide members with a number of flexible services to enable them to meet certain financial and non-financial needs. This could include lifecycle needs such as education and weddings; personal emergencies such as unemployment and sickness; natural disasters; as well as investment opportunities such as building up assets and expanding a business. Groups may be formed purely for financial purposes (e.g. savings and lending) or financial activities may only be part of other cultural, religious or professional associations. Beyond the group delivery approach, these institutions are characterized by a huge savings component, flexibility and informality of operations, relatively low interest rates and limited outreach (Ehigiamusoe, 2011).

Co-operatives societies have also played a significant role in the development of rural finance in Nigeria. As is the case in most developing countries, co-operatives are a common access to financial services for the poor. Primarily, these institutions provide the poor with the opportunity for savings mobilization and credit. A co-operative society can be defined as 'an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise' (ICA, 2012). Certain features of co-operative societies include voluntary and open membership, democratic control by members, autonomy and independence, community participation, and the primary objective of continuous development of their members.

With the rapid increase in co-operative societies from about 32 in 1940 to 314 in 1950, the Co-operative Bank Limited was established by the government in 1953[28] (Onuoha, 1986). The rationale was to take advantage of this expansion and employ the banks as an instrument for promoting rural finance to the poor who were scarcely reached by commercial banks and the mainstreaming of informal financial institutions into the formal financial system. With this government intervention, other regional and state co-operative banks began to emerge following this mandate to reach the poor through co-operative banks. This intervention of government as well as the further decision of early co-operative banks to transform into commercial banks resulted in the loss of autonomy and a neglect of their commitment to member and community development

[28] Even with the establishment of the Co-operative Bank Limited in 1953 and the introduction of other branches across the country, several community based co-operative societies still existed across Nigeria.

as they were required to meet the same requirements as commercial banks. The introduction of collateral requirements, market rates on loans and the closure of rural branches in a bid to move towards a more profitable market, led to the exclusion of co-operative societies as they were crowded out. Finally, the declining relevance of agriculture in the economy by the early 1980s encouraged further decline in co-operative societies as the bulk of the co-operative movement was by the agricultural co-operative societies (Ehigiamusoe, 2011).

With declining crude oil prices in the 1980s[29] and the negative impact of the Structural Adjustment Programme (SAP) adopted in 1986 on the welfare of the poor, the Peoples Bank of Nigeria was established in 1989. The mandate was to provide financial services to the poor and micro entrepreneurs – petty traders, artisans, farmers etc. Although the operational structure of the bank was derived from the Grameen Bank, the extent to which the agenda was implemented is subject to contention. Service delivery was through group lending with frequent repayment instalments. Despite wide outreach in the first 3 to 4 years, the bank began to experience difficulty in fulfilling its obligations to both depositors and borrowers. This was particularly due to poor repayment performance. The public perception of this attempt by the government to assist the poor through subsidized credit was interpreted as charity. Borrowers saw this as their opportunity to share in the 'national cake' and hence, majority of borrowers defaulted in their loans. Poor institutional structures as well as a distressing financial sector led to the collapse of the bank (Ehigiamusoe, 2011).

Over the years, the government has initiated other rural credit schemes with the aim of tackling poverty through increased access to financial services for the economically active poor (Okojie *et al.,* 2000 and Ajakaiye and Adeyeye, 2001). Some of these initiatives include: Community Banks (CBs), Better Life Programme (BLP), Family Economic Advancement Programme (FEAP), National Poverty Eradication Programme (NAPEP), and the Department of Food, Roads and Rural Infrastructure (DFFRI). These programmes like the ones before them have however been daunted with problems such as huge transactions cost, poor implementation, management inefficiencies, high default rates, corruption and a bias towards urban credit allocation. Following the collapse of these initiatives and their inability to meet the financial needs of the growing poor, several unregulated MFIs and other NGOs emerged to

[29] With the heavy dependence of the Nigerian economy on crude oil (see section 3.1), declining oil prices would exert a downward pressure on foreign exchange earnings and government expenditure.

drive the provision of microfinance to the poor in Nigeria. Particularly, these organizations grew rapidly over the last two decades of the twentieth century and have continued to increase ever since. These institutions particularly laid the foundation for the development and expansion of modern microfinance in Nigeria.

4.4.2 MODERN MICROFINANCE

With the widely acclaimed success of the Grameen microfinance model in Bangladesh in the late 1980s, several Grameen-like non-governmental organisations (NGOs) began to emerge in different communities across Nigeria during this period. These NGOs were committed to addressing the problem of poverty or some other social ill particularly among women in rural areas through the supply of affordable financial, health and social empowerment services. However, over time for majority of these NGOs, microfinance emerged as the primary services provided. Through institutional restructuring, the provision of non-financial activities was separated from financial services as sister organizations were set up to implement the former. Some early NGO MFIs include the country women association of Nigeria (COWAN), NALT united self-help organization (NUSHO), lift above poverty organization (LAPO), development exchange centre (DEC) and community development foundation (CDF).

Particularly, support from donor agencies and the existence of a support network among these NGOs led to a rapid rise in their development. Donor support came in the form of subsidized credit, grants, training and technical support and institutional development from Ford Foundation, UNDP, Grameen Foundation, Oxfam-NOVIB amongst others. For instance, between 1993 and 2004, the Ford foundation provided capacity building grants worth NGN 19 million to 241 organisations and refinancing loans worth NGN 205.4 million to 241 organisations (Ehigiamusoe, 2011). As discussed in section 3.3, this period coincides with the second wave of attempts to provide financial services to the poor. With the understanding that the poor are potential entrepreneurs, donor support was targeted towards the provision of financial and non-financial services to the poor with the goal of building capacity.

Recognizing the increasing role of these institutions and in line with the United Nations designation of the year 2005 as the International Year of Microcredit, the Central Bank of Nigeria (CBN) enacted the microfinance policy framework in 2005. Overall, the microfinance policy framework is designed to: increase financial access, promote the integration of the informal financial sector into the formal sector, enhance service delivery by MFIs, and contribute to rural finance development (CBN, 2005).

This is expected to lead to employment creation and increased productivity of the active poor, with ensuing increase in income and increase in the standard of living. The policy framework also called for the professionalization and regulation of microfinance practice in Nigeria. This is particularly important for client protection against unfair practices and to guarantee proper financial disclosures (Osthoff, 2005).

In establishing the framework for the operations of microfinance, private sector-driven microfinance banks (MfBs) were required to be licensed as a unit bank or as a state bank. The former is given a license to operate branches within a given community with minimum paid-up capital of NGN20 million per branch. The latter can operate branches across all parts of the state in which they are registered, subject to meeting the required minimum paid-up capital of NGN1 billion. With regard to the participation of existing financial institutions in the microfinance industry, universal banks currently engaged in providing microfinance services are required to set up a subsidiary or a department to handle these activities, subject to meeting the appropriate minimum paid-up capital. Previously licensed community banks were all required to obtain a license and transform into a unit or state MfB within 24 months from the date of the policy approval; also subject to meeting the capital requirements. This framework also recognises certain membership-based, credit-only MFIs (NGO-MFIs) which are not mandated to come under the supervision of the CBN but rather to submit periodic reports to the CBN. They are restricted to providing microcredit and prohibited from mobilizing savings from the public. However, NGO-MFIs who meet the capital requirements for MfBs, can either convert fully into an MfB or incorporate a subsidiary to handle the MfB activities. This is the case of the case-study MfB employed in this study - LAPO MfB, a subsidiary of the LAPO NGO group.

The microfinance policy framework is expected to address certain lapses in the microfinance industry such as: weak capital base, weak institutional capacity and low outreach. With this framework establishing a positive platform for the growth of microfinance, the Nigerian microfinance industry experienced rapid growth; from an initial licensing of 8 Microfinance Banks in 2006 to 724 as at October 2008. This included 117 new entrants and 607 initial community banks (CGAP, 2011). Consolidated asset and equity of the MfBs increased by 136 percent and 248 percent respectively between 2005 and 2008 (see table 4.4 below). This period also coincides with the third wave of microfinance attempts; characterised by the understanding that providing financial services to the poor can be a profitable venture and that financially sustainable MFIs are likely to be more effective in providing microfinance. This reported growth in size with regards to value and outreach of the Nigerian microfinance industry is a characteristic of the commercialisation of microfinance. This is also accompanied by rapid increase in interest rates as MFIs sought to achieve financial sustainability. Microfinance rates in Nigeria currently range between 18 percent and 72 percent annually (LAPO, 2013).[30]

Table 4.4: Consolidated Balance Sheet for Nigerian MfBs 2005-2008 (US$ millions)

	2005	2006	2007	2008 (June)
Exchange rate (NGN to USD)	130.00	134.00	120.00	115.00
Total Assets	354,329	410,866	629,583	838,174
Loan Portfolio	111,903	123,124	190,419	282,929
Total Liabilities	275,277	315,727	447,826	563,123
Deposits	220,950	253,797	343,481	437,180
Equity	79,052	95,139	181,757	275,051

Source: CGAP, 2011

However, turmoil brewing from the 2008 global financial crisis revealed certain flaws in the institutional capacities and capital base of these MfBs. In November 2010, 224 MfBs were stripped of their operating licenses. Amongst other things, poor asset quality, poor corporate governance, weak risk management and weak internal control were cited as reasons for the withdrawal of the licenses. In an attempt to tackle these challenges, the microfinance policy framework was revised in 2011 to account for these weaknesses. This revised framework provides that MfBs be better managed, adequately capitalized, and operate in a sound and safe manner. Recent figures from the CBN shows significant recovery with reported increases in key performance indicators. The significant increase (60 percent) in assets and liabilities between 2010 and 2012 is largely attributed to renewed investor confidence in the microfinance sector. Investible funds attracted by the microfinance sector also increased from N9.0 billion in 2011 to N11.8 billion in 2012. Similarly, the shareholders' funds and paid-up capital increased by 7.6 and 9.2 per cent to N47.3 billion and N45.4 billion, respectively. Deposits as well as loans and advances also increased by 13.6 and 27.9 per cent, respectively (CBN, 2011, 2012).

Overall, the Nigerian microfinance sector has experienced strong growth in the recent past and this growth is expected to continue under supportive government policies.

[30] See Table A.2 in Appendix A for a comparative pricing analyses of perceived strong LAPO competitors

One top MfB in Nigeria that has consistently enjoyed rapid growth with international and national recognition is the Lift above Poverty Organisation (LAPO) MfB. Particularly, compared to other MFBs; LAPOs strength lies in its outreach to the poor and female clients as shown in table 4.5 below. Although Babura MFB reports higher values for loans, deposits and assets, the number of active clients suggests that her clients are relatively non-poor compared to LAPO clients. Thus, LAPO microfinance intervention is employed as the case study in this research work. LAPO annual dropout rate of about 30 percent is typical of the high rates of dropout recorded in the microfinance industry. This figure also includes savers who may drop-out after accumulating savings for an intended purpose.

Table 4.5: Comparison of LAPO and other Key MFBs in Nigeria

	LAPO	Fortis	Babura	SEAP	Accion
Gross Loan Portfolio	108,410,675	38,829,581	905,247,319	59,419,085	12,124,656
No. of active borrowers	559,227	16,965	1,825	349,470	14,426
% of female borrowers	0.9251	0.72	0.4866	0.91	0.6698
Borrower retention rate	0.6864	NA*	0.8445	0.6645	NA
Deposits	62,715,664	40,186,337	480,508,767	42,264,281	3,479,411
Borrowings	27,477,079	858,149	NA	NA	NA
Financial revenue	55,558,818	12,148,300	400,847,911	15,498,247	8,938,279
Assets	132,167,524	49,830,608	1,222 347,941	62,942,003	16,925,354

Source: MixMarket, 2013
* NA means not available

4.5 LIFT ABOVE POVERTY ORGANISATION (LAPO), NIGERIA

LAPO is a pro-poor privately owned non-governmental organization (NGO) established in Benin City, Nigeria in the late 1980s. It is committed to the economic and social empowerment of LIHs through the provision of affordable financial and non-financial services. In 2010, LAPO obtained the CBN approval to set up LAPO MfB operating as a state MfB; and in 2012, it gained the approval to operate as a national MfB. At present time, LAPO services are offered in Nigeria and Sierra Leone to both rural and urban clients. Its 326 local units spread across 5[31] out of the 6 geo-political zones in Nigeria served some 756,904 active savers and 559,227 active borrowers as at December 31, 2012. The development track record of LAPO has been characterised by high growth rate and rapid progress towards financial sustainability (See table 4.6 below). From 2009 to 2013, the client base grew by an outstanding 234.5 percent. LAPO now serves more than 1,000,000 clients with over 90 percent of

[31] South-South, South-West, South-East, North-Central and North-East

them women. To service the growing client base, LAPO disbursed about NGN 20.2 billion in loans as at the end of 2013 (LAPO, 2013).

Table 4.6: Sustainability and Performance Indicators of LAPO MfB

	2008	**2009**	**2010**	**2011**	**2012**	**2013**
Assets (NGNbn)	5.39	7.64	9.93	14.03	20.63	27.57
Loan portfolio (NGNbn)	3.56	4.01	7.41	11.39	16.92	23.44
Growth (%)	*83.1*	*12.6*	*84.9*	*53.6*	*48.6*	
No. of clients	N/A	304, 385	442, 974	623, 307	861, 078	1,018,106
Female clients (%)	98.0	98.0	N/A	93.4	92.5	92.8
Active savers	245,144	243,055	355,502	518,187	756,904	
Growth (%)	*82.6*	*-0.9*	*46.3*	*45.8*	*46.1*	
Active borrowers	200,115	195,016	303,882	421,126	559,227	658,138
Growth (%)	*54.8*	*-2.5*	*55.8*	*38.6*	*32.8*	
No. of local units	171	226	230	268	302	321
Retention rate (%)	N/A	N/A	N/A	67.2	68.4	N/A
Portfolio at Risk (PaR)	1.33	2.28	1.40	0.99	N/A	1.18

Source: Mixmarket, 2014

LAPO MfB is adopted as the case-study microfinance intervention in this research work; as it meets the definition and conceptualization of microfinance in this study. As is presented in the subsequent sections, LAPO MfB provides both financial (credit, savings and insurance) and non-financial services to the poor. As mentioned in the literature review, we hypothesize that these features and their implementation processes affect the utility or disutility that clients experience with microfinance use; and also their ability to expand capabilities. Hence, we proceed to understand the organizational products and services delivered by LAPO and the operational procedures that guide their delivery.

4.5.1 Operational Procedures, Products and Service Delivery

LAPO's effective strategy is established based on the Grameen Bank model of group lending. Although other non-group individual lending methodology exists and is increasingly gaining thrust in the LAPO intervention, the majority of clients are group-based. The target clients are predominantly poor economic active women who run microenterprises characterised by limited access to the formal financial sector, enterprises owned and run by one person; and operating from makeshift tables or kiosks, booths and market shops. For these clients, access to and use of microfinance is only possible with participation in a lending group or by choosing to save with LAPO MfB. While the former includes access to credit, savings, insurance and non-financial services, the latter only guarantees access to savings and non-financial services. Based on the definition of microfinance in this study, this study covers clients who are been served by and engage in the group practice. Additionally, clients who qualify for individual loans must be at least relatively ‘less poor’ compared to clients who engage in group lending. They are more likely to own some form of collateralized asset which qualifies them for individual loans. Thus, with our emphasis on poverty reduction, clients who engage in group lending are perceived to be more suitable for the study.

LAPOs operational procedures allow for groups to be formed during loan drives[32] when client support officers (CSOs) market LAPO products to identified groups of potential clients or when groups of prospective clients approach LAPO for loans. LAPO groups consist of a minimum of 10 clients and are self-formed on the basis of proximity, association and/or occupational homogeneity. Particularly for the poor, membership in a group is the main pathway to accessing microfinance. This reflects the social capability dimension of microfinance. It also suggests that certain individuals who do not have a rich wealth of social relationships or affiliations may be excluded. However, this is not expected to be a major challenge in the Nigerian context as communal living is the order of the day. Potential clients must be at least 18 years old, own a durable business, commit to regularly attend weekly union meetings, and must live in the district where the union is sited. Once the lending groups are formed or new clients are accepted into an existing group, clients are required to provide their address, two passport photographs and a guarantor who may be their spouse or any other individual who can attest to their character. They are then expected to go through a 6 weeks probation period which includes a series of training on money management, loan use and budgeting, and a commitment to attend weekly group meetings during and after probation. During the probation period, service users are generally provided with information on the financial and non-financial services provided by the MFI, how to access these services as well as the contractual requirements involving their use.

At the end of the probation period, service users qualify to apply for credit. To do this, all members have to give their signature as approval that the loan should be granted. This process is repeated each time a new loan is applied for. By doing this, they all stand as a surety for the repayment of loans. This represents a formal sign of joint liability. Here, although loans are issued on an individual basis, the repayment liability

[32] These are marketing exercises where the CSOs go into the community to market LAPO products and services.

rests on the entire group. When individuals are unable to meet their repayment, the group is jointly held liable. LAPO heavily relies on collaterals in the form of group solidarity, as well as cash collateral (mandatory savings requirements) and client guarantors. It is only when LAPO is unable to claim repayments from the group that it explores other options such as selling off clients' personal properties or holding guarantors liable. For this reason, LAPOs practice is that groups be self-formed. The monitoring of loans is also done by clients. As far as LAPO is concerned, accessing a clients' capacity to repay loans ends with proof of a viable business to which the loan is to be invested. It is expected that the joint liability feature of group lending will encourage peer monitoring and make group members responsible for monitoring their peers. As regards peer support and pressure, there is no specified way as to how this is done. This is left to the prerogative of the different unions.

All of these suggest that the delivery of the LAPO microfinance intervention is consistent with the prescribed practice discussed in chapter 3. However, it is important to examine if this is the reality on ground. Are groups actually formed based on peer selection? What is clients approach to peer monitoring? As mentioned in chapter 3, group lending involves the transfer of information, monitoring and enforcement costs to the clients. How do they deal with these costs? In all, how does the microfinance implementation processes affect the utility or disutility they experience with using microfinance and in turn their potential for capability expansion? It is important to note that the operating strategy is the same for rural and urban areas. As regards the focus on women, LAPO considers itself to be pro-women; and so although it targets poor women, it does not exclude male clients who demand for its services. Beyond the implementation processes, we also consider the features of the LAPO intervention and their potential for capability expansion.

4.5.1.1 Loan Products

LAPO MfB offers three main loan products designed to meet the emerging and varied needs of her clients (See table 4.7 below).

Table 4.7: LAPO MfB Loan Products

Type of loan	Interest Rate %	Average Duration
Regular Business Loan	2.2%	30 weeks
Farming Loan	2.2%	12 months of two stages of 6months each
Festival Loan	2.2%	4 months

Source: Clients Relations Unit LAPO MfB limited, 2013

Since January 2013, all borrowing clients pay a monthly flat rate of 2.2[33] percent and an additional 1 percent processing fee. In 2013, LAPO increased the minimum loan size from NGN 30,000 to 50,000. This increase is the result of inflation[34] and the continuous demand by LAPO clients for higher loans (LAPO, 2013). The regular business loan is LAPO's core loan product designed to finance working capital needs of clients; with weekly repayments. The farming loan has a longer repayment cycle, accounting for seasonality and low-productivity of subsistence agriculture. Repayment on the farming loan is made monthly and it attracts a 3 percent insurance premium. The festival loan is designed to finance the needs of LAPO's clients during holiday and festive periods (Christmas and Eid). Festival Loans range from 30,000 to 50,000 NGN and are repaid in three monthly installments after a one month grace period. Through a dynamic incentive process, the loans are disbursed progressively to members of the group (see table 4.8). Other loan products[35] that clients can apply for depending on how well they have been able to meet past repayment liabilities include: mid-term loans, small business loans etc.

Table 4.8: Loan Size by Loan Type

Loan Size per cycle	Regular Business Loan	Farming Loan
1st	50000	50000 at start off
2nd	70000	Hereafter amount varies and depends on the farm needs
3rd	90000	
4th	110000	
5th	130000	
6th	150000	
7th	170000	

Source: LAPO Admin Records, 2013

In the past, LAPO has been accused of charging too high interest rates. For instance, Sinclair, 2012 in his book '*Confessions of a Microfinance Heretic*', largely accuses LAPO of charging extortionate rates. He rests his arguments on the findings by MFTransparency and Planet Rating. Particularly, he criticises LAPO for charging 144

[33] This was recently reduced from 2.5 percent.
[34] To express the initial loan amount (NGN 30000) in 2014 Naira, we adjust for inflation using the CPI for all items. The CBN adopts the November 2009 index as the base year. Comparing this with the January 2014 index which is reported to be 153.26, the 2014 cost of a 2009 NGN 30000 loan is approximately NGN 46000.
[35] Other loans issued by LAPO include mid-term loan, small business loan etc. (see Appendix A for Table A.2)

percent annual percentage rate[36] (APR) on loans as well as the illegal intermediation of savings by LAPO.

> 'The decrease in interest rates coupled with the increase in the level of cash collateral resulted in an increase of the average Effective Interest Rate (EIR) for the clients to 125.9% from 114.3% before…. as the client remains with LAPO, the APR can reach between 99% and 144% by the third year (depending on the loan amount and increase at each cycle) due to the cost of accumulating weekly savings that cannot be withdrawn' (Planet Rating, 2011:5-7).

In the light of these criticisms, LAPO has since 2010 become licensed as a Microfinance Bank which allows for the legal intermediation of savings. The recent decrease in interest rates from 2.5 percent to 2.2 percent was accompanied with a reduction in mandatory savings which would imply a reduction in the APR. In addition, we find that LAPO rates are consistent with interest rates charged by other top MfBs in Nigeria (See appendix A for Table A.1). Some of the reasons for high interest rates in Nigeria include high operating and infrastructure costs. For example, LAPO must provide power generating plants for all her branches. In 2008, operating costs of MFIs in Nigeria was almost 47 percent of total loan portfolio (MixMarket, 2008)[37]. In the same year, LAPO reported financial expenses equal to 13.3 percent of its average portfolio[38]. Additionally, LAPO has often argued that high repayment rates of over 95 percent prove the affordability of the interest rates charged. Nevertheless, in line with the objectives of this study, clients experience with loans and particularly their affordability of the interest rate will be explored. As mentioned in chapter 3, the features and implementation processes of microloans - loan size, repayment frequency, and interest rate - influence service users experience with microfinance. They affect the utility or disutility that clients experience with microfinance as well as their ability to achieve capability expansion from the use of microfinance. These factors will be explored in this study with particular attention to their potential for expanding or reducing clients' capabilities.

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[36] The APR here reflects the cost of capital and consists of the interest rate, any fees charged and forced savings.

[37]http://www.mixmarket.org/mfi/benchmarks?mix_region__c=All&country__c=Nigeria¤t_legal_status__c=All

[38] (https://www.cia.gov/library/publications/the-world-factbook/geos/ni.html)

4.5.1.2 Savings

LAPO MfB primarily offers two main[39] savings products – mandatory savings and voluntary savings accounts – with each product distinct in service terms. The mandatory savings account accompanies the regular loan account and is a prerequisite to accessing microcredit from the institution at the group level. This comes in two forms: first, before any loan is issued, clients are expected to have saved NGN1000 and 10% initial deposit of the approved loan amount; or NGN1500 and 5 percent initial deposit of the approved loan amount before loans are granted for individual and group loans respectively. Second, with every weekly loan repayment made, there is an associated mandatory weekly savings (see Figure 4.4 below). This mandatory savings balance serves as loan guarantee (cash substitute) which the clients cannot withdraw from until they have paid off their credits.

Figure 4.4: LAPOs repayment structure

LAPO initial loan size = NGN 50,000
Interest rate p/annum = 26.4%
Interest rate p/month = 2.2%
Loan period = 8 months or 30 weeks

Monthly interest on loans = 2.2% or 0.022 * 50, 000 = 1,100
Principal + Interest = 50,000 + 8,800 (1,100*8months) = 58,800
Weekly loan repayment to LAPO = 58,800/30 weeks = 1,960

Weekly Compulsory savings = Savings for clients [a] (540) + Savings for the union purse [b] (100) = 640
Total weekly repayment = NGN 1,960 + NGN 640 = NGN 2,600*

[a] CBN regulatory policy is that clients MUST have savings outside their repayment plan, hence the 540 monthly savings.
[b] This is for the union purse which is set by LAPO to cushion the effect of a defaulting or delinquent member
*Repayment is incomplete if this sum is not fully paid

Although individuals retain the right to their mandatory savings, in the event of a default within the group, LAPO might make deductions to fulfil the obligations arising from joint liability. While this represents a form of collateral for the MfB, some studies[40] point to the drawback of mandatory savings; namely that, it leaves clients unable to access their own savings in times of difficulties and results in clients forgoing interest income that would otherwise be earned on an individual savings account. According to Pagura (2003), the forgone interest income indirectly increases the effective rate of borrowing. Also, the potential of losing savings in the event of

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[39] Just like the loan products, there are other non-standard savings products provided by LAPO. See appendix A for Table A.3
[40] (Fribig *et al.*, 1999; Pagura, 2003; Armendariz de Aghion and Morduch, 2005; Osthoff, 2005)

default is a cost to clients. On the other hand, voluntary savings is dependent on clients' free will and clients are free to make withdrawals at any time for any amount. This account earns interest at a rate of 2 percent per annum but does not qualify a client to access loans or insurance (LAPO, 2012). As noted in the literature review, savings is expected to increase the capability of the poor to meet certain lifecycle, emergency and investment needs (Rutherford, 2000). In this study, we will investigate if this is the reality for LAPO clients and what their experience is with the mandatory and voluntary savings.

4.5.1.3 Insurance services

Micro-insurance services are a recent introduction at LAPO MfB, and are provided in partnership with Goldlink Insurance Plc. This includes insurance for life and disability, market place fire, and childbirth insurance. Plans are also underway to include comprehensive health insurance. LAPO clients – individual and group borrowers – pay 0.5 percent insurance premium per loan. In 2012, 2788 clients benefited from these services with a total compensation of NGN 102 million (see table 4.9 below). Considering the low use of insurance services in Nigeria, the growth in the number of beneficiaries from 792 in 2011 to 2,788 in 2012 (252 percent) implies a spectacular growth in the level of financial inclusion (LAPO, 2012). As mentioned in the literature review, the use of insurance is expected to expand clients' capabilities to protect themselves from income and expenditure shocks that are likely to adversely affect the poor. Hence, it would be important to explore clients experience with these insurance products and particularly how well they are able to enhance the expansion of capabilities.

Table 4.9: LAPO MfB Micro-insurance Scheme

Risks Covered	2011		2012	
	No. of Beneficiaries	Compensation Received	No. of Beneficiaries	Compensation Received
Death	649	29, 480, 000	1, 128	55, 767, 890
Fire	112	6, 468, 400	290	23, 880, 000
Medical	30	286, 790	1, 292	19, 053, 100
TPD*	1	120, 522	78	3, 241, 133
Total	792	36, 355, 712	2, 788	101, 942, 123

*TPD: Temporary and Permanent Disability

Source: LAPO MfB Limited Annual Social Report 2012

4.5.1.4 Non-financial services

LAPO MfB recognizes that the Nigerian poor face multidimensional deprivations and that the provision of non-financial services in addition to financial services has the potential of expanding the capabilities of the poor. The non-financial services provided by LAPO include:

First, financial and business education programmes

- money management
- loan use
- financial literacy, and
- budgeting

Second, in partnership with LAPO NGO, LAPO MfB provides health and social empowerment programmes directed towards creating awareness on

- HIV/AIDS prevention
- gender equality
- maternal and child health
- family planning
- adult literacy
- the provision of legal advice, and
- the provision of child education scholarship (LAPO, 2012)

While the former is more directed towards increasing the productive use of microfinance, the latter focuses on social empowerment and other welfare related measures. We will therefore expect them to have a direct or indirect positive effect on increased capabilities at the business and household level. The LAPO MfB social empowerment report shows that in 2012, 1,946 LAPO MfB clients facing gender-based injustice in the form of deprivation of their rights to inheritance, benefited from legal aid services provided by LAPO NGO. In the same year, a total of 14,290 clients benefited from malaria, HIV, blood sugar and blood pressure tests with 383 clients receiving cervical/breast cancer screening. As mentioned in the literature review, these services are important for creating and expanding capabilities of the poor; making them relevant in this study. Although the types of non-financial services provided by LAPO are more targeted towards individual or household capabilities rather than business inclined, this still remains relevant for this study.We however placed an emphasis on the *right training* at the *right time* provided in the *right way*. Hence, it would be important to explore the quality of these services, clients experience with them and particularly how well they are able to enhance the expansion of capabilities.

4.6 CONCLUSION

This chapter examined poverty and microfinance in Nigeria. With the contextual emphasis in this study, this chapter explored the Nigerian economic and financial background to establish the contextual need and relevance of this study. It particularly described the multidimensional nature of poverty in Nigeria and highlights its significance for the capability approach to poverty adopted in this study. It also established the high level of financial exclusion of the poor, the growing poor population, and the implication of this for the growing size of the Nigerian microfinance industry. One of the largest MFIs in Nigeria – LAPO MfB which provides both financial (credit, savings and insurance) and non-financial services to the poor, was selected as the case-study MFI in this research work as it meets the definition and conceptualization of microfinance in this study. Hence, the final sections of the chapter are devoted to understanding the organizational products and services delivered by LAPO and the operational procedures that guide their delivery. This provides contextual information required to evaluate microfinance features and their implementation processes. This includes information about who LAPO services users are, what services do they have access to and use, and how these services are delivered.

CHAPTER FIVE

ANALYTICAL FRAMEWORK AND RESEARCH METHODOLOGY

5.1 INTRODUCTION

The previous chapter reviewed the relevant literature on microfinance and established that there is indeed a gap which is identified as the need for studies that look beyond impact to investigate the features and characteristics of microfinance delivery and use which have potential for 'harm' and 'good' from the clients' perspective. Having established the conceptualization of poverty and microfinance in this study, this chapter presents the analytical framework adopted for tackling the research problem. It is designed to identify analytical and methodological approaches that will guide and inform the rest of the thesis and allow for answering of the research question. Given the emphasis on the context/perception of microfinance clients and recognising the different components of microfinance that contribute to the clients overall experience, the goal is to identify research approaches that allows the researcher to account for these factors. This chapter consists of four main sections. It begins with discussing the research approach and the theoretical frameworks that guide their implementation. Next, it discusses mixed methods as an appropriate methodological framework consistent with the research approaches selected. This is followed by a description of the fieldwork exercise beginning from the selection of the study area to the collection of the required data. Finally, the techniques for analysing the research data are presented.

5.2 THEORETICAL BASIS FOR THE RESEARCH APPROACH: THE INTERPRETIVE, CAPABILITY AND PARTICIPATORY POVERTY ASSESSMENT APPROACH

This section presents the theoretical justification for the research approach adopted in this study. The research approach refers to the research plan and includes the method of collection, analysis and interpretation of data. These methods are informed by certain philosophical or theoretical assumptions that guide the issues being addressed. Additionally, the nature of the research objective or problem also guides the research approach adopted. With our conceptualisation of poverty as 'capability deprivations' and the emphasis on understanding the potential of microfinance for poverty reduction from the 'clients' perspective', this study employs three theoretical frameworks that guide the research approach. The Interpretive, capability and participatory poverty assessment approaches are identified as appropriate frameworks for addressing the research questions.

5.2.1 The Interpretive Approach (IA)

This study adopts the interpretive approach to conducting social science research. The IA focuses on human beings and the way they interpret and make sense of social reality. 'Interpretive approaches start with the insight that to understand actions, practices and institutions, we need to grasp the relevant meanings, beliefs and preferences of the people involved (Bevir and Rhodes, 2004: 130)'. Hence, given that answering the research questions identified in the previous chapter requires that the researcher accurately conveys the perception of microfinance clients, the IA is appropriate. The IA is increasingly being employed to a variety of studies in the area of psychology, sociology, political science, management and consumer studies.

In capturing the experiences of microfinance clients, this study employs the methodology developed by Wilhelm Dilthey, which is summarized in Tappan's (2001) detailed review. Dilthey argues that in contrast to the natural sciences, social science research must account for the subjectivity of human beings. He argues that human perspectives i.e. the way people think, feel and act is shaped by the 'lived experiences' of individuals. This lived experience summarizes an individual's human existence and is subjective in nature. For a researcher to understand and interpret the lived experiences of individuals, it has to first be expressed. This can be done in writing (a book, film, poetry), through art or an interview narrative. However, the multiplicity of human perspectives creates problems of prejudice and bias.

Hence, Dilthey tried to find ways to objectively interpret expressions of lived experiences in order to understand people. He suggests that in order to successfully do this, the cultural, historical and psychological context of individuals must be taken into account. By arguing that humans do not live in a vacuum, he proposes that the interpretation and understanding of respondent experiences should be done within a specified context. The researcher needs to understand that social reality is socially constructed. However, he recognises that despite attempts to ensure objectivity, there is no such thing as a non-positional understanding. 'Researchers understand by continuous reference to their own perspectives' (Yeboah, 2010:107). This implies that the researchers lived experiences and thus perspectives can influence their understanding and interpretation of the lived experiences of others. While this problem may constitute a constant feature of social science research, it can be ameliorated through increased exposure of the researcher to the lived experiences of the researched. This is believed to improve the understanding and interpretation of research findings. This understanding that social reality is socially constructed will guide the selection of a research methodology, the study area, data collection, analysis, and the interpretation of research findings.

5.2.2 Participatory Poverty Assessment (PPA) Approach

Conventional monetary and capability poverty estimates have been critiqued for being *externally* prescribed, and for not accounting for the views of the poor themselves. Traditional approaches to investigating poverty have focused on quantitative aggregate measures of income and welfare. This includes well-known measures such as the dollar a day measure of poverty, the Human Development index, and the Gini coefficient with indicators such as expenditure, consumption, education, health etc. As mentioned in chapter 2, these measures only tell a partial story. They neither reveal location specific variations nor subjective elements of the experiences of the poor with poverty or the coping mechanisms adopted by different individuals (Baulch and Masset, 2003). In light of these issues, there has been an increasing realisation amongst policy makers and development practitioners that the inclusion of the perspectives of the poor is an important requirement for a more comprehensive understanding of poverty.

This is the main focus of the PPA - getting the poor themselves to participate in deliberations about the meaning, dimensions and consequences of poverty (Chambers, 1994, 1997). The PPA approach emerged from participatory rural appraisals (PRAs), defined as ‘a growing family of approaches and methods to enable local people to share, enhance and analyse their knowledge of life and conditions, to plan and to act’ (Chambers, 1994:57). It employs data collection and analysis methods that account for contextual differences i.e. data collection methods that ‘attempt to understand poverty dimensions within the social, cultural, economic and political environment of a locality’ (Booth *et al*., 1998:52). It emphasizes poor people’s capacity for understanding and analysing their own reality. It empowers them to make judgements on their welfare which in other approaches would be externally imposed.

Participatory poverty assessments (PPAs) have proven to be effective in capturing the multi-dimensional and culturally contingent aspects of poverty. Several World Bank poverty assessment studies have also employed qualitative and participatory methods to provide complementary information to household surveys (Narayan et al, 1999). For instance, the *Voices of the Poor* project which sampled over 60,000 voices from 78 PPA studies conducted across 47 countries, identifies a wider set of capability dimensions than is usually covered by the traditional approaches. Certain emerging themes from this study include: hunger, powerlessness, deprivation, violation of dignity, resilience, social isolation, solidarity, resourcefulness, state corruption and gender inequity. With the research questions - how do microfinance clients define poverty, and what capabilities do they value and have reason to value – adopted in this study, the PPA is adopted alongside the IA as appropriate approaches.

There are two underlying conventions that distinguish the PPA from other research approaches. First, it actively engages the "respondents" in the research process using open-ended questions and participatory methods. Second, by placing importance on the perspective of the respondent – 'giving them a voice', it is expected to empower respondents. Though difficult to quantify, PPAs offer valuable insights into the various meanings, and dimensions of poverty that standard poverty assessments are not likely to capture. Some reasons for this include: first, the use of open-ended and unstructured/semi-structured questions allows for the emergence of dimensions of poverty not known to the researcher but important to the community. Second, PPAs have the potential to account for power dynamics within and outside the households. They are also able to better illuminate and negotiate power dynamics between the non-poor and the poor, between men and women and between members of different social groups. Nevertheless, they do not replace information generated from traditional macro-level surveys, but rather provide crucial complimentary information on poverty.

However, given the heterogeneity in communities, one question that arises is: whose voice is being heard. Where communities have different ethnic groups and cultural traditions, the PPA approach has no established technique or guidelines on how to reach a single community view. Furthermore, certain disadvantaged groups are likely to decline from voicing opinions that oppose the more powerful and influential members of the community, due to fear of harm. Hence, it has been argued that the PPA approach is likely to explore existing social relations (da Cunha & Junho Pena 1997). For instance, in the context of microfinance interventions, power struggle within the groups may prevent some clients from voicing their opinions for fear of harm. In order to mitigate these problems, the researcher will ensure that data collection is conducted in private where every participant can voice their opinions without fear. Also, in order to ensure that everyone's voice is heard, a purposeful sampling technique will be employed to ensure that various categories of clients including women, men, group leaders, new members, old members, and clients who have (not) experienced repayment difficulties are included in the study. In this way, we will be able to capture a wider perspective of clients.

Besides, some people - particularly the extremely poor - maybe excluded from the groups. This approach by focusing on microfinance clients does not take care of such exclusions. It also often involves small samples, which raises questions about how representative the sample is of the population. An individual's assessment of own condition can also be subjective and prejudiced as a result of social conditioning and limited information. The approach is therefore complex and by its own nature contains multidimensional analysis.

5.2.3 Applying the Capability Approach as an Evaluative and Prospective Framework

In operationalising the CA, Alkire (2008b:5) argues for the need to distinguish between two applications of the CA: evaluative and prospective. An evaluative application of the CA precisely assesses two states of affairs and asks, which one has expanded capabilities to a greater extent, which capabilities have expanded or contracted, – by how much, for how many people and for how long? On the contrary, a prospective application of the CA assesses a working set of activities and policies that are; at any point in time, most likely to engender considerable capability expansion – 'together with the processes by which these policies/ activities/ recommendations are generated and the contexts in which they will be more likely to deliver these benefits'.

Applying the CA as an evaluative technique requires that policies or programs be assessed based on their ability to promote individual freedoms as well as the achievement of functionings that people value. One inherent limitation of using the CA as an evaluative framework is that it may be too focused on assessing alternatives as regards their effects on human capabilities, making it less valuable for making recommendations. Although evaluations may and every so often do contribute towards recommendations, the focus of the exercise is entirely different. It explores the benefits and disbenefits associated with different states of affairs as these appear to different groups and to people with different values or in different situations. Ultimately, they refer to information on whether individual capabilities have expanded or contracted, rather than why and how such expansion or contraction occurred.

Yet, another important issue of concern is: which alternative is more able to advance human capabilities, and which possible recommendation should or could we make from using the CA. This is the main objective of the prospective application of the CA – to identify which alternative is likely to generate a greater stream of expanded capabilities. It also covers an equally vital set of issues relating to causality and process (why and how): what changes to existing activities/practices, institutional, cultural, social, economic and political structures would expand capabilities. From the above discussion, it is obvious that both methods of analyses are inter-related. Sen argues that the methodologies appropriate for evaluative and predictive exercises should be guided by "what serves the goals of the inquiry" (Sen 2004: p 595), bearing in mind that these goals will differ significantly.

Given the research objective and research questions adopted in chapter 3, the evaluative and prescriptive frameworks are adopted as an approach to answer specific research questions. The evaluative approach is applied in answering the question: how do the poor evaluate the ability of microfinance to spur the expansion of capabilities for the poor? Having identified the capabilities that clients value and have reason to value, the CA is adopted as a framework for evaluating what capabilities have expanded following increased access to and use of microfinance – by how much, for how many people, for who etc. On the other hand, the prospective approach is applied in answering the question: what borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor?

5.3 METHODOLOGICAL APPROACH: THE MIXED METHODS APPROACH

Several factors shape the decision of which methodology to adopt and these include: the researchers' perception of the social world - what can be known (ontology), what knowledge can be acquired and how (epistemology); the aims and objectives of the study; the contextual characteristics of the study area; the academic background and resources available to the researcher (Snape and Spencer, 2003; Creswell, 2003). Research methods tend to be defined along the qualitative /quantitative divide. For instance, researchers are usually trained, specialized, and recruited along single methods of social enquiry. Although this tradition ensures quality control and intellectual coherence, it is quite limiting (Rao and Woolcock, 2003).

The quantitative strand comes from empiricism and hence promotes the use of empirical and structured techniques to enable replication as in the natural sciences. It assumes the existence of a physical and social world independent of subjective perception. It therefore supports the use of quantitative research methods involving large samples, highly structured and empirical techniques of data collection (Benton and Craib, 2010). With the qualitative strand, reality is socially constructed and acceptable knowledge is subjective. Based on the postulation that the social world depends on the subjective perception of social actors, the research process focuses on understanding the meaning individuals give to social phenomena (Saunders et al, 2009). It therefore supports the use of qualitative research methods – small samples and in-depth interviews - to identify the reality behind each social phenomenon.

This study however applies a methodological orientation that is not limited to a single method of social enquiry. It applies a problem-centered, pluralistic and result-oriented approach. The idea is to prioritize the research objectives and to apply appropriate methodological techniques to achieve the objective regardless of what side of the divide the method belongs (Patton 1990; Creswell, 2003). This therefore allows for a mixed method approach (Robson, 2002) which involves a combination of the qualitative and quantitative method in understanding social reality (Hentschel, 1999; Bamberger, 2000; Creswell, 2003). The IA and PPA provide theoretical support for employing qualitative research methods in the collection and analysis of data. The capability approach allows for the collection and analysis of quantitative, qualitative and subjective data. In achieving the research objectives, a qualitative research method is employed to:

- identify the capabilities that microfinance clients in the Nigerian context value and have reason to value;
- evaluate the implementation processes and different components of microfinance interventions and their effects from the viewpoint of service users;

A quantitative research method is employed to:

- To evaluate the effectiveness of microfinance as a tool for poverty reduction.
- To investigate clients microfinance practices and their effect on the expansion of capabilities.

There have been suggestions on how to integrate these two research methods in the mixed method approach. Creswell (2003) proposes three forms of integration: the concurrent, sequential and the transformative. Concurrent integration refers to a situation where the researcher simultaneously applies the qualitative and quantitative data in providing a comprehensive analysis. With sequential integration, the researcher begins with one method and then develops and elaborates the other method based on the findings from the first. Transformative integration employs a theoretical perspective which combines both methods in a concurrent and/or a sequential form. Rao and Woolcock (2003) also propose three integration methods: sequential, parallel and iterative. In the parallel approach, researchers conduct the qualitative and quantitative analysis separately and then make comparison of the results. Sequential lending here is similar to the conceptualization by Creswell (2003) as explained earlier. The iterative approach involves returning to the field to resolve apparent disparities and clarify unanswered questions using alternative methodologies.

Although these studies provide a general idea of integrating research methods, they do not tell us how this integration should be done at the various phases of the research process. While this is possible, integration of research methods at all phases of the research process proves to be a difficult undertaking. In this study, the researcher attempts to integrate the qualitative and quantitative research methods as much as possible throughout the various stages of the research process – data collection, analysis and interpretation of findings. In doing this, a sequential integration process is employed. Beginning with the qualitative research exercise, the findings from this exercise will be incorporated into the design of the quantitative research. For example, the construction of data collection instruments and the interpretation of empirical findings in a quantitative study can be enriched by complementary qualitative findings. In the same way, statistical data can be used to buttress or clarify the qualitative findings from interviews, focus groups and key informants (Robson, 2002; Bamberger, 2000).

The qualitative and quantitative findings will be used to provide reliability checks and complement each other (triangulation). The growing acceptance of the mixed methods in development research is based on the realization that no data collection method or analytical technique is free from drawbacks and that inherent bias in one method could possibly be corrected by other methods (Creswell, 2003). For example, qualitative data is crucial for effective model construction, data analysis and interpretation in terms of understanding the effect on poverty reduction as opposed to just measuring the effect (Rao and Woolcock, 2003). However, the mixed methods approach is disadvantaged by high technical complexity and it is time and resource consuming. Additionally, the absence of a consensus in the literature on how or when qualitative and quantitative methods should be integrated, limits the use of this approach (Rao and Woolcock, 2003).

5.4 FIELDWORK

Having established the direction of this study and deciding the action plan for the successful achievement of the aim, the next agenda is the implementation of this plan. This is done through a fieldwork exercise. This section presents a reflective explanation of how this is undertaken, beginning with selecting an appropriate case-study area and MFI, collecting data and the technique for analysing this data.

5.4.1 SELECTION OF THE CASE STUDY AREA

The decision of where to conduct any research is very important to every research activity. To a great extent, this decision is often guided by the contextual suitability of the location in question, as well as the interest and imagination of the researcher, rather than just the need to apply scientific knowledge to answer a couple of research questions (Bechhofer and Patterson, 2000). Hence, the decision to adopt Nigeria as the case study for this research is no accident. Nigeria is the home country of the researcher and she has lived in the country for over 20 years. The choice of Nigeria is also in conformity with the aim of this thesis. Given the rapid expansion of microfinance and high poverty rates in Nigeria, the country fits the brief. A strong contextual emphasis combined with the objective of investigating microfinance from the clients' perspective has also guided the selection of the case study. The case study selection begins with selecting a community and then identifying a fitting microfinance intervention that can enable the researcher to answer the research questions. In selecting the community, the following criteria were used: poverty rates similar to national rates, the presence of more than one MFI with interventions spanning over 3 years, the researchers' knowledge of the study area as well as the safety of the researcher.

Based on the specified criteria, the researcher selected Edo State, located in southern Nigeria as the case study for this research. Beyond the purposive selection of the study area, it was also important that the study area possessed poverty characteristics similar to the national rates so that results could be applied to other communities. Table 5.1 shows that across various measures of poverty, this is the case.

Table 5.1: Case Study Poverty versus National Poverty rates 2010 (%)

	Food Poverty		**Absolute Poverty**		**Moderately poor based on 2/3 of the weighted mean household per capita expenditure regionally deflated (Relative Poverty)**		**Dollar per day based on adjusted 2005 PPP**	
	Poor	Non Poor	Poor	Non Poor	Poor	Non Poor	Poor	Non Poor
National	41.0	59.0	60.9	39.1	69.0	31.0	61.2	38.8
Edo State (study area)	39.4	60.6	65.6	34.4	72.5	27.5	66.0	34.0

Source: NBS, 2012

With the emphasis on context in this study; the researchers' knowledge of the cultural, economic, linguistic and social, characteristics of the study area also influenced the choice of this state. This satisfies the argument that researchers engaging in fieldwork should be well-informed of the values, social organisation and economic issues of the study area before undertaking data collection (Hershfield et al., 1983). The ability to communicate in the common language of the study area was particularly important, given the high level of illiteracy among respondents. Although the literacy rate in Nigeria is high, the literacy level among the poor is low and majority of the poor communicate in 'pidgin English'. This meant that the administration of the interviews and questionnaires had to be done in 'pidgin English'. A key advantage of understanding this local language was that the researcher could administer and translate the questions by herself, thus maintaining good control over the fieldwork exercise. Additionally, as Devereux (1992) notes, a good knowledge of the language of the study area gives respondents the opportunity to express their lived experiences in a convenient and fluent way and enables the collection of richer information.

The argument for selecting a microfinance intervention with tenure of over 3 years is that such MFI is likely to have clients who have been in the program for a long time and can provide a richer experience about products or features that affect the expansion of capabilities. Such an MFI is also likely to have over 4[41] loan cycles such that the implementation practices would have assumed regular patterns. These patterns can then be studied as regards their potential for capability expansion. Having selected Edo State, all formal microfinance institutions in the state were subjected to the above criteria. Employing these criteria, Lift above Poverty Organisation (LAPO) MfB was identified as the case study for this thesis. Although LAPO MfB operates in 26 out of the 36 states in Nigeria, it only gained the license to operate in multiple states in 2012.

[41] As mentioned in the previous chapter, each cycle is a period of 8 months or 32 weeks.

Hence, as at the time the exercise was conducted in 2013, we could only guarantee its intervention spanning over 3 years in Edo State. This further verified the selection of Edo State as the study area.

5.4.1.1 Edo State: Economic, Financial and Socio-Cultural profile of the study area

Edo State is located in Southern Nigeria, with Benin City as the state capital. It is surrounded by Kogi State in the north, Delta State in the south, Ondo State in the west, and Delta and Kogi States in the east. The people of Edo State come from various ethnic groups, including Bini, Esan, Afemai, Okpamheri, Okpe, Akoko-Edo, Ora, and Igbanke. The results of the 2006 census put the state's population estimate at 3,233,366 (NPC, 2009**).** The backbone of the state's economy is agriculture. This includes farming of subsistence and commercial crops such as yams, cassava, oil palm, plantains, corn and vegetables. The state is often tagged a 'civil servant' state occasioned by government dominance of the formal sector, while the informal sector is dominated by trading activities.

Benin City is home to most government agencies who are the main employer of the salary-earning population. Majority of the formal banking institutions are situated in the state capital with only sparse distribution in other areas. It is reported that there are about 20 bank branches per million inhabitants in Edo state (EFInA, 2010). Towards this end, semi-formal and formal financial institutions play a dominant role in providing financial services in the state. This is consistent with national statistics estimates where about 71 percent of Nigerians are said to borrow from family members and relatives (EFInA, 2010). Here, we find that borrowing as well as saving with family members is predominant in the Edo society. These social networks are often responsible for financing life-cycle events such as weddings, funerals activities and assisting relatives in need of help**.** There is also the presence of money lenders whose operations are informal. Although their activities are often shrouded in secrecy, they are frequently used to raise funds for emergencies. We also find that it is a common practice to patronize individual thrift collectors – *olidara* – who provide daily or weekly collections and savings of monies for typically market traders in Edo State. Despite the growing presence of formal MFIs/MfBs, there still appear to be a high demand for informal financial services.

As regards the socio-cultural characteristics of Edo State, there are traditional roles for men and women. Outside government employment, men tend to be involved in farming, carpentry, transportation, electrical and mechanical repairs or sales; and women tend to be petty traders, hairdressers, and dressmakers. It is often not common for women to own land or properties as this is a male dominated society where patriarchy is practiced. However, women's ownership to land or properties depends on marriage and they retain ownership to land as long as they remained married to the household. It is predominantly a patrilineal state with a gerontocracy style of rulership. Although statutory laws allow for women to inherit properties following the death of their husband, in practice this is often overridden by local customary law of succession. As discussed in the previous chapter, across Nigeria and in Edo State, majority of women occupy lower socio-economic status compared to their male counterpart. The above characteristics of the study area underscore the need for MFIs in this community and the relevance of the services they provide to their predominantly female clients.

After selecting the study area and the case-study MFI, the next step is to implement the chosen research and methodological approach discussed earlier. The goal is to ensure that the method of data collection, analysis and interpretation confirms with the theoretical underpinnings set out for the study. While the ability of the researcher to control the data collection process might be perceived as an advantage, the quality of data however, depends on the researcher's capability and knowledge. Additionally, in developing countries fieldwork requires much discretion, endurance and preparation in negotiating complex situations (Leslie & Storey, 2003). In spite much preparation and precision, the field work exercise may get out of order just because daily living in such countries is characterized by uncertainties and lack of order.

With these challenges in mind, the researcher conducted a thorough search for available data that can enable answering the research questions. An initial search through available data showed a dearth of quality data appropriate for answering the research questions. For example, the Nigerian Living Standard Survey conducted by the NBS provides data on people's livelihood drawn from a national sample. However, this dataset does not contain data suitable for understanding the implementation processes of microfinance interventions or service users' perspectives with regard to the effect of microfinance. Given these factors, and bearing in mind the crucial role of the context in this study, it therefore became imperative that the researcher conducts a fieldwork exercise to generate the required data.

5.4.2 Gaining entry into the field – Branch and Group selection

Following several trips to Nigeria and personal appeal to some senior staff members at LAPO, the application for permission to adopt LAPO MFB limited as the case study for this thesis was granted by the Bank's management. The fieldwork began in January 2013 and ended in May 2013. Members of staff at LAPO MfB limited were helpful and instrumental in facilitating access to service users. The researcher was provided with an authorization letter from the management that allowed visitation to any of the bank's branch offices and request for assistance as regards contacting groups and individual clients.

Once the researcher obtained a list of the names of branches in Edo State, 3 out of the 26 branches were randomly selected. This was done by the researcher without any influence from LAPO. The groups and individual clients who engaged in the research process were also selected by the researcher, independent of LAPO. While the number of branches selected was influenced by resource constraints, the choice of specific branches was purposive to capture both urban (James Watt) and semi-urban (Oka, Evbotubu) areas. James Watt branch is located in a commercially active area with less than 10 minutes' walk to a number of commercial banks, telecommunication offices, the popular New Benin and Oba markets, and the city centre which is popularly called Ring-Road. This branch is able to serve the large number of women who are traders in these markets.

Oka branch is located towards the outer area of Benin City, in a bustling semi-urban district. The two closest commercial banks in this area are 10 minutes' drive away. Oka branch is surrounded by four popular markets: Ugbekun, Umelu, Abico and Oka markets, respectively, and several trading shops and stalls. Each of these trading points is at least 3 to 20 minutes' walk away from the LAPO branch office. This branch is able to serve the densely populated women traders in these markets. Evbuotubu branch is located in a semi-urban district of the city (Evbuotubu quarters), and it is approximately 25 minutes' drive to the busy city centre. The area is a fast-growing commercial active centre of the expanding capital city. This branch is able to serve traders in Evbuotubu market, who are predominantly women, and several shop owners and stalls located within a close radius of 3 kilometres. Even so, there are marked presence of commercial bank activities in the area but the closest of such is about 30 minutes' walk away from the market. Although few LAPO groups are present in rural areas in Edo State, the absence of a branch network to coordinate the group activities made it difficult to conduct any data collection exercise in these areas.

As mentioned in the previous chapter, the service users studied entail microfinance clients who are been served (i.e. credit, savings, insurance and non-financial services) through group lending. It was therefore considered best that the initial sampling of clients begin at the group level. From the selected branches, 5 randomly and 2 purposely selected lending groups were sampled. This includes 3 from the urban area and 2 from each of the semi-urban areas, making a total of 7 lending groups. The purposely selected groups include a group that consists of male clients only and a new group that had only been formed in less than 8 months as at the time of conducting the interview. In all, the sample includes 4 small groups with less than 20 members and 3 large groups with 30 members and above (see table 5.2 below). 4 out of the 7 groups were formed before 2008 and hence are more than five years old. Apart from the 2 new groups, initial discussions with the CSOs suggest that the older groups have all experienced exit and entry of clients since their formation. This is expected to provide a rich pool of clients with wide experience.

Table 5.2: Sample Groups - formation and membership

	Location	Membership Size	Gender Distribution		Formation Year
			Female	Male	
Group1	James Watt	18	0	18	2007
Group2	James Watt	46	35	11	2007
Group3	James Watt	10	10	0	2008
Group4	Oka	31	24	8	2004
Group5	Oka	11	11	0	2012
Group6	Evbotubu	30	30	0	2003
Group7	Evbotubu	13	8	5	2012

Source: Authors computation from primary data

For the initial contact with service users, the researcher accompanied the CSOs to weekly group meetings. During each of these meetings, the CSO introduced the researcher to the group and informed them that approval had been obtained for the exercise. The researcher is introduced as a student who knows much about the community and is undertaking the research as partial requirement for a university degree. This helped to establish the authority and credibility of the researcher. With this, the researcher then went on to inform group members of the purpose of the exercise, what is required of those who agree to participate, the ethical issues that guide the exercise. The purpose of this is to build some form of relationship with the groups and to establish a bond of trust with service users. This strategy satisfies the suggestion by Lofland and Lofland (1984) that researchers demonstrate sufficient knowledge of the community and respondents as a sign of competence to undertake the intended study. At this stage, the research information sheet and consent forms are given to the service users to indicate their interest to participate in the study. Obtaining clients' consent is one of the ethical considerations involved in social science research. The next section discusses the wider ethical considerations that apply to this research and what attempts are made by the researcher to ensure that ethical practice is maintained.

5.4.3 ETHICAL CONSIDERATIONS

Ethical considerations are important concerns in social research, particularly when it involves fieldwork. This is so because it entails an intrusion into the private lives of respondents as they are required to disclose confidential information that is capable of exposing them to certain risks. Particularly, investigating this confidential information and placing it in the public domain raises ethical issues. In this study, the researcher recognizes the potential risk respondents may face. Respondents who disclose distressing experiences with LAPO or those who contrary to the regulations of the intervention may have spent all or part of their loans on consumption could be punished by LAPO. With this potential risk to respondents, it is imperative that the researcher observes ethical practice.

In complying with ethical practice, the researcher provides prospective respondents with an invitation to participate. This invitation package documents the purpose of the research; ethical considerations, the consent form, and the researchers contact details. This basically provides details of the research, their rights as participants as well as the obligations of the researcher. Respondents are informed of the potential benefits as well as the risks they face if they choose to participate. The choice to participate is completely voluntary, devoid of any form of inducement or threat. Obtaining informed consent is seen as a continuous process throughout the fieldwork exercise and not just a single event. However, given the literacy levels of the respondents, it became obvious that verbal orientation and approval was the appropriate method of obtaining informed consent. Respondents were continuously informed of their rights to withdraw from the study at any time and to refrain from answering any question they are not comfortable with. The anonymity of respondents is also preserved in this study using pseudonyms that cannot be traced to the actual names, location and group of respondents. Ethical practice also requires that the researcher takes responsibility to ensure own safety in conducting the research (Oliver, 1997). Having obtained informed consent and scheduling convenient data collection times with respondents, data collection constitutes the next objective. Beginning with the interviews and then the questionnaires, the process and instruments for data collection are discussed next.

5.4.4 INTERVIEWS

Interviews are valuable ways of eliciting expressed lived experiences and gaining an insight into the perspective of the interviewee with regard to a particular subject (Kvale, 1996). This data collection tool is significant for achieving two of the objectives in this study which include:

- To identify the capabilities that microfinance clients value and have reason to value, and
- To evaluate the implementation processes and different components of microfinance interventions and their effects from the viewpoint of service users.

Qualitative interviews are employed in this study as a generative technique, appropriate for eliciting expressed lived experiences of microfinance service users. This entails a conversation between the interviewer and the interviewee, where the former asks questions to elicit statements and facts from the latter. This method of data collection has its roots in the IA, PPA and CA approaches, all of which 'give some privilege to the account of social actors, agents, individuals, or subjects, such as data sources, and which assume or emphasize the centrality of talk and text in our ways of knowing about the social world (Mason, 2002:225)'. At this point it is important to reiterate that the need to examine clients experience and to hear from the clients themselves is drawn from propositions in the literature that, it is not enough to evaluate microfinance with the mere conclusion that it has a positive or negative impact on the poor. This body of work as discussed in chapter 3 has led to an increasing call for studies that look beyond impact to evaluate the features and characteristics of microfinance delivery and use that have the potential for poverty reduction from the clients' perspective.

Specifically, semi-structured interviews are employed in this study. This involves an open but yet focused set of questions allowing room for the interviewer to ask additional questions and probe for details and new ideas based on the response to previous questions. This interview format is appropriate when the researcher desires in-depth knowledge of the social phenomena, while maintaining some level of control over the interview process. The researcher deliberately begins with as few questions as possible and then used active follow-up questions, prompts and probes to elicit more information and to probe that her understanding of the responses is what the interviewee intended to convey.

Selection of respondents was done purposively. This entails the selection of respondents in a non-random and deliberate fashion. It usually involves preferentially recruiting respondents from one or more predefined groups who are more knowledgeable and experienced in the area of interest. This allows for the purposive sampling of information rich-cases related to the subject under study, thus increasing the strength of the in-depth analysis. In choosing the criteria for selecting respondents, the researcher assumes that the following category of clients will provide a rich pool of information as regards clients experience with microfinance.

1. group leaders (7)
2. clients who have been in the intervention for a long period of time (5)
3. new clients (7)
4. clients who who have been able to maintain prompt repayment (referred to as successful users in this study) (7)
5. clients who have encountered repayment problems by not meeting at least one repayment schedule (referred to as struggling borrowers in this study) (7)
6. clients who had previously dropped out of the intervention and rejoined (2)

This mixture of respondents is expected to shed more light on what factors account for the difference in client experience. As regards group leaders, group meetings are usually held in their homes and they are also responsible for collecting repayments. Hence, they are expected to possess personal as well as group information on the experience of their members with microfinance and what implementation processes, microfinance features as well as borrower practices are more likely to cause harm or good. The range of experience between long-term participating clients with over 5 years in the intervention and new clients is also expected to provide a rich body of knowledge as regards clients experience with the implementation processes and features of microfinance. Although during the initial contact, service users were open to let the researcher know how long they had been in the intervention and what their experience has been with repayments, the leaders were also asked to identify struggling and successful members. Interviewing successful and struggling members is expected to shed more light on what implementation processes/ features of microfinance as well as borrower characteristics or practices account for the difference[42].

An attempt was also made to include the experience of previous clients who have left the intervention. This refers to clients who exit their lending groups and drop out of the intervention by closing their savings and loan accounts with no intention of coming back[43]. However, after consultation with LAPO staff, it became clear that there was often tension in interacting with exited clients as regards recounting their experience with LAPO. To this effect, LAPO staffs as well as the group members were not willing to point the researcher to exited clients. Nevertheless, the researcher was made aware of a forthcoming clients' unmet service needs survey which was been conducted by LAPO in 2013. In order to capture the view of exited clients, this study draws from the finding of that report which covers 42 exited clients spread across 21 branches. In conducting the interviews, the respondent also finds two respondents who had previously exited the intervention. It is however important to cautiously mention that there was the tendency of the researcher to select from the extremes as regards meeting the criteria. For instance, selecting the same-gender groups or interviewing the longest participating service user in a group etc. The researcher also had informal conversations and observed the practices of the CSOs who are directly involved with engaging the clients. LAPO staffs were also consulted when the researcher faced any challenge or any issue requiring clarification.

5.4.5 CONSTRUCTION OF THE INTERVIEW GUIDE

Recall that the required qualitative data is expected to provide information on service users' evaluation of the implementation processes and features of microfinance as well as the capabilities that they value and have reason to value. Thus, the interview guide (see Appendix B) employed in this study is designed to generate the relevant information. The implementation processes explored in this study include the ease of access to microfinance, the service delivery, group lending and women targeting. Questions were designed to gather information on service users experience with

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[42] It is important to note that the term 'struggling' and 'successful' clients is consistent with the terminology used in the groups. Discussion with group members and leaders pointed to the fact that clients were categorized based on their experience with repayments.

[43] This does not include clients who temporary exit the intervention due to personal or family related factors.

microfinance; how they came in contact with the service provided, their assessment of the service delivery, if they feel it has benefited them and to what extent, what implementation processes or features of microfinance has benefitted them the most, why and for what purposes. Specifically, the interview guide raises questions about service users experience with loans, interest rates, savings and non-financial services as features of microfinance. The goal is to identify which aspects of these features of microfinance and their implementation processes have the potential for good or harm from the clients' perspective. Initial discussion with the CSOs responsible for the groups sampled, revealed that no member of the selected groups had made a claim on their insurance. Based on this finding, insurance was excluded from the list of microfinance features to be examined. The argument for this is that even though all LAPO clients pay for insurance, service users who have not made a claim or actually benefitted from this service cannot give a true assessment of this service as regards its potential for good or harm or its potential for poverty reduction.

Aware of the significance of understanding the variation in clients experience across various socio-demographic characteristics, the interview guide also collects information on service users' demographics. Additionally, we also expect that clients experience with microfinance might also differ with their socio-economic status. We hypothesize that clients with higher socio-economic status are more likely to use loans for business purposes as against poorer clients who might have more contending uses for loans. For example, compared to poorer clients, less poor clients are less likely to spend loans on children's fees because household finances will accommodate for such expenses. Hence, the interview guide also collects information on occupation, spouse occupation, household financial situation – in terms of main source of income and other sources (if any), what other coping mechanisms or options would they have fallen back on in the absence of access to this service; and finally, their wider experiences with accessing and using financial services. In mostly patriarchal communities such as the study area, beyond the clients' occupation, their socio-economic status is largely linked to that of the household. This in turn, particularly for predominantly female microfinance clients is mainly determined by the husband's income (that is if there is a spouse). This therefore makes spouse occupation a robust variable for determining clients' socio-economic status. These socio-demographic characteristics are also employed as control variables in the quantitative analysis.

5.4.5.1 Operationalizing the Capabilities Approach

The final section of the interview includes questions designed to capture and understand what constitutes poverty from the perspective of LAPO clients. As discussed in chapter 2, there is yet no universally accepted list of relevant capability dimensions; and so is the process by which they should be decided. Even though Sen considers a basic set of capabilities as discussed in chapter 2, he places emphasis on identifying and prioritizing freedoms in the domains that people value and have reason to value. And more importantly, that these value judgements should be determined by the subjects of interest and not externally imposed. Hence, he does not consider his list of basic capabilities to be universal. As shown in chapter 2, in reviewing the more prominent capability sets in the poverty literature, Alkire (2008a) identifies five methods for selecting capability dimensions. These methods include existing data, normative assumption, public consensus, deliberative participatory processes, and empirical evidence. As discussed in chapter 2, these methods have been used either singularly or in a combination of 2 or more methods to define widely recognised capability sets. As Alkire notes, the validity of the selected capabilities is likely to be improved when a combination of two or more selection techniques are applied, and when the process of selection is clearly made known. This is the approach adopted in this study.

Most importantly, in selecting appropriate dimensions, the primary concern is 'the freedoms that microfinance clients value and have reason to value'. With the absence of appropriate existing data for LAPO clients, capabilities are selected in this study using a combination of public consensus, deliberative processes and normative assumptions. Clients are specifically asked the following questions: in your opinion what is poverty? What are the characteristics of a poor person? To you as a LAPO client, what is it that if you cannot do, will make you consider yourself to be poor? This is employed as a participatory process for soliciting the dimensions of poverty that microfinance clients' value, whilst ensuring that the value judgements are made by clients themselves. Clients' responses (see the next chapter) are analysed to identify recurring themes and arrive at a possible consensus of those capabilities that clients' value. Beyond the capabilities that clients' value, the researcher makes a normative assumption that clients have reason to value the increased ability to achieve successful business outcomes.

As Alkire (2008a) notes, these assumptions may be drawn from the researchers' own views, theoretical propositions, psychological views, or popular conventions within the literature. In this study, the assumption that clients have reason to value the increased ability to achieve successful business outcomes, is made bearing in mind the characteristics of microfinance clients as well as the potential and associated cost of microfinance. First, as mentioned in the previous chapter, microfinance clients are self-employed individuals who rely on micro enterprises as their main source of income. Although monetary resource in the capability literature is not considered to be an end in itself, it is yet seen as a means to an end. Particularly in the Nigerian society where there is no social welfare system and there is a dearth of basic amenities and social infrastructure, the ability to achieve capabilities[44] is largely linked to the ability of individuals to earn sufficient income enough to finance the achievement of capabilities. For example, take one of the capability dimensions selected by Nussbaum (2000), 'health' – including good health, adequate nutrition and shelter, income plays an important role in the achievement of these capabilities. Previous uses of capabilities such as work (Naryan et al, 1999), employment (Alkire and Foster, 2007), and non-farm self-employment (World Bank LSMS, 2000), support the importance of the increased ability to achieve successful business outcomes.

Additionally, given the cost of borrowing, it is assumed that service users are only better off if they are able to ensure sufficient returns on their businesses to cover the associated liabilities that arise from microloans. It is important to mention that when put together, this cost might be quite significant as it includes the interest on loans, weekly compulsory savings[45], cost of insurance, as well as the potential cost of default by other group members. Although we recognise the increasing use of loans for consumption purposes, and that this might have a positive effect on household and other welfare related capability dimensions, it nevertheless comes at a cost to repayment possibilities as well as the return on loans. Yet, even for those who engage in non-business use of loans, the ability to own a business that generate enough returns

[44] We recognise that there are certain capabilities, particularly 'social capabilities' that are not necessarily linked to income but rely on the capabilities of a group of people. Nevertheless, we argue that the ability of an individual to individually achieve capabilities is rather superior. Take microfinance clients for instance, the only reason why they need to rely on the 'social capabilities' that arise from group lending in order to access microfinance is because they are not able to do so on their own.

[45] Although this might not apply to all microfinance interventions, it does apply to LAPO. Even though savings are made available after the loan cycle, service users still have to generate enough income to meet the weekly savings.

to meet repayments ameliorates this risk. This emphasizes the need for clients to value the increased ability to achieve successful business outcomes.

With an understanding that the most regular LAPO loans are issued for investment in a microenterprise, we argue that microfinance clients have reasons to value the increased ability to generate profitable returns in their investment. Nevertheless, in order to avoid limiting capabilities to monetary resources, this study focuses on the ability of clients to achieve profitability. Drawing from economic theory, one way to achieve this is through economies of scale. Particularly, when we consider scale factors, this can be achieved by increased business size, increasing products, developing new business and increase in business asset. Profitability can also be enhanced through reduction in cost which can result from the increase in scale. Increased capability at the business level is also required because of its instrumental importance for realizing other poverty reduction goals. Hence, this study assesses the ability of microfinance to increase the ability of microfinance clients to increase business size, introduce new products, reduce cost, develop new business, and increase business asset. This explicit and transparent description of the assumptions and claims behind the use of these capability dimensions is expected to add tremendous value to the selection process, enable critical review of the underlying assumptions, and allow for criticisms and suggestions for improvement. It is important to mention that the selected business outcomes are not exhaustive and represent a limitation in the study.

5.4.6 ADMINISTERING THE INTERVIEWS

In all, semi-structured interviews were conducted with 35 service users. Based on the preference of service users, interviews were held in the evenings at the homes of service users when they had returned from the business activities of the day and were less busy. The idea was to allow respondents select a familiar environment or natural setting where they will be comfortable enough to provide honest responses. On the average, interviews lasted for about 45 minutes during which the researcher assumed nothing; but probed with follow-up questions to understand and unearth emerging issues. This was the estimated time for conducting the interviews and does not suggest that only little discussion was undertaken. As mentioned, the interviews are semi-structured which meant that the researcher did not have to go from one question to the next. The priority was to make sure that all the questions were answered. For instance, in asking a respondent ‘how did you come to know LAPO’, they are most times likely to provide an answer that covers other issues like ‘if they contacted or were contacted by LAPO', 'why they decided to do so at the time', 'what was required of them to access the service', 'how this was provided' etc. The approach from the researcher was therefore to probe to confirm her understanding of what experiences had been shared and to point them towards those questions that had not been answered. Given the literacy levels of respondents, it was considered appropriate for the researcher to administer the interviews as well as the questionnaires. Questions were translated to 'pidgin' English[46] and read out to respondents, thus enabling higher response rates. The researcher was vigilant for conflicting responses and ensured that before leaving the selected communities, questionnaires were reviewed to check for unanswered questions, mistakes or inconsistencies.

All interviews were recorded using an audio recorder and transcribed afterwards using pseudonyms to preserve the anonymity of respondents. During the 6 months data collection period, the researcher worked with staff members at LAPO MfB, interacting with them to gain an insight into their relationship with service users and the implementation processes of the intervention. The data employed in this analysis includes information gathered from interviews with service users, discussions with staff members LAPO MfB at and other sister organizations in the LAPO group, and participant observation. But for time constraint, service users were generally enthusiastic about participating in the interview. The researcher had to explain that she was working with a time schedule and could not interview everyone indefinitely, but assured the respondents that the questionnaires will cover more respondents.

5.4.7 QUANTITATIVE DATA COLLECTION

In conducting research, it would be ideal to study the whole population but due to resource constraints, oftentimes only a small portion of the population can be studied. This selected part of the population is called a 'sample' and is often studied with the intention of drawing knowledge about the population. It is important to ensure that the sample is representative of the population as it allows the findings to be generalisable to the population. Statistical sampling ensures that all elements of the population have known or equal probability of being selected[47] (Abrami et al, 2001). Common statistical sampling techniques include simple random, proportional, multi-stage, and

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[46] The Edo language is the native language of the study area. Although all respondents understand pidgin English which is used across the country, the ability to interact with the respondents in their language before the interview session began made them more comfortable and open.

[47] Sampling without replacement does not give sampling units an equal chance of being included in the sample. However, the problem is negligible when sampling from a very large population.

cluster sampling. One underlying factor with these sampling techniques is the practice of random sampling. Hence in this study, random sampling is used at different stages of the sampling process.

Besides the purpose of the investigation and the size of the population, the sample size depends on three other factors: the margin of error; the confidence level; and the level of variability within the population of interest (Yeboah, 2007). Common confidence levels used in social science research are .05 or .01. For categorical data[48], Bartlett et al. (2001), argues that the 5 percent margin of error is acceptable. In estimating the sample size, Israel (2009) suggests the formula below

$$\boldsymbol{n = \frac{N}{[1 + N(e)^2]}}$$

where

N = population

n = the sample size

e = alpha level

At LAPO, the population of clients in Edo State was considered to be classified information and not made available to the researcher. However, the total number of clients as at 31 Dec 2012 totalled 861, 078. Given that LAPO operates in 26 states, this would give an average of approximately 33,118 clients per state. Using the above formula, the sample size is estimated as follows

$$\boldsymbol{n = \frac{33118}{[1 + 33118(.05)^2]} \cong 400}$$

However, due to time and resource constraints, it becomes obvious that the researcher is unable to cover this sample size. Hence, the sample size was set at 80 respondents. Yet, due to difficulties faced during the fieldwork exercise in terms of availability of respondents, the quantitative data analysed in this study is drawn from only 62 service users. As with the interviews, the questionnaires are administered in the evenings at the service users' home. This meant that on days when the service user had a bad day, a long business day or faced traffic getting back home, data collection had to be shifted to a more convenient time. It was also not possible to gather the data early on because the service users were concerned with making their daily bread and interrupting that would be at a cost to service users. Also, the business places for most of the service users were not conducive for collecting the required data. This sample size is a major

[48] This study uses categorical data as is discussed in section 5.

limitation of this study. Nevertheless, the sampling literature proposes 30 observations as the minimum sample size for any significant statistical analysis (Tabacnick, and Fidell, 2001). With this, the researcher is still able to conduct significant statistical analysis

5.4.8 QUESTIONNAIRE CONSTRUCTION AND ADMINISTRATION

The questionnaire (see appendix C) is designed to generate quantitative data relevant for capturing service users' evaluation of the capability expansion potential of microfinance as well as the relationship between clients' microfinance practices and capability expansion. Though the construction of the questionnaire began before the fieldwork exercise, it was completed in the field as findings from the qualitative data informed the construction of the questionnaire. This way, the quantitative data can reflect contextual factors which quantitative data collection methods are often criticized of ignoring. In total, it consists of 3 main sections. The first 8 questions collect information on clients' socio-demographics. These variables were important for exploring variations in the data and are statistically controlled for in order to hold constant their effect when assessing the relationship between clients' microfinance practices and capability expansion. The next 11 questions collect information on clients group and loan practices. The final section consists of 2 sets of five questions each, 10 in total, capturing the extent to which the use of microfinance has enabled an increase in capabilities at the household and business levels. As mentioned earlier, the 5 indicators of increased ability to achieve successful business outcomes represents freedoms that microfinance clients have reason to value, and the 5 household capabilities which are selected in the next chapter represents freedoms that microfinance clients' value.

As with the qualitative interviews, the questionnaire was administered by the researcher and data collection was done at the respondents' home. The questions were translated to 'pidgin English' and read out to respondents. This enabled higher responses as it allowed questions to be explained to respondents. This method of administering the questionnaire has been argued to be a good way of collecting information quickly (Bell, 1999). The researcher was vigilant for conflicting responses and ensured that before leaving the selected communities, questionnaires were reviewed to check for unanswered questions, mistakes or inconsistencies. Secondary data collected from the CBN, NBS, previous studies, newspapers, online resources and brochures from LAPO MfB were obtained to complement primary data. This data is important to supplement or triangulate the researcher‘s own data. Informal conversations with LAPO staff and participant observation were also important sources of information. They provided valuable insights into service users' perception of the microfinance interventions. It is often alleged that insider research lacks the objectivity necessary for credible investigation because of the researcher‘s emotional investment in the context (Anderson and Herr, 1999; Alvesson, 2003). Bearing this in mind and having lived outside the community for a long time, the researcher made conscious effort to conduct the observation from an outsider's perspective. On the balance, however, the advantages that accrued to the researcher for being an insider outweighed that of being an outsider, especially considering that the issue of context was pivotal to the study.

5.5 DATA ANALYSIS

Data analysis actually begins with the preparation of the data for analysis. For the qualitative data, this includes the translation and transcription of the data. With the quantitative data this includes entering the data into a statistical analysis tool. In this study, the data was first entered into an Excel spreadsheet. This was then followed by the coding and categorization of open-ended questions. Variable categorisations found to be unsuitable for analysis due to no or very few cases were carefully combined and re-categorised to make them suitable. For example, 'marital status‘, as a four-category variable, (single, married, divorced, widow/widower) was combined into two categories (married and single) for better analysis. Also, 'number of children', as a six-category variable (0, 1-2 … 7-8, more than 8) was combined into three categories (0, 1 - 4 and 5 and above). This re-categorisation was mainly to achieve more than 5 observations in each category. After cleaning the data and double-checking to confirm that the correct data has been entered, the data analysis commenced; beginning with the qualitative and then the quantitative.

5.5.1 QUALITATIVE DATA ANALYSIS:

The process of qualitative data analysis can be grouped into seven stages: organizing the data, engaging with the data, generating themes and categories, data coding, interpretation of data through analytic memos, developing alternative understanding, and report writing (Marshall and Rossman, 2006). It involves making meaning of the subject matter and is inherently intertwined in the research design, data collection and interpretation. In other words, data analysis is essentially done throughout the research process, consciously or unconsciously. Through a systematic reading and coding of the data, recurrent themes linked to the research questions are identified. In doing this, an iterative and inductive research process is adopted; as the research themes are defined and refined based on the emerging data. The qualitative data was transcribed and analysed using a qualitative data analysis software called Nvivo. This software program was used to code and organise the data generated from the interviews. It is important to note that coding of themes was not done automatically by the software. This is done by the researcher, including identifying recurring themes, analysis existing links, and finally interpreting what the findings means as regards achieving the research objective.

First, clients' responses are analysed to identify what implementation processes or features of microfinance have benefitted them the most, why and for what purposes, and which of these have the potential for good or harm. In exploring the variations in clients' responses, Secondly, to follow through with the need to identify what clients' value, the qualitative analysis concludes with an explicit analysis of service users responses to the questions: 'In your opinion what is poverty? What are the characteristics of a poor person? To you as a LAPO client, what is it that if you cannot do, will make you consider yourself to be poor? This allowed the researcher to identify the recurring capability themes as described in the next chapters. Overall, in discussing the results, the researcher moves across the data and the existing literature to create links and situate the research findings within the wider literature. In reporting the findings, direct quotes from respondents are used to support the credibility of the discussion and conclusion.

5.5.2 QUANTITATIVE DATA ANALYSIS

This comprises of the construction of the model specification and the empirical analysis. These two components are discussed below.

Model Specification

5.5.2.1 Measures of Poverty Reduction and their Aggregation

The dependent variables employed in the analysis to be reported here concerns poverty reduction measured as increased capabilities at the business and household level. In addition to the five business level capabilities selected earlier, drawing from the qualitative findings, five other capabilities that clients value are selected at the household level. At the business level, poverty reduction was captured in terms of proven ability to increase business size, business asset, reduce cost, develop new business, and introduce new product. At the household level, poverty reduction was captured in terms of proven ability to increase contribution to household finances, emergencies, savings, assets and child education. In all, 10 dependent variables were constructed to capture increased capabilities that clients' value and have reason to value.

For each of these variables, respondents were asked how much they have been able to increase their capabilities since joining the intervention. Responses ranged from 0 to 2, where 0 was identified as 'not at all', 1 was 'somewhat', and 2 was 'very much'. These scales are interpreted as 'no increase', some increase', and 'significant increase' in capability respectively. This method of data collection has been widely used in social science research but; there remains a wide debate surrounding whether to use an odd or even scale, the optimum number of options on the scale, as well as the validity and general reliability. Odd numbered scales are largely supported for their ability to provide a neutral point, ensuring that respondents do not fabricate opinions instantaneously. However, supporters of even numbered scales claim that in reality individuals always have an opinion and are never neutral on issues. Additionally, they argue that there is a risk in providing a mid-point 'non-committal' option to respondents, as this leads to uninformative data arising from respondents opting out. One shortcoming with the even numbered scales is that in forcing response by excluding the 'neutral' option, there is the tendency for positively skewed result as the validity of the data can be compromised due to social desirability i.e. people more likely desire to be seen in a positive light. In order to avoid this bias, respondents were informed about the anonymity of the research data and also encouraged to provide honest responses as a copy of the results will be sent to LAPO MFI. They were informed that honest responses will thus provide LAPO with additional information to meet their needs.

One way to decide the number of scale points is to determine whether the subject of interest is bipolar or unipolar. The former refers to a situation where responses can fall on one side of a midpoint (neutral) or the other. For example, an HR administrator might want to know if the work day is too short, just fine, or too long. Here, length is a bipolar construct. The latter refers to a situation where the constructs lend themselves purely to an amount–here; there is either the maximum amount or none of it. For instance, in asking service users' about capability increases arising from the use of microfinance, we expect responses to fall between: 'extreme' or 'very much' increase and ‘no increase at all’. We can safely assume a midpoint like ‘somewhat’ increase. This three point response scale can be expanded to a four-point scale by adding a response option ‘very little’ between the midpoint and the lower anchor. However, given the context, it is considered best to apply the former as the latter might make it more complex for the respondents to wrap their minds around. For instance, it might be difficult to distinguish ‘very little’ from ‘somewhat’. Although five and seven point scales are widely used, the ultimate conversion of these scales to a three point scale for analysis and report writing supports its use in this study.

As regards the reliability of the data, Cohen (1983) concludes that for effective analysis, a three point scale is necessary at a minimum and a nine point scale at a maximum. Additionally, Chang’s (1994) argues that in terms of reliability, the knowledge of the subject and the uniformity of respondents’ understanding of the different options play a significant role. From a review of previous research, he also argues that as the number of response options increases, the likelihood of error increases as respondents’ understanding of the different options are likely to differ. Given the interviewer-administered approach to data collection adopted in this study, the researcher was able to clearly define the meaning of each scale point to the respondents to achieve uniformity and thus, greater reliability. With this, each individual capability indicator represents a categorical ordered variable capturing the capability expansion potential of microfinance from the clients’ perspective.

Going further, a composite indicator was constructed for each poverty dimension (i.e. household and business) using the 5 relevant dependent variables. For example, the composite indicator of increased ability to achieve successful business outcomes is constructed by adding up the coded responses to each of the five business outcomes and then carefully assigning them into the three corresponding poverty reduction scales. For 5 variables with coded responses ranging from 0 to 2, the values ranged from 0 to 10. Values from 0-3, 4-6 and 7-10 were assigned into the ‘not at all’, ‘somewhat’ and ‘very much’ poverty reduction status respectively. However, after adding up the responses for each dimension, at the household level, all respondents had composite values greater than or equal to 4. Similar results were found at the business level where 61 out of 62 respondents had composite values greater than or equal to 4. First, this means that all service users had experienced at least ‘somewhat’ reduction in poverty as a result of joining the intervention. Second, it means that the composite variables had to be categorised as binary variables with ‘0’ and ‘1’ representing ‘somewhat’ and ‘very much’ poverty reduction.

Yet, this approach applies equal weights to the different indicators included in the composite variables for each dimension. This is not always the case as certain indicators may be more dominant in capturing the variations in the model than others. Hence, we construct composite indicators that account for these differences. An additional pair of composite indicators was constructed using a principal component analysis (PCA). As mentioned in chapter 2, this is a data reduction technique used to convert a multivariate data into fewer dimensions. It helps to identify if all of the variables should be used or if there are any redundant variables, so that we can express all of the variables using fewer components or factors that capture the maximum possible information or the variation in the original data (Jolliffe, 2005). At the business level, the PCA retains two components explaining about 73 percent of the variation in the data. At the household level, 2 components are retained explaining about 76 percent of the variations[49]. The retained components are then used to construct the composite index. With this, each respondent now has two pairs of composite indicators and 10 individual capability indicators that measure increased capabilities at the business and household levels.

5.5.2.2 Measures of Predictors

With the objective of answering the question: what borrower related microfinance practices are better associated with higher expansion of capabilities for the poor, the predictors are centred on clients’ group and loan practices.

Group Practices

Clients’ group practices are measured using a three-item measure. First, Clients practice of peer monitoring is measured by the extent to which they stay informed about ‘know use’ and influence the use of loan by their peers (ranging from ‘no’ recoded as ‘0’ to ‘yes’ recoded as ‘1’). As shown in figure 3.1 and as argued in the microfinance literature, service users have an incentive to perform peer monitoring and enforcement duties in order to reduce the risk of potential loan defaults. This is because by engaging in these practices, service users can monitor loan use, verify the project returns of their peers, mitigate any extra cost arising from joint liability, thus creating a positive effect on poverty reduction and service user overall experience (Simtowe and

[49] See appendix D for summary of the PCA construction

Zeller, 2006; Aghion, 1999; and Stiglitz, 1990). Secondly, findings from the interviews suggest that although the threat of social action upon loan default is evident in all groups, a large portion of service users are passive as to the actual use of peer pressure or social sanctions in enforcing repayments. Clients' practice of repayment enforcement is measured by the extent to which clients engage with defaulting clients with the intent to achieve repayment (ranging from 'voluntary' as 0, 'moral suasion' as 1 and 'peer pressure' as 2). Voluntary refers to a situation where service users leave defaulting clients to of their own volition make repayments. Moral suasion refers to a situation where service users carry out some form of action to encourage and persuade defaulting clients to make payments. With peer pressure[50], service users employ more forceful measures to demand for repayment such as visiting the defaulting members' houses and/or harassing them, t etc.

Loan Practices

Clients experience with loan use is measured using a five-item measure. This includes loan size (ranging from loan amounts between N30000 and N80000 recoded as 0 to loan amounts greater than N80000 recoded as 1), the use of loans for non-business purposes (ranging from yes recoded as 0 to no recoded as 1), use of loans outside LAPO (ranging from yes recoded as 0 to no recoded as 1), separating business money from household finances (ranging from no recoded as 0 to yes recoded as 1), and difficulty making repayments (ranging from yes recoded as 0 to no recoded as 1).

The model can therefore be specified as

$$\begin{aligned}
&\boldsymbol{Poverty\ reduction^{*}} \\
&\qquad = \boldsymbol{\alpha} + \boldsymbol{\beta_1 age} + \boldsymbol{\beta_2 gender} + \boldsymbol{\beta_3 education} \\
&\qquad + \boldsymbol{\beta_4 number\ of\ children} + \boldsymbol{\beta_5 occupation} \\
&\qquad + \boldsymbol{\beta_6 spouse\ occupation} + \boldsymbol{\beta_7 loan\ cycle} \\
&\qquad + \boldsymbol{\beta_8 repayment\ enforcement} + \boldsymbol{\beta_9 know\ use} \\
&\qquad + \boldsymbol{\beta_{10} influence\ use} + \boldsymbol{\beta_{12} loan\ amount} + \boldsymbol{\beta_{13} other\ use} \\
&\qquad + \boldsymbol{\beta_{14} loan\ outside\ LAPO} + \boldsymbol{\beta_{15} separate\ business\ money} \\
&\qquad + \boldsymbol{\beta_{16} difficulty\ repaying} + \boldsymbol{\mu}
\end{aligned}$$

With the small sample size, the inclusion of too many predictors is likely to overcrowd the model. Hence, two separate models estimating the relationship between poverty reduction and group practices and loan practices are constructed. However, as mentioned earlier, client characteristics are important for exploring variations in the data; and are statistically controlled for in order to hold constant their effect when assessing the

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[50] Although the interviews show that the use of savings for repayment is a regular practice in enforcing repayment, this is usually undertaken by the group as a whole with or without the cooperation of the MFI (i.e. depending on what type of saving is involved). Hence, it is not considered to be an individual practice of enforcing repayment.

relationship between clients' microfinance practices and capability expansion. Hence, an initial regression is conducted to estimate the relationship between clients' characteristics (age, gender, education, number of children, occupation, spouse occupation, and loan cycle) and poverty reduction. Client characteristics found to be statistically significantly related with poverty reduction are included as control variables in these models. Table 5.3 below presents a summary of the predictor variables as well as their categorisation.

Table 5.2: Description of Socio-Demographic, Loan and Group Practice Variable

Variables	**Categories**
Age	< 30 31-50 >50
Gender	female male
Marital status	single married
Number of children	1-3 >3
Educational level	< secondary > secondary
Occupation	trader service providers
Spouse occupation	farmer traders Service providers Skilled workers
Years in LAPO	1-5 6-10
Loan cycle	1-6 7-12
Loan amount	< 80000 80000 and more
Non-business use of loan	Yes No
Borrowing outside LAPO	Yes No
Separate business money	No Yes
Repayment difficulty	Yes No
Repayment enforcement	Voluntary Moral suasion Peer pressure
Know use	No Yes
Influence Use	No Yes

Source: Fieldwork Data, 2013

5.5.2.3 Empirical Analysis Techniques

The empirical analysis conducted in this study is divided into 2 sections with each addressing one of the 2 quantitative objectives in this study. The first is designed to evaluate the effectiveness of microfinance in the expansion of capabilities from the clients, perspective. It begins with a descriptive statistics of the data using frequencies and contingency tables. Beyond presenting the demographic and socio-economic characteristics of clients, frequency tables were employed to analyse clients' expansion of capabilities and to what extent. Contingency tables were used to analyse the relationship between the socio-demographic and explanatory variables on the one hand and the two composite capability indicators: business and household poverty outcomes (see section X for the calculation of the composite dependent variables). The Pearson chi-square test is used in assessing the significance of these, and statistically significant relationships are flagged. Cross-tabulations were valuable because they guided the inclusion of variables in the logit regression.

The second involves the use of logit regression to investigate what borrower-related characteristics and microfinance practices are better associated with higher expansion of capabilities for the poor. As mentioned in chapter 2, the regression approach is one of the widely used statistical techniques for analyzing capability expansion and is employed in this study as a more preferred technique for achieving the research objective. Particularly, the logit and OLS regression models are constructed to predict poverty reduction given the selected explanatory and control variables. Other techniques include: 'scaling and ranking solutions, fuzzy set theory, and the multivariate data reduction techniques' (Chappero-Martinetti and Manuel Roche, 2009: p 171). Scaling techniques are generally more appropriate at the macro level making them unsuitable for the micro level data used in this study. Although fuzzy sets are used for micro-level analysis, they are more appropriate when it is assumed that there is only a partial degree of achievement, such that the cut-off point between an expansion and no expansion of capabilities is quite complex and vague. Given that the questionnaire is designed to collect ordered responses on the extent of capability expansion, with implicit cut-off points, this technique is unsuitable for available data. Multivariate data reduction techniques such as the PCA mentioned earlier are particularly appropriate when dealing with a large list of poverty indicators, as they facilitate the aggregation of variables (Di Tommaso, 2007; Klasen, 2000; Kuklys, 2005; Roche, 2008). Given the 5-piece set capability indicators applied in this study, the PCA is employed in data aggregation.

Methodology - Logit Regression Model

Multivariate regressions models are often plagued with multicollinearity among the explanatory variables. This refers to a statistical condition where the explanatory variables are highly correlated. It has been argued that multicollinear variables contain redundant information making them unnecessary in the same analysis (Tabachnick and Fidell, 2001). In this case, although the coefficients remain unbiased; the standard errors tend to be large resulting in non-significant results (Menard, 2001). In order to cross check for multicollinearity in the data, the researcher constructed a correlation matrix to estimate the correlation among the exploratory variables. In this study, if high correlation (> 0.8) is found among any two variables, the required action will be to drop one variable after cautious consideration of the theoretical implication of such an action.

The next step is to test the null hypothesis that borrower-related practices have no effect on poverty reduction. It is important to mention that the analysis here is conducted using the composite business and household capability indicators as the dependent variables. In assessing the effect of clients' practices on the capability of service users, this study employs logit regressions. This is a binary outcome model where the dependent variable is typically a binary response taking on values of 0 and 1. The logit regression is considered a more accurate and valid estimation technique due to its ability to accommodate the inherent binary nature of the composite dependent variables. These variables measure whether a service user has experienced 'somewhat' or 'very much' expansion in capabilities with each variable expressed as:

$$\boldsymbol{y} = \begin{cases} \mathbf{0}\ \boldsymbol{if\ somewhat} \\ \mathbf{1}\ \boldsymbol{if\ very\ much} \end{cases}$$

The logit regression model estimates the probability that y=1 (very much) as a function of the control and explanatory variables. The advantage of the logit model is that it ensures that the resulting predicted probabilities lie between 0 and 1.

$$\boldsymbol{p} = \boldsymbol{pr}(\boldsymbol{y} = \mathbf{1}|\boldsymbol{x}) = \boldsymbol{F}(\boldsymbol{x}'\boldsymbol{\beta})$$

Here, $F(x'\beta)$ is the cumulative distribution function for the logit distribution and can be represented as:

$$\mathbf{F}(\mathbf{x}'\boldsymbol{\beta}) = \Lambda(\mathbf{x}'\boldsymbol{\beta}) = \frac{e^{x'\beta}}{1 + e^{x'\beta}} = \frac{exp(x'\beta)}{1 + exp(x'\beta)}$$

With the ordered logit model, the sign of the coefficient shows whether the likelihood that y=1 increases or decreases with an increase in *x*. The magnitude of the coefficient is irrelevant because they differ by scale factor and rather than been able to interpret a particular outcome, we can only identify if an increase in a given independent variable makes y=1 more or less likely. However, it is possible to estimate the marginal effect of a unit increase in the independent regressor x_q on the probability of y=1. This can be summarised as:

$$\frac{\partial p}{\partial x_j} = \Lambda(x'\beta)[1 - \Lambda(x'\beta)]\beta_j = \frac{e^{x'\beta}}{(1 + e^{x'\beta})^2}\beta_j$$

This enables us to express the percentage increase/decrease in the probability that y=1 associated with a unit increase in the independent variable. Hence, the marginal effects are also computed for the logit results. The estimates for the marginal effects are interpreted as: each unit increase in the predictor variable decreases or increases the probability that y=1 by the marginal effect expressed as a percent (Katchova, 2013). The ability of the logit regression to predict the relationship between the dependent variable and multiple independent variables also confirms with the argument in social research that rarely does a single variable sufficiently explain a social phenomenon. It therefore improves our understanding and insight of multifaceted social reality as it allows the researcher to evaluate the unique effect of the selected borrower-related practices. Finally, the PCA composite models are constructed. Given that the PCA index results in continuous data, the ordinary least squares (OLS) regression is employed in analysing this data. The results are only used to compare the logit regression results and to confirm the relationships already identified.

5.6 CONCLUSION

In this chapter, the author presented the analytical framework adopted for tackling the research problem. It therefore constitutes the blueprint that will guide and inform the rest of the thesis. Given the capability approach to poverty and the emphasis on understanding microfinance from the service users' perspective, the Interpretive, capability and participatory poverty assessment approaches are identified as appropriate analytical and theoretical frameworks for addressing the research questions. In line with the selected research approaches, the mixed methods approach is applied to data collection and analysis. The fieldwork exercise through which this is done is justified and described in a reflective fashion; beginning from the selection of the study area and MFI, to the collection of the required data. As regards the selection of Edo State and LAPO MfB as the case study area and the case MFI respectively, the researchers' intimate knowledge of the socio-economic characteristics, language, customs and physical environment enhanced the successful implementation of the fieldwork. The discussion showed that the economic, financial and socio-economic characteristics of Edo State depicts a conducive environment for microfinance intervention and is ideal for the study.

The data collection process is also designed to be fluid enough to provide contextual information, which is vital to the study. Yet, due to resource constraint, and the uncertainties and the general lack of order associated with living in developing countries, it was unable to achieve the estimated sample size. In all, 35 and 62 service users were interviewed for the qualitative and quantitative survey. In ensuring the sensitivity of the questionnaire to the context of the study, qualitative data from the interviews informed the construction of the questionnaire. In ensuring the reliability and validity of data collected, the researcher conducted all qualitative and quantitative interviews, and checked and cross-checked for inconsistent data in the field. The qualitative interviews were transcribed, coded, organised, interpreted, and the findings incorporated into the quantitative analysis. For the quantitative data, data analysis was conducted using frequency distributions, contingency tables and logit and OLS regressions.

Very importantly, based on normative assumptions drawn from the characteristics of microfinance clients, the potential and associated cost of microfinance, economic and finance literature as well as the broader Nigerian context, the researcher selects certain business outcomes that microfinance clients should value. This includes an increased ability to increase business size, introduce new products, reduce cost, develop new business, and increase business asset as indicators of increased ability to achieve successful business outcomes. Further findings in the subsequent chapter justify the researchers' choice to adopt this measure of poverty reduction.

CHAPTER SIX

EVALUATING MICROFINANCE IMPLEMENTATION PROCESSES AND FEATURES FROM THE CLIENTS' PERSPECTIVE

6.1 INTRODUCTION

How do microfinance clients perceive poverty – what capabilities do they value? What is service users experience with the implementation processes and features of microfinance? These are the questions that this chapter set out to answer. The literature review presented in chapters two and three emphasizes identifying and prioritizing the freedoms that people value, and points to the need to investigate the features and characteristics of microfinance delivery and use from the clients perspective. Hence, this chapter is designed to identify the capabilities that microfinance clients' value and also their evaluation of the implementation processes and features of microfinance interventions. The latter is done with a focus on identifying which of these have the potential for harm or good from the viewpoint of service users? It begins with a brief description of the demographics of the respondents. This is expected to provide a general picture of who they are and their socio-economic status. The next two sections focus on clients' experience with group lending and women targeting as implementation processes on the one hand and then loans, interest rates, savings and non-financial services as features of microfinance on the other. The interviews showed that, particularly for LAPO clients who were been served through group lending, their experience as regards the access to and delivery of microfinance, is determined by group practices. Hence, these factors are explored alongside group lending. As mentioned in the previous chapter, quantitative analysis will be employed to triangulate the findings. This is followed by an analysis of clients' perception of poverty and the capabilities that they value. The final section concludes the chapter with specific attention to providing answers to the questions under review.

6.2 SOCIO-ECONOMIC PROFILE OF SERVICE USERS

From the table 6.1 below, we can say that clients are predominantly married (82%) women (74%) aged between 20 and 60 (85%), responsible for one dependant or more (88%), educated to at least secondary level (65%), with relatively low socio-economic status. The gender representation is typical of the pro-women initiative of microfinance interventions. The high rate of married respondents can be associated with the perception that clients who have responsibilities to their spouse and children are less mobile unlike single clients. This is believed to make them less risky, more disciplined and committed to fulfilling loan repayments and thus more appealing to lending groups. Further analysis also shows that married couples are more likely to have more number of children/ dependants. With the high level of poverty in Nigeria and the absence of any form of social or welfare system, the married are more likely to have a greater need to patronise MFIs both to raise and manage finances for their business and households. The data also shows the outreach of MFIs to the economically active poor as the age bracket '20-60' represents the core of the Nigerian labour force. The high representation for the 20-40 age bracket is in line with the previous discussion on the high level of unemployment in Nigeria and how this has driven a large portion of the population to operate informal microenterprises.

Table 6.1: Descriptive Statistics of the Qualitative Respondents

Demographic characteristics	Categories		Frequency	Valid Percent	Cumulative Percent
Age	Valid	20-40	15	42.9	42.9
		41-60	15	42.8	85.7
		61 and above	5	14.3	100.0
		Total	35	100.0	
Gender	Valid	Female	26	74.3	74.3
		Male	9	25.7	100.0
		Total	35	100.0	
Marital status	Valid	single	6	17.1	17.1
		married	29	82.9	100.0
		Total	35	100.0	
No. of children	Valid	None	4	11.4	11.4
		1-4	18	51.5	62.9
		5 and above	13	37.1	100.0
		Total	35	100.0	
Education	Valid	primary	12	34.3	34.3
		secondary	23	65.7	100.0
		Total	35	100.0	
Occupation	Valid	trader	23	65.7	65.7
		service provider	10	28.6	94.3
		pensioner	2	5.7	100.0
		Total	35	100.0	
Spouse occupation	Valid	not applicable	6	17.1	17.1
		trader	12	34.3	51.4
		service provider	13	37.2	88.6
		skilled	4	11.4	100.0
		Total	35	100.0	
Loan cycle	Valid	1-6	27	77.1	77.1
		7-12	8	22.9	100.0
		Total	35	100.0	

Source: Author's computations based on primary data collected from LAPO clients. Traders: food stuff, cloth, drinks, provisions, beauty products etc.; Service providers: hair stylists, fashion designers, catering, transport, craftsman; Skilled: teachers, pensioners, bankers, civil servants

As is typical with microfinance clients, about 95 percent of LAPO clients are self-employed, home-based entrepreneurs engaged in small retail kiosks, street vending, artisanal manufacture, food processing and other micro-scale service provision. Also, spouse occupation is considered to be an indication of extra support or contribution towards the household well-being. For 86 percent of the married clients, their spouses are also engaged in informal microenterprises with non-skilled labour. Only 14 percent report that their spouses are engaged in formal employment with skilled labour. It is not necessarily the case that skilled labour implies higher income but, it is more likely to imply a more stable source of income with the potential for higher level of capability expansion.

6.3 WHAT IS CLIENTS EXPERIENCES WITH MICROFINANCE (FEATURES AND THEIR IMPLEMENTATION PROCESSES) FROM THEIR PERSPECTIVE?

Having identified the socio-economic characteristics of respondents, the researcher proceeds to explore clients experience with microfinance. As mentioned in chapter 3, different features of microfinance as well as their implementation processes result in differing effects on the expansion of capabilities for service users. Hence, this section presents service users' evaluation of group lending and targeting women as implementation processes on one hand; and loans, savings and non-financial services as features of microfinance interventions. The focus is to identify which of these have the potential for harm or good from the viewpoint of service users? This is in line with recent calls in the literature for: (i) the need to understand what financial services the poor need and which benefit them the most, why and for what purposes (Reed, 2013; Maes and Reed, 2012); and (ii) the need for more empirical studies to investigate the features and characteristics of microfinance that have the potential for both good and harm (Stewart et al., 2010, 2012).

6.3.1 GROUP LENDING

Group lending is the foundation of most microfinance interventions (Johnson and Rogaly, 1997; Armendariz de Aghion and Murdoch, 2005, 2010); as it enables access to financial services for the poor. In order to successfully ensure sustainable access, Marr (2001) argues that groups must fulfil two key objectives: organisational and financial sustainability. While the former is achieved through the self-management of the microfinance group as a social network, the latter requires that group members perform duties of screening, monitoring and loan repayment enforcement. It has been argued that explicit or implicit joint liability (i.e members are jointly liable for loan repayments in the case of any defaults in the group) creates an incentive for clients to carry out these duties. While most of the earlier studies (Ghatak, 1999, 2000) focus on how group dynamics allows for high loan repayment, thus ensuring the sustainability of the MFI; there is little research on how it affects clients' poverty reduction. With a focus on the latter, Marr (2001) concludes that it cannot be assumed that the process of group formation, monitoring and repayment enforcement have a neutral effect on poverty reduction. Hence, in evaluating group lending as one of the implementation processes of microfinance, we evaluate clients experience across these different stages of group lending.

6.3.1.1 Peer selection

First, the method of group formation and screening influences the inclusion of the poor in lending groups. With the argument that service users have an incentive to self-select group members in order to mitigate the risk of default, some studies (Hulme and Mosley, 1996; Marr, 2001) find that this method of peer-selection tend to exclude the poor as other members fear their inability to meet repayment requirements. With the LAPO intervention, the qualitative data shows that groups are formed based on self-selection. This is supported by further evidence that word of mouth (from a friend, a relative, group leader, or LAPO staff) is the main source of knowledge about LAPO. In this case, prospective clients require the approval of existing members to join an existing group. Even with a new group, the initiating member(s) need to meet the minimum requirement of 10 group members, and so, have to self-select other members based on certain criteria.

It was generally reported that members are accepted based on trust and personal association. This therefore creates the possibility for exclusion. When we consider the fact that peer selection is based on trust and social relations that provide sufficient information about the level of risks, we cannot ignore the possibility that prospective clients who lack these assets will be excluded. However, expressed clients experience with group formation suggests no evidence of exclusion in the LAPO intervention. All respondents report to have been accepted in groups that they approached. Even when poorer clients are excluded from certain groups, they are still faced with the option of forming their own group with members with whom they share trust and other social relations. As evident in the quote below, it was more likely for clients to report their refusal to join an existing group and instead set up a new one.

> I called one of my friends and told her that I want to join LAPO. We went to one union but we did not like the way they were operating in that union. We went to the office to meet the manager; He gave us the CSOs contact and said we can form our own group. That was how we came together with other people that we trust to form the group (RESP 35, Female, 40, 1)

Second, it is expected that peer selection is done based on assortative matching. This implies that service users have sufficient information about the risk status of their peers such that, risky or safe borrowers form lending groups with their kind (Ghatak, 2000). Research findings on the method of group formation reveal that microfinance groups start off as heterogeneous and fragmented groups, suggesting that information about the defaults risk of their peers is imperfect. The result is that, information levels across group members vary. For example, existing members who introduce prospective members were observed to have high levels of information about the prospective client while other group members relied on the information held by the former. Hence, initial information levels were found to be generally superficial across respondents. In this case, the entire group as well as LAPO officers have to rely on the introducing members' access to information and also set incentives to increase their willingness to share this information. The question is: how effective is this practice in mitigating risk, and what is the effect on group members.

Particularly in large unions[51] where over time, as the groups grow and new members are introduced, members have to depend on the judgment of others to assess the credit worthiness of clients; social relations might be relatively weak. This study finds that in the LAPO intervention, members try to achieve some form of insurance by insisting that the introducing member accepts to guarantee the repayments of the new member in the event of a default, even using their own savings as collateral.

> If someone new comes, we have to make sure that the existing client introducing the new client does not default and he must be willing to agree that if the person defaults his savings will be used to pay. As long as he says he can pay back and he has a business to invest the money (RESP 6, Female, 67, 12)

[51] While there is no universally agreed appropriate group size, a group size of 10 members is often considered appropriate. On the other hand, Ghatak and Guinnane (1999) consider 20 members to be a very large group. Hence, for the purpose of this study, groups beyond 15 members are considered as large. In this study, we find 4 out of the 7 groups are large.

> In this union, when members come to join, we rely on the trust of the existing member who is introducing the new client. However, we cannot differentiate the good from the bad when they come. (RESP 32, Female, 30, 3)

The above quotes further illustrate the heterogeneity in group formation and reveal that the screening process is partial and incomplete. Similar to Marr (2002) who finds that overtime joint liability fades as service users rely on individual collaterals (e.g. sale of asset of the defaulting member), the above quotes reveal a new and interesting finding regarding the use of individual guarantees to new members. One implication of this is that, individuals who do not have such strong social ties that can serve as guarantee, may be excluded from the group. It is important to note that the literature on group liability does not involve such individual one on one guaranty but assumes that the group members jointly screen and guaranty each other. This finding therefore confirms our argument in chapter 3, that, performing group duties might come at a cost to service users, thus, creating an additional incentive for them to find possible ways to reduce and/or transfer these costs to other group members.

Finally, the selection of clients into LAPO groups allows them to take advantage of the collective capability of the group as regards accessing microfinance. For all respondents, aside the potential cost of joint liability, participation in a group sits well with the service users who not only recognize this delivery method as an organizational policy but also recognize that outside group lending, they do not meet the requirements for individual loans. Section 6.3.4.3 further discusses some of the social capabilities that service users enjoy from participation in the group.

In conclusion, we find that as proposed in the literature, group formation in the LAPO intervention is done based on peer selection. Although this creates the possibility for exclusion of prospective clients who do not meet the selection criteria, it does not appear to be the case at LAPO microfinance as service users experience showed no exclusion. On one hand, it can be argued that the LAPO intervention is robust enough such that even if potential clients are excluded from existing groups, they are able to self-form groups. On the other hand, a wider sample consisting of clients and non-clients may reveal exclusion as some prospective clients may lack the social capital needed to self-form a new group. Secondly, lending groups start off and remain heterogeneous as service users have imperfect information about the risk status of their peers. This implies that service users remain exposed to greater risk of moral hazard. Noteworthy with the LAPO intervention is that, unable to raise information to verify the risk status of prospective clients, service users use individual guarantees to insure this risk. This not only supports the possibility of exclusion for those who do not have such relationships that can serve as guarantee, but also supports the literature that there is an associated cost of raising the required information.

6.3.1.2 Peer Monitoring

First, based on the joint liability feature of group lending as mentioned in chapter 3, defaults within the group comes at a cost to other members with possible setbacks to the capability expanding potential of clients. Hence, service users have an incentive to monitor loan usage by their peers. This is known as ***peer monitoring***. This involves scrutinizing their group members to ensure that loans are not used in a way that endangers loan repayment. Beyond group formation, it is expected that effective use of peer monitoring will reduce the risk of potential loan defaults as group members can verify the project returns of their peers, mitigate any extra cost arising from joint liability, and have a positive effect on poverty reduction and service user overall experience with microfinance (Aghion, 1999). It is therefore important to examine how well service users are able to perform this task of peer monitoring; with significant implication for the expansion of capabilities.

At LAPO, group members are responsible for monitoring their peers. It is expected that one basic requirement for effective monitoring is the knowledge of the use of loan by peers; and so service users were asked about this. Quantitative data (see table 6.2 below) shows that less than 5 percent of respondents claim to have knowledge of the use of loan by their peers. The 2 respondents who knew the use of loans by their peers were found to be group leaders. This explains their access to information that might not be available to others. This low level of monitoring as depicted in the quote below was the general practice across all groups.

> I'm not aware of how members spend their money but we are close enough to know each other's business (RESP 31, Male, 40, 1)

The question is: what is the reason for this low level of monitoring even when service users have an incentive to engage in monitoring. One reason for this might be the high use of loans for non-business purposes. With about 60 percent of respondents reportedly engaged in the non-business use of loans and less than 5 percent informed about the use of loans by their peers, there cannot be any substantial form of monitoring in existence.

Table 6.2: Extent of Monitoring

	Categories	Frequency	Valid Percent	Cumulative Percent
Know use	No	60	96.8	96.8
	Yes	2	3.2	100.0
Use of loan for non-business purposes	Yes	38	61.3	61.3
	No	24	38.7	100.0

Source: Fieldwork Data (2013)

Based on responses from service users, it was observed that although the existence of a business activity to which loans will be invested is emphasized at formation, over time, the focus on the use of loan diminishes and loan repayment becomes the priority. This therefore raises questions about the effectiveness of peer monitoring in addressing moral hazard at LAPO**.** This result is however consistent with other findings suggesting that peer monitoring in microfinance interventions is rather passive. This includes results from the Malawi Rural Finance Company (MRFC), intervention where members in general had deficient information about the characteristics of other group members (Simtowe and Zeller, 2006). In the case of *La Chanchita* microfinance intervention in Peru, less than half of the service users had carried out any form of peer monitoring. It was mainly done on an inconsistent basis as it was considered to be an expensive process (Marr, 2002).

While Marr (2002) finds that monitoring is low due to the cost of monitoring, this study finds that with LAPO microfinance intervention, monitoring is low because there is an implicit understanding among group members that the poor have varying needs and face multidimensional deprivations (see section 6.3.4). Hence, even though members are strongly advised to invest their loans in economically productive activities, there is an understanding that some part of that loan will almost always be used for household purposes and that service users often relied on other sources for loan repayment outside the returns from their businesses. This is consistent with findings from Ghana (Yeboah, 2010) where peer monitoring was found to be passive due to the widespread use of loans for non-business purposes. In conclusion, the result shows that peer monitoring in the LAPO intervention is significantly low due to imperfect information as well as an implicit understanding amongst service users that loans will more often than not be used to meet some of the multiple deprivations that the poor face. It therefore suggests that the risk of moral hazard persists in the LAPO intervention. As shown thus far, this exposure to risk represents potential damage to the capability expanding potential of service users

6.3.1.3 Peer support

Peer support refers to the individual or collective assistance which group members provide to their peers. This is capable of increasing individual capabilities or access to social capabilities that members can benefit from. This study recognizes the role of social structures in shaping individual and social capabilities. It particularly focuses on the lending group and the role of social relations within the group to increase the capability of service users. For microfinance clients, the lending group plays a crucial role in the extent to which they can successfully take advantage of MFIs to access and use microfinance. Acceptance in a lending group offers the opportunity to obtain credit while the exclusion from a lending group restricts the access to resources. This is the recognition that access to microcredit is currently and perhaps also in the future, dependent on group participation, such that changes to the entire group are very much likely to affect individual capabilities.

In the LAPO intervention, peer support includes lending of money to their peers to complete loan repayment, support their businesses and meet welfare related needs. Service users unanimously agree that the lending group had enabled them to share ideas and build social networks which have been vital to the success of their businesses. The study found that financial relationships among group members were embedded in social relationships. This social network and inherent social capital is an important tool for combating poverty. Group members attended funeral, child naming and other social ceremonies of their peers. For example, peer support during life cycle events could include financial contribution to support the member, the supply of human capital to engage in productive activities (e.g. during weddings and funerals, group members may volunteer to help with catering, hospitality, cleaning etc), as well as the social solidarity that comes from having members in the event.

> I like the group lending because in the union, even if I cannot share my problems with everyone, there will be one or two persons that I can meet to help me if I have a problem (RESP 1, Female, 42, 3)

> We have a unanimous agreement in the union to contribute and pay for defaulting members and then the member repays. During and outside union meetings we encourage ourselves and talk about repayment and business issues - where to buy goods, what products to buy etc. (RESP 10, Male, 65, 8)

Another form of peer support has to do with assisting in loan repayment. This goes beyond personal relationships where individual members lend to their peers; internal funds may be set up by the group itself to assist members when they experience negative shocks that affect their repayment ability. Money lent to complete loan repayment of peers can be considered as voluntary peer support because members could refuse to meet the obligation of a defaulting member. However, this will result in a total collapse of the lending contract. Here, the MFI bears the loss of the loan obligation as well as the enforcement costs; and the group members bear the loss of future access to loans, and in some cases any savings contribution. Hence, others may argue that this form of peer support is involuntary and that it is the terms and conditions of their borrowing that leads them to do this.

> Even when there is a problem, we can assist one another to make sure that the LAPO repayment is complete (RESP 14, Male, 34, 4)

> Members are friends and help one another when anyone cannot complete their weekly payment and even in the case of default we bear one another's burden (RESP 17, Female, 42, 12)

Supporting evidence for the latter is evident in the above quote which shows that supporting repayment of peers may be influenced by joint liability. Here, support is fuelled by the desire to complete LAPO repayment; even when this comes at a cost or a burden to service users. Hence, we recognise that despite the potential for increased capability for the receiving client, peer support implicitly means that the supporting client(s) stand the risk of losing their money to other members. As becomes evident further on, service users resent this because they not only bear the cost of repayment enforcement, but are often unable to enforce repayment as the enforcement mechanism is incomplete.

In conclusion, peer support of business and other welfare related needs enable service users to share ideas and build social networks vital to the success of their businesses, raising social capital and for accessing 'group' capabilities. However, peer support in terms of financially assisting peers who face repayment challenges often comes at a cost to service users as the supporting client(s) stand the risk of losing their money as they are often unable to enforce repayment.

6.3.1.4 Peer pressure

Similar to findings from Peru (Marr, 2001), evidence from the LAPO intervention shows that with low monitoring, microfinance groups rely heavily on the use of peer pressure or other forms of social sanctions to enforce repayment. Some of these include: pressurising the defaulting member and the member who introduced them to repay the loan, exercising a double repayment penalty or an interest charge on defaults. They could also face the threat of expulsion from the group, denial of access to future loans, and also the use of the defaulters' savings to fulfil the repayment obligation. These practices are reflected in the following quote:

> In this group, if any member defaults, the person who introduced them is made to pay from their savings. If this is not enough, everyone is made to contribute. We currently have 2 members that have defaulted and LAPO took from everybody's savings to pay (RESP 1, Female, 42, 3)

Although the quote above suggests the use of individual guarantees, the researchers' observation during the group meeting suggests that this is not a sufficient tool for enforcing repayment. In this group, 2 members – a mother and her daughter – had defaulted. While the mother introduced the daughter, the group as at the time of the meeting (2 weeks after the default) had not been able to pressurize the introducing member to meet the defaults. Hence, in enforcing joint liability, LAPO made deductions from the mandatory savings of all group members. Unlike findings from Marr (2002) where over time, joint liability is gradually abandoned and the use of social sanctions increases, this study finds that joint liability remains relevant in the LAPO intervention. Even when social sanctions are in place, LAPO enforces joint liability such that group members are made to bear the cost of default; *then after*, group members can embark on attempts to retrieve the default amount. This is evident in the quotes below.

> If someone defaults we collectively meet the repayment requirement and then collect the money later. Anyone who defaults will pay double when they are making repayments (RESP 21, Female, 41, 1)

> When someone doesn't pay, the union combines to pay and the person is responsible to pay back with interest. We know the house of each other (RESP 26, Female, 43, 8)

> In this union, we have a contribution so that when members default, we withdraw from the savings to cover it up. We then send about 3 delegates to collect the money. (RESP 31, Male, 40, 1)

Whether the repayment of default is done voluntarily from individual savings or from a group purse, or enforced through collective sanctions in terms of deductions from mandatory savings, there is an associated cost to service users as mentioned in the previous section. With each loan cycle, clients are obligated to make mandatory savings which they are not allowed to access before the end of the loan cycle. This accumulates overtime and at the end of the cycle comes to a significant 40% of the loan amount. The use of this mandatory savings as loan guarantee (i.e. collective sanction) is in fact the most frequently used sanction because it primarily benefits the MFI officers as the financial records stay clean, repayment rates are high, loan portfolios keep growing and officers' are able to attain their performance targets. However, peer pressure and the use of collective sanctions have the potential to radically erode group cohesiveness. When the use of savings as loan insurance leads to the loss of clients hard-earned savings; both because of low levels of information as well as lack of support from the MFI in recovering these savings, a deep sense of distrust emerges between members; eroding group cohesiveness and potentially crumbling the group dynamics.

> I do not like the fact that I am held responsible for defaulting clients. This process affects the social solidarity among members who are supposed to be friends (RESP 26, Female, 43, 8)

As evident in the quote above, material losses are compounded by the damage to social relations between group members which results from the violent confrontations that take place during the implementation of social sanctions and peer pressure. Drawing from the experience of exited clients, the 2013 LAPO unmet service needs survey point to this joint liability feature as well as the use of savings as loan guarantee as key reasons for client attrition (LAPO, 2013).

Interactions with service users showed that without the actual implementation of social sanctions, there is an inherent threat of social sanction in all groups and service users strongly rely on this to ensure repayment of loans. Members threaten to socially ostracise defaulting members, shame them by sending group members to their houses, place of work, and disclosing their default to the public. Given the strong communality in the Nigerian society, these measures appeared to be very potent as respondents claimed they would do anything including borrowing from other sources just to repay their debt than to face the wrath of their peers. These findings suggest that compared to the actual use of social sanction in ensuring loan repayment, this inherent threat of social sanction acted more as a deterrent against default.

Similarly, quantitative evidence in Table 6.3 below reveals that only about 17.7% of respondents use peer pressure as a method of enforcing repayment (see section 5.5.2.2 for a discussion of the repayment enforcement categories). These were particularly group leaders. Additionally, in groups where old clients who introduce new members are held liable for the default of the new client, the old clients were seen to engage in some form of peer pressure It was common to find out that aware of the threat of social sanctions at the group level, service users do not consider it necessary to engage in any form of repayment enforcement on an individual basis. 69.4% of service users upon default by their peers are passive as to the actual implementation of social sanctions in enforcing repayments, but rather leave the defaulting clients to make repayments of their own volition.

Table 6.3: How do you enforce repayment?

	Categories	Frequency	Valid Percent	Cumulative Percent
Repayment Enforcement	Voluntary	43	69.4	69.4
	Moral Suasion	8	12.9	82.3
	Peer Pressure	11	17.7	100.0

Source: Fieldwork Data (2013)

As with all other expected client duties, this practice of not engaging in repayment enforcement has the potential for harm as it means that service users have to bear the cost of default. However, from the service users' perspective, implementing social sanctions and peer pressure is expensive. For instance, apart from the social cost mentioned earlier, going to the defaulters' home or workplace to demand for repayment is at an expense of time spent on ones' business. This is particularly so for long-term defaults where the service user is completely unable to meet the repayment. Service users argue that if the group as a whole is unable to enforce repayment, then any attempt to do so on an individual level will only mean incurring additional cost. Although the researcher was aware of a situation in the intervention where the police and legal action were employed, these do not reflect the experiences of respondents as this has not been employed in any of these groups. This is understandable given the cost and bureaucracy involved. Nevertheless, an attempt is made in the next chapter to quantitatively investigate the relationship between clients individual practice of engaging in peer pressure and poverty reduction.

Overall, the above findings show that LAPO groups were self-formed as prescribed by the literature. Peer monitoring is less employed among LAPO clients as more emphasis was on loan repayments rather than the use of loan. Union members count on the threat of group sanctions to motivate members to meet their repayments regardless of the use of loan. While components of group lending such as the social capital, solidarity and peer support gained is esteemed among service users, the joint liability feature of group lending and particularly the use of savings as loan guarantee hold considerable potential for generating negative effects on client welfare.

6.3.2 TARGETING WOMEN

As mentioned in chapter 3, microfinance is generally implemented as a pro-women initiative. This has been argued to have positive outcomes on gender equality (Cheston and Kuhn, 2002), women empowerment (Pitt et al., 2006), as well as higher household benefits (Khandker, 2003). However, in line with Johnson (2000), the analysis conducted in this section is done with an understanding that microfinance participation will always have different effects on men and women. This study will explore the variation in the microfinance experiences of men and women, and the potential effect on their expansion of capabilities.

First, we find that while gradual micro increases in loan size and the frequent meeting in public places are more suitable to the type of businesses run by women, these same features are likely to discourage men from participating in microfinance.

> The loan suits women because they are the ones that trade most and also because the small size of loan and gradual increases does not suit men who always want larger loans (RESP 31, Male, 40, 1)

> Men are proud and they feel starting with NGN30000 is too small. They also feel like LAPO is for women (RESP 34, Male, 48, 4)

The economic activities engaged in by women in Nigeria and in Africa at large predominantly involve micro-scale business operations run from home with household labour, requiring minimal start-up capital, fixed assets or any special skill (Ledgerwood et al., 2013). Hence, the structuring of microfinance loans to suit female-dominated businesses naturally endangers the participation of men in the microfinance intervention. This is evident in the second quote above. The emphasis that microfinance is a pro-women initiative also has a similar effect.

Second, female service users report an increase in empowerment as participation in the microfinance intervention has enabled them take control of their lives through the expansion of choices. This is evident in the following quotes:

> The targeting of women is good because it is a good way to encourage, support and create employment for women like us who take care of the home and do everything we can to train our children (RESP 23, Female, 35, 1)

> Before I joined LAPO, whenever my children are sent home from school for tuition fees or they return from school sick, I will have to wait for my husband. Now, I can take care of them and deal with some of the problems before he comes (RESP 19, Female, 34, 2)

This is consistent with the argument that microfinance empowers women (Kabeer, 1999; Pitt et al, 2003). We also find evidence to support the argument that a good way to improve the well-being of the household is through the empowerment of the woman (Khandker, 2003; Cheston and Kuhn, 2002). One respondent stated:

> The woman is the pillar of the house and the woman is the neck but the man is the head. Where the neck goes is where the head goes. And women work more in the house. The woman is more aware of the concerns of the children and the needs of the home. The man just gets up in the morning and leaves the house. So when LAPO wants to affect the household, it is a better approach to do it through the woman because even the man in Africa leaves the business of the household to the woman (RESP 8, Female, 46, 4)

However, unlike findings from the Grameen Bank in Bangladesh where relatively higher benefits accrue to the household when loans are targeted to the women rather than men (Ledgerwood, 1999), we cannot make such conclusions as the interview questions were not designed to generate the information required for such conclusions. Nevertheless, the quantitative analysis reported in the next chapter would provide useful insights into the relative benefits of microfinance for men versus women.

Finally, as we explore the variation in men and women experiences, one unexpected finding is the gender imbalance in LAPO group formation and participation. Gender imbalance can be seen as disproportionate gender representation in a given population owing to factors such as biological differences; direct or indirect discrimination/ harassment, and/or victimisation on the ground of gender; as well as sexist attitudes that may stem from traditional stereotypes of gender roles. Of the 7 groups sampled, only 3 groups were mixed; 3 groups consisted of women only and the last group of men only. Even the mixed groups were confirmed to have begun as women only.

> We are afraid of bringing men into this union because we are afraid that if the man defaults, we might not be able to get the money back. The women in the union are however married and live with their husband and so cannot run away (RESP 21, Female, 41, 1)

> In this union we have only women because if men come in, there might be struggle for power as the men might want to make the decisions (RESP 4, Female, 46, 7)

> This union is all men and this is how we want it (RESP 13, Male, 27, 2)

We find 2 reasons for this gender-biased selection of group members. First, female clients consider it less risky to accept women than men into the female dominated groups. The dependence of the woman on her husband and also her obligation to her family creates a sense of insurance as other group members can trust that she will not abscond with the loan. This is however not the case for the male participants. They are considered to be more mobile than the women. Secondly, Nigeria is largely a patriachical society; and so women fear the potential power struggle that may ensue from accepting prospective male clients into the groups. The last quote also confirms that the same gender bias is evident in the male group. This practice has the potential to reinforce rather than challenge the prevailing gender bias in the Nigerian society.

Overall, the empowerment of women in terms of the increased ability to support the household and greater independence, are key benefits of using microfinance as reported by female LAPO clients. Nevertheless, the targeting of women and labeling of microfinance as a pro-women initiative might foster the exclusion of the male poor from participation in microfinance.

6.3.3 LOANS AND INTEREST RATES

There is no doubt that ***microcredit*** is core to the delivery of microfinance interventions and their characteristics - loan size, use, repayment frequency, and interest rate - influence the experience of the service users with microfinance.

6.3.3.1 Loan sizes

As mentioned in chapter 4, the regular LAPO loans begin at NGN 30,000[52] and this initial loan amount does not vary. Subsequent increase in loan sizes is based on dynamic incentive where, with each new loan cycle, loan size increases by NGN 10,000. Although loan increases can be declined by individual choice or by objection from the group leader and other members, this does not appear to have been a common practice. Objections are often seen to indicate problems with repayments and so service users are likely to accept higher loans to show otherwise. As shown in Table 6.4 below, loan cycle has a statistically significant relationship with the number of

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[52] Although the initial loan size during the fieldwork stood at NGN30,000 this amount has since been increased to NGN50,000.

years in LAPO and the loan amount. This implies that service users are more likely to continue to use loans as they remain in LAPO and also enjoy the increase in loan size with each new loan.

Table 6.4: Loan cycle by Number of years in LAPO and Loan amount

Variables	Categories	Sample Size (%)	1-6 (%)	7-12 (%)
Years in LAPO*	1-5	42 (67.7)	42 (87.5)	0 (0.0)
	6-10	20 (32.3)	6 (12.5)	14 (100.0)
Loan Amount*	< 80,000	48 (77.4)	43 (89.6)	5 (35.7)
	80,000 and more	14 (22.6)	5 (10.4)	9 (64.3)

Source: Fieldwork Data (2013)
* indicate statistical significance at the 1% significance level

The table also shows that about 22 percent of service users had loans equal to or greater than NGN 80,000. As mentioned in chapter 3, in line with Ledgerwood (1999) who calls for an upper limit on loans, we argue that while higher loan sizes might increase clients' ability to take advantage of bigger investment opportunities, it comes with relatively higher repayment burden. High loan sizes might also lead to an increasing use of loans for non-income generating activities. What is clients experience with the increasing size of loans as regards loan repayment and use?

As regards repayment, we find differing opinion between those who have actually experienced loan defaults and those who have not. We find that the latter strongly believe that the loan size plays a significant role in the repayment ability of a client. Particularly, for them, their ability not to encounter repayment difficulty is tied to their practice of borrowing within their debt capacity. These views captured in the quotes below appear to be shared by both male and female, new and older clients, and clients in different groups.

> The main reason why I have succeeded is that I don't take more than I can handle even when I qualify for a higher loan (RESP 4, Female, 46, 7)

> I have never had any difficulty with repayment. People face difficulty when they don't work every day or they spend their loans on personal use or they take more than they can carry (RESP 11, Female, 61, 1)

> I also do not take any loan that is above my capacity. If your business cannot give you NGN6000 in a week but you take up a loan that has such a repayment structure, it will only lead to disaster (RESP 16, Male, 47, 3)

> I have heard people say that LAPO money is blood money but I've used it for my business and found it not to be true. This is only the case when people have challenge with repayments and this happens when you take more than you can handle (RESP 28, Male, 31, 4)

Although the use of loan is explored later on, it is interesting to find only RESP11 who is in her first cycle, considers the use of loan to play a role in default. This is the usual orientation given by LAPO to service users during the probation and might account for her response. For respondents who have faced challenges with repayments, this has very little to do with the loan size. According to them, repayment challenges were more related to family challenges, poor business conditions, and changes in repayment structure such that service users could not meet the weekly repayment requirements for their current loans.

> The weekly loan is too stressful. I have not had any problem servicing my loan but it is my salary that I have been using to make repayments. So the business wasn't able to make the repayments. When you pay money with interest, you have to look for money from somewhere else to join to pay them back. That is why I look for money to pay them (RESP 3, Female, 61, 12)

> I have experienced difficulty because of the weekly repayments and also they reduced the repayment period from 10 months to 8 months. This is not helpful (RESP 10, Male, 65, 8)

> The problem with repayment is when you take higher than your capacity and when people go through challenges maybe in their family or health wise. For example, the last time I took the loan and closed my account, it was because my husband had an accident and I could no longer work for a while. I now know that even when you qualify for NGN100, 000 and you know you can only handle NGN40, 000 at the moment, it is better you go for NGN40, 000 (RESP 26, Female, 43, 8)

However, when we look at the characteristics of RESP 3, 10 and 26, they all have loan amounts equal to or greater than NGN100, 000. RESP 3 is a pensioner who is currently engaged in trading clothes. Her response suggests a situation where even though repayment has always been met; the business activity is unable to generate sufficient returns on loans. She particularly mentioned a decrease in sales arising from the new entrant of high-street fashion shops who sell imported products. Although the quote from RESP 26 who is also a trader points to the importance of borrowing within ones debt capacity, she however prioritizes the accident of her husband as the main reason for her default. According to her, this led to her inability to engage in productive activity for some time and therefore her inability to generate enough income to meet repayments. With an extensive literature on the uncertainties and shocks facing poor people in both the livelihoods and microfinance literatures, there appears to be supporting evidence for her argument. Further analysis showing that both service users did not engage in the non-business use of loans and cross-tabular analysis (Table 6.5 below) showing no statistically significant relationship between loan size and repayment difficulty.

Table 6.5: Loan size by Repayment difficulty and Loan Use

Variables	Categories	Sample Size (%)	1-6 (%)	7-12 (%)
Repayment difficulty	Yes	15 (24.2)	12 (25.0)	3 (21.4)
	No	47 (75.8)	36 (75.0)	11 (78.6)
Non-business use of loan	Yes	38 (61.3)	29 (60.4)	9 (64.3)
	No	24 (38.7)	19 (39.6)	5 (35.7)

Source: Fieldwork Data (2013)
* indicate statistical significance at the 1% significance level

6.3.3.2 Loan Use

As is typical practice with most microfinance interventions, regular loans at LAPO are primarily given for investment in microenterprises. However, empirical evidence shows that microloans are used for countless purposes other than investment in income-generating activities. In soliciting clients experience with loan use, this study asks service users if they had consistently used all or part of their loans for non-business purposes. Table 6.5 above demonstrates that 61.3 percent of service users indicate the use of loans for non- business purposes. However, given the social desirability syndrome discussed in the previous chapter, we expect that this figure could be greater than reported above. Though it has now been accepted that the use of loans for non-business purposes increase capabilities at the household level (Johnson and Rogaly, 1997; Hulme and Mosley, 1996), this study argues that this might negatively affect repayment capacity therefore increasing client's vulnerability to indebtedness and poverty reduction. Therefore, we asked respondents about their experience as regards the use of loan. Particularly, this study assesses what service users have used their loans for and how this affects their repayment experience; with particular attention to the potential for good or harm. The finding is consistent with the argument that loans are largely used to meet household and other welfare needs, with child education been the most commonly cited. While this represents increased capability of service users to meet these household needs, the question is does it come at a cost to repayment ability?

Service users tend to hold the view that the use of loan does not matter as long as repayment is made when due. This view captured in the quotes below appears to be shared by male and female, new and older clients, clients in different groups and across different socio-economic class. For instance, RESP 14 who is a transporter popularly called ‘bike rider’, has in addition to using part of his loans for maintaining his motorcycle which he uses for business, also used loans for children education.

> I have used the loan to train my children and also maintain my business asset to ensure sustainability of my business. Not all loans are used for business because there are problems in the home that must be taken care of. No matter the advice from the CSO, people have their own reasons for borrowing money and that’s what they use it for. What is important is that they are able to make repayments. For me, even though I take LAPO loan, I can still use it for my children school fees as long as I know that when I need to make repayments I can make it (RESP 14, Male, 34, 4)

With his comments that there are household needs that need to be met, this finding is consistent with recent observation that if these basic financial needs are not at least partially met, it would be unwise to lend to the poor exclusively for productive investment. This is because at most, the loans will be used to meet the more basic financial needs – consumption smoothing, risk management in dealing with emergencies, and accumulating large sums for life-cycle needs (Rutherford et al., 2013). Further evidence from the quotes below suggests that this is a routine practice in LAPO with all or part of loan amount used to meet nuclear and extended family needs.

> The last one I took, I shared between myself and my younger sister, my own part of it, I used to purchase some business equipment (RESP 4, Female, 46, 7)

> The last loan I took is not for business but to pay my brothers son school fees. Now that my business has grown I do not have to use the loan for business as long as my business can generate the repayments (RESP 8, Female, 46, 4)

One reason for the continuous use of loans for non-business purposes is the well documented fact that oftentimes, business and household finances are not distinct (Armendariz de Aghion and Morduch, 2005). The results show that 21 percent of respondents did not keep their business finances separate from household finances. When we compare this with the 61.3 percent who use loans for non-business purposes, it would suggest that even when business and household finances are separate, service users still use loans for non-business purposes.

Table 6.6: Repayment Difficulty by Loan Use and Separate Business Money

Variables	Categories	Sample Size (%)	1-6 (%)	7-12 (%)
Non-business use of loan	Yes	38 (61.3)	10 (66.7)	28 (59.6)
	No	24 (38.7)	5 (33.3)	19 (40.4)
Separate Business Money	No	13 (21.0)	4 (26.7)	9 (19.2)
	Yes	49 (79.0)	11 (73.3)	38 (80.8)

Source: Fieldwork Data (2013)
* indicate statistical significance at the 1% significance level

In light with the objective of this chapter, this study considered whether how loans were used and managed had implications for repayment ability. We assume that a positive relationship between these two so that increasing use of loans for non-business purposes comes with a potential harm to repayment ability. However, as shown in Tables 6.6 above, cross-tabular analysis shows no statistically significant relationship between repayment difficulties on one hand and the use of loans for other purposes and the practice of separating business finances from household finances on the other hand.

6.3.3.3 Repayment Frequency and Enforcement

Additionally, while frequent and regular installment is argued to ensure high repayment rates and instill fiscal discipline into service users; this comes with relatively higher repayment burden. Given the characteristics of clients, it is important to examine what their experience is with making repayments. Service users unanimously cite short repayment intervals as one of the features of microfinance loans that have the potential to harm clients experience with microfinance. Loan repayment at LAPO currently follows a weekly pattern; and service users experience confirms the burden associated with this repayment pattern.

> The monthly payment is better because you know you have a target. The weekly one puts a lot of stress on the client. Once you make one repayment, you have to start struggling for the next week and that's where it becomes bad for those who borrow more than their capacity. (RESP 2, Female, 28, 3)

> The problem is this weekly scheme, because the repayment period is too close. Not all businesses are able to generate such repayments with additional income for house keep. This becomes a problem particularly when you move up the loan cycle (RESP 20, Female, 56, 13)

From the quotes above, there are two evident reasons for the experienced repayment burden. They include: poor business conditions and economic fluctuations that may restrict the expansion of businesses; and the use of dynamic incentive without a corresponding increase in the repayment period. This finding is consistent with results from Ghana where service users complained of repayment difficulties owing to 'limited economic absorptive capacity of the community (poor markets), and increasing loan sizes with no commensurate extensions in repayment periods' (Yeboah, 2010: p234).

Some other reasons for repayment difficulties as identified in the 2013 LAPO unmet service needs report include external shocks that arise from natural disasters, changes in government policies and the illness or loss of a family member. Exited clients complained to have experienced difficulties due to flash floods and loss of businesses arising from the government urbanisation exercise which saw the demolition of clients businesses. These clients report that during times like these, the pursuit of repayment by LAPO is done in a way considered to be 'heartless towards their plight'. Particularly, in addition to losing their homes and sources of livelihood, many have had to exit the intervention partly due to the repayment difficulties but primarily due to the repayment enforcement practices which left them worse off at times like this (LAPO, 2013: p35).

6.3.3.4 Interest rate

Finally, interest rates represent the cost of lending and the higher they are, the lesser the net gains to service users. Service users generally consider the interest rate on LAPO loans to be acceptable, particularly when compared with other options such as money lenders.

> If they give you 1000 naira, you'll pay 25 naira on top[53]. I would say I don't have a choice because I need the loan, this is the cheapest I have seen and so I can say the interest rate is ok (RESP 1, Female, 42, 3)

> The interest is very good because I know of other meetings where you get to pay higher interest on the loan and you don't have savings (RESP 18, Female, 39, 3)

In conclusion, these findings confirm that microcredit as a key component of the microfinance intervention has the potential for influencing service users' utility or disutility with microfinance. As regards loan size, non-defaulting clients consider high loans to negatively affect repayment capability due to the relatively higher repayment burden while, defaulting clients argue otherwise, pointing to external shocks to the family and business as the major cause of default. The quantitative evidence however

[53] This reflects clients understanding of the 2.5% monthly rate of interest charged on LAPO loans.

supports the latter. Yet, we cannot fail to mention that service users who report repayment difficulties also have loans of NGN 100,000 and above. Loans are used to meet business and other household needs. From the service users' perspective, this represents increased capability to meet household needs but with no cost to repayment ability? Service users widely hold the view that the use of loan does not matter as long as repayment is made when due. The quantitative evidence also shows no significant relationship between loan use and repayment difficulty. Service users unanimously cite short repayment intervals as one of the features of microfinance loans that have the potential to harm clients experience with microfinance. One reason for this been the high repayment burden that comes from the use of dynamic incentive without a corresponding increase in the repayment period. Last but not the least, service users generally consider the interest rate on LAPO loans to be considerably cheap, particularly when compared with other options.

6.3.4 SAVINGS

As mentioned in chapter 4, LAPO MfB offers voluntary and mandatory savings accounts. The resulting accumulated savings as mentioned in chapter 3, are expected to increase the capability of the poor to meet certain lifecycle, emergency and investment needs (Rutherford, 2000), and over time act as a catalyst in their freedom from the vicious cycle of poverty. However, as is the interest of this study, this section will investigate clients experience with savings – voluntary and mandatory – but particularly with certain features of mandatory savings that have been identified to possess the potential for harm.

Respondents widely affirm the ability of savings to increase their capability to meet life cycle needs, cushion financial shocks and accumulate both household and business assets. Savings is used to complement the loan so that service users do not depend too much on the loans. This finding supports the fact that the poor do save (Morduch, 1999; Rutherford, 2000). It is often said that MFIs who require mandatory savings find it difficult to raise voluntary savings as service users fear the loss of both savings sets in the event of any problem individually or at the group level. At LAPO, while this is the case with mandatory savings, service users' voluntary savings is only at risk when they default. Any default at the group level only affects their mandatory savings. Nevertheless, we find only 10 out of the 35 respondents in the qualitative survey engage in voluntary savings. These respondents are predominantly female (7) and married (8). Yet, a higher percentage of men (33 %) as against women (27 %) in the sample engage in voluntary savings. Although the difference is little, one reason for this in the Nigerian context might be the fact that the men are often relied on for relatively higher capital intensive projects. For instance, living expenses – rent or building a house, purchase of a car, child education etc. are often financed by the men while the woman meets the day-to-day running of the household. While the relatively less risk to voluntary savings encourage its use, the low rate of interest on voluntary savings discourage its use.

Turning towards mandatory savings, as mentioned in chapter 4, these are of two types. This is clearly evidenced in the quote below.

> You have to make savings before you are given any loan. There is also a mandatory savings that you do every time you make repayment. When you have completed your repayment you can then withdraw from your savings (RESP 12, Female, 46, 2)

These mandatory savings are used as loan guarantee (cash substitute) such that in the event of a default within the group, LAPO might make deductions from this savings to fulfil the obligations arising from joint liability. This potential of losing savings in the event of default by peers is a cost to clients; and is capable of damaging the social cohesiveness of the group as mentioned in section 6.3.1. Even in the absence of default, service users are unable to withdraw these savings until repayments are made. Hence, it leaves clients unable to access their own savings in times of difficulties and results in clients forgoing interest income that would otherwise be earned on an individual savings account.

Nevertheless, service users generally appreciate the fact that mandatory savings requirement is embedded in the repayment structure. The mandatory savings facility is preferred as it instills some level of fiscal discipline.

> The compulsory one is better because if it is only the voluntary one I do not think I will be able to save like that. I used to make voluntary savings but now I only do mandatory because of some current expenses (RESP 12, Female, 46, 2)

Service users note that without this mandatory requirement, such level of discipline and commitment to accumulate savings would be unrealistic. Particularly, the fact that at the end of each loan cycle, they are able to have accumulated savings for themselves is a motivational factor. Hence, although mandatory savings are perceived as additional cost to credit (Wright, 1999) due to the inability to withdraw until repayment is complete, LAPO clients are satisfied with the level of fiscal discipline that mandatory savings instills. However, service users express their disquiet with the potential harm that arises from the use of savings as collateral in the case of default. The researcher also witnessed this firsthand during the fieldwork exercise. This was the experience with the only respondent who noted that she was exiting the intervention after the conclusion of her current cycle. In her union, they had 2 members (a mother and her daughter) who had recently defaulted and absconded from the community. To fulfil their joint liability requirement, the LAPO official had informed the group that the default is been withdrawn from their savings. Although all respondents noted their displeasure with the situation at hand, this lady was very upset, sat apart from all other members and noted that after 6 years in the intervention, she has had enough of losing her savings in paying for the defaults of others.

6.3.5 NON-FINANCIAL SERVICES

As mentioned in chapter 4, LAPO MfB provides a series of financial and business education programmes on one hand and health and social empowerment programmes on the other hand (see section 4.5.1.4). These services are important for creating and expanding capabilities of the poor as mentioned in chapter 3. This section explores clients experience with these services, and particularly what characteristics of these services or their implementation process have the potential for good or harm; and how well they are able to enhance the expansion of capabilities.

All service users reported to have benefitted from the financial and business education programmes during the probation period and at subsequent times when the CSO may provide business advice to allow service users take advantage of seasonal or economic changes.

> I give an example of a woman who was ignorant of a deposit slip, pass book or cheque before joining LAPO. And so was been cheated by her husband but after been introduced to these concepts by LAPO, she was able to ask her husband about the where about of the payments she could identify in his pass book or deposit slip (RESP 8, Female, 46, 4).

Respondents generally agree that these non-financial services are helpful and beneficial to the expansion of capabilities for service users; with male clients calling for more business development trainings or skill development, and female clients calling for more business advice and information.

Service users who have been in the intervention for at least a year also reported to have benefitted from the awareness creation exercises for one or more of the health and social programmes. Those who reportedly have not benefitted from these programmes have nevertheless heard about them and are likely to be new clients or older clients who are not regular in group meetings. As with the business education programmes, respondents generally agree that these non-financial services are helpful and beneficial to service users.

Beyond creating awareness, some service users who meet certain criteria get access to some services that have direct effect on the expansion of capabilities. For example, service users who meet certain repayment standards can enter their children into a scholarship scheme where the children sit for an examination and those who meet the cut-off mark are awarded a scholarship. Additionally, women who have been in the intervention for at least 6 months before having their babies are entitled to a NGN20, 000 maternal and child health assistance fund. Just 3 out of the 35 respondents have benefitted from these more criteria-determined non-financial services. Of the three, one group leader has benefitted from a scholarship awarded to her grandchild and the other two have benefitted from the free medical check-up. While these services have a definite positive outcome, one of the recipients had this to say:

> I have benefited from the health program but all they did was to test our blood pressure. I think the service is not good enough and should be improved. Also, the selection process for the children scholarship is not clear and LAPO is been deceptive and does not keep to their promises. There are children who qualified for these benefits but we did not hear from them again (RESP 10, Male, 65, 8)

The above quote is in line with concerns in the literature about the quality and outreach of these services (Gonzalez, 2003). Additionally, the perception that LAPO is 'deceptive' shows the ability of the ineffectiveness in the delivery of non-financial services to challenge the very important 'trust' that ought to exist between financial service providers and their clients. This is further buttressed by the quote below. Although RESP 2 is a single lady without children, she reports the experience of other women in her group and the resulting disutility with the microfinance intervention. The notion that 'they do not keep their promise' also has the potential to affect the trust that service users ought to have for the intervention. Lack of trust can affect service users' continuous use as well as their willingness to save with the intervention.

> I am however not happy because they do not keep their promise. For example, there are 2 women in this union who qualify for the NGN20, 000 maternal and child health

assistance; but even after 10 months of having their babies have not received the benefit (RESP 2, Female, 28, 3).

Additionally, if the fund expected to support maternal and child health are only provided months after the child has been born, this suggests that the service is not meeting the required need.

In conclusion, respondents generally find non-financial services to be beneficial to the expansion of capabilities; with male clients calling for more business development trainings or skill development, and female clients calling for more business advice and information. However, the obscurity surrounding the access to some of the more criteria-determined non-financial services is potentially damaging to the utility derived from the use of microfinance as well as the trust that ought to exist between financial service providers and their clients.

6.4 HOW DO MICROFINANCE CLIENTS PERCEIVE POVERTY, AND WHAT CAPABILITIES DO THEY VALUE AND HAVE REASON TO VALUE?

This section explores service users' perception of poverty as expressed during the interviews. Similar to the approach employed in the *Voices of the Poor* (Narayan et al., 1999), an inductive approach is employed to uncover the dimensions of poverty that the poor value and to capture their perception of poverty. This required that the researcher sets aside her prejudices about what the poor value, and instead capture their values. In line with the conceptualization of poverty in this study, the finding shows that poverty is a multidimensional concept. Service users were specifically asked about their perception of poverty and what they consider to be the characteristics of a poor person. We find that both men and women, young and old, associate poverty with unemployment or the inability to engage in productive activities that can generate income, and the inability to provide basic material household needs.

Especially for the poor, access to a stable wage employment emerged as a key defining factor. As mentioned in chapter 4, whether in urban, semi-urban or rural communities in Nigeria, unemployment remains relatively high; and so is poverty. Particularly for the poor, who can rarely find permanent wage employment, they engage in informal microenterprises with daily wage labour and low earnings. For LAPO clients, the poor are perceived to be 'those who do not have a job'.

*I see the poor as someone that does not have a job (*RESP 7, Female, 43, 1)

> *I see the poor as people who are not productive or hard working* (RESP 23, Female, 35, 7)
>
> *I see the poor as someone who is lazy, or afraid of going into business* (RESP 24, Male, 42, 2)
>
> *Poverty for me is not lack of money. It is a mindset that I cannot do anything that brings in money* (RESP 16, Male, 47, 3).

Some important points evident from these quotes include the struggle for a means of livelihood rather than emphasizing a minimum standard of living. Particularly, it is almost irrelevant what job or business one is engaged in. As long as one is not lazy but bold enough to ‘struggle’ for a means of livelihood, then they are not considered to be poor. Given the absence of a social welfare system and the dearth of basic amenities and social infrastructure in the Nigerian context, the ability to engage in productive activities capable of raising sufficient income to finance the achievement of capabilities is key to escaping poverty. Particularly, given that at least 80% of respondents are married with at least one dependant, the importance of a stable source of income cannot be overstated. Given the subject of interest – microfinance clients, the success of their microenterprise becomes paramount.

This particularly justifies the researchers’ choice to measure poverty reduction as increased ability to achieve successful business outcomes. Given that all LAPO service users already own and run microenterprises of their own, increased capabilities for business profitably can be considered as indicators of poverty reduction as this reduces their vulnerability to poverty. As mentioned in the previous chapter, this study adopts an increased ability to increase business size, introduce new products, reduce cost, develop new business, and increase business asset as indicators of successful business outcomes.

Secondly, poverty is consistently perceived as the inability to provide basic material needs of food, water, clothing, and shelter. This material well-being aspect of poverty is relatively well known. For the poor, it is often a daily struggle to meet basic material need for food, water, clothing and shelter. This becomes acute without a job, or productive land or other sources of income.

> *I don’t see myself as poor because I can pay school fees, rent, cloth my children and provide 3 square meals for my children* (RESP 8, Female, 46, 4)
>
> *When someone cannot feed, clothe and send their children to school that is when you can say they are poor. I don’t see myself as poor* (RESP 12, Female, 46, 2).

> *I see myself as someone who is struggling but not poor because I can cloth my children and pay their school fees*. (RESP 18, Female, 39, 3)

In employing material well-being as a measure of poverty, most studies that employ the individual as the unit of analysis, have focused on the ability of the poor to meet these basic material needs for themselves. However, these quotes show that in the Nigerian context, service users value the ability to provide these basic material needs for their households. This does not imply that the former is not important; but numerous examples of parents going without food in order to feed and clothe their children are well documented in the literature (Narayan et al., 1999). In addition to the traditional basic needs, child education is generally considered to be an important capability that service users' value. Particularly for the poor, an educated child is widely seen as 'hope for a better tomorrow'. Evident in the second quotes is a sense of powerlessness and helplessness. The fact that as a parent, you know the right thing is to provide for your family, but you just cannot do it', is considered to be the major characteristic of the poor. This reinforces the need for the capability approach which emphasizes an increased ability to 'do' and 'be'.

Based on these findings, increased capability at the household level is selected as an important dimension that service users' value. Even for the unmarried and those without children, these service users also value increased material well-being. In selecting indicators for increased ability to meet basic material needs, increased ability to contribute towards household finances, child education, household savings, household assets and household emergencies are selected to proxy increased capabilities at the household level. For instance, increased contribution to household finances is employed as an indicator of increased consumption (food, water, clothing and shelter). Similar indicators have been used in terms of measures of food and non-food expenditure (World Bank Living Standards Measurement Survey). Providing for the household also requires certain household assets such as sleeping beds, cooking items etc. In all, these capabilities are similar to two of the poverty dimensions – material wellbeing (food, asset, work) and social wellbeing (ability to care for, raise, marry and settle children) – selected in the *Voices of the Poor* (Narayan et al., 1999). As with the indicators of increased ability to achieve successful business outcomes, these household indicators are not exhaustive and subject to criticisms and debate. As is common with empirical research, the researcher faced the challenge of selecting measurement tools or proxies. However, the use of the selected household capabilities and business outcomes is justified by their use in other reputable studies (Narayan et al., 1999; World Bank LSMS, 2000).

Although the capability approach emphasizes the individual as the unit of analysis, the poverty reducing effect of microfinance often transcends the individual to the household and business level. Therefore, studies focused on the individual alone, are unable to capture much of the poverty reducing potential of microfinance (Hulme, 2000). Much impact assessments since the late 1990s now ask respondents about increased capabilities at the individual, business and household level (Chen and Dunn, 1996). This study adopts this approach. At the business level, factors such as returns to investment and profitability have been widely used to explore the effects of microfinance. However, it is now widely recognized that with low income households, poor book keeping, the widespread use of loans for non-business purposes and the fungibility of financial resources makes it difficult to separate business from household activities (Zeller et al., 1997). By assessing individual capability increases at the household level, this study addresses the issue of fungibility as loans diverted from the business will most likely end up in the household. Additionally, increased capability at the business level means little except it is positively accompanied by welfare related outcomes. This study therefore retains the individual as the unit of analysis but yet captures the household and business outcomes.

In conclusion, service users' perceptions of poverty place value on a stable source of livelihood, and the ability to meet basic material household needs. In line with the capability approach, service users speak less about income and more about the capability to achieve functionings. One limitation of this approach is that it does not consider the type of employment, the earning capacities of the productive activities or the extent to which these basic material needs are met. For instance, what is the nutritional value of the food provided, what kind of shelter is provided? This however points out the situation in Nigeria where the emphasis is on 'surviving' – meeting the basic necessities and not on the extent to which they are met.

6.5 CONCLUSION

This chapter explored service users experience with the different features of microfinance as well as their implementation processes to identify the potential of these for good or harm. Based on the capability approach to poverty adopted in this study, it also identified the capabilities that service users' value. Beginning with the former, the results confirm the proposition that the various implementation processes and features of microfinance have unique effects on service users with differing potential for good or harm.

As regards group lending, group formation in the LAPO intervention is done based on peer selection as proposed in the literature. Although service users experience showed no exclusion, the criteria for selecting group members as well as the use of individual guarantee to insure risk suggests the possibility of exclusion. This imperfect information about the risk status of peers means that groups start off and remain heterogeneous. With low information levels as well as an implicit understanding amongst service users that loans will more often than not be used to meet some of the multiple deprivations that the poor face, peer monitoring was basically low. While monitoring repayment ability during weekly group meetings was more dominant, monitoring the use of loans was basically non-existent. Heterogeneous groups as well as low monitoring levels suggest that service users are exposed to greater risk of moral hazard. While peer support of business and other welfare related needs enable service users to share ideas and build social networks vital to the success of their businesses and for raising social capital important tool for combating poverty; peer support in terms of financially assisting peers who face repayment challenges often comes at a cost to service users as the supporting client(s) often lose their money as they are often unable to enforce repayment due to incomplete information. Finally, while the threat of social sanction is widely used and relatively potent as regards its usefulness in enforcing repayment, the actual implementation of social sanctions and peer pressure comes at a cost to service users, including damaging social relations. Hence, while we can argue that social capital develops more with successful repayment of loans; this study cannot argue based on the available data that social capital develops more with time. This is beyond the scope of the study and would require more data for its analysis. Hence, the researcher identifies this as an unanswered question and calls for further research to investigate the long term impact of microfinance on social capital.

While the targeting of women fosters the empowerment of women in terms of the increased ability to support the household and greater independence, this as well as the labelling of microfinance as a pro-women initiative might foster the exclusion of the male poor from participation in microfinance. As regards microcredit, the opportunity to consistently access loans with ease despite the lack of collateral is identified as a major source of utility. Yet, the characteristics of microcredit show differing potential for good or harm. First, we find some inconclusive result as regards loan sizes. Non-defaulting clients consider high loans to negatively affect repayment capability while defaulting clients argue otherwise. Even though quantitative findings support the latter, we cannot overlook the fact that service users who experienced repayment difficulty had loan amounts greater than NGN100, 000. With loan use, loans are largely used to meet business and other household needs. This not only represents increased capability to meet household needs but from the service users' perspective, does not come at a cost to repayment ability? Service users widely hold the view that the use of loan does not matter as long as repayment is made when due. Service users unanimously cite short repayment intervals as one of the features of microfinance loans that have the potential to harm clients experience with microfinance. One reason for this been the high repayment burden that comes from the use of dynamic incentive without a corresponding increase in the repayment period. Last but not the least, service users generally consider the interest rate on LAPO loans to be considerably cheap, particularly when compared with other options available to them.

Service users generally consider savings to be beneficial to the expansion of capabilities. Particularly, the opportunity to safely accumulate mandatory savings while making repayments stands out for service users. However, the potential to lose savings due to its use as loan guarantee for default by peers is considered damaging to service users experience. Non-financial services are seen to be beneficial to the expansion of capabilities. However, the obscurity surrounding the access to some of the more criteria-determined non-financial services is potentially damaging to the utility derived from the use of microfinance as well as the trust that ought to exist between financial service providers and their clients.

With regard to identifying what capabilities service users value and have reason to value, the selection of capabilities, In conclusion, service users' perceptions of poverty place value on a stable source of livelihood, and the ability to meet basic material household needs. In line with the capability approach, service users speak less about income and more about the capability to achieve functionings. Firstly, this particularly justifies the researchers' choice to measure poverty reduction as increased capabilities at the business level. Secondly, with the result showing that in the Nigerian context service users value the ability to provide basic material needs for their households, increased capability at the household level is selected as an important dimension that service users' value. In addition to the basic needs of food, water, clothing, and shelter, child education was perceived as a key capability that service users value. In selecting indicators for increased ability to meet basic material needs, increased ability to contribute towards household finances, child education, household savings, household assets and household emergencies are selected to proxy increased capabilities at the household level. Hence, in addition to the 5 indicators of increased ability to achieve successful business outcomes [54], this study adopts 10 capability indicators that microfinance clients value and should value. These indicators remain subject to criticisms and debate.

[54] These indicators as discussed in chapter 5 include: increased ability to increase business size, introduce new products, reduce cost, develop new business, and increase business asset.

CHAPTER SEVEN

MICROFINANCE AND POVERTY REDUCTION

7.1 INTRODUCTION

Having identified the capabilities that microfinance clients' value and have reason to value, this chapter evaluates the effectiveness of microfinance, as well as the role of clients' microfinance practices in the expansion of capabilities. In order to achieve these objectives, this chapter addresses the questions: how effective is microfinance in enabling the expansion of capabilities for the poor? What borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor? As discussed in chapter 3, beyond a client-focused approach to the evaluation of microfinance, client-related practices also dictates the ability of clients to experience poverty reduction. Hence, the evaluation of microfinance should also account for this practices and their effect. In achieving the set objectives, this chapter begins with a descriptive analysis of the quantitative data; providing a general picture of the characteristics of the respondents. The next section evaluates the effectiveness of microfinance in poverty reduction at the business and household levels using frequency tables and cross-tabulations to explore variations across clients' demographics. This is followed by a regression analysis of clients' group and loan practices on one hand and poverty reduction on the other. The final section concludes the chapter with specific attention to providing answers to the questions under review.

7.2 RESULT FINDINGS AND DISCUSSION

Presenting the results begins with a description of the 62 clients for which quantitative data analysis is conducted in this chapter. Drawing from the figures in Table 7.1, we find similar demographics as with the qualitative data. Clients are predominantly self-employed female (75.8%), married (88.7%), traders (75.8%), responsible for at least one dependant, and educated to secondary level (58%) . It is important to mention that all service users including the non-married had at least one dependant or more. This implies that the increase in contribution to child education can be analysed without any required adjustment to the data. As mentioned earlier, these variables are used in exploring variation in the data and as control variables for the OLS and logit regressions.

Table 7.1: Socio-demographic Profile of Quantitative Respondents

Service user characteristics			Frequency	Valid Percent	Cumulative Percent
Age	Valid	< 30	9	14.5	14.5
		31-50	44	71.0	85.5
		>50	9	14.5	100.0
Gender	Valid	male	15	24.2	24.2
		female	47	75.8	100.0
Marital status	Valid	single	7	11.3	11.3
		married	55	88.7	100.0
Number of children	Valid	1-3	40	64.5	64.5
		>3	22	35.5	100.0
Educational level	Valid	< secondary	26	41.9	41.9
		> secondary	36	58.1	100.0
Occupation	Valid	trader	47	75.8	75.8
		service providers	15	24.2	100.0
Spouse occupation	Valid	Not Applicable	6	9.7	9.7
		traders	20	32.3	42.0
		Service providers	20	32.3	74.3
		Skilled workers	16	25.8	100.0
Loan cycle	Valid	1-6		77.4	77.4
		7-12		22.6	100.0

Source: Author’s computations based on primary data collected from LAPO clients
Occupation: Traders include petty traders in food stuff, cloth, drinks, provisions, beauty products etc. Service providers include transporter providers, hair stylists, fashion designers, craftsmen, construction workers, and caterers. Skilled workers include teachers, pensioners, bankers, and civil servants.

7.2.1 HOW EFFECTIVE IS MICROFINANCE IN ENABLING THE EXPANSION OF CAPABILITIES FOR THE POOR?

With an understanding of clients’ characteristics, the next task is to answer the first research question: how effective is microfinance in enabling the expansion of capabilities for the poor? In answering this question, we examine the expansion of capabilities at the household and business level as mentioned in the previous chapter.

7.2.1.1 Microfinance and the ability to achieve Successful Business Outcomes

This section assesses the changes in service users’ ability to achieve successful business outcomes since joining the intervention. As shown in Table 7.2 below, these changes are measured using the three-category ordinal response ‘not at all’, ‘somewhat’, and ‘very much’. As mentioned in chapter 5, five indicators of increased ability to achieve successful business outcomes which microfinance clients’ have reasons to value, were selected. These variables were selected by the researcher based on normative assumptions drawn from the characteristics of microfinance clients, the potential and associated cost of microfinance, as well as the wider economic theory.

Table 7.2: Business Outcomes

BUSINESS OUTCOMES	Not at all (%)	Somewhat (%)	Very much (%)
Increased ability to expand business size	0 (0.0)	11 (17.7)	51 (82.2)
Increased ability to add new product	1 (1.6)	12 (19.3)	49 (79.03)
Increased ability to reduced cost	2 (3.2)	26 (41.9)	34 (54.8)
Increased ability to develop new business	34 (54.8)	21 (33.8)	7 (11.2)
Increased ability to increase business asset	4 (6.45)	29 (46.7)	29 (46.7)

Source: Fieldwork Data (2013)

Regarding service users ability to grow their businesses as a result of joining LAPO, about 82% and 18% of service users say that this has increased 'very much' and 'somewhat' respectively. This implies that all service users have experienced an increase in their business size with the probability of larger increases than small. Further cross-tabular analysis (see Table 7.3 below) of variations in the data shows statistically significant relationship between age and the increase in business size. Service users in the age bracket '31-50' tend to experience more increases in business size. Additionally, one would also expect same for traders as against service providers given that for the latter, increase in business size oftentimes requires some form of training or equipment. This does not appear to be the case; as across both categories of occupation, about 80% of respondents report 'very much' increase in business size. In summary, the results suggest that at a minimum, the use of microfinance allows for an increased ability for business expansion.

Table 7.3: Increased Business size by Age and Occupation

Variables	Categories	Sample Size (%)	Somewhat (%)	Very Much (%)
Age**	< 30	14.5	4 (44.4)	5 (55.6)
	31-50	71.0	5 (11.4)	39 (88.6)
	>50	14.5	2 (22.2)	7 (77.8)
Occupation	trader	75.8	8 (17.0)	39 (83.0)
	service providers	24.2	3 (20.0)	12 (80.0)

Source: Fieldwork Data (2013)
** indicate statistical significance at the 5% significance level

The introduction of new products refers to the addition of other products/services that are oftentimes similar to the present income-generating activity. For example, a hair stylist who has since joining LAPO, begun to sell hair products (hair shampoos, conditioners, moisturizers etc.) in addition to providing hair styling services. This is a common practice and a significant livelihood strategy among the poor, as it enables them to diversify and reduce risk. As mentioned in the qualitative chapter, this is part of the financial education provided by LAPO. This involves identifying seasonal and economic changes and providing advice to service users on possible areas of business diversification. As mentioned in the previous chapter, this also appears to be a major part of the benefits from social capability; the ability of service users to advice one another on new opportunities for business growth and profit. In all, when asked about the ability to introduce new products, 79% and 19% of service users responded ‘very much’ and ‘somewhat’ respectively. For example, a service user involved in catering services, mentioned that since joining LAPO, she has been able to provide event decoration alongside. We find only 1 (2%) respondent who has not introduced new products at all. Further analysis shows that this is however a new client in the first year of joining LAPO and in his first cycle.

Beyond adding new products, occupational or business diversification can also be extended to include developing new business. However, for 55% of clients, the use of microfinance had not in any way led to the development of new business. In all, when asked about the ability to develop new business, 34% and 11% of service users responded ‘somewhat’ and ‘very much’ respectively.

Table 7.4: Develop New Business by Occupation

Variable	Categories	Sample Size (%)	Not at all (%)	Somewhat (%)	Very Much (%)
Occupation**	trader	47 (75.8)	28 (59.6)	18 (38.3	1 (2.1)
	service providers	15 (24.2)	6 (40.0)	3 (20.0)	6 (40.0)

Source: Fieldwork Data (2013)
** indicate statistical significance at the 5% significance level

Further cross-tabular analysis of variations in the data across clients’ demographics shows statistically significant relationship between occupation and the development of new business (see Table 7.4 above). Service providers tend to experience a relatively higher increase in the ability to develop new business than traders. One reason for this can be the ease of entry in trading activities compared to service provision. For traders, developing new business might require the acquisition of new skills. In all, the use of microfinance more likely led to the addition of new products than the establishment of new businesses altogether.

The ability to reduce cost by buying in large quantities or at wholesale prices in order to reduce cost is another capability that has been greatly expanded by service users’ use of microfinance. For example, a service user engaged in the sale of drinks and food provisions reported that as a result of using microfinance, she now buys her stock directly from the wholesalers at relatively lower prices. Given that service users businesses are generally in markets where sellers are price takers, it is almost impossible to increase revenues by increasing prices. Nevertheless, buying in bulk reduces input costs thus increasing profit margins. 97% of service users have experienced a reduction in the cost of doing business. Further cross-tabular analysis of variations in the data across clients' demographics shows statistically significant relationship between clients' age and gender, and the reduction in business cost. As shown in Table 7.5 below, older clients as well as female clients are more likely to experience a reduction in cost. In all, the use of microfinance more likely led to the addition of new products than the establishment of new businesses altogether.

Table 7.5: Reduced Business Cost by Age and Gender

Variables	Categories	Sample Size (%)	Not at All (%)	Somewhat (%)	Very Much (%)
Age**	< 30	9 (14.5)	2 (22.2)	4 (44.4)	3 (33.3)
	31-50	44 (71.0)	0 (0.0)	19 (43.2)	25 (56.8)
	>50	9 (14.5)	0 (0.0)	3 (33.3)	6 (66.7)
Gender**	Male	15 (24.2)	2 (13.3)	8 (53.3)	5 (33.3)
	Female	47 (75.8)	0 (0.0)	18 (38.3)	29 (61.7)

Source: Fieldwork Data (2013)
** indicate statistical significance at the 5% significance level

Finally, we examine the ability to increase business assets resulting from service users' use of microfinance. About 94% of service users are reported to have experienced some form of increase in their business assets as a result of using microfinance.

Table 7.6: Increased Business Asset by Gender, Education, Years in LAPO, and Loan cycle

Variables	Categories	Sample Size (%)	Not at All (%)	Somewhat (%)	Very Much (%)
Gender**	Male	15 (24.2)	2 (13.3)	8 (53.3)	5 (33.3)
	Female	47 (75.8)	0 (0.0)	18 (38.3)	29 (61.7)
Education*	< secondary	26 (41.9)	3 (11.5)	18 (69.2)	5 (19.2)
	> secondary	36 (58.1)	1 (2.8)	11 (30.6)	24 (66.7)
Spouse Occupation**	Not Applicable	6 (9.7)	0 (0.0)	3 (50.0)	3 (50.0)
	Traders	20 (32.3)	4 (20.0)	9 (45.0)	7 (35.0)
	Service providers	20 (32.3)	0 (0.0)	13 (65.0)	7 (35.0)
	Skilled workers	16 (25.8)	0 (0.0)	4 (25.0)	12 (75.0)
Years in LAPO*	1-5	42 (67.7)	0 (0.0)	23 (54.8)	19 (45.2)
	6-10	20 (32.3)	4 (20.0)	6 (30.0)	10 (50.0)
Loan cycle*	1-6	48 (77.4)	0 (0.0)	23 (47.9)	25 (52.1)
	7-12	14 (22.6)	4 (28.6)	6 (42.9)	4 (28.6)

Source: Fieldwork Data (2013)
* and** indicate statistical significance at the 1% and 5% significance level respectively

Further cross-tabular analysis shows statistically significant relationship between the increase in business assets on one hand and clients' gender, education, number of years in LAPO and loan cycle on the other.

As shown in Table 7.6 above, female, more educated clients, clients whose spouses are engaged in more skilled occupation and those with fewer years in the intervention are more likely to experience higher increase in business assets. Similar patterns were observed in Burkina Faso (Mknelly and Kevane, 2002), where female service users during their early years with the intervention invested in productive capacity (improving market stall, buying larger cooking pots, etc.) and thereafter barely invested in asset accumulation.

In all, some noticeable conclusions can be gathered from evaluating the effectiveness of microfinance in enabling successful business outcomes. We find that at the minimum, the use of microfinance engendered poverty reduction at the business level. When we consider the composite business indicator as shown in Table 7.7 below, we find that 35.5% and 64.5% of respondents experience 'somewhat' and 'very much' expansion of capabilities at the business level.

Table 7.7: Composite Business Outcome Indicator

	Categories	Frequency	Valid Percent	Cumulative Percent
Composite Business Outcome	Somewhat	22	35.5	35.5
	Very much	40	64.5	100.0

Source: Fieldwork Data (2013)

This is more likely to arise from a significant increase in the capability to increase business size, add new products (i.e benefit from economies of scale), reduce business cost by buying in bulk, increase business asset and relatively less likely to arise from an increased ability to develop new business.

7.2.1.2 Microfinance and Capability Expansion at the Household Level

Based on the analysis of the qualitative data presented in the previous chapter, five variables were selected to capture the capabilities that microfinance clients' value. These variables mainly evaluate the effectiveness of microfinance in enabling the expansion of individual capabilities at the household level as regards consumption ability, asset accumulation, and empowerment. As with the previous section, we evaluate changes in household outcomes since service users joined the intervention using the three-category ordinal response shown below.

Table 7.8: Capability Expansion at the Household Level

HOUSEHOLD CAPABILITIES	Not at all (%)	Somewhat (%)	Very much (%)
Increased contribution to household finances	0 (0.0)	11 (17.7)	51 (82.2)
Increased contribution to children education	4 (6.5)	12 (19.3)	46 (74.1)
Acquired household assets	4 (6.5)	11 (17.7)	47 (75.8)
Increased ability to handle household emergencies	0 (0.0)	21 (33.8)	41 (66.1)
Increased contribution to household savings	1 (1.6)	22 (35.4)	39 (62.9)

Source: Fieldwork Data (2013)

As regards the ability of microfinance to enable increased contribution to household finances, the all service users affirmed that the intervention had done so; with 82% and 18% reporting ‘very much’ and ‘somewhat’ increase respectively. This is expected as in line with the inclusive finance literature which argues that regardless of the reasons for which loans are given, loans will eventually be spent to satisfy unmet basic needs; service users during the interviews consistently mentioned that, loans were frequently used to meet household needs. Further cross-tabular analysis of variations in the data shows statistically significant relationship between the increase in household finances and clients’ age; with older clients experiencing relatively higher positive outcomes (see Table 7.9 below).

Table 7.9: Increased Household Finances by Age

Variables	Categories	Sample Size (%)	Not at All (%)	Somewhat (%)	Very Much (%)
Age* **	< 30	9 (14.5)	0 (0.0)	4 (44.4)	5 (55.6)
	31-50	44 (71.0)	0 (0.0)	6 (13.6)	38 (86.4)
	>50	9 (14.5)	0 (0.0)	1 (11.1)	8 (88.9)

Source: Fieldwork Data (2013)
*** indicate statistical significance at the 10% significance level

As regards the increased contribution to child education, only 6.5% of service users reported that microfinance had not enabled an increase in their contribution to child education. However, 74.2% and 17.7% reported significant ‘very much’ and ‘somewhat’ increase respectively. This is also consistent with the qualitative finding which identifies child education as the most commonly mentioned non-business use of loans. Further cross-tabular analysis shows statistically significant relationship between increased contribution to child education and clients’ age, occupation and number of years in LAPO (see Table 7.10 below). Particularly, older clients, service providers and clients with longer number of years in the intervention experience relatively higher increased contribution to child education.

Table 7.10: Increase Contribution to Child Education by Age, Occupation & Years in LAPO

Variables	Categories	Sample Size (%)	Not at All (%)	Somewhat (%)	Very Much (%)
Age**	< 30	9 (14.5)	2 (22.2)	3 (33.3)	4 (44.4)
	31-50	44 (71.0)	2 (4.5)	5 (11.4)	37 (84.1)
	>50	9 (14.5)	0 (0.0)	4 (44.4)	5 (55.6)
Occupation*	trader	47 (75.8)	1 (2.1)	12 (25.5)	34 (72.3)
	service providers	15 (24.2)	3 (20.0)	0 (0.0)	12 (80.0)
Years in LAPO**	1-5	42 (67.7)	4 (9.5)	5 (11.9)	33 (78.6)
	6-10	20 (32.3)	0 (0.0)	7 (35.0)	13 (65.0)

Source: Fieldwork Data (2013)
* and** indicate statistical significance at the 1% and 5% significance level respectively

Increase in household assets such as televisions, mattresses, cooking stoves etc., is considered to be an important measure of household wealth and indeed an indicator of the effectiveness of microfinance (Morris and Barnes, 2005). Only 6.45% of service users reported that the use of microfinance did not result in increased acquisition of household assets. The ability to handle household emergencies is considered to be an indicator of clients' resilience to vulnerability and a significant determinant of poverty reduction. All respondents report that since joining the intervention, this has increased; with 66.1% and 33.9% reporting significant and 'somewhat' increase respectively. As regards the ability of microfinance to enable household savings, 98% of service users have experienced an increase to do so since joining the intervention.

Hence, as regards the effectiveness of microfinance in enabling the expansion of household capabilities of the poor, we find that at the minimum, the use of microfinance engendered poverty reduction at the household level. When we consider the composite household indicator as shown in Table 7.11 below, we find that 17.7% and 82.3% of respondents experience 'somewhat' and 'very much' expansion of capabilities at the household level.

Table 7.11: Composite Household Capability Indicator

	Categories	Frequency	Valid Percent	Cumulative Percent
Composite Household Outcome	Somewhat	11	17.7	17.7
	Very much	51	82.3	100.0

Source: Fieldwork Data (2013)

In conclusion, we find that microfinance is an effective tool for poverty reduction. At the minimum, the use of microfinance enables some form of poverty reduction. At the business level, this is more likely to arise from a significant increase in the capability to increase business size and add new products (i.e benefit from economies of scale), and less likely to arise from an increased ability to develop new business. At the household level, this is more likely to arise from significant increases in the ability to contribute to household finances, child education, and household emergencies.

7.2.2 WHAT BORROWER-RELATED MICROFINANCE PRACTICES ARE BETTER ASSOCIATED WITH HIGHER EXPANSION OF CAPABILITIES FOR THE POOR?

Before exploring borrower-related practices, an attempt is made to test the independent variables for multicollinearity (see Appendix C.2). There are two variables ('Loan cycle' and 'Years in LAPO') for which we find correlation values of 0.78. In this case, 'Years in LAPO' was dropped completely from the model. We did find that the loan cycle showed a significant relationship with poverty reduction at the household level. Due to its significance to the model, it was retained as a control variable. As mentioned in the methodology chapter, the small sample size (62 observations) limits the number of explanatory variables that can be included in the models. Hence, the main models which investigate loan and group practices only contain control variables that are found to be statistically significantly related to the dependent variable. Logit regression is employed in analysing the data while OLS regression is employed to check for robustness of the results. As mentioned in chapter 5, the logit regression is a binary outcome model where the dependent variable is typically a binary response taking on values of 0 and 1[55]. It is important to mention that these results do not reflect impact but rather the relationship between the selected client characteristics/practices and poverty reduction.

7.2.2.1 Socio-Demographics

Older, female, and more educated clients are more likely to experience increased ability to achieve successful business outcomes. For each additional age category, clients are 24% more likely to experience increased capabilities at the business level. Female clients are 40% more likely to experience increased capabilities at the business level. For each additional educational category, clients are 22% more likely to experience increased capabilities at the business level. Clients with spouses in more skilled occupations and those in the lower loan cycle are more likely to experience increased capabilities at the household level. At the household level, older clients, clients with spouses in more skilled occupations, and those with lower loan cycles are more likely to experience increased capability at the household level. With the variable 'age', the t-value can be considered to be approximately 0.10 which will indicate

[55] See section 5.5.2.3 for further discussion on the Logit regression model.

statistical significance at the 10% significance level. The significance of 'age' in the marginal effect model supports this argument. For each additional age category, clients are 13% more likely to experience increased capabilities at the household level. Clients with spouses in more skilled occupations are 9% more likely to experience increased capabilities at the household level. For each additional loan cycle, clients are 26% less likely to experience increased capabilities at the household level. Having identified the relationship between clients' characteristics and poverty reduction, we focus on clients practices.

Table 7.12: Logit Regression Coefficients for Poverty Reduction and Socio-demographics[c]

Poverty Reduction at the Business Level [a]			**Poverty Reduction at the Household Level [b]**		
Independent Variables	Logit coefficients	Marginal effects (dy/dx)	Independent Variables	Logit coefficients	Marginal effects (dy/dx)
Age	1.40**	0.24**	Age	1.12***	0.13***
	(0.04)	(0.02)		(0.11)	(0.09)
Gender	2.34*	0.40*	Gender	-0.81	-0.10
	(0.01)	(0.00)		(0.37)	(0.37)
No. of Children	-0.66	-0.11	Education	-1.04	-0.13
	(0.33)	(0.32)		(0.23)	(0.21)
Education	1.28***	0.22**	Spouse	0.76***	0.09***
	(0.08)	(0.05)	Occupation	(0.09)	(0.07)
Occupation	0.66	0.11	Loan Cycle	-2.18*	-0.26*
	(0.42)	(0.41)		(0.01)	(0.00)
Spouse	-0.31	-0.05			
Occupation	(0.43)	(0.42)			
_cons	-7.26**		-cons	3.23	
	(0.02)			(0.23)	
Prob > Chi2	0.01		Prob > Chi2	0.09	
Pseudo R2	0.20		Pseudo R2	0.16	
LR Chi2 (6)	16.38		LR Chi2 (6)	9.46	
N	62		N	62	

Source: Fieldwork Data (2013)
*, **, and *** indicate statistical significance at the 1%, 5% and 10% significance level respectively
[a (b)] Dependent variable is the composite business (household) capability indicator
[c] Based on data constraint, each regression contains client demographics for which earlier cross-tabular analysis suggest a relationship.

7.2.2.2 Loan Practices

While the qualitative chapter provides service users perspectives on what features of loans have the potential for harm or good, this section looks at clients loan practices. As shown in Table 7.13 below, the loan practices explored in this study borders around loan size, use and repayment. Overall, the descriptive statistics shown below suggests that LAPO clients show relatively 'good' loan practices. These are practices that the literature suggests will lead to greater increases in capabilities (see section 3.5).

Table 7.13: Descriptive Statistics of Clients Loan Practices

Variables	Categories	Sample Size (Frequency)
Loan amount	< 80000	48 (77.4)
	80000 and more	14 (22.6)
Non-business use of loan	Yes	38 (61.3)
	No	24 (38.7)
Borrowing outside LAPO	Yes	6 (9.7)
	No	56 (90.3)
Separate business money	No	13 (21.0)
	Yes	49 (79.0)
Repayment difficulty	Yes	15 (24.2)
	No	47 (75.8)

Source: Fieldwork Data (2013)

At LAPO, loan sizes vary with the dynamic incentive strategy. However, service users had the sole choice and responsibility of applying for higher loans after successful repayment of a previous loan. We argue that while higher loan sizes might increase clients' ability to take advantage of bigger investment opportunities, it comes with relatively higher repayment burden. High loan sizes might also lead to an increasing use of loans for non-income generating activities. Although taking loan amounts beyond debt capacity is one of the most cited reasons for default we do not find a statistically significant relationship between higher loan amounts and repayment difficulties, or the use of loan for non-business purposes as shown in the previous chapter.

In line with the objective of this chapter, we test for a relationship between loan amount and the reduction in poverty. Clients with lower loan amounts (i.e < NGN 80,000) and those who are financially disciplined enough to separate business funds from household funds are more likely to experience increased capabilities at the business level. Clients in the higher loan category (greater than NGN80,000) are 30% less likely to experience 'very much' increase in ability to achieve successful business outcomes. The result also rejects the null hypothesis that clients' practice of financial discipline measured by the practice of separating business finance from household finance, has no relationship with poverty reduction. Clients who separate business funds from household funds are 23% more likely to experience 'very much' increase in ability to achieve successful business outcomes. This is one of the financial training provided by LAPO and this result shows positive business outcome.

Table 7.14: Logit Regression Coefficients for Poverty Reduction and Clients Loan Practices

Poverty Reduction at the Business Level			**Poverty Reduction at the Household Level**		
Independent Variables	Logit coefficients	Marginal effects (dy/dx)	Independent Variables	Logit coefficients	Marginal effects (dy/dx)
Age	1.55**	0.23*	Education	-1.72***	-0.18**
	(0.02)	(0.01)		(0.07)	(0.04)
Gender	1.93*	0.29*	Spouse	0.61	0.06
	(0.01)	(0.00)	Occupation	(0.18)	(0.16)
Education	1.18	0.18***	Loan Cycle	-4.45**	-0.47**
	(0.11)	(0.09)		(0.03)	(0.02)
Loan Amount	-2.02**	-0.31*	Loan Amount	1.99	0.21
	(0.02)	(0.00)		(0.25)	(0.24)
Other Use	-0.15	-0.02	Other Use	-2.49**	-0.26**
	(0.84)	(0.84)		(0.03)	(0.02)
Loan Outside	0.76	0.12	Loan Outside	2.96**	0.31**
LAPO	(0.51)	(0.50)	LAPO	(0.04)	(0.03)
Separate	1.52***	0.23**	Separate	0.06	0.01
Business Money	(0.07)	(0.04)	Business Money	(0.95)	(0.95)
Difficulty	0.45	0.07	Difficulty	-0.27	-0.03
Servicing Loans	(0.59)	(0.58)	Servicing Loans	(0.81)	(0.81)
_cons	-7.25*		-cons	4.74***	
	(0.01)			(0.08)	
Prob > Chi2	0.00		Prob > Chi2	0.04	
Pseudo R2	0.28		Pseudo R2	0.28	
LR Chi2 (6)	22.37		LR Chi2 (6)	16.16	
N	62		N	62	

Source: Fieldwork Data (2013)
*, **, and *** indicate statistical significance at the 1%, 5% and 10% significance level respectively

From the qualitative findings, it was apparent that loans were typically used to finance tuition fees for children, household emergencies etc. It has been argued that oftentimes, the poor have basic needs which if unmet, regardless of the reasons for which loans are given; loans will eventually be spent to meet these needs (Rutherford et al., 2013). Similarly, Johnson and Rogaly (1997) consider it a futile task for MFIs to attempt to direct loans to a specific use or try to monitor use. In this study, we also hypothesize that while the use of loans for non-business purposes might improve poverty outcomes at the household level, it comes at a cost to successful business outcomes. As expected, clients who used loan for business purposes only are less likely and those who desist from borrowing outside LAPO are more likely to experience increased capabilities at the household level. The regression analysis discussed above affirms the household poverty reducing potential of non-business use of loans. Compared to those who engaged in the non-business use of loans, clients who use loans for business purposes only are 26% less likely to experience ‘very much’ increase in household capabilities. Additionally, clients who desist from borrowing outside LAPO are 31% more likely to experience 'very much' increase in household capabilities.

7.2.2.3 Group Practices

As shown in figure 3.1 and as argued in the microfinance literature, service users have an incentive to perform peer monitoring and enforcement duties in order to reduce the risk of potential loan defaults (Simtowe and Zeller, 2006; Ghatak, 2000, 1999; Aghion, 1999; and Stiglitz, 1990). This is because by engaging in these practices, service users can monitor loan use, verify the project returns of their peers, mitigate any extra cost arising from joint liability, thus creating a positive effect on poverty reduction and service users overall experience. Hence, we examine these practices and their effect on poverty reduction. It is expected that clients who practice higher levels of monitoring and more stringent enforcement practices will enjoy higher expansion of capabilities due to their ability to mitigate risk. As shown in Table 7.15 below, the group practices explored in this study borders around enforcement mechanisms, ability to know and influence use of loans by peers. The statistics below show low levels of enforcement and monitoring mechanisms.

Table 7.15: Descriptive Statistics of Clients Group Practices

Variables	Categories	Sample Size (Frequency)
Repayment enforcement	Voluntary	43 (69.4)
	Moral suasion	8 (12.9)
	Peer pressure	11 (17.7)
Know use	No	60 (96.8)
	Yes	2 (3.2)
Influence Use	No	15 (24.2)
	Yes	47 (75.8)

Source: Fieldwork Data (2013)

First, the variable 'know use' which measures service users knowledge of loan use by their peers was dropped from the estimation by the statistical software; as less than 5% of respondents reportedly knew the use of loans by their peers[56]. A more advanced level of monitoring will be the ability of clients to engage in practices that can influence the prudent use of loans by their peers. The result shows that clients who are able to influence the use of loans by their peers are more likely to report higher increase in capabilities both at the household and business level. Although the increase in capability at the business level is not significant, we find statistically significant

[56] The logit regression requires that each possible outcome/category should contain at least 5% of the responses.

household results with a 22% more likelihood of increased household capabilities for service users who are able to influence use compared to those who are not. This result could also be interpreted to mean that groups that work better together with higher social cohesion, create a more positive dynamic.

Table 7.16: Logit Regression Coefficients for Poverty Reduction and Clients Group Practices

Poverty Reduction at the Business Level			**Poverty Reduction at the Household Level**		
Independent Variables	Logit coefficients	Marginal effects (dy/dx)	Independent Variables	Logit coefficients	Marginal effects (dy/dx)
Age	1.29**	0.23*	Education	-2.33**	-0.25**
	(0.03)	(0.01)		(0.04)	(0.02)
Gender	1.71**	0.30*	Spouse	1.01**	0.11*
	(0.02)	(0.00)	Occupation	(0.04)	(0.01)
Education	0.81	0.15	Loan Cycle	-2.69**	-0.30**
	(0.23)	(0.21)		(0.03)	(0.01)
Enforcement	-0.38	-0.07	Enforcement	-0.15	-0.01
	(0.39)	(0.38)		(0.79)	(0.79)
Influence Use	0.47	0.08	Influence Use	2.06**	0.22**
	(0.55)	(0.54)		(0.04)	(0.02)
_cons	-6.53		-cons	2.56	
	(0.03)			(0.25)	
Prob > Chi2	0.01		Prob > Chi2	0.01	
Pseudo R^2	0.18		Pseudo R^2	0.24	
LR Chi2 (6)	14.4		LR Chi2 (6)	13.85	
N	62		N	62	

Source: Fieldwork Data (2013)
*, **, and *** indicate statistical significance at the 1%, 5% and 10% significance level respectively

7.2.3 ROBUSTNESS CHECK: PRINCIPAL COMPONENT ANALYSIS (PCA)

As mentioned in chapter 5, the individual capability indicators may contribute different magnitudes to the variation in the dependent variable. Thus, rather than apply equal weights to the different capability indicators as currently done with the previous composite variables, a better approach is to construct a composite indicator that accounts for these different weights and captures the maximum possible information in the original data. This is expected to serve as a robustness check for the estimated logit models. The resulting composite indexes (PCAbusiness and PCAhousehold) constructed using the PCA (see Appendix C2), are analysed using OLS regression. The higher explanatory power of these models support the decision to apply the PCA as it allows us to account for more of the variation in the dependent variables compared to the initial logit models.

At regards clients' loan practices and poverty reduction at the business level; table 7.15 shows similar results to the logit regression. Loan amount is negatively related with poverty reduction. On the contrary, the practice of separating business finances from household finances is positively related with poverty reduction. With poverty reduction at the household level, the OLS result shows consistent result with the logit findings.

Table 7.17: OLS Regression Coefficients for Poverty Reduction and Clients Loan Practices

Poverty Reduction at the Business Level		**Poverty Reduction at the Household Level**	
Independent Variables	Coefficients	Independent Variables	Coefficients
Gender	1.33* (0.00)	Age	0.45*** (0.07)
Education	0.59** (0.04)	Gender	-0.34 (0.26)
Occupation	1.14* (0.00)	Spouse Occupation	0.27** (0.05)
Loan Amount	-0.77** (0.02)	Loan Amount	-0.55*** (0.09)
Other Use	0.07 (0.77)	Other Use	-0.49*** (0.06)
Loan Outside LAPO	0.26 (0.55)	Loan Outside LAPO	0.69 (0.11)
Separate Business Money	0.67** (0.05)	Separate Business Money	0.25 (0.41)
Difficulty Servicing Loans	-0.06 (0.83)	Difficulty Servicing Loans	0.01 (0.95)
_cons	-1.17 (0.28)	-cons	3.36* (0.00)
Prob > F	0.00	Prob > F	0.06
Pseudo R2	0.38	Pseudo R2	0.23
F (8, 53)	4.21	F (8, 53)	1.98
N	62	N	62

Source: Fieldwork Data (2013)
*, **, and *** indicate statistical significance at the 1%, 5% and 10% significance level respectively

The use of loans for business purposes only is negatively related with poverty reduction at the household level. Non-borrowing outside LAPO is positively related with poverty reduction at the household level; although this result is not statistically significant, it confirms the logit findings. However, contrary to the logit results, we find that loan amount is negatively related to poverty reduction at the household level. Although this result is statistically significant compared to the former, there is no obvious empirical explanation for the difference in result.

With regard to group dynamics, table 7.18 below shows that the ability of clients to influence loan use is positively related with poverty reduction at the household level; with an expected 0.53 unit increase in poverty reduction. The OLS results also show similar contradiction as regards repayment enforcement.

Table 7.18: OLS Regression Coefficients for Poverty Reduction and Clients Group Practices

Poverty Reduction at the Business Level		**Poverty Reduction at the Household Level**	
Independent Variables	Coefficients	Independent Variables	Coefficients
Gender	1.30* (0.00)	Age	0.51** (0.03)
Education	0.5*** (0.08)	Spouse Occupation	0.25** (0.05)
Occupation	0.97* (0.00)	Enforcement	-0.15 (0.33)
Enforcement	-0.22 (0.22)	Know use	1.12 (0.13)
Know Use	-0.16 (0.84)	Influence use	0.53*** (0.08)
Influence Use	0.02 (0.94)		
_cons	-0.5 (0.72)	-cons	0.79 (0.53)
Prob > F	0.00	Prob > F	0.05
Pseudo R^2	0.32	Pseudo R^2	0.17
F (6, 55)	4.36	F	2.32
N	62	N	62

Source: Fieldwork Data (2013)
*, **, and *** indicate statistical significance at the 1%, 5% and 10% significance level respectively

7.3 CONCLUSION

This chapter is designed to contribute to the empirical evidence on the poverty-reducing effects of microfinance as well as the role of clients' microfinance practices in poverty reduction. It also allowed us to identify the capability indicators through which these business and household poverty reduction outcomes are mediated. Thus, the analyses tests the effectiveness of microfinance in enabling poverty reduction, the instruments of transmission, as well as the microfinance practices that are more or less likely associated with higher levels of poverty reduction. Based on the conceptualisation of poverty adopted in this study, poverty reduction is examined in terms of increased business and household capabilities considered to be valuable to LAPO clients.

Some noticeable conclusions can be gathered from evaluating the effectiveness of microfinance in enabling the expansion of capabilities. We find that at the minimum, the use of microfinance engendered poverty reduction at the business level; with 35.5% and 64.5% of respondents experiencing 'somewhat' and 'very much' expansion of capabilities respectively. This is more likely to arise from a significant increase in the capability to increase business size, add new products (i.e benefit from economies of scale), reduce business cost by buying in bulk, increase business asset and relatively less likely to arise from an increased ability to develop new business. Service users aged between 31 and 50 who represent the core of the Nigerian labour force are more likely to experience significant increase in business size. We also find that older and female clients are relatively more likely to experience significant reduction in business cost. Service providers are more likely to develop new businesses and benefit from economies of scope. Lastly, female, more educated, service users with spouses in more skilled occupation, those with fewer years in LAPO and fewer loan cycles are more likely to experience an increase in business assets. Similarly, we find that at the minimum, the use of microfinance engendered poverty reduction at the household level; with 17.7% and 82.3% of respondents experiencing 'somewhat' and 'very much' expansion of capabilities respectively. This is more likely to arise from significant increases in the ability to contribute to household finances, child education, and household emergencies. The increased contribution to household finances is significantly higher for older service users. Increased contribution to child education is significantly higher for service users aged between 31 and 50, service providers, and those with more than 6 years in the intervention. In conclusion, we find that microfinance is an effective tool for poverty reduction.

As regards clients loan practices and poverty reduction, clients with lower loan amounts (i.e < NGN 80,000) and those who are financially disciplined enough to separate business funds from household funds are more likely to experience increased capabilities at the business level. At the household level, service users who use loans for non-business purposes and those who desist from multiple borrowing but rather stick to LAPO loans, are relatively more likely to experience increased capabilities. With regard to group practices, the result shows that peer monitoring measured as clients' ability to influence the use of loans is associated with higher increase in capabilities both at the household and business level. Although the increase in capability at the business level is not significant, we find statistically significant household results with a 22% more likelihood of increased household capabilities for service users who are able to influence use compared to those who are not. Nevertheless, it is important to mention that these findings are limited by the relatively small sample size as mentioned in chapter 5. Hence, appropriate care and nuance is necessary in the generalisation of these findings.

CHAPTER EIGHT

CONCLUSION: SUMMARY AND RESEARCH FINDINGS

8.1 INTRODUCTION

For many developing countries, microfinance continues to be considered as a very important instrument for poverty reduction. The widely held assumption is that providing financial services to poor households, enables them to become micro entrepreneurs, accumulate savings, improve their income, smooth consumption, manage risks and eventually escape the vicious cycle of poverty. Yet, there is great controversy as regards the poverty reducing effect of microfinance. Critics argue that microfinance has not improved incomes, but has led to increased indebtedness of the poor, even leading to suicide in some cases (Reed, 2013). A more recent body of literature to which this study is designed to contribute towards is the recent call to approach the delivery and evaluation of microfinance from the clients' perspective and vantage point.

The first is the call for a shift to a client-focussed approach to microfinance following a number of devastating sub-prime microfinance meltdown and the recent client over-indebtedness that rocked the sector (Bateman and Chang, 2012; Sinclair, 2012; Harper 2011 and Klas, 2011). This includes the need to understand the contextual factors that influence the financial behaviour of the poor; which financial services they need; and which financial services benefit them the most, why and for what purposes (Reed, 2013; Maes and Reed, 2012). The second is the increasing evidence from more rigorous randomised control trials (RCTs) that questions the much anticipated positive impact of microfinance on poverty (Banerjee et al., 2009; Karlan and Zinman, 2009; Pande et al., 2012; Stewart et al., 2010, 2012; and Duvendack et al., 2011). These studies call for more empirical studies to investigate the features and characteristics of microfinance that have the potential for both good and harm; and that future research can gain more value by identifying how, and under what circumstances do microfinance interventions benefit the poor.

The third is the call for a wider focus on inclusive finance. This body of work highlights the diverse needs of the poor and calls for a client-focused approach to the evaluation and delivery of microfinance (Bauchet et al. 2011). This is one that accounts for the diverse needs of the poor and recognises that not all products/features will be beneficial to all clients all the time. Additionally, in order to generate improved products and services that flexibly and reliably serve the poor, we need to understand their experiences with the products they are currently exposed to and identify the features and characteristics of microfinance that have the potential for both good and harm. The above review exposes a gap in the literature. This is the need for studies that look beyond impact to investigate the poverty-reducing potential of the features and characteristics of microfinance delivery and use from the clients perspective. Most studies[57] that attempt to investigate the features of microfinance intervention focus on individual components like loan repayment frequency, interest rate, savings and group lending technique. These studies also assess microfinance interventions from the viewpoint of MFIs rather than microfinance users.

This thesis therefore examined the poverty reducing effect of microfinance features, their implementation processes, and clients' microfinance practices, from the service users' perspective. Following a review of the relevant literature on microfinance, and drawing on some theoretical frameworks: the Capability Approach, the Interpretive Approach and the Participatory Poverty Assessment, it addressed this significant problem which has previously not been adequately examined. An analytic and methodological framework was also designed based on the theoretical approaches selected. LAPO microfinance intervention in Edo State, Nigeria consisting of both urban and semi-urban areas whose customs, livelihoods, and language the researcher had wide knowledge of, was selected for the study. This conclusion chapter summarises the thesis, presents the main and statistically significant findings in the study, discusses the limitations and methodological implications of the thesis, and finally presents some areas for further research.

8.2 SUMMARY OF THE THESIS

The introduction chapter presented the research problem that this thesis is designed to address, the justification of the study and its significance, the objectives of the study and the research questions framed to answer them, the methodology, scope and limitations, and finally the conceptual framework of this thesis. Chapter two reviewed the literature on poverty with the goal of identifying an approach to poverty that is relevant for addressing the research problem. This includes a review of three of the most widely used approaches to poverty (monetary, capability, and social exclusion), as well as the unresolved issues in the existing literature. In accounting for the

[57] Stiglitz, 1990; Aghion, 1999; Ghatak and Guinnane, 1999; Marr, 2002; Ahlin and Townsend, 2007; Fischer and Ghatak, 2010

multidimensionality of human life, Amartya Sen’s capability approach to poverty is adopted as a much wider human development approach to poverty. This approach emphasises the reduction of poverty through the expansion of valuable freedoms and therefore places emphasis on identifying and prioritizing the freedoms that people value. Therefore ‘the things that people value and have reason to value’ remained the primary concern in selecting appropriate dimensions; with the resulting research question: what capabilities do microfinance clients in the Nigerian context ‘value and have reason to value’?

Chapter three reviewed some of the recent and relevant literature on microfinance. It reviewed the theoretical literature on microfinance, including the imperfection of financial markets and the implication for the poor, why we need microfinance and how microfinance services are provided. Next, it provided a review of the recent discourses in the microfinance literature, specifically (i) the recent client indebtedness that plagued the microfinance industry, (ii) the growing concern that the perceived positive impact of microfinance has not been realised and (iii) the call for a wider focus on inclusive finance. A review of these debates uncovered a call in the literature for studies that ‘*listen to clients and approach the delivery and evaluation of microfinance from the ‘clients’ vantage point*. Asking: what it is that they are looking for when they utilize financial services? What features of microfinance are beneficial and which are not (Maes and Reed, 2012:1-2)’? With this, a gap in the literature is identified, and the research questions and objectives defined. The research gap is particularly defined as: the need for studies that look beyond impact to investigate the features and characteristics of microfinance delivery and use from the clients perspective. Drawing from the theory of consumer demand proposed by Lancaster (1966), a conceptualization of microfinance which allowed us to account for the features and implementation processes of microfinance; and thus enabled the achievement of the research objective is employed. Overall, this chapter argued that the utility or disutility of microfinance stems from the effect of the different features of microfinance interventions, as well as the use to which microfinance is put.

Chapter four of this study examined poverty and microfinance in Nigeria. With the contextual emphasis in this study, this chapter explored the Nigerian economic and financial background to establish the contextual need and relevance of this study. It particularly described the multidimensional nature of poverty in Nigeria and highlights its significance for the capability approach to poverty adopted in this study. It also established the high level of financial exclusion of the poor, the growing poor population, and the implication of this for the growing size of the Nigerian microfinance industry. In line with the definition and conceptualization of microfinance in this study, LAPO MfB which provides both financial (credit, savings and insurance) and non-financial services to the poor, was adopted in this chapter as the case-study MFI. This chapter discussed the organizational products and services delivered by LAPO and the operational procedures that guide their delivery. It also provided contextual information required to evaluate microfinance features and their implementation processes. This includes information about who LAPO services users are, what services they have access to and use, and how these services are delivered.

Chapter five presented the analytical framework adopted for tackling the research problem. It therefore constitutes the blueprint that guides and informed the rest of the thesis. It adopts the interpretive, capability and participatory poverty assessment approaches as appropriate analytical and theoretical frameworks for addressing the research questions. In line with the selected research approaches, the mixed methods approach is applied to data collection and analysis. The fieldwork exercise through which this is done is justified and described in a reflective fashion; beginning from the selection of the study area and MFI, to the collection of the required data. Yet, due to resource constraint, and the uncertainties and the general lack of order associated with living in developing countries, it was unable to achieve the estimated sample size. In all, 35 and 62 service users were interviewed for the qualitative and quantitative survey respectively. Finally, the rationale for the way the data collection instruments were designed, the questions included, the way they were administered as well as the appropriate data analysis techniques for the qualitative and quantitative data were presented. Very importantly, based on normative assumptions drawn from the characteristics of microfinance clients, the potential and associated cost of microfinance, economic and finance literature as well as the broader Nigerian context, the researcher selects certain business outcomes that microfinance clients should value. This includes an increased ability to increase business size, introduce new products, reduce cost, develop new business, and increase business asset as indicators of increased capabilities at the business level. Further findings in the subsequent chapter justifies the researchers' choice to measure poverty reduction as the increased ability to achieve successful business outcomes.

Chapter six as the first empirical chapter addressed the first two research objectives and their corresponding research questions. This chapter explored service users experience with the different features of microfinance as well as their implementation processes to identify the potential of these for good or harm. Based on the capability approach to poverty adopted in this study, it also identified the household capabilities that service users' value. It answered the questions: What is service users experience with the implementation processes and features of microfinance? How do microfinance clients perceive poverty – what capabilities do they value? Particularly, it explores clients' experience with group lending and women targeting as implementation processes on the one hand and then loans, interest rates, savings and non-financial services as features of microfinance on the other. This chapter is largely a qualitative chapter as it employs data generated from the interviews. Nevertheless, quantitative data sourced from the questionnaire was employed to triangulate the findings. The findings are discussed in the subsequent section.

Chapter seven contributes to the empirical evidence on the poverty-reducing effects of microfinance as well as the role of clients' microfinance practices in the expansion of capabilities. It addressed the last two research objectives and their corresponding research questions. These include: how effective is microfinance in enabling the expansion of capabilities for the poor? What borrower-related microfinance practices are better associated with higher expansion of capabilities for the poor? The analysis of the former is done using frequency tables and cross-tabulations to explore variations across clients' demographics. The latter is done using logit and OLS regressions. It is important to note that this does not constitute an impact analysis. The findings are discussed in the subsequent section.

8.3 SUMMARY OF SIGNIFICANT FINDINGS

This section presents the summary of the research findings by addressing the research questions individually. Insightful and significant findings that contribute to the literature on microfinance are acknowledged; with the broader implications explained.

8.3.1 WHAT ARE THE EXPERIENCES OF CLIENTS WITH MICROFINANCE (FEATURES AND THEIR IMPLEMENTATION PROCESSES)?

The results confirm the proposition that the various implementation processes and features of microfinance have unique effects on service users with differing potential for good or harm. As regards group lending, group formation in the LAPO intervention is done based on peer selection as proposed in the literature. Although service users experience showed no exclusion of the poor, this creates possibility for exclusion of the poor. Further use of trust and personal relations as criteria for selecting group members as well as the use of individual guarantee to insure risk due to imperfect information, supports the possibility of exclusion. This imperfect information about the risk status of peers means that groups start off and remain heterogeneous. This is contrary to the assumption of assortative matching proposed in the literature. With low information levels as well as an implicit understanding amongst service users that loans will more often than not be used to meet some of the multiple deprivations that the poor face, peer monitoring was basically fictional. This finding is contrary to the proposition in the literature that peer monitoring mitigates ex-ante moral hazard (i.e. the use of loan in a way that jeopardises loan repayment). Heterogeneous groups as well as low monitoring levels suggest that even with group lending, service users are exposed to greater risk of moral hazard.

Peer support of business and other welfare related needs enable service users to share ideas and build social networks vital to the success of their businesses and for raising social capital which is an important tool for combating poverty. However, financial assistance to peers who face repayment challenges often comes at a cost to service users as the supporting client(s) often lose their money as they are often unable to enforce repayment due to incomplete information. Finally, while the threat of social sanction is widely used and relatively potent as regards its usefulness in enforcing repayment, the actual implementation of social sanctions and peer pressure comes at a cost to service users, including damaging social relations. These findings therefore make a contribution by showing how group dynamics work in reality and therefore how we should understand group lending. Group dynamics is used in a flexible way by service users who indeed have their own social relationships and ties, and who utilize this collective resource in complex ways – including how people are selected into groups, the use of loans and the decision to monitor or not to monitor loan use, how repayments difficulties are handled, and so on. The reality is highly complex in ways that are only revealed more completely once we actually focus on and listen to what participants are saying.

This study finds that the targeting of women fosters women empowerment in terms of the increased ability to support the household and greater independence. This is similar to findings from Pitt et al., (2003) and Kabeer (1999) who conclude that microfinance enables women to take ownership and control of their own life. However, we find that the labelling of microfinance as a pro-women initiative might foster the marginalisation of male participation in microfinance. This is evident in the existing gender imbalance in group formation and participation; and also consistent with the argument that microfinance is unlikely to challenge the existing gender roles (Hulme and Mosley, 1996). It however shows the social embeddedness of microfinance and in part how well the gender relations around women have been successfully harnessed by providers.

As regards microcredit, the opportunity to consistently access loans with ease despite the lack of collateral is identified as a major source of utility. Yet, the characteristics of microcredit show differing potential for good or harm. First, we find some inconclusive result as regards loan sizes. Non-defaulting clients consider high loans to negatively affect repayment capability while defaulting clients argue otherwise. Even though quantitative findings support the latter, we cannot overlook the fact that service users who experienced repayment difficulty had loan amounts greater than NGN100, 000. With loan use, loans are used to meet business and other household needs. This not only represents increased capability to meet household needs but from the service users' perspective, does not come at a cost to repayment ability? Service users widely hold the view that the use of loan does not matter as long as repayment is made when due. Service users unanimously cite short repayment intervals as one of the features of microfinance loans that have the potential to harm clients experience with microfinance. One reason for this been the high repayment burden that comes from the use of dynamic incentive without a corresponding increase in the repayment period. Last but not the least, service users generally consider the interest rate on LAPO loans to be relatively cheap, particularly when compared with other options available to them.

Service users generally consider savings to be beneficial to the expansion of capabilities. Particularly, the opportunity to safely accumulate mandatory savings while making repayments stands out for service users. However, the potential to lose savings due to its use as loan guarantee for default by peers is considered damaging to service users experience. Non-financial services are seen to be beneficial to the expansion of capabilities. However, the obscurity surrounding the access to some of the more criteria-determined non-financial services is potentially damaging to the utility derived from the use of microfinance as well as the trust that ought to exist between financial service providers and their clients.

8.3.2 How do microfinance clients perceive poverty, and what capabilities do they value and have reason to value?

Service users' perception of poverty places value on: a stable source of livelihood and the ability to meet basic material household needs. Hence, this study measures poverty reduction as an increased ability to achieve successful business outcomes and increase household capabilities. First, especially for the poor, access to a stable wage employment emerged as a key defining factor. Whether in urban, semi-urban or rural communities in Nigeria, unemployment remains relatively high; and so is poverty. Particularly for the poor, who can rarely find permanent wage employment, they engage in informal microenterprises with daily wage labour and low earnings. Given the absence of a social welfare system and the dearth of basic amenities and social infrastructure in the Nigerian context, the ability of individuals to engage in productive activities capable of raising sufficient income enough to finance the achievement of capabilities is key to escaping poverty. For LAPO clients, the poor are perceived to be 'those who do not have a job'. Given that all LAPO service users already own and run microenterprises of their own, increased capabilities for business profitably can be considered as indicators of poverty reduction as this reduces their vulnerability to poverty. Hence, this study adopts an increased ability to increase business size, introduce new products, reduce cost, develop new business, and increase business asset as indicators of successful business outcomes.

Secondly, in employing material well-being as a measure of poverty, most studies that employ the individual as the unit of analysis, have focused on the ability of the poor to meet these basic material needs for themselves. However, this study finds that in the Nigerian context, service users value the ability to provide these basic material needs for their households. This does not imply that the former is not important; but numerous examples of parents going without food in order to feed and clothe their children are well documented in the literature (Narayan et al., 1999). In addition to the basic needs of food, water, clothing, and shelter, child education was identified as a key capability that service users value. In selecting indicators for increased ability to meet basic material needs, increased ability to contribute towards household finances, child education, household savings, household assets and household emergencies are selected to proxy increased capabilities at the household level. Hence, in addition to the 5 business capability indicators mentioned above, this study adopts 10 capability indicators that microfinance clients value and should value. The selection of these indicators remains subject to criticisms and debate.

8.3.3 HOW DO THE POOR ASSESS THE ABILITY OF MICROFINANCE TO SPUR THE EXPANSION OF CAPABILITIES FOR THE POOR?

Some noticeable conclusions can be gathered from evaluating the effectiveness of microfinance in enabling the expansion of capabilities of the poor. We find that at the minimum, the use of microfinance engendered poverty reduction at the business level. This is more likely to arise from a significant increase in the capability to increase business size, add new products (i.e. benefit from economies of scale), reduce business cost by buying in bulk, increase business asset and relatively less likely to arise from an increased ability to develop new business. Service users aged between 31 and 50 who represent the core of the Nigerian labour force are more likely to experience significant increase in business size. We also find that older and female clients are relatively more likely to experience significant reduction in business cost. Service providers are more likely to develop new businesses and benefit from economies of scope. Lastly, female, more educated service users, those with spouses in more skilled occupation, fewer years in LAPO and fewer loan cycles are more likely to experience an increase in business assets. Similarly, we find that at the minimum, the use of microfinance engendered poverty reduction at the household level. This is more likely to arise from significant increases in the ability to contribute to household finances, child education, and household emergencies. The increased contribution to household finances is significantly higher for older service users. Increased contribution to child education is significantly higher for service users aged between 31 and 50, service providers, and those with more than 6 years in the intervention. In conclusion, we find that microfinance is an effective tool for poverty reduction.

8.3.4 WHAT BORROWER-RELATED MICROFINANCE PRACTICES ARE BETTER ASSOCIATED WITH HIGHER EXPANSION OF CAPABILITIES FOR THE POOR?

As regards clients loan practices and poverty reduction, clients with lower loan amounts (i.e < NGN 80,000) and who are financially disciplined (i.e. separate business funds from household funds), are more likely to experience increased capabilities at the business level. At the household level, service users who use loans for non-business purposes and those who desist from multiple borrowing but rather stick to LAPO loans, are relatively more likely to experience increased capabilities. With regard to group practices, the result shows that peer monitoring measured as clients' ability to influence the use of loans is associated with higher increase in household capabilities.

8.4 METHODOLOGICAL IMPLICATIONS OF THE STUDY

Although the capability approach emphasizes the individual as the unit of analysis, the poverty reducing effect of microfinance often transcends the individual to the household and business level. Therefore, studies focused on the individual alone, are unable to capture much of the poverty reducing potential of microfinance (Hulme, 2000). By assessing individual capability increases at the business and household level, this study addresses the issue of fungibility of loans, captures the household and business outcomes of microfinance and yet retains the individual as the unit of analysis. Adopting the CA, IA, and PPA to form the theoretical basis of the research approach, this study adopts a definition and measurement of poverty that allows us to account for the multidimensional needs of the poor and to prioritize those dimensions that matter to them. It also adopts a definition of microfinance that allows us to account for the different features of microfinance and explore their contribution to clients' overall experience. It gives a voice to service users, revealing their experiences with microfinance and exposing what implementation processes or features they find to have negative or positive poverty reducing effects. It also provides empirical insights into those borrower-level factors that are positively or negatively related to poverty reduction.

This study represents a major advancement from previous attempts to evaluate microfinance in Nigeria; particularly in terms of the research approach adopted. For instance, the construction of the questionnaire based on information from the interviews gives us the advantage of employing contextually embedded data. Most studies have employed one method of analysis and even where the mixed method approach is employed, the data is collected independently. Previous studies[58] have been limited to investigating single components of microfinance (e.g group lending, savings, loans), and have therefore resulted in an incomplete understanding and explanation of microfinance interventions. This study goes a step further from these earlier studies and demonstrates that a holistic approach is a more effective way to investigating microfinance interventions. For instance, finding that amongst service users, there is a general perception that loans are often used for non-business purposes as the poor have varying needs and face multidimensional deprivations, helps to explain the low level of peer monitoring at the group level.

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[58] see Stiglitz, 1990; Aghion, 1999; Ghatak and Guinnane, 1999; Marr, 2002; Ahlin and Townsend, 2007; Fischer and Ghatak, 2010; Oni and Adepoju, 2011

The use of both quantitative and qualitative research approaches allows us to effectively articulate and reflect the characteristics of microfinance users, the context in which microfinance interventions operate and their implementation processes. It allows us to account for the heterogeneity in service users, examine clients perspective of the effect of microfinance on poverty as a whole, as well as the effect of the different features of microfinance, and explore why the observed impacts occur. The emphasis on those outcomes which microfinance clients value and have reason to value as well as going beyond clients perception of microfinance as a whole to investigating their experience with the different features of the intervention is a major contribution of this study. This is because clients are more likely to report positive benefits as the poor are very much likely to believe that any service targeted at them is for their own good. Particularly in a country like Nigeria where there is little or no welfare support, any scheme targeted at the poor is highly appreciated.

8.5 LIMITATIONS OF THE STUDY

This study is however faced with certain limitations. Although one aim of the study was to provide generalizable findings about microfinance in Nigeria, due to resource limitation, only one microfinance intervention in 1 out of the 36 states in Nigeria is examined. In a sense, this limits the generalizability of the findings to service users in this intervention. Nevertheless, most MFIs in Nigeria, like LAPO, adopt some form of the Grameen model. There is therefore a strong possibility that these findings will apply to other interventions in Nigeria. The relatively small sample size for both the qualitative and quantitative analysis also represents a major limitation of the study. As applies to studies centred on the capability approach, the decision to explore poverty at the business and household level, as well as the respective capability indicators selected remain an issue for debate. Additionally, the lack of access to repayment, dropout and expulsion rates due to data unavailability is a limitation. Finally, while the focus on clients' perspective can be seen as a strong point of the research, it also represents a limitation as it implies that the study is unable to analyze the supply side functioning in detail. In addition, analysis of client related practices does not cover all the potential sociological and psychological factors that may influence service users' decisions and ultimately affect their poverty reduction experience.

8.6 AREAS FOR FURTHER RESEARCH

The implication of the findings is the need for a greater focus on the contribution of the different features and implementation processes of microfinance, to the expansion of capabilities. Although the Grameen Bank has put to an end the use of joint liability in its intervention, it still remains widely used. With the evidence in this study suggesting that those clients duties (assortative matching, peer monitoring, support and loan repayment enforcement.) which based on joint liability have been argued to not only ensure the sustainability of the MFI but also affect poverty reduction, are either non-existent or have potential damaging effect on poverty reduction, the effect of group dynamics on poverty outcomes begs for further studies. In addition, the heterogeneity in group formation as well as the use of innovative methods by service users to insure risk constitutes a significant finding in this study and requires further research if this is to inform policy. These issues raised could frame the research questions for further studies. Although most studies have focused on women empowerment and microfinance, findings from this study calls for the need to explore the impact on male service users as they are assuming a greater portion of service users.

Most of these findings would remain hidden in an MFI focused study. Hence, more studies need to pay more attention to listening to the experiences of service users and evaluating microfinance from their perspective. There is also the need for comprehensive and contextual studies employing larger sample sizes and covering different MFIs in much wider geographical locations. Further studies can also attempt to develop valid constructs to account for those sociological and psychological client factors as well as the institutional characteristics of MFIs that affect the outcome of microfinance use. This thesis contributes to the literature by giving service users a voice.

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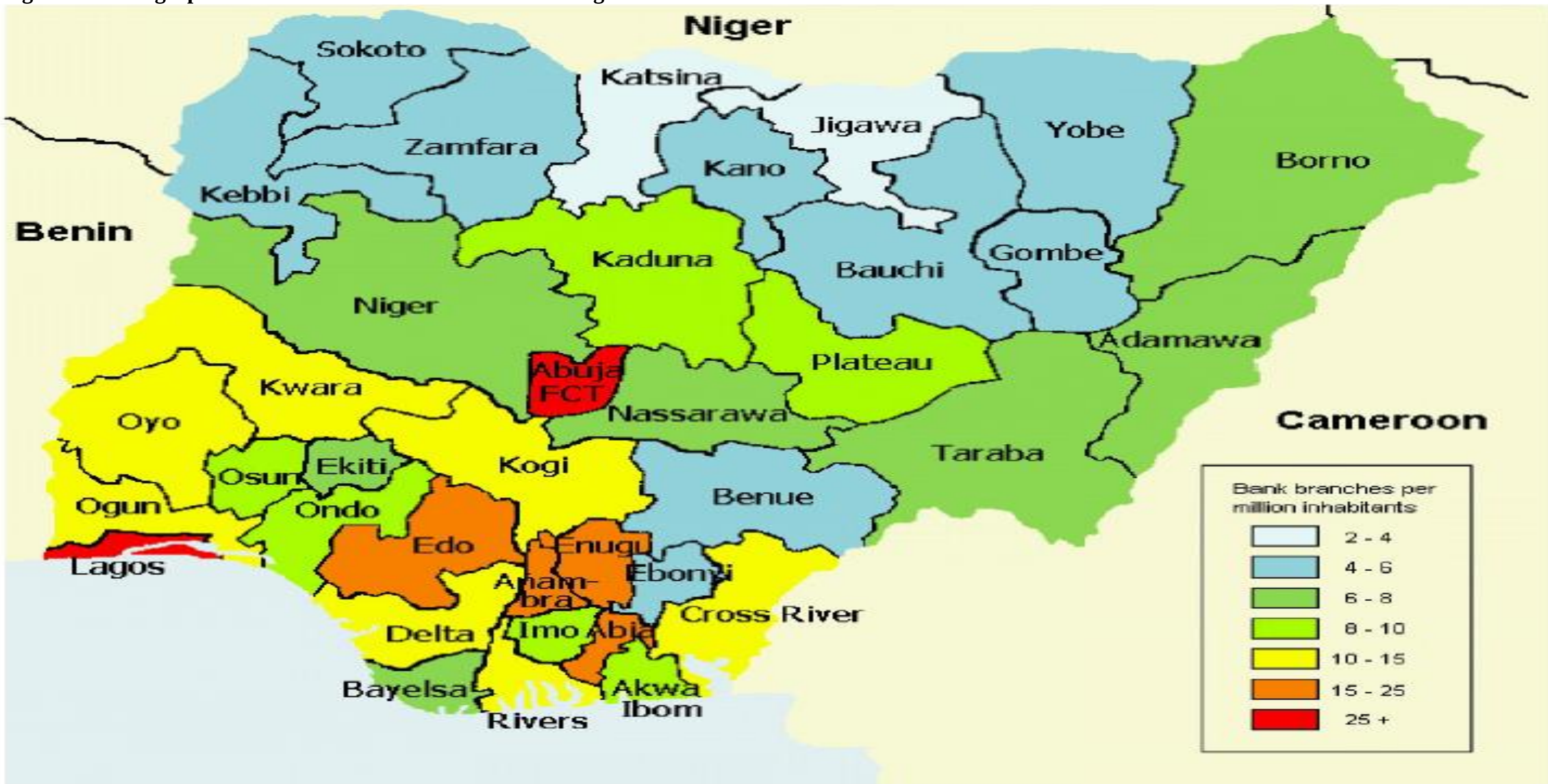
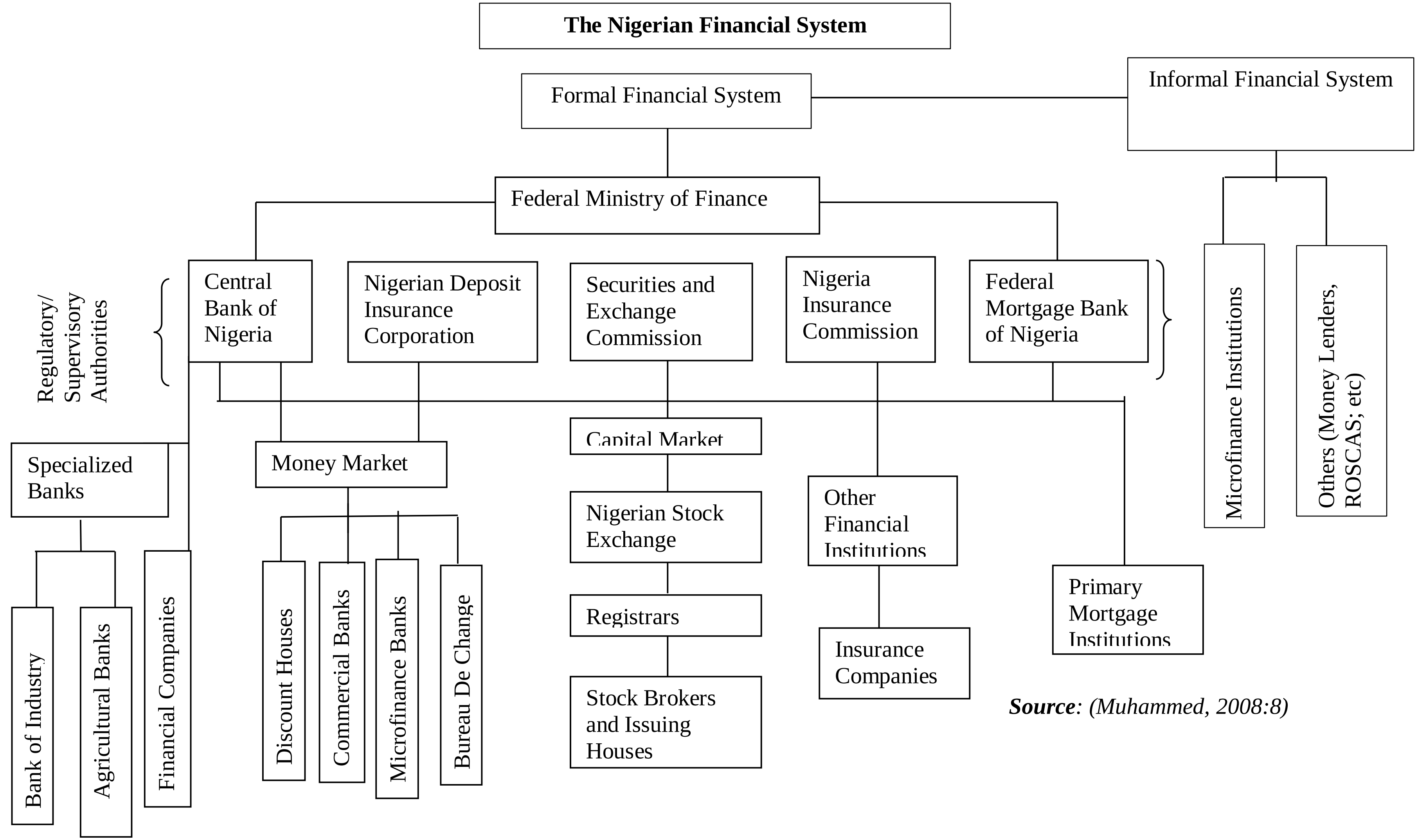
APPENDIX A:

Figure A.1: Geographical Distribution of Bank Branches in Nigeria



Source: EFInA, 2010

Figure A.2: Structure of the Nigerian Financial System



***Source**: (Muhammed, 2008:8)*

Table A.1: Interest Rate on LAPO Loan Products (Amount is in Nigerian currency (Naira))

Description	Reg. loan	Mid-term loan	Agric. loan	SBL	Asset loan	Education loan	Special loan
Minimum loan	10,000	20,000	50,000	50,000	20,000	15,000	15,000
Maximum	150,000	75,000	500,000	500,000	150,000	40,000	250,000
Interest rate	26.4% p.a.	26.4% p.a.	26.4% p.a.	26.4% p.a.	26.4% p.a.	12% p.a.	26.4% p.a.
Methodology	Group	Group	Group / individual	Group / individual	Group	Group	Group
Loan duration	8 months	8 months	1-12 months	1-12 months	10 months	1-8 months	6 months
Collateral	Nil	Nil	Nil	Nil	Nil	Nil	Nil
Grace period	2 weeks	2 weeks	30-60 days	1 month	1 month	1 month	1 month
Fees (loan processing)	1% of loan amt.	1% of loan amt.	1% of loan amt.	1% of loan amt.	1% of loan amt.	1% of loan amt.	1% of loan amt.
Risk premium	Nil	Nil	Nil	Nil	Nil	Nil	Nil
Insurance premium	0.5% of loan amt.	0.5% of loan amt.	3% of loan amt.	0.5% of loan amt.	0.5% of loan amt.	0.5% of loan amt.	0.5% of loan amt.

Source: LAPO (2013)

Table A.2 Comparative pricing analyses of perceived strong LAPO competitors

S/N	Product/ Services	SEAP	ACCION	AB	Grooming Centre	TrustFund	LAPO
1	Interest on loan products	18% per annum (1.5% per month)	72% per annum (6% on a 6-monthly basis)	54% pa (4.5% per month)	13% per annum (1.08% per month)	3% per month	26.4% per annum (2.2% per month)
2	Interest on savings	NA*	2% per annum	4% per annum	NA*	2%	2% per annum
3	Interest premium or risk premium	#500 or 1.6%	1%	NA*	#600 or 1.8%	Nil. In the event of default guarantor pays	0.5% per loan amount
4	Loan duration	40 weeks	24weeks	At least 3 months	23 weeks	4 months	30 weeks
5	Registration / participation fees	#1100	NA*	NA*	Nil	1000	Nil
6	Loan application fees	#200	NA*	NA*	Nil	800	Nil
7	Loan processing fees	NA*	2.5% of loan amount	2.5% of disbursed amount	Nil	4% of the disbursed amount	1% of loan amount disbursed
8	Initial deposit	10% of disbursed amount	20% of disbursed amount	NA*	10% of disbursed amount	Nil	5% of the disbursed
9	Other charges	NA*	NA*	NA*	Nil	Nil	Nil

* NA means not available or not disposed to investigating officer
Source: Research Unit, LAPO Academy (2013)

Table A.3: Overview of LAPO Savings Products

Types of savings product	Methodology (group/individual)	Savings deposit size (minimum/maximum)	Interest rate	Duration/ Withdrawal	Fees/ charge
Regular savings	Group	About N100-400 (Naira) per week or monthly respectively.	2% p.a.	At any time	Nil
Savings plan	Individual	N500-10,000 (Naira) week/monthly	3%-6% p.a.	3-12 months	Nil
Union (Voluntary) savings	Group and Individual	N100 and above	2% p.a.	At any time	Nil
Union Purse savings	Group	500 at deposit	2% p.a.	At any time	Nil
My Pikin Savings	Group and individuals	200 and above weekly	2% p.a.	At any time	Nil
Term deposit	Individual	30,000 and above	6%-14% p.a.	At any time	Nil
Individual savings	Individual	1000 and above	2% p.a.	At any time	Nil

***Source**:* LAPO (2013)

APPENDIX B: QUALITATIVE INTERVIEW GUIDE

A. Background and Personal Information

1. ____

First Name **Surname**

2. Age: less than 21 ( ), 21-30 ( ), 31-40 ( ), 41-50 ( ), 51-60 ( ), more than 60 ( )
3. Gender: Male ( ), Female ( )
4. Marital Status: single ( ), married ( ), divorced ( ), widow/widower ( )
5. Number of Children (dependent children/wards): 0 ( ), 1-2 ( ), 3-4 ( ), 5-6 ( ), 7-8 ( ), more than 8 ( )
6. Level of Education: none ( ), primary school ( ), secondary school ( ), tertiary ( ): other (specify) ……………………………………

7a. Occupation: ……………….……… 7b.Occupation of Spouse: ……………….

8. Type(s) of business(s): ……………………..………………………………..

9. Time (year) joined scheme (number of cycles): …………………….……

B. Experience of Service Users

Introduction: I would now like to you ask you about your experience with the service you received from LAPO microfinance. Firstly:

Accessing the service

1. Did you contact LAPO, or did they contact you?
    - When was this?
    - If they contacted the service provider - How did you find out about LAPO? e.g. media, word of mouth, from another agency, looked them up
2. Why did you decide to contact LAPO/decide to take up their offer?
    - any particular issues you were concerned about - why

Service delivery

1. How did LAPO provide the service to you - was it a one-to-one meeting, a group workshop, or something else?
    - Was this your preference, or would you have preferred something different?
2. How many times have you had contact with them, was it several times, or just once?
    - Have you received any follow up support?
    - When was their first contact and most recent contact
3. How would you describe the person(s) you saw/spoke to – how knowledgeable, helpful, approachable were they?

Did they give you information/advice/help with anything else e.g.

- advice on money management and budgeting
- debt advice
- how to get affordable loans and credit

- saving and savings accounts

4. What help/advice/service did you receive from LAPO?

Probe fully –

- what information did you provide to them
- what information/advice was given to you
- what action was suggested
- How useful was the help/advice/service you received from LAPO – why (not)?
    - what was most useful
- Are there any ways in which the help/advice/service you received from LAPO could have been better?
    - what would you want to change
    - what would be helpful

5. Did the service meet your needs/expectations – why (not)?
6. Would you use LAPO again - why (not)?
7. What do you think would have happened if you hadn't received the help/advice/service you received from LAPO? What alternative options would you have had? Probe as appropriate e.g.:
    - none/would have gone without
    - friends/family
    - using more expensive alternatives/products e.g. high interest credit
    - another organisation(s) providing a similar service

C Access to and use of financial services

Introduction: I would now like to ask you some questions about your use of financial services.

In terms of the financial services that are available to you locally, do you have: [ask of those not already discussed]

- a local bank branch
    - have you used it in the last 6 months
    - what types of account do you have e.g. basic bank account, savings account
- a local Credit Union
    - are you a current member, what services do you use e.g. loans, savings account
    - if not, is this something they would like to have/be a member of
- a doorstep lending service (Esusu/Olidara)
    - have you used it in the last 6 months – probe for details
    - if not, is this something they would like to have/use
- Do you currently have any of the following types of credit?

- loan from a bank/building society
- loan from friends or family
- loan from other lender
- other

- Are there any types of credit you would like to have but have not been able to get – probe for details

D Household finances

Introduction: Do you mind if I ask you some questions about your household finances?

What is your main source of household income?

Do you have money coming in to the house from any other sources?

- Earnings from employment (own or partner‟s)
- Benefits (including state pension)

In general how would you describe your current financial situation, would you say you:

- are getting by ok and are able to save money
- are just getting by, but don‟t have any money to spare
- struggle to make ends meet
- have problematic debts and arrears

E. Specific Features

Group Lending

- How did you become a member of your group?
- How long have you been together? (Probe: how is group sustained? dropouts?)
- What is the relationship between your group and the institution?
- What change(s) will you like to see in your group?
- What do you particularly like about your group?

Targeting Women

- What is your opinion about targeting women only?
- To what extent has access to financial services influenced your relationship with spouse, members in the community, etc?
- What do you like about being targeted as a woman? (what don‘t you like?)

Interest Rates

- What is the interest rate charged/given on loan/savings? What is your opinion about that?
- Do you borrow money from elsewhere? If yes, how does it (interest rate) compare with what is charged elsewhere?

Loans

- How do you describe access to credit facilities? (probe: easy, competitive, complicated, rationed etc).

- What features do you require in a loan? (explain: convenience, proximity, size, promptness,
- How important are loans to you?
- What is your repayment experience?
- What have you primarily used the loan(s) for? (seek clarification for multiple use for different cycles).
- Is that what you intended to use loan(s) for? If not, what is the reason?

Savings

- Which savings facilities do you use?
- Which one do you prefer, voluntary or compulsory and why?
- What do you like about savings facilities offered?
- What will you like to change if you had a chance?

Non-Financial Interventions

- Apart from financial services, **can you identify** other services that the institution offers? (Probe: offers training on group activities, setting up business, technical advice?). If any, how helpful were they?
- Did you have any non-financial services from the institution? (explain) If yes. What were they?
- What non-financial services will you like the institution to provide and why?

F. Finally

In your opinion what is poverty?
What are the characteristics of a poor person? To you as a LAPO client, what is it that if you cannot do, will make you consider yourself to be poor?
How will you describe the status of your household before you joined the intervention?
Are there any changes in your household that can be attributed to the intervention?

THANK YOU FOR YOUR TIME

Can I give you a ring if there is anything we need to clarify later?

APPENDIX C: QUANTITATIVE QUESTIONNAIRE

A. Background and Personal Information

1. ____

First Name **Surname**

2. Age: less than 21 ( ), 21-30 ( ), 31-40 ( ), 41-50 ( ), 51-60 ( ), more than 60 ( )

3. Marital Status: single ( ), married ( ), divorced ( ), widow/widower ( )

4. Number of Children (dependent children/wards): 0 ( ), 1-2 ( ), 3-4 ( ), 5-6 ( ), 7-8 ( ), more than 8 ( )

5. Level of Education: none ( ), primary school ( ), secondary school ( ), tertiary: other (specify) ……………………………………

6a. Occupation: ………………….………. 6b.Occupation of Spouse: …………

7 Type(s) of business(s): ……….…………………………………………………

8. Time (year) joined scheme (number of cycles): …...…………………..……

B. Group Activities and Dynamics

9. What is the name of your group? ……………………...……..……………

10. How was your group formed? …………………………..…...………………

11. How many members are in your group? ….………………...……………..……

12. How do you enforce repayments? …………..…………..………...

13. Do you know how other group members use their funds? **No** ( ), **Yes** ( ) (please explain)……………………….……………………

14. Are you able to influence other members in the proper use of funds? **No** ( ), **Yes** (please explain)…………………..…….……………………….

C. Lending and Interest Rates & Perception of MFI

15. Amount of last loan: ……..………………………….

16. Do you (sometimes) use loans for other purposes? (such as paying school fees, hospital bills etc): no ( ): yes ( ): other(specify)…........................………….

17. Do you borrow from other sources?: yes ( ): no ( ). If yes, what source (s)……

18. Do you keep your business money separate from money for personal or household expenses?

19. Have you encountered any difficulty in servicing your loans?: no ( ): yes ( ): other (specify) ………………………………………………………………

D. Non-financial Interventions

20. Do you make use of any non-financial services provided by the scheme?:……

21. If any, how will you describe these non-financial services? beneficial ( ); not beneficial ( ); other (specify) …………………………………………..............

E. Effect on Business

How has your participation in the scheme enabled you to do the following	Very much	Somewhat	Not at all	Other (specify)
Expand business size				
Add new products				
Reduce costs by buying in greater volume or at wholesale prices				
Develop new businesses				
Increase business assets				

Effect on Household

How has your participation in the scheme enabled you to do the following	Very much	Somewhat	Not at all	Other (specify)
Contribute/increase contribution to household finances/income				
Contribute/increase contribution to education of children				
Contribute to the acquisition of household assets				
Increase the ability to cope with household emergencies				
Increase household savings				

Table C.1: Correlation of the Predictor Variables

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)
Age	1.00																	
Gender	0.13	1.00																
Marital Status	0.00	-0.08	1.00															
No. of Children	0.25	0.10	0.26	1.00														
Education	-0.24	-0.09	-0.09	-0.12	1.00													
Occupation	-0.13	-0.38	0.08	-0.02	0.09	1.00												
Spouse Occupation	-0.12	0.08	-0.07	-0.24	0.42	-0.04	1.00											
Years in LAPO	0.38	0.14	0.02	0.13	-0.11	-0.06	0.03	1.00										
No. of loan Cycle	0.35	0.03	-0.05	0.00	-0.16	-0.03	-0.01	0.78	1.00									
Loan Size	0.21	-0.05	0.19	0.00	0.06	0.05	0.11	0.61	0.53	1.00								
Other use of loans	-0.06	0.13	-0.03	-0.10	-0.26	0.01	-0.19	-0.33	-0.19	-0.03	1.00							
Loan outside LAPO	0.20	0.06	0.22	0.01	-0.05	-0.06	-0.12	0.22	0.17	0.17	0.14	1.00						
Separate business money	0.00	0.07	0.19	0.05	0.12	-0.26	0.02	0.01	-0.10	0.27	0.00	-0.03	1.00					
Difficulty repaying	-0.27	-0.23	0.03	-0.21	0.20	0.05	0.08	-0.41	-0.23	0.03	0.06	0.06	0.07	1.00				
Repayment enforcement	0.15	-0.22	-0.04	-0.02	-0.26	0.13	-0.04	0.32	0.40	0.45	-0.02	-0.00	0.11	-0.03	0.07	1.00		
Know use	0.16	0.10	0.06	0.05	0.15	0.11	-0.15	0.26	0.11	0.33	0.04	0.05	0.09	-0.11	0.04	0.12	1.00	
Influence use	-0.27	-0.14	-0.20	-0.36	0.13	0.05	0.12	-0.17	0.12	-0.05	-0.09	-0.05	-0.10	0.20	-0.14	-0.13	-0.32	1.00

Source: Authors own computation

PRINCIPAL COMPONENT ANALYSIS (PCA) CONSTRUCTION

The goal of the PCA is to reorganise the data so that many of the original variables can be summarised with very few components that capture maximum possible information on the variation in the variables. With regard to the business capability indicators, table 1 below shows significant correlation between some of the variables which justifies the use of PCA.

Table 1: Correlation of Business Outcome Indicators

	SIZE	Nproduct	Rcost	newBIZ	BIZasset
Business Size	1.0000				
New Product	0.7901	1.0000			
Reduced Cost	0.4276	0.3936	1.0000		
New Business	-0.0486	-0.0050	0.2487	1.0000	
Business Asset	0.3080	0.3291	0.4305	0.3047	1.0000

Source: Author's computations based on primary data collected from LAPO clients

The eigen values for the original business outcomes are reported in table 2 below. The first component explains 48 percent of the variation in the data. The second and third components explain an additional 25 percent.

Table 2: Principal Components, Eigen Values and Proportion of Variance Explained

Component	Eigenvalue	Difference	Proportion	Cumulative
Comp1	2.3972	1.1434	0.4795	0.4795
Comp2	1.2538	0.6672	0.2508	0.7302
Comp3	0.5866	0.0303	0.1173	0.8476
Comp4	0.5562	0.3503	0.1113	0.9588
Comp5	0.2059		0.0412	1.0000

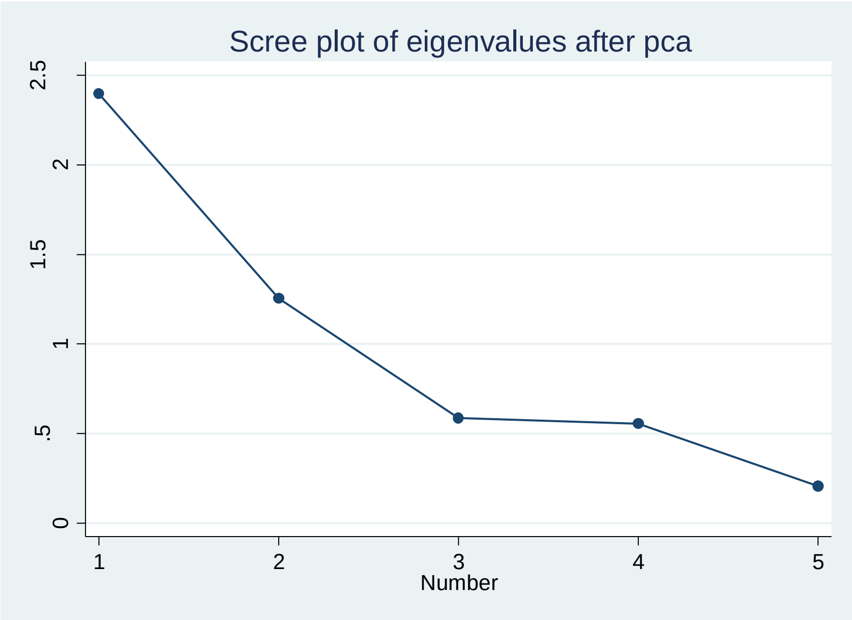
Principal components loadings (eigenvectors)

Variable	Comp1	Comp2	Comp3	Comp4	Comp5	Unexplained
Business Size	0.5352	-0.3710	0.2223	0.0979	0.7190	0
New Product	0.5350	-0.3394	0.2699	0.2288	-0.6880	0
Reduced Cost	0.4728	0.2197	-0.1509	-0.8363	-0.0780	0
New Business	0.1560	0.7459	0.6234	0.1666	0.0533	0
Business Asset	0.4236	0.3775	-0.6829	0.4592	0.0281	0

Source: Author's computations based on primary data collected from LAPO clients

In all, the first 2 components explain about 73 percent of the variation in the data. Next, the component loading tells us the correlation between the original variables and the components.

Figure 1: Scree plot of Business Outcomes Eigenvalues



In deciding how many components to retain for the analysis, the Kaiser rule states that we retain components with eigen values above 1. Based on table 2 above, we retain the first 2 components with eigen values greater than 1. With 2 components, we are able to explain at least 60 percent (Reduced cost) and at most 86 percent (Business size) of the variation in the variables (see table 3 below). Usually, for simplicity of analysis and interpretations, components are

Table 3: Principal components loadings (eigenvectors)

Variable	Comp1	Comp2	Unexplained
SIZE	0.5352	-0.3710	0.1408
Nproduct	0.5350	-0.3394	0.1693
Rcost	0.4728	0.2197	0.4037
newBIZ	0.156	0.7459	0.244
BIZasset	0.4236	0.3775	0.391

Source: Author's computations based on primary data collected from LAPO clients

The PCA score for each observation is constructed as:

Score1 = .5352SIZE + .5350Nproduct + .4728Rcost + .1560newBIZ + .4236BIZasset

Score2 = - .371SIZE - .3394Nproduct + .2197Rcost + .7459newBIZ + .3775BIZasset

Thus, the PCA index for each observation is constructed as **Score1 + Score2.** At the household, the PCA index is calculated using the relevant household components.

In constructing the household PCA index, we also find significant correlation between the variables as shown below.

Table 4: Correlation of Household Capability Indicators

	FINANCES	CHeducation	ASSETS	EMERGENCIES	SAVINGS
FINANCES	1.0000				
CHeducation	0.4620	1.0000			
ASSETS	0.4789	0.1812	1.0000		
EMERGENCIES	0.4705	0.3021	0.4994	1.0000	
SAVINGS	0.4670	0.1717	0.5659	0.8449	1.0000

Source: Author's computations based on primary data collected from LAPO clients

With regard the components, we find that the first 2 principal components explain about 76 percent of the variation in the data.

Table 5: Principal Components, Eigen Values and Proportion of Variance Explained

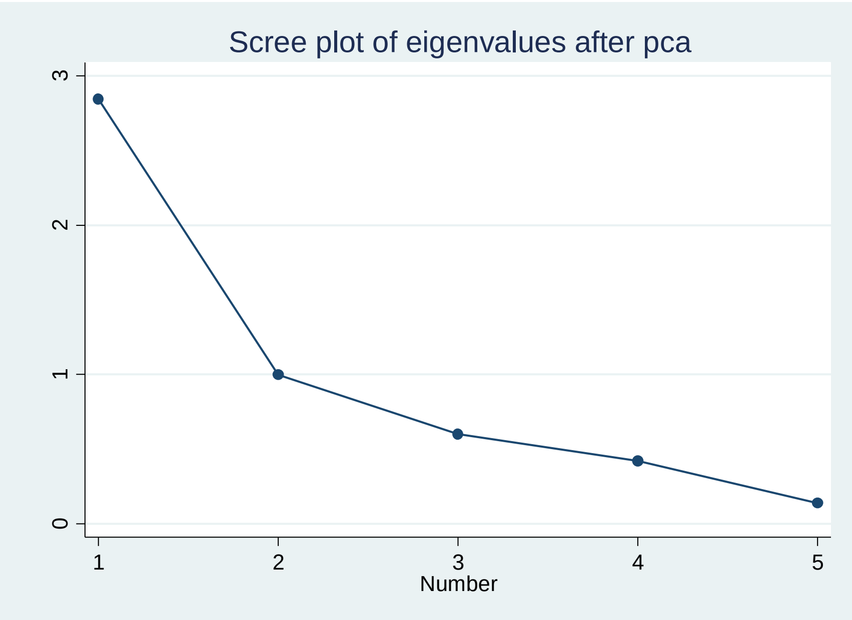
Component	Eigenvalue	Difference	Proportion	Cumulative
Comp1	2.8439	1.8463	0.5688	0.5688
Comp2	0.9975	0.3969	0.1995	0.7683
Comp3	0.6006	0.1812	0.1201	0.8884
Comp4	0.4193	0.2807	0.0839	0.9723
Comp5	0.1385		0.0277	1.0000

Principal components loadings (eigenvectors)

Variable	Comp1	Comp2	Comp3	Comp4	Comp5	Unexplained
FINANCES	0.4466	0.3567	0.3652	-0.7333	-0.0466	0
CHeducation	0.2869	0.8054	-0.2494	0.4336	0.1370	0
ASSETS	0.4400	-0.2069	0.6978	0.5199	-0.0798	0
EMERGENCIES	0.5140	-0.2212	-0.4759	0.0115	-0.6784	0
SAVINGS	0.5104	-0.3637	-0.3017	-0.0618	0.7158	0

Source: Author's computations based on primary data collected from LAPO clients

Figure 2: Scree plot of Household Eigenvalues



2 out of the 5 components have eigenvalues close to or above 1. This means that these components explain at least as much of the variation as the original variables. The component loadings reported below represent the correlation between the components and the original variables. These loadings suggest high correlation as 8 out of 10 of the estimated values are above 0.3 and below -0.3.

Table 6: Principal components loadings (eigenvectors)

Variable	Comp1	Comp2	Unexplained
FINANCES	0.4466	0.3567	0.3059
CHeducation	0.2869	0.8054	0.1188
ASSETS	0.4400	-0.2069	0.4067
EMERGENCIES	0.5140	-0.2212	0.1999
SAVINGS	0.5104	-0.3637	0.1273

Source: Author's computations based on primary data collected from LAPO clients

The table below shows the Kaiser-Meyer-Olkin (KMO) measure of sampling adequacy. With values greater than 0.5, we can confirm that the individual capability variables have a lot of redundant information in them; thus warranting the PCA.

Table 7: Kaiser-Meyer-Olkin (KMO) measure of sampling adequacy

Business Capability Indicators		**Household Capability Indicators**	
Variable	**kmo**	**Variable**	**kmo**
Business Size	0.5987	Household Finances	0.7706
New Product	0.6159	Child Education	0.5656
Reduced Cost	0.7831	Household Assets	0.8474
New Business	0.5464	Household Emergencies	0.6532
Business Asset	0.7575	Household Savings	0.6306
Overall	0.6524	**Overall**	0.7234

Source: Author's computations based on primary data collected from LAPO clients