

*Address by Kevin McCort, President and CEO of CARE Canada
to Queen's School of Business Alumni
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Good evening,

I hope you enjoyed the video – it refers to the theme of power, and tonight I'll be speaking primarily about financial empowerment of the poor, mainly women, how we do it, and why it is so important. There are many aspects of CARE that I could speak to, but this theme seems particularly apt, given the audience and current events.

In the précis I prepared for this talk about "[Climbing the economic development ladder](#)" I wrote that "You can't simply dump a western market system on a developing society and expect it to work for the most needy and vulnerable." I prepared that summary before the recent chaos in the financial markets – and it now looks like you can't always expect a Western market system to work here either!

The sub-prime crisis essentially started with the practice of extending credit to people whom, in hindsight, should not have received loans. They were not able to handle the debt, and once they started to default, the whole system has been shaken to its core.

CARE understands the economics of poverty, as we make it our business to work with poor people in economically viable ways, and one of the first essential steps is starting with savings, not debt. Akin to the first step on a ladder, savings is where you start.

You can climb from there, moving from rotating savings/lending groups to microfinance, where small sums are borrowed to expand businesses or cover seasonal expenses. Most activity in this realm is in the informal market and relatively small scale. Benefits accrue mostly at the family level.

For some, the next step on the ladder is creating formal enterprises, still small, but approaching 'medium sized' status with employees, contracts and even "brand". In many developing countries, these businesses are under-capitalized and under-developed and excluded from most financial markets. The result is the power of the small and medium sized enterprises sector to create jobs and wealth remains untapped.

I'll explain tonight how CARE is helping to build sustainable, resilient economies in some of the most unstable environments you can imagine. We work at all of the three steps of the ladder I've outlined, ultimately enabling people and businesses to create and participate in the type of economy that most of you would recognize.

I'll also draw recommendations from our experience that the new Government must consider when crafting its aid policy, paying special attention to Africa.

First though, why should anyone listen to what CARE has to say? Our bona fides then, starting with our history and focus:

- established in 1946, we created the concept of the “CARE Package” through our relief programs to post-world war II Europe;
- we’ve evolved into an organization focused on poverty elimination, but with an equally strong commitment to humanitarian work;
- we focus on the poorest which means CARE works mostly with women. Our programs disproportionately involve women and for a host of good reasons.

Next our actual reach, depth and expertise:

- we have over 15,000 staff worldwide, working in nearly 70 countries;
- CARE Canada manages 3,000 of these staff, and spends an average of \$150m on our programs every year;
- We are the Canadian International Development Agency’s largest partner NGO, 2nd largest partner of the World Food Program and are among the top partners of the United Nations Refugee Agency (UNHCR);
- Board members include Hon. John Manley, Prof. Janice Stein (UofT), Dr. Martha Piper (former Pres. UBC), Denis Desautels (former Auditor General) and Madame Louise Frechette (former UN Deputy Secretary General).

We know what we are doing, and we are efficient. 95% of our expenditures are directly related to our programs, thanks to our ability to use relatively modest amounts of private funding to leverage substantial institutional funds. We regularly use a donated

dollar to generate a further \$10 to \$15 in programs. So if you like what we do, make a donation and we'll do even more of it!

Although CARE works in every part of the developing world, and we apply our economic development programs everywhere, tonight I'm going to focus on Africa. Here's why.

One of the most successful financial interventions in poor countries is microfinance, yet this is largely undeveloped as a sector in Africa. Many of you are familiar with this concept, thanks to the Grameen Bank and Mohammed Yunus, winner of the Nobel Prize for his pioneering work in this field. Latin America and Asia are home to flourishing microfinance industries, yet Africa remains largely untouched. Why is that? And what can CARE do about it?

First, some of the factors contributing to the underdeveloped financial sector in Africa drawn from our research on the subject:

- The vast majority of the poor still lack access to even the most basic financial services. A total of 725 million people live in sub-Saharan Africa, 75 per cent of them on less than two dollars a day. This means almost 550 million people, or over 100 million households, living in poverty. The poor lack access to financial services partly because of vastly underdeveloped financial sectors: in countries like Ethiopia, Uganda and Madagascar, the ratio of bank branches to people is

less than 1:100,000 compared to a ratio greater than 50:100,000 in some developed countries.

- Population density (or rather the lack of it) also impedes access to financial services in sub-Saharan Africa. While in Bangladesh there are 985 people per square kilometer, and in India 336, Kenya reports a population density of 59, Niger has 11, and Gabon a mere 5.2 people per square kilometer. Non-African countries with similarly low population densities, such as Kazakhstan and Belize, have correspondingly low level of access to financial services. Low population density and poor infrastructure increase the costs of delivering even the most basic financial services to consumers. These factors also limit the ability of consumers to productively use financial services, as they have limited access to markets.
- Socio-cultural factors also impact access to financial services in Africa, including: cultural norms, class and caste systems and historic exclusion of minorities; language barriers; gender bias; age bias; challenges of verifying legal identity; the false perception of many African bankers that the poor are not creditworthy; and chronically low and falling education levels.
- Finally, doing business in Africa is hard work. Red tape and taxes mean that 27 of the 35 least business friendly countries are in sub-Saharan Africa. For many African entrepreneurs, operating legally brings headaches and few benefits. As a result, 42 percent of the region's economy is informal, the highest proportion in the world. In Malawi only 50,000 people -- out of a population of 12 million --

have formal jobs in the private sector. Endemic corruption compounds the poor business environment to make Africa a difficult place to work and do business.

The consequences of the lack of financial access are significant. Recent World Bank data regarding the correlation between financial sector development, poverty and inequality shows that financial development through the broadening and deepening of the financial sector improves overall economic growth. New data shows that it also reduces overall income inequality by disproportionately increasing the incomes of the poor. Countries with better-developed financial intermediaries experience faster declines in measures of both poverty and income inequality.

But how do we get there? Where do you start, and why now?

There is an important step that often precedes microfinance, and that, for CARE is step one on the economic development ladder. Village, or group savings and loan programs - I'll refer to them as VSL programs - were piloted by CARE in Niger in 1991. The approach which CARE developed builds on a traditional model to create VSL Associations. This is a self-selected group of people, usually unregistered, who pool their money in a fund from which members can borrow. The money is paid back with interest, causing the fund to grow. The regular savings contributions to the group are deposited with an end date in mind for distribution of all or part of the total funds, including interest earned, to the individual members, usually on the basis of a formula that links payouts to

amount saved. This lump sum distribution provides a relatively large amount of money that each member can apply to his/her own needs.

Members receive a return on their savings investments that ranges from a low of 30% per annum to a high in excess of 100% - far more than is paid by any commercial bank anywhere in the world. They are able to save on a flexible schedule and in whatever amount they wish, since the savings amount and schedule are established within the group. They are able to borrow with a minimum of fuss, since only peer approval is required in order for a member to access loans and insurance benefits. They can obtain loans that range from small change to several hundred dollars in later years. Typical loans are in the order of \$10-20, which is far too small for microfinance institutions to cost-effectively administer. The group can also set up an insurance fund (often called a Social Fund) for members to mitigate the effects of unforeseen disasters.

CARE has taken the original model of VSL, which was based on a fixed amount of weekly savings, month-long loans, and a memory-based system of record-keeping, and developed the model to accommodate loans of variable lengths and amounts and systems of savings that allow for flexible contributions – and even shareholdings.

With experience CARE has developed a formula for the VSL methodology that ensures its success:

- Members self-select to form a group, and save money in the form of shares. The savings are invested in a Loan Fund, from which members can borrow and must repay with interest;
- VSL Associations are comprised of 10-30 members, averaging about 22 members. This size enables the group to strike a balance between creating a useful pool of capital and keeping meetings manageable;
- Membership is open to both women and men, but at least three of the five Committee members elected must be female in the case of mixed Associations. Members who hold public office are not eligible for Committee positions;
- Associations are autonomous and self-managing, basing their system of governance, policies, and operating procedures on a written constitution. This is fundamental because their goal is institutional and financial independence;
- All transactions are carried out at meetings in front of all the members of the Association, promoting transparency and accountability;
- The cycle of savings and lending is time bound. At the end of an agreed period or 'cycle' the accumulated savings and service charge earnings are shared out among the membership in proportion to the amount that each member has saved throughout the cycle;

- All members have an individual passbook. The starting and closing balances of the Social Fund and Loan Fund are memorized at each meeting; and
- Associations meet at regular intervals during their first cycle, either weekly or fortnightly as the members agree. After the Association completes a cycle and becomes independent, meetings may reduce in frequency to once every four weeks.

VSL is for the poor and the very poor. It enables them to manage their household cash flow more efficiently and flexibly and to invest in income-generating activities that secure and stabilise their cash income. It has a dramatic impact on self-respect and social capital, particularly among the women who form 70% of the membership. CARE has nearly 1.5 million people involved in VSL programs in Africa – we have set a ten year goal of increasing this to 30 million, a critical mass that we believe is necessary to help launch a micro-finance revolution in Africa similar to that which has occurred in Asia and Latin America.

Tonight however, I won't spend a lot of time on the ins- and outs of creating and running a microfinance institution (referred to as an MFI) – plenty of ink has been spilt on that subject elsewhere. But I would like to spend some time on ways to create clients for MFIs since conceptually, MFIs often form step two on the ladder – where you go when VSL no longer satisfies your needs.

We can, and do, help VSL participants move up-market, but also know what makes this transition more likely to succeed. We recommend that community members participate in VSL programs for several years before they take the next step up the ladder to participate in the more formal microfinance system. Indeed, evidence shows that the financial service needs of the vast majority of clients are satisfied by VSL. However, after a few years, some VSL members may have a demand for financial services that cannot be met with group funds and it is time to take the next step. Once again CARE has a formula and a strategy for helping people climb to the next rung:

- First and foremost CARE ensures groups have attained financial and operational sustainability. CARE has learned from experience that people have to be ready for commercial debt as unprepared clients can be a liability to a microfinance bank - not an asset!
- The capacity and financial literacy of the groups and members must also be sufficient to ensure they can assess offers from MFIs and decide clearly what is in their self-interest;
- We need to ensure that client needs are real, i.e. demand driven. CARE will not encourage groups or individuals to take on debt from an MFI as an automatic next step. This step must be based on real demand by the members for additional resources. The assessment of whether a group is ready to move up also needs to

be based on their performance in a VSL program. A group that experiences high default rates or is unable to conduct their share-out without external help is not ready for the added responsibility of external funds.

- CARE also works alongside MFIs that are in a position to provide higher-level financial services such as loans, to ensure appropriateness of the loan products and lending approach. We work to secure the lowest possible transaction costs for the group(s); we facilitate the outreach activities of the MFI, and monitor the relationship to ensure that the MFI respects the integrity of the group(s);
- Finally, we work with groups to build their understanding of the terms and conditions of MFI engagement, often essential to avoid over-indebtedness;

This combination – first with family/community savings and loans, then with formal/commercial relationships between individuals/groups and microfinance banks – contributes to a financially literate and active population, and creates the conditions for taking the third step on the ladder – building a middle class and filling in the missing middle.

From our work with entrepreneurs trying to grow their businesses, we have developed an understanding of the barriers to entrepreneurship prevalent in the developing world. At the level of small and medium sized enterprises, or SMEs, a lack of access to capital, onerous regulatory environments and negative market conditions encourage

entrepreneurs to operate informally and at the same time prevent their businesses from growing.

Millions of informal micro-entrepreneurs who are being supported through microfinance still find they cannot take their business to the next level. The gap between the formal and informal markets is often vast, and seemingly insurmountable. The poor don't have the capacity to reach further "up" into the formal economy, and the formal economy sees little or no benefit from reaching "down" into the informal.

CARE characterizes this problem as the "missing middle" – a situation where businesses have outgrown the capital available from microfinance institutions, yet can't access capital from the formal banking sector. This is compounded by the fact that informal businesses often can't find ways and means of connecting (for example) to the supply chains of formal businesses either.

To overcome this double gap, CARE has been working to supply or connect small businesses to investment capital, trade and risk finance, as well as providing business development services aimed at helping small businesses from within the informal sector make connections and trade with those in the formal markets.

What I've presented tonight forms an overview of CARE's philosophy and strategy for helping people in the developing world climb the economic development ladder. Now the question is why?

There is a strong feeling from some quarters that encouraging market solutions to poverty is economic imperialism that does not truly help developing countries. At CARE we disagree. All our experience and research proves that helping poor people access finance at a level appropriate to their needs and skills helps the poor lift themselves out of poverty.

The organization Freedom from Hunger found that for their microfinance clients in Ghana, incomes had increased at twice the rate of non-clients. Clients also significantly diversified their income levels. But beyond incomes, the same study showed that clients' children were healthier and performed better than non-client children in terms of weight-for-age and height-for-age. This trend is evident whenever the impact of microfinance is assessed -- increased household incomes translate directly into increases in health and education levels of household members.

CARE's own research into our VSL program showed similar results. CARE completed an expenditure survey of randomly selected client and non client households in Tanzania and Mali. In Tanzania, where a program targeting households supporting orphans and vulnerable children or the chronically ill was assessed, results showed that VSL participation improved the odds that a household would choose to spend money on education, "no matter what." That is, a VSL household was more likely to spend on education even if it had orphans and vulnerable children or chronically ill members and even if it had other expenses, such as for medicine or clothing. Similarly, VSL

participation improved the odds that a household would spend money on clothes, send a member to a health center, or buy medicine without a prescription, regardless of whether that household had vulnerable members within it.

In Mali, in a program designed to reduce child labor, the assessment found that children in participating households spent fewer hours per week doing domestic work, reducing their domestic workload by 18 per cent compared to pre-participation levels. At the same time, the number of hours children spent working outside the home was also reduced for participant households, this time by 25 per cent. The study found that 33 per cent more children in participant households were regularly attending school. These statistics held true regardless of whether the children in the house were living with their biological parents or were orphans living with extended family. In other words, households participating in VSL programs in Mali were better able to support both their own children and also orphaned and vulnerable children in their care.

As these examples illustrate, in Africa we find compelling cases that show how access to financial services is increasing household income levels, and at the same time increasing their access to healthcare services, education, and basic needs such as clothing and medicines. We also have evidence that financial services make it possible for families to pull their children out of the labor force and return them to school. But perhaps most critically, we see that these services can help households to support the chronically ill and orphans and vulnerable children in areas hard-hit by HIV and AIDS. It is also evident that access to a range of financial services can contribute to peace and

foster good governance and democracy. An increase in income means that poor people will be able to pay their taxes and dues, and in turn will be better positioned to hold local politicians and policy makers accountable. It has also been shown that the gains poor households experience through access to financial services are sustained over time.

So if these are the gains we see in countries with relatively low levels of penetration by financial services, what might we expect to see if microfinance services were available at scale? To answer this question, we can look towards Bangladesh, where approximately 37 per cent of the population access financial services through microfinance providers. In the early 1990's, the World Bank conducted the most comprehensive study of the impact of microfinance on poverty levels of participants and their communities in Bangladesh. The study found that participants significantly increased their consumption levels, with a steady 5 per cent of clients moving above the poverty line each year by participating in microfinance programs. Households were able to sustain these gains over time. But the benefits didn't end with the participants, but were experienced village-wide through overall increases in village wage levels. Average rural household incomes increased in program villages, even for non-program households. In fact, this in-depth study found that microcredit accounted for 40 per cent of the entire reduction of moderate poverty in rural Bangladesh and that microcredit's spillover effects among non-participants reduced poverty among this group by some 1.0 per cent annually for moderate poverty and 1.3 per cent annually for extreme poverty.

Bangladesh also provides a clear link between the scaling of microfinance, the reduction of poverty, and the empowerment of women. Microfinance has not only contributed to lower poverty rates in the country, but has also influenced women's choices of family size and the education of female children. According to a recent study by the International Center for Diarrheal Disease Research in Bangladesh, the fertility rate in Bangladesh has decreased from 7 children per woman in the 1970s to 3.3 by 2000. This drastic decline can be attributed to changes in income, women's education, age at marriage, and women's empowerment; according to several studies, microfinance has positively impacted several of these factors, including income, access to resources, women's empowerment, and even the ability to pay for girls' education. By 2004, Bangladesh had already achieved the Millennium Development Goal for gender parity at the primary and secondary educational levels.

So if Bangladesh and selected cases in Africa are any example, in addition to increased incomes and consumption levels we should expect that achieving significant levels of access to financial services will result in a dramatic difference in the lives and status of poor women, a reduction in child labor, an increase in children's educational level, better health of women and children, and strong and inclusive economies.

In developing countries, the correlation between access to finance and access to healthcare is strong. Providing the poor with access to financial services could push rural healthcare past a tipping point, where the poor are able to command quality health services, even in remote areas, because they are able to pay for such services.

Achieving universal access to financial services in sub-Saharan Africa over the next ten years won't be an easy investment, but the returns will be substantial. Not only should we expect to see millions of people move out of poverty, but we will also fundamentally change the vicious cycle of poverty, poor health, and lack of education into a virtuous cycle of rising household incomes, improving health care, and better education.

So again, the bottom line is that markets CAN be made to work for the poor, and can be turned into a tool to fight poverty. So what do we need to do now to make it happen?

We need to create the conditions for a financial revolution in Africa, by purposely developing a financial system that works for poor people. This would see a commitment to universal access to financial services – and would encompass group savings and loans, formal microfinance and programs targeted at helping integrate small and medium sized enterprises with the formal economy.

We've just had a federal election. Although the party in government has not changed, we are nevertheless at a point where we have an opportunity as a nation to reevaluate our role and our strategy as a country in the global fight against poverty. This is what CARE is recommending for our new federal government:

- Canada needs to invest in poor people, not just their governments.
- Don't reinvent the wheel. NGOs like CARE already have the experience, the assets and the infrastructure to deliver these kinds of programs. Canada must invest via the non-governmental sector, including supporting partnerships between NGOs and financial services companies interested in helping develop their 'base'.
- Canada needs to think big, to think about continent wide, game changing strategies based on sectoral expertise. And we must stop being tied to narrow national geographies built around "focus countries". Industry doesn't think in terms of just "focus countries", so why should our national development policy?
- Canada must make Africa a priority for economic development. As I noted earlier the microfinance revolution has already taken off in the Americas and Asia. Africa is the new fertile ground.
- Finally Canada must make performance management target or outcome based, and move away from input oriented/micromanagement practices with their partners.

The UN estimates that sub-Saharan Africa needs to grow at 7% per year for it to make progress towards reaching its Millennium Development Goals. Building resilient,

inclusive and broad-based financial markets is surely a good way to contribute to these goals.

If we are going to bring about real change and actually make progress in fighting global poverty, we need to change our approach and our way of thinking. Up til now many of our approaches have been like a moving sidewalk – moving forward (and occasionally backwards) but rarely moving up. CARE believes it's time to get off the sidewalk and onto the ladder. From village savings and loans, to micro finance, to small and medium enterprises, the people of the developing world have the power to climb out of poverty. By supporting CARE and our economic program, you have the power to help them do it.

Thank you for your time and attention.