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# **BREAKING THROUGH:**

**THE EXPANSION OF MICRO-ENTERPRISE  
PROGRAMS AS A CHALLENGE  
FOR NON-PROFIT INSTITUTIONS**

**Maria Otero**



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FOR NON-PROFIT INSTITUTIONS**

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**ACCION INTERNATIONAL**

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*"We shall not cease from exploration  
And the end of all our exploring  
Will be to arrive where we started  
And know the place for the first time."*

*T.S. Eliot, "Four Quartets"*

## TABLE OF CONTENTS

	<b>Page</b>
Acknowledgments	7
Foreword	9
I. EXPANSION OF MICRO-ENTERPRISE PROGRAMS: A PERSPECTIVE .....	11
A. Introduction .....	13
B. The Concept of Program Expansion by Non-profit Institutions .....	16
1. Defining Expansion .....	16
2. Expansion by Whom: The Case for Involving Non-profit Institutions .....	24
3. Expansion for Whom: Program Beneficiaries .....	28
4. Expansion of What: Credit for the Poor .....	30
II. INSTITUTIONAL DEVELOPMENT IN THE EXPANSION OF MICRO-ENTERPRISE PROGRAMS ....	33
A. Introduction: The Perspective of Non-Profit Institutions .....	35
B. An Institution's Vision .....	38
1. Vision Defined .....	38
2. An Example of Institutional Vision .....	39
C. The Institution's Structure .....	43
1. Structural Configuration .....	43
2. The Institution's Policies and Procedures .....	46

3. Transforming the Structure of Non-profit Organizations .....	48
D. The Financial Systems .....	50
1. Financial Management .....	51
2. Financial Analysis .....	56
E. Human Resources .....	58
1. Profile of the Staff .....	59
2. Administrative Policies .....	61
3. Recruitment and Selection .....	63
4. Incorporation into the Institution .....	64
F. The Institution and Its Context .....	66
1. Client Participation .....	66
2. Commercial Sector Institutions .....	66
3. Non-profit and Development Institutions .....	67
4. Government .....	68
5. Donor Organizations .....	68
G. Conclusion .....	69
<b>III. FACTORS THAT INFLUENCE EXPANSION IN MICRO-ENTERPRISE PROGRAMS .....</b>	<b>71</b>
A. Introduction .....	73
B. Summary of Major Findings .....	74
1. On Expansion .....	74
2. On Models of Expansion .....	75
3. On Non-profit Institutions and Their Development .....	78
C. Issues to Address in the Expansion of Micro-enterprise Programs .....	79
1. Applicability of Expansion to Non-profit Institutions .....	79
2. Program Sustainability .....	79
3. Methodological Considerations .....	80
4. Contextual Consideration .....	81
5. The Constraints of Program Expansion .....	82
D. Conclusion .....	82
<b>BIBLIOGRAPHY .....</b>	<b>85</b>

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A special word of gratitude to my ACCION colleagues whose work has inspired this document. Capsulized in Pedro Jimenez' contagious enthusiasm, "Oye, chico, esta cosa va pa' grande"<sup>1</sup>, the ideas behind this document emerge from the unending energy and commitment that have built each ACCION program.

The participants at the Puerto Salinas, Ecuador, conference of October, 1988, also deserve recognition. Their insights and recommendations are integrated in Chapter II and reflect the collective effort of over 50 colleagues from 33 micro-enterprise programs in 12 Latin American and Caribbean countries.

My thinking on this topic also benefitted from enriching discussions with persons who are participating in the PACT

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1. "Hey, man, this thing is going to get big"

**Expansion of Benefits Program, especially Peggy Clark, Ford Foundation; Larry Reed, Opportunity International; Beto Brun, Panamerican Development Foundation; Manuel Montoya, Accion Comunitaria del Peru; Jeffrey Ashe, Ashe and Associates; Paul Rippey, Council for International Development; Meg Bowman, Technoserve; Carlos Castello, ACCION International; Elaine Edgcomb, SEEP; and Carolyn Stremlau, PACT.**

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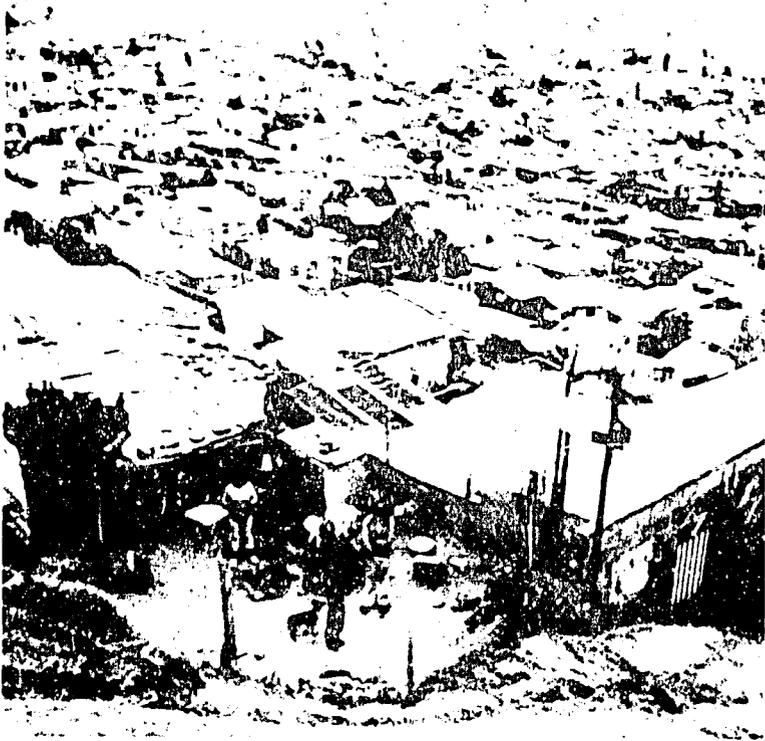
**Maria Otero**

## **FOREWORD**

Given the economic conditions and growth of the informal sector in the developing world, it has become imperative to explore ways to expand services and to reach greater numbers of micro-entrepreneurs in that sector with development efforts. Many programs of micro-enterprise development are currently operating across the globe. The challenge addressed by this document is that of scaling up these and new programs in order to reach ever-greater numbers of micro-entrepreneurs working in the informal sector.

This document draws on the experience of programs affiliated with ACCION International throughout the Americas, to delve into the subject of micro-enterprise program expansion. It is partially based on findings from an institution-wide conference held in Puerto Salinas, Ecuador in October, 1988.

The document describes the process of expansion, including prerequisites, characteristics, institutional structure, and planning. Included are guidelines for institutions on how best to confront the challenges posed by expansion, with special emphasis on vision, financial systems, human resources and contextual considerations. And finally, factors that influence and/or limit expansion in micro-enterprise programs are explored.



CALMEADOW / CONNELL

## CHAPTER I

### EXPANSION OF MICRO-ENTERPRISE PROGRAMS: A PERSPECTIVE

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## **A. INTRODUCTION**

The informal economies in developing countries continue to grow. The migration patterns into urban areas in the 1960s and 1970s, and the excess of labor force occasioned by the models of growth during this period, have joined the economic crisis of the 1980s to further swell the informal economies (Sanyal and Ferrin, 1986; Mezzera, 1989; Tokman, 1987). As many have noted, the growth of the informal sector has stimulated a high level of interest among policy makers, planners, scholars and development professionals (Tendler, 1987; Levitsky, 1988). How the informal sector contributes to the national economy of a developing country, and what potential it offers for expanding growth in a country are among key subjects of current debate (Liedholm and Mead, 1987; Biggs, Grindle and Snodgrass, 1988; Boomgard, 1989).

The reasons for interest in this sector vary. Governments and policy makers, aware of the political implications of this growing sector, are intent on formulating a framework for understanding the dimensions of the informal sector, for drafting key policy guidelines, and for allocating resources to reach this expanding population. To them, the informal sector constitutes an important variable in the country's economy and requires a response. In many developing countries, the same questions regarding the informal sector emerge:

- what should the government's role be in integrating this sector into the country's broader economy?
- are legislation and existing policies the main barriers to enabling this sector to evolve to its full productive potential, and if so, what conditions must exist for policy reforms to take place? and
- what linkages between the formal and informal economies should be fostered through policies and programs?

Interest among development professionals and donors focuses more closely on examining the methods and results of channeling resources to the informal sector, and on determining the most effective vehicles for doing so. The questions that underlie their interest, while not excluding broader policy issues, emphasize program development and institutional growth. To them, the questions that dominate the debate include:

- what is the measure of success of the delivery systems that reach the informal sector's population?
- what constitutes a sustainable program with the capacity to continue to benefit this population over the long term?
- what are the best mechanisms and instruments to analyze the economic activity of this heterogeneous population?

The responses to these broad-level concerns will necessarily involve a review of the current experience working with this sector.

While efforts to address policy issues have emerged, especially in recent years, the significant accomplishment of the last ten years has been the design and implementation of micro-enterprise programs that provide services, especially credit, to the smallest-scale members of the economically active population in developing countries (Farbman, 1981; Blayney and Otero, 1985; Hull, 1988).

Most of these programs started in the 1970s and early 1980 as demonstration or model efforts operated by non-profit institutions that were interested in experimenting with ways of

assisting the economic activities of the urban poor. Today, while many of these projects have failed or fallen short of expectations, other experiments started by non-profits have grown into large and sustainable programs. These provide a series of important lessons about the factors that contribute to success and failure when addressing the informal sector (Hossain, 1988; Goldmark and Rosengard, 1983; Gomez and Saladin, 1987; Boomgard, 1989). Current state-of-the-art studies and program designers analyze these current methodologies, delivery systems, and viability potential in order to construct more effective delivery efforts that can meet the challenges these programs will face in the 1990s.

This document has evolved against this background –on the one hand the growing need to respond to broad policy concerns regarding the informal sector, and on the other the recognition that it is essential to improve the existing assistance efforts. Its discussion emerges from a conference in October, 1988, organized by ACCION International, a U.S. private voluntary organization working in micro-enterprise development, at which its then 33 affiliated non-profit development organizations from Latin America, the Caribbean and the U.S. met in Ecuador. All of these organizations implement micro-enterprise programs that vary in size and duration, and are described in greater detail below.

The conference sought to address issues of the implementation of micro-enterprise programs by non-profit development organizations and their subsequent growth. Their goals included:

- o To analyze the desired characteristics of non-profit development organizations involved in micro- enterprise development;
- o To identify and explore the key issues of effective organizational development for non-profit organizations that implement micro- enterprise programs; and
- o To design and fine-tune the policies and strategies that would enable each institution to conduct the work of the next five years with greater effectiveness.

## **B. THE CONCEPT OF PROGRAM EXPANSION BY NON-PROFIT INSTITUTIONS**

The theme of expansion of micro-enterprise programs provided a framework for this conference. The participants represented organizations that are ACCION affiliates and that have operated micro-enterprise programs for several years. Many have demonstrated the capacity for growth and sustainability and currently are searching for the best way to expand their program activity.

The concept of a new level of expansion of micro-enterprise programs over the coming decade reflects the exigencies of the sector these programs reach; a fluid, ever-growing, increasingly complex series of heterogeneous business activities conducted by some of the poorest members of the society. The conditions of the informal sector—not only its size and level of need, but also its limited access to resources—dictate the importance of structuring programs that can expand in a significant manner and respond more effectively to larger numbers of this population.

The demand for services provided by micro-enterprise programs, especially in credit, is paramount to this discussion. The experience of existing programs indicates that the demand for program services in most settings is currently much greater than the programs can meet. The nature and degree of existing demand will become one of the determinants of how and where programs choose to expand. In most cases, the pattern of growth of existing programs has been a progression from the large urban centers to the secondary cities and the rural towns.

### **1. Defining Expansion**

*The concept of expansion of micro-enterprise programs refers to the process of reaching ever-increasing numbers of micro-entrepreneurs with specific services, such as credit, and of making possible a subsequent growth of benefits to this population.* Expansion, as conceptualized in this document, applies to micro-enterprise programs that are not new but, through their experience, have demonstrated the capacity to scale up to a significantly increased level. It assumes the existence of an institutional expertise, a methodology of action, and a system of information that have overcome the

obstacles most programs encounter in their early phases and have emerged as strong, viable and long-lasting.

To place the concept of expansion within the existing experience of micro-enterprise projects, one can identify four major stages of growth present in the evolution of micro-enterprise projects. These stages emerge from the programs affiliated with ACCION and characterize their evolution, even when the models and strategies for growth among them are different:

- a. ***Start-up Stage:*** This stage lays the groundwork for project implementation. It includes feasibility studies, survey studies on the micro-enterprise population, the creation of a new institution or the restructuring of an existing one, the structuring of a board, the involvement of local support, the definition of goals and objectives, the acquisition of resources for initiation, the hiring and training of staff, the design for a methodology for application, the interaction with the population the project will reach, and the establishment of systems for program implementation.

This first phase may not include any implementation of project activities, but rather consist of the institutional and methodological preparation for the project. Activities are related to the nature of the program as well as to the institutional ingredients necessary for implementation. Often, this stage alone can take one or two years.

In ACCION's experience, many micro-enterprise projects that today are operating successfully in various countries – the Dominican Republic, Costa Rica, Paraguay, and Bolivia, for example – started in a similar way. Chile, the most recent program, presents a good example of this stage of growth.

In 1987, ACCION and a group of individuals from the private sector in Chile initiated activities to create an organization to promote micro-enterprise (ACCION International Annual Report, 1988). The first step was to form a corporation, PROPESA, and to complete its legal and regulatory steps. During the following year, PROPESA secured funds through a grant from U.S.A.I.D. to serve as a guarantee fund against loans from local banks. It also obtained its first loan from

Citibank during this phase. Approximately US \$75,000 was donated by local companies to help finance start-up costs. PROPESA also used this time to conduct a detailed feasibility study that determined the size of the micro-enterprise sector and the level of demand for services. The program hired and trained staff, and concentrated on the promotion of the program through the media. By the time the program opened its doors at the end of 1988, its staff was fully trained, its funds were secured, its systems established, and it was able to begin addressing the large demand. During the first month after the press conference that launched the program, over 1,600 persons approached PROPESA to join the program.

One interesting feature of PROPESA's start-up phase has been the emphasis on securing local contributions and loans, which avoided the total dependence on outside grant money. The program's success in obtaining a \$25,000 loan from Citibank before it initiated lending activity demonstrates the importance and potential of linking non-profit organizations with the banking sector from the outset. A U.S.A.I.D. grant was utilized to facilitate this process and assist in establishing long-term relationships with local sources of funds. Other ACCION-affiliated programs launched in the past five years, such as the Paraguayan Foundation for Development and Cooperation, the Foundation for the Promotion and Development of Micro-enterprises (PRODEM) in Bolivia, and AVANCE in Costa Rica, have also secured loans or substantive local financial resources during their early years of operation.

Today, PROPESA is in the early stages of the second phase of its growth, and operates in Santiago.

- b. **Model Stage:** During this stage the micro-enterprise program begins its lending and training activities for micro-entrepreneurs. Experience shows that if the groundwork was carefully laid during start-up, then a high demand for program services, combined with the staff's technical expertise and motivation, and the available resources and effective systems, contribute to a program that grows quickly and successfully. In a good program, this period is known as the "honeymoon", when repayment is near or at 100 percent, the program is promoted by word of mouth, and

the staff concentrates on fine-tuning the existing effective systems. At this stage, the program establishes efficiency indicators for its performance that become part of the overall goals of the project. In a new institution or an existing one that has started a micro-enterprise program, this stage is crucial to establishing the work ethos and the vision that will guide its future work.

The program in Guatemala which has been operating since July, 1988, presents a good illustration of this stage (Revere, 1989). The micro-enterprise program began through two existing local institutions –The Technical Foundation (FUNTEC) and the Foundation for Development of Socioeconomic Programs (FUNDAP)– that had previously focused their work on rural development programs. The initiation of their micro-enterprise strategies required institutional changes, staff preparation, the establishment of norms and procedures, the development of a methodology, an analysis of the target population and a series of other tasks completed during the start-up stage. The programs began to operate only when resources were secured and when the local institutions and staff were fully prepared to implement a demanding program.

During the first nine months of operation, the programs disbursed nearly 1,600 loans, totalling about US \$660,000 to 1,476 micro-entrepreneurs. The average size of loans was about \$400. By August, 1989, at 15 months of operation, the programs continued to grow, now totalling over 2,600 loans. Additionally, the number of offices expanded, from two at the outset to six, one year later. Costs per unit lent were calculated from the outset and, at 12 cents per quetzal lent, showed considerable program efficiency during this first stage.

The programs have also established a comprehensive and effective information system that has enabled them to monitor portfolio activity as well as track impact data. Hence, even in the first year of operation, the programs can determine the level of change among beneficiaries in areas such as income, employment, and assets.

During this period, the programs have also maintained a strong repayment record, which has been monitored very

carefully to assure that problems are identified and addressed immediately. Hence, the programs in Guatemala appear to be in the process of successfully completing this stage of growth and will have the basis to enter the next stage.

- c. ***Consolidation-with-Growth Stage:*** After one or two years of operation, during which the program indicators –both of level of activity and level of efficiency– demonstrate successful evolution through the model stage, the program enters a third stage. At this time it focuses on strengthening the institutional and programmatic factors that will enable it to stabilize its work and to continue its growth. During this period many programs expand activity to new areas, such as a new city or region, and establish the needed changes in organizational structure to do so. Structural and management issues –personnel, financial management, the role of mid-level management, and long-term planning – receive particular attention. The implementing institution also designs a strategy to obtain resources for its activities, which may include soft loans from international donors as well as loans from local commercial banks.

The best examples in the ACCION network to illustrate this stage are the program in Bolivia, which is entering its third year of operation, and the program in the Dominican Republic, which has been at this stage for the last three years.

In Bolivia, the Foundation for the Promotion and Development of Micro-enterprises (PRODEM), experienced a model stage similar to that described in Guatemala, with enormous growth and demonstration of quality in efficiency and methodological areas (Jackelen, Blayney, and McGill, 1987). It reached nearly 5,000 micro-entrepreneurs with nearly US \$2.9 million in loans averaging under \$200. From the outset women constituted over 65% of its beneficiaries, a figure maintained during the program's tenure. Its repayment rate was never below 99 percent and only an insignificant sum was defaulted in this period.

With this experience, PRODEM is now in the stabilization and-growth stage, and is concentrating its efforts on opening regional offices throughout the country to increase

its level of activity. It has also secured funds for this new stage and is in the process of making institutional changes and preparing the staff for this new stage. PRODEM's monthly activity as it begins this stage includes lending over US \$200,000 each month, reaching about 150 new borrowers, maintaining a growing portfolio of about \$500,000, and interacting with nearly 5,000 program participants (ACCION, 1989a).

The Association for the Development of Micro-enterprises, (ADEMI), in the Dominican Republic, founded six years ago, provides an example of an institution that has progressed successfully through the stages defined here (Gomez, 1989). Since 1986, ADEMI has been in this third phase: consolidation with growth. During this period, the number of its offices grew from 14 to 19 around the country, and its annual number of loans grew from around 3,000 to its current level of 5,000. During its tenure, the program has reached over 6,000 micro-entrepreneurs with over 22,000 loans. The amount it has lent every year has grown considerably, because some borrowers now access larger loans for equipment purchase.

Three interesting developments in ADEMI reflect its institutional and programmatic evolution to this stage. First, the staffing configuration of the organization has changed dramatically in the last three years. Whereas in 1986 70 per cent of the staff was administrative and 30 percent was field staff, that ratio has reversed in this third stage. Today, 71 per cent of ADEMI's 88 employees are field staff and 26 per cent are administrative (Gomez, 1989). Institutionally, this evolution of the staffing pattern is very significant for an organization seeking to expand its program.

Second, in the last three years ADEMI has demonstrated the capacity to cover its operating costs with program revenue. Its self-sufficiency in 1985 stood at 76 per cent. It has been 103, 100 and 128 percent for 1986, 1987 and 1988, respectively. Its portfolio during this period also grew by nearly 300 per cent in real terms, to \$1 million.

Finally, as ADEMI completed its second stage, it encountered a potentially severe problem of delinquency which had grown to 25 per cent in 1986. By attacking this

problem head on and increasing recuperation—in 1987 delinquency appeared as 14 percent, and stood at 9.7 per cent in 1988—ADEMI was able to overcome the potentially devastating effect of a continued high level of delinquency. Had ADEMI proved unsuccessful in lowering the arrearage level, it would not have advanced effectively through its stage of stabilization with growth.

Nearly all Accion-affiliated programs fall into one of these three stages of micro-enterprise program growth.

- d. **Expansion Stage:** At this stage a program crosses a new threshold of growth, and is able to reach a significant number of clients. In general, ACCION defines "reaching a significant number" as providing credit and services to 10,000 or more clients in a year. The nature of this expansion can vary considerably depending on a variety of internal and contextual factors that will determine the institutional structure and funding base. This document directs its discussion to this stage of growth in micro-enterprise programs.

It is important to point out that none of the ACCION-affiliated programs appear under this category. In fact, only a handful of programs worldwide have reached this level; the Grameen Bank in Bangladesh and the Bakan Kredit Kecamatan Program in Indonesia are two of the most noted ones. For those institutions that desire to enter this stage, preparing the groundwork to make this possible constitutes their biggest institutional challenge.

The evolution of a micro-enterprise program is reflected in these stages. Advancement from one stage to the next requires successful completion of each stage. Programs do not start by plunging into the third or fourth stage without passing through the first two. This sequential and gradual evolution is important because it emphasizes developing a vision of the process towards expansion from the outset. It implies that the early stages create the building blocks, at both the institutional and programmatic levels, to enable expansion to take place (Smith and Tippett, 1982).

Conceptualizations of the institutional development of non-profit organizations amplify this discussion. For example,

implicit in the stages of growth outlined are the concepts of effectiveness, efficiency and expansion set out by David Korten in his 3-E Model for program evolution (Korten, 1980). It is interesting that these characteristics of an effective program occur in the case of micro-enterprise development, and evolve in a sequential manner as programs grow.

After looking at the stages of evolution of a program, one can identify five main indicators of a program's stature before studying its potential to engage in expansion as defined here. Programs poised to enter the expansion phase should exhibit the following characteristics:

- a. ***The program has established a proven track record:*** The program has developed the systems and the institutional capacity to undertake gradual but constant growth. That is, the program has evolved from a small effort to a significantly larger one and has successfully adapted its structure, methodology, and operating systems to enable it to grow. These programs recognize the stages of growth of a micro-enterprise program, and the internal processes that enabled them to arrive at their current level of activity.

Further, these programs have established themselves within their working milieu, and are considered serious and effective programs by their beneficiaries, other organizations, and donors.

- b. ***The program demonstrates effective capacity at its current level of effort:*** In addition to gradual growth, the program currently operates in a satisfactory manner at its given level of activity. While there are many facets within a program to take into account in determining its relative effectiveness, existing evaluations, studies of results, and other tools will indicate, in a general manner, the program's integration of all the elements that provide it with relative capacity at the level it is operating.
- c. ***The program currently reaches a thousand or several thousand beneficiaries:*** The threshold of expansion defined here refers to those programs that already reach a large population, possibly of several thousand beneficiaries. The program has clearly defined the population it seeks to assist,

and has conducted studies and surveys to verify the existing demand for the services it offers. Demand for the program's services constitutes a key variable in the process of expansion the program will undertake.

- d. ***Operations are at a regional or national level:*** Programs that have created an infrastructure and the systems to move beyond operation in a small setting, such as one city, can consider broader expansion. Their experience has demonstrated the capacity for thinking in progressively larger terms, and the potential for expanding to a further level of activity.
- e. ***The program has achieved a high level of self-sufficiency:*** After several years of operation, these programs have demonstrated the capacity to lower costs gradually and increase their own capacity to cover operating expenses from the income earned in the program. These programs may be partly or fully self-sufficient, and in some cases may generate additional revenues to maintain the value of their loan portfolios or even to capitalize them. In addition, they must demonstrate this capacity for self-sufficiency over a given period of time, rather than fluctuating widely in this area.
- f. ***The program has developed a diverse resource base:*** The program has moved beyond the acquisition of grant money to conduct its activities and has established its own revenue base as a combination of earned income, loans from various sources and donations.

## **2. Expansion by Whom: The Case for Involving Non-Profit Institutions**

In addressing the question of expansion of micro-enterprise programs, this document limits itself to focusing on indigenous, non-governmental organizations. While financial institutions and community-level organizations have considerable experience in this field, the issues they confront when addressing the topic of expansion differ from those faced by non-profit organizations. The emphasis on these non-profit, private organizations recognizes their contribution to micro-enterprise development, and enables the discussion to

highlight the advantages, strengths and limitations that they face as their work evolves from model or demonstration efforts to larger, more demanding programs.

The discussion also draws from ACCION's experience and therefore focuses on situations pertinent to Latin American and Caribbean countries. The lessons in micro-enterprise development obtained in these regions provide the expertise for this document. Although the analysis and the recommendations suggested here may be applicable to both Asia and Africa, it is important to recognize that the wide diversity in economic growth, population size, institutional capability and contextual factors in these regions of the world make this discussion regionally focused and relevant. At the same time, since micro-enterprise programs share many commonalities, one can draw lessons from program experiences in other parts of the world, as is done below, as well as adapt this discussion to other settings.

The established wisdom on non-profit development organizations has been that they are good candidates to initiate model or demonstration micro-enterprise programs. They generally demonstrate a variety of advantages, such as proximity to the beneficiary or client population, a willingness to experiment with a new methodology, the capacity to operate with small programs geared to a high-risk population, and the capacity to combine credit provision with non-financial assistance (Farbman, 1981). Many of the earlier studies of delivery systems to reach micro-enterprises attribute these and other useful characteristics to local organizations and support the argument that their role in micro-enterprise promotion should concentrate on the start-up of programs.

Additionally, the interest of donors and practitioners in involving private sector financial institutions in extending credit to micro-enterprises also has supported the demonstration role by non-profit organizations. The argument has been that large micro-enterprise programs should be created and implemented by the banking institutions once the local non-profit organizations have demonstrated the possibility of working with micro-enterprises. This approach creates an opportunity for increasing access to local banking and financial resources for micro-enterprise development. On the one hand it decreases the dependence on grant and highly subsidized money, and on

the other it signifies the availability of substantial financial resources for micro-enterprise support.

The interest in engaging financial institutions to lend to micro-enterprises also reflected a general sense that the universe of non-profit organizations lacked the financial and institutional capability to expand programs beyond the small, pilot stage. Additionally, the issue of program self-sufficiency emerged as a paramount topic in this debate, and appeared as a distant goal for a number of micro-enterprise programs.

Observers also assumed that the link between a demonstration project and a financial institution would occur through the client. As part of its demonstration efforts, the non-profit organizations would prepare micro-entrepreneurs to manage and utilize credit, and would release them gradually into a direct credit relationship with a commercial institution. In fact, the graduation of project beneficiaries or clients from a demonstration project into the commercial sector has been an underlying goal of most micro-enterprise programs.

The evolution of micro-enterprise programs in the last few years has taken place in a manner that is not entirely aligned with the observations and assumptions summarized above. Based on ACCION's 17 years of experience in 13 countries, several significant assertions about micro-enterprise programs can be made today, which include the following:

- a. ***New non-profit institutions have emerged that are specifically designed to promote micro-enterprise development.*** These are conceived with a philosophy that borrows from the financial sector and emphasizes the financial viability of these programs. In many cases, these institutions do not rely exclusively on grants but include the cost of money in their calculations for long-term sustainability. The vision that guides these institutions differs from that of the majority of the non-profit organizations that were involved in the earlier stages of micro-enterprise development, which depended entirely on grants for their activities.
- b. ***Some non-profit organizations have developed large programs, have designed and applied the needed management and information systems, have established a***

**high level of self-sufficiency, and have demonstrated the capacity to move beyond the demonstration role originally attributed to them.** While this development often applies to the newer institutions, it also includes older ones that have evolved in this direction. In Latin America, programs in Bolivia (Foundation for the Development and Promotion of Micro-enterprises – PRODEM), Peru (Accion Comunitaria del Peru – ACP), Dominican Republic (Association for the Development of Micro-enterprises – ADEMI) present three examples of non-profit organizations whose micro-enterprise programs more closely resemble what was formerly envisioned as being implemented only by a financial institution.

- c. **Certain non-profit organizations have made self-sufficiency a high priority, and this has played an important role in determining the way the programs and the institutions have evolved.** These organizations have developed institutional structures, reporting mechanisms, and financial know-how that are also more akin to those of a financial institution than to those of a non-profit. In some cases, the specific methodology selected for credit delivery, and the population targeted by the program, constitute part of the strategy for developing a sustainable, long-term micro-enterprise program.
- d. **The graduation of beneficiaries from demonstration projects to the commercial institutions has not occurred as anticipated.** The banking sector in general has not opened windows for micro-enterprise lending, except in cases where donors or international agencies have promoted and funded it. Non-profit organizations have opted to retain their oldest and most trusted clients, and the clients themselves also have preferred to maintain this relationship. Hence, with very few exceptions, the link between a non-profit organization and the banking sector has not been created through the services to the micro-entrepreneur.
- e. **In several countries, non-profit organizations have approached banks as an alternative source of financing for their programs.** These relationships remained tentative for a long time, in part because banks did not consider these organizations viable borrowers, and in part because non-profit organizations balked at the high cost of borrowing

from the commercial sector. Nevertheless, these linkages evolved as these institutions requested loans for credit funds, and were able to meet the bank's collateral and other requirements. In the case of ACCION, 39 percent of the total credit fund of its 37 affiliates is financed through non-concessionary loans to the implementing affiliate, half of which comes from local banks (ACCION, 1989b). In this experience, the significant involvement of the commercial sector in micro-enterprise development has occurred through loans provided to expanding programs that are implemented by non-profit organizations rather than through direct loans to individual micro-entrepreneurs.

Given the evolution of a cadre of non-profit organizations that support the above assertions, their entrance into the fourth stage—expansion—makes a great deal of sense.

It may be that this expansion will require fundamental institutional changes in a non-profit organization that were not necessary before. The institution may assume a structure and procedures akin to those of commercial institutions. One can argue that while remaining non-profit, adapting institutional factors from commercial institutions could represent an interesting evolution for non-profit organizations that have the lead in micro-enterprise development work, and are on the cusp of expanding their programs. Further, after years of successful pilot programs directed at a growing population, these organizations agree that while small may be beautiful, it may also be insignificant.

### **3. Expansion for Whom: Program Beneficiaries**

The micro-enterprise programs considered in this document reach the population that constitutes the core of the informal sector in developing countries. The following provides some guidelines for understanding the nature of this population, based on the work that ACCION has conducted in the last ten years, as well as on other studies of the informal sector in Latin America.

Micro-entrepreneurs are poor men and women who live in large and secondary cities and are self-employed in a wide variety of economic activities. In almost all countries, the

definitions of a micro-enterprise are the economically productive activities engaged in manufacturing –carpenters, shoemakers, tailors; in commerce– street vendors, hawkers; and in service –maintenance, repair, and transportation.

Definitions also use specifics about the number of employees and asset size of the firm as additional indicators, and often conclude that firms with fewer than ten employees and fixed assets under US \$10,000 constitute a micro-enterprise in Latin America (Blayney and Otero, 1985; Boomgard, 1989). Most micro- enterprises, however, tend to be considerably smaller than these figures would indicate, and on average employ fewer than five persons and have assets of around US \$1,000 (Christen, 1985; Christen, 1987).

Many studies, especially at the country level, outline the characteristics of a micro-entrepreneur (Escobar, 1989; Hossain, 1988; Parra, 1985). In spite of their heterogeneity, a summary of these findings provides a broad profile of the persons these micro-enterprise programs currently reach and would continue to assist through expansion. The profile includes the following:

- While they are not often new migrants into the urban setting, these persons tend to share a rural background, either personally or removed by one generation. The strong patterns of rural to urban migration of the last two decades result today in micro-entrepreneurs who have spent many years or a lifetime as city dwellers.
- Most micro-entrepreneurs learned their skills from relatives or neighbors, functioned as apprentices to improve their expertise, and have used their trade as a source of income for several years. In the case of street vendors and others engaged in commercial activity, there is no particular learned skill. These persons enter into this line of work because there are almost no barriers to doing so and because it offers a source of livelihood.
- Formal education has been minimal for most of this population. In many countries, the large majority has not completed the sixth grade. Among women, the education level tends to be even lower. In fact, many micro-entrepreneurs cannot read or write.

- Women predominate among micro-entrepreneurs, especially in the smallest firms and in firms that make clothing or process food. Among vendors, especially in market places, women comprise the large majority. A significant number of them are heads of households, and their dependents rely on their income for subsistence.
- No more than ten percent of micro-entrepreneurs have access to financial resources from formal lending institutions (Christen, 1989b). The vast majority are unable to meet the collateral requirements for a loan from a bank, and rely on moneylenders for their working capital.

#### **4. Expansion of What: Credit for the Poor**

The micro-enterprise programs considered here concentrate their work on the extension of credit to micro-entrepreneurs. These loans are provided quickly, often taking one week for loan review and approval; and disburse small amounts, primarily for working capital. Loans are also short-term, an average of sixteen weeks; charge commercial or higher interest rates; and are processed with a minimal level of paperwork and time from the borrower. Most of these loans are provided to self-selected groups of three to five micro-entrepreneurs and range in size from under US \$200 in ACTUAR/Bogotá in Colombia to over US \$700 in the Foundation for the Promotion and Development of Micro-enterprises (PRODEM) in Bolivia. The average loan size among these programs is US \$458, or about US \$160 per borrower (ACCION, 1989a).

Expansion of credit provision for micro-entrepreneurs implies a process of increasing the number of micro-entrepreneurs that can obtain small, short-term loans from the program. The program's priority is to transfer a significant level of financial resources in the form of credit to producers who currently do not have access to the country's financial and banking systems. This redistribution of resources, called by some the "democratization of credit", becomes one of the priorities of these programs as they enter into a stage of expansion.

With the process of growth, most micro-enterprise programs tend to concentrate on the provision of credit and gradually to lessen their activities in additional services, especially training.

This analysis looks to programs that can expand the clients' capacity to produce effectively, to assure and expand jobs, and to increase people's income. Note that these results are often considered impact, the by-product of credit.

***The focus of this document is the institutional issues that contribute to an institution's capacity to enter the fourth stage of micro-enterprise program expansion.*** The participants in the 1988 Conference organized these issues around five broad categories of institutional growth and development: institutional vision; the structure of an institution; internal systems, particularly financial; human resource development; and the relationship of the institution to its context.

These topics in institutional development constitute the subject of Chapter II. The chapter highlights the conference proceedings and provides additional illustrative and analytical material to expand the discussion. Chapter III draws together the main themes examined in this document, and provides guidelines on how institutions can approach the challenge of expansion.



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**CHAPTER II**  
**INSTITUTIONAL DEVELOPMENT**  
**IN THE EXPANSION**  
**OF MICRO-ENTERPRISE PROGRAMS**

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## **A. INTRODUCTION: THE PERSPECTIVE OF NON-PROFIT INSTITUTIONS**

Effective development of the implementing institution is a key determinant in the expansion of micro-enterprise programs. The experience and review of programs in the last decade indicate that serious deficiencies in the internal management capability of non-profit institutions have constituted an important contributor to project failure (A.I.D., 1989). Observers and evaluators of micro-enterprise programs agree that strategies to strengthen institutions must be included in any long-term micro-enterprise development plans (Grindle, Shipton and Mann, 1986).

Institutional development should emerge as a point of departure for the challenging venture of expansion in a micro-enterprise program. This chapter discusses the relationship between project expansion and institutional development, and draws material from the conference in Puerto Salinas, Ecuador, mentioned above. The discussion reflects the experience of the implementing institutions represented in Salinas. Five categories in institutional development emerged from a consensus among conference participants as the most important frame for this presentation.

It should be noted that the majority of the micro-enterprise assistance organizations involved in this discussion find themselves in a variety of places on the continuum of program

growth. As described above, some have reached the second stage, while others are at various levels of development within the third stage. Only a few appear ready to entertain a fourth stage of expansion in the near future. However, all institutions appear somewhere on this growth continuum and agree that the subjects related to institutional development addressed below are paramount to their movement towards expansion.

Institutional development theory is a complex area of study encompassing a variety of variables that together contribute to the well-being and the growth of an institution. It is useful to draw briefly from the organizational development literature to orient the discussion that follows.

Organizational development is a process of renewing an organization's capacity to initiate, create, and confront needed changes so as to remain viable, to adapt to conditions, to solve problems, to learn from experience, and in the process become a more mature institution (Lippitt, 1969). In the long term, it is an effort to develop the institution's problem-solving capacities and to equip it with the ability to renew its internal processes as a changing environment and new priorities dictate.

Strengthening the human resources in an institution to improve its organic functioning constitutes the mainstay of institutional development work (Huse, 1975). It is, after all, the varied capacities of the individuals who comprise the institution that will translate into organizational competence.

Three commonalities underlie most theories of institutional development and are pertinent to the institutions that implement micro-enterprise projects. First, institutional development is a process of change in which all the variables that make up the institution are constantly evolving. This concept corresponds to the process of change described in successful micro-enterprise programs, suggesting that program expansion requires a concurrent pattern of change within the implementing institution. Second, it engages a systems approach of interdependent and interacting components that comprise a whole. Changes in any part of the system will affect other parts. Finally, institutional development makes use of behavioral sciences to strengthen institutions. Training and technical assistance, for example, have become important vehicles for increasing an institution's capacity to operate.

To visualize the many areas that comprise an institution's system and that must be addressed when expanding a program, it is useful to divide institutional development into subsystems that interact and evolve. Three key subsystems are identified here:

- **The structural subsystem:** This constitutes the organizational structure of an institution –its units, departments, and divisions. Also found here are work rules, communications systems, lines of authority, and norms and procedures for planning, coordinating, controlling and decision-making. From the perspective of institutional sustainability, especially in the case of institutions that conduct micro-enterprise programs, this subsystem is perhaps the most important, yet it remains difficult to address.
- **The human resource subsystem:** This consists of the skills and abilities of an institution's members, the leadership and philosophy that directs it, and the style –formal and informal– that operates. This subsystem also includes staffing patterns, rewards and incentives, and personnel evaluations. Issues related to human-resource development appear here, which are often mistakenly equated with the whole of institutional development. While this is the most accessible subsystem because it defines individuals, and their roles and tasks in the institution, improvements in this area alone will not lead to a stronger institution.
- **The external interaction subsystem:** For micro-enterprise programs, this subsystem emphasizes the capacity to influence the existing policy and regulatory environment in which these institutions operate, and to respond to external demands, innovations or constraints. The emphasis placed on this subsystem depends on the stage of development of the institution. For example, a newly formed institution will pay greater attention to bolstering its structural and human-social subsystems before concentrating on this subsystem.<sup>1</sup>

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1. See Wendell L. French and Cecil H. Bell, **Organization Development**, Englewood Cliffs, New Jersey: Prentice-Hall, Inc., 1978, pp. 40-45 for a more detailed discussion of subsystems. These authors identify two others –tasks and technological subsystems– which, in the case of micro-enterprise programs can be incorporated into the structural and human-resource subsystems.

**Micro-enterprise assistance institutions are made up of these subsystems, and yet also exhibit an enormous diversity of philosophies, structures, and methodologies on which they base their work. Regardless of how different the institutions are, their emergence as strong, local development institutions with the capacity for self-sufficiency and growth follows a similar path.**

**The five categories that follow touch all issues related to the three subsystems defined above. The first, institutional vision, provides the framework for addressing the other more specific factors in institutional development considered here –the institutional structure, the financial systems, the human-resource system, and the organization's interface with the outside world.**

## **B. AN INSTITUTION'S VISION**

### **1. Vision Defined**

**A non-profit organization in the field of development draws on the philosophy that underlies its founding to define a vision about its work. An institution's philosophy –the set of basic principles that guides its work, encompasses its values, summarizes its beliefs, and orients its objectives– emerges from the collective view of the leaders who initiated the institution's development process.**

**In the early stages of institutional growth, the originators of an institution's vision locate themselves on the board of directors and often hold key decision-making positions within the institution, such as the executive director. These individuals become crucial in defining a long-lasting sense of vision for the institution that can translate into its objectives and its strategy for action. Often, the founders of non-profit organizations in developing countries continue to work with the institution for an extended period of time, thereby increasing their influence over institutional philosophy and direction.**

**The challenge of maintaining a clearly defined vision for an institution becomes greater as the institution grows, as its leadership changes, and as it interacts with a changing environment that influences its decisions. Further, the institution's vision will remain isolated from its work unless it is**

transferred to senior and mid-level management, to its field workers and, through its staff, to the program's beneficiaries. Hence, the institution faces the constant dual task of assessing its evolving sense of vision and at the same time keeping its staff knowledgeable about and accountable to it.

In the case of institutions that conduct micro-enterprise assistance programs, the institutional vision must also reflect a balanced relationship between the social thrust of the institution, which relates to its beneficiary population, and its financial concerns, which relate primarily to its sustainability through self-sufficiency. While complementarity between these financial and social goals may appear paradoxical, the institution's sense of vision must address this dilemma and provide the guidance that a staff needs to maintain clarity in its work.

## **2. An Example of Institutional Vision**

In the case of ACCION and its affiliated programs, the definition of vision has evolved considerably over the last few years. The organization bases its work on the promotion of individual self-reliance through the creation of employment opportunities for the poorest sector of the economically active population in Latin America. This vision has emerged as a set of four principles that both ACCION and its affiliated programs uphold as the backbone of their work (ACCION, 1989b). It is provided here as an illustration of vision as defined by a cadre of non-profit institutions in micro-enterprise assistance programs.

- a. ***The institutions should reach the poorest of the economically active population, with a particular emphasis on women:*** The micro-enterprise sector covers a broad range of types and sizes of businesses, most of which are outside the formal credit system. ACCION-affiliated institutions seek strategies for reaching the poorest of the economically active urban population, thereby reaching an increasing number of women, who predominate in the poorest sectors.

The affiliated institutions utilize very similar methodologies to reach this population; however, a wide variety of strategies are designed and conducted by each institution.

In Colombia, several organizations assist in the creation of family enterprises or "famiempresas". In Bolivia, the female market vendors that line every market in the capital city comprise the majority of this program's beneficiaries, since they are among the poorest of the economically active population.

- b. ***The institution should focus on scaling up its program to reach significant numbers of beneficiaries:*** ACCION's experience demonstrates that the technology and know-how of micro-enterprise programs have been sufficiently tested by a variety of entities to move the institutions beyond the pilot-program stage. In the Latin American context, institutions should seek to establish credit and training programs that strive from the outset to reach increasing numbers of people, reaching several thousand in the first three years. The intent to expand program activity must be present at the beginning of the program, or at the birth of an institution.

It is interesting that some of the newer organizations, especially those created in the last six or seven years and affiliated with ACCION, have embraced this principle as the underpinning of their institutional development and their program strategy. The number of clients that have received credit or training in three organizations –ADEMI in the Dominican Republic, Paraguayan Foundation in Paraguay, and PRODEM in Bolivia– founded in 1983, 1985, and 1986, respectively –totals over 17,000 to date.

- c. ***Institutions should strive for financial sustainability in which the income generated by interest and fees covers administrative costs:*** The concept of financial self-sufficiency is foreign to most non-profit institutions. However, micro-enterprise programs generate revenue that, with appropriate cost reductions, can make an institution self-sufficient. ACCION has established this concept as an integral part of its vision of micro-enterprise assistance. Perhaps it is this factor that most distinguishes institutions in micro-enterprise assistance from other non-profit organizations.
- d. ***Institutions should seek to develop direct links between themselves and financial institutions, to integrate the***

**formal and informal sectors:** In the long term, the private commercial sector should be meeting the credit and other financial needs of micro-enterprises. At present, the gap between these two sectors is so wide that the process of integration that institutions can pursue has been slow. They often begin by creating a point of contact between micro-enterprises and bankers –program beneficiaries make loan payments at banks or maintain a savings account. Later, through ACCION-managed guarantee funds, banks are requested to make their own resources available to these institutions. After receiving and paying back a bank loan, the institution becomes a credible client of the bank.

If an institution wishes to implement a large, growing micro-enterprise program, the definition of its vision becomes an initial building block in program expansion. The concept of program expansion must be expressed directly in the institution's statement of what it seeks to do. The following points suggest factors that can be incorporated into a process of defining vision towards expansion:

- a. ***Involving the staff in defining institutional vision:*** For an institution to maintain clarity of vision and congruence between its vision and its actions, it must involve its staff in reviewing and defining its vision. Whether through staff meetings, annual conferences, or other mechanisms, an institution must solicit consensus among its staff members regarding its vision, and the philosophy that underlies it. People are much more likely to support and uphold something they have helped to create; hence the participation of staff members in this ongoing process contributes to the institution's capacity to carry out its vision. It also prepares the staff for the changes that must occur with expansion.
- b. ***Making the institution accountable to its vision:*** Institutional programs and activities emerge from the vision the institution has molded for itself. As part of its process of growth, the institution must periodically examine the degree to which its programs express its vision. While this task appears simple, the complexity of a vision grounded in development goals, as is the case of micro-enterprise assistance institutions, requires careful and objective

interpretation. In the ACCION case, for example, the vision described encompasses many variables, all of which must be manifested in a balanced way in its work. More importantly, the process of examining vision and action is a most useful tool in enabling the staff to clarify its own thinking about institutional vision and to align its work more directly with it.

- c. ***Making institutional vision an integral part of institutional decisions:*** Whenever an institution makes policy and overarching program decisions, it should measure these against its defined vision. This is the primary responsibility of the board of directors and the institution's director, whose broad-level decisions regarding institutional direction and program development must reflect a grasp of the factors that underlie the institution's existence. This relationship is particularly important in the field of micro-enterprise development, where growing interest and access to funds can sidetrack an organization from its original purpose.
- d. ***Integrating contextual changes into an institution's vision:*** In the case of institutions involved in micro-enterprise assistance, the rapidly changing environment of activities in the informal sector will determine in part the way an institution evolves. In Latin America, where government involvement, multilateral funding and societal attention have cast the informal sector into a spotlight, the challenge for an institution is to integrate these changes into its vision without being swept up by the allure of the attention that informal sector activities are receiving. Maintaining clarity of vision in the increasingly complex and closely observed context constitutes an important goal for institutions that are progressing to expand their micro-enterprise assistance programs.
- e. ***Making expansion part of the institution's vision from the outset:*** Experience demonstrates that organizations that have incorporated expansion into their initial vision of their work have also shown greater capacity to adapt institutionally to program expansion. Even at the start-up and pilot stages, a vision of scaling up activity is reflected in the three institutional subsystems that comprise the organization.

- f. **Selecting a leader to project institutional vision:** Some organizations emerge out of the visionary strength of an individual who is able to translate his or her vision into a strong institution. Persons such as Ela Bhatt of the Self-employed Women's Association (SEWA), or Muhammed Yunus of the Grameen Bank of Bangladesh (GBB), have inspired the creation of exemplary institutions based in part on their capacity to translate their vision into action. Many potential leaders, although still anonymous to an outside world, operate in micro-enterprise assistance organizations. Although their skills in this area may be limited, a key part of their role is to interpret the institution's vision and to assist the staff and beneficiaries to assume ownership of this vision. Often, the executive director assumes this role, although it can also be relegated to a board or staff member who is adept at this task.

### C. THE INSTITUTION'S STRUCTURE

The major issue to address in this section is the degree to which an institution's structure is poised for expansion, and what steps it must take to assure that it is. Assessing the structural subsystem of an institution is a long and detailed process. However, in this discussion, the purpose is to highlight the most important aspects an institution must consider that relate to program growth.

Two areas of analysis emerge in studying an institution's structure from this perspective. First, one must review the **structural configuration of the institution**—the internal compositions of its units and divisions—to determine how it would evolve as its micro-enterprise program expands. Second, one must review the **internal policies and procedures of the institution**, that is, the way it plans, sets up norms, decides, communicates, and evaluates; these constitute a second component of an institution's structure that must also evolve with expansion.

#### 1. Structural Configuration

Most non-profit institutions display similar internal structures, often illustrated in organizational charts. These feature a board of directors, an executive office, a program

department, and a financial department. Additional departments in areas such as legal matters, evaluation and research, training, and others may also exist separate from the program department. In most cases, the finance department is relatively small in staff and resources in comparison with the program department, where most of the staff and activity are concentrated. Finally, the organization operates under one roof.

As micro-enterprise programs have grown, these structures have yielded to others more suited to program expansion. Two major changes have occurred as evidence in most ACCION-affiliated programs.

***First, the financial department has become increasingly important in these institutions.*** Well-trained personnel with strong financial skills have become a requisite for this department. Services in micro-enterprise programs have become more specialized, with a growing tendency to offer credit to more clients. The progression has been towards a "minimalist" approach that does not encompass a variety of other services. This emphasis on credit has enhanced the functions of the financial department. Most organizations currently use computerized systems for financial reporting and analysis. The financial department's input into planning and implementing the program has become a crucial ingredient in determining the program's rate of growth. In fact, the program department cannot operate effectively without close coordination and information exchange with the financial unit.

***Second, institutions have created regional offices or branches throughout a broader geographic area that are equipped to handle program and financial activity in a given zone or region.*** As a program grows, additional offices are opened to increase its outreach. The structure of a headquarters office with several regional offices currently characterizes several of the institutions that have reached the third stage of program growth.

This evolution has also brought about additional internal changes. The institution hires a cadre of mid-level managers to operate the regional offices and thereby expands managerial responsibility beyond the few senior managers who previously managed the institution. The decentralization of functions and decisions becomes necessary under this new structure. In short,

as micro-enterprise programs grow, the layers of decentralized program operation units within the organization's structure also grow.

The Grameen Bank of Bangladesh (GBB), presents an interesting illustration of this structural development. When GBB started its activities it had a central office and branch offices. Today, after enormous program expansion, the GBB is composed of a hierarchy of units that create six layers within the institutional structure: the smallest units are groups of villagers who gather into centres, which respond to branch offices. These branch offices answer to area offices which in turn are accountable to the zone offices. The latter interact directly with the headquarters office in the capital, Dhaka. Hence, in ten years the institution has reached 450,000 landless peasants in 9,500 villages through a highly decentralized system that contains the elements for continued expansion (Hossain, 1988).

A second example of how expansion affects institutional structure emerges from the ACCION-affiliated programs in Colombia. This approach to micro-enterprise development encompasses at least a dozen autonomous non-profit institutions, each structured in a more centralized fashion. Each of these organizations covers a given region or location in the country; in some cases, two organizations may also serve the same area. While these institutions remain relatively small and independent, they operate in a fully coordinated manner, and are accountable not only to themselves, but also to the cluster of a dozen institutions gathered in an umbrella organization –the Association of Solidarity Groups.

The collective vision of the institutions that comprise this association is manifested in various ways: the use of solidarity groups for credit provision; uniform monitoring systems; constant information exchange among the institutions; and periodic workshops and conferences that serve to maintain these entities on a common path. In a sense, they operate as a large decentralized organization with autonomous subsidiaries. In this model, program expansion occurs through the growth of the member organizations, and through the inclusion of additional members in the association. Further, some of the institutions have also opened regional branches, thereby incorporating elements of the GBB approach into this configuration.

While there is no one route to expansion in micro-enterprise development programs, the concept of long-term expansion must prevail from the outset and must be related to the way the institution chooses to structure itself. Most previous experiences show that a process of decentralization or horizontal growth in the institution's structure accompanies the growth of a micro-enterprise program and brings with it implications at every level within the institution. This process is apparent even in the case of Colombia, where the individual institutions decentralize operations as they grow.

## **2. The Institution's Policies and Procedures**

Connected to the structure are the major mechanisms in the institution's system that link structure to action. The following five mechanisms were highlighted at the 1988 conference as most important for this discussion:

- a. **Planning:** In the context of program growth, this factor relates not only to what the institution will do and the goals it establishes for itself, but also to how it will evolve structurally to accomplish its work. Planning, therefore, operates at two different levels, and involves different individuals for each.

On the one hand, the organization is planning the short-term – annual – accomplishment of its objectives, by setting goals that are usually expressed in terms of new participants reached, loans disbursed and training/technical assistance conducted. Field staff, regional managers and others within the staff participate fully in this process. On the other hand, the planning function must also look beyond the next year or two and lay the building blocks to expand the structure of the institution to respond to program growth. Board members, the executive director, and others in the more senior positions, should participate in this planning level.

- b. **Norms and Procedures:** An institution that is intent on expanding its sphere of activity must demonstrate seriousness in the manner in which its norms and procedures are established from the outset. Non-profits, especially when small and functioning in one office, often maintain a relaxed approach toward this area of institutional development. In many instances, they operate without

written guidelines to steer management decisions. This level of procedural informality cannot enable an institution to grow.

Any plan for program expansion will require considerable energy in this area from the outset. On the programmatic side, for example, the credit policy and the procedures for its implementation must be clearly spelled out in a document that is available to all staff members and also periodically revised. The same is true for other basic guidelines such as personnel policy, reporting systems, and lines of authority. Most non-profit organizations are likely to identify similar sets of norms and procedures that are necessary for effective operation.

- c. **Decision-making Process:** The institutional decentralization that parallels program growth requires that the decision-making function within the institution be designed to become decentralized. Unless the two go hand in hand, even a flawless expansion-oriented institutional structure will fail, because it will remain controlled by a few.

Individuals operate better when they have a voice in making decisions that affect their work and lives. In micro-enterprise assistance programs, decentralized decision-making also enables program expansion to take place. Some of the fastest growing and most effective programs gradually turn over an increasing number of decisions to field and regional staff. These decisions pertain primarily to approval of loans, level of activity, and new geographic areas to cover.

One of the most demanding challenges for an executive director is identifying which decisions must involve him or her at the different stages of growth of a program.

- d. **Communication Flows:** When an institution grows to two or more offices, its internal system of communication shifts dramatically. The importance of information flow from the bottom to the top becomes more important when most of the institution's activity occurs in branch offices.

Decentralization can turn into fragmentation if the communication channels among its member parts are not

functioning properly. Communication systems must become more structured, must rely more on the written word, and must include specific periodic activities that facilitate the flow of information.

3. **Controls and Evaluation:** Decentralization also means that the bulk of the organization's daily activity – which translates into hundreds or thousands of monthly loans – rests in the hands of its mid-level managers, who direct the regional offices. The written and verbal flow between the central office and the branches will determine the degree to which the program operates efficiently. Hence, the establishment of control systems that are simple, yet provide the institution's directors with timely and key information, is one of the most important ingredients of effective program expansion.

### 3. Transforming the Structure of Non-profit Organizations

Perhaps the most difficult question that emerges from the discussion of program expansion and institutional development is the degree to which a non-profit institution's structure is appropriate for carrying out nationwide micro-enterprise assistance programs. Certainly the traditional, vertical, one-dimensional structure that many associate with a non-profit proves inadequate for building larger programs, and shows considerable deficiencies even with smaller programs.

Non-profit institutions have experienced these limitations and have found creative ways to revise their structural make-up to conduct micro-enterprise programs successfully. The institutions that illustrate these changes today are very different in composition from those of several years ago. The examples that have preceded in this discussion highlight some of these changes.

***As the new threshold of program expansion presents itself, these same institutions may have to undertake the additional structural changes that will transform them from traditional non-profit institutions into an alternative structure that is better suited to this new level of expansion.*** This contention supports the concept of the institutional evolution of non-profits, and argues against the notion that once a non-profit

institution has reached a maximum level of activity, it must relinquish its work. In the final analysis, the process of institutional evolution may lead a non-profit to shed its current status and assume a new one, perhaps one more closely resembling a financial-sector institution. This structural transformation may call for continued decentralization; it may require a new structure; or it may lead to exploring various structural options that can be combined. For example, the creation of a credit union alongside the non-profit organization to assume the functions of lending and savings mobilization, is one option under consideration in Colombia. In the case of Bolivia, the fundamental feature of expansion involves the creation of a micro-enterprise development bank that would replace the existing non-profit organization.

How institutional transformation takes place will vary among institutions and country contexts. Nevertheless, closely linked factors emerge that each institution must consider as it moves along its growth path:

- a. ***The Role of its Board and Staff:*** An institution with a committed and active board of directors is in a much better position to tackle these innovative yet risky endeavors than one that must depend primarily on staff. In fact, revising an institution's structure and enacting these changes should remain a board's responsibility. Hence, a strong, active and committed board constitutes a first prerequisite for advancing in this institutional evolutionary process.
- b. ***Legal and Regulatory Issues:*** The process of program expansion may require that the institution assume additional activities, such as capturing savings. Its non-profit status may limit its capacity to undertake new ventures and it may explore other institutional modalities. The laws and regulations that exist in each country will be a determining factor in how an institution chooses to structure itself.
- c. ***Feasibility of Institutional Changes:*** Parallel to a plan for program expansion, which requires a feasibility-study process, the institution should also seek assistance in exploring the alternatives in institutional evolution. Assessment by an outsider who has substantial knowledge of non-profit organizations and of the country's context will

provide important information in this process and suggest alternatives that the institution may have ignored.

- d. **Financial Resources:** Any program expansion will require a considerable infusion of funds for loans, technical assistance and other inputs to aid the institution's evolution. As discussed below, locating the funds for program expansion constitutes one of the biggest challenges for non-profit organizations, and must occur in tandem with the process of transforming the institution's structure.
- e. **Human Resources:** Program expansion will require the addition of staff members who have managerial and financial expertise. It often means that the institution will expand its mid-level cadre of professionals, as well as its field staff. The skills that are needed, and the training these individuals will receive, should be clearly spelled out. Establishing a methodology for hiring and training new staff can assist in the process of team building.
- f. **Affiliation with U.S. PVOs:** As a local non-profit organization evolves, so should its relationship with its U.S. partner agency. The latter often provides technical assistance, and a component of structural transformation should focus on the relationship between these organizations and on assuring that technical assistance is adapted to the institutional changes.

#### **D. THE FINANCIAL SYSTEMS**

Perhaps the most dramatic transformation for institutions that conduct micro-enterprise programs of significant magnitude appears in the area of financial management and analysis. The financial techniques needed to manage a program properly require know-how and technology that non-profit institutions often lack, but have sought to acquire by hiring trained financial persons and by introducing computerized information systems.

All financial management and analysis revolves around the institution's sources and uses of funds. The discussion of financial systems among program directors of micro-enterprise programs that are moving toward expansion focuses on four

broad areas. The first two, under the rubric of **financial management**, incorporate policies and administration. The second category, **financial analysis**, integrates portfolio analysis and self-sufficiency analysis. Most financial issues related to program expansion can be incorporated into these categories.

Each section presents a summary of factors, including some that programs can fail to institute from the beginning. These are highlighted because they are the most relevant to a process of expansion and because they undergo a fundamental shift in focus as the program grows.

## **1. Financial Management**

### **a. Policies:**

- o **Fundraising Policies:** As a micro-enterprise program grows, its sources of income should change, expanding from standard donor grants to include private-sector contributions, soft loans, commercial loans and other inputs. The fundraising policy of the institution also merges with the institution's capacity to generate its own income and to develop an asset base. The institution undergoes a fundamental shift from a grant-receiving entity to one that aspires to a gradual reduction of subsidies. The nature of its fundraising effort therefore changes. Income sources are now sought not only to cover the cost of programs but to carve the way for long-term sustainment.

This changing policy also reflects a progression in thinking within these non-profit organizations. They have evolved from focusing on a fundraising mode, to cover costs, to establishing serious pricing policies that examine the real cost of providing services. They become more concerned with the needs of the client who will pay for these services and with keeping their costs competitive.

Once an institution defines its fundraising policy as a tool towards self-sufficiency, it begins to explore creative, experimental and at times risky alternatives far beyond grant-seeking. Examples can include capturing savings from borrowers; obtaining funding for a guarantee fund and

thereby gaining access to commercial loans; and conducting local fundraising efforts to build up an endowment or asset base for the institution.

This process often requires technical assistance from individuals who have skills beyond proposal preparation and who can address these more complex issues in a fundraising strategy. It also requires that the institution begin forging linkages with groups and institutions previously considered outside the non-profit realm, such as financial institutions, the central bank, chambers of commerce, the private sector, and others.

- **Credit Policies:** A relatively simple task that begins at the outset of a credit program, an institution's credit policy becomes an important instrument both for achieving self-sufficiency and for conducting an effective program. The factors that enter into a credit policy respond to the needs of the borrowers as well as to the needs of the institution. A credit policy must reflect an understanding—as expressed in interest rates, types of loan, terms of loan, payment schedule and others—of the particular needs and potential of the program's beneficiaries. At the same time, the credit policy must take into account the expansion plans of the program, which require a much more sophisticated analysis and understanding of how to disburse credit. Further, it requires the capacity to convert a given credit policy into a tool for short- and long-term financial projections for the institution.

In short, as the program grows, the importance of the institution's credit policy as a tool for its planned expansion becomes greater. The role that the credit policy plays in its expansion effort reinforces the need for well-trained financial analysts in the institution.

- **Risk Protection Policies:** Program expansion involves risks that can be minimized through the policies the institution establishes. The major source of risk emerges from repayment and default problems in the credit fund that decapitalize the program in a short time.

Although programs may not entirely establish a loan loss reserve or a mechanism that will take defaults into account, this is an indispensable component of planning the long-term

**sustainability of the micro-enterprise effort because it assists in maintaining the real value of the credit fund. These policies should certainly be instituted during the model stage and revised as the program grows.**

**Insufficient liquidity constitutes a second type of risk in a program, often experienced when grant or loan funds are delayed or when a program cannot elicit resources to continue its expansion. Under these circumstances, the institution must set up a policy that enables the credit program to operate on its own rotation and to keep the beneficiaries secure about the reliability of future loans, which is a major incentive for repayment. In some cases, capturing savings, a percentage of which can be used for lending, becomes an important way of addressing this risk.**

**The most difficult and damning risk for these programs presents itself through high inflation rates or hyperinflation such as those experienced in several Latin American countries in the past few years. The credit fund loses its value in real terms, and real interest rates are not charged, thereby further decapitalizing the institution. It is important to highlight the difference between an inflationary environment within which most programs operate and are able to maintain their real value, and a hyperinflationary situation where market distortions are so high that the program gradually diminishes in size.**

**b. Administration and Control:**

- o *Information Systems:* The quality of the financial management of an institution depends on the information system it has established to collect, process and analyze information. This constitutes the one area in which most resources, time and effort will be spent to yield something effective, and the complexity of this topic remains outside the scope of this document.**

**Computerizing an information system is of course a must for a micro-enterprise program. Interestingly, programs that begin their activities with a computerized system fare better in information collection and analysis than those that convert from manual to automated systems after a period of time. A**

shift in the information system midway through the growth of a program creates considerable disruption and lends itself to significant gaps and mistakes in the database needed for key decisions.

At the same time, a computerized system that is designed to facilitate financial management must enjoy certain characteristics or it also will create a bottleneck. Its monitoring and control function requires software that is custom-designed for micro-enterprise programs and non-profit organizations. Its accounting system must flow from a logical chart of accounts. Among the most important features of this monitoring system are:

- fund accounting that enables the institution to properly track income and expenses;
  - an input method that requires information be punched in only once for all analysis;
  - both the software and the hardware capacity to grow and incorporate expanding and decentralized operations;
  - preparation of a handful of reports that are timely, straightforward and adequate for decision-making. These include reports on the credit fund, such as daily disbursements, daily recuperation, delinquency specified by time period, interest earned, and portfolio analysis by office and field worker. Basic financial ratios related to liquidity should be included. Additional periodic financial reports, such as profit-and-loss statements, income statements and financial statements for the institution, are also necessary.
- o ***Budgeting and Financial Projections:*** Budgeting constitutes a key financial planning tool for the institution.<sup>2</sup> It provides control over a program's performance. It also enables a manager to compare a budget with real expenditures and to make the necessary adaptations over

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2. For a detailed explanation of these topics, see Robert Peck Christen. 1989. **Financial Manager's Manual for Micro-business Credit Program Operators.** Forthcoming. ACCION International, Cambridge.

time. Most institutions develop annual budgets that are divided by program or regional office activity and that summarize the operational and credit resources required for program implementation. During the first three to five years—while the program is at the model stage and at the consolidation-with-growth stage— one major challenge is to reach its break-even point.

Financial projections assist an organization to calculate its break-even point by determining its level of activity under certain conditions. These conditions fall into two categories. Those pertaining to the program itself include client location, size of loan and terms of lending, level of effort per field staff member, salary cost structures, repayment rate, and general administrative issues. Assumptions about external economic variables such as inflation, exchange-rate fluctuations and prevailing interest rates also enter into this exercise.

The budgeting and financial process provides an excellent forum for the management, the board members and the staff to define the program's priorities and goals and to apply these in a budget. Several considerations help an organization conduct an effective budgeting and financial projection process:

- Clarity in the institution's goals and objectives is paramount for sound budgeting. It enables the organization to formulate them in the budgeting process and to establish clear indicators of program performance that can be measured later against actual output and expenditures.
- Budgets and financial projections must be realistic. Because they are sensitive to minor changes in the assumptions that underlie them, these assumptions must be calculated with careful thought and sufficient information. A program can suffer more from optimistic projections than from conservative assumptions about its work.
- Budgets must contain a margin of error for unforeseen events, some of which can be caused by miscalculated assumptions. For example, if project demand or the repayment rate are lower than projected, these factors

will affect the overall budget. Conservative estimations regarding the project's performance are one way to build in a sufficient margin in budgets.

Budgeting and financial projections must be complete but kept simple. While there are sophisticated long-range tools for budgeting and planning, these can be time-consuming and unnecessary for institutions in the early stages of program development. As the program matures and reaches the expansion stage, it can turn to more complex tools that predict portfolio projections with great accuracy.

## **2. Financial Analysis**

a. **Portfolio Analysis:** Analyzing the credit fund portfolio is a daily task in micro-enterprise assistance programs. Several factors receive particular attention as the fund grows:

- o **Rotation:** A basic characteristic of micro-enterprise programs is the fast rotation of their portfolios. With loan terms as short as six to eight weeks, a portfolio revolves several times each year, enabling these programs to lend significant funds with a relatively small original fund. In Colombia, for example, ACCION-affiliated programs have lent out nearly US \$5 million in loans in five years on an original \$400,000 credit fund.

This feature of micro-enterprise programs requires careful and constant analysis because it is a determining factor in how quickly a program can grow.

- o **Repayment Rates:** Along with volume and adequate institutional capacity, the program's repayment level is a key contributor to the program's sustainability. In fact, program expansion cannot be considered unless a program has demonstrated a consistently adequate repayment rate over at least two years. Changes in a program's repayment rate, and the reasons behind those changes, must be identified and studied as soon as they happen in order to take necessary actions.

Daily assessment of payback patterns also requires timely information about loan behavior which the staff can analyze

for corrective measures. In the program in Bolivia, for example, the repayment rate has been above 99.2 per cent during the first two-and-a-half years of operation. Staff members attribute this success in part to a system for studying delinquency that identifies overdue payments hours after they happen, and initiates a flurry of activity to assure recuperation.

Understanding the causes of delinquency enables an institution to identify the factors within its own policies or manner of operation that may contribute to poor repayment. Before considering the expansion of a program, any such institutional constraints to adequate repayment must be revised. These can include the number of beneficiaries per field worker, the terms established for payments, the sense of ownership the borrowers feel towards the program, and many others.

- o **Break-even Point:** Every program strives to reach its break-even point, when the revenues it generates cover the costs of the program. This point arrives once the program attains a portfolio size that must be maintained, which leads in turn to managerial decisions about credit policy, staff size, and the pattern of growth for the program. Long- and short-term planning also emerge from these calculations.
- b. **Self-sufficiency Analysis:** Institutions that implement micro-enterprise programs define program self-sufficiency as a major goal. The most important factors that contribute to self-sufficiency are: the size of the program –volume is necessary to generate enough income to cover costs; the cost of money– the interest rate that the program uses should reflect the cost of lending; and repayment –the level of repayment in a program also will affect program revenue.

There are two ways of defining self-sufficiency that an institution must utilize to determine its own level:

- o **Operational Self-Sufficiency:** Most commonly used by donor agencies and implementing organizations, this concept of self-sufficiency operates when income is equal to or greater than expenses. Programs calculate the operating costs of delivering credit and compare them to the income obtained through interest and other fees. The ACCION-

affiliated programs demonstrate that operational self-sufficiency improves as a program advances successfully through its stages of development, and reaches or exceeds 100 percent at the third stage, consolidation and growth. Before proceeding to the fourth stage of expansion as defined here, a program should have established its capacity to cover its operational costs. Programs that provide extensive training and other services tend to separate these costs from the costs of lending in order to establish the self-sufficiency of the credit operations.

- **Financial Self-Sufficiency:** The above concept of self-sufficiency, while a useful tool for a micro-enterprise program, remains incomplete. It does not take into account additional factors that contribute to self-sufficiency. Inflation, for example, not only decreases the real value of the credit portfolio, thereby lessening its ability to cover rising operating costs, but it also reduces the number of borrowers that it can reach (Christen, 1989a).

Financial self-sufficiency measures the ability of programs to cover both direct operating and financial costs and to maintain the real value of the portfolio. In relation to long-term sustainability, programs must consider the importance of maintaining financial self-sufficiency, especially in contexts where inflation is high. In these cases, programs may allocate a considerable percentage of earned income to maintain the real value of their portfolios and thereby are less able to cover operating costs. As programs gear up for expansion, they must understand how to use these tools for measuring self-sufficiency and must apply them to their own programs.

## **E. HUMAN RESOURCES**

This area of institutional development considers the individuals who compose the institution. Through the structural subsystem of the institution, they channel their skills and abilities to carry out the work of the institution as well as to give it an identity. This area receives the greatest attention in the field of organizational development because many of the interventions for institutional development use the human-resource subsystem as the initial vehicle for changes in the

institution (Lippitt, 1969; Huse, 1975). Also, the unspoken fallacy that equates human-resource development with institutional development often contributes to this emphasis. In fact, human-resource development is one component or subsystem of a larger whole.

The discussion of this subject from the perspective of program expansion concentrates on four areas: profile of the staff; administrative policies; selection and recruitment; and incorporation of staff into the institution. While the first two areas are guides for managing and developing staff, the latter two are processes that strengthen this subsystem.

### **1. Profile of the Staff**

Like any institution that grows, a micro-enterprise assistance program usually starts with a skeleton staff of several persons, and gradually increases its numbers, sometimes doubling or tripling in size to respond to the program's growth. The institution's approach to building a long-lasting human-resource base for the program emerges as one of its most challenging and important tasks. It involves hiring and training individuals to carry out tasks; more importantly, it is the most significant way in which an institution's vision is interpreted and applied. Therefore, the profile or portrait of the staff that the institution seeks will contribute to identifying the appropriate resource base. Four areas of consideration contribute to establishing a clear profile of the staff in micro-enterprise programs:

- a. **Human Quality:** In an effective micro-enterprise program, the beneficiaries should have access to most of the staff. Even the internal auditor will spend time in the field interviewing borrowers. In fact, when the program focuses on the needs of the beneficiaries, it engages everyone in exchanges with them. Each staff member must therefore exhibit a capacity for quality interaction with low-income-level populations. This quality is often found in the staff of non-profit development organizations, whose background tends to be in the social sciences and in social development work. In the case of micro-enterprise assistance programs, however, institutions also draw staff members from the banking sector, where knowledge of and experience with a low-income population is scarce.

This sense of "human quality" is crucial for the field staff, which can operate effectively only by establishing a strong, trusting relationship with the program beneficiaries. Human quality reflects a conviction that low-income people are capable and creative individuals who merit an interaction based on respect. By and large, most field staff arrive at the job with strengths in the area of personal interaction or quickly develop them. Ironically, however, members of the technical staff often lack these skills because often they have not worked with this population. In short, everyone on the staff must share a sense of commitment to both the institution and the people it reaches: in ACCION-affiliated programs, this is labeled "mística".

- b. **Creativity:** Most formal educational systems that graduate the staff of micro-enterprise programs do not foster a creative, analytical approach to work. The traditional formal education systems that prevail throughout the developing world often rely on learning by memory and rote methods. It is much easier to find field and technical staff who will follow instructions without questioning them rather than persons who will reflect critically on their work and contribute to improving it.

Because the nature of work in a micro-enterprise assistance program requires a great deal of self-supervision, especially among the field staff, it is imperative to identify individuals who have the capacity to develop a creative, analytical streak in their work. Fostering this characteristic in the staff, through the management style, workshops, and informal interactions, contributes to establishing an effective decentralized system of operations. As discussed below, an important part of incorporating an individual into the institution includes training in fine-tuning his or her analytical and creative skills.

- c. **Team Work:** As micro-enterprise assistance programs grow, they develop small units of operation through regional or branch offices. Each of these units must work as a team to carry out its work in an effective manner. Often, team-building skills must be present in the upper- and mid-management levels before they can be instituted among field workers. Because the level of daily activity is so high for

both field and office staff, it is very easy for programs to fragment themselves into small isolated units and to lose sight of the overall effort.

Persons who have experience with a consultative management style and with the capacity to build a working team are essential in micro-enterprise assistance programs.

- d. **Technical Skills:** The expansion of micro-enterprise assistance programs requires the staff to acquire varied skills. The field workers, for example, may have only a high-school degree or may have completed their university degree only recently. To work in micro-enterprise programs, they need skills in community development, as well as in finance for credit provision and management. On-the-job training characterizes much of the field worker's activity. After one or two years, this person can be well versed in micro-enterprise development and engage in training and technical assistance as well.

For other positions, however, technical knowledge is paramount. Staff in the financial and the computer departments, for example, must demonstrate considerable expertise in their fields in order to carry out the roles required by an expanding program. These are the two areas where most programs suffer as they move along their growth continuum; they repeatedly find the need to hire persons with a background in banking rather than social development. Integrating those persons who have the needed skills into situations where they must understand the dynamics and complexities of micro-enterprise assistance represents one of the harder tasks for senior management.

## **2. Administrative Policies**

In the early stages of program growth, an institution should develop personnel policies and spell them out clearly in a manual. Most non-profits in micro-enterprise assistance, however, demonstrate a gap in this area, in part because the task of handling personnel tasks falls on the executive or financial director, both of whom are also responsible for more immediate priorities. Hence, hiring occurs as the need arises

with some written guidelines but mostly in a generally informal manner.

The growth of a program, especially one that receives a new infusion of capital, requires quick hiring of persons to fill a variety of positions. Written policies on which to base selection and recruitment activities should exist and be reviewed annually, and should include at least the following:

- a. **Guidelines to Personnel Policy:** These include the factors that determine how an institution hires personnel and usually takes into account labor and other codes in each country.
- b. **Job Description:** Each position in the institution must include a clear definition of responsibilities. As new positions emerge, creating this definition should precede hiring.
- c. **Salary Policy:** The range of salaries for all positions, including the benefits package and other factors should be included.
- d. **Incentive Policies:** Since most non-profit institutions pay relatively low salaries, some have incorporated incentive packages that increase a person's income level or offer special training. Especially in the case of field workers, an incentive package based on the size of their portfolio, its repayment rate, the new entrants into the program and other variables, can assist in stimulating motivation and rewarding effective work. ADEMI in the Dominican Republic, has had enormous success with this approach (Gomez, 1989).
- e. **Staff-development Policies:** Linked to the incentive package, an institution must determine the level and type of staff-development activities it will undertake. This component of a personnel policy is different from incentives because it identifies training for staff to be conducted as part of improving their capacity to work. Often, budgetary constraints eliminate the flexibility an institution maintains in this area, however, there are many low-cost methods of including staff development into an overall personnel policy.

- f. ***Evaluation of Performance:*** Each institution requires an established system for assessing the quality of each staff member's work on a regular basis. There are a wide variety of ways to conduct this task, including ones that are participatory and that pay special attention to weak or deficient areas of a person's work.

### **3. Recruitment and Selection**

Hiring staff is a time-consuming, costly task. The process of recruiting and selecting new personnel requires that the institution have an established system for hiring, which can vary depending on the position under consideration. For example, as a program expands and opens new branches, an institution may hire five, ten, or more field workers at the same time. It may also need to strengthen its financial department and to increase the number of regional directors.

Especially in the case of hiring field workers, there are several creative and productive ways of operating. For example, an initial newspaper ad can yield many possible candidates whose number is then narrowed to around thirty for initial interviews, conducted by regional directors and their staff. These interviews further limit the group of applicants to around twenty. The remaining candidates are then invited to continue in the process of selection by participating in a five-day training program for field workers that the institution provides as part of its hiring technique. These twenty applicants receive the training in micro-enterprise assistance, and in the process undergo close observation in the areas of personal interaction, technical skills, capacity to work with others, initiative, creativity and other important assets that are difficult to capture in interviews.

By the end of the five days, the institution identifies the most promising candidates for the field worker positions, and in the process has already trained them for their work. The remaining applicants receive a letter acknowledging their participation in the training and remain in the institution's file for future openings. Hence, the selection process has allowed for close observation while incorporating the training needed for the job.

A second example of hiring field workers is based on a series of questionnaires and interviews conducted by field and mid-

level staff. The questionnaires ask a wide variety of questions and are designed to highlight the analytical capacity of the applicant as well as his or her ability to interact with the beneficiary population. The staff analyzes the answers not as right or wrong but on the quality of thought and coherence. On the basis of their assessments, the executive director interviews a small number for the openings available, and the positions are filled through consensus.

Several characteristics emerge from these approaches to hiring that underlie their effectiveness:

- o the job description is clear, outlining in detail the responsibilities assigned;
- o the institution has established norms for hiring that guide the staff in the process;
- o there is considerable involvement on the part of staff in the hiring process, some of which extends beyond the traditional one-to-one interview mechanism;
- o training and other tools, such as questionnaires, are integrated into the hiring process;
- o the addition of new members to the staff receives a detailed and careful institutional approach.

#### **4. Incorporation into the Institution**

Once the institution has hired its staff and continues to replenish or expand it, the most demanding task is the integration of the staff into the institution. While there are a variety of methods for accomplishing this, staff training is one of the most powerful and important.

Two major types of staff training are most appropriate for human-resource development in a micro-enterprise program. The first, *training in analytical thinking*, seeks to provide tools for disaggregating, analyzing and solving problems. It utilizes the daily work experience of the staff as the point of entry for its content. For example, field workers and regional coordinators can choose specific aspects of their work, such as program

promotion or delinquency issues to discuss, using a process of analytical thinking that helps new staff members understand the causes and the solutions in each case. Equipping the staff with the capacity to utilize analysis in their daily work requires short, periodic training sessions. These sessions can combine broader relevant topics such as an analysis of poverty, the informal sector, and approaches to development, with more specific hands-on topics. This training requires one or two hours a week and can be built into the staff's working schedule on a regular basis. It is conducted by someone on the staff with participatory techniques and case examples, and is low cost.

The second type of training emphasizes *technical skills*. While any staff training session will combine both analytical and technical skills, it is important to highlight the latter because many assume that staff members have mastered technical skills that in fact remain outside their grasp. In micro-enterprise programs, "how to" relates to a variety of activities, including calculating interest rates, developing simple profit-and-loss statements, interpreting computer printouts, and assessing program impact. The program's staff in particular should receive constant, periodic upgrading of financial and other technical skills.

Other activities, such as training outside the organization and visits to micro-enterprise programs in other countries, complement the human-resource development function of an institution. Often, the opportunity to observe a similar program will inspire staff members to suggest instituting more creative or effective approaches in their own work. In the case of ACCION, staff trips to other programs have been an effective way to transfer additional skills. In situations where several organizations work in tandem, as is the case in Colombia, periodic two- or three-day workshops for one or two staff members from each organization has been one mechanism for providing this training.

Clearly, the above examples encompass the major areas that an institution must address in the human resource subsystem. Staff training as a focus for human-resource development becomes important in two ways: it prepares the staff to assume increased technical and analytical responsibility under expansion; and it integrates institutional development factors that in part determine the institution's strength.

## **F. THE INSTITUTION AND ITS CONTEXT**

The final area of consideration for institutional development looks outward from the organization and examines its interaction with its environment. The organization's interface with other institutions and individuals begins at the start-up stage of growth and assumes greater complexity and importance as the institution moves toward expansion. During the second and third stages of program development, an institution will begin to dedicate considerable time to this subsystem and will often develop a strategy to promote greater interaction with certain groups in the society.

Five major categories of players comprise the environment for most micro-enterprise development institutions; they are discussed briefly below.

1. ***Client Participation.*** Micro-entrepreneurs make up the first category. As beneficiaries of the institution's programs, they will ultimately determine the value and usefulness of its work. For most of the staff in the institution, developing a trusting relationship with the borrowers while conducting an efficient, closely monitored program is the basis of their activity. Many of the topics discussed above, especially in the areas of human resources, assist in developing a strong relationship with the program's beneficiaries. Additionally, arrangements such as beneficiary committees or elected representatives create a structure within the institution to interact directly with the beneficiaries and to include them in the evolution of the program.
2. ***Commercial Sector Institutions.*** Each micro-enterprise development institution can develop a strategy for strengthening its interaction with this sector that is based on specific expected outcomes: collaboration in working with the informal sector; increasing the banking sector's knowledge of micro-lending; learning important financial tools from the banks; obtaining relevant training and knowledge; and securing resources for program expansion. This interaction often occurs at the initiative of the non-profit institution; its tenacity will be the most important contributor to achieving results. In many cases, board members become the conduit to the financial sector and can

become important players in shaping substantive changes, such as the creation of second-tier lending institutions, or the revision of banking policies.

As the program grows, the institution's relationship with banks and other commercial entities changes. In the early stages, a program will emphasize linking borrowers with a bank through savings deposits, repayments made at bank branches and other mechanisms to begin to bridge the gap between the bank and the institution's borrowers. Later, the institution will seek loans from the bank and will obtain a guarantee to assure their approval. Finally, the institution will attempt to obtain a credit line from the bank and will use its own asset base and experience as guarantee for the loan.

3. ***Non-profit and Development Institutions.*** The third area constitutes interaction with other institutions, including non-profit organizations, universities, and other organizations. Inter-institutional exchange in this case implies establishing links based on specific objectives that are defined by each institution. For example, an institution's interaction with other non-profit organizations could focus on a variety of objectives: exchanging information; collective advocacy around common themes; planning a broader agenda for micro-enterprise development; taking on specific functions, such as training; or several others. Building effective relationships with these institutions requires clarity about the reasons behind the interaction and the results that will emerge from it.

In a similar way, institutions outside the country, especially non-profit development organizations in the United States (U.S. PVOs) constitute a source of information, technical assistance, financial resources and support for the indigenous non-governmental organizations. Few dispute the value of establishing direct links between a local non-profit institution and U.S. PVOs; however, the nature of that relationship and its concrete results will determine its worth. Based on its institutional vision and its plans for program expansion, the local institution should define the objectives of this relationship and establish a collaborative, long-term commitment.

4. **Government.** A fourth category of interaction relates to the public sector and constitutes one of the most complex tasks for non-profit institutions. In Latin America, the last five years have shown increasing governmental interest and involvement in the informal sector. Policy initiatives, new programs, and resource allocation are the most obvious examples and are already apparent in many countries. Non-profit institutions must design a strategy for interacting with the public sector, recognizing that in most cases governments are in the process of defining their own policies and initiatives towards the informal sector.

Because governments impact on the work of non-profit institutions in a wide variety of ways, the institution must decide where to channel its energy in interacting with the public sector. For example, regulations can restrict or expand the mandate of non-profit institutions; influence resource flow to the informal sector; regulate economic activity at the micro-enterprise level; and influence production and marketing factors at a macro level that also affect micro-entrepreneurs. By the same token, government programs can define the agenda for reaching this population; establish policies in terms of lending that may set the agenda; involve new ministries or other government entities in program implementation; and determine the way resources are allocated.

As governmental involvement unfolds, a non-profit institution must be prepared to understand the reasons behind the government's decisions and to participate in this process in a way that does not detract from its major activity as a provider of credit and training to micro-enterprises.

5. **Donor Organizations.** These comprise the final category. As micro-enterprise development institutions proceed to expand their programs, their relationship to donor institutions will change. Once micro-enterprise programs reach the expansion stage, their source of funds is not limited to grants, but includes soft loans and other mechanisms to expand their portfolio. These programs are now willing to consider larger sums of more expensive money available through multilateral agencies, and therefore must respond to the requirements and procedures these carry. Interaction with the donor becomes more

**complex than a grantee-funder relationship and requires that the institution determine its funding needs and work with the donor agencies based on its own funding needs and repayment capacity.**

## **G. CONCLUSION**

Planning for expansion in a micro-enterprise program requires a detailed look at many of the steps outlined in this document at a level of detail that is beyond the focus of this discussion. Financial projections and analysis in particular will demand detailed study, usually with the assistance of outside advisors. ACCION programs in Bolivia and the Dominican Republic currently are undertaking these steps. Other factors, such as legal and regulatory considerations, addressed in a brief manner here, demand considerable research and expert assistance. Other issues related to adequate information systems and management style are also priorities for consideration.

Institutional development issues as presented here constitute the initial yet most challenging step for non-profit institutions that are intent on expanding micro-enterprise programs. The topics covered here will provide the backbone for all expansion efforts. Each institution can explore its own capacity for expanding its micro-enterprise programs by reflecting on its development in these areas.

## EXPANSION AND INSTITUTIONAL DEVELOPMENT: ISSUES TO CONSIDER

VISION	INSTITUTIONAL STRUCTURE		FINANCIAL SYSTEMS		HUMAN RESOURCES		CONTEXT
DEFINITION	STRUCTURAL CONFIGURATION	PROCEEDINGS	FINANCIAL MANAGEMENT	FINANCIAL ANALYSIS	GUIDES AND PROCEDURES	PROCESSES FOR HUMAN RESOURCES	CLIENT PARTICIPATION
VISION STATEMENT	DECENTRALIZATION	PLANNING	POLICIES	PORTFOLIO ANALYSIS	STAFF PROFILE	RECRUITMENT & SELECTION	COMMERCIAL SECTOR INSTITUTIONS
STAFF INVOLVEMENT	- Role of Board and Staff	- Norms and Procedures	- Fundraising	- Rotation	- Human Quality	- Clarity	NON-PROFIT AND DEVELOPMENT INSTITUTIONS
ACCOUNTABILITY TO VISION	- Legal/Regulatory Issues	- Decision Making	- Credit Policy	- Repayment Rate	- Creativity	- Established Norms	GOVERNMENT
VISION AS INTEGRAL TO DECISION	- Feasibility	- Communication Flow	- Risk Policy	- Break-even Point	- Team Work	- Integration of Training	DONOR ORGANIZATIONS
VISION AND INTER-ACTION WITH CONTEXT	- Financial Resources	- Controls and Evaluation		- Self-sufficiency	- Technical Skills	- Staff Involvement	
EXPANSION AND VISION	- Affiliation with US PVO's		ADMINISTRATION & CONTROL		ADMINISTRATIVE POLICIES	INCORPORATION INTO INSTITUTION	
			- Information systems		- Personnel	- Training as Tool for Staff Development	
			- Budget and financial projections		- Salary	- Analytical	
					- Incentives	- Technical	
					- Staff Development		



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### CHAPTER III

## FACTORS THAT INFLUENCE EXPANSION IN MICRO-ENTERPRISE PROGRAMS

## **A. INTRODUCTION**

The concept of scaling up micro-enterprise programs is extensive and complex. In this document, the discussion has limited itself to the experience of one organization, ACCION, and its affiliated institutions, and has emphasized the relationship between institutional development and program expansion. For non-profit organizations, this relationship becomes the most important prerequisite for the transition from the early stages of program growth to large, national micro-enterprise efforts.

This chapter pursues the discussion beyond institutional development to address additional factors to consider in the analysis of expansion endeavors. The first part highlights the major conclusions about expansion stated or implied in the previous chapters. This summary of the major ideas underlying this approach to expansion serves as one step in the process of delineating the institutional, programmatic, and structural implications behind program expansion.

Second, this chapter highlights additional key issues to be incorporated into any debate about program expansion: the sustainability of programs; methodological considerations; the contextual factors that influence expansion; and the limitations of expansion for micro-enterprise promotion. The discussion explores the main issues under these subject headings and raises questions that must be addressed in the ongoing debate and analysis.

## **B. SUMMARY OF MAJOR FINDINGS**

### **1. On Expansion**

- a. ***Expansion of micro-enterprise programs can be defined in terms of numbers of persons reached by a specific service.*** It implies an increase in the supply of a service, in this case, credit for small working capital loans to an ever-increasing population of low-income producers. An assumption, based on current experience and recent studies, is that the demand for increased services exists in every urban center, particularly in the densely populated capital cities.
- b. ***The expansion of micro-enterprise programs is the culminating phase in an overall scheme that identifies the stages of growth of micro-enterprise programs.*** In this sense expansion represents part of a methodology that has proven sound and applicable in a variety of settings. The experience of the last five years among ACCION-affiliated programs demonstrates a pattern in the evolution of these programs. This discussion attributes this evolution to the presence of a variety of identifiable factors. Program expansion, therefore, is not an enigmatic or sporadic process but one determined by the steps an institution takes to lay the groundwork for it. These steps are integrated into the stages of growth of a micro-enterprise program: the start-up stage; the model stage; the consolidation-with-growth stage; and finally, the expansion stage.
- c. ***For expansion to occur in micro-enterprise programs, it must be planned from the beginning.*** An institution that seeks to take a micro-enterprise program to the expansion stage must define this vision at the earlier stages, when the program is small and experimental. Expansion implies fundamental changes at the institutional level that cannot be incorporated easily unless the planning starts when the program begins operating.
- d. ***The expansion of micro-enterprise programs brings with it a growth in the benefits derived, in particular in the areas of job maintenance and creation, and income enhancement.*** Most analyses of micro-enterprise programs demonstrate that access to financial resources and training

for the smallest-scale producers and retailers leads to an improvement in their lives, often measured in terms of jobs and income. As the programs grow, an increasing population derives these benefits. Additionally, a small percentage of these producers transforms their enterprises from micro to small.

## 2. On Models of Expansion

***While the stages of growth in micro-enterprise programs can be identified, a variety of strategies or models can carry programs through these stages.*** Two major models emerge from ACCION's experience:

- a. ***Decentralized, Single-Institution Model:*** Perhaps the best-known model for expansion is the creation of one non-profit institution that focuses on credit provision and training for micro-entrepreneurs. Through the use of group lending mechanisms—solidarity groups—and individual loans, the institution concentrates on gradually expanding its program activity through the creation of small subsidiary branches or regional offices that increase its coverage. In this process, the institution develops a highly decentralized, horizontal structure that reaches into several regions in the country and manages its operation through close interaction with the headquarters office.

Perhaps the best example of this structure at an advanced stage is the Grameen Bank in Bangladesh (GBB), briefly described in Chapter II. This model also predominates among the affiliated institutions in the ACCION network and has developed to different degrees in each case. ADEMI, in the Dominican Republic, is one of the oldest and best known examples of a successful use of this model (Gomez, 1989). Other programs, such as PRODEM in Bolivia, ASEPARE in Honduras, Acción Comunitaria del Peru (ACP), and Asesoría Dinámica a Micro-empresas (ADMIC) in Mexico are at various stages of decentralizing their institutional structures for program expansion. Additional programs, such as AVANCE in Costa Rica, the Paraguayan Foundation for Cooperation and Development, the Foundation for Ecuadorean Development, and the Eugenio Espejo Foundation, are at earlier stages in the process of

decentralization, and still concentrate their activities in one region or city.

- b. ***Multi-institutional, Decentralized Model:*** The second model involves the coordination of various non-profit institutions to extend credit and training to micro-entrepreneurs in various regions of the country (Guzman and Castello, 1988). As described in Chapter II, these institutions are independent and varied in their institutional formation and development approach. They all, however, agree to operate as a broad, decentralized unit, using the same methodology of group lending, and the same monitoring and information systems in their micro-enterprise programs. Each institution and its program grows through the various stages suggested in this document. At the same time, each institution participates in an established system of information exchange, staff development, program analysis and evaluation.

This model of expansion of micro-enterprise programs also requires a second-tier umbrella organization that serves as the coordinating and technical assistance instrument for all the participating institutions. This organization assumes responsibility for effective coordination among the implementing institutions and designs the systems for collecting information that enable every institution to operate as part of a larger unit.

Colombia offers the best example of this approach. Its second-tier organization, the Association of Solidarity Groups, gathers over one dozen local institutions as members. In the aggregate, these institutions have reached over 16,000 micro-entrepreneurs in the country. On a monthly basis, they extend over 650 loans totalling about US \$320,000. Their combined portfolio is nearly US \$1.6 million (ACCION, 1989a).

This model has accomplished expansion by incorporating additional institutions to its network—seven in the last three years— and by encouraging them to grow and expand individually. The approach requires careful attention to elements not present in the single-institution model, such as establishing consensus among a dozen boards and

**executive directors, and developing a process based on consensus to plan and develop the programs in a uniform manner. It also requires a commitment from each institution to be accountable to the network and to establish a collaborative effort in fundraising and other key areas of work.**

**The second-tier organization plays an important role in maintaining the unity of this highly decentralized system. It establishes the agenda for building consensus, and brings the institutions together on a regular basis. Additionally, the Association in Colombia recently has evolved to operate as a financial intermediary for its member organizations that will facilitate obtaining resources and allocating them in the most efficient manner.**

**The application of each model varies depending on contextual circumstances. The degree of regionalization in Colombia, as well as its highly developed system of non-profit institutions in social development, rendered the multi-institutional model the most responsive to the setting. In other countries, such as Guatemala, one observes a hybrid approach. It coordinates the micro-enterprise programs of a few institutions, which decentralize their operations in a manner akin to ADEMI, but coordinate their work according to the Colombia model. ACCION and its affiliates operate a model covering Latin America and the Caribbean that is similar to the Colombian one, in which ACCION carries out the role of a second-tier technical assistance and coordination institution.**

**These expansion models share basic characteristics that are worth summarizing:**

- o They rely on a high level of decentralization coordinated by a headquarters office or an umbrella organization.**
- o Uniform monitoring and evaluation procedures comprise the main elements of the information system that is established for expansion.**
- o Staff development is an integral part of the program's implementation.**

- The structure of each institution is designed to allow for program expansion through the addition of more offices in a single-institution model, or more institutions in the multi-institution one.
- A consultative decision-making approach relies on consensus-building among regional branches or institutions.
- Strong financial departments provide the information and analysis needed for program implementation.
- They demonstrate willingness to experiment, especially in securing funds for the programs and in utilizing financial tools for the effective use of resources.

### **3. On Non-profit Institutions and Their Development**

- a. ***Non-profit institutions have played an important role in advancing our understanding and experience of how to provide financial services effectively to a growing population of low-income producers in developing countries.*** The bulk of what we know about reaching the informal sector has been gleaned from the demonstration and model programs of non-profit institutions. Promising efforts have emerged that provide a basis for future work in this arena.
- b. ***The growth and experience of non-profit institutions during the last five years provide a strong justification for their moving into the expansion stage. This phase will enable them to reach several thousands or tens of thousands of micro-entrepreneurs.***
- c. ***There is an intrinsic relationship between institutional development factors and a program's capacity to reach the stage of expansion outlined in this discussion.*** An institution that aspires to implement a large, national-level micro-enterprise program must begin its strategy by assessing its internal adequacy. Institutional vision, structure, systems, human resources, and external interface constitute the priority areas that it must address.
- d. ***Non-profit institutions that are on the verge of launching into program expansion must consider institutional***

***modifications that may transform their institutions from non-profits into another structural formation.*** This concept of structural transformation for organizations that have defined themselves as non-profit entities constitutes an important point of reflection and sets the agenda for their work in the coming decade. With this challenge, non-profit institutions will again be charged with experimenting as they have in the past, and with providing innovative yet fundamental pieces of the puzzle of micro-enterprise development.

## **C. ISSUES TO ADDRESS IN THE EXPANSION OF MICRO-ENTERPRISE PROGRAMS**

### **1. Applicability of Expansion to Non-profit Institutions:**

Not all non-profit institutions are poised to expand micro-enterprise programs to the level outlined here. While program expansion as defined here constitutes one important challenge in this field, it also presents only one approach to assisting micro-entrepreneurs. Not every institution should attempt it. Many non-profit organizations will continue to implement relatively small programs utilizing a variety of methodologies and contributing to knowledge in other areas of micro-enterprise work. Further, while the concept of scaling up micro-enterprise programs addresses one of several key issues to consider in the coming decade, it does not suggest that scaling up will resolve the myriad of factors related to the economic activities of low-income populations.

However, non-profit institutions that concentrate on providing credit to the smallest-scale producers must analyze expansion as a persuasive approach to extending benefits to a significant population and to assuring that the program is sustainable over the long term. This document has suggested some of the major areas that an institution must consider if it is to graduate to the expansion stage.

### **2. Program Sustainability**

Sustainability in micro-enterprise credit programs remains an arduous task. Few programs have achieved it. Nevertheless, a growing number of non-profit organizations have given this

issue priority and have structured their programs to respond to it. In the ACCION network, micro-enterprise programs demonstrate a tendency towards increased self-sufficiency as the programs mature and grow (ACCION, 1989a). ADEMI, in the Dominican Republic, for example, has been self-sufficient for several years, reporting its income as 128 percent of total expenses for 1988. Others, such as PRODEM in Bolivia, the Paraguayan Foundation, AVANCE in Costa Rica, and several programs in Colombia, also are approaching 100 percent self-sufficiency due to increased efficiency and program growth.

Keeping the issue of self-sufficiency in the forefront of program objectives is a crucial ingredient of adequate program expansion.

### **3. Methodological Considerations**

Programs that have progressed along the growth stages defined here have done so through the use of a successful methodology for credit provision. Often based on the formation of small groups known as solidarity groups, these programs provide credit with rapid loan application and review procedures; variable loan terms suited to meet the borrower's needs; commercial or higher interest rates; built-in repayment incentives; and training and technical assistance.

When a program reaches the expansion stage, this methodology may undergo an adaptation that allows the programs to handle a much larger clientele. For example, the formation of groups may require an additional step that gathers a larger number of persons under one loan. In this way, the program can process one transaction and expand its outreach.

Methodological changes have implications for the participation of beneficiaries or clients in the program. Expansion may offer the borrower increased decision-making power over loan provision and credit management. It may also extend client activity into depositing savings or, as is the case in the Grameen Bank, into establishing and managing a parallel credit fund for emergency purposes. As the expansion stage approaches, micro-enterprise institutions are likely to experiment with their successful methodology and develop a new one for this stage.

#### **4. Contextual Considerations**

While there are many factors to consider in this area, they vary considerably from country to country. Policy issues, the political climate, the nature of the micro-enterprise sector, the characteristics of the banking sector, and the availability of resources are among the most obvious subjects that will partially regulate the institution's decision to expand. As the institution evolves through the stages of growth outlined here, it will address these topics and maintain an up-to-date analysis that will facilitate expansion.

Inflation will plague micro-enterprise programs in all countries. Recognizing the reduction of money's value during an inflationary period is the key to understanding how the assets of an institution can erode gradually. For example, a review of the institution's portfolio and its value in real terms is a basic yet often ignored manner of defining its evolution. Adjustments to maintain the real value of the portfolio will affect the institution's ability to cover its costs and to achieve self-sufficiency.

An institution must master certain tools of financial management when operating in an inflationary environment. The strategy and technology of financial management that aims to fight inflation applies to financial entities, regardless of their objectives. In micro-enterprise lending institutions, as in other organizations, program continuation depends on maintaining the institution's equity. Mechanisms including management of cash flow, the mix of assets and liabilities within the institution, and the inclusion of inflation in adjusted financial statements, will assist an institution to manage its finances in an inflationary setting.

Inflation influences non-profit institutions that operate on grants and subsidies through the increase in the overall level of prices, and their reduced ability to pay for goods and services, especially for the program's staff and other operating costs. Often, additional grants can assist in minimizing the impact of inflation. In micro-enterprise programs, however, inflation carries added implications. It erodes the institution's ability to cover its costs because it reduces the value of its assets, and forces it to pay future liabilities, such as loans, with cheaper money.

## **5. The Constraints of Program Expansion**

While expansion of micro-enterprise programs represents an exciting avenue for assisting the informal sector, several factors will affect the degree to which this approach evolves:

- The size of the informal sector in developing countries is growing at a fast pace; even with expansion, programs will reach a small percentage of this population. Even programs that include tens of thousands of clients in their portfolio will not be responding completely to the need for resources among the smallest-scale producers and retailers. In the long term, both expanding programs and increasing the number of programs that reach the expansion stage may address this constraint more adequately.
- Access to funds in substantial amounts is a prerequisite for expanding a portfolio, and this factor may remain a major constraint for programs. Some programs in the early stages have experienced a shortage of funds, while others have run the risk of being "overfunded" at the expansion stage. Resource availability must be established before launching the expansion stage. The major multilateral funders still focus on government-based programs and are only beginning to discover the role of non-governmental institutions as substantive contributors in this area. The availability of funding from donors and other sources may become a major determinant of expansion.
- The capacity both to train staff and to manage the institutional transformation suggested here with the available human resources may also constrict expansion. The skills needed to implement these programs are complex, and an institution may need to spend time preparing a cadre of mid-level managers before expanding its program.

## **D. CONCLUSION**

The expansion of micro-enterprise programs by non-profit institutions defines one agenda for micro-enterprise assistance that is still very experimental and yet promises to break new ground in reaching the informal sector in Latin America. Many questions remain unanswered, and require attention before

programs attempt to initiate these efforts. The implementing organizations will address many of these issues as they progress along the growth spectrum suggested in this document.

There are, however, additional issues that must be studied which are beyond the framework of this document or of the implementing institutions. Many of these require research, some of which is already in process, advancing in a parallel line with program implementation. Among the most important issues are: how micro-enterprises develop and grow; the significance of this productive sector within the economy; the governmental response to this increase of activity by autonomous non-profit institutions; the evolution of policy formulation towards informal sector activity. Hence, non-profit institutions must not only look internally to prepare for expansion, but must also draw from the wealth of information that is emerging from research and from developments at the policy level. At that juncture, they will become pivotal players in responding to the needs of the poor in their own countries.



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