The SEEP NETWORK

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# Conflict and Post-Conflict Environments: Ten Short Lessons To Make Microfinance Work

## Abstract

*Today, practitioners are working in places where conflict is resurgent and political stability is tenuous at best. This Progress Note explores the key ingredients to the success of microfinance programs in conflict and post-conflict environments.*

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## Introduction

Expert opinion once stated that microfinance is appropriate only in politically and economically stable environments. Events in the world since the early 1990s have brought about stunning and sudden changes in the political and economic systems of entire regions. In some regions, conflict appears to be endemic, with periods of stability punctuated by violence. In others, stability is altogether elusive. For more than a decade, practitioners have started or maintained microfinance operations during or after a conflict. It seems the world has entered a new era of prolonged conflict during which the microfinance community is being called on more frequently to provide economic development opportunities.[1] In this heightened environment of conflict, microfinance practitioners have responded by starting and sustaining programs that provide key livelihood support services during conflict and assisting in post-conflict reconstruction.

The question is, "How do we make microfinance work not only after the conflict, but also in the absence of peace and stability?" This Progress Note explores the key ingredients to the success of microfinance in conflict and post-conflict environments today. Microfinance is only one of many tools that can be used in conflict and post-conflict situations and should not be considered the sole solution to promoting economic development. In 2001, the U.S. Agency for International Development's Microenterprise Best Practices project published a series of technical briefs on post-conflict microfinance. The series emphasized that microfinance can be successfully implemented in post-conflict environments if three essential conditions are met: (1) sufficient economic activity that can use credit services, (2) a relatively stable client population, and (3) a certain degree of political stability. Currently, political stability is proving to be less essential than originally thought. Today, practitioners see microfinance implemented successfully in places where conflict is resurgent and political stability is tenuous at best.

The SEEP Network's Financial Services Working Group (FSWG) examined its members' experiences in Bosnia and Herzegovina, Cambodia, Iraq, the Palestinian

**Lessons Learned from Conflict and Post-Conflict Environments**

1. Focus on the Clients' Security
2. Work with Trusted Institutions
3. Provide a Range of Services
4. Adjust Product Design and Delivery
5. Separate Microfinance from Relief Operations
6. Share, Cooperate, and Collaborate with Stakeholders
7. Think Long Term
8. Develop Human Resources and Ensure Staff Safety
9. Ensure Access to Information and Systems
10. Maintain Portfolio Quality

West Bank and Gaza, Sierra Leone, and South Sudan. The FSWG also reviewed recent publications on the topic to compile the following lessons for making microfinance work in these difficult environments.

## 1. Focus on the Clients' Security

Practitioners should begin by looking at the clients' or communities' strengths and assets. Some core principles of microfinance hold true in any environment. For instance, credit is not an appropriate intervention for individuals who are not economically active and have no means to repay it. Although well-timed and properly structured loans can assist clients in rebuilding their lives, borrowing can frequently make clients feel less secure if they doubt they have the ability to repay. *Any service that enhances security is a good place to start with clients*. Providing such a service may require looking beyond microcredit.

> In Cambodia, CARE has learned that providing a secure place to deposit money is a necessary component to building trust among the rural poor.

As a complement or alternative to credit, safe and secure savings programs are powerful tools to use when assisting communities in building and protecting their assets. Aside from providing a safety net for clients, safe savings programs can rebuild trust in the community and institutions. Savings can also be a source of individual or communal pride, a strong sign that the community can rebuild its life itself. For communities that rely on trade, practitioners may consider payment and transfer services that enable clients to pay suppliers and transfer funds without having to carry cash.

## 2. Work with Trusted Institutions

> CHF International learned that religious leaders offered the greatest support and assistance in entering and staying in a community in Iraq.

*Practitioners should work within the surviving or emerging structures that have the trust of the population.* This effort may require some unusual and challenging approaches in societies where most institutions are tainted by the conflict. In Cambodia, CARE recognized the importance of savings, but "cooperatives" and "credit unions" are associated with the terror and forced collectivism of the Khmer Rouge. In developing its savings mobilization project, CARE worked with the respected village heads to create local "savings banks" rather than follow a traditional cooperative model. CARE obtained the initial and ongoing support of the trusted village leaders to implement the program.

In Iraq, CHF International had to quickly distinguish itself from the Coalition Forces. It did so through building trust by meeting with leaders from all sectors (business, government, legal, banks, and religious) to both promote its product and distinguish its staff from the military. It has noted that *as the society begins to settle down, the influence of different community leaders and institutions can change*—the program cannot necessarily rest on the early relationships it established. Practitioners also warn that local institutions are even less able to implement microfinance after a conflict than in a normal situation because they are so focused on relief activities, have very low capacity, and may be torn by ethnic tensions. As a result, the choice of partner becomes even more important and challenging in a conflict or post-conflict environment, and it may require creating a local organization rather than selecting one.

## 3. Provide a Range of Services

Development activities alongside relief efforts have a role in conflict and post-conflict environments because a section of population can take advantage of them. *Microfinance and other microenterprise development activities can and should be approached from a development perspective at the outset, rather than as a relief activity*. Sharing information and coordinating activities with relief and economic development projects can assist in articulating the strategy and tactics for moving families from receiving relief to cash grants to financial services.

> Through a certificate system and linkages with its programs in refugee camps in Sierra Leone, the American Refugee Committee was able to provide refugee entrepreneurs with preferential access to credit on their return.

These services can be coordinated by different organizations or one organization, provided a clear distinction exists between relief services and financial services (see "Separate Microfinance from Relief Operations" below). As an example, American Refugee Committee (ARC) takes a holistic approach, linking their refugee operations to their microfinance services by certifying entrepreneurs in refugee camps. Certified entrepreneurs receive preferential access to ARC's microfinance operations in their home country. This system encourages refugees to repatriate and provides ARC with a base of good microfinance clients. ARC has limited its microfinance services to accessible areas, while focusing on small grants and training in areas that are difficult to reach.

## 4. Adjust Product Design and Delivery

Conflict and post-conflict environments may require creative adaptations to product design and delivery mechanisms: the level of trust is low, people are displaced, physical and financial infrastructure is limited, travel is dangerous, closures thwart timetables, and destruction of property used for collateral is commonplace. *Product design and delivery must allow for general instability and potential economic interruptions.*

In the case of Iraq, CHF reported that individual loans allowed for faster loan delivery and more immediate impact. Individual loans also enabled credit staff to structure loans according to the client's situation. Since the *intifadah*, microfinance institutions (MFIs) in the West Bank and Gaza have had to be much more involved in the business analysis of group members to understand the vulnerability of members' situations—a task that the group was frequently not able (or willing) to do. They also decided to make smaller loans after analyzing businesses and sectors, rather than adhere to the programmed steps in the methodology. In both countries, MFIs benefit from an educated staff and client base.

> The Sudanese Microfinance Institution in Sudan learned that most traders needed to take their loan money to neighboring Uganda or Congo to purchase supplies, return to Sudan, and then sell enough products to afford the first loan payment. In response, SUMI now offers a grace period on its loans, with the first payment due two weeks after disbursement. This adjustment has caused no negative effect on repayment.

*In situations in which the clients have a fairly low education, it may be necessary to make products and services as simple and standardized as possible once the design of the product and delivery mechanisms is complete.* In Cambodia, Catholic Relief Services (CRS) affiliate TPC has successfully used a village banking methodology modified to suit rural and agricultural-based businesses.

Given the lack of collateral and mobility of clients, *lending in conflict and post-conflict situations requires strong and effective guarantees*. The character of clients, witnessed through personal guarantees and references, is even more important when fighting or violence starts and clients are not easily located. MFIs need to carefully screen clients and then stay in contact with them, the cosigners, the family, and community leaders during times of crisis. It is also important to be prepared for delays in collection and articulate alternative arrangements should clients not be able to meet or come to the office to repay.

## 5. Separate Microfinance from Relief Operations

Relief, development, and peacemaking activities can operate concurrently, but it is important not to confuse them—*separating microfinance from relief operations is necessary for success.* Multisector organizations may face a period of overlap or "cohabitation" between microfinance and emergency operations. It is important to create a programmatic wall between microfinance and relief operations to ensure that microfinance has appropriate measurements and incentives for performance, which usually requires a separate manager or management team. To be blunt—repayment rates are unimportant to a manager who is concerned with mortality rates.

> In EKI Bosnia, internal confusion was communicated externally so clients were unclear when World Vision was operating as a relief activity and when it was operating as a microfinance activity. World Vision established EKI as an independent MFI, creating a separate identity, and EKI is one of the leading MFIs in the country.

It is preferable to create or use a separate legal institution with its own office. Practitioners note, however, that this may not be possible in a chaotic environment. Indeed, opening an office outside of an organization's secure area may pose security risks. In any case, microfinance operations can create a distinct image; when clients are presented with a new face, they likely will not confuse relief and business. They can develop and market microfinance services under a different name and logo. World Relief Mozambique managed this identity problem by using CARE Mozambique to manage its relief distribution in areas where World Relief had microcredit operations. In Sudan, Chemonics International created and registered the Sudanese Microfinance Institution (SUMI) as a Sudanese company with a Sudanese board of directors and a separate office from Chemonics' broader program. The image of the institution is completely Sudanese, which has made it easier to differentiate it from international relief efforts.

## 6. Share, Cooperate, and Collaborate with Stakeholders

Although often unthinkable in stable competitive environments, sharing detailed information with other practitioners on issues such as security, product terms and conditions, and client information is mutually beneficial in an unstable environment. Holding regular meetings or even developing a local microfinance network or working group of practitioners assists in articulating promising practices in the local environment and promotes lateral learning.

> The United Nations Capital Development Fund, the American Relief Committee, World Relief, and World Hope have developed principles for microfinance and grant use in Liberia that are influencing donors' and practitioners' agendas.

A local network or group can also educate donors and local leaders on microfinance practices. Many donors working in emergency relief have little or no experience in microfinance—their main objective is to alleviate suffering, create stability, and get money into the hands of the community. Local politicians share this goal. Practitioners and donors need to establish guidelines for economic development activities and gain the support of local leaders. *A donor/practitioner consortium that offers a consistent message and consistent approach to microfinance has more credibility with national and local leaders.*

## 7. Think Long Term

Building a sustainable MFI takes several years, even in the best of conditions. The high costs of operating in a dangerous environment lengthen the time it takes to become profitable. Donor assistance in conflict and post-conflict environments often operates with much larger sums of money and on a much shorter time frame than development assistance. In the worst-case scenario, donor funding cycles can pressure practitioners to adopt unsustainable lending practices to "get the loans out the door." *Practitioners should work together with donors to design funding mechanisms that permit continued institutional development of the microfinance program after the emergency funding has expired.* Ideally, donors should allow for longer-term funding cycles (three or more years) to allow for more consistent planning and time to achieve sustainability. Alternatively, practitioners and donors need to develop strategies for making short-term funds last as long as possible. One organization agreed with its donor that it would fund every disbursed loan with fresh grant funds, both new loans and repeat loans. As clients repaid the principle, the MFI was allowed to place it in a bank account for covering operating expenses in future years. This method enabled the MFI to quickly draw down grant funds and build up cash reserves for future deficits.

## 8. Develop Human Resources and Ensure Staff Safety

Finding experienced technical staff can be more difficult in conflict and post-conflict environments: many people may have been killed or may have fled, education has been interrupted, and more highly educated people have frequently left the country. To complicate matters, the most qualified staff is quickly employed by donors and relief agencies at salary levels higher than an MFI can pay.

> When the Foundation for International Community Assistance (FINCA) started operations in Kosovo, it brought in highly trained staff from FINCA Kyrgyzstan to form borrowing groups and train local credit officers at the same time, thus satisfying the donor's desire to disburse quickly.

Hiring a strong director from the beginning is extremely important in difficult and chaotic times. *Hiring the right directors is expensive—and keeping them is too.* In an emergency setting, expatriate directors frequently have more success with donors and a greater ability to interact with the relief community. At the same time, expatriate managers may not be able to go into certain areas due to the security situation, or they may not be able to deal effectively with certain members of the community. In addition, expatriate contracts usually last only one to three years. If funds are flowing in the early years, microfinance programs can benefit from bringing in one or more teams of expatriates to train local staff and identify and groom a replacement senior management team. This process includes developing a clear succession plan with specific targets and dates to make the transition from an expatriate director to a national director.

Multisector organizations that start microfinance operations frequently draw on their relief staff. Although a trained relief staff is an attractive human resource pool, *organizations should not use the microfinance program to provide guaranteed employment of relief workers.* The skill sets of relief staff do not necessarily translate well to microfinance, and clients may be confused if the same staff that once provided relief are now providing financial services. Instead, the organization should try to hire or develop experienced technical staff with the appropriate skills. MFIs frequently train young people straight from commercial school, technical training colleges, and universities.

Keeping staff safe is as important as training them and can be as difficult. With battles raging and unsafe roads, *MFIs have to do what is necessary and pay what is required to keep staff secure*. This effort may involve adaptations in product delivery. Although most of the banks in Iraq were sorely lacking in basic banking infrastructure, they provided CHF a safe place to store money and a functioning credit window. CHF was also able to disburse funds using the banks' checks, reducing the risk to staff of lootings and muggings.

## 9. Ensure Access to Information and Systems

Unforeseen events may prevent staff and clients from reaching the office. It is important that MFIs safeguard their records and make them available from remote locations. *Fortunately, technology is making access and backup efforts easier and more reliable*. CHF Iraq requires that its staff keep key documents and information safe and accessible by scanning documents and storing them outside the office. A CRS affiliate, ASALA, overcomes closures in the West Bank by maintaining their management information system (MIS) on line at all times so loan officers and administrative staff can work from home. FTP sites can be used for online access to all office files. *Most importantly, management needs to develop a communications strategy in emergencies so it can locate all staff and inform them of emergency procedures.*

## 10. Maintain Portfolio Quality

The final, and perhaps most important, lesson learned is that portfolio quality can and must be maintained. Many MFIs achieve this goal by responding faster, beefing up collection departments, and having managers get more involved in collection efforts. Other tactics include instituting new procedures, such as involving courts, officials, or local leaders. Internally, maintaining portfolio quality requires a strong MIS that provides timely and accurate information, enables credit officers and management to monitor repayment daily, and allows managers to hold credit officers responsible for their portfolio quality. Operating in the dark without financial reports increases the potential for poor performance.

When a client's productive assets are destroyed, managers must decide what to do on a case-by-case basis. Some institutions have made good use of selectively rescheduling loans and even refinancing loans to enable proven businesses to recover. Others insist that making such exceptions can undermine the lending program. Practitioners agree, however, that if loan terms and conditions are appropriate for the current conditions, the need to reschedule is less likely. *The key is to keep focused on maintaining the incentive to repay—the promise of receiving another loan.*

> Several of CHF's Iraqi clients died or had their shops destroyed. CHF held its clients and guarantors to their obligations. In some cases, CHF permitted slightly longer repayment periods to account for the unstable environment.

As a Save the Children affiliate in the West Bank noted, "[FATEN] made a major mistake in the beginning [of the *intifadah*]. We read the writings of some experts who said that microfinance shouldn't be done in times of conflict, so we totally stopped disbursing for a while. This hurt us and our clients. It was a major error. It damaged the primary incentive that clients have for repaying—the opportunity to get additional financing. Without that, repayment plummeted. After a while, we realized that this was a mistake, resumed lending, and repayment recovered."

## Conclusion

Microfinance products can be delivered effectively in conflict and post-conflict contexts. Meeting this challenge requires an agreement among donors and practitioners about "best practices," as well as an understanding that the conditions in which clients are living may require a departure from traditional approaches. An overarching lesson from SEEP practitioners is that a solution applied in one environment may not work in another, which brings the focus back to management and staff. Management and staff must be capable of adapting and improvising, and at the same time remain extremely focused on portfolio quality and long-term sustainability. The true challenge lies in finding appropriate staff that can manage both the technical work and the difficult circumstances.

## Notes

[1] Business development services (BDS) are not included in this note, although the authors strongly believe that these services can play a vital role in economic development in the conflict and post-conflict environment.

[2] The contributing authors to this note share the belief that microfinance refers only to attempts to provide financial services on a financially and institutionally sustainable basis and specifically excludes economic assistance programs disguised as microcredit or highly concessional loan schemes.

[3] From *Microfinance Following Conflict*, Brief No. 4.

## Resources


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