

# **THE ROLE OF MICROFINANCE FOR THE POOR IN REPUBLIC OF KOSOVO**

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## ***Abstract***

*Microfinance is the provision of financial services to low-income, poor and very poor, self- employed people. It has been stated that since 1976 when Professor Mohammed Yunus and Grameen Bank in Bangladesh establishes the first microcredit program, dedicated poor people, especially for women's, represent the origin of microfinance.*

*By the early twenty –first century, tens of millions of people in more than 100 countries were accessing financial services from microfinance institutions (MFIs). The risk, which commercial banks see by providing the financial services to poor people, is not a problem for Microfinance Institutions (MFI's). The aim of this paper is to analyze how the MFIs in Kosovo has been approached to the poor people and, which is resulting in their life.*

*MFI's in Kosovo begins, with operation of international non –government organizations (NGOs) and donors' activities, with aim to develop economic programs after the armed conflict in 1999 ended. Since 2000 in Kosovo a number of MFI's has been emerged. There are 14 MFIs that operate in Kosovo, by operating mainly in rural zones, which presents 18% of the financial sector in terms of loan base and 7% of the total loan amount.*

*Despite the progress of MFI's that is presented, additional support is necessary, in particular on relation with the investors and donors who provide the funds for small loans, in regard of approaching more poor people in Kosovo. In the continuity I consider that giving some modest recommendations, it will contribute to the future studies.*

***Keywords:*** *Microfinance, MFIs, Poor people, Kosovo*

## **1. General Overview on Microfinance**

Lack of access to credit is generally seen as one of the main reasons why many people in developing economies remain poor (Hermes and Lensink, 2007). There are microfinance institutions which have demonstrated that it is possible to serve the poor client, operate in a financially sound manner and reach scale, Barr (2005). Since the first microfinance program has been established in Bangladesh in 1976, by Prof. Muhammad Yunus, the importance of microfinance has been increased all around the world. Nowadays, establishment of microfinance has occurred in many countries, despite on the level of the development.

Several studies explain the importance and the crucial role that microfinance has on social and economic development. Since its foundation, the microfinance was about lending to the rural poor for income-generating purpose- mainly through solidarity group loans of small and smallest amounts. Following, microfinance has evolved into a more comprehensive development tool, with the aim to supply access to financial services for all unbanked people in emerging and developing markets,

Lützenkirche (2012). In addition, financial services are not limited; in general include savings and credit. However some microfinance organizations also provide insurance and payment services, Lendgerwood (2000).

According to, Vetrivel&Kumar Mangalam (2010) limited access to credit for the poor, is directly connected to practical difficulties arising from the discrepancy between the way of operation followed by financial institutions and the economic characteristics and financial needs on low income households. For example, when the commercial lending institution, requires to borrowers to have a stable source of income of which principal and interest can be paid back and also require for collateral with clear title, and not every household can meet these criteria. Hence, bankers see the risk to cooperate with low income household. At this line, the development of the microfinance sector is based on the assumption that the poor possess the capacity to implement income-generating activities but limited by lack of access to an inadequate provision of savings, credit and insurance facilities (Hulme & Arun 2009).

Therefore, the efforts to explore, such "specific problems that poor people have in gaining access to financial services at an affordable cost, particularly as a result of their lack of collateral" and the, "impact pathways of microfinance on enterprises, households and individuals"(Duvendack et al,2011) has prompted interest in microfinance, to create a broad theoretical literature.

Otera(1999), defines microfinance "as the provision of financial services to low-income, poor and very poor, self-employed people", which is, evolved as an economic development approach intended to benefit low-income woman and men (Lendgerwood, 2000). Therefore, microfinance services can help low-income people reduce risk, improve management, raise productivity, obtain higher returns on investments, increase their incomes, and improve the quality of their lives and those dependents, Robinson (2000). According to UNDP report (2008), microfinance caters particularly to low-income or vulnerable clients who have no access to mainstream financial institutions.

### **1.1. Beginning of microfinance**

There are many considerations, that microfinance is no longer being treated as a new development, by arguing for its long existing history and practice. For example, Siebel (2003) stated that in microfinance in Europe, dates back to enormous increases in poverty, since the 16<sup>th</sup> century by taking into consideration, development of microfinance in Ireland<sup>1</sup> and Germany<sup>2</sup>, two states with different

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<sup>1</sup> The case of Ireland , 1720- 1950 : how self – help and legal backing created a mass microfinance movement , until a cap on interest rates brought it down ( Siebel, 2003)

<sup>2</sup> The case of Germany ,1778 – now - How self –help , regulation and supervision created the world's largest microfinance system ( Siebel ,2003)

stories. Microfinance starts as informal institutions, followed with expansion as formal institutions.

However, the roots of microfinance can be found in many places, but the best known story is that of Muhammad Yunus (pioneer of microfinance) and establishment of Bangladesh's Grameen Bank (Armendáriz & Morduch, 2005). Microfinance in the beginning was called microcredit and lending was the focus. A group lending, a mechanism that essentially allows the poor borrowers to act as guarantors for each other, was the innovation that allowed Grameen to grow explosively, Armendáriz & Morduch (2005).

Constantly, development of the Yunus Microfinance, estimated to be an instrument for poverty alleviation, which arouses debates in international dimensions. To support this view the United Nations (UN) declared in 2005 to be the International Year of Microcredit.

The Nobel Peace Prize 2006 was awarded jointly to Muhammad Yunus and Grameen Bank, "for their efforts to create economic and social development from below"<sup>3</sup>. In this regard it is worth to state, what Molenarr (2008) highlighted, for great importance that microfinance give all around the world, as per the success showed by placement of development goals and the International Year of Microfinance and award with the Nobel Prize to Muhammad Yunus Molenarr.

In this line expansion of microfinance across the globe went hand in hand with expansion into urban areas in higher- as well as low- income countries, although, in quite a few countries microfinance focused on urban areas right from the start, Lützenkirche (2012).

## **1.2. Microfinance approaches to the Poor**

Poverty still remains one of the most important economic and social problems, hence being one of the most intense and researched topics to date. As Otero (1999) emphasizes, microfinance enables poor, self-employed people to create productive capital, to protect the capital they have, to deal with risk, and to avoid the destruction of capital. It attempts to build assets and create wealth among people who lack them. For the very poor, microfinance becomes a liquidity tool that helps smooth their consumption patterns and to reduce their level of vulnerability. "Nearly 3 billion poor people in developing countries lack access to the basic financial services needed to help them manage their precarious lives" (CGAP, 2009)

As Barr (2005) underlines, that over the last thirty years, microfinance institutions have developed a strong track record in alleviating poverty and advancing the economic needs of low- income households. In addition, microfinance institutions play a complementary role in the banking system by extending credit to borrowers

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<sup>3</sup> See: [http://www.nobelprize.org/nobel\\_prizes/peace/laureates/2006/](http://www.nobelprize.org/nobel_prizes/peace/laureates/2006/)

whom banks view as too costly or too risky to reach (Barr, 2005). This provision of the credit to the poor has proved to be a powerful tool in development (Roy, 2003). Also, financial services could enable the poor to leverage their initiative, accelerating the process of building incomes, assets and economic security, (Vetrivel&Kumar Mangalam, 2010)

### 1.3 Expansion of Microfinance Institutions

It is valuable to make financial market work for the poor, because this helps to understand what is taking place in the core of the financial market system – what services are provided by whom, to whom, and how – and what is the impact, because this financial inclusion refers to people and business having access to appropriate and affordable financial services, Lendgerwood (2013).

The progress on increasing the microfinance institutions by reaching at 3.133 in 2005, from the 618 that was in 1997, is the evidence for the microfinance role. Norwegian Nobel Committee 2006 stated that microfinance can help people to break out of poverty, which in turn is seen as an important prerequisite to establish long lasting peace, Hermes and Lensink, (2007).

According to, State of the Microfinance Summit Campaign report 2007, all around the world are 3,316 microcredit institutions, reaching 133,030,913 clients. 92,922,574 of who were among the poorest when they took their first loan. Of these poorest clients, 85.2 percent, or 79,130,581, are women. In this report are included Institutional Action Plans (IAPs) were submitted by 873 microfinance institutions (MFIs) in 2007. Together, these 873 institutions account for 92.4 percent of the poorest clients reported. Assuming five persons per family, the 92.9 million poorest clients reached by the end of 2006 affected some 464,612,870 family members<sup>4</sup>.

Table 1: Figures as of December 31, 2006

Data Point	Finding
Number of MFIs Reporting (1997–2006)	3,316
Number of MFIs Reporting in 2007 Only	873
Percent Poorest Clients Represented by 873 MFIs Reporting in 2007	92.4%
Total Number of Clients (as of 12/31/06)	133,030,913
Total Number of Poorest Clients (as of 12/31/06)	92,922,574
Total Number of Poorest Women (as of 12/31/06)	79,130,581
Number of Poorest Family Members Affected (as of 12/31/06)	464,612,870

Source from: (table 1: Figures as of December 31.2006) State of the Microcredit summit campaign report 2007)

Several, “models “for microfinance, many countries have substantial microfinance sectors and the main activity is on providing microfinance services rather than the

<sup>4</sup> See more : State of the Microcredit Summit Campaign Report 2007.

grander goal of social transformation. Microfinance initiatives have emerged as an alternative to the well documented failures of government rural credit schemes to reach small farmers, and the formal banking sector to provide services to low-income households (Hulme & Arun, 2008).

Microfinance is an instrument that, under the right conditions, fits the needs of a broad range of the population—including the poorest—those in the bottom half of people living below the poverty line. While there will be people in this group who will not be suited for microfinance because of mental illness, etc., the exclusion of this small percentage of the population will likely not be a limiting operational issue for MFIs (Morduch,2002). However, as mentioned, the microfinance model is far from perfect, but with continued support from international organizations microfinance sector will be an increasingly powerful force in bringing about sustainability and balanced increases in the quality of life of the poor in developing countries, (Roy 2003).

## **2. KOSOVO MIKROFINANCE**

In view of , NGOs and other Relief organization that continually, examines various instruments that are appropriate and relevant in making the transition from emergency relief to sustainable development in Post – Conflict situation, (Das,2003), it is not surprising, if microfinance sector in Kosovo is in need to be improved.

In addition, the approach of the MFI to new environments requires understanding with financial system of a country. This enables microfinance providers to be better informed about the needs and current positioning of services and products, and identification of the institutional gaps and the potential for partnership between different types of institutions, to reach the poor cost efficiency, Ledgerwood (2000). The fact is that, Post- conflict countries are in stage of changing environment, and it is important for microfinance institutions (MFIs) to adapt to the transition and evolving political, social and economic changes that occur (Das,2003).

For any post – conflict country the rehabilitation of overall infrastructure is a priority, thus, immediately after the war ended in 1999 in Kosovo, support and the need for capital projects for reconstruction, for economic, social, and political development, was unavoidable. In following, microfinance Institutions (MFIs) started to operate as non-governmental organization (NGO), supported by international donors, thus becoming an important factor for economic growth.

Currently in Kosovo the banking sector is dominated by foreign banks, which account for about 90% of all banking assets. The microfinance sector in Kosovo has been operating since 1999. There are 14 MFIs, operating mainly in rural areas,

which are approved by Regulation UNMIK Regulation 2008/28 and by the Central Bank of Kosovo (CBK)<sup>5</sup>

During the year of 2000, the Association of Microfinance Institution of Kosovo (AMIK) has been established, with the aim to engage together the group of MFIs in order to support the needs of Kosovo's small and micro business sector (SMS) and to push facilities growth in the microfinance industry. Current member of AMIK are: Agency for Finance in Kosovo (started as a Project of Mercy Corps), FINCA-Kosovo, KEP Trust, Kosovo Grameen Mission Arcobaleno Micro Credit Fund, KosInvest (a Project of World Vision), MESHTEKNA, PERSPEKTIVA 4, QELIM Kosova, START (developed by Islamic Relief).<sup>6</sup>

MFIs operating mainly in rural zones, which presents 18% of the financial sector in terms of loan base and 7% of the total loan amount (AMIK, 2010). Trends for Kosovo MFIs show that strong growth in outreach continued in 2008 and into 2009.

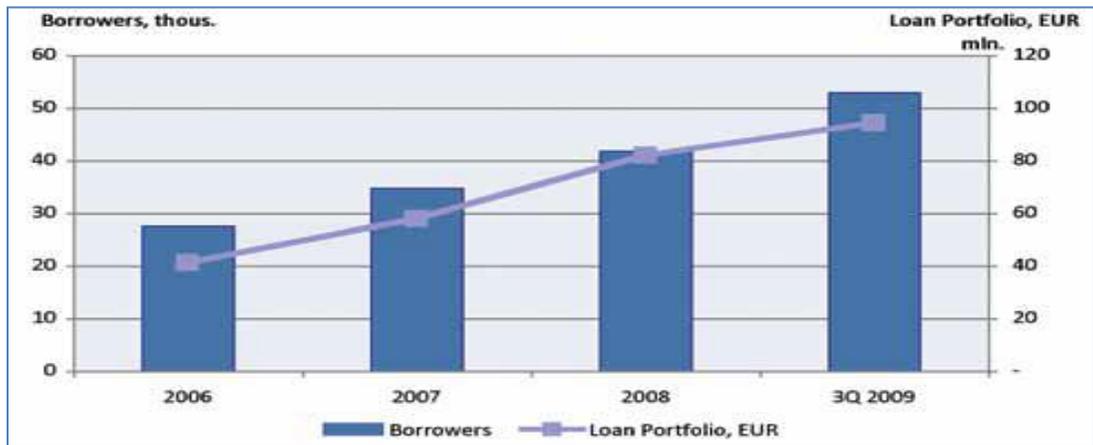


Figura 1

The number of financial institutions does not show any substantial changes during 2009-2012 periods, even this sector continues to be dominated by foreign owned companies, whose assets constitute of 91.6 percent of total sector assets ( CBRK, 2013).

Table 2 Number of Financial Institution

Description	June 2009	June 2010	June 2011	June 2012
Commercial banks	8	8	8	8
Insurance companies	11	11	11	13
Pension funds	2	2	2	2
Financial auxiliaries	28	29	32	36
Microfinance institutions	19	17	17	19

Source: CBK (2012)

## **2.1. Microfinance approaches to the poor in Kosovo**

Kosovo has the highest number of poor people in the Balkan<sup>7</sup>, with 34,5% of its population living below the poverty line, as example, on less than 1.55 Euros per day, with about 12% living in extreme poverty, or on less than 1 Euro per day. Remittances<sup>8</sup> from the Diaspora play a crucial role in providing an informal social safety net for poorer households, making up for the absence of essential social services<sup>9</sup>(Country Strategy 2013- 2016).

Microfinance has been considered as an instrument for fighting poverty and instrument for post-conflict rebuilding. “ Microfinance can fund self – employment and ease the financial constraints on poorer households, but its limited potential to generate jobs means it cannot be the anchor for economic recovery overall “<sup>10</sup>

According to (UNDP Report,2008)<sup>11</sup> development of microfinance in very short time with support of internationally assisted program to support following the devastating 1992-1995 conflict in Bosnia e Herzegovina, is the best evidence for a role that microfinance play in post – conflict countries. As it mention, by Ana et.el,(2010), microfinance often hailed both as a tool for fighting poverty and as a tool for post-conflict reconciliation. In Bosnia and Herzegovina, microfinance appear to be a better tool for aiding its participants quest of wealth and escape from poverty on an individual basis, than for addressing wider problems of social integration of institution building, (Ana at el, 2010).

UNDP report<sup>12</sup>, state that microfinance cannot be seen as a panacea for financing post- conflict economic recovery, but can make a critical contribution to the process of sociopolitical reconciliation. However, Barr(2005) highlights on how microfinance as a form of financial development, at least in its initial stages, can thrive without relying heavily on government regulation or support, or strong legal institutions that permit the poor to borrow against their assets or creditors to collect.

In Kosovo after the war in 1999, the financial donors and microloans, has been seen as the main support for the agriculture sector in Kosovo. Agriculture is estimated to be with crucial role for economic development, by following the economic development is a key for poverty alleviation.

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<sup>7</sup> see ;amik.org

<sup>8</sup> Remittances are an important source of support to households, particularly for financing education and health ; <http://www.undp.org/content/undp/en/home/librarypage/crisis-prevention-and-recovery/crisis-prevent-recovery-report-2008-post-conflict-economic-recovery>

<sup>9</sup>Contry Strategy 2013-2016, file:///C:/Users/City%20Computer/Downloads/Country-Strategy-Kosovo+2013-16%20(2).pdf

<sup>10</sup> Ibid pg 84

<sup>11</sup><http://www.undp.org/content/undp/en/home/librarypage/crisis-prevention-and-recovery/crisis-prevent-recovery-report-2008-post-conflict-economic-recovery>

<sup>12</sup><http://www.undp.org/content/undp/en/home/librarypage/crisis-prevention-and-recovery/crisis-prevent-recovery-report-2008-post-conflict-economic-recovery>

The interest rates of MFIs in Kosovo may not be suitable for all clients. MFI institutions provide more space for agriculture crediting in Kosovo rather than the commercial banks, which offer few possibilities for smaller farmers to access in their products. The clients of three MFIs<sup>13</sup> researched, (Konxheli& Bekaj, 2012), shows that 26% of them are clients of agriculture products. Almost all MFIs in Kosovo are credit oriented. While the credits play a very important role in creating, increasing and developing business activities , in which case farmer are willing to increase their capital up to 50 percent the favorable ambient is created in Kosovo, (Shkodra et.al 2012) .

There are thoughts that microfinance does not necessarily affecting the alleviation of poverty. According to Mersland&Strom (2009), there are claims that microfinance with its maturity, is abandoning its mission to serve the poor, while the mission of all microfinance institutions (MFI) is to provide banking services to the poor, that is, to provide small sums to very poor borrowers. Furthermore, critical appraisal of Chowdhry (2009) emphases that, while microfinance has developed some innovative management and business strategies, its impact on poverty reduction remains in doubt.

### **3. Conclusion**

Microfinance services need to be reachable for poor people, self- employed people, farmers, and other interested for the services and products that are provided by MFIs, in the country that is developed.

In a view of some critics, microfinance with its maturity is abandoning its mission to serve the poor, and microfinance cannot be seen as a panacea for financing post conflict economic recovery. However, we see capacity that microfinance has to prove, to be with value (income generation) and source of happiness increase (poverty reduction) for poor people.

By promoting in a wider range, the microfinance services will be more know from the poor people, mostly living in rural zone, because it presumed that this people do have limited access in financial services, even they do not see any possibility to generate income and to be self- employment (as is the case with farmers, with low standards of the life)

From criticism that the high interest rates are not favorable for the MFI clients, and a slight drop in a number of loans that observed in recent years, the result of the development of MFIs is not missing, it still continues to improve continuously. However MFIs in Kosovo still need for more support from state government, donors and foreign investor also.

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<sup>13</sup> Beswlihdja/Zavet Micro- Finance (BZMF), The foundation of Internatinal Community Assistance , Agency for Financing in Kosovo (AFK) ; see ( Konxheli and Bekaj 2012.)

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