Final Paper

Independent Study

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Tittle:

Analysis of the Bright Kids Uganda (BKU) Microfinance Business Model in Generating Income for Poor Families in Uganda: A Benchmarking Model Study

I. Theoretical Background

Poverty is a worldwide socio-economic problem. Hence, its awareness is much more favored at the international level of finance and governance. For example, the World Bank, United Nations (UN) and International Monetary Fund (IMF) have developed various programs and projects that would improve the life of the poor, ensure health improvement and sustainable growth and development. (Ssewamala, Sperber, Zimmerman, & Karimli, 2010)

Microfinance program has been generally regarded as a development strategy that can enhance the economic performance of the poor. In the past two decades, microfinance programs have been considered by the development economists as one of the foremost strategies for poverty reduction. Although some researchers argue that Microfinance has not really succeeded in its role as grassroots economic developer in the sense that it has not been effective in reaching the poorest (Hulme & Mosley, 1977). Therefore, it is important to make an analysis to reveal that microfinance loan made significant impact on the loan beneficiaries in the study area which lead to poverty reduction. It is also important whether the microfinance institution already performed in effective and efficient operations.

Effective and efficiency refers to how well the institution allocate the input resources such as asset, subsidies and personnel to produce output measured in terms of the loan portfolio and poverty outreach. In other words, it refers to how well these institutions utilize their inputs to produce optimal outputs. According to Rosenberg (1994), Reynolds & Thompson (2002), Barres et al. (2005) and Kipesha (2013), efficiency is an important attribute in any organization including microfinance institution for a number of reasons. Firstly, input resources used by the institution are scarce and limited since donors are unwilling to fund the microfinance institution to the required capacity to serve all poor clients. Secondly, the rapid growth of microfinance institution sector across the world has increased competition for donor funds. Third reason is the recognition of the institution by development expertise as a promising and new tool for poverty alleviation has increased the need for their efficiency in the use of public funds. Fourth, increased competition among the organizations themselves has resulted into lowering interest rates and operating more efficiency. Finally, profitability potentials of microfinance industry have attracted commercial banks and other private investors to engage into microfinance business with efficient operations, better utilization of the resources and reduction of the amount of wasted and lastly most of the donors are now interested in funding MFIs which are sustainable and efficient (Tahir and Tahrim, 2013).

Efficiency measurement in the microfinance institution is also very crucial as it presents information about the organization performance especially on the use of resources and minimization of wastes. While effectiveness measurement in microfinance institution is important to measure the goals achievement. It helps organizations in setting their targets for monitoring activities through better management of their bottlenecks and its barriers hindering the performance and also helps the measurement, monitoring and improvements of results leading into increased performance and profitability of the organization.

II. Research Questions:

1. How is the current business model practice in the Bright Kids Uganda' microfinance program?
2. How is the business model practice in the Bright Kids Uganda compare to other organization's model?
3. What is the evaluation to improve the current microfinance program in the Bright Kids Uganda?

III. Methodology

The study utilized the qualitative literature review and interview methodology. The analysis provided as an examination of the past research studies, and qualitative data through interview with program participants and organizations. The interviews were conducted by the group project of the GSPIA' summer research intern team, which the author became one of the team. The analysis will also provide the benchmarking process with the other world's best practices.

IV. Organization Profile

Bright Kids Uganda is a children and youth organization located in Katabi, Uganda about nine kilometers north of Entebbe, Uganda. In April 2000, Victoria Nalongo Namusisi, current Director of BKU, first founded the organization to rescue kids on the streets. The issue of the poor and those suffering from HIV/AIDS not only affect the community in Katabi but also echoes the whole story of

Uganda. Moreover, many of the children at the organization are orphans. They have no support from either parent or any other family, even though some have next of kin living in the Katabi area. Unfortunately, many of these families cannot afford to support their children due to subject to extreme poverty. Not only helping abandoned children from the street, BKU also offers food and support for the children who are caught in this situation, so that they could live with family and continue pursuing education. Presently, BKU is home to around 120 of the children from ages of two months to 18 years old, of which the number is increasing each year. Furthermore, BKU also supports another community-based youth and families to receive support for the school fees. (BKU Social Business Plan, 2014)

One of the projects under the Bright Kids Enterprises is developing a Community Development Fund which performs as a primary resource for supporting BKU development activities in Katabi. This fund program is particularly aiming families and single mothers of children supported by BKU. It implements a small-scale micro-loan projects which the goal is to increase self-reliance and income generation for the beneficiaries of the loans. (BKU Social Business Plan, 2014)

In the beginning of the project, sequences of loans have been distributed to single mothers of BKU children. Most of the participants have been paid back in full. Each loan participant either produces Ugandan crafts, owns a small family stall of food for sale, and/or runs a beans and rice restaurant. The loans provide opportunity for the families to keep foodstuffs supplied, as well as much-needed charcoal for cooking, thus increasing sales and income, supported by the loans. The microloans by the organization have facilitated vulnerable community in self-sustainability, starting at mostly 150,000 UGX, then 165,000 UGX, and 200,000 UGX for a third round. Finally, the funds could potentially grow to include other peoples of the wider area in Uganda with the boosted capacity and development of the organization. (BKU Social Business Plan, 2014)

V. Current Microfinance Model in the Bright Kids Uganda

Bright Kids Enterprises (BKE) has been operating its micro-finance program since 2014. In 2015, BKE also started its mission to empower disadvantaged communities to Barlonyo, village in the northern part of Uganda. BKE provide financial assistance to poor families by generating two different model-operations in the Entebbe (main office area) and Barlonyo (Northern Uganda). Therefore, we will discuss these two operations into different part.

1. Entebbe Model

The business model practice for the microfinance project in Entebbe is the individual model. The participant could directly apply to the loan individually to the organization. The disbursement process is quite simple. It can be divided into four process: business proposal application, review and visit, contract signing, and finally fund disbursement.

First, the loan participants need to develop their business proposal, which simply about the condition of current business and prospects. If they are applying for a loan to start a business, they must give a similar proposal detailing their intent for the business and, similar to a current business owner, how they plan to use the funds provided by BKU for their endeavor.

Second, the organization will review the business proposal and verify the validity of the applicant's application. The organization will visit the business' physical location, checking the business' records, and taking documentation of the place, and file all of them to the participant's application. If the applicant is seeking a loan to start their business, the organization will establish an interview to consider whether the plans for the loan and for the business can be substantiated.

Third, the applicant is then conducted to sign a contract once their proposal is approved by the committee. The contract between the loan participants and BKU summaries an agreement specifying the amount to be disbursed, the interest rate (a one-time charge of 12%), the repayment schedule (usually in monthly basis), and repayment time limit (12 months). The organization's accountant will be the one who tracks repayment until its completion.

The loan participants can make a payment through directly come to the office, or during program visitation, or also using mobile money. The program coordinator will regularly visit the loan participants, to do a check up on the borrower's business and help them by making a recommendation which can help their business. The participants also need to come to the monthly meeting in the main office to give the opportunity for the participants to meet the organization, share the problems, pay their loan, promote their business, or just share the lesson learned with another participant. From the organization side, this is a way to maintain a productive relationship with the borrowers and a community building.

2. Barlonyo Model

Unlike the individual model in Entebbe, the model in Barlonyo applied the Grameen Bank group model in which participants need to form a group and trust each other to pay back their loans. The organization develop the microfinance project in Barlonyo to improve community's economy after shattered by armed conflict and civil war. The Barlonyo model also has a local program coordinator who assists monthly meetings and cooperates with the organization about the loan participants condition and repayment of the loans.

The general loan process in the Barlonyo microloan program, including: business plan, group formation, business training, and cash disbursement. First, the participants will discuss to the organization about their business condition or business plan. The organization will have a close examination of the business and the needs within the community. Once the loan participants agree with the term and willing to participate in the group lending model, the organization will offer a loan. Second step, the organization will find other participants who willing to join in the group loan program and places them in groups of five.

Third step is the business training. The training will cover basic accounting and finance, marketing, goal setting, record-keeping, financial literacy and every participant need to complete it before they get the funds. Each member in the group has to pass the training in order to receive a loan. Finally, they will get the cash disbursement subsequently. The loan repayment is done monthly through the program coordinator in Barlonyo. It will be done along with the meeting between the groups and the coordinator, also to discuss if there is any issue. The coordinator will then meet with the organization during the organization visit.

One concern regarding the group lending model is that they need to rely on each other in order to receive new loans and thus, repayment become really crucial for the group' business progress. The groups have different approaches to handle with internal conflict, a different number of meetings per month, and different methods to manage the repayment issues. However, all groups in Barlonyo have created a collateral system to offset the gaps in repayment.

VI. Discussions of the Microfinance Business Model for BKU

a. Benchmarking Process with Another Model Practice

- Grameen Bank

The idea of Grameen Bank was developed by Muhammad Yunus in 1976. The idea of the program was born in the village of Jobra, Bangaladesh, when he had a field visit with his students. He met a lady working with bamboo and then surprised to realize that her status could be bonded labor if she was not able do manage five takas or around $22 cents to buy raw materials. She explained that she needs to pay 10 percent per week of her loan to local money lenders. In some cases, people even charged until 10 percent per day, in which eventually makes people who start borrowing with them only get poorer instead of getting better economically. Then, Muhammad Yunus lent 856 takas (or equal to $27) to 42 people in Jobra village and conveyed them to repay without interest. Since then, he formulated a model of group lending loan in the region in effort to help the poor and improve their conditions. Grameen Bank reaches 80,511 villages and has 7.4 million borrowers and recently passed the $US 6.6 Billion mark in loans to the poor. Grameen Bank has also successfully initiated product diversification through forming Grameen Shakti for the development of renewable energy resources for poverty eradication. In 2006, it creates impacts to 700,000 beneficiaries and 3.85 MW installed power capacity.

There are some characteristics which explains why Grameen is a widespread and accepted as leading model in the microfinance practice across the world (Josee, 2008):

> *1. Targeted to poor*: This model focuses on the poor and answered their need for access to financial system. The loan is disbursed based on certain criteria such as: size of the land property, condition of the house, and household's income.

2. Door step service: The model also broke the typical approaches of general financial institution. They go directly to clients and approach them, instead of clients to bank in this system. All the financial services are distributed through regular meetings in the community. This creates opportunity for all the poor for financial services.

3. Less Collateral: In the Grameen Bank model, loans are generally disbursed without collateral. Unlike conventional bank, clients who could not access funding due to lack of collateral or were not able to complete several documents required by the bank, can still get loans from Grameen. The model believes that poor people should be bankable in order to improve their life, hence the system needs to be more focus on the cash flow and client's repayment history, rather than a physical collateral such as land and building.

4. Repeated and increased volume of loans: The loan in Grameen Bank is disbursed in cycle from 1 to 1.5 years' time period. The loan cycle can be reiterated and the volume of the loan growths in each cycle. This system can create a possibility for the clients to repay the loan in different installments.

5. Good repayment: The model is surprisingly could generate repayment rate above 95% in the region. The success factor of this accomplishment is because the model could implement the right methodology and strong discipline in the system.

6. Focus on women: Grameen clients are exclusively women, because they believe that women are a key driver of family's economic improvement. This system has contributed to women empowerment in Bangladesh and is an inclusive system for poor families.

7. Fast growing: Again, due to their model which is easy access to loan, easy repayment schedule, door step service, and strong financial discipline implemented in the system, their business could grow fast in the region.

8. Impact on marginalized groups: Grameen Bank model has positive impact on the lives of the poor. Not only has impact in income generation, Grameen has increased awareness on health and education among the disadvantaged community. It has been found helpful on cultivating living condition of the marginalized society. Access and control over resources, collaborative action of the society, and contribution of women on decision making has improved through Grameen Bank model.

b. Comparation Analysis between Bright Kids Uganda Microfinance Model with a Grameen Bank Model Practice in Nepal

1. Cost Analysis

In Nepal, the major cost-related problem for the microfinance project is the excessive overhead cost. When an organization starts a new project, it suffers numerous costs such as: group formation cost, training and awareness cost, higher interest rate for the deposit, and the other costs related to additional support programs to the client. For the organization, it would take at least 1 to 2 years for the project to achieve operational break even, it would take even longer time in some challenging areas, like hill area.

The similar problem is found the practice of Bright Kids Uganda's microfinance project. The organization still require setting up an overhead cost, which currently depends on the funding from the donors and grant donation. It is even harder for BKU to project the operational break-even position of the program because the lack of accounting system in the project and the whole social enterprise business. However, the scope and model in BKU is considerably simpler than the other model in Nepal or Bangladesh.

2. Institutional Capacity

The working system in Nepalese microfinance institution is still conventional. Most of the practices are still lack of expertise in information technology and organizational management. The bookkeeping and other accounting systems are still depending on manual works. Since there is no proper IT system, the works become time consuming and uninteresting for the staff. However, it is understandable because to build a system for their works will be very expensive and it is not affordable for microfinance institutions in Nepal.

In comparation with the Bright Kids Uganda, they still got a lot of working to do in terms of the institutional capacity. The bookkeeping and other accounting practices are still manual and lack of information technology. In the BKU case, they lack fund resources and human resources to run the project. Transparency, integrity, and accountability of the management are essential for the project. Meanwhile, BKU had to face this problem in several years ago and had to restructure their organizational system. Having said that, the institutional capacity become a common problem for the microfinance project institution in developing countries. It is challenging for microfinance institution to balance their stability, sustainability, and the growth while they are trying to solve the community's problems. They need to divide a focus on how to manage their internal organizational development while on the other hand, they are trying to develop their beneficiaries.

3. Interest rate

Ideally, interest rates should be arranged competitively to offer the uppermost potential rate of interest on savings and a low rate on loans. This should be done so that the interest rate will cover exactly the total operating costs of the microfinance project. In the context of Nepalese microfinance, the interest rate is not the problem but rather the easy availability of the loan is the main problem. The interest rate of Nepalese microfinance is around 18 to 25 percent. The interest rate set up is considering the financial cost, operating cost, administrative cost, future growth projection and the inflation rate in the country. The interest rate even higher in the leading private sector institution at around 20 to 25%. The average private sector institution has documented profitability at 20% interest rate, however the government initiated Grameen Bank model in Nepal are in loss by charging the same interest rate. It has been reported that the effective management system also has a big role in the sustainability of the microloan practices. The suitable interest rate in Grameen system is 20% to 25% with effective management system for future expansion (Josee, 2008).

Currently, Bright Kids Uganda is implementing a flat annual interest rate 12%. In addition, the average interest rate applied by a microfinance or banking institution in Uganda is around 18-45%. Therefore, compare to the general practice in Uganda and Nepal, it has determined that the current annual interest rate is considerably too low. In this regard, it is recommended that BKU raise its flat annual interest rate between 15-18%. Although, this rough estimate would need to be justified through further calculation. The program needs to manage its interest rate at a level which would cover its expenses, while not being a burden for its participants. Ideally, in order to decide the most effective interest rate, a pricing formula would need to be configured. This formula would cover administrative expenses, cost of funds, loan profits losses, capitalization rates, and investment income. During the writer's involvement in the program, such an endeavor in estimating the formula was not feasible, since the current project does not have its own financial calculation for profits and losses. Albeit it could be understood that the organization wants to help the community and not the increase the burdens of the beneficiaries, but the BKU also need to think about their growth and their sustainability to even create a bigger and wider impacts to the society.

4. Operational Procedure

In Nepal, most of the microfinance institution are replicating the Grameen Bank model that founded by Muhammad Yunus. Some non-governmental organizations, microfinance banks, and the cooperatives are using modified Grameen model that are designed based on their needs and conditions. In Nepal, most of microfinance institutions create a center that included 40 to 50 members in one. The model in Nepal also has regular monthly meeting and monthly collection system. Even though some of the microfinance institution have applied weekly and periodical collection system. In the case of Nepal, the monthly model is suitable in the area with scattered and low-density population, especially hills. In terms of the operation, few microfinance institutions in Nepal also already diversified its loan products. The diversification is including consumer loan, irrigation loan, renewable energy loan, etc. (Josee, 2008)

Meanwhile, in the Bright Kids Uganda, as stated above, it has two essentially different model implemented in two different areas. The group of five lending model in Barlonyo and individual lending in Entebbe. The group lending model in Barlonyo could be considered as the Grameen Bank model, in which it is a group centered micro financing system that depends on group liability as a replacement of the collateral requirement by the individual. The group model in Barlonyo success depends on the social pressure and security of joint financial responsibility, also service in person to loan recipients. The practice in Barlonyo could be deliberated as well-practice system since it can maintain high repayment rate. However, the operational in the Entebbe region, which adopt individual system creates some challenges and need to be addressed by the organization.

VII. Conclusion and Recommendations

The common challenge for the microfinance practice around the world right now is how to create a sustainability operation and durable service of microfinance. The microfinance institution needs to maintain their organizational management and development while leveraging an impact on their operated society. Microfinance business model delivers service at the door-step of the poor based on the value that the disadvantaged society should have an open access to financial services, for that reason the bank or financial institution should go to the people. This value endorses credit or financial access as a human right.

Generally, microfinance institution is operating on around 20% to 25% interest rates, which is usually still not sufficient to cover the operating also overhead costs and the risks that they need to face. Most of the microfinance practices are in loss due to low interest rate and lack of institutional capacity and management. In the case of Bright Kids Uganda, they are experiencing both of these problems.

Another recommendation and takeaway from the benchmarking model is product diversification. Even though there are some discussion to review whether microfinance programs should be separated from other development programs and managed independently. Nevertheless, in many practices around the world, the microfinance institutions have impressively adapted the Grameen Bank's approach and formulated applicable financial service technologies to perform success. Many microfinance institutions have acquired microfinance program as their core activities and have product diversification to boost their operation as sustainability plan. The Bright Kids Uganda already has some other business units to support their development operation, but there are some rooms for improvement in their practices.

On top of that, the microfinance project mission, regardless of its model, is to support the poor families to help themselves to alleviate the poverty on their life. It is aimed to the poor, predominantly underprivileged women, and therefore an effort to reach out the poor is a must and a non-negotiable mission. The Bright Kids Uganda need to achieve and maintain sustainability as a current directional goal, so that it can develop its program outreach without any constraints, including fund or organizational constraints.

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