Microfinance in protracted refugee situations: Lessons from the Alchemy Project

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1.0 Introduction: Microfinance and Refugees

The problem of how to support refugees[1] and other forcibly displaced people in protracted situations continues to challenge aid agencies. A protracted refugee situation is one in which refugees have been ‘stuck’ for a period of time[2] beyond their initial displacement, where they are unable to return to their homes, and no solutions to their predicament are in sight. One of the defining characteristics of protracted refugee situations is the rapid decline in the supply of humanitarian assistance, including food aid. Agencies now increasingly recognize the need to support the efforts of displaced people to pursue their own livelihoods, but there are few resources available. Aid agencies have experimented with interventions such as income generating or cash-for-work programs, but these are often the first programs to be cut, and in general they are not well resourced, understood or evaluated.

Microfinance services[3] in developing countries, especially South Asia, are now well established and have shown significant success in poverty reduction (Simanowitz 2002). In situations of forced displacement, microfinance has not been widely attempted, because refugees and IDPs are considered too risky an investment for a variety of reasons outline below. However, as increasing numbers of refugees and IDPs remain ‘stuck’ in protracted situations, some NGOs have introduced microfinance services for refugees, and have had some positive results. [4]

There are several reasons why microfinance should be considered as one option to support the livelihoods of forcibly displaced people. First, by going beyond the traditional relief-based culture of handouts, it offers a more dignified way to support refugees. Second, it offers a range of services those refugees in protracted situations need, and which traditional relief doesn’t provide, including credit, savings facilities, even micro insurance. Participation in a microcredit program eventually will provide refugees with a credit history that will benefit them if they apply for loans from larger banks. Third, it is potentially sustainable, and not tied to donor cycles, particularly if microfinance institutions can be brought into the community. Indeed, in using microfinance to support refugees, the goal is to provide a conduit to the formal banking sector. In this sense, the use of microfinance for refugees represents the kind of crossover programming that spans both relief and development interventions. It is a

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[1] The term ‘refugee’ is used in its broadest sense here to refer to registered refugees, asylum seekers, and those with various types of temporary permission to stay. It does not include migrants who have come to find work, although clearly it is often difficult to separate categories of people from the same conflict-affected country.

[2] Jeff Crisp (2002) demarcates five years for the period, but there is no particular justification for any minimum period, the key feature is that the displaced are trapped in an economic and legal limbo.

[3] Microfinance constitutes a range of financial services, including credit, savings facilities, money transfer services, insurance and currency exchange, which are targeted at low-income people. These services can potentially be provided by community groups, NGOs, commercial banks, and moneylenders. See ‘Microfinance Good Practice Principles in War-Affected Contexts’, draft, Concern International 2004.

[4] For example, ARC in Sierra Leone and Guinea, CORD in Zambia and World Relief/FCC in Mozambique.

transitional type of intervention that can be used as a complement to traditional grant-based relief programs, as a way to support host communities, and to support reconstruction when refugees repatriate.

Over the past ten years, the fields of microfinance and poverty reduction have created a substantial body of knowledge and best practices (see Bibliography). Microfinance practitioners have developed program standards and best practices in order to have a common language and to improve program quality.[5] Recently, additional principles for conflict-affected areas have been added.[6] Importantly, many relief organizations have realized that they should not attempt microcredit if they cannot meet recognized standards, because of the potential for damaging the credit culture of the area.

This paper explores the challenges for using microfinance services to support displaced livelihoods, and, drawing on best practices in microfinance, suggests ways in which program design can be adapted to take into account these challenges. The paper outlines some of the main institutional and structural obstructions associated with protracted refugee situations, and suggests how these obstructions can be circumvented by incorporating the lessons of microfinance into program design and creating new kinds of programs for refugees. The paper explores the circumstances under which different microfinance services are possible in displaced contexts, and the conditions under which they should be introduced and undertaken. It also suggests ways in which relief and in-kind loan programs can complement microfinance services, for example, by enabling people who are not 'ready' for a microcredit loan, to jumpstart their livelihoods and develop their capacity to engage with microfinance institutions. The paper draws on the experience of the Alchemy Project, and experimental program aimed at understanding best practices for supporting refugee livelihoods.

1.1. The Alchemy Project

The Alchemy Project is an experimental program aimed at exploring ways to support the livelihoods of displaced people in Africa. The Project's approach is to develop a relationship with a partner NGO in the field by providing loan capital for different kinds of programs (e.g. microcredit, in-kind loans, livestock), and then working with our partners through the placement of interns, as well as workshops, project exchanges and site visits, to assess the impact of the loan program on refugee livelihoods and wider social effects

The Alchemy Project is based on the following premises and assumptions:

- We recognize that it is a mistake to target displaced people while excluding the host communities in which they live and which often supports them. In many cases, the host community or local population is as badly off as the displaced people living among them, and providing only the displaced with aid or livelihood

[5] See Donor Guidelines for International Best Practices (1995) [get full reference]; CGAP, http://www.microfinancegateway.org/impact/guide2.htm.

[6] See 'Microfinance Good Practice Principles in War-Affected Contexts', draft, Concern International 2004.

resources is unfair, unethical, unsustainable and ineffective. Programs focused on refugees can aggravate negative or lead to resentment and harassment, unwillingness to host refugees and pressure on the government to impose more restrictions.

- However, in many host countries, refugees are physically separated from local communities by government policy that requires them to live in camps. Such policies also frequently deprive refugees of their social and economic rights to pursue a livelihood. Encampment policies discourage the economic and social mixing of displaced and locals, but in most cases, there is some interaction between the two populations, especially in the form of camp markets or trade between locals and displaced.
- Therefore, the Alchemy Project uses different approaches: where displaced people live amongst their hosts, program resources are provided to both populations; where displaced people are separated and at significant disadvantages to their hosts, as in camp situations, resources are generally provided only to refugees.
- A long-term goal of the AP is to support the expansion of existing microfinance or banking services in the host country in question, so that these services can become available to displaced people and their hosts. We seek to encourage and enable a credit-based culture in contrast to the dominant grant-based culture that exists in most humanitarian situations.

The paper emerged from the Alchemy Workshop held in Maputo, Mozambique, in February 2004. This document is intended for agencies seeking to implement credit-based programs in refugee and IDP settings and host communities. It is a work in progress, and we hope it will serve to stimulate further debate and discussion.

2. Constraints to providing microfinance in refugee situations

Refugees live in a variety of situations: some in camps, some self-settled amongst local population in rural areas, and others in urban areas. Camps can be in remote and isolated regions, near the border and confronting serious security problems, or they can be close to towns, in relatively security, and with access to humanitarian assistance and economic opportunities in the town. Most refugees do not live in camps, but are self-settled, that is, they live outside camps, both in remote rural areas primarily engaged in farming or pastoralism, or in metropolitan areas pursuing a range of informal sector activities. Their living situation and particularly their rights in host countries have implications for the kinds of livelihoods that are possible for them, and for program interventions such as microfinance.

There are at least four key factors that set refugees apart from non-displaced host populations, and make them greater risks for microcredit. These factors are often the reasons why traditional microfinance institutions choose not to engage with refugees. Those microfinance organizations that have engaged successfully with refugees have been careful to design their programs so as to take these factors into consideration when designing and implementing microcredit for refugees.

2.1. Insecurity and Difficulties with the host community

Refugees and other displaced people often live in situations where they are exposed to the violent conflict or persecution that caused their displacement. Refugees living near the border are often caught up in, or targeted by the conflict in their home countries when it spills over the border (e.g. Burundian refugees in Tanzania, Sudanese refugees in northern Uganda, Afghan refugees in Pakistan, Burmese in Thailand, etc.) Urban refugees are usually not directly exposed to the conflict, but they often fear pursuit from their home countries and believe themselves to be in danger. While local people may also be caught up in this insecurity, the displaced are at greater risk by virtue of their links with the home country, their marginalized and isolated position (socially and geographically), and the weakness of the legal system protecting them. Even if this insecurity is intermittent, it can create problems for refugee business enterprises, inhibit travel, obstruct market opportunities, and place refugees at increased risk for their lives and property.

Refugees can also encounter local crime, police harassment and other security problems. In some cases, including urban areas like Johannesburg, the local population has resisted refugees' presence in the marketplace, and they have created problems ranging from refusal to buy goods and services from refugees to reporting their presence to the police.

In addition to physical insecurity, in most cases, displaced people are often close to destitution and lack basic needs. Under these circumstances, many will need relief to sustain them, even thought they may be capable of microenterprise. This means agencies must find ways to provide both relief and microcredit without confusing the two programs. As we discuss below, different approaches can be used to get people onto needed relief and at the same time developing their capacity to engage with a microfinance organization.

2.2. Instability and Mobility

A second factor structuring the refugee context is the possibility of further displacement, in the form of onward migration, repatriation or resettlement. In protracted situations, while refugees seem to be 'stuck', many are planning or hoping to leave – either to return home, or to move on to other more promising places, or to be resettled. In addition, refugees are sometime forcibly or unexpectedly relocated, as a result of forces beyond their control (such as changes in government policy, attacks, camp relocation). The sudden departure of refugees is one of the biggest headaches for credit programs because it means loans are not repaid, rotating loan funds are lost, and the loan program's credibility is compromised. For example, in western Zambia, nearly half of the refugees in CORD's program in Mayukwayukwa, spontaneously repatriated to Angola in 2003, many without full repayment of their loans, and this had a knock on effect as people saw how others 'got away with it'. The higher probability of future mobility creates an increased risk of abscondment and potential problems with repayment, and makes refugees a riskier prospect for potential creditors. As a consequence, clients face higher interest rates, shorter business cycles and tighter repayment schedules.

2.3.Loss of Rights

Refugees are more likely than their hosts to be deprived of the legal, social and economic rights that enable them to pursue a livelihood outside camps or designated zones. The refugee policy environment created by the host government can include prohibitions or restrictions on freedom of movement, the right to work and own land or business property, [7] and difficulties with obtaining licenses. These constraints limit refugees' ability to engage in economic activities, and frequently obstruct – but do not end-- their ability to earn a living

While all of these problems exist for local people too, the displaced are at greater risk in these respects. For them, insecurity, further displacement and lack of economic rights are structured into their livelihood context. Any intervention that seeks to support displaced livelihoods must build these factors into program design and implementation.

2.4. Traditional relief agencies and the culture of free services

In protracted refugee situations the long-term presence of relief agencies and personnel with entrenched practices and attitudes about relief programs can create difficulties for microfinance programs. Relief agency personnel, both local and international, can be strongly invested in grants-based programming, and resistant to new ideas about livelihoods or loan-based programs. Incidents of fraudulent behavior and abuse of power by both refugees and agency staff have been reported in refugee camps, and these problems are probably higher risks in camp contexts. One commenter writes, "The population that is used to free-services, is easily tempted to exploit the system—often characterized by failing control mechanisms--to its own advantage. And staff can be tempted to abuse their power over extremely vulnerable beneficiaries."[8]

A widely held view in the microfinance industry is that it is generally a mistake for refugee agencies lacking technical expertise to attempt to provide microcredit. One problem that arises is that refugees end up receiving relief handouts with one hand and making loan payments with the other. Given the longstanding association, in the minds of refugees and aid workers alike, of UNHCR with hand-outs and 'free' assistance, it may be useful to separate microcredit programs from UNHCR or relief organizations that have traditionally handed out grants. The grant mentality will be deeply associated with these agencies, and it is difficult for an agency to switch from grant and handout mode to loan mode. The skills and mindset needed to manage and administer microcredit programs are different from those found in traditional relief programs. A separate agency, de-linked from the relief agency, should manage and dispense loans to refugees, so that microfinance and relief services are always delivered through different channels or

[7] For a detailed discussion of these rights, see *World Refugee Survey* 2005, particularly their useful list of 'Anti-Warehousing Rights' (pp. X).
[8] Ton de Klerk op cit.

departments.[9] E.g. in Mozambique, World Relief delivers traditional refugee assistance, while a separate microfinance branch, FCC, has a special refugee microfinance program as part of their country-wide microfinance services. Similarly in West Africa, ARC separates microfinance from its other programming.[10]

Unqualified agencies that try to provide microcredit to refugees and then fail, or weak programs that promote bad practices, can create problems for the refugees and undermine the ability of more qualified agencies to implement effective programs. Weak programs will also discredit the idea of using microcredit for refugees, leading to reduced donor funding. Industry experts emphasize that before attempting to provide microcredit services, agencies should have good track records in microfinance, and considerable technical support. Many experts urge that microfinance should not be treated as a short-term NGO program, provided for a limited period, -- or approached as an NGO project that will end when the funding runs out. Stopping and starting a microcredit program does more damage than good, and undermines the credit culture (that will hopefully replace the grant culture).

However, as refugee agencies search for ways to support refugees, inevitably situations arise where agencies without microfinance technical expertise attempt to implement a microcredit program under less than optimal conditions. When this happens, programs can be improved if attempts are made to abide by best practices, and to take note of lessons learned. Microcredit is one among many livelihood support options, including contingency grants, business training, and savings promotion programs. Microcredit should only be chosen as an option when the agency has the skills to do it correctly. A variety of tools and best practices are available on the web (see Bibliography), and lessons for refugee situations can also be drawn from microfinance attempts to target the poorest sectors of the community (Simanowitz 2002). The remainder of this paper summarizes and adapts these lessons for refugee situations.

3. Adapting Microfinance Best Practices for Refugee Situations

Through increasing their understanding of refugees' situations, MFIs can improve their outreach and their effectiveness. In turn, by increasing their understanding of microfinance, refugee agencies can make their programs more effective.

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[9] The separation of loan programs from relief agencies is not always possible. In field situations where program officers are responsible for both loan programs and traditional relief programs, it is difficult to explain that one program requires repayment and the other does not. In such cases, it might help to explain to refugees that different donors require different conditions for each program. When programs are carefully explained to refugee populations, and their cooperation and understanding is sought from the beginning, everyone – refugees and NGOs alike--is more likely to work together to make the program work.

[10] This model is similar to that of BRAC's IGVD program in Bangladesh which got people onto relief and then developed their capacity to engage with the MFI.

3.1 Foregoing sustainability and improving outreach

Many successful microfinance programs for refugees do not aim at operational or financial sustainability. While interest-bearing loans are possible for many clients, not all refugees are able to meet stringent repayment conditions, and there is a grater likelihood that the program will require overall external support. As in all communities, in refugee situations market forces operate to serve the less poor and more powerful or organized. Not all poor and marginalized refugees are appropriate candidates for microfinance, and they should be targeted for other kinds of programs (see below). But some refugees who could benefit from microfinance, including those labeled as 'vulnerables', are less present in programs as a result of self-exclusion, deliberate or unintentional program policy, exclusion by other clients, or by dropping out of the program. Agencies should understand which refugees they are not reaching and why. Often it is left to local staff to identify the vulnerable persons in a refugee situation; but it is useful to establish context-specific, objective, simple and measurable criteria concerning vulnerable populations, that could be used for planning, monitoring or evaluation purposes. Reaching all refugees in the community requires deliberate targeting and motivation of poorer or more vulnerable people[11]. - Active targeting leads to a greater focus and inclusion. Products can be designed to be appropriate for those who are more vulnerable

3.2 Appropriate products and services for different refugees

Microfinance services for refugees should be designed to reduce poverty, risk and vulnerability. Like the very poor, refugees need a mix of financial services, including different forms of grants and credit, savings and money transfer services. Other financial and non-financial products, such as emergency loans, insurance or educational inputs can help refugees cope with emergencies, smooth consumption, and generally reduce their risk and vulnerability.

However, clients' needs for flexibility and a range of products must be balanced with the agency's capacity to manage a complex portfolio. For example, while it is important that loan amounts are appropriate to meet the special needs of refugees, agencies should not over-estimate the required loan size. Loans that are too big are more difficult to manage. If an agency has the capacity to offer larger loans, and the demand is great enough, it may be a valuable service, but large individual loans are more complex and demand greater capacity to manage than small or group loans. Another example is the dilemma of whether to provide transportation subsidies, given the isolated location of many refugee camps. Although transportation subsidies can help, there is a risk that they become co-opted by rich traders.

A refugee population comprises individuals and households with different capacities and

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[11] In refugee situations, vulnerables' include "older persons, the disabled, women in late pregnancy, severely malnourished or those in severe psychological distress". UNHCR sometime also includes minority groups and children (below the age of 18) in this category. See UNHCR, *Handbook for Emergencies*, 2nd Edition, 1999. p.101.

needs, depending on when they have arrived, what they are able to bring with them, and what kinds of supporting networks are available to them in the host community. Newly arrived refugees are often economically vulnerable as they have lost their property and have to rebuild their livelihood in a new economic environment, often one with few economic resources such as a newly established refugee camp. For **new arrivals**, interventions should be relatively low risk until the refugee's creditworthiness determined, and the likelihood of further movement or repatriation established. Programs for new arrivals might include a 'starter' grant, or in-kind loans for activities such as horticulture or animal husbandry.

Those refugees with kin or ethnically similar people in the receiving community are at an advantage, as they are more likely to be able to borrow goods and resources, including sometimes land or shared houses. Refugees who have been in the community for longer periods, are more likely to have some access to resources.

3.2.1 Step Programs

Programs should be 'stepped' or graduated according to refugees' needs. ARC's Income Generating program in Guinea has successfully implemented a three-step model. Start-up grants enable economically vulnerable, or newly arrived refugees to start micro-businesses. If they are successful they become eligible for micro-credit services, beginning with a first step, small basic loan. Less economically vulnerable clients are not eligible for start-up grants; instead they have direct access to basic loans. The 'start-up grant' phase can also be left out if economic conditions allow the immediate start-up of a loan program. After successful repayment of their basic loans, clients are eligible for an advanced loan to grow and develop their existing micro-businesses. Both the basic and advanced loans carry a nominal interest charge, in order to simulate normal microcredit programs, create a credit culture (rather than a culture of free services) and thus build a strong understanding of credit for the refugees' return.

3.2.2 In-kind loans

Refugees who are not 'ready' or appropriate candidates for microcredit can be helped with **in-kind loan** programs. In-kind loans provide small livestock or equipment (such as bicycles, sewing machines, henhouses, fishing gear, or agricultural inputs). Repayment takes the form of community services, surplus products (that are distributed to more vulnerable members of the community), or livestock offspring (that are distributed to the next "borrower"). In-kind loans can support refugee livelihoods and build trust between the agency and the refugees.

These programs have less demanding repayment requirements and are more easily managed by relief agencies. Livestock and other in-kind loan programs can help build collateral, rebuild livelihoods, and increase household food security. (Children's protein requirements can be met with goat milk, for example.) Such programs can also prepare the client for participation in a microcredit program, by building familiarity and trust between refugee clients and NGO staff.

The provision of small stocks (goats, sheep, chickens, ducks) either for breeding or trading purposes are good starter programs.[12] Small stocks require low capital to purchase, reproduce fast (goats, for example, produce an average of 1.8 kids per birth) and are marketable in a short time (kids and lambs are marketable five months after birth; chickens can be even cheaper and faster). Small stocks can be distributed to communities on credit – repayment being either in cash or in the form of offspring.

However, in providing small stocks, it is crucial that:

- Clients have husbandry skills and experience in raising livestock either as pastoralists, agro-pastoralists or farmers;
- A feasibility study is done first. For example, the setting must be suitable for animal husbandry. E.g. chickens are often too delicate for hot camps, or there may not be enough space for livestock grazing or browsing in cramped camps.
- Clients should be supported with training and extension services; Local veterinarians or community animal health workers should be consulted and engaged in the program, and if possible, agricultural or veterinary extension services should be provided or at least subsidized.
- There must be a ready market for the finished stocks close by. Transportation to markets is costly and often beyond the capacity of agencies.

Some refugee situations where in-kind or livestock loans are likely to be better options than monetary loans:

- Where the refugees are newly arrived, and there is insufficient familiarity with potential clients
- Where security problems make the presence of cash a risk, or where there are no savings or safe storage places to keep cash
- Where agencies lack the capacity or experience to manage the complexities of monetary loans.

3.2.3 Savings and Money transfer services

Refugees benefit from other financial services, such as flexible **savings** or **money transfer services**, which could help build the financial base needed to start an enterprise. Many refugees receive remittances from relatives overseas, and they should be enabled to access these easily and without undue expense. A money transfer service could be a real boon, and one that might be relatively easily managed by an agency.

The provision of **savings** facilities in camps and remote rural areas is a boon to refugees. Since these kinds of facilities are often lacking in the area, it is wise to extend them to the local community too. Savings should be easily accessible, both for deposits and withdrawals. Similarly, assistance with receiving and sometimes sending remittances is useful to clients.

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[12] Aklilu, Y. and M. Wekeser (2001). "Livestock and Livelihoods in Emergencies: Lessons Learnt from the 1999-2000 Emergency Response in the Pastoral Sector in Kenya." Medford, MA, Feinstein International Famine Center

3.2.4 Supporting programs and services: Training and marketing assistance.

In addition to microfinance services, agencies can assist refugee microentrepreneurs with other services such as **marketing assistance**, and pre- and post-loan business development **training**.

Training of individuals, loan groups and loan committee before loan disbursement is highly valued by group members, and increases the success of programs. While training in business plans, accounting, and leadership are useful, refugee clients might benefit most from help with understanding the local economy, refugee policies, how best to market their products, and social constraints they might face in the host community. Training packages like Start Your Business can help improve business plans. Once loans are disbursed, there should be follow-up training related to business development. Workshops can be used to challenge and brainstorm business ideas, provide business advice, and encourage innovation.

ARC (Guinea) makes business training a prerequisite for grants or loans. The loan or grant groups have to present business plans in their application forms, which serve as an assessment tool for ARC. Prior to the disbursements, attendance at a one-day training session is required. In addition monthly two-three hour training sessions, amplifying on the topics in the original pre-loan training, are organized which occur on the days of repayment of the loans. Topics include: -business management and planning, -record keeping and inventory for illiterates, -pricing and costing, -marketing. Training sessions are designed for clients with low literacy skills and limited formal education. [13]

For refugees with no in-country business experience, **marketing assistance** can help businesses. Refugees often cannot access markets and cash economies, either because they live in isolated and remote border areas, or because the government's policy requires refugees to stay in camps or restricts freedom of movement. (In some cases, refugees are only allowed to travel to specific markets on specific days or they need to obtain a permit from the Refugee Officer to leave the camp, and this process can be burdensome and time-consuming.) Remoteness and isolation of camps increases transportation costs and difficulties both for refugee entrepreneurs themselves and for getting their goods to markets. Street markets in or just outside the camp can encourage trade. Agencies can support street markets by building hangars to shelter them, and otherwise encouraging collaboration between refugees and local people.

Refugees who must travel long distances to urban markets experience problems relating to lack of familiarity both with local market conditions (demand and prices). Although refugees are often quick to grasp the local market conditions, and in some cases, outdo the local entrepreneurs, and even come to control local markets (as in Boane and other urban areas in Mozambique), it is helpful to provide marketing assistance.

[13] Ton de Klerk, June 2004. "Evaluation of the Income Generation Program of American Refugee Committee for Liberian Refugees in the Forest region of Guinea." RRD-Consultancies

Some ways in which agencies can support camp economies and provide assistance with marketing:

- NGOs and UNHCR can purchase items for use in the camp, such as wooden furniture, soap, or food produced by the refugees, from refugees rather than from external markets.
- When movement outside of camps is permitted, other market possibilities beyond the immediate vicinity can be researched. Alternative outlets for selling produce can be found. If it is possible to connect with trading organizations, such as Tradecraft or 10,000 Villages, they can take hand made crafts and other goods overseas to sell. In Johannesburg, art and clothing made by refugees were marketed through the Touch of Africa cooperative.
- NGOs can provide assistance with marketing by way of workshops, and presentations by (friendly) local entrepreneurs.

3.3. Meeting Program Challenges in refugee situations

This section describes approaches that have been used to address the special risks and problems of providing microfinance services to refugees. Programs should anticipate these risks and adapt the program design.

3.3.1. Missing requirements: Collateral and documentation

Refugees' lack of legal documentation and collateral need not doom the loan if appropriate alternatives can be identified. Collateral and repayment requirements must be strict, but realistic, and it is important to build trust and familiarity between NGO and refugees before a program is started. When agencies work with refugee organizations, groups and leaders the resulting familiarity will enable more confidence about the degree of risk inherent in refugee communities, such as the possibility of repatriation. Familiarity will also give implementing agencies more confidence about being flexible about loan requirements such as collateral.

Refugees and asylum seekers might not have **legal documentation** that allows them to remain in the country for periods long enough to complete the loan cycle. For example, in Mozambique, asylum seekers had documents permitting them to stay in country for only two months at a time, so the microcredit organization, FCC, was taking on considerable risk in offering four to six month loans. It might be possible to waive documentation requirements once the implementing agency is familiar with the community, and has the cooperation of key members and leaders who can help detect loan risks.

Refugees sometime lack proper **identification** and cannot cash checks or open bank accounts so monetary loan disbursement mechanisms may require adaptation. Agencies will need to find ways to **work with cash** for both loan disbursal and repayment. In unstable environments, there could be security implications when large amounts of cash are carried around, so precautions must be taken both to safeguard refugees and loan officers. This is an important management issue.

Ideally **collateral** would be given before a loan, to increase repayment commitment. Agencies that have tried to make loans without collateral seldom recover most of those loans, unless they are very small (loans of $10 or less need not require collateral). However, many refugees have little physical collateral to offer because of their flight circumstances, and this requirement can mean many refugees are unable to obtain loans. How to manage repayment in the absence of collateral?

- **Alternative forms of collateral** can be identified. Where refugees have access to farmland, collateral can take the form of vegetables raised by the refugees and then assessed for its market value. Such collateral, however, is very risky as crops may be lost to weather, disease or poor farming practices. Such collateral would be most successful if it could be done jointly with an agricultural program providing expertise to the farmers, and a buyer to reduce the costs of seizing and selling the crops.
- Where no collateral is possible, **loan terms** can be adjusted. For new refugee clients, depending on the business cycle, frequent loan repayments can strengthen the relationship between the loan officer and the refugee client, and help the loan officer understand the refugee's goals and plans. Some businesses with quick turnover allow for weekly payments, others bi-weekly or monthly. At the beginning, the shortest possible period is recommendable.
- Collateral could take the form of savings, or group guarantees.
- Collateral could be provided over time, in small installments as a loan is repaid.

In general, **innovative collateral strategies** are preferable to no collateral. However, some caveats should be in place. Some agencies have provided microcredit using controversial repayment strategies. These include working with the government so that refugees who did not repay their loans were not permitted to renew their documents. Another is working with UNHCR to withhold ration cards to force refugees to make payments. The use of "coercive" repayment strategies or negative incentives is controversial. Some argue that any kind of dependence on government officials to implement a program is unwise, as their cooperation is not always reliable. Nor is it wise to use UNHCR to help enforce repayment (e.g. by withholding ration cards), as this reinforces the unhealthy link between UNHCR and the loan program. It is also argued that such an approach is problematic from an ethical point – denying documents and ration cards to refugees is a violation of their rights. Overly strong pressure to repay – whether from a group or the agency-- can have negative or even dangerous consequences. There have been cases where refugees, desperate to repay in order to stay in the program, have engaged in prostitution, or have used loan sharks to borrow loan installments.

However, agencies using such strategies counter that there is no evidence that they hurt refugees, and in some cases, it is the refugees themselves who suggest such approaches. For example, in Maputo, before FCC took over and started to require physical collateral, the refugees suggested to World Relief (then implementing the program) that to ensure the continuation of the microcredit programs, documents should be denied to non-payers.

3.3.2. Interest rates and repayment problems

Interest increases a program's sustainability by creating additional income beyond repayments that cover administrative costs. Interest rates and repayment frequency should be based on institutional cost assessment, inflation, market rates, risk, and client capacity. In refugee situations, setting appropriate interest rates can be difficult. Refugees are a high credit risk, and accordingly the charge on the loan should be higher than for non-refugees. But high interest rates increase the burden on refugees, when rates for local people are lower. Some experts have suggested that since refugee programs are not meant to be sustainable, charging **nominal interest** can be a way to create a good credit culture. The level of 'nominal' interest is difficult to establish. Some have suggested that the rate should at least cover inflation plus several percent. In Islamic areas, where interest cannot be charged (because it is *haram*), service charges on the loan can be imposed instead. Service charges have also been used in lieu of interest in other settings.

A hidden problem with making repayment on time is that refugees fear losing their position in the program, and resort to alternative means to get the funds required for repayment. There is anecdotal evidence in some camps that refugees resort to loan sharks to ensure that they can adhere to repayment schedules. Other even more risky strategies to get the repayment amount might also be in use. This is a difficult problem to uncover, as refugees are reluctant to reveal this practice, but agencies should create independent monitoring and evaluation systems that can get to the bottom of repayment practices.

Refugee leaders can encourage repayment, resolve conflict and disagreements, and work with NGOs to develop effective and workable programs. However, it is important that the refugee community sees the leaders as legitimate. In camps, leaders can exert pressure on borrowers to repay on time. However, if leaders have too much power, this can lead to other problems in the camp, including excessive coercion to repay.

3.3.3. Group lending

The existence of organized groups in the community is an asset in loan programs because:

- They create strong pressures to repay, and through their networks, can track down absconders. When repatriation looms, strong group organization can enable loan repayment.[14]
- Groups can combine funds to meet the high initial outlay required to setup larger businesses;

[14] For example, it is intriguing to contrast the different group experiences of Angolan refugees in CORD's programs in Nangweshi camp and Mayukwayukwa settlement in western Zambia. In Mayukwayukwa, nearly half of the settlement spontaneously repatriated in 2003, without repaying their loans, By contrast in Nangweshi, where there was strong group control, there were only a few cases of spontaneous repatriation – and they first repaid their loans.The two camp populations were different in origin (Nangweshi was a camp of former Unita supporters), and community pride and group pressure differed in each camp. See Alchemy Workshop Report 2004.

- Groups are self-monitoring and members support each other. They can ensure that those who will not be able to repay don't join in the first place, or the group will carry a member not able to pay in a bad month until she is able to regain lost ground.

Group loan schemes only work in environments of trust, where clients are willing and able to take responsibility for each other's debts. Refugees are often less familiar with and trusting of each other, and their experience does not always incline them to work easily with others. Before introducing a group scheme, it is important to analyze the community carefully in order to avoid creating or exacerbating conflicts where communities are fragile. In both camps and urban areas, the refugee community is often weakly bound together and fragmented. There tends to be lack of trust and little willingness to enter into groups for loan and business purposes. In these situations, it is preferable to work with individuals, and put in place other safeguards to reduce the risk of absconding and non-payment.

In some settings, where entire villages leave together or refugees are familiar with each other, groups can be quickly re-constituted, and refugees themselves set up rotating credit programs or ROSCAs (revolving credit and savings associations). For example, the Likilimba system (or 'likelemba' as it is known in Kinshasa) is familiar to those from the DRC. Each member puts a fixed amount every month and gets the whole lot by turns. Such schemes can be supported or adapted for refugee situations.[15] Where traditional rotating credit schemes familiar from the home country are re-started by the refugees themselves, these groups can supported with loan programs. It is best to work with existing groups – they should not have formed just for the purpose of a loan.

ARC Guinea makes use of the 'solidarity group' model, wherein several individuals receive their loans jointly and are jointly responsible for on-time repayment. Basic loans are provided to 'solidarity groups' of 5-7 individuals. Large advanced loans are provided to smaller 'solidarity groups' of 2-4 persons, generally composed of remaining members of a former 'basic loan group'. However, clients could also apply with individual members of other groups who have repaid their loans. ARC propagates the group concept to facilitate social integration of the beneficiaries, and to encourage mutual assistance and group businesses. Beneficiaries are encouraged to set-up joint businesses, or at least to purchase their goods together as a means to economize on transport costs or to negotiate discounts on 'bulk'-purchases. [16]

Group micro-schemes tend to be composed of **women**, partly because women are targeted and partly because men consider the loan amounts too small for business purposes. Many believe that credit programs for women are more likely to succeed, because men are bigger credit risks – more likely to abscond or misuse funds. However,

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[15] A good model is the MMD program in Niger (see a description at http://www.careusa.organization/careswork/projects/NERO65.asp/)

[16] Ton de Klerk, June 2004. "Evaluation of the Income Generation Program of American Refugee Committee for Liberian Refugees in the Forest region of Guinea." RRD-Consultancies

gender imbalance can lead to problems if men perceive that they are being discriminated against, and that women are benefiting more. Agencies report being pressured by men to increase loan amounts, and to extend programs to men. Women also report pressure from their husbands to use the loan for other purposes than it was intended, or not to repay the loan.[17]

In refugee communities, particularly camps, where there is strong pressure for refugee participation, **refugee loan committees** often approve loans or manage programs. Under these circumstances it is important that careful management and accountability controls be in place. Agencies should work closely with the loan committee to ensure transparency and smooth functioning. Someone with finance or accounting background should be regularly reconciling and preparing financial reports. When handling money, loan committees should be accountable to the agency, and the agency must check that money is being handled transparently and appropriately. Loan committees should also be monitored for gender equity. In many cases, men dominate loan committees, even though more women are loan recipients.

Should refugee loan committees be given incentives?
There is some debate about whether local loan committees add value, given that they need training and incentives to ensure that they feel valued and can support their families. Incentives can be a contentious issue. Various incentive options include committees being given access to loans, or performance related incentives, in which the committee receives some proportion of the amount collected from the interest of the loans. While this motivates the committee to collect funds and also to declare the funds collected, it also creates the risk of the committee exerting undue pressure to recover funds. Another problem occurs when loan committees try to get kickbacks for "assuring" loan approval. Providing incentives to loan committees is not essential, but could be a useful strategy if carefully monitored.

3.3.4. Repatriation, resettlement or onward migration

As the likelihood of repatriation increases, there is pressure to obtain livelihood resources, since returnees expect minimal assistance and little in the way of resources in their home countries. With the camp focused on repatriation and short term priorities it can be difficult to get refugees to think about long-term business strategies. Spontaneous repatriation is a problem for loan programs, and it is difficult to build this risk into a program.

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[17] The role of husbands when woman are loan recipients is a controversial one. Some programs have found that when husbands give permission, or sign documents as co-guarantors, this reduces domestic conflict, and decreases the likelihood that husbands complain about time spent at meetings, etc. However, the issue of husbands' co-signatures is a double-edged sword. In some countries (like Swaziland), the microfinance institution requires that women possess a legal document called "husband's authority to borrow", which is signed by the husband. This eliminates any confidentiality in dealing with the women, and can lead husbands to view themselves as having authority over the woman for the loan (since without his contribution she would not be able to receive a loan). In one reported case in Swaziland, the man took the whole amount from his wife and used it to pay "lobola" (dowry) for another wife. Of course the first wife could not repay the loan after this.

All parties involved with the refugees, including the host government, refugee leaders, resettlement organizations, and UNHCR, must build an understanding about how repatriation or resettlement will be managed in the loan program. When UNHCR initiates voluntary repatriation or resettlement, agencies can plan repayment schedules accordingly. Part of the conditions of resettlement could be that the refugees must have first cleared all outstanding debts with the loan program. Some lending programs have invited a representative of UNHCR to sit on the credit committee and provide any needed information about the potential resettlement or repatriation of each applicant to help inform lending decisions.

It might be necessary to **make loan periods shorter** to reduce repatriation risk. In general, loan cycles should be shorter than in non-refugee situations. A repayment period of 3 months preceded by a grace period of 1 month has worked in some cases. The downside of short cycles is that it encourages short-term business such as buying and selling with no long-term sustainable options.

Loan officers should perform **frequent monitoring** visits - at least twice per month. Refugees are a flight risk, no matter how large their businesses, and it is necessary to monitor for indications that the client may be planning to leave. Such indicators include selling of assets or significant decrease in stock kept on hand.

Refugees can be engaged to work out a compromise solution, such as the possibility of **cross-border programs**. It may be unrealistic to expect that the same scheme can be continued across the border, since refugees often come from all over the country of origin and will spread out again when they return. However, in West Africa, ARC has developed the *Refuge to Return (R2R)* approach, which links financial services to refugees in their country of refuge with those in their country of return through a transferable credit history methodology. By applying sound microfinance practices and providing the necessary incentives for repayment, ARC has successfully provided loans to Sierra Leonean refugees in Guinea and Liberia, and built a leading microfinance institution (MFI) in Sierra Leone to serve them upon their return

3.3.5 Ensuring transparency and controlling abuse of power

Since program abuses and fraudulent behavior or abuse of power are more likely to be high risks in refugee situations, it is advisable that refugee microfinance programs have higher high staff ratios than non-refugee ones. Good management systems relating to planning, client service and administration are also very important.

Other program design and monitoring factors that contribute to success are t*ransparency* of client selection procedures and all money handling, disbursement and repayments of grants/ loans. *Control* mechanisms, including strict monitoring practices, should be in place to preclude abuse of power or fraud.

4. Conclusion and Recommendations

The use of microfinance in refugee situations has two goals. One is to support refugee livelihoods both in their host countries and when they return home. There is now growing evidence that microcredit can help refugees start and sustain small enterprises.[18] A second goal is to provide refugees with a conduit from the informal to the formal or semiformal banking sector. Programs specially designed for refugees, are crucial first steps in enabling them-- and optimally their hosts as well-- to gain experience with microfinance organizations. One of the benefits of participating in microcredit programs is that refugees can establish solid credit histories, which can then be used to gain access to the saving or credit resources offered by banks and microfinance institutions. Agencies can help refugees gain this access, but some caution should be exercised. Traditional microfinance institutions tend not to lend to refugees because they are high-risk clients. In South Africa, after lobbying by refugee advocates, the Nations Trust, a local microfinance institution, agreed to lend to a few refugee clients, but the experiment failed as most of the refugee clients simply disappeared. Care should be taken when working with mainstream institutions, that future opportunities for refugees are not spoiled by inappropriate promotion of refugees before they have proved their creditworthiness.

The successful implementation of a refugee microfinance program can set the stage for other microfinance institutions to enter the community. Indeed, once conditions for microfinance exist in a refugee setting, agencies should seek ways to bring in a microfinance organization.

Microfinance for refugees thus represents an approach to poverty reduction and the kind of crossover programming that spans both relief and development interventions. It is a transitional type of intervention that can be used as a complement to traditional grant-based relief programs, as a way to support host communities, and to support reconstruction when refugees repatriate.

Host Government Advocacy

Microfinance services and refugee livelihoods alike are supported when governments allow refugees to work outside of camps, and undermined when there are government restrictions on refugee work and movement. It is crucial that refugees are granted the economic rights and freedoms set out in the 1951 Refugee Convention.[19] All refugee agencies, including microfinance ones, should be involved in lobbying the government for economic protection (e.g. a stop to police harassment), and the recognition of rights and access to markets on behalf of the refugees. With persistent lobbying there are cases of refugees' economic situation improving. For example, in Maputo, police frequently confiscated products being sold by the refugees on the streets. With lobbying from

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[18] See 'Microfinance as Support for Livelihoods: Evidence from the Field", forthcoming from the Alchemy Project (www.famine.tufts.edu).

[19] For a full discussion of these rights and the relevant Articles in the Convention, see *World Refugee Survey 2004,* http://refugees.org/wrs04/statistics.html

refugee agencies, this practice subsided, and refugees now ‘only’ have to contend with demand for bribes by the police.

Before designing and implementing microfinance interventions, it is important to understand both what the refugee community brings, by way of traditional financial systems, group and leadership structures, skills, and rural/urban experience, and what the refugees encounter by way of government policies, the host community, and security problems. In protracted situations, these conditions evolve and change over time, and programs should be dynamic so as to keep up with new opportunities and obstacles. Livelihood interventions, including credit-based programs, are most effective when they are flexible and designed with specific refugee characteristics in mind, but they should build on best practices.

The economic contribution of refugee entrepreneurs can be a potential win-win situation for both host countries and refugee communities. Their economic contributions can be maximized by agencies advocating for their rights to work and freedom of movement.

We invite further discussion and comments from agencies and individuals seeking to support refugee livelihoods with credit-based interventions.

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