

Economic Review - MARCH 2005

POVERTY REDUCTION THROUGH TARGETED PROGRAMMES: MICROFINANCE AND DECENTRALISATION

In March, the Central Bank of Lesotho hosted a mission from GTZ and African Rural and Agricultural Credit Association (AFRACA). This was a response to the Bank's request for technical assistance in microfinance issues, including review of the policy and legal framework. The two, microfinance and decentralisation of public services (through the introduction of local government), can play a pivotal role in poverty reduction...

MICROFINANCE

Introduction

Microfinance is generally defined as the provision of microcredit by microfinance or other institutions to low income, micro and small entrepreneurs, mostly in the informal sector, who do not have access to the formal financial institutions, to help them engage in productive activities or improve their small businesses. Microfinance has existed for some time in Lesotho, with credit cooperatives being the oldest. Recently, the sector has been growing and informal financial institutions, in the form of rotating savings and credit associations as well as burial societies, have gained popularity. These institutions mobilise savings from members and extend credit to those who need funds.

The role of Microfinance in Poverty Alleviation

Experience in other countries shows that microfinance can help in poverty reduction by improving access to credit to finance viable small/micro business ventures in the private sector. Promotion of the private sector as an engine of accelerated growth has been identified by the Government of Lesotho as one of the major challenges towards development and poverty reduction. As stated in the budget speech for 2005/2006 fiscal year, a policy framework for supporting growth of the private sector is vital for Lesotho.

Access to credit by the poor and rural communities could raise incomes and thereby improve their living standards. This would be possible if the borrowed funds were invested in viable income generating projects. At present, funds accumulated by most of the savings and credit associations in Lesotho are mainly used to finance consumption. This may have to change so that these funds can be used for investment purposes by members of these associations.

The Lesotho Poverty Reduction and Strategy (PRS) identifies lack of access to credit by the poor as one of the major hindrances to the success of small, medium and micro-enterprises, which are mainly run by Basotho. The promotion and enhancement of Group/ Village Savings and Credit Schemes as well as the Savings and Credit Cooperative Organisations should be explored as the main tools for providing the poor with access to credit. The transformation of microfinance institutions to direct funds towards productive and income generating activities should be one of the major areas of focus.

Conclusion

Microfinance could have a positive impact on poverty reduction if it focuses on productive investment activities as opposed to financing consumption. However, there may be a need to address certain structural issues that are likely to impede the success of microfinance projects. These include access to

markets and institutional support and training in business development.

DECENTRALISATION OF PUBLIC SERVICES

Aims and Objectives

Decentralisation is broadly viewed as a strategy towards the improvement of planning and implementation of the provision of public services. It entails incorporating the local needs and conditions while meeting regional and national social and economic objectives. In addition, it promotes more efficient and effective allocation of scarce government resources through improved planning and utilisation of such resources. It also promotes participation of the communities in decision making as well as transparency and accountability by government.

Financing Challenges

Decentralisation involves transfer of the responsibility for delivery of a set of public services from the central government to local authorities. To deliver such services, the local governments should have adequate and sustainable financial resources at their disposal. Thus the issue of fiscal decentralisation, which entails the transfer of financial resources and the establishment of an efficient resource base for the local authorities is important for the success of the system. A fiscal transfer framework that clearly states rules and regulations for the utilisation of funds by local governments should be established. This would ensure that allocated financial resources match the functions and responsibilities assigned to local governments.

The budget for the current fiscal year provides M50 million to the Ministry of Local Government for the purpose of meeting the initial costs of the envisaged Local Government. This is only an interim measure as the Government is fully aware of the need to bestow financial responsibility on the local authorities for decentralisation to be successful. In this regard, the Ministries of Finance and Development Planning and Local Government have been assigned the joint responsibility to devise a policy framework for fiscal decentralisation.

Such a framework could, among others, address issues such as the establishment of an efficient and sustainable resource base for successful execution of local government functions; guidelines for distinguishing activities that could be financed from central government grants, and those that should be financed by locally generated revenue; criteria for tax redistribution and sharing with the Central Government; and putting in place systems for strengthening, management and control to ensure efficient use of resources.

Decentralisation and Poverty

Policies which support decentralisation are to a large extent viewed as effective means of addressing the problem of poverty and paving the way towards sustainable development. However, empirical evidence indicates that decentralisation is not guaranteed to alleviate poverty and bring development.

The role of Local Government in Lesotho and the services that it is envisaged to deliver are central to the country's development agenda as spelt out in the PRS and the National Vision 2020. According to the

PRS, the Government of Lesotho is committed to ensuring the participation of the nation in the development process as a strategy to address poverty. It is in this regard that the Government is heading towards the introduction of Local Government and decentralisation of public services.

Broadly speaking, decentralisation could be linked to poverty alleviation through two of its main objectives. Firstly, enhanced participation of the community in the decision making process, through improved representation could mean that policy makers and implementers at the local level get to know the needs of the community and could as such focus on areas of priority to particular communities. Secondly, successful decentralisation should result in efficient and better delivery of basic social services. Improving access by the poor to basic services, such as health, education, water, sanitation and transport enhances human capital and increases labour productivity thus fostering access to economic opportunities.

Conclusion

For decentralisation to contribute to poverty reduction, policies that drive it should ensure that scarce resources are allocated to activities that are highly likely to have the greatest impact on the poor by reducing their levels of deprivation and vulnerability. Some of the important factors for successful poverty focussed decentralisation include, firstly, the availability of sufficient resources at the disposal of local authorities to fulfil their major task of providing basic services to the communities. Secondly, local human capacity should be strengthened and structures for monitoring the activities of the Local Government should be put in place to enhance proper use and management of public funds.