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Failure by Design: The Rise and Fall of a Microfinance Institution in Zambia – a case of Pride Zambia

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Abstract

Contemporary microfinance has been taken to task over a number of possible failings. At the same time insight into grassroots microfinance institution (MFI) failure is lacking. To that end this paper seeks to articulate and explain different stakeholder narratives about how a once promising Zambian microfinance institution actually failed while seeking to become a for-profit MFI. There are presently few in-depth studies of failed MFIs in those countries where microfinance is still emerging, just as it is in sub-Saharan Africa (SSA), and greater focus upon high profile performers in South Asia and Latin America, which leaves other developments in regions such as SSA much less represented. Using field data from Zambia this study examines the failure of Promotion of Rural Initiatives and Development Enterprises (PRIDE Zambia, hereafter PZ) initiative. It finds poorly practiced governance and accountability mechanisms, and unstable relationships between international donors and the Board, the Board and CEO and with middle management, to be central to its final failure. The study also reveals a lack of transparency and disregard for moral obligations, and poses serious questions about how it and its finances were managed and accounted for, even while this MFI still provided much needed financial services to the poor and vulnerable clients.

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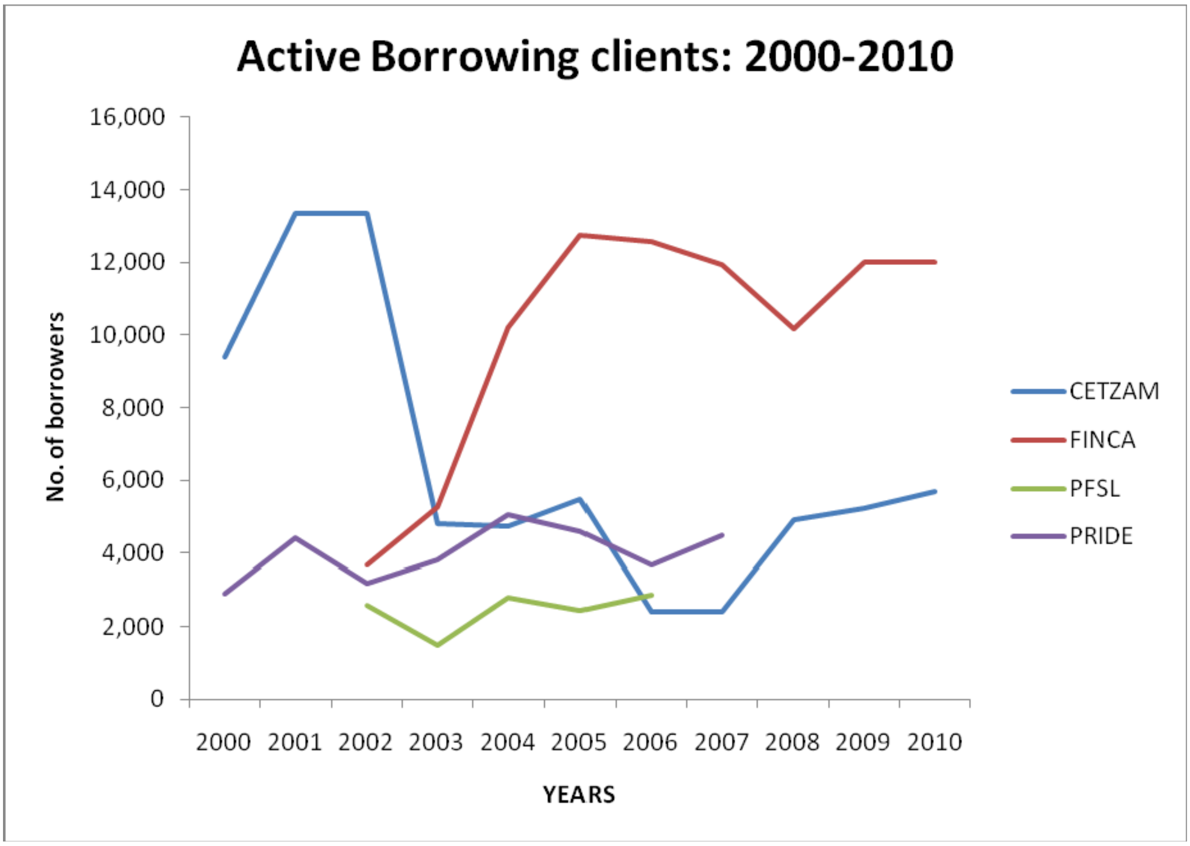
Introduction

MFIs are organizations which were originally set up in order to help finance those small scale micro-enterprises and local economic activities which were largely excluded from formal finance and mainstream banking practice. However, in Sub-Saharan Africa, microfinance is not yet widespread and most low income earners, including many of the poor, cannot access financial services (CGAP, 2009; Spencer &Wood, 2005) while poverty is officially widespread and acute (World Bank, 2009). There are also significant disparities in the level of development and performance across different countries (MIX, 2010). While the developed microfinance institutions (MFIs) of South Asia and Latin America are challenged to become more commercially viable, emerging – often donor dependent - MFIs in sub-Saharan Africa can struggle to survive. Inexperienced staff, questionable working practices, poor internal controls, substandard governance (Mersland and Strom, 2009; Hartarska, 2005) and inadequate management information systems all contribute to African MFI underperformance (CGAP, 2009). In Nigeria, for example, a lack of competent and skilled 'human capital' has been identified as a particular failing (Microfinance Africa, May 2010). In Zambia, Siwale (2006) previously scrutinized CETZAM's near collapse and observed how its subsequent restructuring embraced policy and senior management, product diversification, and further grassroots staff changes in branches. Similarly, Moroccan MFIs were found to lack the necessary skills, knowledge and experience with some being accused of fraud and embezzlement of depositors' funds. Studies elsewhere suggest that many crises are not just random, one off events apart, but originate in serious, and maybe also potentially predictable and/or avoidable, management and intelligence failings (Vaughan, 1996). Underperformance shadows MFI development in Southern Africa (Lafourcade, Isern, Mwangi, & Brown, 2005; Chiumya, 2006; Dixon, et al, 2007) and formal evaluations of impact assessment, program replication, client outreach and financial sustainability (Copestake, 2002) typically suggest that progress here lags significantly behind that which has been claimed for South Asia and Latin America (MIX, 2010; Basu, Blavy, & Yulek, 2004).

The Zambian Context

Zambian MFIs' donor dependence (Bateman, 2010) has potentially serious implications. For example, Musona (2002), Chiumya (2006), and Dixon et al (2007) reveal how relatively high operating costs, delinquency and default, low client intake/retention, potential fraud, and high staff turnover impede sustainability, and much vaunted outreach levels have been lagging behind East Africa for example. This high dependence on donor funds that can be found in many sectors in Zambia is particularly damaging in microfinance, where financial sustainability is of fundamental importance. Indeed, many face important management and corporate governance challenges. Major Zambian MFIs, except for FINCA, have struggled to reach desired client numbers (fig 1.0). As early as 2002, certain donor driven MFIs nevertheless maintained that market-based approaches could 'transform' this situation even though most Zambian MFIs were only just founded in the late 1990s (Siwale, 2006). Since then microfinance has not grown in line with outside expectation (see figure 1.0 regarding major MFIs) and Chiumya (2006) indeed identified rising signs of its possible stagnation and contraction. The PZ case is therefore broadly emblematic of microfinance development at large and indicative of the threats posed to it.



Source: Compiled from MIX and CGAP database: MFIs Trends

Zambian MFIs might potentially provide much needed, but hitherto scarce, financial services in a country where, even by prevailing standards, access remains extremely low (FinScope, 2010; Mattoo and Payton, 2007). The Association of Microfinance Institutions of Zambia (AMIZ) has estimated that the industry's outreach is in the region of 250,000 to 300,000 active borrowers (largely due to an influx of new consumption based MFIs). 19 out of 25 licensed MFIs founded in the last 5 years have indeed been expressly consumer lending based. Since these MFIs do not emphasize small scale enterprise development they simply require formal employment before making a loan. However, an estimated 60,000 borrowers occupy the same enterprise loan market niche in which PZ operated. Additionally, the scope of services has also been particularly limited, with little savings mobilization to date (Dixon, Ritchie, & Siwale, 2006). The law however has changed following the 2006 Banking and Financial Services (microfinance) Regulations Act which has enabled MFIs to mobilize further public deposits and savings. According to BOZ, 4[3] out of 25 licensed institutions have been granted deposit taking licenses. More importantly, the Act has established governance rules and formal accountability channels with the central bank, so that MFIs might evolve into limited companies with identifiable share holders (AMIZ magazine, June 2010). However, there is as yet little serious empirical study of Zambian microfinance, where institutional performance data is still considered proprietary, and remains difficult to access[4]. Enhanced disclosure might reveal more but, so far, the few impact studies have concentrated upon CETZAM (Cheston, et al., 2000; Copestake et al. 2001; Copestake, 2002), except for Copestake, Bhalotra and Johnson's (1998) study of the Peri-Urban Lusaka Small Enterprise (PULSE). No similar impact studies have been conducted on PZ itself.

In explaining the demise of PZ this paper, argues that Zambian microfinance development has been largely donor driven and 'top-down', leaving many precariously founded, and soon needing to reorganize in fear that they might otherwise fail. Even certain stakeholder accounts of PZ's own failure diverge, especially between its funders and managers, and also frontline. By articulating and explaining what happened when PZ actually failed, and how this failure was variously accounted for, this paper highlights how the most well-

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[3] The four are: Pulse Financial services Ltd, FINCA Zambia Ltd, Micro Bankers Trust (MBT) and CETZAM Financial services Ltd.

[4] Personal communication with the Director of the Association of microfinance institutions of Zambia (Lusaka, July 2010)

intentioned/altruistic international donors can still find themselves in a 'no win' position as their much –vaunted developmental initiatives materialize.

Investigating failure of microfinance institutions is important because of the significant resources they leverage in regard to poverty alleviation. The study is also warranted by the dearth of empirical research about developing country MFI failure, especially in a SSA context, where commercialisation might increasingly override other governance issues. This study can help bridge a number of prevailing gaps in knowledge by observing how failure actually originates and materializes in the light of different stakeholder accounts of it. There are few notable field studies of what happens when and while MFIs fail (Fisher, 2002), especially those under pressure to commercialize. Other accounts of failed MFIs- especially those from under researched areas like sub-Saharan Africa are liable to be ignored because they might also challenge current fashionable 'best practices'. Such accounts likewise question prevailing heroic success stories of 'bottom-up' development institutions arising from pioneering regions of South Asia and Latin America. However, other organizational studies elsewhere (Francis and Zheng, 2010; Mellahi and Wilkinson, 2004, 2010; Tedlow, 2008) indicate the importance of learning from successes, crises and failures alike. While it might be argued that, economic, political, historical, cultural and geographical context is important, other MFIs elsewhere might well draw lessons from the PZ case.

The rest of the paper proceeds as follows. The following section reviews the existing literature about organizational failure at large. It is followed by an outline of the approach here adopted to gather and interpret the necessary data from what was an inevitably highly charged field situation. It then details the PZ case in terms of stakeholder accounts of its eventual failure. Finally the particular implications of these findings are discussed.

Literature review/conceptual framework

According to industrial organization literature, the causes of organizational failure can be attributed to external factors, largely beyond the control of managers (McGahan, and Porter, 1997; Rumelt, 1991). Supporters of this view argue that organizational failure does not imply management ineffectiveness or inefficiency (Mellahi et al., 2002), while organizational studies' literature places more emphasis on internal organizational factors as cause of failure (Tedlow, 2008). This position attributes failure primarily to operating problems within the firm as a result of the actions or inactions of managers in a changing environment (Barker & Duhaime, 1997 in Amankwah-Amoah and Debrah, Y.A. 2010, p. 640). Based on this perspective, failure can be associated with a lack of managerial foresight and failure of top management (and Board of directors) to respond. For example, Mellahi (2005) argues that, board members fulfil an advisory duty as they are expected to bring in knowledge and experience from their past managerial experiences and (and in some cases) membership on other boards. Also, Mellahi and Wilkinson (2004) find composition of top management teams and managerial succession to be particularly salient with respect to organizational failure, while Hambrick and Mason (1984) add, an organization is “a reflection of its top managers”. Mellahi and Wilkinson (2010) also observe that, “symptoms’ of organizational failure include market share erosion, persistent low or negative profitability, shrinking critical-that is financial, human, and technological-resources, and /or loss of legitimacy (p.533).

According to Gillespie and Dietz’s (2009) definition of failure, “locus of control for the failure is internal to the organization even though the context for failure may involve external influences” and occurs as a result of “actions, or negligent inaction” from managers (p. 129). This view of failure has found support amongst researchers arguing for effective governance within MFIs (Mersland and Strom (2009), while others find the microfinance sector to have experienced some major failures where, among other reasons for these failures, the inadequacy of governance practices was to blame (Labie, 2001). In addition to weak governance practices, there has been a tremendous growth and institutionalization process experienced by some organizations that is providing an interesting area for further research (especially in SSA) aimed at improving internal control mechanisms, especially mechanisms linked to board action. Accordingly, Mersland and Strom (2009) suggest that financial performance improves with local rather than international directors supported by an internal board auditor, while Hardy et al. (2003) argue for a better MFI regulation. CGAP (2008) identified poor governance as a major obstacle to MFI growth. In the microfinance literature, the analysis of governance has evolved from a principal-agent theory to a more complex, multi-stakeholder one (Giovanna Pugliese, 2010). The discussion here is partly guided by Mellahi and Wilkinson’s (2004) integrative theoretical framework that asserts that: ‘any attempt to explain organizational failure must take into account both the interplay between contextual forces and organizational dynamics’ (P. 34).

Research Methods

Organizational failure in practice is a complex phenomenon which is unusually difficult for intending researchers to design and rigorously control, especially while the process is still under way, and the full consequences may not have materialized (Mellahi &Wilkinson, 2004). The PZ case was part of the longer term study described below and employs a combination of internal documentary sources (including correspondence between the Swedish International Development Authority – SIDA - and PZ Board members and minutes of meetings) as well as semi-structured interviews with SIDA officials, the Director of the Association of Microfinance Institutions, and former PZ managers. It draws upon both the researcher's own long term 'indigenous knowledge', including prior doctoral fieldwork conducted in Zambia between November 2003 and July 2004, but for this specific purpose, the study relies upon close intensive research conducted between July and August 2010 to reveal more about PZ's final failure. The prior fieldwork included three months of observing/shadowing loan officers' (and clients) at work

A case study approach was adopted in line with prior suggestion that "in general, case studies are the preferred strategy when 'how' or 'why' questions are being posed, when the investigator has little control over events and when focus is on a contemporary phenomenon within some real-life context" (Yin, 2003: p 17). As Eisenhardt (1989, p.542) noted, research studies that are rich in qualitative data are particularly useful for providing "a good understanding of the dynamics underlying [a] relationship, that is, the 'why' of what is happening". Furthermore, the use of case studies enables researchers to provide detailed description of *in situ* actions. The research sought data which could provide a telling narrative about unfolding events at PZ in response to key questions such as:

-Why did such a promising development institution fail?

- What made and produced the manner of its failure?

- What lessons might other MFIs draw from it?

To explore these and other issues, access to documents (made possible under freedom of information) from the Swedish embassy in Lusaka also shed important light on Pride Zambia and its dealings with the donors, while in situ interviews with key informants reveal further internal conflict and struggle. Given the complexity of this study, it was important that the methodology should reveal both the 'multiple realities' of the key events and also illuminate the uncertainty and anxiety surrounding them. This proved particularly difficult for some leading authority figures, PZ's board of directors and senior manager included, although it is often difficult to persuade managers and others closely bound up with failed organizations elsewhere to freely and openly participate in research exploring how such failure actually occurs (Barker & Patterson, 1996). Only after repeated assurance did the former CEO agree to be interviewed but even then there were such objections to audio-recording that the researcher was duly instructed not to take notes of discussions unless expressly told to do so. After persistent attempts to secure interviews, two Board members still declined, and duly ignored further email requests. SIDA differed in that it facilitated due access to correspondence and board meeting minutes in the period from 2006 to December 2008. Such different sources allowed triangulation of data to increase the reliability of the findings.

PZ at Founding Stage

Before failing in 2009, this was one of Zambia's largest donor funded MFIs. It was founded as Pride Africa in February 2000 following a project funding agreement between PRIDE Africa SIDA. At the time its main stated goal was to be the premier financial services provider to the personal and small micro medium enterprise (SMME) markets. Its Board was appointed in May 2001, under PRIDE Africa Zambia and duly contracted PRIDE Managements Services Ltd (PMSL) from Kenya to manage the venture. However, this arrangement proved unsatisfactory and costly and in 2003 a loss of US$560, 000 was reported (Memo, 2008). In 2004, the Board replaced PSML with a locally appointed CEO, tasked to implement a business restructuring plan to 'transform' the venture into a Shareholding Company and attain self-sustainability by 2006 and attract equity and/or loan capital. PRIDE Zambia's reported outreach peaked in 2004 with 5,037 active borrowing clients[5] (56 percent women) but client numbers had started to decline by December 2005 to 4,591 (see fig. 2.0) against a benchmark of 8,000 active clients. Documents indicated that PZ never achieved its target client numbers of 11,000 in 2006 and 12,000 in 2007 as set out in its Business Plan 2005-2007.

[5] These numbers refer to borrowers with loans outstanding

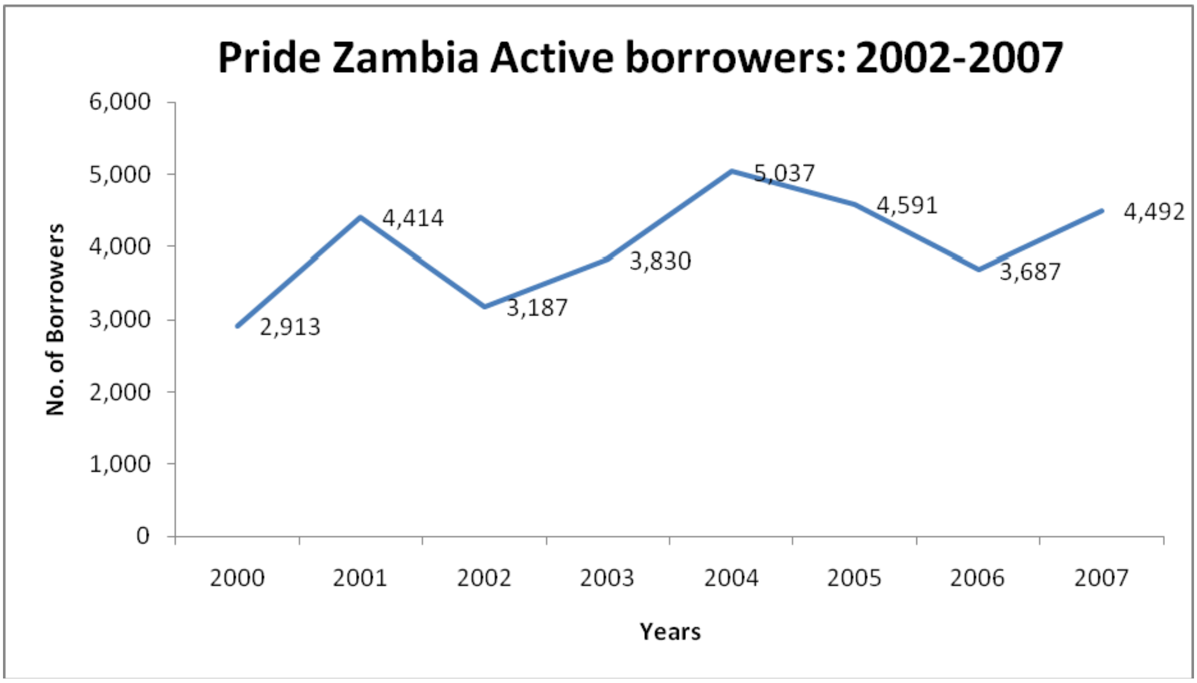

Fig 2.0

(Note: 2007 client numbers increased mainly due to an increase in salary guaranteed and individual loans in an effort to remain sustainable. They should be treated with caution as there were no independent records from AMIZ and MIX to confirm this).

Portfolio at risk was estimated at 7.38 percent as at June 30, 2004[6], but rose to 50.08% (MIX, 2007) by 2006. All but one branch incurred losses. Borrowers per loan officer dropped to 119 against the target of 350. After 2007, client numbers remained largely unidentifiable (Acting CEO, August, 2008).

In its 8 years of existence, PRIDE had introduced four loan products:1) *Group Loan Scheme*: targeted at low-income entrepreneurs with an initial loan threshold of K350, 000 (US$78); 2) the *Premium Loan* which targeted medium income entrepreneurs who worked in groups of five at an initial loan threshold of K3 million (US$667); 3) the while the *Salary Guaranteed Loan* which could extend credit to a maximum amount of K15 million (US$3334) to salaried employees in the formal sector; and 4) the *Individual/Business* loan aimed at entrepreneurs

[6] Reported figures on borrowing clients, PAR and loan portfolio from three different sources could not be reconciled. Figures reported in Musona's report (2004), AMIZ Annual Microfinance statistics (2004), the MIX Market website, and other material made available for this study contained many inconsistencies. For example, PAR, >30 days was reported to be 5.25% on MIX market and yet internal records indicated 7.38%. These figures should be taken with caution. The entire Zambian MFI sector lacks an authoritative and credible database.

with a guarantor and collateral for loan advances. PZ formally expected to register its first surplus in 2005 after implementing performance enhancing measures (2004 report to SIDA). However, its performance (Fig. 1.0), like that of other Zambian MFIs was considered unimpressive as a result of overzealous expansion, coupled with frequent top management changes, loose adherence to set lending procedures, relatively inexperienced frontline workers, and also deeper insinuations about possible large scale financial fraud by its credit officers and/or top management staff (Dixon, et., al. 2007).

Prior research had already uncovered highly stressed relationships between senior management and branch managers as well as growing private frustration amongst frontline loan officers, some of whom feared that further commercialization would undermine their jobs. The set lending methodology could be manipulated to meet targets and there were also reports of possible fraud (Siwale, 2006). Client groups were becoming ineffectual wherever loan officers were more preoccupied with stringent debt collection than enabling further group formation and development. Staff turnover increased among those who were most uncertain about the institution's future under the new CEO whom some privately considered to lack relevant grassroots experience. They also feared 'PZ's possible incorporation into mainstream banking on the basis that it still lacked the necessary systems and capabilities and would be found wanting as a result. Some clients however also claimed that PZ was on par with other MFIs in respect of its local reputation for being 'opportunistic and uncaring', a proverbial 'vulture' capitalizing others vulnerability and financial illiteracy for its own, largely self-serving ends.

PZ Post Founding: 'Transformation' 2006-2009

Anticipating what demands Zambia's new 2006 Act for non-bank financial institutions would place on PZ, in January 2006, SIDA requested a transformation Consultancy from Enterprise Solutions Global Consulting with the intention of planning how it would become a limited liability company. SIDA pledged 240,000SEK equivalent to USD 29560 for a plan[7] which would cover 2006-2009. Documents obtained from the Swedish Embassy revealed that the co-operating partners had also been concerned about how PZ intended to respond to low client numbers by opening more branches rather than expanding its existing branch network

[7] Bank of Zambia introduced a new legislation in 2006, which among other things required all non-bank financial institutions to transform into shareholding companies. PZ had to comply and convert itself into a company limited by shares rather than guarantee. This meant that new investors were required besides SIDA.

and staff. The partners also expressed concern about its rising portfolio at risk (>30 days PAR) which then stood at 50%, and wanted to know how much progress had been made to reduce PAR and improve debt recovery. Risk management and organizational improvement were SIDA's declared key priorities. Meanwhile, the PZ Board used the business plan 2006-2009 to request special support for employee retrenchment packages, renegotiate long term loan conditions, and secure additional operational funding. However, co-operating partners only agreed to a two years grace period on the loan, rejected the retrenchment proposals, and maintained that they would only consider new funding on condition that PAR 30 fell below 5% (Board meeting minutes, 06/11/06-accessed 4/8/10, SIDA).

While SIDA's contracted law firm prepared documents for converting it into a limited company by shares, PZ's problems then became increasingly public. In early 2007, the Embassy was informed that the CEO had accused certain staff with corruption, and the same staff later produced other allegations in a letter dated March 2, 2007 which counter-accused the CEO of 'destroying' the institution. The CEO had also approved a loan to the Board chairman on the understanding that it would be liquidated against allowances. This letter was sent to a private independent newspaper along with a copy to Zambia's State House in a manner that surprised both SIDA and the Board – and brought wider political factors into the equation.

The Zambian Drug Enforcement Commission (DEC) without delay sought to investigate the accused staff while the Board formed a special working group to deal with the allegations about the CEO. The CEO was duly suspended in a move which other staff deemed a 'cover up' for the Board's own negligence. Later the same month the CEO was dismissed as the investigators detected 'administrative irregularities', misuse of office and failure to follow established procedures. Otherwise DEC made so little progress that the case was dropped after 8 months and the three accused members of staff were discharged.

This did not prevent PZ's continued downward spiral. SIDA documents suggested that in 2007 the financial position deteriorated with a loss of US$550,000 compared to US$270,000 in 2006 so that PZ in effect was insolvent. A SIDA memo dated 18/9/2008 had claimed that the 2007 audit report showed that PZ's liabilities exceeded its balance sheet assets - clearly implying negative equity – obliging PZ to apply for a moratorium on the payment of interest and amortization. In early 2008, its application was approved, but loan disbursements were then suspended, while active client numbers thereafter remained unknown. In the midst of all this SIDA desperately sought other potential investors to inject new lease of life into PZ (acting CEO, Lusaka, June 2008) and also comply with Bank of Zambia's new regulations. SIDA maintained that the transformation and subsequent takeover of PZ represented a 'turnaround' opportunity as the quote below reveals:

> "A positive development of the company (after transformation) would mean that the original objectives are still met, and that PZ would continue to be an important player in Zambian microfinance. We are confident that this way forward is the correct one, as things are today. It is therefore SIDA's recommendation to the Board to support the transformation process by making possible the soon conversion, and furthermore the takeover of the company by the new investors".

Meanwhile, audited financial statements for 2006 were still not ready by January 2008. In April that year, SIDA wrote to the Board Chairman about the latest developments thus:

> "As I informed the Board at the last AGM, held on April 3 2008, SIDA has been assisting PZ in the search of investors for the company, in order to try and tackle a very difficult financial situation. During the last 6 months, there were several contacts with microfinance investors. Despite initial interest, they all preferred not to go further in the discussions as they became aware of the financial status of PZ".

The eventual takeover of PZ occurred in May 2008, with new owners later requesting SIDA to write off the loan if it was to continue. On 18 September 2008, a SIDA memo supported the proposal, but did not hide its disappointment with the position PZ had found itself in:

> "SIDA has supported PZ since its establishment in 1999, with grants (15.4 MSEK) and loan (8.8 MSEK). The idea behind the support was to make a show case; '*microfinance for the poor is viable in Zambia'*. After 9 years of operations, we can conclude that PRIDE Zambia has not been able to become financially viable".

The SIDA episode finally came to a close when PZ was sold to new investors for as little as US$1! So what made and produced this dramatic failure? To answer this question it is important to follow the different stakeholder narratives which have since emerged (Law, 2006), beginning with the following inside, outside, and donor led accounts of the key actions and events concerned.

Failure From The Insider: Informant Accounts

One key informant, who had first joined PZ as loan officer and then became a senior manager, before acting as CEO between 2007- 2008 – the transition period, gave a moving account of how events unfolded. Asked him what he thought he replied:

> "The CEO that took over in 2004 came from a corporate banking background with no experience in either retail banking or microfinance. His vision was to turn PZ into a bank but without much internal consultation. He was very formal in style, intimidating and insensitive to contributions from junior staff. To support his ambition, he quickly approved of new expensive rented premises for the head office to portray PZ's new image. He also made reshuffles and dismissed those he considered a 'threat'. New products got introduced as a way of broadening our financial base and ensuring sustainability. All this was initially exciting until he began interfering in the client assessment procedures with a view to favour those known to him by tribe, political affiliation or just as relations. As you would expect, big loans were being disbursed anyhow, making follow ups difficult-especially on those with the approval of the CEO. For some unknown reasons, the CEO struggled to trust anyone in PZ, and ended up creating 'spies' amongst staff. As a result unhappy employees (especially loan officers) went on a revenge path as the CEO applied a 'divide and rule' management style, creating tensions that blocked proper communication lines. So a battle ensued between some employees who wanted to 'protect' PZ and the CEO who most internal staff thought was fraudulent. To protect his interests, the CEO recruited an internal chief auditor from his former work place without formal interviews. This infuriated some of us who knew what was going on at a senior level and in my view this was the beginning of the end".

Asked about the Board's position he responded that:

> "The board was not fit for purpose and never used to read reports sent to them, making it easy for the CEO to manipulate the situation. They were heavily dependent on what the CEO thought. Board members, we thought, were more interested in allowances from the frequent meetings held than the viability of PZ. Poor accountability meant that little was known about the magnitude of the problem. Money for lending and operational purposes ran out and SIDA refused to pump in money and instead suggested that new investors take over. The ownership of the institution needed to change in order to comply with Bank of Zambia's 2006 Act. So SIDA funded the audit of the organisation in order to ascertain its financial position. The audit done by an independent consultant revealed the financial position as dire – PZ was insolvent! This infuriated SIDA as it became apparent that the Board had been incompetent. The audited books were so bad that investors with initial interests pulled out. The PAR reached record levels of 65% (as against stipulated levels of 5%). PZ was terminally distressed and technically insolvent. This poor performance and turn of events were obviously disappointing for

> the donors who over the years pumped in a lot of money to the tune of K14billion. Ironically, SIDA was not receiving all the reports and if they did, then it could be that unpleasant information was hidden, filtered or 'massaged' by the CEO".

Was the Board's inaction largely due to indifference and lack of vigilance or was it an intentionally calculated way of 'turning face' and thus evading and denying PZ's looming failure? Certain sources would suggest that, though Board members attended formal meetings they came largely unprepared, not having read those documents sent to them. How, then, did PZ's Board members measure up? Did they have the necessary qualifications and experience? These questions are difficult to answer because two Board members declined to be interviewed. However, these other sources here implied that, as well as Board instability, a basic 'lack of commitment' also prevailed.

Unfolding events as seen by those that actually did the grassroots work equally revealed deep rooted crumbling within PZ:

> Things on the ground were not as good as the figures suggested. Donors were at times kept in the dark or figures manipulated to please them by concealing our real problems such as the rising PAR. We needed their financial support because repayments were not as good and at times clients used their money to pay for those defaulting and in other cases loan insurance fund to clear arrears. The pace of commercialisation was being pursued hastily with limited internal consultation. Sustainability was a word no one wanted to hear as we associated it with threats from the top if we failed to meet set targets. As loan officers we felt very insecure with messages like 'donors want to pull out' and 'donors want clients in big numbers'. In addition the flow of communication between branch staff and senior management was very problematic- I mean the CEO was very rigid and not listening to our views even though we were the ones with 'ground' knowledge of PZ's performance out there. I could say that PZ was a divided institution from inside long before new investors came in. Most of us were very suspicious of the CEO and his vision for PZ. Also the system was very porous and those with accounting background would collude in stealing clients' money. The trouble is that took long to catch up with those involved in fraud and so most got away with it" (Former loan officer).

After buying PZ for just US$1, its new investors were expected to reorganize it, and make it more sustainable in compliance with the regulatory Act. However, interviews revealed something unexpected: these new investors did not have the capital to invest and could not borrow from banks due to their lack of credibility. It was alleged that they instead siphoned all the remaining money amid further mutual recriminations. This in effect created what Bedeian and Armenakis (1998) called *the cesspool syndrome* where competent people leave the organization. In this case, most senior employees left the 'sinking ship' as soon as the new ownership became clear.

> "Systems simply broke down, workers went without salaries-and as one would expect under those circumstances, they (especially loan officers) started 'helping' themselves to loan monies that clients paid back. Each branch would collect money for its own salaries and then contribute a certain percentage towards head office costs. Eventually, loan disbursement came to a halt as the new owners mismanaged whatever was collected. Some clients lost out on their savings in form of loan insurance fund as new owners transferred clients' money (that had previously been under a separate account) to the main operational account and 'chewed' it. In the end, poor hard working clients with fully paid up loans lost out. However, clients on salary guaranteed loans gained because they never paid deposit upfront before borrowing and the evolving mess meant that loan deductions through their employers could not be continued. Equally, employees never received their terminal benefits and had no one to drag to court. It was a very bitter ending for employees especially for those that had been with PZ for a longer time. With hindsight, I think the CEO had set in process a target-driven managerialist culture that opened the door to institutional chaos and eventual demise of Pride Zambia" (former senior manager, Lusaka, Aug, 2010).

Documents obtained from the Swedish Embassy (4/8/2010) indicated that the new owners desperately needed new injections of capital as a SIDA communication on December 18, 2008 revealed:

> "Thank you for your letter received by e-mail November 13. As we have earlier mentioned, the Swedish Embassy is currently ending all contributions to the financial sector, and is not in a position to enter into new commitments. However, would you need assistance in identifying potential institutional investors from Sweden, please do not hesitate to contact us"

The new owners had no face to lose in the absence of media and regulatory scrutiny. Many clients with group loans (mostly women and less educated) were so unaware that they continued with loan repayments, not realizing that loan officers would simply appropriate these dues instead. The then CEO claimed to be suspended and dismissed on the basis of an anonymous internal letter that was widely circulated outside. He further claimed that events took a different political turn when this letter accused him of supporting one of the main Zambian opposition parties and practicing tribalism. The letter had alleged that the CEO was corrupt and had divided and mismanaged the institution. His response was to blame the Board for his dismissal, claiming the required disciplinary process was ignored. He identified one dominant Board member who had reputedly 'hijacked' this process after having opposed his original appointment – a claim which was disputed. He maintained that his dismissal had created a 'management vacuum' and that problems escalated when branch staff collected money from clients only to pocket it themselves , in some cases because their own salaries were not being paid. He believed that PZ would not have collapsed as it did had it not been for 'political' interference from those Board members seeking to take over the institution. In an effort to apportion blame, he further claimed that his successors mismanaged the remaining portfolio and, while he expressed relief to have been cleared of allegations, he claimed to have left PZ with relatively little. Asked what he would have done differently, he admitted:

'I should have been more ethical in my dealings with the Board chairman-whose loan advance I approved against lending rules'.

Failure From The Outside: An Executive Account

Pride Zambia was affiliated to AMIZ and its Executive director could have offered further insights about its failure. However, it was only after repeated probing that put this 'down to mismanagement', especially to conflicts between its senior management, CEO and Board. Board members allegedly undermined the CEO by so colluding with certain subordinates that other middle management officers filled the resulting power vacuum thus:

> "Microfinance in Zambia has evolved overtime. However, what is seemingly disturbing is the aspect of failing to differentiate between issues of governance and management. There was a lot of 'political' interference from the Board and as a result those in management were failing to make independent decisions based on information from the ground. In addition, controls on lending and business ethics were basically ignored. For example we heard through the press that the CEO was recommending friends and relatives to borrow against laid down lending procedures, undermining loan officers and the head of credit, while holding them responsible for non-repayments. This created anger amongst middle management and some loan officers who then decided to take their frustrations to the press. By this time the damage was already done as the practice became widespread and junior staff started inviting their friends and relatives as well and malpractices became widespread. Liquidity crisis added to the already dire situation. PZ lost a lot of money as its salary guarantee loan scheme backfired. For instance, PZ extended huge salary based loans to Zambia's central bank junior staff but failed to collect back most of it as the system got manipulated.
>
> As things deteriorated, donors withheld funds and asked Board members to dissolve themselves as they were allegedly not performing and not in control of things. By the new Central Bank regulations, SIDA

could not have shares in PRIDE, so they then decided to open up to private investors to take over. Privately, some board members had interest in buying it and it is understood that some of them were ‘pulling some strings’ behind the scenes and unduly delaying the process. In my view, it is fraud on a large scale which pushed PZ to its knees. I also think that SIDA was in hurry to get rid of PZ because they had a reputation to protect. In addition new owners lacked experience and understanding of microfinance. They had a banking business background which did not sit well with the grassroots group lending methodology. Sadly, it was a case of embezzling from the poor, the very people PZ was meant to help out of poverty.” (AMIZ-Director, July 8, 2010)

Interviews with a senior officer from the non-bank financial institution’s department at Zambia’s central bank revealed that PZ was not actually registered even after its new owners were given two years to comply with the new regulation rules. The Bank of Zambia had little formal information about PZ and one official claimed that anything they did know came largely through SIDA and ‘the grapevine’. The new owners had intended to comply but never got around to it, leaving it free-*floating* at the time of collapse.

Failure from the Margins: the Donor’s Account

The Country Director at the Swedish Embassy claimed:

“As SIDA we wrote off the loan as a last attempt to save PZ. From our perspective, PZ had serious management problems, operated with an NGO mindset rather than a banking or profit driven spirit. However, with hindsight, we think that perhaps SIDA was too involved and yet we didn’t have an articulated microfinance policy to guide our relationship with PZ. SIDA was not there to directly manage the institution but expected PZ to report on how it used the monies loaned to them. The whole process lacked clear lines of accountability” (interview, 4/8/10, Lusaka).

Another key player at SIDA with direct experience of its dealings with PZ reflected that:

“I think we learned a lot from PZ case. The way in which SIDA supported the creation and growth of PZ did in fact in many ways contradict our own microfinance policy, as well as general “best practice”. Still, SIDA tried to get something going to “make a positive impact” in microfinance in Zambia and other countries. But, to make the long story short, I think we underrated the difficulties in mainly the following: having a local Board of Directors without any own financial interests in the business and not financial experts themselves, the general levels of corruption in Zambia and “creating” an organisation that from our point of view was independent, but from many PZ staff/Board was “SIDA property”.

He further added:

“One main problem was the setup, and the view from PZ that SIDA would always come to the rescue. In real terms, it was an independent organization, and the only SIDA connection by 2006 was a loan. So when internal problems started to come to our knowledge, we had contacts with the then CEO, and later the Board. I am not sure why the internal situation collapsed; some have mentioned tribal struggles (the CEO was Lozi, most middle management were Bemba), or some of the Board members

> having big influence, or that the CEO was finding corrupt behaviour among the staff. Financial numbers were getting redder, and despite meetings with the Board (also some times with other sponsors) very little action was taken to halt the fall. I got the impression that the Board did not really realise their responsibility for PZ. It was obvious the Board did not control events".

Other documents revealed that by end of 2007 SIDA had lost confidence in the Board's capabilities, and as its financial situation deteriorated donors asked the Board members to dissolve following several years of continued losses.

When asked what SIDA could have done differently, he replied:

> "I think that the massive support from SIDA helped a lot in creating an organisation that was not really efficient and responsible. Easy money can be detrimental in these cases. Good MFIs often grow step by step, not too much donor money, and with strict internal controls. In addition, there were too many SIDA programme officers involved, and not all with microfinance expertise. About as many as seven (7) different programme officers were involved in decisions regarding PZ during the last seven years. This probably did contribute to some lack of consistency in the advice given and complicated relations with PZ. Needless to say, SIDA would not give support to a similar setup today".

Discussion

Power (2007, p 10) has observed that 'empirical case analyses suggest that rigidities of core beliefs, managerial distractions, disregard for the views of outsiders, lack of regulatory compliance and difficulties in assembling critical information tend to be systemic factors contributing to organisational failure'. These different stakeholder accounts would suggest that relevant information might have been available but was not acted upon at the appropriate level of seniority right up to the Board. Self-generated failure materializes through a series of different events and misguided and/or dysfunctional actions (Mellahi, 2005; du Plessis, 2008) and in this case early warning signals were either disregarded or dismissed altogether. In addition the donor SIDA's own frequent changes of officers dealing with PZ (7 different officers in 8 years) was another contributory factor since most such officers were later admitted to have lacked the necessary understanding of grassroots microfinance in practice.

While PZ management lacked transparency, SIDA also underestimated its ownership problems. The question must be asked: who actually owned PZ? Without shareholders SIDA became the de *facto* owner. Mersland and Strom (2009) have emphasized how uncertain ownership of not-for-profit MFIs can potentially inhibit their performance. PZ had started as a non-profit, donor-funded project, focused on the provision of credit and did not have a *local ownership* identity and many assumed that 'it belonged to donors' with no other financial interests at stake. It was thereby taken for granted that SIDA would control how *their* funds were used (Hartarska, 2005) even if SIDA trusted that others would take prime responsibility. Such blurred accountability created space to embezzle donor (free) money and mismanage clients' funds. In short, ambiguity about who constitutes the 'principal' in not-for-profit MFIs duly blurs managerial 'agent' accountability further down the line. SIDA's unquestioning support may also have increased outreach (by local standards) without achieving the sustainability necessary to overcome early donor dependency. SIDA was latterly desperate to exit from a 'failed showcase' situation originally intended to demonstrate that '*microfinance for the poor is viable in Zambia*'. Even when it hurriedly supported a first takeover bid from a small number of 'reputable' Zambian businesspersons it also failed to invite other outside interest.

The self-generated roots of PZ's failure encompassed: overexpansion, inadequate skills/working practices, organizational instability, mismanagement and fraud and malfeasance. As the number of branches overstretched PZ's management capacity, this translated into lenient credit policies, inefficient/distorted information systems, loose internal control and, ultimately, substandard governance. SIDA itself pinpointed Zambia's poor repayment culture as well as those who mismanaged PZ's growth in particular. Other MFIs have also struggled to identify Board members with appropriate backgrounds who are both willing and able to monitor management effectively (Labie, 2001). Data about board members' background was not available here although the chairman was a local University Business School academic. Another was a Government permanent secretary and the other three with NGO backgrounds. According to Mersland and Strom (2009) MFIs primary tasks are to reach more clients in the poorer strata of the population and then achieve financial sustainability and here PZ failed to accomplish both. It never adopted Steinwand's (2000) recommendation about internal auditing and allowed its CEO to appoint an auditor who only reported directly to him alone. The findings do however question Mersland and Strom's (2009) assertion that local Boards improve MFI performance –in this case the PZ board was local but also ineffective and ultimately not fit for purpose. Finally it is no surprise that this saga took a political turn as it also has in India and Bangladesh (Financial Times, 3/3/2011) since leaders and supporters of Zambian opposition parties often claim to be victimised as soon as they are perceived to be a threat to official power. In the PZ case, political and tribal factors might have played a significant role in explaining internal power struggles.

Conclusions and implications

The case study has shown that MFIs in Zambia and elsewhere, that are donor driven and 'top-down', can be so precariously founded that they come under pressure to reorganize or fail. This high dependence on donor funds that can be found in many sectors in SSA is particularly damaging to microfinance, where financial sustainability is of fundamental importance. The implication of this finding is that successful MFIs need not have a perpetual external push as donors' money in most cases tends to give a 'false start' that was never there and ultimately leads to abuse of resources or failure. Microfinance institutions could fail when they are not conceived or designed to be sustainable. The findings of this study have implications for how international donors engage with the local constituency in various development initiatives aimed at reducing poverty in developing countries. Local ownership matters as it creates a sense of 'belonging to' necessary for promoting cohesion within the organization. It can also significantly change how MFIs' resources are managed for their sustainability and clients' outreach. In the case of PZ it was not clear as to who owned the firm's resources.

The most important implication of this study is that while PZ case is specific to Zambia, the conditions for 'successful' MFIs can be generalised to other donor-led MFIs elsewhere. A competent and motivated board together with institutional capacity are critical to advancing microfinance. Consistent with other studies on institutional capacity, MFIs that lack both human and systems capacity stand in danger of jeopardizing further growth. The implication here is that sufficient flows of donor funds are not a guarantee for success. The transparency in organization management can be regarded as much more important as demonstrated in PZ's case. Pride Zambia's downfall highlights in some sense persistent weaknesses in corporate governance, not just there but at other MFIs in developing countries where microfinance is still emerging. MFIs need good governance that ensures transparency of processes and clear lines of accountability amongst stakeholders in relation to MFI's mission. For this to happen, MFIs boards should be in positions to challenge and act as a check on executives, and have the relevant background experience. In addition, MFIs need to invest in up to date management information systems that are well supported by established business ethics. This work therefore makes a contribution to understanding the reasons for failure and towards a case for a local context regulatory policy framework able to protect MFI's client deposits and further sustainable growth. The analysis made here also has considerable implications for 'best practice' within the microfinance industry undergoing commercialization. Replication and adaptation of policy models are never easy: historical, economic, cultural and political context can be crucial.

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