Local funds, and their potential to allow donor agencies to support community development and poverty reduction in urban areas: Workshop report

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SUMMARY: This paper describes the growing number of local funds or local institutions through which international agencies or national governments channel resources to support community initiatives. It discusses the advantages that these can have over more conventional projects in reducing urban poverty (including their flexibility, fast response time, demand-driven nature and local accountability). It discusses how they differ from social funds, and points to their strategic value in changing official perceptions of “the poor”, in strengthening the capacity of urban poor organizations and in enhancing partnerships between community organizations and municipal governments. The paper ends with a discussion of the challenges that these local funds pose, both for the local institutions who manage them and for donors who fund them.

I. INTRODUCTION

ONE DIFFICULTY FACING all international agencies is how to support the “civil society” side of good governance; or, more specifically, community-based initiatives, especially those that require little money and are distant from these agencies’ central offices. Most international agencies recognize the need to support community-based initiatives, especially where local government structures are weak, ineffective or corrupt. Many recognize how cost-effective community-based initiatives can be in meeting basic needs and in reducing poverty. After all, in most cities in low- and middle-income nations, a significant proportion of all homes and neighbourhoods, and the infrastructure and services they contain, are organized, built and managed by low-income groups and their community organizations. But how can international donors develop funding mechanisms to support this? It implies supporting far more projects with far lower average costs. Ask any staff member from an official bilateral agency or the World Bank to manage fifty times the number of projects with an average cost of one-fiftieth of their current project portfolio, and they would resign. Any international agency would face an impossible administrative burden and far higher staff costs if its central offices had to support a multiplicity of (often) low-cost, diverse, distant initiatives, especially if each proposal had to be reviewed on the ground and monitored and evaluated to ensure compliance with its initial objectives.

Setting up funds in each city in low- and middle-income nations, or channelling funds through some local institution, can be an attractive way
of solving this problem. It shifts the decision-making process and most of the administrative burden and transaction costs to the place where the proposals originate. From there, it is much easier, quicker and cheaper to check on proposals and monitor their implementation, using a network of people with local knowledge in the location. It can minimize the need for expensive expatriate staff; all international agencies who have expanded their offices in low- or middle-income nations with international staff face difficulties with staff costs. But it is a big step for any international donor to entrust the funding it manages (and for which it has to be accountable) to local institutions or local funds.

II. LOCAL FUNDS

THERE ARE MANY examples from which international donors can learn about local funds or local institutions which support community initiatives – and to which community organizations can apply for funding or other forms of support. These include local funds to support community and municipal initiatives in Zambia and Uganda, funded by the UK Department for International Development; a range of local institutions in Central America that manage funding from the Swedish International Development Cooperation Agency (Sida); the ten-year experience of the Thai government's Urban Community Development Office; and the 30-year experience of the Carvajal Foundation in Cali (Colombia). These all recognize the need to make funding available through institutions located in each city, that can respond rapidly, can fund community organizations directly and can fund a large and diverse range of initiatives, including those requiring very small grants or credits. Most of these local funds have sought to strengthen community-local government partnerships. Some have also sought to set new standards of transparency and accountability to city populations. There are also community development funds in operation in Pakistan, South Africa, Cambodia, Zimbabwe, Namibia, the Philippines and Lao PDR.(2) Many of these have concentrated on offering subsidized and non-subsidized loans to support community activities; others have preferred to work through small grant finance, stressing counterpart contributions in order to ensure high levels of local ownership. Some have combined both of these.

An international workshop in February/March 2002 exposed international donors to a range of examples of local funds.(3) At this workshop, case studies showed how these could draw funding from a range of sources, including international donors, national governments and local governments. There were also case studies of local foundations and of local institutions through which international donor funding was channelled. Most of the case study presenters were people who had been involved in setting up and running these local funds (there is a list of the case studies at the end of this report, with details of how these can be obtained). What became clear from the different presentations was the very considerable range and diversity of experiences from which donor agencies can draw.

The key question for the workshop was what role can such local funds or local institutions have in more effective poverty reduction in urban areas? Urban areas were the focus, in part because of the recognition that the scale and depth of urban poverty has been underestimated, in part because of the proven capacity of community-based organization and
action to reduce urban poverty, in part because urban contexts require different types and mixes of initiatives from rural areas.

III. THE POTENTIAL ADVANTAGES OF LOCAL FUNDS

LOCAL FUNDS SHOULD have the following advantages over conventional processes through which donor agencies fund projects:

Reduce the time and the cost for community organizations accessing resources. When community-based groups or local NGOs apply for funding to international agencies in Europe or North America, it often takes many months before a decision is reached. With a locally-based fund, the time between the request and the decision can be reduced to a small fraction of this i.e. one or two weeks for most requests (with provision for even more rapid responses in the case of emergencies). Locally-based institutions can also make application procedures easier and less costly for community organizations – and even allow them to apply in their own language.

Be really demand-driven and create effective systems of absorption for external funds. Donor agencies know that their funding allocations should be more demand driven, but it is difficult for them to match their funding (and funding structures) to the huge diversity of demands in the countries they support. Local funds can be far more demand driven by having funds that urban poor groups can draw on as and when needed – so funds are “pulled” through the system by people’s needs, not “pushed” through by external development agendas.

Support constant pro-poor engagement with local processes that more distant agencies cannot achieve. Local funds allow responses to particular local circumstances that distant agencies cannot achieve – including fast responses to changing circumstances (and disasters). They can support learning and adaptation rooted in local contexts and ensure support for the kinds of long-term processes (and local institutional changes) that make poverty reduction more effective (especially the development of more effective partnerships between community organizations and municipal authorities). They can also more easily support community-directed precedents that demonstrate to local politicians and staff of governments and international agencies more effective ways of reducing poverty. Diverse groups who do not normally receive funds can receive support – including youth groups and senior citizens – and, if structured carefully, they can provide a more systematic support for the needs and priorities of women. Local funds can also make special provision to support the less-organized groups, the poorest groups and the groups that face discrimination to develop their own proposals. The location of the decision-making within the locality also creates a different dynamic in communities. Local groups recognize that decisions can be influenced, and become active in developing their own projects and activities. They can also do so, drawing on the advice and support of staff from the local fund. The process is very different from a long wait for a decision from a distant group over which they have no influence – which can, of itself, be disempowering.

Be able to respond to a multiplicity of needs (including some that require very little funding), be more flexible and support many different entry points for reducing poverty. Most donor agencies cannot manage many requests for small amounts of funding because of the high cost of processing and managing...
each of them. It is also difficult to assess the relevance of each proposal. All donor agencies are under pressure to keep down staff costs. Yet many good community initiatives require small amounts, at least initially as low-income groups come together to develop a new initiative; or small amounts are needed to complement the support that has been negotiated from some local government agency or other local body. Because they are local, funds and their staff and decision makers are more able to be flexible – but with flexibility enabling more relevance rather than corruption.

Avoid the tendency of donor agencies to swamp or “overfund” promising local initiatives. One critical lesson from many successful development interventions is that too much funding leads to initiatives that cannot be sustained and often destroys or damages the initiatives. Yet many donor agencies overfund initiatives because they have difficulty in spending their funds and prefer to spend in large chunks. Initiatives that seek to keep down unit costs and try, wherever possible, to fund themselves through what low-income households are willing and able to pay have much greater possibilities of being sustained and of growing in scale. A focus on keeping down unit costs and making maximum use of low-income groups’ capacity to save and to pay is also one key reason why many urban poor federations have large-scale programmes, despite limited support from donor agencies.

Many local funds also use loans, often combined with support for community-based savings groups. Loans can help to ensure high levels of local ownership; people will not invest in processes that do not make sense to them if they know that they will have to repay even a part of the costs. High levels of local engagement reduce the chances of corruption if there is an implementing agency that is not the community. Loans also help to increase efficiency and sustainability by encouraging one community to repay some or all of the funds, enabling others to benefit. Loan management increases communities’ management skills, not only in areas of immediate financial management but also by their engagement with other financially-minded groups. Many of the presentations at the workshop also emphasized how the use of savings can add a further dimension. Many local funds support community-based savings schemes, and savings activities in a community can change the way in which participation occurs. Savings brings a community together to consider the scarcity of resources and the scale of need in a new way. Communities start to build up new processes to manage their scarce collective resources. Community leaders are held to account in ways they were not before. And communities expect to be treated as equals when their own funds form a part of the investment capital.

Developing downward accountability as well as upward accountability. The application procedures and decision-making processes in local funds can be kept transparent, so that information is widely available within the city regarding the existence of the fund and the application procedures. In addition, information can be made available regarding the processes through which decisions are made, and who applies for funds, who receives funds and why. The physical and institutional distance between donor agencies’ decision-making processes and the low-income groups that are meant to be the main beneficiaries of their funding make downward accountability very difficult. Channelling donor funding through local funds or local institutions allows far more accountability downwards (to low-income citizens and their community organizations) as well as upwards (to the agencies that fund it).

Leveraging additional funds and support from local government agencies or local offices of agencies from higher levels of government or national agencies, and mobilizing urban poor households' own resources. Many local funds generate two to three times as much counterpart funding from local sources. However, where local funds require community organizations to provide counterpart funding, it is recognized that this can take the form of contributions in kind or through labour contributed to the initiative rather than capital up front.

Building poorer groups’ asset bases. Different case studies pointed to the large multiplier effects of the projects supported by local funds, as the value of the assets created by the support was many times the value of the funding actually provided. Revolving funds also allow communities to use limited funds many times over, with each revolution increasing asset bases.

Providing a alternative channel to support poverty reduction outside of government. There is a growing tendency among many donor agencies to concentrate their funding on governments that they judge to be “good”. But this penalizes many of the poorest people in the world, who suffer not only from inadequate income and asset bases but also from incompetent or repressive governments. Local funds can allow donor agencies to channel funds directly to community-based organizations in countries where they do not want to support governments.

Thus, local funds provide a means of acting on what has been learnt from effective poverty reduction initiatives, including the need to work with and strengthen representative organizations of the urban poor, to support more productive relationships between urban poor groups and local government agencies, and to support the many different forms of interventions that help reduce poverty.

IV. MORE STRATEGIC ROLES FOR COMMUNITY FUNDS

THE PROCESS OF setting up and supporting local funds can be used strategically to change the approaches of local governments and national agencies to poverty reduction. For instance, local funds can:

Create opportunities for linking community organizations so that they can learn from each other and support each other. Experience with local funds shows the importance of feedback from the initiatives it supports for both internal and external learning (including, crucially, learning from initiatives that did not work or achieved less than expected). Local funds can serve as a point of shared learning within a city, between the different community initiatives therein, and as a point of coordination for the different international and local NGOs that work in that city. They can also support community-to-community exchanges between cities, and such exchanges have proved very effective in building capacity and in supporting learning at community level.

Strengthen representative structures and federations of the urban poor and their capacity to negotiate with local authorities (and change the way that they operate). This includes supporting the inclusive, savings and credit schemes of urban poor groups, which provide the foundations for the growing influence and effectiveness of federations of the urban poor in many nations.

Change official perceptions of “the poor” to one that recognizes their compe-
tences and capacities and, as a result, also change institutional relationships between “the poor” and government agencies. This includes changing existing institutions so that they can more effectively support poverty reduction – for instance, as in the experience of PRODEL in Nicaragua in “downscaling” the work of a bank so that its many branches could serve the credit needs of lower-income households.\(^{14}\)

**Strengthen municipal government.** Most of the case studies of local funds showed that there were explicit mechanisms to strengthen partnerships between community organizations and local government agencies. Some also provided support to local government initiatives, as well as community-based initiatives. Some local funds were municipal government initiatives.\(^{15}\)

**V. COMMONLY EXPRESSED CONCERNS**

**WILL LOCAL FUNDS** to support community initiatives bypass local governments and, in some sense, absolve them of their responsibilities? Create parallel structures which mean duplication and poor coordination? As noted above, the experience with local funds presented at the workshop showed how local funds have played key roles in strengthening the relationship between community organizations and local governments. This is often through funding precedent-setting initiatives whose validity was recognized by, and then supported by, local governments.

**Without donors controlling the allocation of funding, will local funds spend donor funding inappropriately?** Any local fund will come under strong local pressure from politicians, government employees and other influential people or institutions to fund initiatives that bring little benefit to urban poor groups. But this risk can be minimized through paying careful attention to the fund’s structure and functioning. A stress on transparency and accountability upwards and downwards can limit such risks. One important lesson from the experience with some funds is that mistakes or experiences with projects that were less successful than anticipated are not hidden but shared and discussed, and thus used as opportunities for learning.

**Will it be difficult for international agency staff not to be in a position to make the decisions about what receives funding?** Some background papers pointed to resistance within donor agencies to passing responsibility for local funding decisions to local bodies.\(^{16}\) Discussions at the workshop also gave examples of donor staff responsible for particular country programmes being reluctant to support local funds – in part because they did not fit into the country programming process. Many of the donor-funded local funds discussed at the workshop had to be funded outside that donor’s conventional country programmes.

**Will international donors see local funds as easy ways of spending their funds and so set them up too quickly, demanding that they spend money before they have in place the structures and relationships to allow them to spend funding well?** Local funds are about supporting more effective change processes to address urban poverty, not about convenient ways in which donors can spend funding.

**Will international donors think that they are already supporting local funds through social funds?** Although there are some similarities between the local funds described at the workshop and social funds – and they have comparable objectives in terms of being able to respond quickly to local demands

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15. The presentation by Yves Cabannes highlighted the number of municipal authorities in Latin America that have set up funds to support community initiatives.

16. See, for instance, Satterthwaite, David (2002), Local Funds; Some Notes on What has been Learnt over the Last Fifteen Years, one of the background papers for the workshop.
and reach low-income groups – the local funds are more rooted in particular localities, closer to grassroots groups and more flexible in what they can support – with the overall objective of supporting a constant pro-poor process in the locality in which they are based. They are likely to support a more diverse range of initiatives and groups, including many initiatives that require small amounts of funding. They also strive to achieve greater levels of accountability and transparency to community organizations within the locality than social funds. Most local funds are also not within government agencies, unlike most social funds. And crucially, most local funds are not mechanisms for immediate poverty relief but, rather, mechanisms for changing political relationships by enabling low-income groups and their community organizations to address their needs.

VI. NEW INTERPRETATIONS OF SUSTAINABILITY

INEVITABLY, ONE OF the key issues raised in the workshop was the sustainability of local funds. Two themes were stressed. The first is that the key point about sustainability for development is sustaining the processes by which poverty is reduced – and this can draw not only on the resources that poor households have but also on market instruments, state support, local charity or funding from external donors. One key role of local funds is precisely sustaining the process through which poverty is reduced and bringing in support from all these sources for this process. The advantages of interventions that achieve full cost recovery are obvious, when and where they do deliver for the urban poor (or sections of them), since they require no external funding and can more easily “go to scale” – but most “market” interventions fail to reach the poorest and many remain sustainable only if economic conditions are stable.

The second theme that was stressed was the need to distinguish between project sustainability, programme sustainability and institutional sustainability in seeking to expand and “sustain” local funds.

VII. CHALLENGES FACING LOCAL FUNDS

LOCAL FUNDS NEED to learn from each other but also to recognize the need to have their structure and procedures rooted in local contexts. Local funds have common goals and are based on many shared principles, but they need to be shaped according to what works best in each location. Strong, representative community-driven processes are among the best influences for making local funds respond to local circumstances.

Local funds obviously work best where there are representative and inclusive community-based organizations formed by urban poor groups and local governments that are sympathetic and capable of being supportive. But these conditions do not exist in most low-income and many middle-income nations. This does not mean that local funds cannot work, but it does imply a need for caution, for care in setting up appropriate institutional arrangements, including those that support inclusive community-based organizations – such as the savings and credit groups formed largely by women that are such a key underpinning for many urban poor federations. Local funds should not be pressed to spend donor funding before the institutional arrangements are in place. One participant with long experience in supporting local funds and local institutions

17. See the paper by Diana Mitlin in this issue on “Sustaining markets or sustaining poverty reduction?”, which was written in response to the workshop discussions.
in Central America commented that if local funds are developing fast, they are probably not working with the poorest groups.\(^{18}\)

Local funds may increase considerably the staff time needed per unit of donor funding spent. This is especially so if the funds seek to make all available funding go as far as possible and to leverage support and buy-in from local government and other government agencies. It can also be time-consuming for staff if the fund makes special provision to support the less-organized, articulate and powerful groups in developing and implementing proposals, and to be available to urban poor groups. For instance, something as basic as helping a women’s group get a bank account can be very time-consuming.\(^ {19}\)

Other challenges facing those who manage local funds that were raised in the discussions included:

- the difficulties in managing expectations and maintaining trust, especially for pilot schemes where funding is only available for a short period;
- setting appropriate conditions for obtaining matching resources from community groups without discouraging the groups with the least resources;
- developing the capacity to monitor progress and measure outcomes;
- avoiding the fund becoming a substitute for what local governments could or should be doing;
- learning how best to connect the fund to supporting inclusive community processes and skill development (getting the right balance between supporting community groups taking over many key tasks but not dumping all the transaction costs on them).

There is also a need for all local funds to continually ask such key questions as:

- whose institutional capacity, political clout and knowledge base is the local fund strengthening?; and
- what implications do local funds have for further access by urban poor groups to local capital and other resources?

VIII. CONCLUSIONS

THE STAFF FROM the international donors that attended this workshop agreed that they, individually and collectively, should explore ways of setting up and supporting local funds. They recognized that supporting local funds requires a recognition that “the poor” are and should be key actors in any poverty reduction programme, and a recognition of their competencies, capacities and rights to influence priorities and manage processes. It also requires a recognition that poverty will be reduced only if it includes strengthening the asset bases of low-income groups and increasing their influence. These are perceptions that are still far from being universal among governments and international agencies. Yet the effectiveness of local funds (and of most other measures to reduce urban poverty) depend on this change in perception.

As a final rallying call at the end of the workshop, it was noted that low-income communities are getting ready, are organizing (federations of the urban poor are growing and developing in many nations) and innovating. Are governments and international donors ready to develop the institutional means to support them?

18. This comment was made by Alfredo Stein, who has worked with Sida in setting up and supporting local funds and local institutions in Costa Rica, Nicaragua, El Salvador and Honduras.

19. Liseli Bull-Kamanga described the time-consuming process needed to do this in a project supported by the C3 Fund in Zambia.
THE CASE STUDIES AND OTHER PAPERS PRESENTED AT THE WORKSHOP

The Asian Coalition for Housing Rights produced a special 32-page issue of its newsletter *Housing by People in Asia* on “community funds”. This included coverage of local funds and community funds not only in Asia but also in Zimbabwe, Namibia, and South Africa. The publication also drew out lessons that have been learnt from these experiences and is available from ACHR, 73 Soi Sonthiwattana 4, Ladprao 110, Bangkok 10310, Thailand; e-mail: achr@loxinfo.co.th; web site: www.achr.net

For Latin America and the Caribbean

*Experience with Local Funds for Municipalities and Communities in Central America* – Alfredo Stein. This concentrated on experiences of local funds supported by the Swedish International Development Cooperation Agency (SIDA) in Costa Rica (FUPROVI), Nicaragua (PRODEL), El Salvador (FUSAI) and Honduras (PRIMHUR). This was supported by Stein, Alfredo (2001), *Participation and Sustainability in Social Projects: The Experience of the Local Development Programme (PRODEL) in Nicaragua*, IIED Working Paper 3 on Poverty Reduction in Urban Areas; available from: www.Earthprint.com or downloadable from www.iied.org/rural_urban/downloads.html

*The Urban Trust Fund in Kingston, Jamaica* – Morin Seymour


*Municipal and NGO Funds in Latin America; An Overview* – Yves Cabannes

Africa

*Introduction to the DFID-supported C3 Funds in Uganda and Zambia* – Jo Beall


*The C3 Fund in Lusaka and Ndola* – Liseli Bull-Kamanga and Nick Hall. This was supported by: Bull-Kamanga, Liseli and Nick Hall (2002), *The City-Community Challenge Fund (C3) “Zambia; A Case Study”.*

*Local Funds for Civil Society; the Value Added by the uTshani Fund in South Africa* – Diana Mitlin. This was supported by Baumann, Ted and Diana Mitlin (2002), “The South African Homeless Peoples’ Federation: Investing in the Poor”.

Asia

*The Experience of the Urban Community Development Office/Community Organization Development Institute in Thailand and Other Experiences in Asia* – Somsook Boonyabancha. This was backed up with the special issue of the Asian Coalition for Housing Rights’ newsletter on local funds.

Participants also received Boonyabancha, Somsook (1999), “The Urban Community Environmental Activities Project, Thailand”, *Environment&


Two other written papers were also made available, but not presented:
Local Funds; Some Notes on What has been Learnt over the Last Fifteen Years – David Satterthwaite

Local Initiative Facility for Urban Environment; Global Evaluation Results and Recommendations – UNDP

Unless other details are given, most of these papers can be obtained electronically by contacting IIED’s Human Settlements Programme at humans@iied.org