More responsibility and more impact: lessons learned and new principles in microfinance Investment

RTB 1 // Microfinance

Moderator

Xavier Reille
Microfinance Industry Team Leader, CGAP

Speakers

Femke Bos
Fund Manager, Triodos Investment Management

Claude Falgon
Board Member, Advans

Stefan Fischer
Investment Manager, Blue Orchard Investments

Guillermo Salcedo
Deputy Director, Department Loans and Investments, Oikocredit

Executive Summary

Microfinance seems to be obvious: volume multiplied by 4 in 5 years, $8 billion, but at the same time it is in "crisis" according to the media. What impacts can we expect?

In the first part we will ask our panel for their opinion on the microfinance issues, and whether or not the media is exaggerating.

Secondly, which opportunities they see for delivering social value.Microfinance is more and more integrated in the world economy. If after the independence of developed countries most of the initiatives were public, microfinance would now be part of the development system, that is to say private, but with a social commitment. Recently some non responsible behaviour has occurred. Reputation and risk is very important as any harm to microfinance will affect the whole industry. Guidelines to overcome the issues are: better MFI governance, more transparency, implementing local regulation, Credit Bureau, client protection, increased social performance measurements, diversification towards new tailor- made products (Insurance, deposits, savings, mobile banking etc.), and equity in some partners (cooperatives, small businesses, etc.)

Synthesis

According to **Advans**, Microfinance is an important element of the overall development strategy as viewed by the donors and development financial institutions. If after gaining independence most of the initiatives were governmental, microfinance is now part of the development system, in other words private, but with a social commitment. Recently some non responsible behaviour has occurred:

- Some MFIs have experienced extensive growth over the past several years; the number of branches has increased as the market is deemed to be infinite.
- If an MFI increases its size , it is more respected and attracts more money.
- Each country which faced a crisis at some point in time was considered very "successful" before the crisis. Examples include Benin in the 90s, Bosnia and Morocco more recently and India at the moment.
- Managerial incentives: incentive to grow, loss of control, less training of local agents.
- Governance issues: some boards do not exercise the appropriate level of management supervision ; governance requires skills, s money and time.
- Shareholders responsibility: some have too short investment prospects (4/5 years) when microfinance needs time and investors with long term commitment.
- Some institutions now have overly aggressive marketing practices, unfit for credit activity: they target good clients of competitors and offer them twice the borrowed amount from the competitor, without any rigorous analysis of client's ability to repay, but by guaranteeing several times the value of the loan (land or house title). This leads, or will lead, to over indebtedness and a systemic crisis as in countries mentioned previously.

For **Blue Orchard, Credit Risk**, Reputation, Political interference and Governance are the 4 main issues.

- Credit risk is important for any bank, when a customer cannot pay back interests and principal it is not good for the client, the growth of the country, the MFI nor the microfinance sector. Excessive debt in not specific to microfinance, the last financial crisis was mainly a debt crisis.
- A private company needs the creation of credit bureau and lack of transparency in order to collect information on clients (history, incomes, debts etc.), to make scoring available to everybody, to monitor the activities of the competition and to educate clients.
- Microfinance is not just about access to finance but also about improving the quality of life.
- Redesigning rather than borrowing financial systems from the North which are tailored to the needs of the people is essential. For example, Mobile Banking: phones are more easily accessible than branches in some areas, particularly those areas with no public transport.

For **Triodos Investment Management**, the issues are:

- Consolidating, reducing the activity, and diversifying the products in some countries when feasible. Occasionally, when insurance exists, the Credit Bureau get ignored by MFIs!
- To limit over-indebtedness, a document entitled "The Principles for Client Protection" has been signed with 40 other organizations.
- To look at the voting rights in the IMFI's,
- To take minority equity in some case
- On measurements: scoring the MFI's. What can be done, especially with the bad ones?
- Microfinance losing its virtue causing a decrease in interest from large investors. Some investors might leave entirely as they choose to invest in long-term projects (I.e. Pension plans)

For **Oikocredit** (GS), given its broad investor base (43,000 investors), reputation risk is perhaps the most important aspect of all, as any harm to microfinance will affect us, discouraging interest of investors.

- Oikocredit for several years has been measuring and monitoring the social performance of its project partners
- We were one of the first MIVs to sign the "Client Protection Principle" and have progressively embedded it into our financing criteria and contracts with the MFI's
- Attention to over-indebtedness of clients and other social criteria, along with

financial criteria are included in the selection of partners.

- The quality of investment is higher and the social impact is better.
- There is more focus given to empowerment and more attention to the poor.

In the second part we will investigate the opportunities which can deliver social value.

One of the strategic targets for Oikocredit is to develop direct investments in non financial sectors in accordance with present activities of microfinance. In agriculture we have been leaders in 10 countries to learn direct finance. How can cooperatives have a direct impact on the family? Priority is set on environmentally friendly, energy saving and fair trade projects. We will be more present in Africa.

Triodos Investment Management is diversifying its activities of Insurance and Small Business with job creation as Energy saving, Biomass, Solar systems, Organic and Fair Trade.

Blue Orchard with their Bamboo affiliate is developing a business model that works outside financial services like healthcare does in India, by generating power from rice dust and agriculture waste.

Advans was created in 2005 with 6 development financial institutions (DFIs). Their objective is to establish a network of microfinance banks based on the same model where Advans is the main shareholder. Advans aims at being a leader and at establishing new standards in countries where it invests. From the beginning, Advans institutions have provided credit, collected deposits and offered simple payment services targeting micro-enterprises. After a year, more SMES' are served and more payment services are offered (such as checks, cards and mobile banking) Advans institutions started in cities and gradually moved into rural areas after they broke even.

Rapporteur officiel:

Marc-Henri Stroh, Oikocredit

Questions/ Answers :

- Social performance measurement is easier with large MFI's due to greater resources (mainly in the number of staff).
- Financial services have to be provided in a sustainable way which is where several public projects have failed in the past. There is a need for regulation, especially when moving to deposits. While some organisations might lose the initial social targets and look more at profits, others are refocusing on social performances where a small profit is needed for the long term to find the right balance.
- Equity: organisations of all the participants have some equity but it is not the major part of their portfolio (i.e. 8% for Oikocredit). They take more time to decide (18 to 24 months), need a decision board and more long term investment (7/8 years) as well as a more stable organisation to help to improve governance.