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BONUS PAPER WRAP-UP ISSUE

Acute Poverty Alleviation Through Women's Targeting by Microfinance Programs
by Alexandra Dobra

Microfinance Mission Drift?
by Roy Mersland and R. Øystein Strøm

Child Labour and Schooling Responses to Access to Microcredit in Rural Bangladesh
by Asadul Islam and Chongwoo Choe

Competition and Wide Outreach of Microfinance Institutions
by Hisako Kai

Microfinance Policy and Regulatory Framework in Uganda
by General Caleb Akandwanaho S S

Do Interest Rates Matter? Credit Demand in the Dhaka Slums
by Rajeev Dehejia, Heather Montgomery and Jonathan Morduch

Who is Reaching Whom? Depth of Outreach of Rural Micro Finance Institutions in Ghana
by Kofi Awusabo-Asare, Samuel Annim, Albert Abane and Daniel Asare-Minta

Global Recession and Sustainable Development: The Case of Microfinance Industry in Eastern Europe
by Dr Dragan Loncar, Christian Novak and Dr Svetlana Cicmil

Bringing Financial Services to Africa's Poor
by Kristin Helmore, Sybil Chidiac and Lauren Hendricks

Consumption, Commercial or Mortgage Loans: Does it Matter for MFIs in Latin America?
by Adrian Gonzalez

Strategies for Effective Loan Delivery to Small-Scale Enterprises in Rural Nigeria
by Benjamin Okpukpara

Building Social Business Models: Lessons from the Grameen Experience
by Muhammad Yunus, Bertrand Moingeon and Laurence Lehmann-Ortega

Asia – Commercialise Microfinance
by Nicholas Kwan, Kelvin Lau and Elizabeth Lee

Microfinance Stakeholders - Guiding Hands
by Godfrey Supka

AML/CFT: Strengthening Financial Inclusion and Integrity
by Jennifer Isern and Louis de Koker

Microinsurance: A Safety Net With Too Many Holes
from Knowledge@Wharton

Financial Access 2009: Measuring Access to Financial Services around the World
from CGAP (Consultative Group to Assist the Poor)

INSIDE Page

EDITORIAL

Field Notes: Winds of Change in Arequipa

I have just returned from the XII Annual FOROMIC sponsored by the Inter-American Development Bank's Multilateral Investment Fund (MIF) in Arequipa, Peru, with the perception that the winds of change are upon Latin America's microfinance sector.

Over the past decade, commercial business models for microfinance have been lauded as a sustainable mechanism for building inclusive financial sectors and providing economic opportunities for the large unbanked populations in the region. Meanwhile, integrated models that offer additional support such as business training, financial education and health services fell out of favor, criticized primarily for not being scalable. At this year's FOROMIC, participants seemed more open to business models that seek to help clients avoid over-indebtedness, become empowered and alleviate poverty for themselves and their families. "Responsible lending" was the catch phrase.

Experts are beginning to question the impact of purely commercial models on end users. Faced with deteriorating portfolio quality and weakened client loyalty, commercial microfinance institutions (MFIs) such as ProCredit, humbly stated that returns would be down significantly in 2009 from 2008, but noted their commitment to promoting financial education for their clients going forward. Regulatory frameworks, in turn, may not be protecting loan consumers from an oversupply of loans. Rudy Araujo, Secretary General of the Asociacion de Supervisores Bancarios de las Americas, suggested that supervisors have perhaps been wrong in assuming that market forces would take care of the over-indebtedness problem on their own.

Mibanco, this year's winner of MIF's "Best Microfinance Institution Award" has followed a nearly purist commercial model. This year, at the FOROMIC, Mibanco announced a partnership with MIF through which the bank will offer business training for 100,000 of its women clients. Dean Karlan and Martin Valdivia's recent research in FINCA Peru (May 2009) shows that business training had a significant effect in reducing client desertion. This research suggests that integrated models can make good business sense and begs the question of whether financial education can also have a positive impact on an MFI's bottom line. This was a hot topic in Arequipa, where there was ample discussion about the need to reduce over-indebtedness by offering financial education and greater transparency.

The tone that I observed in Peru was perhaps sparked by the effects of the global financial crisis, but it was a long time coming. After a decade of convincing commercial investors that microfinance is the best way to obtain a double bottom line, can the industry convince its investors to reconsider the business case for providing more than just financial services? If we can re-shape the discourse, I have no doubt that we can generate new and enthusiastic demand for socially responsible investment in microfinance without sacrificing initiatives to provide financial education and other important non-financial services by MFIs to their clients.

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CGAP **MICROFINANCE DEALBOOK**

POWERED BY MicroCapital

TOP SEPTEMBER 2009 MICROFINANCE TRANSACTIONS

The CGAP Microfinance Dealbook publicizes microfinance capital market transactions in an effort to bring greater transparency to the industry. Additional deals are published periodically at http://www.microcapital.org/cgap-microfinance-dealbook. Parties to microfinance transactions are also encouraged to submit their deals via this website.

Investor	Investee	Region	Amount (USD)	Type
Overseas Private Investment Corporation (70% risk participation)	Citi	*	250,000,000	Debt
Overseas Private Investment Corporation	Microenterprise Growth Facility	LAC	125,000,000	Debt
Banco de Credito del Peru	Financiera Edyficar (Purchase from CARE)	LAC	80,000,000	Equity
Small Industries Development Bank of India	Bandhan	SA	~51,900,000	Debt
Carlos Slim Foundation	Grameen-Carso	LAC	40,000,000	Debt
Dutch Ministry for Foreign Affairs	Micro & Small Enterprise Fund (MASSIF)	*	22,000,000	Unspecified
BlueOrchard Private Equity	Asmitha Microfin Limited	SA	~10,200,000	Equity
Inter-American Development Bank	Microenterprise Growth Facility	LAC	10,000,000	Equity
Banco de Credito del Peru	Financiera Edyficar (Purchase from MicroVest)	LAC	8,200,000	Equity
responsAbility Global Microfinance Fund	ProCredit Kosovo	ECA	~7,635,338	Debt
Sociedad Hipotecaria Federal	Financiera Independencia	LAC	~7,500,000	Debt
Micro & Small Enterprise Fund (MASSIF)	Alios Finance Group	SSA	~7,000,000	Debt
Impulse Microfinance Investment Fund (Incofin)	ProCredit Holding	WW	~5,844,000	Debt
responsAbility Global Microfinance Fund	ProCredit Albania	ECA	~5,090,225	Debt
Dexia Micro-Credit Fund (BlueOrchard Finance)	VISION	LAC	5,000,000	Debt
Triodos Microfinance Fund	AccessBank	ECA	5,000,000	Debt
Triodos Microfinance Fund	India Financial Inclusion Fund	SA	5,000,000	Equity
Triodos-Doen, Triodos Fair Share Fund & Triodos Microfinance Fund	Prizma Mikro	ECA	4,400,000	Debt
responsAbility SICAV Mikrofinanz-Fonds	ProCredit Kosovo	ECA	3,272,288	Debt
Hivos-Triodos Fund & Triodos-Doen	KWFT	SSA	~3,000,000	Debt
Dexia Micro-Credit Fund (BlueOrchard Finance)	Opportunity Albania	ECA	2,940,000	Debt
Dexia Micro-Credit Fund (BlueOrchard Finance)	FINCA Kosovo	ECA	2,917,000	Debt
Dexia Micro-Credit Fund (BlueOrchard Finance)	Confianza	LAC	~2,563,664	Debt
responsAbility SICAV Mikrofinanz-Fonds	ProCredit Albania	ECA	2,181,525	Debt
Impulse Microfinance Investment Fund (Incofin)	Grameen FSPL	SA	~2,078,790	Equity
Vision Microfinance Fund (Absolute Portfolio Management)	CRAC Senor de Luren	LAC	2,000,000	Debt
Rural Impulse Fund (Incofin)	Crezcamos	LAC	~1,562,175	Equity
Incofin CVSO	Crecer	LAC	1,500,000	Debt
Lok Capital	Asirvad Microfinance Private Ltd	SA	1,500,000	Equity
Dexia Micro-Credit Fund (BlueOrchard Finance)	PRIZMA	ECA	1,433,500	Debt

Regions: *EAP - East Asia and Pacific, ECA - Europe and Central Asia, LAC - Latin America and Caribbean, MENA - Middle East and North Africa, SA - South Asia, SSA - Sub-Saharan Africa, * - Investee location may not indicate the final destination of the funding because investee is an intermediary*

Amounts: *Deals denominated in local currency are indicated by a tilde (~); a double asterisk (**) indicates that the transaction included funding of non-microfinance services and the amount shown is an estimate of the allocation specifically to microfinance*

SPONSORED CONTENT

International Finance Corporation
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KNOW A FUND

Microfinance Enhancement Facility: An interview with Mark Berryman of the International Finance Corporation

Microfinance Enhancement Facility

The Microfinance Enhancement Facility (MEF) is a microfinance investment vehicle that was established this year in response to the global credit crisis to refinance loans to well-established microfinance institutions (MFIs). MEF was founded by the International Finance Corporation (IFC) and KfW Entwicklungsbank. IFC, a member of the World Bank Group, made new investments totaling USD 16.2 billion in fiscal 2008. IFC's microfinance investment activities reached nearly USD 1.3 billion in 2009 through over 160 projects in over 60 countries. Mark Berryman, of IFC's Global Financial Markets Microfinance Group, recently spoke with MicroCapital:

MicroCapital: Please briefly describe the founding of MEF and its fundraising.

Mark Berryman: MEF held a signing and launch ceremony on February 5, 2009, at which the first USD 280 million was committed: USD 130 million by KfW and 150 million by IFC. Thereafter, the Austrian Development Bank invested USD 25 million, the German government invested USD 36 million and the European Investment Bank invested USD 50 million; so USD 391 million is now subscribed. The next two closings will take MEF to its target size of USD 500 million.

MC: What is the lending activity to MFIs?

At the fund launch in February 2009, we held the first Investment Commitment meeting and approved the first set of loans to MFIs. On May 13, MEF disbursed its first loans totaling USD 30 million dollars to eight MFIs. The next disbursement will take place in coming weeks, and the volume will be USD 80 million.

MC: What has demand been like?

MB: The demand differs across regions. In October and November, the need was over USD 1 billion dollars of refinancing for MFIs. This is looking at a survey of approximately two hundred top MFIs. These estimates were based on growth projections that have changed with the unfolding of the crisis over the last three to six months. MFIs in general have reduced their demand, and many are focusing on portfolio quality and at the same time beefing up risk management. These are generalized outcomes of the financial crisis and, again, it's going to differ by country and institution.

MC: Please describe the product offered.

MB: MEF provides short-term senior loans (2 to 3 years) to MFIs pari passu with other notes outstanding at the MFI level. It offers both fixed and floating rates and will offer local currency going forward. The product offering may change as determined by the Board in accordance with changes in the financial markets.

MC: What is the pricing?

MB: The pricing of individual loans to MFIs is market based. MEF was set up to kick in where private funds are not available.

JUST THE FACTS

Fund name: Microfinance Enhancement Facility

Date established: February 5. 2009

Portfolio: $30m, 8 microfinance institutions

Share classes: Euros, US dollars, local currencies

Net asset value: $391m as of October 2009

Target net asset value: $500m

Founders: International Finance Corporation and KfW Entwicklungsbank

Investors: International Finance Corporation, KfW Entwicklungsbank and the Austrian Development Bank

Managers: BlueOrchard Finance, Cyrano Management and responsAbility Social Investments

Fund Secretariat: InnPact S.ar.l.

Hedging advisor: Cygma Corp.

Custodian: Credit Suisse

Website: http://www.ifc.org/ifcext/about.nsf/Content/FinancialCrisis_MEF

MC: Are all the MFIs that have received funding existing members of the three fund managers' portfolios: Blue Orchard Finance, Cyrano Management and responsAbility?

MB: Not all MFIs will be existing clients of the fund managers. Any interested MFI is welcome.

MC: When do you anticipate full disbursement of the fund?

MB: Full disbursement will depend on demand. The funds will be lent to those who have the largest need for refinancing. MEF is not a bailout facility. It was built to support strong institutions experiencing funding gaps due to the crisis. Depending on the geography of the demand, the MEF will be able to supply refinancing on an as-needed basis. MEF investors agree that project should be a temporary solution, and when the crisis turns around the project will either evolve or it could get wound up by shareholders.

MC: What was the primary challenge faced in bringing the project together?

MB: There were many challenges, but everyone agreed it was important to move quickly because private funding was disappearing. We got it up and running in record time of less than two months.

MC: What would you say enabled that record time?

MB: The key factor was total support from IFC management and also our close collaboration with KfW.

MC: Do you have a long working relationship with KfW? Can you give examples of such partnerships?

MB: KfW is one of our closest partners in microfinance. This includes setting up greenfields in markets with little to no access to finance and working with network partners and microfinance investment vehicles.

MC: What else would you like the public to know about this project?

MB: The project is flexible to meet the needs of MFIs as they change with the evolving financial situation and financial sector. In our view, these types of vehicles should not crowd out the private sector. The facility was set up to help stabilize funding for systematically important MFIs and their clients.

PAPER WRAP-UPS

Acute Poverty Alleviation Through Women's Targeting by Microfinance Programs

By Alexandra Dobra, published by the Munich Personal RePEc Archive, March 2009, 8 pages, available at: http://mpra.ub.uni-muenchen.de/16874/1/MPRA_paper_16874.pdf

This paper is literature review regarding the merits of female-targeted microfinance. Firstly, the author points out that as of 2005 women are a majority of the poor, making up 70 percent of people in the world living on USD 1 per day. She also points out their likelihood of staying poor due to oppressive "patriarchal norms." Although women are "precarious" public economic agents, they tend to have multiple responsibilities in the private sphere and therefore have "various potentialities for development."

The author also states that women tend to spend earned income on the family, thus helping to decrease household poverty rates. According to the Women's Entrepreneurship Development Trust Fund, women spend 18 percent of their microfinance income on schooling, 55 percent on medical services and household goods and 15 percent on clothes. The author also refers to a World Bank finding that female loan repayment rates tend to be higher that that of men. The World Bank also shows that gender inequality is a retardant to growth itself.

The author also looks to female empowerment as an important effect of microfinance. She states that "access to self-employment" for women promotes "self-confidence and the capacity to play an active role in society." Additionally, empowerment has been found by the World Bank to have a positive correlation with "indices of development" relating to gender inequality as well as with the Human Development Index, a quality of life measure based on life expectancy, education, adult literacy, gross enrollment and gross domestic product. A study by the Women's Empowerment Program in Nepal showed that 68 percent of women with access to credit also make "familial scheduling, schooling [and marriage]" decisions. The URWEGO Opportunity Bank of Rwanda showed that credit access led to 68 percent of female clients gaining increased self-respect and 38 percent increasing "notions of enterprise management." A program in Tanzania from the Women's Entrepreneurship Development Trust Fund reports that economic empowerment went so far as to provide women the ability to "emancipate themselves."

Despite all this, the author still believes there is room for improvement in microfinance as it relates to gender. She points to creating microfinance programs that are more sensitive to cultural norms. For instance, it might be important to distinguish between societal gender inequality that is based on "high separation of the public/private sphere [and] low social mobility," and the type that is more rooted in "gender distinction in access to resources."

Microfinance Mission Drift?

By Roy Mersland and R. Øystein Strøm, published by Elsevier Ltd, July 2009, 9 pages, available for purchase at: http://www.sciencedirect.com/

This paper studies the tendency of microfinance institutions (MFIs), as they grow, to cater to groups that are different from those normally considered to fall under the "mission" of microfinance. Generally, this mission includes serving low-income people who have less access to credit - often poor, rural women. To investigate this possible mission drift, loan size, lending methodology and gender bias were studied in 379 MFIs in 74 countries using data taken over 4 to 6 years. Average loan size did not increase from 1999 to 2007. There has not been a move from group-liability to individual-liability loans. Nor has there been an increased proportion of urban loans compared to rural loans. However, there is less gender bias now, meaning that the tendency to lend to females more than to males has decreased. Overall, the authors feel that there has not been a mission drift in microfinance.

The average loan size from 1999 to 2007 was USD 747, adjusted for purchasing power parity (PPP). The authors consider this to be a relatively small loan size. Furthermore, the average loan size has decreased by 2.2 percent from 1999 to 2007. This is seen by the authors as evidence that low-income borrowers are still being targeted by MFIs.

Lending methodology was measured to compare group and individual lending. The authors found that most loans are made to individuals. However, group lending increased by 3.3 percent during this period compared to individual lending. The authors view this as a sign that microfinance continues to meet its mission.

It has also been tradition that MFIs would target rural regions more than cities as the former are generally thought to have less access to mainstream credit. The authors found that rural lending grew by 9.5 percent from 1999 to 2007 compared to urban lending.

Lastly, the authors find that there has been a decrease of 35 percent from 1999 to 2007 in terms of preference for female clients. Though this may seem inconsistent with the microfinance "mission," it does indicate less gender bias. Therefore, the authors do not see this result as particularly harmful and claim that it does not necessarily indicate mission drift.

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MicroCapital would like to recognize the individuals at CGAP, the Microfinance Information Exchange and the Microfinance Gateway for their outstanding work disseminating information on microfinance. Thank you!

Child Labour and Schooling Responses to Access to Microcredit in Rural Bangladesh

By Asadul Islam and Chongwoo Choe, published by Munich Personal RePEc Archive, January 2009, 49 pages, available at http://mpra.ub.uni-muenchen.de/16842/1/schooling-child_work_Bangladesh_Asad.pdf

This study presents a statistical analysis on the adverse effects of microcredit on child labor and children's schooling in Bangladesh. Designed to be nationally representative, it compares 2,034 households in 13 districts across 91 villages. The study involves a treatment group, which received microcredit and a control group of people from the same villages who did not receive microcredit but are "observationally similar."

Dr Asadul and Dr Chou refute the claims made by scholars that "access to credit [has] a positive effect on children's education," especially when given to women, who generally prefer spending income on their children's health and education. They argue that microcredit has an adverse effect on children largely because loans result in the establishment of household enterprises that require extra labor. Since the amount of the loan is usually not large enough to cover external labor, child labor is used. Furthermore, short repayment periods and high interest rates may also cause parents to temporarily resort to child labor. According to the authors, "while microcredit programs can alleviate poverty and contribute to rural economy in the short term, they can also result in unintended consequences adversely affecting children's schooling, which could exacerbate poverty in the longer term."

The empirical findings of the study are divided into the following four sections:

1. Impact Estimates by Children's School Age: The study finds that the adverse effect of microcredit is most significant on primary school children. Girls in primary school are particularly affected, and more so when microcredit is obtained by men. School enrollment for girls decreases by 33 percent when credit is obtained by women, compared to 41 percent when credit is obtained by men. At the secondary school level, there is still a negative impact on girls' schooling when women obtain credit, but there is no effect when men obtain credit. The effect on boys at the secondary school age was statistically insignificant.

2. Impact Estimates by Household Income: Since participation in microcredit has a positive effect on income, using income as a variable would conflict with the very nature of this study. Therefore, to try to eliminate bias, the authors used parental education as a substitute for income, believing that increased education would have a positive correlation with increased income. The results showed that the more education parents received, the more likely it would be that their children attended school and did not work. In households in which parents only completed primary school, children's school enrolment decreases by 29 percent and child labor increases by 9 percent.

3. Microcredit, Household Income and Child Schooling: When microcredit is given to high-income households, the probability of child labor decreases and children's schooling improves. A 10 percent increase in credit given to high-income families reduces child labor by 0.4 percent and improves schooling by 0.8 percent.

4. Impact Estimates by Land Ownership: Land ownership is used here as a symbol of wealth. In poorer households, or those with less land, microcredit decreases the probability of school enrollment for girls, but also decreases the probability of child labor for boys. In less poor households, the result is reversed, perhaps due to the greater need for boys to work on the land.

According to this study, the most vulnerable - girls, young children, those with less education and those with the lowest incomes - are the most adversely affected. To decrease the necessity of households to resort to child labor, the authors suggest extending repayment periods, reducing interest rates and increasing loan sizes to allow for the employment of external labor. In addition, they propose more financing at the village level rather than the household level. Finally, they emphasize the need for other policies that directly target children's education to complement microfinancing.

Competition and Wide Outreach of Microfinance Institutions

By Hisako Kai, published by Munich Personal RePEc Archive, September 9, 2009, 12 pages, available at http://mpra.ub.uni-muenchen.de/17143/

Hisako Kai describes how most microfinance institutions (MFIs) that aim for socioeconomic improvements, which are termed "socially-motivated" MFIs, gear their efforts towards expanding their levels of outreach, both in terms of providing to the poorest people ("width outreach") and maximizing their number of clients ("length outreach"). Attaining wide levels of outreach requires MFIs to utilize external subsidies and cross-subsidies, where gains from more profitable clients are used to subsidize loans to unprofitable borrowers. It is assumed that poorer clients tend to have higher default rates, while the relatively wealthy clients receive larger loans and are thus more profitable to MFIs.

Many previous theoretical studies claim that competition has adverse impacts on profitability and cross-subsidization of socially-motivated MFIs, which could lead to limitations on the width of their outreach capabilities. First, they show that competition causes a decrease in "dynamic incentive," which refers to the event where clients are able to obtain loans from other lenders without paying back their original loans to their initial lender, thus decreasing their payback incentives. As clients borrow from multiple lenders, default rates increase and profitability and cross-subsidies of MFIs fall. Second, these studies argue that competition may lead to a decrease in "productive" clients for socially-motivated MFIs. Profit-centered MFIs that enter the industry target larger loans at the wealthiest of the pool of poor clients, which causes these clients to switch over from incumbent, socially-motivated MFIs that provide smaller loans. Third, new MFI entrants may lead to a fall in interest rates. Though this may benefit borrowers, the overall income that MFIs generate from interest rates will decline, leading to a drastic decrease in cross-subsidies used for poorer clients. These analyses claim that that the adverse effects of competition place a budget constraint on socially-motivated MFIs, and lead to lessened financial self-sufficiency or a less wide level of outreach.

Despite the fact that theoretical literature suggests that competition among MFIs leads to these effects, Ms Kai argues that there is insufficient empirical research to conclude that competition affects wide outreach or causes poorer borrowers to drop out of the microfinance market. Through an empirical analysis of data from 2003 to 2006 on 450 MFIs from 71 countries, she aims to study the impact of competition among MFIs on (1) the width of outreach to assess whether they can still reach the poorest of the poor and (2) the financial self-sufficiency of socially-motivated MFIs.

The results of the empirical research depict that intense competition between different types of MFIs does decrease the wide outreach capabilities of socially-motivated MFIs, which leads to poorer borrowers dropping out of the market. However, it does not worsen financial self-sufficiency or lead to an increase in subsidy dependence, which shows that competition does not increase MFI dependence on external subsidies. Ms Kai also concludes that the harm of competition on wide outreach decreases as MFIs gain experience. More experienced MFIs limit the reduction of their wide outreach, as they have greater market power and greater possibilities for technological advancement, making them less vulnerable to increased competition.

Microfinance Policy and Regulatory Framework in Uganda

By General Caleb Akandwanaho S S; published by Uganda's Ministry of State for Finance, Planning and Economic Development; July 24, 2009; 8 pages; available at: http://www.finance.go.ug/docs/Introduction%20to%20Microfinance%20bklet.pdf

In 1999, the Bank of Uganda (BOU) created the Policy Statement on Microfinance Regulation as a framework for Ugandan microfinance institutions (MFIs). The statement served the policy needs of Tier 1, 2 and 3 MFIs; however, it was unable to provide for Tier 4 institutions. Furthermore, the existence of multiple laws scattered across various policy documents, as opposed to a consolidated legal framework afforded to Tiers 1 to 3 MFIs, has made it difficult for Tier 4 MFIs to protect savings and provide consistently reliable service.

To consolidate the existing policies and to ensure the safety of savings at Tier 4 financial institutions, this paper addresses the issues of regulation for Tier 4 institutions and proposes plans through 2015 to implement a corresponding legal framework.

Five objectives of a new policy framework in the Ugandan microfinance sector are outlined:

1. Increase Access to Microfinance Services Countrywide

Challenge: One of the biggest challenges facing the microfinance sector in Uganda is the concentration of financial institutions in urban and peri-urban areas, as indicated by a high concentration of people per financial institution.

Solution: Financial intermediaries, whose outreach is more diverse in rural areas, are needed to assist MFIs that are overwhelmed with borrowers. Savings and Credit Cooperatives (SACCOs) can act as intermediaries between MFIs and borrowers. While conventional banks require a minimum deposit of USD 67, the Kenya Union of Savings and Credit Cooperatives Ltd, for example, accepts deposits of USD 2.70.

2. Improve Safety of Savings Through Effective Regulation and Supervision

Challenge: Taking deposits and lending to entrepreneurs has resulted in losses where transparency is not practiced.

Proposed solution: Intermediaries must ensure that the depositor is able to access his/her savings when they want them (according to agreed withdrawal terms). This can be achieved through close supervision and thorough operations management by a Microfinance Regulatory Authority (MFA) to ensure repayment of loans and that proper procedures are followed by intermediaries.

3. Enhance Microfinance Institutional Sustainability

Challenge: Capacity building serves primarily urban areas, is generally only targeted to MFI managers rather than MFI members and can be very costly. MFI members are not inclined to hold managers accountable for fraudulent behavior and mismanagement.

Solution: The Uganda Cooperative Savings and Credit Union (UCSCU) must begin forming SACCOs and giving them the tools to build capacity amongst microfinance management, staff and members. This includes logistical support, certification in operations and management, certification in corporate governance, management tools, governance tools and enhanced monitoring and evaluation techniques.

4. Improve Consumer Awareness and Demand for Cost Effective Financial Service Delivery

Challenge: Several institutions that once played a role in increasing public awareness, such as the Co-operative Education and Publicity Programme (CEPP), collapsed during the decline of the cooperative movement.

Secondly, the authors argue that inadequate, inaccurate and delayed and warnings regarding fraudulent behaviour have left the unsuspecting public more vulnerable to "Get Rich Quick" schemes.

Solution: Borrowers must be trained to recognize healthy MFIs. The MFA should be in charge of developing and monitoring health indicators for Tier 4 MFIs. Under this development scheme, "Consumer education messages will be designed and standardized training modules developed." Furthermore, transparency regarding pricing and performance must be practiced by MFIs.

5. Develop Institutional and Product Range in the Microfinance Industry through Research and Training

Challenge: Research on Uganda's financial sector is lacking, particularly where informal financial institutions are concerned. Second, microloans and other activities in the informal sector are not being documented scrupulously and consistently. Third, service delivery across different tiers of the financial sector is very costly.

Do Interest Rates Matter? Credit Demand in the Dhaka Slums

By Rajeev Dehejia, Heather Montgomery and Jonathan Morduch, published by the Financial Access Initiative and New York University Wagner School, May 2009, 41 pages, available at: http://financialaccess.org/sites/default/files/Do%20Interest%20Rates%20Matter%20May%2009_0.pdf

This study attempts to show how sensitive borrowers are to rises in interest rates. It measures the change in overall demand for loans after an increase in the interest rate. The study was done at SafeSave, a credit cooperative in Dhaka, Bangladesh. SafeSave has the convenience of a credit cooperative as the loan officers visit borrower's homes, but also the flexibility of a bank in terms of repayment schedule within a given month. However, outstanding interest must be paid on a monthly basis. For the study, interest rates were unexpectedly raised from 2 percent per month to 3 percent per month in two branches of SafeSave but not a third branch, which was the control set. The data from 1999 to 2001 was collected monthly on 5,147 customers, not all of whom participated throughout the study. Average loan size ranged from USD 48 in the branches that underwent interest rate change, to USD 37 in the branch that did not.

The primary result of the study is that borrowers at SafeSave decreased loan demand significantly as a result of the increase in the interest rate. The change was measured in terms of elasticity, the percentage change in loan balance after the change in interest rate. A one percentage point increase in the interest rate resulted loan demand decrease ranging from 36 percent to 44 percent over the course of 12 months. Overall, this decrease is explained by borrowers taking smaller and more frequent loans after the interest rate jump and repaying them more quickly.

Additionally, less wealthy borrowers appear to decrease their loan demand more than wealthier borrowers due to the increase in interest rates. The categorization of "less wealthy" and wealthy was based on initial savings balances. The interest rate jump from 2 to 3 percent per month resulted in the loan demand of less wealthy borrowers decreasing by 43 percent and the loan demand of wealthier borrowers to decrease by 13 percent.

Who is Reaching Whom? Depth of Outreach of Rural Micro Finance Institutions in Ghana

By Kofi Awusabo-Asare, Samuel K. Annim, Albert M. Abane and Daniel Asare-Minta, published by the International NGO Journal, April 2009, 10 pages, available at: http://www.academicjournals.org/ingoj/PDF/Pdf2009/Apr/Asare%20et%20al.pdf

This paper studies the socioeconomic status of clients being reached by different types of microfinance institutions (MFIs) in Ghana. Using a poverty index, the study shows which type of MFIs reach relatively poor or rich clients. The study also attempts to explain these results through reasons relating to the "source of funds, strategies for outreach and mission of the institution." Lastly, MFI policy recommendations are made.

The study uses a "Microfinance Poverty Assessment Tool," to measure socioeconomic status. This measure, developed by CGAP (Consultative Group to Assist the Poor), calculate a household relative poverty index based on housing characteristics, food security and vulnerability, livestock and consumption. The study included 1,600 clients. The MFIs were separated into rural and community banks, non-governmental organizations (NGOs), savings and loans companies, credit unions and susu collectors (mobile bankers running a small savings a loan operation). Sixteen MFIs were selected in addition to one makeshift "MFI" that was simply a group of susu collectors.

The index was divided into five "quintiles," namely, the lowest (poorest), below average, average, above average and the highest (richest of the poor). It was found that rural and community banks and NGOs reached the broadest group, ranging from the poorest people to the richest. Credit unions reached those in the range of "below average" to the richest. Lastly, savings and loan companies and susu collectors reached from the "average" clients to the richest.

The authors found that institutions that employ peer selection and loan qualification requirements tend to cater to higher-income clients. Peer selection involves potential clients forming a group, choosing members believed to be trustworthy in terms of repayment. This is likely to eliminate the poorest clients. The same can be said for a situation in which potential clients must prove to the institution that they "qualify" for a loan based on their economic characteristics such as income and assets. On the other hand, institutions that select clients by committees reach lower income clients, especially when these institutions rely on donors who have a specific interest in reaching poor clients. Committee selection involves "technical advisers, representatives of the district assembly, loan officers of the rural bank and representative of the donor institution" voting on which clients to select. If the donor institution specifically wants to reach the poorest clients, this outcome is often met. Generally, rural and community banks employ peer selection and/or committee selection. NGOs use peer selection, but allowe non-financial contributions such as produce in order to open credit access to poorer clients. Susu collectors generally have a group insurance scheme. Therefore clients self-select based on their ability/willingness to make a contribution, thus eliminating the poorest clients. Similarly, credit unions and savings and loan companies have economic requirements for loan qualifications that may segment out poorer clients.

The authors point out that social and political interference, such as political patronage, was the main thing preventing selection committees from reaching poor clients. Therefore, they believe that avoiding this pitfall should be an important policy concentration for MFIs. Also, they mentioned the success of financial NGOs that allowed clients to make non-financial contributions such as vegetables. They believe this is one way for MFIs to reach the poorest clients.

Global Recession and Sustainable Development: The Case of Microfinance Industry in Eastern Europe

By Dr Dragan Loncar, Christian Novak and Dr Svetlana Cicmil, published September 2009, 10 pages, available at http://www.microfinancegateway.org/gm/document-1.9.39138/MICROFINANCE%20PAPER-%20FINAL%20VERSION.pdf

This research paper addresses why the microfinance industry in Eastern Europe performs cyclically and is more vulnerable to contemporary economic trends than is microfinance in other regions. The paper is divided into three sections: general microfinance trends, microfinance trends in Eastern Europe and the impact of the current global recession on microfinance in Eastern Europe.

According to the paper, the microfinance industry is considered to be "resilient to the economic cycles." Since the poor are less dependent on global economic trends, repayment rates have remained relatively stable, with "top-tier" microfinance institutions (MFIs) reporting average repayment rates well above 90 percent. From 2003 to 2007, the microfinance sector expanded its customer base by about 25 percent per year, reaching more than 100 million clients globally by the end of 2007 with an estimated loan volume of USD 25 billion. This rapid growth has attracted institutional investors, development agencies and NGOs, all seeking to make socially responsible investments (SRIs) while enjoying a high rate of return. "Due to the nature of the microfinance business and [its] trends, top-tier MFIs have been reporting more favorable results than conventional commercial banks in many countries."

The authors point out, however, that the counter-cyclic nature of the microfinance industry does not apply to Eastern Europe. Repayment rates were at 98 percent in 2007, but fell to 80 percent in 2009. It is expected that women, who make up over 80 percent of MFI clients in the region, will be the hardest hit. This is partially due to large loan sizes (averaging around USD 1,600) and a preference for individual lending instead of lending groups, which help mitigate delinquency and default risk. Furthermore, in the majority of countries in the region, microfinance is not fully integrated into local financial systems due to a lack of adequate legal and regulatory frameworks. In Serbia, for example, "the Law on Banks allows only the traditional commercial banks to lend money," forcing MFIs to operate via commercial banks, thus increasing their administrative costs and interest rates.

The peculiarity of microfinance in the region, the authors claim, "predominantly lies in the macroeconomic structure of the Eastern European economies," including the following points:

- Incomplete economic transition in the former communist countries
- High inflation (sustained high food prices) and drop in real income
- Higher cost of capital after a long period of unsustainably cheap funding made available to MFIs
- Dominance of individual lending (as opposed to group lending), which increases the cost per borrower and risk of default
- High average size of microloans, which concentrates credit risks and in many cases puts MFIs in direct competition with conventional commercial banks
- Lack of local deposit base due to incomplete regulation of the microfinance business in many countries
- Withdrawals of the existing deposit base over the recent months
- High dependence on foreign funding in hard currency coupled with local currency depreciation
- High dependence of borrowers on remittances from abroad, which have decreased
- Unstable internal organizational structure of MFIs and poor networking among local MFIs (within national associations), resulting in low negotiation power
- Relatively underdeveloped MFI management and lack of adequate risk management

Despite the negative outlook for the microfinance industry in Eastern Europe, the authors remain optimistic that MFIs will "probably emerge as stronger organizations." They suggest that MFIs should slow their growth plans, reward clients who have paid on time with further loans, improve internal efficiency and turn to a deposit-led approach. Many of these suggestions, however, would require regulation changes.

Bringing Financial Services to Africa's Poor

By Kristin Helmore, Sybil Chidiac and Lauren Hendricks, published by CARE, September 2009, 143 pages, available at: http://www.care.org/getinvolved/advocacy/access-africa/

This report addresses CARE's approach to providing Africa's poor with financial services. CARE's Village Savings and Loan Associations (VSLAs) give poor women the means and confidence to build more prosperous futures for themselves and their families.

CARE VSLAs are built by women living on less than USD 2 a day who collectively save pennies each week and make small loans to each other to support new business ventures, such as farming, jewelry making or beer-brewing. Because members borrow from each other, there is a low default rate on loans and much lower interest rates, compared to the 100 percent sometimes charged by traditional moneylenders.

CARE's VSLA approach is part of its larger Access Africa program that aims to bring financial services to 30 million people in 39 African countries over the next 10 years. At least 70 percent of people served will be women.

Consumption, Commercial or Mortgage Loans: Does it Matter for MFIs in Latin America?

By Adrian Gonzalez, published by the Microfinance Information Exchange, September 2009, 16 pages, available at: http://www.themix.org/sites/default/files/MIX%20Data%20Brief%20No%203%20Sept%202009_0.pdf

This study explores whether loan product mix affects the performance of a microfinance institution (MFI) using data the Microfinance Information Exchange (MIX) collected on credit types from 322 MFIs throughout Mexico, Latin America and the Caribbean.

When compared to microenterprise loans, higher shares of consumption loans are associated with higher yields, higher profitability, yet lower portfolio quality.

Strategies for Effective Loan Delivery to Small-Scale Enterprises in Rural Nigeria

By Benjamin Okpukpara, published by the Journal of Development and Agricultural Economics, May 2009, 8 pages, available at: http://academicjournals.org/JDAE/PDF/Pdf2009/May/Okpukpara.pdf

This work studies the determinants of microbusiness loan acquisition for rural entrepreneurs in Nigeria. In order to increase access to formal credit to rural areas, the government has enacted various microcredit programs specifically targeting the rural poor. However, according to the author, most of these programs have fallen short of their goals due to "poor targeting" and a "lack of organized ways of administering loan to the rural enterprises." Therefore, this study attempts to ascertain which strategies can overcome the problem of low access to microfinance services.

The study took place in the poor, rural states of Abia and Anambra. A total of 136 microenterprises from these states were selected at random and surveyed. Entreprenuers were asked questions relating to what factors determine whether or not they obtain a loan. Additionally, survey information was collected from 20 informal financial institutions and 14 formal financial institutions.

Of the 136 enterprises, 34 were able to obtain loans, 27 of these from informal financial institutions. However, not all enterprises attempted to obtain loans. Of those who did, 55 percent of formal loan applications were accepted, and 94 percent of informal loan applications were accepted. According to entrepreneurs surveyed, informal institutions do not generally require asset collateral, and they do not have a bureaucratic application process, thus making their loans easier to obtain. However, those surveyed claimed that both formal and informal loans are more easily obtained when the applicant has a good loan repayment record, when there is more competition between institutions, and when the interest rate is higher. In the case of interest rates, higher rates often equate to greater loan access because borrowers are willing to lend to more, perhaps "riskier" clients when the interest rate is higher. Additionally, it is important to note that interest rate changes did not greatly effect the desire of entrepreneurs to obtain a loan.

To determine loan provision institutions rely heavily on, in order of average importance: loan history, enterprise type, experience, gender (males preferred) and collateral. As strong repayment history generally predicts reliability for future repayment, it was, on average, the most highly valued indicator of credit-worthiness by financial institutions. Agricultural enterprises were found to have a lower likelihood of receiving credit than other types of enterprises. This is important because most rural enterprises in Nigeria are agricultural. Financial institutions cited uncertainty and risk in agriculture as the reason for this discrimination. In both agricultural and non-agricultural enterprises, entrepreneurs with a higher level of experience were more likely to obtain loans. It was also the case that men were more likely than women to receive loans. This can be explained by a range of factors from "lack of assets to traditional and customary factors in African institutions." Lastly, possession of a fixed asset on the part of an applicant made them more likely to receive a loan, but the relationship was relatively weak. Formal institutions did, however, generally require fixed assets as collateral, but informal institutions often did not.

Based on this information, the author recommends policies that should be put forth by both the government and financial institutions. He recommends business training to increase productivity and to help to build repayment history. He also sees microinsurance as important to minimizing the risk involved in agriculture. Finally, to remedy gender discrimination, the author suggests that lenders institute quotas to make sure that a certain percentage of their loans go to female borrowers. This would encourage not only acceptance of female applicants, but could also catalyze a proactive effort to seek out female entrepreneurs.

Building Social Business Models: Lessons from the Grameen Experience

By Muhammad Yunus, Bertrand Moingeon and Laurence Lehmann-Ortega, published as a working paper by the HEC International Business School, February 2009, 27 pages, http://www.microfinancegateway.org/gm/document-1.9.39135/Building%20Social%20Business%20Models.pdf

The authors argue that governments, nonprofit organizations (NPOs), multilateral institutions and existing for-profit companies cannot sufficiently address poverty. Governments tend to be inefficient and prone to corruption, NPOs are highly dependent on donations for funding, multilateral institutions have not made a sufficient impact and for-profit companies that claim to exhibit corporate social responsibility (CSR) will always prioritize financial profit over all else. Therefore, the authors justify the need for "social businesses" that integrate aspects of both profit-maximizing companies and socially-motivated NPOs.

The paper first defines the concept of a social business, which has risen from the experiences of the Grameen Group, a network of 27 organizations linked to the Grameen Bank of Bangladesh. Social businesses borrow aspects of structure, functions and objectives from both profit-maximizing companies and NPOs. They are similar to NPOs in that they prioritize societal improvements, but operate like for-profit businesses in that they aim to recover their cost of operations to maintain self-sustainability. However, social businesses only rely on investors at the beginning of a development project, and unlike for-profit businesses they do not distribute revenues to shareholders, but rather reinvest in the business to benefit their social cause.

The authors first provide an example of what they consider a successful social business model. Grameen Danone Food Limited (GDFL) is introduced as one of the first social business experiments. It was created in 2006 as a joint venture between the Grameen Group and the French Groupe Danone, one of the world's leading health food companies, in order to "bring health through food to a maximum number of people."

Using empirical examples, drawing from the experiences of organizations linked to the Grameen Bank, the paper introduces general recommendations on how to build effective social business models: (1) Social businesses should challenge conventional business models by coming up with innovative business models that will provide high quality products at low costs, making them affordable to low-income consumers; (2) Businesses ought to find complementary organizations with which they can set up long-term partnerships in order to leverage and broaden both expertise and resources; and (3) A continuous process of experimentation is encouraged to fine-tune the business model.

The authors also offer more specific examples of how to maintain the priority of social profit while also keeping stakeholders in mind: (1) The models must be designed to favor social profit-oriented shareholders. They must be reframed to favor all stakeholders that support the company's social mission, instead of merely shareholders, customers, partners and suppliers. (2) The authors emphasize the importance of clearly specifying the social objectives, criteria and constraints of the business. Without this, the company's objective may be unclear to investors, since it plans to aim for both financial profit and social benefits. (3) The model must make adjustments to the traditional business model framework to reflect the company's social goals.

The authors conclude by saying that creating social business models is a difficult but possible process. They believe that there will be a growing interest in the sector since the Grameen Group will encourage others to consider similar ventures and learn from each other.

Asia – Commercialise Microfinance

By Nicholas Kwan, Kelvin Lau and Elizabeth Lee, published by Standard Chartered Bank, August 31, 2009, available at: http://microfinancegateway.org/gm/document-1.9.37784/Asia%20Commercialise%20Microfinance.pdf

This is paper describes the role of commercialization in the transformation of the microfinance industry. The authors note that, though microfinance has been growing in popularity throughout the world in the past few decades, Asia has not maximized its potential in this investment sector. The authors use the term "commercialization" of microfinance to refer to the idea of microfinance institutions (MFIs) becoming highly integrated into the for-profit business and financial sector, rather than the nonprofit, subsidized sector. The authors argue that, especially considering Asia's growing economy, Asian MFIs are well positioned to become more involved in commercialized microfinance and cross-border investment. Many Asian MFIs have begun to further integrate themselves with commercial banks and the financial sector.

This report first examines the increasing role of commercial banks in bridging the gap between demand and supply of microfinance loans, as well as the lack of funding sources for nonprofit MFIs. The authors note that, though the microfinance industry has grown at an unprecedented rate, there is still an excess demand for microfinance loans from a global market of 3 billion people. As the microfinance industry has gained popularity in recent years and has shown that it can be profitable, more commercial banks and other for-profit organizations have begun to enter the industry to fill this gap between demand and supply. Therefore, they argue that commercialization is a tool for banks and organizations to penetrate the market and tap into those that have not yet been reached by existing MFIs.

The authors state that commercialization also helps fill the funding gap that exists in the microfinance industry. In addition, it provides MFIs with new opportunities to access local savings pools and capital markets, accept deposits from the public or even go public, like Mexico's Banco Compartamos did in 2007.

The report refers to data from CGAP (Consultative Group to Assist the Poor) indicating that between 2004 and 2006 foreign capital investment in microfinance tripled to USD 4 billion, arguing that it shows commercialized microfinance has tremendously increased in appeal to the socially responsible investment (SRI) market, due to the sector's double bottom line of financial profit and positive social impact.

The paper compares various countries' outreach and success in attracting cross-border microfinance investments. Of the regions surveyed, Asia has the greatest number of borrowers and savers, but is one of the worst, along with Africa, in terms of foreign capital investment. The authors note, however, that this data must not be interpreted too literally, as one must also taken into consideration intra-regional differences in socio-political and economic situations, as well as structural disparities between MFIs.

Finally, as the authors recommend commercialization is the best way for Asian MFIs to increase foreign investment and further develop the microfinance sector, they identify guidelines called "the four 'R's" to help along this process, which are: resources, risk, return and regulations. Three of the R's come from a paper presented at the 2007 annual Commonwealth Finance Ministers' meeting by Standard Chartered Bank Group Chief Economist Dr. Gerard Lyons, and the fourth R was added by the authors to this report:

- Resources: There ought to be more careful cost control, expanded funding and greater technology.
- Risk and Return: MFIs ought to ensure that the amount of risk that they are taking on is justified by the returns they are earning; product innovation and diversification can help offset increased risk. Transparency within MFIs and the importance of adopting standard reporting practices are also emphasized.

Regulations: The government's involvement is essential to developing the microfinance sector.

Microfinance Stakeholders - Guiding Hands

By Godfrey Supka, published by the International Banking Systems Journal, October 2009, 2 pages, available at: http://www.ibspublishing.com/index.cfm?section=MF09&action=view&id=13428

As part of a special issue on the role of technological systems in microfinance, this article explores how microfinance institution (MFI) stakeholders shape the market for microfinance information systems (MIS). The thrust of the article is that there is an important difference between the microfinance and commercial banking sectors when it comes to information systems and that MFIs depend heavily on key stakeholders such as the Bill and Melinda Gates Foundation, CGAP (Consultative Group to Assist the Poor), International Finance Corporation and German development agency GTZ for guidance and direction in making technology decisions. The conclusion is that "directly or indirectly, it is these stakeholders that influence purchasing decisions by MFIs, on the business case for investment, the process of selection and which products to choose" when it comes to MIS.

The article discusses the Grameen Foundation's Mifos system, which is an open source technology platform for the microfinance industry, which means that it has been developed by a global community of technology professionals and microfinance practitioners. Grameen is helping four or five MFIs use the Mifos system, but there may be many other MFIs using the system without its assistance or knowledge. Grameen is now working on a shared platform where Mifos will be made available as a subscription-based service over the internet for customers in the Philippines.

Rather than backing one particular MIS, CGAP offers grants of up to USD 25,000 for MFIs to improve their MIS. CGAP technology programme senior advisor Xavier Faz was quoted as stating that "The grants enable MFIs to hire a consultant to do a well-formed, technically sound assessment of the investment and to make sure that it is well-aligned to the business plans of the financial institution." Mr Faz observed that USD 1.2 million has been disbursed so far, with 80 projects complete and another 40 ongoing.

As to why MFIs should invest significant funds in a new IT system, Ignacio Mas, a former leader of CGAP's technology programme and the Deputy Director of the Bill and Melinda Gates Foundation, was quoted as stating that "It's actually really hard to sell the proposition that MFIs need a better IT system," given the high initial capital investment. He added that "Branchless banking offers an entirely new value proposition of why [MFIs] should be upgrading their IT platforms, a real business case based on extra business, extra revenue, not just based on cost." Mr Mas also stated that MFIs "need a new IT system so that they can handle transactions through any store without more branches, more tellers and more cost," thereby overcoming "the inconvenience of not being able to transact in the area where [clients] live and work." Branchless banking also promotes rapid and robust transaction processing, as transaction volumes are not "limited to the number of tellers and how fast they can enter transactions."

AML/CFT: Strengthening Financial Inclusion and Integrity

By Jennifer Isern and Louis de Koker, published by CGAP (Consultative Group to Assist the Poor), August 2009, 12 pages, available at: http://www.cgap.org/gm/document-1.9.37862/FN_56_ENG.pdf

This CGAP Focus Note argues that financial inclusion and an effective financial integrity regime can - and should - be complementary national policy objectives. The recommendations of the Financial Action Task Force (FATF) are the international standard for anti-money laundering and combating the financing of terrorism (AML/CFT) regulation. FATF advises countries and financial institutions to enhance their internal controls to address AML/CFT risks, perform due diligence on all new and existing clients, conduct heightened surveillance of suspicious transactions and report suspect activity to national authorities. But what effect do these measures have on access to financial services for the poor?

The FIRST Initiative funded a five-country study to analyze the effects of AML/CFT regulation on access to finance in Indonesia, Kenya, Mexico, Pakistan and South Africa. It concluded that AML/CFT measures can negatively affect access to, and use of, financial services if the measures are not properly designed.

According to the study, access-friendly AML/CFT controls should be tailored to the specific domestic environment and risks, should only be as tight as the country context requires and should realistically match the capacity of local institutions to carry them out.

While FATF envisions controls that are uniform enough worldwide to prevent displacing ML/FT from one area to another, "It also encourages countries and institutions to focus on people and activities that pose a high risk," says lead author Jennifer Isern. "This means that, in some situations, countries might be able to exclude various financial services for low-income people from AML/CFT regulation."

"Several countries have already successfully designed their AML/CFT laws to minimize adverse effects on financial inclusion as well as promote financial integrity," says Isern. The three countries included in the FIRST survey that had enacted comprehensive AML/CFT regimes - Indonesia, Mexico and South Africa - as well as Pakistan were able to amend their AML/CFT controls according to real risks once initial rules were found to discourage the use and provision of financial services to poor clients.

While inappropriate AML/CFT controls can certainly have a negative effect on the services and client base of these providers, well-designed AML/CFT controls can actually provide them with protection and opportunities. AML/CFT controls can help institutions understand their customers better - allowing them to design and market better products and provide better customer service. Financial services providers also find it easier to engage with other institutions (investors, creditors, etc.) if they manage their AML/CFT controls. AML/CFT controls can also help strengthen an institution's overall anti-fraud controls.

Ultimately, when low-income clients are excluded from formal financial services, the goals of the AML/CFT policy cannot be achieved. "While it's challenging to both increase access to financial services and fight ML/FT, customizing AML/CFT policies to the local context and implementing them sensitively are well worth it in the end," says Isern.

Microinsurance: A Safety Net With Too Many Holes

Published by Knowledge@Wharton, September 2009, 4 pages, available at: http://knowledge.wharton.upenn.edu/article.cfm?articleid=2346

This paper contains a detailed discussion of the challenges facing microinsurance. The article notes that there has been some recent innovation in the microinsurance sector, a market that has experienced relatively slow growth compared to the microfinance sector in general.

A new Bangladeshi product, which involves six NGOs (non-governmental organizations) and Bangladesh-based Pragati Life Insurance Ltd, will include life insurance with some hospitalization coverage. It has an initial target of 26,000 customers and plans to scale up significantly after two years. The coverage will be over three- or five-year terms, relatively short time periods, according to Mosleh Uddin Ahmed, CEO of UK-based Micro Insurance Research Centre (MIRC). Mr Ahmed is in Bangladesh to help launch the project and was quoted as stating that a long tenor would not work "given the precarious incomes of the target market." Another innovative feature of this pilot is that policyholders will receive a refund of life premiums paid in addition to 5 percent of their investment income if they make no claims during the life of the product.

The article notes that innovation is a good way to encourage growth in the placid microinsurance market. Microinsurance has been "a hard sell among the world's poor" partly because of "a lack of understanding of how insurance products work, the poor population's general reticence to part with what little financial resources they have, badly designed products and a shortage of localized risk management knowledge among providers." Mr Ahmed points out that even in Bangladesh, where there are thousands of registered MFIs, only 11 licensed life insurance companies offer microinsurance products.

The article highlights the importance of microinsurance in the current marketplace, where sharp fluctuations in commodity prices and diminishing government support for poorer communities are becoming common. Some commentators believe that "This is an ideal time for microinsurance to work alongside the more established microfinance lending and play a bigger role in alleviating the problem" of poverty. The idea is that "People work themselves out of poverty using microlending," and "Microinsurance helps prevent them from falling back into it," according to Dirk Reinhard, Vice Chairman of the Munich RE Foundation.

Apart from the need for innovation, a key challenge is the need for large volumes to achieve economies of scale. In addition, the "risk relationships" are reversed in microinsurance, a factor which makes the need to secure clients' trust very important. As stated by Craig Churchill, head of the International Labour Organization's Micro Insurance Innovation Facility, "The provider puts up the capital and trusts the customer to pay it back" in microfinance but "in microinsurance, the policyholder pays up front and hopes the provider keeps its promise…." He added that "for a tranche of society that probably has never used - let alone heard of - these insurance products, it's an enormous leap of faith."

Equally important is the need for flexibility and customization, as local risks can vary greatly from one village or trade to the next. An insurer can't simply offer rich-world products at lower prices. Instead a product "really has to be redesigned after assessing what the local needs are."

An initiative launched by Max India Ltd and New York Life, called "Max Vijay," offers insurance and long-term savings for low-income Indians. 70,000 policies have reportedly been sold within the first year of its launch.

A Max Vijay customer fills in a one-page form, provides a proof of identity and pays a minimum enrollment premium ranging from the equivalent of USD 20 to USD 52. Subsequent premiums over the 10 years of the policy are optional and investments are guaranteed. In the case of natural death, the claimant receives the guaranteed sum assured and the account value. In the case of accidental death, the claimant receives the account value and double the amount of sum assured. In addition, Max Life has signed an agreement with a national retail chain, I-SERV, to let policyholders manage their policies at 12,500 of its stores, ensuring its accessibility and easy distribution. It is noted that life insurance is easier to "localize" than health, weather, property, agriculture and catastrophe insurance products. Non-life products typically require more extensive on-the-ground knowledge in terms of not only product design, but also administration and monitoring.

Related to the issue of distribution is the role of NGOs in facilitating insurers' access to remote markets. NGOs tend to be more in touch with the client base and in a better position to understand "what's crucial for their well-being." Partnerships between NGOs, insurers, MFIs and community organisations can be beneficial for all concerned. The article notes that governments can in some cases play an important role, for example by providing "individual ID cards to enable faster customer identification and reduce fraud-detection costs, or providing regional health, livestock and weather databases to collect much-needed data to help insurers develop and monitor products."

Once the microinsurance market becomes more established, the authors expect the sector will face many of the same issues that plague the microfinance market today, "notably questions about whether it is indeed helping to lift people out of poverty."

Financial Access 2009: Measuring Access to Financial Services around the World

Published by CGAP (Consultative Group to Assist the Poor), September 2009, 92 pages available at: http://www2.cgap.org/gm/document-1.9.38735/FA2009.pdf

In seeking to give poor people access to critical financial services, policy makers around the world are often hampered by the lack of information they need to tackle this challenge. There often is little data available to answer basic, but important, questions: Who has access to savings or loan accounts? What kind of institutions do these customers use? Which policies actually help to bring financial services to poor people? How do branchless banking and cell phone transactions increase the reach of services?

This CGAP (Consultative Group to Assist the Poor) report provides global indicators and a range of policy recommendations that can help policy makers and regulators broaden access to financial services for poor people. It draws on information provided by financial regulators in 139 countries and identifies barriers that keep formal banking services restricted to the wealthiest people around the world.

The report indicates that people in emerging markets on average have one quarter the deposits and loans of those in developed countries. This means that many poor people do not have important tools that can help them invest in their businesses, spend more on household items or have the funds to cope with crises.

In addition to confirming the vast gulf in the number of savings and loan accounts between rich and poor countries, the report also notes that remarkably few countries collect comprehensive data relating to financial access, outside the value of accounts in their financial systems.

For example, only 30 of the 139 countries surveyed have data on the number of depositors in their regulated financial systems, and just 27 have data on the number of borrowers.

"A lot of countries are considering financial sector reforms in the wake of the global crisis. This can be a great opportunity to also consider policies to broaden financial access to poor people," says Nataliya Mylenko, lead author of Financial Access 2009. "But without the kind of data in this survey, policy makers would find it extremely challenging to tailor policies to their country's needs."

The report, drawing on a range of estimates and survey results, puts the number of bank accounts worldwide at 6.2 billion, or more than one account for every person on the planet. However, as expected, most of these accounts reside in the world's wealthiest nations: 70 percent of adults in developing countries do not use formal financial services, compared to 20 percent of those in developed countries.

Banking sectors in developing countries often target only the wealthiest in the population, according to the report. Poor people often lack the official forms of identification, credit history or even a physical address to secure the most basic financial services.

Governments can address obstacles these "know your customer" requirements pose by ensuring the level of requirements is proportionate to the size of the accounts and transactions of the poor people in their countries.

They can also facilitate access by channeling more payments to poor people directly to bank accounts, potentially benefiting banks, governments and clients. But out of the 139 countries surveyed, only 40 reported that they encourage or mandate government transfers through the banking system; 14 of these are high-income countries and 10 countries are in Latin America. Few countries in other regions are promoting such transfers.

Banks in some countries are increasingly using agents to deliver some services - predominantly those that allow customers to pay utility bills or make loan repayments or deposits. In Brazil, for example, the number of agents handling financial activities is 10 times the number of actual bank branches. Governments can further promote financial access by removing hurdles financial institutions (including microfinance institutions) face when they want to establish new branches or develop agent networks. On the credit side, borrowers in developing countries rely heavily on unregulated lenders or regulated nonbank financial institutions rather than banks, which once again tend to focus on the wealthier segments of society. This report argues that governments need to address consumer protections and balance them against costs borne by the financial institutions themselves to encourage lenders to make credit available to lower income borrowers.

Governments should throw their support behind the establishment of comprehensive credit information bureaus and adequate consumer protection. In high-income countries and Latin America, where retail credit is more developed, more than 90 percent of countries have consumer protection and disclosure requirements, compared to only half of the countries in South Asia and Africa. Of the countries surveyed, 109 have disclosure requirements on loan interest rates. In all, 47 percent of countries have disclosure requirements rather than usury ceilings, while 30 percent of countries use both.

The authors stress that it is important for regulators and governments to gather more information about the characteristics and behavior of their financial systems. This information will help them design policies that correctly target barriers to poor people accessing financial services and that anticipate future changes in behavior and financial systems.

Finally, governments also need to examine ways to prevent over-indebtedness among borrowers. As some countries consider capping loan interest rates and, in some cases, actual loan amounts, further analysis is needed to assess the effectiveness of these policies.