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Mexico's Independencia Acquires Lenders in Mexico, US

Financiera Independencia, a Mexican microlender reporting the equivalent of USD 703 million in assets, recently announced that it will acquire all of the outstanding shares of Apoyo Economico Familiar, a Mexican provider of unsecured personal loans and insurance with USD 77.6 million in total assets, and purchase a 77-percent ownership stake in Apoyo Financiero Incorporated, a microfinance lender serving the unbanked Latino community in San Francisco, California. The transactions will be financed with Financiera Independencia's cash reserves and existing lines of credit. January 8. 2011

Yes Bank Recalls Over $22m in Loans in India; MFIs Plan Litigation

Amid continuing uncertainty in the Indian microfinance sector, Yes Bank Limited, a private bank based in Mumbai, has reportedly recalled the equivalent of USD 22.2 million in loans it advanced to microfinance institutions (MFIs) Ujjivan Financial Services and Equitas Micro Finance India, asking them to have repaid their outstanding balances to Yes by December 31, 2010. Other microlenders received similar requests, with a representative of Spandana Sphoorty Financial Limited reporting that Yes also raised interest rates on the loans it made to Spandana from 12 percent to 17 percent and cut the term of multiple loans from two years to approximately one year. Several of the affected MFIs, including Spandana, have announced that they will be taking legal action against Yes, arguing that changing the terms of the loans is unjustified because the MFIs have not missed payments on their loans. Some MFIs have, however, requested that other banks postpone the MFIs' repayment schedules by six months. December 27. 2010 and January 5. 2011

Asian Development Bank Launches $250m Microfinance Risk Participation Program

The Asian Development Bank (ADB) recently approved the USD 250 million "Microfinance Risk Participation Program" to increase microfinance lending in its member countries including Bangladesh, Indonesia, Sri Lanka, Thailand and Vietnam. The program will enable ADB to accept up to 50 percent of the default risk of loans disbursed by banks to microfinance institutions. December 22. 2010

FMO Commits $7m to MSME Fund for Sub-Saharan Africa

The Netherlands Development Finance Company (FMO), a Dutch public-private partnership that aims to improve developing economies, has committed USD 7.5 million to the Regional MSME Investment Fund for Sub-Saharan Africa (REGMIFA), a Luxembourg-based fund that currently holds stakes in eight institutions serving micro-, small and medium-sized enterprises (MSMEs) in Africa. REGMIFA was launched in May 2010 by German development bank KfW and the German Ministry for Economic Cooperation and Development (BMZ). December 21. 2010

(For more top stories, please refer to the subscriber edition)

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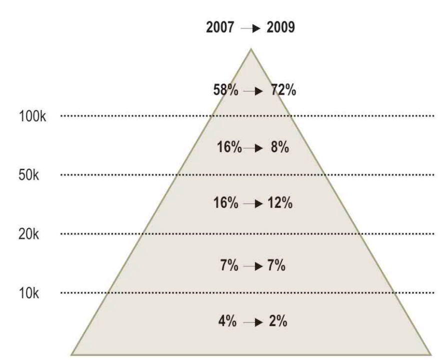
MicroCapital

PHILIPPINES

MFI MARKET SHARE TRENDING 2007 TO 2009 BY MFI SIZE (NUMBER OF ACTIVE BORROWERS)



MARKET INDICATORS*

FIELD NOTES

Ring In the New Year and Wring Out the Backlash: Microcredit Is Not the End; It Is Just the Beginning

I rang in 2010 in this same space asserting that the next "big thing" in microfinance would be the promotion of savings. Shortly after, the Bill and Melinda Gates Foundation announced plans to put USD 38 million toward increasing the capacity of microfinance institutions to offer savings services to poor people. While exciting, this was only the tip of the iceberg. In 2010, the widely read book *Portfolios of the Poor* showed us that poor people can save, despite meager and unstable incomes. Microfinance institutions (MFIs) studying demand reinforced this idea, arguing that more clients need savings than credit. An unscientific review of the institutions reporting to the Microfinance Information Exchange shows that in 2009, borrowers at 537 deposit-taking institutions also represented 55 percent of their total 78 million depositors.

A number of randomized controlled trials or RCTs (considered the "gold standard" in causal evaluation) have begun to show that uptake is high when savings are offered to the poor, even when interest rates are negative. Some studies are showing that savings can lead to greater investment, the empowerment of women and perhaps declines in poverty. The momentum behind this has been huge. In November 2010, the Bill and Melinda Gates Foundation pledged another USD 500 million over five years to expand savings for the poor. Other philanthropic organizations, including the MasterCard Foundation, have put savings on their radar, focusing on youth. Donor institutions such as the International Finance Corporation and the Inter-American Development Bank have also dipped their toes in this area. Even in the US, the City of San Francisco is apparently looking to match students' college savings with the idea that savings can increase enrollment.

The focus on savings has come in tandem with a severe backlash over microcredit, shifting product focus and donor emphasis away from indebting people with low incomes. I would like to suggest, however, that savings alone is a one-legged soldier and put forward four main reasons not to discount the utility of credit.

The first is highlighted in a recent CGAP (Consultative Group to Assist the Poor) paper authored by Glenn Westley and Xavier Martin titled "Making the Case for Microsavings". The business case is laid out well, yet the document shows that - for MFIs ADOPEM in the Dominican Republic and Centenary Bank in Uganda - deposits are not compelling until they are seen as a cross-selling opportunity to draw clients to more profitable microcredit products. Secondly, what of those borrowers who are not borrowing for consumption, but actually to grow their businesses? Can savings alone meet their needs? While Mexico's 80 percent to 100 percent interest rates are hard to repay with the business profits of most microenterprises, in countries where interest rates are more reasonable, credit offers an opportunity to grow a business free of loan sharks. Third, Dale Adams pointed out to me earlier this week that credit is still useful as a "reserve" for unexpected, costly events. Just as people with more money may have credit cards on standby for emergencies, poor people should have access to loans for the same reason. Insurance could help reduce this need somewhat, but its penetration in this segment is still very low. Finally, I still believe that the credit "carrot" remains relevant today. I have been dreaming up ideas of a product supermarket that can leverage the microcredit platform to offer financial services as well as social services such as health, training and others. Credit has shown itself both to draw clients to non-financial services and to finance those services. Until there is an alternative, this is reason enough for me.

About the Author: Ms Barbara Magnoni is President of EA Consultants, a development consulting firm based in New York. She has 15 years of international finance and development experience and has worked with organizations including Goldman Sachs, Chase and BBVA and has advised institutions such as the International Finance Corporation, the US Agency for International Development and the International Labour Organization. She may be reached at +1 212 734 6461 or bmagnoni@eac-global.com.

PAPER WRAP-UPS

Do Multiple Financial Services Enhance the Poverty Outreach of Microfinance Institutions?

By Koen Rossel-Cambier, published by Centre Emile Bernheim and Solvay Brussels School, December 2010, 41 pages, available at: http://www.microfinancegateway.org/p/site/m/template.rc/1.9.49256/

This paper examines the current trend toward product diversification by microfinance institutions (MFIs) and explores whether such diversification leads to greater outreach, in particular when combining microcredit with savings and insurance. It analyzes data from 250 MFIs from Latin America and the Caribbean from fiscal year 2006.

The author argues that if poverty alleviation is the mission of MFIs, then performance should be measured not only by organizational growth, but also by determining whether an MFI's services are relevant and useful to poor people. Social performance assessment is the process by which an organization measures its performance in terms of its social objectives, as well as those of key stakeholders. Various MFI promoters have developed tools to monitor the social performance of MFIs including Imp-Act, the SEEP Network/Argidius Foundation, CGAP (Consultative Group to Assist the Poor), the US Agency for International Development (AID) and ACCION International.

The paper tests three hypotheses: (1) combining multiple financial products enhances the breadth of outreach of MFIs, as measured by the number of people served; (2) combining microfinance products does not enhance outreach to poorer people; and (3) combining financial products can sharpen certain exclusionary gender-sensitive mechanisms.... *(Continued in the subscriber edition)*

Building Social Capital Through Microfinance

By Benjamin Feigenberg, Erica Field and Rohini Pande; Harvard Kennedy School Working Paper no. RWP10- 019; available at: http://dash.harvard.edu/bitstream/handle/1/4449105/Feigenberg_BuildingSocial.pdf?sequence=1

Social capital, defined as "features of social organization, such as trust, norms and networks that can improve the efficiency of society by facilitating coordinated actions," is built up as a result of repeated interpersonal interactions. Yet does accumulated social capital provide a tangible economic return? In this paper, Feigenberg et al argue that the answer is "yes," based on their study of the relationship of group meeting schedules to loan default rates recorded by Indian microlender Village Welfare Society (VWS). The results suggest that building up social capital through the frequent meetings associated with group lending has a statistically significant effect on reducing loan default rates.

The authors selected 110 first-time borrowers and randomly assigned them to groups that met either every week or every month. The loan cycle was 10 months, and each group member was given an individual liability contract, i.e. group members were responsible for repayment of only their own loans. Using a measurement called the "social contact index," the authors measured the amount of social capital accumulated throughout and after the loan cycle. The authors found that a higher level of social contact was associated with borrowers assigned to a weekly meeting schedule, a correlation that continued even after the loan cycle was over; though the increase in social contact was stronger among people with preexisting social ties, such as relatives or neighbors.

Sixty percent of the original study group borrowed again from VWS. The authors studied data on these repeat borrowers to determine whether the social capital built up during first loan cycle had an effect on loan default rates during the second loan cycle. They found that borrowers assigned to a monthly meeting schedule for the first loan cycle were four times more likely to default than were borrowers that had been assigned to a weekly meeting schedule.

To strengthen their argument that it was indeed the increased social contact that lowered the default rate... *(Continued in the subscriber edition)*

Same Game, Different League: What Microfinance Institutions Can Learn From the Large Banks Corporate Governance Debate

By Maria Giovanna Pugliese, published by World Microfinance Forum Geneva, October 2010, 24 pages, available at: http://www.microfinancegateway.org/gm/document-1.9.48253/Same_Game_Different_League.pdf

This paper summarizes lessons that have emerged from the recent corporate governance debate in the banking sector and point out parallels to - and differences from - the microfinance industry.

Many microfinance institutions (MFIs) are currently undergoing a transformation from small, nonprofit, donor-funded social enterprises focused on the provision of “simple” credit products to rapidly growing for-profit corporations, offering a multitude of products to a rapidly changing and increasingly diverse constituency. In the course of these transformations, new stakeholders, such as professional investors, are often brought in to expand an organization’s capital base. As a result, new operational challenges and potential conflicts of interest emerge that require MFIs to adapt their governance structures.

The author identifies five main topics in the contemporary debate on the corporate governance of large banks that have implications for MFIs: role of the board of directors, role of institutional shareholders, risk management, executive remuneration and several others that are addressed as one: transparency, role of external service providers and complex group structures.

The board of directors plays a crucial role as a governance organ in both large banks and MFIs. The responsibility of the board is to define and monitor the execution of the company’s strategy, vision and culture. The current banking crisis has underscored the responsibility of the board for setting strategy, risk profile and risk appetite. A particular challenge for MFIs transitioning to for-profit models is how to articulate a vision and strategy to minimize “mission drift” or departure from core values. To mitigate this risk, the author proposes emphasizing stakeholder multiplicity and the “duty of care” requirement, which is a legal obligation to adhere to a standard of reasonable care while performing any acts that could harm others.

Shareholders play an important role in guiding and monitoring the institutions they own. Investors in MFIs typically invest through specialized funds known as microfinance investment vehicles (MIVs), which increase the separation between organizations and their actual owners. To strengthen the governance role of investors, the author recommends that MIVs and direct investors adopt the United Nations Principles for Responsible Investment, which provide a framework to incorporate environmental, social and corporate governance issues into the practice of investing.

A major facet of contemporary debate centers around the failure of large financial institutions to manage risk appropriately. Traditionally, microfinance institutions have been characterized by tight risk management, as is evidenced by high loan repayment rates. However, as MFIs expand their product offerings and target markets, the risk of default may increase. Also, as MFIs begin to accept funding from external sources, they need to be aware of the risks associated with different sources of financing, such as liquidity risk. The author argues MFI managers should structure appropriate controls around these risks, including, where necessary, the creation of new functions and roles within the organization.

Executive remuneration is receiving a lot of attention in rich countries these days. In corporate banking, executive remuneration is based not only on the wage market but can also be a way to align executives’ personal objectives with... *(Continued in the subscriber edition)*