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MicroCapital Monitor

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OPIC to Guarantee $500m in Loans to SMEs in Egypt, Jordan

The Overseas Private Investment Corporation, a US government agency that supports private sector development, has approved USD 250 million in loan guarantee facilities each for Egypt and Jordan for local banks that lend to microfinance institutions and small and medium-sized enterprises. CHF International and the Middle East Investment Initiative, two US-based nonprofits that promote financial services in developing countries, have been awarded USD 20 million from the US Agency for International Development (AID) to select the local banks and to develop credit standards for the program. AID will also provide technical assistance to the local banks. The guarantees, which are described as "long-term," make up the first part of a USD 2 billion financial support package that was pledged by US Secretary of State Hillary Rodham Clinton during her visit to Egypt and Tunisia in March. July 15. 2011

IDB Commits $10m to Back Building Supply Loans in Latin America

The US-based Inter-American Development Bank has agreed to provide USD 10 million as a partial credit guarantee to Patrimonio Hoy, a microfinance initiative of Mexico-based building materials supplier CEMEX. Patrimonio Hoy, which provides microloans for construction materials, labor and technical building assistance, aims to use the guarantee to reach 750,000 low-income families in Colombia, Costa Rica, the Dominican Republic, Mexico and Nicaragua over the course of five years. Since 2000, Patrimonio Hoy reports having disbursed USD 135 million in loans to 265,000 families. July 4. 2011

FINCA Launches LLC With $74m from IFC, KfW, FMO, responsAbility, Triple Jump

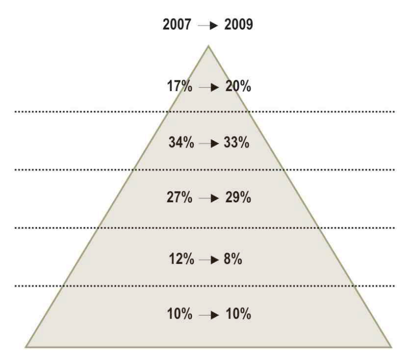
FINCA International, a US-based nonprofit network of microfinance institutions in 21 countries, has established FINCA Microfinance Holdings (FMH) LLC, with investments of USD 35 million from the International Finance Corporation, the private-investment arm of the World Bank Group; USD 15 million from KfW Bankengruppe, a German development bank; the euro-equivalent of USD 14 million from the Netherlands Development Finance Company, a Dutch public-private partnership; USD 5 million from the responsAbility Global Microfinance Fund, a microfinance investment vehicle managed by responsAbility Social Investments AG of Switzerland; and USD 5 million from Triple Jump, a Dutch microfinance investment manager and advisory firm. FMH was established with the goal of approximately doubling FINCA's client base to 1.5 million. FINCA will be the majority shareholder in FMH, and the organization's board will include representatives from the founding investors and others. As of 2009, FINCA reported total assets of USD 467 million. June 24. 2011

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

INSIDE Page

MicroCapital

EUROPE & CENTRAL ASIA
MFI MARKET SHARE TRENDING 2007 TO 2009
BY MFI SIZE (NUMBER OF ACTIVE BORROWERS)



MARKET INDICATORS*

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DEVELOPING WORLD MARKETS

MEET THE BOSS

Judy Kirst-Kolkman, Managing Partner and Head of Fund Management & Administration, and Peter Johnson, Partner and Head of Capital Markets

Judy Kirst-Kolkman and Peter Johnson

Developing World Markets (DWM) is an asset manager and investment bank dedicated to making socially positive investments in order to promote sustainable economic and social development on a global scale. Managing over USD 900 million assets as of March 31, 2011, DWM has invested in more than 140 microfinance institutions (MFIs) in over 40 countries since 2004.

Judy Kirst-Kolkman and Peter Johnson started DWM in 1994. From 1999 to 2004, Judy co-managed, alongside Peter, the DWM I Fund LP, the firm's legacy activity, which participated in approximately 350 IPOs on local stock exchanges. Prior to DWM, she worked in financial management positions for Control Data, 3M Corporation and a real estate development business.

Peter, also a DWM Partner, manages the Capital Markets team. Before co-founding DWM, Peter spent 14 years with Bankers Trust, focused exclusively on emerging markets and opening the company's Egypt office. As an investment banker in London, he restructured Middle Eastern institutional clients' direct investments in Asia, Latin America and Eastern Europe.

MicroCapital: DWM started out managing more traditional emerging markets investments. At what point did you make microfinance the firm's core investment focus?

Peter Johnson: When we started DWM, we managed one of the first emerging markets IPO funds. While not an advertised strategy, we decided that all of the investments we selected would have to meet certain agreed upon socially responsible investment criteria. This was just something we felt strongly about from the outset. But the transition to microfinance really came out of our own philanthropic interests. In 1996, we both became actively involved on the board of Pro Mujer, which provides financial services, healthcare and training to women entrepreneurs in Latin America. Through this initial experience in microfinance, we gained an inside perspective on the financing challenges of MFIs.

In 1999, DWM had a very successful year, so Judy and I decided to use a portion of the business's profits and our investment banking skills to structure the Pro Mujer Loan Fund. Based on our emerging markets experience, we thought this could really work as a funding mechanism, and, well, we found out it did. The now USD 3 million fund is still making loans to Pro Mujer subsidiaries.

We had no idea that this would not only transform our own business but transform the microfinance industry as well. After launching the Pro Mujer Fund, we were approached to structure the first cross-border microfinance securitization instrument in 2004, and we continued to develop the field with additional capital markets transactions in 2005 and 2006 that totaled more than USD 150 million.

Prior to this, microfinance and other social enterprises in the developing world had little or no access to mainstream capital markets. It was at this point that we both just knew that this was the footprint we wanted our business to make, and we have focused on microfinance investments ever since.

MC: What lessons have you learned over 10 years of investing in microfinance?

Judy Kirst-Kolkman: I think one of the most important things we have learned is that not all MFIs are the same. Having invested in over 140, we recognize that there is a wide range of strengths and weaknesses. Due diligence and strong relationship management are the keys to really understanding the organizations that we support in order to provide the most appropriate and sustainable financing solutions.

PJ: That's definitely right. From the beginning, we have been very attuned to the fact that MFIs have a diversity of funding needs across capital structures. To address this, we have developed a portfolio of financing solutions that we are able to offer to our microfinance clients. We provide access to funding through short- and long-term debt, equity and direct capital raises in hard and local currencies. In 2007, DWM structured the first international bond issuance for AccessBank in Azerbaijan, raising USD 25 million. This is definitely something we would like to provide to more institutions in the future, where it would be appropriate. One of the most critical products we offer is funding in local currencies, which provides a much cheaper source of capital for MFIs as compared to funding in euros or US dollars. This is an area I believe that differentiates DWM from similar firms in the microfinance investing space.

From the beginning, we have been very attuned to the fact that MFIs have a diversity of funding needs....

MC: In addition to financial services, what other services do you provide to meet the social elements of your mission?

JKK: Social impact is something we are starting to evaluate much more concretely. Part of our due diligence process is to evaluate and monitor investees on our own social scorecard, which we developed with SNS Asset Management and Oikocredit. It evaluates an MFI's social impact across five areas - outreach and targeting, governance, client benefit and welfare, responsibility to community and staff, and the environment.

Strategic advisory support services is an area around which we have been developing a more coordinated effort as well. For MFIs in which DWM has an equity stake, we provide support to achieve both financial as well as social goals. This requires an experienced in-house team, which we have been building over the past year. Our Operations Manager is regularly working with investees to provide on-the-ground, hands-on technical assistance as needed.

This includes shorter- and longer-term projects in a range of areas, such as human resource development, financial management and capacity building, expansion of products and geographies, risk management and other areas of strategic planning. Our goal is to create added value in our microfinance clients by identifying these opportunities in the origination and post-investment stages.

PJ: I don't think that either Judy or I ever imagined that what we started over 15 years ago would morph and grow this immensely. And the scale that we can now hope to achieve in promoting sustainable development through our company's investments has grown proportionately. So this is an exciting point in DWM's journey, and we are looking forward to see what we can make happen in the next 15 years.

FIELD NOTES

Microinsurance and MFIs…Coverage Against Whose Funeral?

I am back from a week in the Philippines, where I was launching the first study by the Microinsurance Learning and Knowledge (MILK) project on the value of microinsurance for the poor. Microinsurance in the Philippines is quite commonplace and has been growing fast. According to the local department of finance, 59 percent of NGOs and other financial providers targeting low-income people offered microinsurance in 2009. Today, many more of these "delivery channels" are offering microinsurance. This year, rural banks will be allowed to offer insurance directly, which has local players abuzz. Microfinance institutions (MFIs) and rural banks have pretty good profit margins and returns. They've been growing at a solid pace based on their lending business. Why complicate their lives with new products? I suspect there are dual objectives.

The first, of course, is to better serve clients. There seems to be consensus among regulators, insurers and intermediaries in the Philippines that insurance is a good thing for the poor. While hardly a "proven" case (one of the MILK project's goals is to better understand this issue), I was encouraged that a handful of people I visited had benefited from these products. These men and women had been paid claims on funeral and life insurance, which helped them avoid or limit additional borrowing, make new investments and avoid having to beg local authorities for help. One woman's 40-year-old husband died unexpectedly, leaving her with five young children. She had only a low-paying job cleaning a house to fund the entire household budget. As a client of an MFI, she received a funeral and life insurance benefit, which allowed her to pay for most of her husband's funeral costs and pre-pay her eldest son's school fees. It wasn't a perfect solution, but it offered her a bridge while she looked for additional house-cleaning work to support herself and her children as a single parent.

The second reason I believe MFIs and rural banks are attracted to microinsurance is their need to boost returns on their fixed costs. Financial institutions earn commissions on microinsurance and typically require purchase of these products by clients taking out group loans. They can make additional marginal income with almost no effort by using their existing operating structure. This is important because their existing structure is costly. MFIs and banks serving the poor are still quite inefficient by international standards, with operating expenses of the larger institutions hovering between 35 percent and 40 percent. Inefficiency is not the only culprit behind high costs. Weakening credit quality is creeping into the market, and provisioning costs are likely increasing. Lenders face significant competition in urban areas, and there are concerns about client over-indebtedness. The reliance on remittances to repay loans and widespread consumer lending also suggest some risk concentration and vulnerability to macroeconomic risk. Meanwhile, a recently approved credit bureau is still not fully operational.

While microinsurance might provide benefits to lenders on the revenue side of the equation, MFIs and other microlenders seem due for improvements in competitiveness with regards to efficiency, credit-risk management and the development of more appropriate loan products. This will require hard work, transparent pricing and innovation. Slow movers could end up losing out…it may be their funerals rather than their clients' that they need to worry about.

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, or you may follow her on Twitter at BarbaraatEA.

PAPER WRAP-UPS

Foreign Capital Investment in Microfinance: Reassessing Financial and Social Returns

By Xavier Reille, Sarah Forster and Daniel Rozas; published by CGAP (Consultative Group to Assist the Poor); May 2011; 16 pages; available at: http://www.cgap.org/gm/document-1.9.50967/FN71.pdf

This document examines the landscape of foreign investment in microfinance including the financial and social performance of foreign capital in the sector. The analysis includes data from CGAP's "Annual Survey on Foreign Investment" and the Microfinance Information Exchange's Funding Structure Database.

The authors consider the investment landscape within the following three categories:

1) Development finance institutions (DFIs): DFIs provide approximately half of the foreign investment in microfinance, their share having grown from USD 1.7 billion in 2006 to USD 7.5 billion in 2010. The authors conclude that these investments, which are largely hard-currency, fixed-income (debt) instruments, are concentrated in the larger, more established microfinance institutions (MFIs) of Eastern Europe and Central Asia (ECA) and Latin America and the Caribbean (LAC).

2) Institutional investors: Accounting for approximately 30 percent of foreign investment, this group includes a broad range of institutions and funds, including international banks, private equity funds, pension funds and insurance companies. According to the authors, some international banks are now considering offering microfinance products through their own banking networks, thus directly investing in microfinance in local currencies. Others are diversifying their portfolios through investments in agriculture, health and renewable energy. Despite these trrends, the authors argue that opportunities for institutional investors in microfinance are limited by the risk-reward thresholds of these institutions.

3) Retail investors: The authors cite social performance as the primary driving force behind retail investments, which account for approximately 16 percent of foreign investment and are mainly raised through financial cooperatives, such as Oikocredit of the Netherlands, and public placement funds, such as responsAbility Social Investments of Switzerland. The authors state that the growth of retail investments has been hampered by regulations that limit the distribution of microfinance investment funds to retail investors in the US and Europe.

The authors' findings indicate that approximately 50 percent of cross-border investment is channeled through microfinance investment intermediaries, with microfinance investment vehicles (MIVs) comprising most of this volume. The authors argue that competition among asset managers will lead to the consolidation of microfinance asset management firms, thereby bringing down transaction costs and creating efficiency gains for investors and investees.

The authors further examine the financial performance of fixed-income and equity investments, the two main forms of investment in microfinance. Fixed-income agreements, which represent 85 percent of all MIV investment and 70 percent of direct DFI investment, recorded a historic low return of 2.5 percent in 2010. The authors attribute these low returns to: 1) excess supply of and stagnating demand for foreign debt; and 2) lower portfolio quality in some markets leading to higher defaults, thereby necessitating the need for higher loan-loss provisioning. The authors expect returns on fixed-income investments to remain low over the next few years.

Foreign equity, which addresses the lack of risk capital within emerging markets, recorded a compounded annual growth rate of... *(Continued in the subscriber edition)*


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Micro-loans, Insecticide-Treated Bednets and Malaria: Evidence from a Randomized Controlled Trial in Orissa (India)

By Alessandro Tarozzi, Aprajit Mahajan, Brian Blackburn, Dan Kopf, Lakshmi Krishnan and Joanne Young; published by the Center for Microfinance at the Institute for Financial Management and Research; March 2011; 58 pages; available at: http://ifmr.ac.in/cmf/publications/wp/2011/Bednets.pdf

This paper describes the design and results of a randomized controlled trial intended to evaluate the relationship between microcredit and malaria prevention through an experiment conducted in a poor and rural area of Orissa, India. In partnership with Bharat Integrated Social Welfare Agency (BISWA), an Indian nonprofit microfinance institution (MFI), the authors made insecticide-treated bednets (ITNs) available through two schemes and measured the results against a control group that did not receive ITNs. The goals of the study were to test: a) the use of microcredit to promote ITN ownership; b) the impact of ITN usage on the prevention of malaria and anemia; c) the efficacy of prepayment in increasing net re-treatment rates; and d) the difference between charging full price for the ITNs and not charging for them.

A baseline household study was conducted in May and June 2007, wherein the authors randomly sampled BISWA households and collected a variety of household data, including expenditures, individual demographic profiles, health events and relevant costs, and blood samples to measure hemoglobin levels and to test for malaria. The number of pre-existing bednets, along with self-reported usage of those bednets, was also collected.

Mr Tarozzi et al randomly divided 141 villages served by BISWA into three categories: a) a control group, which was not eligible for any interventions; b) a "free" group, in which households were provided complimentary ITNs; and c) and a "microfinance" group, which was sold ITNs and re-treatment packages at unsubsidized prices.

In the "microfinance" group, participants could either pay in cash or borrow the money from BISWA. ITN borrowers were charged the standard BISWA annual interest rate of 20 percent, with a one-year term. Households from the final group were also given the option of prepaying the cost of two future re-treatments of the bednets, although they were also informed that survey personnel would visit the village after six months and one year, at which time the households could pay cash for the re-treatment.

As a first step, Mr Tarozzi et al wanted to test the uptake of ITNs and specifically the differences in usage between the free groups and microfinance groups. In the sample villages, the authors found that 52 percent of households purchased at least one ITN, with the vast majority choosing a BISWA loan contract as their method of payment. In these villages, the average purchase was 2.3 ITNs per household, versus 2.8 ITNs per household in the free distribution group. The authors concluded that the value placed on bednets is dependent upon "past exposure to malaria" and finds "earlier [bednet] usage perhaps associated with higher perceived benefit."

Self-reporting indicated that households in microfinance villages used ITNs more commonly than the control villages, but less frequently than free-distribution villages. In the microfinance villages, Mr Tarozzi et al found that many families used the new ITNs to replace their old, un-treated bednets, with an emphasis on providing higher quality coverage to younger members of the household.

By offering prepaid re-treatment plans, the experiment was designed to test the impact of "sunk-costs," in which prepayment may make households more likely to take advantage of a service in the future. Indeed, the authors found a "remarkable difference" between households in the villages that chose to purchase an ITN along with two prepaid re-treatments and those that waited to decide until... *(Continued in the subscriber edition)*

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