Options for a New Microfinance Promotion Agency

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Preface

The idea of a Microfinance Promotion Agency (MPA) is not new. As the Microcredit Summit *Declaration and Plan of Action* pointed out, "in industrialized countries, there is discussion among funders, policy makers, and practitioners that an organizing entity to manage microfinance funds would be greatly beneficial." In fact, some practitioners have suggested that an MPA is a necessary entity for the continued expansion of the industry. According to Thomas Joseph, "the summit leaves us with no institutions or mechanisms to address this issue, although it is mentioned in the Plan of Action." Serious discussions have also been initiated in the U.S. around the need for a "microenterprise intermediary" which would attempt to mobilize financing, set performance measures for the industry, and move the field to more maturity stages.

Our presumption is that there are not any new brilliant ideas or silver bullets. Indeed, there is an extensive and diverse community of effective organizations and institutions, which is on course to stimulate significant growth in microfinance. We further presume that an opportunity exists to convince the G-20 and the G7/8 to invest significant incremental sums in microfinance. This Options paper explores the nature of those functions worthy of incremental investment. The G-20 and G7/8 are searching for good concrete policy initiatives that also improve the governance of international institutions. There is an opportunity to mobilize the political and financial commitment that will fulfill the development potential of microfinance.

The paper is organized in two parts. The first part describes possible functions for a new Microfinance Promotion Agency. It, in turn, has four sections:

- Information and communications technology development for microfinance institutions
- Training support and development
- Raising capital for the industry
- Rating standards / certification

In the second part, issues of agency parentage and governance are considered. Some preliminary commentary on the potential shareholders, funders and locations for a new agency are offered. In addition, the section suggests several progressive governance features for the new agency's constitution – to ensure that it has state-of-the-art mechanisms to enhance participation, transparency and accountability.

Introduction

Microfinance is widely perceived as an approach with significant further potential for poverty alleviation and economic empowerment. The purpose of this paper is to present a menu of possible functions that an international institution might assume to help achieve that potential. What are the options for mandated activities that might lever an increased contribution of microfinance for development?

The paper is designed for practitioners from the industry, concerned NGOs, and international organizations. It does not recount the dimensions and past contributions of microfinance. It does highlight some parameters of potential growth. One caveat: we cannot over emphasize the diversity and heterogeneity of microfinance institutions and their potential clientele.

Microfinance began alleviating poverty several decades ago when organizations in Latin America, Bangladesh, and other developing nations began testing the notion of lending small amounts to impoverished people (mostly women). By the 1980s, the success of institutions such as ACCION and Grameen prompted many NGOs and International Organizations to provide microfinance services. As more microfinance institutions (MFIs) proved that the poor were reliable borrowers, entrepreneurial, and willing to work hard to escape poverty, the microfinance industry grew to a remarkable 8,000 MFIs in 1999.

The 1997 Microcredit Summit was a salient event. It launched a campaign to provide microfinance services to 100 million of the world's poorest families by 2005. By the end of 1999, Microcredit was already reaching 23.5 million, of which 13.8 million represent the poorest. In the past decade, a number of myths about microfinance were shattered.

The poor have proven that they are credit worthy and can save. There are examples that serving the poor can be sustainable. CEGAP reports that 63 of the world's top MFIs had an average rate of return, after adjusting for inflation and subsidies, of about 2.5% of total assets. For example the Bank Rakyat Indonesia generated a US$178 million profit in 1996 from its UDES programme and Grameen has stopped negotiating for new grants or soft loans since 1995. Given the opportunity to receive a small loan, which can make all the difference between staying poor and working out of poverty, many choose to take the loan and work towards independence.

The critics of micro credit challenge the very idea of putting the poor in debt, and doing it with limited donor funds which could be directed to more urgent concerns, like immunization, food, shelter and childcare. They remark on the increase of domestic violence, prostitution and discrimination towards women who accept loans. Critics point to studies that conclude most of the time men control the money. In contrast, other studies have shown that women's access to funds often reverberates through the entire community. Microfinance can be a vehicle for a variety of desirable social changes, such as gender equity, health care, and education. MFIs and IOs stress that they do not see microcredit itself as *the* solution to poverty, but that other investments in social programs by IOs and national governments are essential for eliminating poverty. MFIs can target the poorest and still become self-sustainable.

Conventional wisdom indicates it is necessary for MFIs to be dependent on government or donor grants, to target the poorest. However, such organizations as the Centre for Agriculture and Rural Development

(CARD), Credito con Educacion Rural (CRECER) and the Foundation for International Community Assistance (FINCA Uganda), prove that self-sufficiency is possible. Case studies of the MFIs, provide empirical evidence that "there is no necessary trade-off between serving large numbers of the poorest households and the attainment of [institutional self-sufficiency] by an MFI." Gibbons and Meehan make the case that if the microfinance community wants to reach large numbers of the poorest, they must become self-sustainable. "We believe that only by pursuing commercially motivated, for-profit strategies will MFIs, particularly those working with the poorest, achieve our primary goal of reducing poverty among truly large numbers of the poor and poorest." Their studies of CARD, CRECER and FINCA Uganda argue that MFIs need to expand their vision for the microfinance industry, moving away from public subsidies, and adopting good banking practices. However, the Asian Development Bank contends that the less-established MFIs lack capacity to leverage funds in commercial markets; are unable to provide a range of products and services compatible with the potential clients' characteristics; do not have an adequate network and delivery mechanism to cost-effectively reach the poorest of the poor, particularly those concentrated in resource-poor areas and areas with low population densities. That is not to say self-sustainability is the preferred model for all MFIs. MFIs can subsidize loans, offering more "affordable" interest rates using donor funds. The difference lies in the ideological approach of the organization, and the environment in which it works.

As "god-parent" for the 8,000+ members of the microfinance community, the MPA would be mandated to aid these institutions in achieving the *Microcredit Summit Declaration*. Current resources fall far short of the billions believed necessary to reach the 100 million poorest by 2005. A United Nations Capital Development Fund (UNCDF) Special Unit for Microfinance (SUM) called for technical backstopping of the existing portfolio of 20 projects that represent US$ 40 million. In 1998, USAID committed $138.4 million worldwide in support of micro-enterprise development activities. In January 2001, the World Bank approved a $151 million loan to the government of Bangladesh for microfinance activities. In the past 10 years, the Inter-American Development Bank invested US$452 million in micro enterprise programs. During the period of implementation of the Micro 2001 program, the Bank will increase its investment in microenterprise development, to the equivalent of US$500 million over five years.

The MPA could act as a powerful magnet for incremental resources, market and promote microfinance, publicize and promote best practices, act as a public utility providing services that are beyond the scale of individual MFIs in areas such as applied technology, training, insurance and guarantees, matchmaking with the private sector, rating standards, certification, and lobbying national governments for favourable tax treatment for MFI access to capital.

The MPA would not reinvent the wheel, but complement the existing efforts of organizations such as CGAP, UNDP, FAO, and UNESCO. Through strong team cohesiveness it could ensure that all MFIs have access to the right skill mix and resources. The MPA's mandate, enhancing resources by an order of magnitude increase through new shareholder investments, must not overshadow its foremost objective of poverty alleviation and empowerment of the poor.

Part One: Possible Roles for a New Microfinance Promotion Agency

1.1 Technological Development

> *…Donors should pay more attention to the process of software development. I find it a bit appalling, in fact, that we go around the world shouting the praises of `sustainability' and `financial/accounting soundness', and in the next breath say in one glib phrase `implement an MIS'. It isn't that simple.….Building high-quality computer software requires an enormous amount of effort, skill tenacity, attention to detail, and MONEY!*
>
> - *Andrew Mainhart, Microfinance Systems Consultant*

The role of information and communication technologies (ICT) in microfinance has become an important topic of discussion among donors and practitioners in the sector. Cost-reducing efficiencies enabled by computerization make it an essential element in any strategy to expand the reach of microfinance services to greater numbers of the world's poorest. Yet practical experience has shown that MFIs wishing to upgrade to automated systems of information management face a myriad of challenges and constraints ranging from high costs and infrastructure problems, to shortages in the human and organizational capacity necessary to effectively implement the new technologies.

An initial review of the field identifies a number of programs and resources available for assisting MFIs with the transition to new technologies. In addition, a variety of software and hardware products aimed specifically at microfinance institutions have emerged on the private market, but there appear to be few evaluation methods, and divergence views over what constitutes best practice in their application.

As such, the purpose of this section is to 1) summarize some of the key issues related to the use of ICT's in microfinance, with a focus on internal information management systems; 2) provide an overview of existing initiatives to support the development of IT systems in microfinance, and 3) suggest some potential functions of a new Microfinance Promotion Agency for supporting ICT development.

Background: the role of technology in sustainable microfinance development

The MFI sector is comprised of thousands of small organisations that serve on average in the range of 500 - 5000 clients each. Institutionally, MFIs can take many forms, including credit and savings co-operatives (credit unions), NGO s that combine a lending program with other development objectives, government institutions created to run loan schemes for a specific target group, i.e. farmers, or sector (housing), and small banks. The heterogeneous nature of MFIs creates barriers to innovation and limits one-size-fits-all technology, however, the last ten years have seen the introduction of numerous new technologies and innovations that have assisted in lowering the risks and the costs of micro lending, enabling financial self-sufficiency for many MFIs.

As MFIs - both new and established - explore strategies for maximizing their reach to new populations of clients, they are discovering that access to well-designed computerized information systems is one catalyst for success.

Case example: The CARD Bank

The experience of the CARD Bank in the Philippines illustrates the interdependence of technology and institutional performance. CARD was established as a non-profit lending program in 1986. It began with a manual information system “supported by an old typewriter and a battery-operated calculator”, and later adopted a computerised spreadsheet program to monitor quarterly results. In 1996, with a client-base of 6,800, CARD made a commitment to reach one half million rural poor. A computerised information system was developed over a two-year period that significantly reduced the burden on staff of manual data recording, processing and reporting. Following the implementation of its new information system, CARD realized rapid growth, reaching 30,000 clients in 2000, with close to 600 new clients being added each month. Since the expansion, it has also achieved financial self-sufficiency. CARD’s innovative program technology is now being adopted by other MFIs in the country, enabling an even larger impact on the rural poor.

Challenges of ICT systems development in the MFI sector

Whether manual, computerised through spreadsheets, or through more advanced software applications, careful attention to implementation and maintenance of a good information system will result in increased data accuracy and processing speeds, better decision-making, and improved productivity for the organisation. The growing attention being given to MIS in microfinance raises the question of what defines a good information system, and of how the managers of MFIs - untrained in advanced computer system design - can determine what system will best serve their particular needs and goals.

Levels of information management

MFIs have two main information systems requirements: the accounting system, which centers on the operational chart of accounts and general ledger, and the portfolio or loan tracking system, which monitors the performance of each product offered by the institution. MFIs usually offer a limited number of products – usually credit or group and/or individual loans. As MFIs take a more progressive approach to customer-service, it is more common to see services like savings and checking accounts, term deposits, and even insurance being added. The diversification of services will have an impact on systems design. In addition, some MFIs maintain data about the client group, usually at the request of external donors seeking to measure the socio-economic impact of their investment.

Most MFIs started out with manual systems of accounting and loan tracking, and for small institutions with 1000 or fewer clients and limited plans for growth, this continues to be the preferred method, given the high costs of computerisation. A second level of MFIs has also developed which uses spread-sheet based systems (Excel or Lotus) for tracking loans, often relying on one or two stand-alone computers located in the main office to enter data collected manually from the field. Users like spreadsheets for the ease with which they can create, alter, and analyze data with a few simple commands, and many MFIs with 10,000 clients or more get by with this level of computerization.

Ultimately, however, as MFIs move to scale up their operations, they recognize the need for much more accurate and comprehensive information than can be provided by a manual or spreadsheet-based system. While easier to understand, these methods are slow, prone to error and corruption, and limited in their ability to consolidate information from multiple branches. For larger institutions, a computerized database enabling prompt reporting, and the expression of complex relationships between large quantities of data, is an essential tool of doing business.

The most challenging characteristic of MFIs for systems and software developers is that though simple in structure, MFIs are individually idiosyncratic. The sector has spawned a range of irregular institutional models without standardised norms or procedures, and has adopted methods of interest and payment calculation that vary widely from village to village or region to region. Many of these variations occur often within the same organisation. There are also differences in currencies, languages, and reporting requirements in different countries, diverse political, economic, and legal operating environments of MFIs.

For all of these reasons, there is no one-size-fits-all approach to automation. Instead, MFIs seeking to upgrade their information systems must choose among three basic options: purchase an off-the-shelf system; modify an existing system; or develop a custom in-house system. A fourth option is to select an off-the-shelf accounting package, but design an in-house portfolio system. This approach has been used quite widely since many accounting packages - ACPAC and General Ledger software are two examples - conform to international standards of accounting, and most portfolio systems, by contrast, have no standards and are unique to the institutions that support them.

Options for system development

Off-the-Shelf systems

The last ten years has seen the emergence of dozens of software applications tailored directly to the unique methodologies of the Microfinance sector. Several of these were developed as in-house MFI systems before appearing for sale on the software market. Examples include MicroBanker, developed by the Food and Agriculture Organisation. MicroBanker is one of the most established and successful Microfinance technologies, with over 35 clients and 1000 installations in 26 countries. Bancosol software, developed by the ACCION affiliate by the same name in Bolivia, and CLAMS, developed by World Relief, were developed to suit the specific needs of their parent MFIs, and efforts to adapt them by other institutions have had only limited success. More recently, new products like eMerge (based in Cape Town), Loan Performer (Kampala), and A-3 Partners MFI Software (Seattle) have appeared which target the sector as a whole by offering a flexible range of options for customisation. In addition to these are the growing number of locally developed systems available in every country, that have the advantage of being designed for the local operating environment, and are available with local technical support.

Custom designs

Limitations in the flexibility in off-the-shelf software packages present many MFIs with the need to hire programmers to custom design certain parts of the information system, or to develop a new one from scratch. This raises further questions about staffing – should the institution develop its internal capacity by hiring in-house programmers, or should it use outside consultants? Scarce numbers of qualified software technicians and managers in developing countries, who will work for MFI salaries, is a major challenge. Locally developed systems are a good option for some MFIs, but risks involved include the instability of new systems, their isolation from industry standards and the product improvement cycles offered by commercial companies; and the long time frame involved in development (often exceeding two years). Almost all of the institutions that opt for custom development report that the costs and demands upon the organisation's resources vastly exceeded their expectations when starting out.

Additional costs and constraints

However the institution decides to proceed, there remain a number of additional decisions to be made that will determine the final cost and performance capabilities of an information system. Some of these depend on factors that are external to the MFI.

- *Network architecture.* The main choices include: a stand-alone computer; peer-to-peer-networks; multiple computers in a server-based local area network (LAN); and a wide area network that connects computers in various locations.
- *Infrastructure.* This refers to the quality of electrical systems at the head office and branch offices; the quality of phone service; availability of affordable Internet access for systems that don't have their own server; building security; ability to control for temperature, humidity, and dust.
- *Extra costs*. MFIs must take into account the expenses involved in upgrades to the work site, i.e. wiring, hardware accessories, security, furnishings, etc.; the cost of insurance and higher utility bills; software licensing fees and maintenance contracts, and extra staff time during the development phase and for training. On average, an MFI is looking at a time frame of 12-24 months for implementation, at a cost of $100,000 or more to modify or develop a new system.
- *Macro issues*. The broader policy environment regulating the supply of information and communication technologies is an additional constraint. There are many factors – from international tariffs, to investment climates, to bandwidth capacities, to the ideological orientation of national governments - that determine what degree of connectivity is possible.

Programs and initiatives to support ICT development in Microfinance

Given the current demands for a rapid scaling up of the microfinance industry, several organisations have begun initiatives to help MFIs acquire ICT resources. These initiatives are primarily being delivered in the form of information and research, technical consultants, and financial assistance. Though modest in scale, together they represent a good first effort at charting a common language of standards and good practise for this new field of development. The following summary of initiatives is based on a relatively superficial scan of the literature, and is not intended to be comprehensive.

Consultative Group to Assist the Poorest (CGAP) Information Systems Services

The CGAP/ World Bank consortium of donor agencies has pioneered some of the most comprehensive services to date for promoting IT development in micro finance. In 1998, CGAP sponsored the publication of *Management Information Systems for Microfinance Institutions* (Waterfield and Ramsing), an excellent resource combining practical information for lay people, along with detailed specifications for database programmers on the unique information components of MFIs. The CGAP Handbook has been successfully used by many MFIs and remains a hallmark document for the field.

CGAP has also established the CGAP Information Systems Services on the its Web site, "a service to assist MFI managers in the process of selecting an IS application that best suits their organisation's needs." The site contains consumer reports on commercially available software applications, a ten-step guide for selecting and implementing software; and a glossary of common information technology terms. Here again, CGAP is leading the way in presenting the most up-to-date knowledge available on the subject in a concise and accessible form. The Consumer Report section of the site is still new, and currently offers evaluations of only three products, however the plan for the future is to continue to add new reports as new products become available.

USAID Micro enterprise Innovation Project

USAID has produced some valuable research and capacity building initiatives for IT development. Most significant was its 1999 publication of *Management Systems for Micro finance: An Evaluation Framework*, by Andrew Mainhart of Development Alternatives, Inc. The *Evaluation Framework* is another excellent tool for assessing the quality of commercial and internally developed information systems. It is widely in use among MFIs, donors, and systems developers, and has been adopted as the primary methodology for CGAP's Consumer Report and Ratings Service.

Coinciding with the publication of the *Evaluation Framework* in March 1999, the Micro enterprises Best Practices Project hosted the first seminar ever on information systems for micro finance, in Washington. The meeting attracted 40 participants from the sector, and provided a benchmark for future networking and co-ordination of knowledge and resources.

UN Capital Development Fund/ UN Development Program – Special Unit on Microfinance (SUM)

The UN Special Unit on Microfinance (SUM) was established in 1997 to coordinate the micro finance activities of the UN. MicroStart, a SUM pilot project developed to support start-up costs of promising micro finance operations, is helping to disseminate best practise knowledge on ICT and other aspects of institutional development through an innovative combination of funding and technical support.

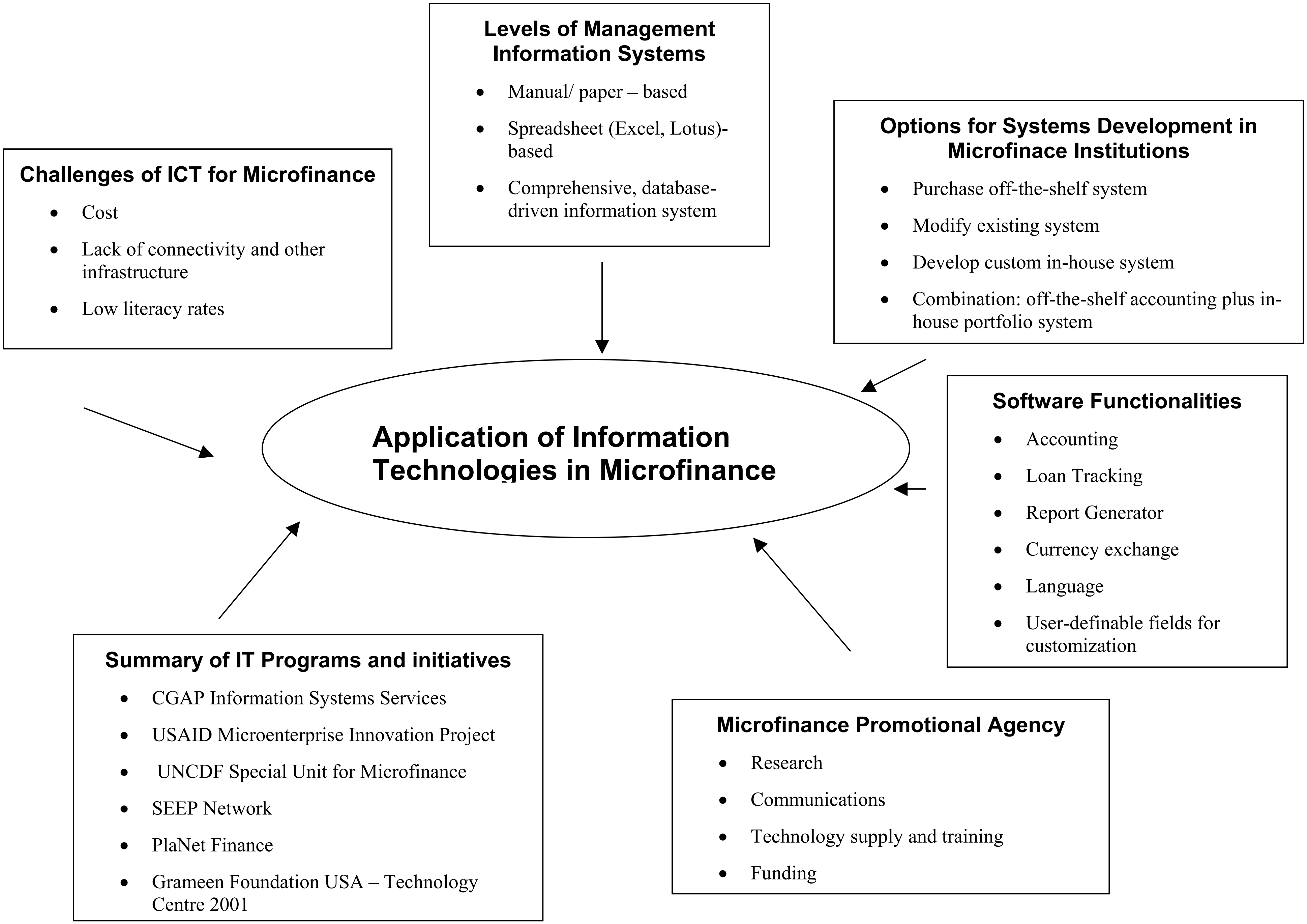
MicroStart aims to build organisational capacity and efficiency during the early planning stages of fledgling institutions, including through the financing of computerised information systems. MicroStart grants consist of two main components:

- A technical services component in which an international best practitioner, preferably southern-based, will provide consultation and technical services to the local recipient organisations;
- A "micro capital" grant of up to $150,000 for investment in fixed assets such as computers and MIS systems, and other overhead costs.

In January 1999, MicroStart had country programs underway in 12 countries with plans to establish 25 in all by the end of that year. Unfortunately, the Web site does not offer any current information on the status of the MicroStart micro capital projects since then.

Small Enterprise Education Program (SEEP) Network

The SEEP Network is an association of 56 North American private and voluntary organizations which support micro and small enterprise programs in the developing world. SEEP's Poverty Lending Working Group, a program representing 237 village banks through its member affiliates, has sponsored seminars and organised innovative research on a range of topics, some of them directly related to information system knowledge and practises. In 1998, after having "witnessed the Microfinance industry struggling with the best way to approach the IS challenge", SEEP collaborated with the Citigroup Foundation to fund ten $50,000 grants for MFIs undertaking institutional development. Five of these were awarded for MIS projects. The experiences of the five grantees – Catholic Relief Services, Katalysis, Pro Mujer, Save the Children, and World Relief – are documented in the Fall 2000 issue of the SEEP newsletter, *Nexus*.



- Diagram 1 -

Technological Development

PlaNet Finance

PlaNet Finance is a virtual institution that uses the Internet as a medium for promoting all aspects of the Microfinance industry. Its PlaNet Systems program offers free web site development and hosting for Microfinance institutions. This appears to be a popular and very effective communications tool for MFIs to present their programs to one another and to a global audience. PlaNet Systems also offers grants of computer equipment to assist its members in getting connected to the Internet.

Grameen Foundation USA

Plans for the launch of a new Technology Centre in 2001 will aim at providing some practical solutions to the problems experienced by MFIs in applying new technologies. It plans to launch new programmes that focus on delivering wireless information technology, such as cell-phones, handheld computers and Internet access. Some of the technologies explored will include

- Wireless Management Information Systems (cell phones, palm pilots) that cut the time needed to process the paperwork of a loan-officer by half
- Cyber Kiosks in rural areas, which will ultimately be administered and maintained by the poor
- Establish joint ventures between MFIs, microfinance programs and major IT companies.

Pride Africa - DrumNet

DrumNet is a recent initiative of Pride Africa, which is helping to facilitate greater access to computerized information networks by small and micro enterprises in Africa. It operates through the use of Info Kiosks located throughout the branch network, which clients can log on to with the use of swipe cards. DrumNet is exemplary of the many innovative ICT applications emerging from the MFI secor that are rapidly building up the technological capacities of developing countries.

Initiatives to Bridge the Digital Divide

A final category of initiatives is worth highlighting. These are the organisations and programs that areassisting developing countries to gain access to information and communications technologies for use in promoting sustainable development. These include International Institute for Communications and Development (IICD); the Network Start-up Resource Centre; the World Bank InfoDev; the USAID Leland Initiative; and the UNDP Sustainable Development Networking Program; all engaged in activities to extend connectivity to the poorest and most isolated regions of the world.

Functions of a new Microfinance Promotion Agency

The preceding overview of technological issues in microfinance suggests an immediate need for research, infrastructure, and expertise in excess of what is currently available. This report's brief scan of the field turned up a total of four publications on computerisation in microfinance, one donor-sponsored Website (CGAP), and two targeted grant programs reaching at most 20-30 organisations over the past two years. There is room for innovation in Microfinance; as such some general suggestions for expediting the development and application of appropriate information technologies and expertise in the microfinance sector are listed below.

Research

The sector would benefit from the creation of a comprehensive database documenting the status of information technologies in microfinance. How many MFIs have adopted technologies and how many are still using manual methods? Where are they? Which institutions, regions and countries are most progressive in facilitating computerisation? What has been the experience of front-line practitioners in developing countries in adapting to new technologies, and what can we learn from them? How do MFIs finance their information systems? What strategies have been successful for attracting funding from donors or investors for IT development? What is the impact on performance of different technological interventions? The MPA could create the foundation for a state-of -the-art knowledge base of the different dimensions of technological development in microfinance.

Communications

The MPA could build upon the communications resources created by CGAP and PlaNet Finance by co-coordinating the expansion of Internet space for housing new data and analysis as it emerges, and for facilitating broad information-sharing among practitioners. The ideal site would include practical tools and resources, access to publications, case studies of IT applications in MFIs, interactive forums, and links to other sites, all of it focused on the topic of information technologies in microfinance.

Technical support/ training

An MPA could certify a directory (or itself support a large field staff) of skilled consultants and project managers to assist MFIs with planning and implementing computerised information systems. The UN SUM MicroStart program has devised an innovative approach that utilizes local experts and advisory teams to guide the technical aspect of institutional development in new MFIs. New kinds of training, tailored directly to the skills required for IT systems development in microfinance, could potentially be delivered on a large scale in different languages and at different sites around the world.

Funding

The MPA can potentially play a central role in raising and channeling funds for IT development in the sector. Financial support can be delivered in the form of direct loans or grants, or through in-kind contributions of services and equipment. In partnership with product designers and vendors, the MPA could potentially become a wholesaler of software and hardware products. It could play an intermediary role in negotiating or administering licensing and maintenance contracts on behalf of MFI, tasks that can be very expensive and time-consuming for small institutions. A specialised IT Grant Facility for Microfinance may have potential for attracting corporate sponsorships from the IT industry.

Advocacy

The Microfinance sector needs assistance with defining and promoting its interests to national governments and the telecommunications industry as a whole. Is there a role for the MPA to lobby for changes? What is the unique mix of communications and technology products and services valued by MFIs in different countries, and how can industry and governments best ensure that these are available to disadvantaged and geographically isolated populations? The MPA can play an important role in working with practitioners at the grassroots level to ensure the inclusion of these issues on the public policy agenda.

1.2 Training Support and Development for Microfinance

Reputable microfinance training programs are currently being offered by several organizations. It is important to build on these programs and make them more accessible, rather than replace them with new programs. Training would be based on fundamental considerations, namely, maintaining a common micro credit language, encouraging best practices, and establishing greater support among stakeholders.

The Microfinance Promotion Agency would encourage continued diversity, recognizing that the success of microcredit has been the rapid and decentralized development of many different models. It may provide its own training, or simply test and support innovative methodologies. Existing material would be exploited, including: software, manuals, publications, videos, audiocassettes, and films.

The MPA could offer support to quality training programs, attempting to fill in the gaps concerning

- promotion of women participants;
- availability of courses in various languages;
- monetary constraints;
- geographical location/transportation;
- local/national/international considerations; and
- re-certification (refresher courses offered at induction, basic, advanced, and specialized levels).

Current programs / training options

Microcredit Summit

During the 1997 Microcredit Summit, a model was developed to determine the *scale and scope* of required microfinance training. It was estimated that 100 million families could be reached with credit for self-employment and other finance and business services. If one field worker can serve 200 borrowers, 500,000 field workers would be needed (assuming a drop-out rate of 15%, the number would increase to 575, 000). The Summit stressed that training and recruitment must include women (at both the field and managerial level), in order to reach female borrowers.

Innovations are necessary; the field of microfinance is in a constant state of evolution. Mechanisms that can capture and transfer new tools and knowledge include:

Mechanisms that can capture and transfer new tools and knowledge include

- Ongoing practitioner exchange through affiliate networks;
- Practitioner exchange across affiliate lines;
- Short-term training opportunities for the quick diffusion of new techniques;
- Documentation that analyzes and describes what is working and why;

- Simple-to-read, practical technical material that help practitioners understand how to implement methods, perform financial analysis, structure and manage portfolios, deliver business development services, and reach the very poor in a cost-effective manner; and
- the use of electronic means of communication for on-line seminars, problem solving, and the rapid exchange of materials.

These considerations focus on the extent of training rather than the training itself, but will be necessary to determine the client-base. The diversity of training needs is considered, and it is recognized that training must be distinct for social entrepreneurs, business executives, field staff and managers. Also, training must be structured to meet the needs of the region in which the training is offered.

USAID w/ SEEP Network

Two Kenyan programs were evaluated by USAID and the SEEP Network and profiled in publications.

Advancing Kenyan Industry through Local Innovation (AKILI) is an organization dedicated to technology development. It offers services that include group training, and use individualized technical assistance. Services aid clients in product development and link them to new markets (after 15 months of training, 85 clients who had participated in this process had increased their income by 35%).

Strengthening Informal Sector Training and Enterprise (SITE) intervenes in the traditional apprenticeship program (most widely used method for skills transfer in Kenya) to shift apprentice training from the transfer of limited skills to innovation, higher quality and greater market responsiveness. The skills of master craftspeople are upgraded through this program, as well as their ability to provide quality training to their apprentices.

Training in these two programs intended to create real tangible benefits (fees that apprentices pay can represent significant income for a master trainer; an improved reputation attracts more paying apprentices). Courses took place as close to the participant's workshops as possible and were held during convenient 'after-hours' to minimize the opportunity costs associated with training.

Grameen Banking

Grameen offers two types of training programs:

- Exposure visit/training - usually offered for one week and is conducted under the supervision of the International Program Department. It begins and ends with a briefing/ review at head office, and involves a field visit. Participants are required to pay US$20/day for training and all other expenses relating to accommodation, and meals.
- Basics Training – is offered for those who wish to replicate the Grameen model, or who are already working along the model (philosophy, accounting, monitoring). This program involves three weeks of intensive training (field and classroom). The cost for this program is $20/day plus all costs associated with accommodation and meals.

Participants may hire a university student who will act as a translator. Grameen will assist with this service, which costs an additional US$20/day. A set of publications is available for students and anyone interested in the Grameen model, for $US25. Course fees are reasonable in comparison to other training programs.

Bank Rakyat Indonesia (BRI) – Visitor Training

USAID and BRI established the International Visitor Program (IVP) in 1996 with a 2-year partnership agreement; in 1999, CGAP signed a partnership agreement. The program is a micro banking service, which offers visitors an opportunity to lean about the success of the BRI unit banking system. It conducts study visit programs, in-class training programs and on-the-job training.

The following programs were offered at BRI:

- Specialized Micro Finance Study Visit – on request, monthly.
- Internal Control for Micro Banking, Human Resources Development Program for Micro Banking, On the Job Training, Specialized Study Visit on BRI Savings – on request for groups of at least 5 people.

The specialized study visit offers training to middle managers, such as Branch Managers and Microfinance practitioners, as well as high level managers. Intensive training focuses on: "How to expand outreach through small MFIs on a non-subsidized, low risk, commercial basis," "How to implement government / Central Bank policy on village owned banks," and "How to develop the mutual benefit of big and small micro finance institutions."

This course offers different training options for various types of clients. Hands-on practical site visits, combined with classroom training appears to give the student a thorough training experience.

Naropa University 2001 Microfinance Training Program

This three-week training program ran in July-August for the 7th consecutive year. The program focuses on best practices and paradigms in program design and management. Essential concepts, analytical tools, experiences and reading provide students with a basic understanding of microfinance. Two sessions were offered this year which are similar in nature. Morning workshops were mandatory, and participant were able to choose from several elective courses each afternoon. Participants were expected to enroll in 8 hours of class per day, and absenteeism was reported to sponsors. One or two hours of 'homework' was required each evening.

Topics this year included:

- Commercial banks in Microfinance - practical issues surrounding mainstreaming of MF within traditional banking institutions)
- The Poor and their Money -developing commercially viable but highly flexible financial services for poor and very poor people in slums and villages
- How Financial Markets and Institutions work - how to create market niches in which microfinance programs can be the providers of excellence, creating debt capacity
- Microcredit and Financial Liberalization - how MF complements other financial sector developments and how the overall evolution of financial policies and markets influences MF
- Microfinance in competitive environment - effects of competition for clients on microfinance institutions

- Developing MFIs to reach the Poor -what factors most affect the achievement of financial sustainability
- Regulation and Supervision - many countries are actively pursuing the creation of specialized MFIs that will have access to funds from the general public and governments through the financial sector
- Microfinance and Public Policy -learn how to use the public arena to advance their institutional interests – roles of major players, politicians, donors, government agencies, and MFIs
- Voluntary Savings Mobilization - collecting voluntary savings from the public etc.,
- Targeting Services to the Very Poor - failure of MFIs to target hard-core poor and identifies the need to focus on risk responsive flexible financial products
- Understanding clients - responding to client demand
- Intro to Microfinance Accounting -basic skills necessary for setting up and understanding accounting systems for MF

Tuition for the 2001 three-week program was US$3700. Participants were responsible for all travel, accommodation and food expenses for the duration of the course.

Faculty includes staff from prominent NGOs. For instance, Consultative Group to Assist the Poorest (CGAP), United States Agency for International Development (USAID), ACCION International, United Nations Capital Development Programme (UNCDP), Save the Children, and Bread for the World. The success of this program is apparent; it is currently in its seventh year of operation. Facilities at Naropa University appear to be excellent.

Access to Microfinance & Improved Implementation of Policy Reform (AMIR) Program

The AMIR Program is a four-year economic opportunities project funded by the U.S. Agency for International Development, implemented in partnership with the Jordanian private sector and various ministries and departments of the Government of Jordan. Its Sustainable Microfinance Training Program (SMTP) is targeted at microfinance practitioners in the Middle East, North Africa region (MENA) and offers participants a basic understanding of microfinance, and supplies students with tools to create and operate a lending program. This program was developed in response to the increased demand for practitioners in Jordan and the MENA region, and seeks to advance the skills of people who are already in the microfinance field. Students include microfinance practitioners, lending institutions, bankers and loan officers, NGO executives and staff, government regulators, economists, and journalists and anyone interested in learning more about the principles of microfinance. Successful students receive certification, which is granted by the Institute of Banking Studies, and recognized by the Jordan Council of Higher Education. Courses run for 8 weeks, with classes 2 or 3 times per week. Courses cost approximately US$700. Course topics include

- basics of microfinance
- identifying, marketing to, and qualifying borrowers
- performance measures

- managing credit risk
- developing Management Information Systems (MIS)

All courses are taught in Arabic. The AMIR curriculum is based on internationally accepted microfinance best practices but is tailored to meet regional needs. Adult learning techniques are employed and involve active discussions, case studies and extensive class participation. All trainers are internationally certified with backgrounds in banking, finance and micro enterprise development. Trainers are native Arabic speakers and have completed intensive training programs.

Microfinance Capacity Building Programme in Africa (AFCAP)

AFCAP is financed by CGAP and the British Department for International Development (BDID). Its training program in Nairobi, Kenya offers a variety of options for organizations.

- Training of Trainers: includes basic modules and more advanced modules that are tailored to meet specific needs of trainers. Approximately 2 days of theory are taught, followed by 3 days of practice delivery to fellow students.
- Basic training topics include: Training Styles, Adult Education and Experiential Learning Cycles, Training Design Consideration, Communication, How Groups Work, and Group Integration.
- Advanced training topics include: Co-training, Feed Back, Learning Styles and the Experiential Learning Cycle, Types of Knowledge and Writing Objectives, Choosing Appropriate Training Activities, Sequencing, Designing Training Materials, and, Physical Space and Visual Arts. Elective courses are also offered in the areas of business planning, MIS and cost allocation.

Programs based on sustainability, especially managing delinquency and setting interest rates, are offered over 3 or 4 days and consider the best practices of these two issues. Distinct programs in Financial Analysis, Accounting, Market Research, and Monitoring are also available.

Participants are videotaped and have the benefit of being critiqued by one another. AFCAP training specialists also critique each participant's performance and suggest areas for improvement. Most of the courses fall between USD350 - 450 per person for one week. AFCAP does not subsidize training costs, but CGAP pays for most of the costs related to course development.

Exchange Program, Microenterprise Best Practices (MBP) Grant Facility, USAID

This division of USAID financially supported exchanges in 1999 between microfinance organizations that are striving to improve their operations. Exchanges occurred with an organization outside of the applicant's network of affiliates or partners, and applicants were expected to articulate a link between their issues, problems or futures plans, indicating what they could learn from the host organization. Linking with peers helped organizations find solutions to problems, share 'know-how' and develop specific technical skills to improve microcredit programs.

Grants ranged from $5,000 – 10,000 and visits were 1-2 weeks. A proposal review committee reviewed applications from legally registered

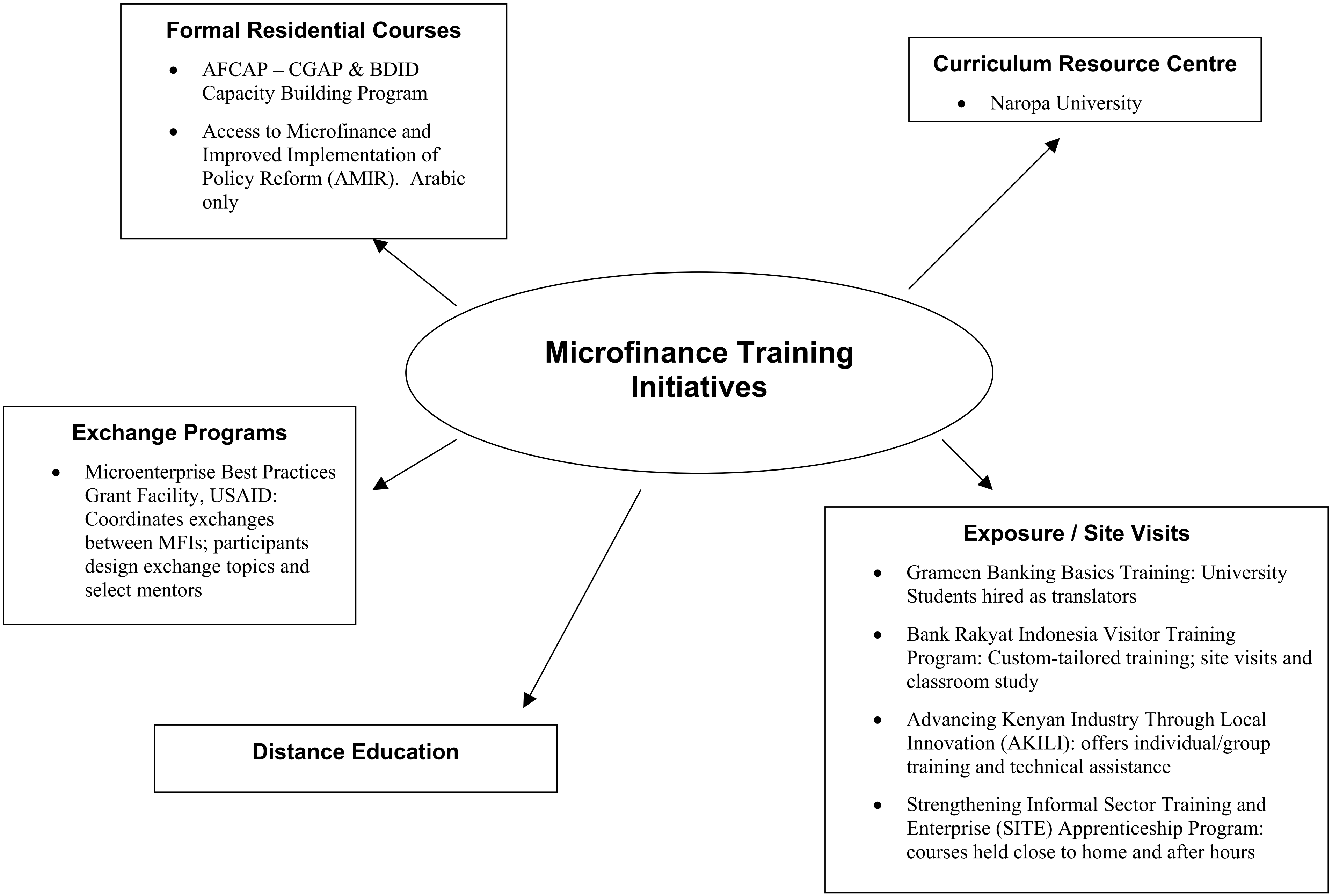
- private voluntary organizations

- non-government organizations
- credit unions
- banks or other specialized financial institutions
- business associations including chambers of commerce
- micro enterprise networks and
- training institutes.

The exchange program covered the costs of transportation and lodging, but applicant organizations were responsible for the cost of participant's salaries, meals and incidental expenses.

Grant recipients were required to track their progress towards original goals and objectives. They provided information to the exchange program in periodic technical reports. Participants were monitored by telephone and site visits.

Participants designed their own exchange topics and selected a mentor or host. Topics included institutional transformation, ownership and governance, lending methodologies, sub sector technology and micro enterprise recycling services.



- Diagram 2 -

Training

1.3 Raising Capital For The Microfinance Industry

Introduction

To achieve the goal of 100 million microfinance users by 2005 the microfinance industry will require significant incremental investments from both traditional and non-traditional sources. The private sector - citizens and corporations – can become donors and sources of financing. Private sector investments must either make economic sense, providing adequate return for risks taken and opportunity foregone, or "social sense," promoting corporate responsibility or a greater good. The MPA could perform any of several functions: Concept Promoter, Lobbyist for Tax Concessions, Donor Information Broker, Retail Promoter, Financial Intermediary, Provider of Private Sector Incentives, Certifier of MNE Sponsorship of MFIs and/or god-parent of APEX Funds. Capital itself will not accomplish the summit goals. Capacity is essential. Some argue it is not possible for the industry to raise the necessary amounts needed for on-lending from the donors and the commercial banks alone. Still others believe capital is not the main constraint to expanding the frontier of microfinance. To the extent that capital is the perceived "bottleneck", the following proposals may be applicable.

Concept promotion

The success of individual MFIs in raising awareness with private donors has been limited; microfinance remains relatively unfamiliar in developed regions.

The MPA could establish itself as a united voice of the industry with a brand name and trademark individuals will recognize and trust. Everyone is familiar with UNICEF: the UNICEF donation box is recognized providing confidence that a donation will support a worthy cause. The MPA could operate as a central contact point for accessing and donating to microfinance. It could undertake large-scale advertising campaigns to educate the public about microfinance and provide centralized fundraising mechanisms. The MPA could undertake large-scale multinational fundraising programs similar to World Vision's Child Sponsorship and 30 Hour Famine programs. The MPA could lend its trademarks to the fundraising activities of approved wholesale organizations as a means of legitimizing individual fundraising efforts. It could publish the benefits of microfinance. The Foundation for International Community Assistance (FINCA) posts the benefit of donations; for example, a donor to FINCA knows that for $75 they will provide a first loan to a micro-entrepreneur. The MPA could be a central information center. In addition, the MPA could promote regions of special need. When a natural disaster strikes and MFIs are at risk of collapse, donors could be notified and capital for this region can be solicited. The MPA could link banks and existing MFIs to encourage the development of new services. Commercial banks are experts in this field and can assist NGOs with micro lending activities to advance into full service financial institutions for the poor. Standard Bank of South Africa's E-Plan is an example of a commercial bank successfully servicing the poor.

Lobbying governments re tax treatment

The MPA could project a united voice lobbying governments to reform regulations to improve the microfinance industry. There is some debate about the "appropriateness" of intergovernmental organizations addressing national tax policies. The MPA could lobby governments for policy change at the request of individual MFIs and represent the industry within intergovernmental organizations. Some examples follow.

Tax-free profits

In Holland, all profits from investments in government approved "green" projects are tax-free. There was such an explosion of interest that Rabobank, the first Dutch bank to launch a green investment fund, was unable to meet the demand. The government has since broadened the scope of green projects and mandated that only 70% of the investment funds must be green. Postbank, Holland's largest retail bank is launching Postbank Green to offer fixed interest, soft loans to green projects and offer investors a lower return on their savings. The investors take advantage of the tax-free status to earn market returns and the bank passes the benefit of the tax on to the borrowers. The Triodos bank offers Individual Savings Accounts (ISA's) in the United Kingdom. The ISA's are a typical mutual fund but invest only in socially responsible investments. Funds of this type could receive a tax-exempt income status or offer a deferral of tax on profits until the money is withdrawn.

Unified tax treatment

Charitable tax deductions are not currently available to most individuals who donate to a foreign charity. If tax treaties were changed to allow foreign donations, MFIs in developing nations could have unprecedented access to charitable resources. Alternatively, the MPA could establish a charitable entity in all countries, perhaps on the model of the Grameen Trust. Money directed to a foreign MFI could be donated to the MPA and a tax receipt issued.

Interest related tax deductions

The MPA could lobby governments to allow for a tax deduction for the interest investors forgo when purchasing a soft bond. The governments could set a benchmark market rate and the difference in value between the soft rate and the market rate would be a tax-deductible donation. Alternatively, the MPA could encourage the use of bonds where a lender donates the interest received to the MFI as a tax-deductible donation. If an MFI or a wholesaler of funds sold such bonds, the wholesaler would in effect be receiving interest free capital; the benefit of which will be passed on to MFIs or used to cover operating costs. The Shared Interest Society currently allows depositors to waive the interest from their investments.

Donor Information Broker

Accessing specific MFIs

Individuals may be more willing to donate if they can be guaranteed the funds will be directed to a region or cause that is important to them. Unless an MFI is large enough to solicit donations directly through the Internet or private fundraising activities they are reliant on wholesalers to collect private funds for them. Private donors are inherently suspicious of contributing to unknown blanket organizations, the funds may be spent on administration and staffing or targeted at causes that the donor is not interested in. The Federation of Agricultural Savings and Credit Unions (FECECAM), Benin's "patriot loans" are a time-deposit product aimed at individuals, immigrant associations or institutions who wish to save, often to invest in their region of origin, at below market rates.

Donor connection with investment

Where an investment is undertaken for a minimal financial return for a broader social purpose, it is important that the social benefits are highlighted so donors have some sense of what they have accomplished. Child sponsorship agencies do this particularly well. Each month, millions of dollars are donated; in exchange the organization provides the donor with periodic hand written letters from the child that the donation has helped. The donor feels a personal involvement in the donation and receives a sense of fulfillment that obligates them to the continued support. The MPA could assume the role of disseminating information to contributors about how their contribution has helped a village or a specific person. Opportunities International Trust Bank shareholder program issues each donor a personalized Shareholders Portfolio that includes photographs of the Trust Bank, the neighborhood and the family being helped. New reports, photos and stories are mailed four times a year.

Unconventional retail promotion

On line marketplace

The MPA could support online marketplaces where MFIs raise money by selling the products of micro-enterprises. Traidcraft imports and distributes handicrafts, fashion goods, stationery, beverages and foods sourced in the developing world. While Traidcraft imports and distributes the goods, the role of the MPA should be limited to a resource provider. MFIs could supply and distribute the goods or provide services to facilitate micro-entrepreneur involvement.

Alternative payment options

MFIs can reduce the risk of exchange rate fluctuations when borrowing from foreign individuals by repaying the interest with the products of borrowers. The MPA could create an alternative monetary system much like a frequent flyer loyalty program. Lenders could receive points instead of monetary interest. Points could be redeemed to purchase goods from MFIs. Lenders receive an item of value equal to a fair market return on their investment.

Financial sector intermediary

Facilitate bank participation

A number of commercial banks have successfully integrated microfinance portfolios into their existing operations. The MPA could disseminate this experience to banks contemplating a microfinance initiative. Training and consulting services could be provided to counter perceptions of Micro-finance as high risk and expensive, and break down socioeconomic and cultural barriers between bankers and micro-entrepreneurs. During the 1970s in India there was a requirement that national banks must lend 1% of the portfolio to the poor, is there a similar mechanism applicable to current microfinance practice?

Ngo-bank joint ventures

Calmeadow has proposed the creation of a new, independent, non-profit organization that would be run as a joint venture by Calmeadow and a financial institution. The financial institution would handle back office and treasury functions, provide loan capital and fund the capital costs of the new entity. Calmeadow would find, screen, and support clients and handle delinquency matters. The MPA could play a facilitative, matchmaking role in establishing such joint ventures.

Direct deposit to micro-finance institutions

Savings mobilization is beneficial to the sustainability of any financial institution. With current advances in telephone and Internet banking, the MPA could support development of a system similar to the Triodos bank's arrangement where residents of the UK can deposit or transfer savings to their ISA through any financial institution. The banks have the right to charge for the transfers but rarely do. MFIs could have access to large quantities of low interest funds where the financial costs and inconvenience to the donor is minimal. The MPA could create an MFI deposit insurance mechanism or subsidize an existing insurance scheme.

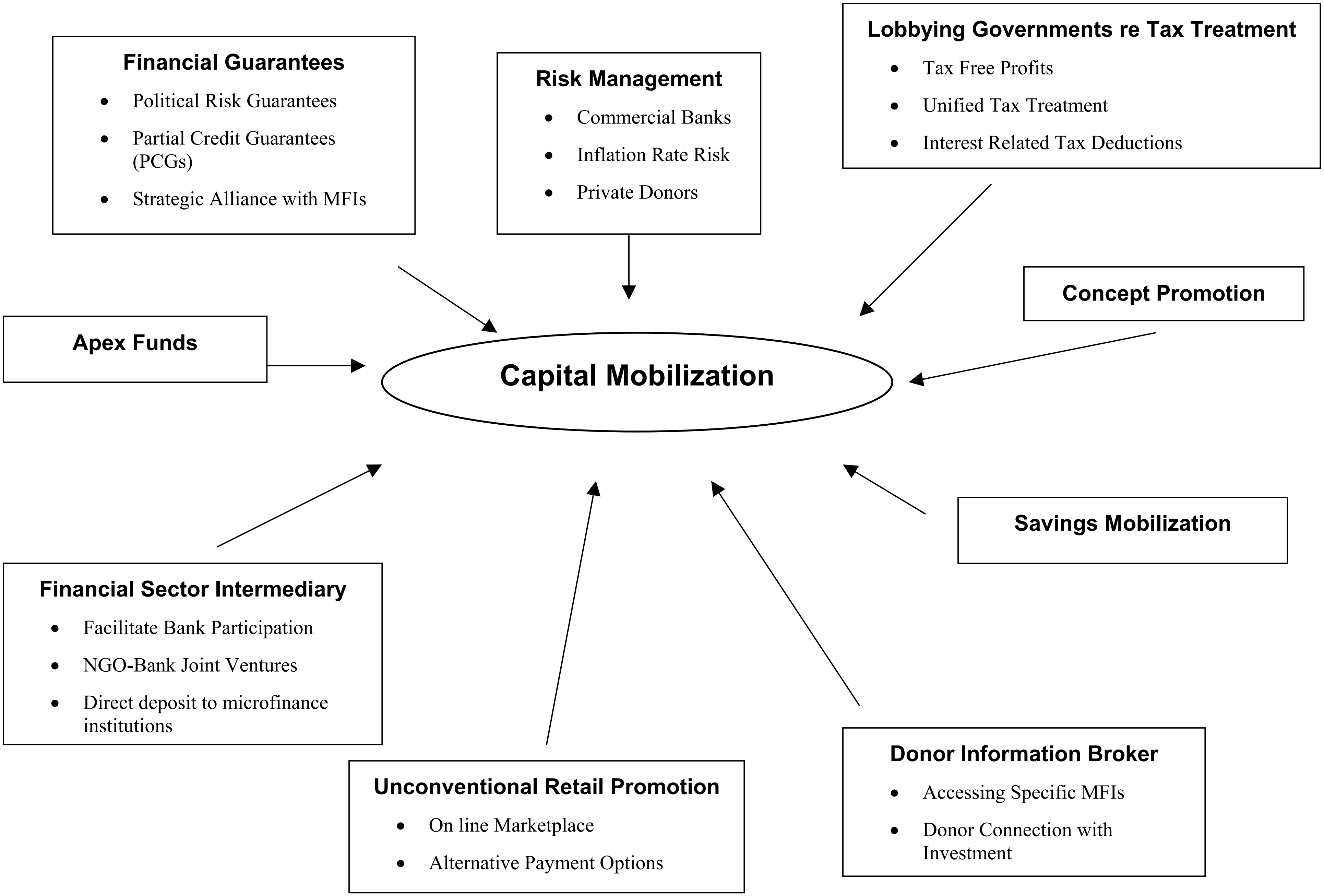
Savings mobilization

Access to savings services can play a critical role in sustainable development by buffering users from crises enabling them to meet basic needs, and by mitigating local economic fluctuations. Despite this, the poor rarely have access to voluntary banking services. Lacking alternatives, the poor are forced to save in the informal sector. They invest in livestock, hide cash at home, and participate in rotating savings and credit associations. The magnitude of the informal sector attests to a demand for services and the scope of "underbanking". Savings can contribute to financial sustainability in an MFI. As a stable capital base, savings mobilization can decrease MFIs from dependence on donor funds, government subsidies and external credit.

Savings mobilization is challenging. It requires accountable governance, strong asset management, flexible savings products, an enabling legal and regulatory environment, and sophisticated management and staff. Most MFIs and donors find this challenging. Donor support of savings mobilization can only be justified by the even higher risk to poor people's savings in the informal sector into which they are forced in the absence of formal or semi-formal alternatives. One cannot assume that the informal sector offers no interest at all. The informal sector can provide superior protection from inflation and profit from livestock can outweigh often-minimal deposit rates of interest. In the case of CVECA banks in the Pays Dogon, where savings are free and a voluntary survey of clients revealed that deposit services are attractive, only 13% of members use the service because livestock is felt to be more profitable. Credit services actually promote the informal sector - to the benefit of the poorest - by offering liquidity while the animals grow to a marketable size.

There is no one-size-fits-all answer to savings mobilization; the onus is on the MFI to align its capabilities with the demands of the clientele. Donors must support the choices made. To recommend standardized features of deposit programmes is to overlook the diversity inherent in microfinance. Deposit services must be sensitive to the reality that the poorest are often illiterate and deposit small sums of often torn and dirty notes. Access is essential. However, it cannot be said that the absence of voluntary savings, "lotteries" and real rates of return will necessarily restrict the success of a deposit programme.

Unequivocally, the primary purpose of savings mobilization is the preservation of the wealth of the poorest. If a deposit-taking MFI fails it could destroy thousands of families and harm the reputation of the industry. Effective supervision is needed. Central regulators could enforce accounting principles, minimum capital requirements and provision policies but typically lack the capacity to monitor MFIs. Donors must ensure external mechanisms are sound but investment in self-regulation and efficient internal control are of equal importance. Donors should support savings mobilization only if they can retain the in-house expertise needed to undertake long-term commitments to strong human resource development and infrastructure transformation. In the short-term donors must commit to the development of savings technologies that better meet the needs of very poor and remote clients.



- Diagram 3 -

Capital Mobilization

The infrastructure of existing commercial institutions could be well suited to reaching the poor but the poorest are rarely prioritized in banking. MFIs work directly with the poorest but often are not legally enabled to mobilize deposits. MFIs can provide clients with voluntary savings services without intermediating savings by depositing mobilized savings in a regulated institution, organizing self-help groups, or facilitating linkages between clients and formal financial institutions.

Supporting institutions to mobilize savings is a high-risk and serious business for which few donors are equipped. While some concern has been expressed about the costs of mobilizing small and microsavings, appropriately designed savings products and effective incentive mechanisms can make microsavings sustainable. Where an MFI chooses to provide deposit services the MPA could provide facilitate the transition by removing barriers. Savings mobilization could challenge all facets of the MPA. Training is a priority. Advocating regulatory changes from government and alliances with private banks could assist savings mobilization. Multilateral deposit insurance for the poorest is another possibility. Ratings and accreditation could build the confidence of savers. Investment in new technology to increase accessibility is needed. In the future lessons learned and infrastructure could be used to address a need for insurance and investment facilities by the poorest.

Risk management

Commercial banks

Guarantees are a way for donor agencies and institutions to make efficient use of limited resources by stimulating a flow of credit from financial markets into microfinance programs. Individual and portfolio guarantees have experienced limited success in increasing lending in microfinance. Intermediary guarantee models, such as Luxmint MicroBank's and ACCION International's Latin America Bridge Fund have been adapted especially for the microfinance sector. Under this model, micro-entrepreneurs are separated from the bank's normal risk/transaction costs, which are handled by a specialized lending organization that acts as an intermediary between the bank and the borrower. An intermediary organization undertakes the appraisal, approval, monitoring, and supervising roles separate the borrower from the bank's normal transaction costs. The MPA could play a valuable role promoting guarantee funds and mechanisms.

Inflation rate risk

MFIs sometimes operate in an environment with unpredictable inflation and devaluation risks. The MPA could alleviate exchange rate risk by creating or subsidizing an insurance fund. Financial institutions could then be in a position to guarantee a real rate of return on loans to MFIs. While the costs of the insurance premium could be passed on to the MFI and ultimately their borrowers, the costs could be justified by access to hitherto inaccessible sources of credit.

Private donors

Individuals desire insulation from the risk of deterioration of capital. Shared Interest's new zero-interest Microcredit Bond is backed by an optional guarantee from the Co-operative Bank. The MPA could organize a central fund specifically to guarantee bond issues from MFIs or it could sponsor organizations to guarantee bonds.

Where foreign individuals deposit funds or purchase bonds it is important that the MFI is protected from exchange rate fluctuation. The risk of exchange rate fluctuation is a barrier. Grameen Trust issues loans to MFIs in local currency and bears the exchange rate risk and subsidizes this service by benefiting from positive exchange rate changes. The MPA could play the role of a deposit intermediary. When an individual deposits funds into a foreign MFI, the intermediary issues the account and deposits the funds in the MFIs local currency. The intermediary bears the burden of exchange rate fluctuations. A diversified intermediary could insulate both the MFI and the individual.

Financial guarantees

The Asian Development Bank's (ADB) Private Sectors Group is an important catalyst for serving the poor. The presence of an established multilateral institution provides a certain level of comfort to the private sectors looking to invest in a developing nation. ADB support of a project is a stamp of approval valued by both government and investors. In addition, the ADB provides a variety of services with regards to the investment. The MPA could emulate several successful ADB programs. The ADB enters Complimentary Financing Schemes where the ADB acts as a "lender of record" on behalf of commercial co-financiers. The ADB arranges for a private sector financier to lend to the developer. The banks cannot turn to the ADB for debt servicing but do enjoy the ADB exemption from withholding taxes, and preferred creditor status in other words, enhanced protection from sovereign risk.

The ADB also offers two guarantee products to private investors for fees charged to either the borrow or the lender:

1. Political Risk Guarantees. Investors receive protection from non-payment due to a variety of government actions such as:
    - Breach of contract by a government entity;
    - Expropriation and nationalization;
    - Currency inconvertibility and non-transfer;
    - Political violence.
2. Partial Credit Guarantees (PCG's). Designed to cover the portion of the debt service that falls due beyond the normal tenure of loans available from a commercial lender they are generally used for projects that need long-term funds to be financially viable. PCG's are comprehensive; they cover both principal and interest for those maturities that cannot be obtained by commercial lenders without credit enhancement. The PCG's can be adapted to cover local currency debt, including domestic bond issues or long-term loans from local financial institutions to meet currency-matching requirements.

Strategic alliance with MFIs

Today, corporations are judged not only on their ability to produce quality products, but also on their stewardship of the environment, their ethical business practices and, increasingly, on their responsibility toward the communities in which they operate. Public acknowledgement of anti-poverty work is good for a corporation's bottom line.

Corporations can play a major role in the reduction of poverty when working directly with MFIs. For example, Opportunity International has launched a micro-loan program using Nike working capital that is targeted at an area of Jakarta where many people have lost jobs as a result of the economic downturn. Nike also reports that in May 1998 they committed to providing small business loans to women in Vietnam and three other Asian countries. The program has been expanded, through the Vietnam Women's

Union and the Colorado-based NGO Friendship Bridge to also include workers who lost jobs. To date, more than 2,300 rural women and former workers have created small businesses in Vietnam. The Nike website reports investigating a microfinance program in Pakistan, but to date has not come to a resolution as to a partner or program.

The MPA could play a vital role in the endorsement of corporate based projects. An MPA corporate relations department could inform corporations about the microfinance industry, train corporate officers about how to become involved with MFIs, what they should look for in a partner or program and how the corporation will benefit from the activity. The MPA could play a lobbyist role, seek out and propose alliances with corporations on behalf of individual MFIs. The MPA could advise on financial, cultural or language barriers, which inhibit the formation of alliances.

Apex funds

"It is very important that global a Microcredit Wholesale Fund be created to support and work through ONLY the local Wholesale Microcredit Funds." *Muhammad Yunus, Grameen Bank*

The global promotion of microfinance through a central institution may risk too much uniformity of approach, at the expense of local adaptation and institutional autonomy. To ensure priority of the poorest, local capacity must be built to support grassroots microfinance programs. Dr. Muhammad Yunus advocates the creation of regional, national, provincial or district level non-governmental wholesalers of microcredit funds (MCFs).

In his paper for the Microcredit Summit Campaign, Dr. S. Ahmed advocates the creation of apex funds as the preferred mechanism for channeling funds to microfinance institutions. Current efforts to deliver funds have proven inefficient; some estimate that about 10% to 25% of donor funds actually reach the poorest, while the rest is spent on administration, overhead, training, institution building and consultants. In contrast, the Palli Karma Sahayak Foundation (PKSF) mobilized US $522.4 million through its partner MFIs at an overhead cost of only 5.47%. One goal of the MPA could be to create apex funds that remain close to the grass roots while delivering funding to the poor and poorest without substantial leakage.

Benedict Kanu, Senior Economist at the African Development Bank supports further expansion of apex funds, stating "..it would be necessary for a micro credit fund to support the establishment of a network of local and field offices through which the fund would operate…. [T]he branches should be decentralized to branch managers with regards to project appraisal, grant, and application assistance to entrepreneurs."

Apex organizations have been criticized for a poor success rate. The PKSF is cited as the exception. However, Dr. Ahmed argues that the PKSF is different because it was created with the intention of becoming an apex and designed to be self-sustainable, with several pre-conditions identified as critical to success.

The MPA could work to ensure the existence of these pre-conditions and create a network of apex funds to distribute financial resources. The MPA could encourage the creation of new funds or support the expansion of existing ones. The MPA could ensure each fund is free from political interference and bureaucracy through a standardization and accreditation process. The MPA could promote the involvement of government, civil society and private sectors while taking steps to ensure the autonomy of the funds. The apex funds could become the primary vehicle to disseminate best practices and new technologies.

1.4 Rating Standards and Certification

Rating standards and certification

MFIs face a distinct challenge when trying to encourage prospective donors and financial markets to back their activities. Although evaluations and assessments are available to MFIs from credible agencies, these tend to be expensive, and lack a common standard that can be applied to the entire industry. Most of the evaluations have not been made public, leaving the methodology and/or results unknown to other potentially interested parties. What is required is a credit rating system that takes into account the nuances of the field, and sends a clear signal to donors and investors of their sustainability. This section discusses the elements that are required for the operation of an effective credit rating standard, and also identifies the best practices related to MFIs.

Ratings, common performance standards, and benchmarking in the microfinance industry, will become increasingly important. First, performance standards contribute to raising the quality and efficiency of MFIs and provide confidence and security for private investors. Second, in competitive environments where there is pressure to commercialize microfinance, regulators view ratings and standards as a way to separate 'mediocre' from 'star' performing institutions. Third, donors are interested in setting performance standards to provide clear benchmarks and guidelines to determine future funding for MFIs. In this context, performance standards can be useful in promoting independent and transparent review of MFIs that should enhance prospects for the growth and capacities of MFIs.

There are two basic approaches that the MPA may take to promote the creation of an industry wide credit rating standard. The first is to take up the function of a credit rating agency itself, establishing a methodology and assembling a team of professionals experienced in the ratings and performance measurement industry. The second option is for the MPA to establish a rating and assessment fund, providing partial financing of rating and assessment services by reputable agencies with experience in the field. Both options would aim for transparent results, fully open to public scrutiny. They also would be structured to considerably lower the costs for MFIs willing to undergo such a rating assessment.

Any successful attempt to promote a transparent, industry-wide credit rating standard would need to focus on a number of crucial elements. The task of the MPA is to decide how to "flesh out" these elements, and provide a suitable methodology that will prove attractive to MFIs and financial backers alike. Either these elements can be set down as the rules used for an in-house credit rating system within the MPA, or as the criteria MFIs and rating agencies need to meet to be eligible to draw from an MPA assessment fund.

A common understanding on the reporting, measurement, and evaluation of MFI performance has not been reached – no surprise given the diversity of providers. Efforts in place to develop rating and certification systems include:

1. PEARLS Rating System. Developed for credit unions by the World Council of Credit Unions (WOCCU), this rating system includes a certification process called Finance Organization Achieving Certified Credit Union Standards (FOCCUS).

2. ACCION Camel. The evaluation guideline for MFIs developed by ACCION International.

3. Girafe Rating System. Developed by PlaNetFinance.

4. MicroRate. Developed by Damian von Stauffenberg of MicroRate.

5. M-CRIL rating system. Developed by EDA Rural Systems (India).

6. MicroBanking Bulletin/ MicroBanking Standards Project. Funded by CGAP.

7. CGAP Microfinace Rating and Assessment Fund.

8. The Philippine Coalition for Microfinance Standards. Developed to serve as guidelines or benchmarks to assess the operations of Philippine NGOs involved in microfinance.

9. Institutional Performance Standards and Plans. Developed by the Committee of Donor Agencies for Small Enterprise Development and Donor's Working Group on Financial Sector Development, United Nations Capital Development Fund.

10. Women's World Banking Microfinance Performance Indicators and Standards.

As these ratings systems indicate, there is extensive experience in selecting, collecting, evaluating, and monitoring the performance indicators of microfinance providers. The basis exists for the establishment of an MFI Certification program.

The MPA could conduct preliminary work in drawing from the experiences and initiatives of other organizations both at a national and regional level to establish performance standards for MFIs. Such work would contribute to building a database from which the MPA could then launch a Certification program for MFIs. The section reviews various options from which the MPA can select performance standards.

Developing microfinance standards involves identifying a minimum set of performance indicators. Relevance and verifiability are important considerations in the choice of indicators. Availability of data is a major constraint particularly for institutions that do not have adequate information systems.

Before acceptable performance standards can be established, MFIs must ensure first that they have a system of adequate internal controls in order to track progress and identify potential problem areas in credit, liquidity, interest rate, operations, and fraud. The MicroFinance Network's Improving Internal Control project is developing a practical manual to guide MFIs through the process of assessing their risk management strategies and improving their internal control systems.

Most often indicators identified in setting performance standards are derived from financial statements. In this regard, financial reporting has to be regular and must conform to standard conventions of accounting. In cases where microfinance operations are not separately treated or reported, adjustments must be made in order to arrive at a more accurate data set. The process of developing standards involves building a database necessary for benchmarking and standards setting, consultations, and consensus building.

MFIs may need to receive training to enhance their ability to collect and manage performance indicators. This service can be provided in a variety of ways, including teaching networks to collect, adjust, and report data at the local level, and providing customized data analysis to compare MFIs.

The MPA could help shape the microfinance industry by reaching consensus on performance standards and launching a Certification program for MFIs. It would seek agreement on common terminology on performance standards and criteria so that they can be uniformly understood and applied. The MPA would need to minimize the burden of collection and evaluation of data. Collecting, compiling, and analyzing outcomes would require a specific set of skills that are generally not one of the core competencies of an MFI; these activities are also time-consuming and costly. There would be a need to encourage MFIs to maintain and continually adapt complex Management Information Systems. The MPA could provide training to MFIs to enhance their ability to collect and manage performance indicators. The MPA could provide technical assistance for MFIs that do not qualify for certification.

The MPA could be involved with increasing public awareness of the proposed standards. The development of an MFI Certification program by the MPA would encourage MFIs to maintain high standards in their operations and would contribute to building infrastructure critical to the development of the microfinance industry.

As an adjunct to the MPA's Credit Rating System, an Impact Assessment Rating can be established (see Annex 1). This can serve as an indicator of how well an MFI is able to contribute to the increase in living conditions for its clients, especially the most destitute. Like the Credit Rating, it can either be conducted directly by the MPA or run as a fund from which those organizations or individuals meeting certain guidelines, and with experience in the field, may be eligible to draw from. A good impact rating would serve as an indicator of an MFIs future financial sustainability, showing its ability to transform the most destitute people of a community into new, dedicated clients.

Microfinance Certification & Performance Standards

Best Practices

- PEARLS Rating System
- ACCION CAMEL
- GIRAFE
- PlaNet Rating System
- MicroRate
- MicroBanking Bulletin Standards Project
- Philippine Coalition for Microfinance Standards
- CGAP Microfinance Rating and Assessment Fund
- Women's World Banking

Possible Activities for MPA

- Develop common understanding on reporting, measurement, and evaluation
- Develop set of performance standards to serve as guidelines or benchmarks
- Develop certification system based on commonly agreed performance indicators
- Provide training to enhance their ability to collect and manage performance indicators
- Provide technical assistance to MFIs which do not qualify for certification
- Increase public and financial awareness of the proposed standards
- Subsidize certification activity
- Fund audits

Part Two: Parentage and Governance of a "New Agency"

2.1 Parentage of the "New Agency"

The "location" of the "New Agency" and the decision on its "voting" shareholders is important, both symbolically and substantively. Control is a sensitive issue. There is the belief that any form of government control is a guarantee of failure, or that paralysis will result if a multilateral agency has a parental role. The contrasting view is that if public money is involved, accountability concerns militate against excluding governments.

Shareholders could include any permutation and combination of existing multilateral units currently in the field (CGAP, UNDCP, UNESCO, FAO, etc.), national government agencies, NGOs, private foundations, and private sector enterprises or financial institutions.

There is a wide spectrum of options for the choice of parents. Simplicity and administrative tidiness would lead to selecting one parent from amongst existing multilateral institutions. Coalition building concerns lead to a multiple parent model like CODEX (FAO/WHO) or the Global Environment Facility (World Bank, UNDP and UNEP). On the cutting edge is the public-private partnership, like UN NetAid (UNDP and CISCO). Current models of international organization Boards include examples where NGOs are provided full participation status like UNAids Program Coordinating Board and the World Commission on Dams.

Criteria to bear in mind in selecting amongst options include effectiveness, measured several different ways; and legitimacy. Effectiveness has several dimensions:

1. *Do not reinvent the wheel*. There is no need to duplicate functions currently being performed well. Ideally, the new "Agency" will bring resources to bear to expand, enhance and complement existing efforts by international and national efforts (for example, but not limited to, CGAP, UNDCP, UNESCO, FAO and UNAids);
2. *Access to the right skill mix and resources*. Organizations outside government have much to offer:
    - Operational effectiveness depends on the commitment of NGOs (ACCION and Grameen, for example);
    - Private multinational financial institutions could bring resources and practical knowledge to the table;
    - Multinational enterprises, concerned about their corporate social responsibility, can contribute marketing and financial resources;
    - Multinational software, hardware, and consulting firms wishing to make a positive social contribution, can provide advisory services.
3. *Maintain the mandate re the poorest*. New shareholders investments, leading to an order of magnitude increase in resources, must not divert the mandate away from poverty alleviation and economic empowerment of the poorest.
4. *Team cohesiveness*. There must be good prospects for cooperative and positive relationships.

Legitimacy has several dimensions:

- Credibility – given the dissimilarity of MCIs, and the wide variation in target groups and the economic and cultural contexts in which they operate, experience and credentials that are widely respected.
- Accountability – they have effective regimes monitoring and evaluating leadership and staff performance. Representativeness – widely based constituencies.
- Transparency – clear and accessible tombstone information.

Some options for parents, i.e. major shareholders, of a new MPA include:

1. Sole parentage – located in the World Bank or UNDP
2. the GEF Model – a new agency reporting jointly to the World Bank and the UN.
3. The UN NetAid model.
4. The Innovative model – something analogous to a partnership of four parties with equal votes – including i) a consortium of international organization; ii) a consortium of national governments; iii) a consortium of NGOs; and iv) one or more private multi-national enterprises.

2.2 Good Governance Features

The support for any new agency will be increased to the extent that it incorporates progressive, state-of-the-art governance features. Whatever the eventual determination of its function and mandate, enhancing participation, transparency and accountability are worthy objectives. Obviously, the governance mechanisms or approaches adopted must be appropriate for tasks set for the agencies. Recommended features would vary with possible functions - researcher, service provider, advocate, central banker.

There are many governance best practices in the international system which may be applicable. Focusing on the goal of participation, we commend the UN's NGO Liaison Service as a model of a dedicated unit to promote partnerships with NGOs. The UNAIDS Program Coordinating Board exemplifies how an inclusive committee of representatives of co-sponsoring organizations can provide for a diverse array of inputs into strategy. Internet Working Groups, based on the example of "UN Women Watch/Beijing +5 Global Forum," can expand and diversify the discussion of key issues and mobilize support. Web pages constructed by the agency officials and governing board members, can provide a focal point for information exchanges about the agency activities and allow for more informal and personal ways for the public and the constituency to interact with the Industry.

With respect to a precondition for transparency, we are impressed by the UN's ECOSOC database on NGOs. To effectively consult, a directory of names and organization contacts must be maintained. The challenge is to create a useful database that will serve for consultation purposes, allowing identification of institutions and individuals by interest area.

Secrets and the appearance of secrecy are anathema. Documents of various kinds can be posted on a Website to allow for public viewing and commentary. The IMF is a best practice example for documents prepared by member countries that present policy intentions regarding the use of IMF resources or staff-monitored programs.

One apparently elementary tool is a comprehensive contact list allowing informed access to staff. The World Bank has a well-organized contact list of its experts and senior staff as well as its regional, country, and media contacts, all available to the public on their web site. Their example could be emulated for an MPA and the relevant representatives of its sponsors and shareholders.

To widen the net in gathering information and views in the policy formulation process, Internet on-line dialogues provide good promise. An excellent example is the Discussion with Scholars and Trade Experts, co-sponsored last October by the WTO and World Bank. Government officials, business representatives, students, NGOs and other interested parties participated in a month-long on-line forum on Trade and Sustainable Development.

Accountability is a sensitive and complex issue at the best of times. In the microfinance field, with diverse types of organizations operating in widely differentiated cultures and economic circumstances, any central or "conditional" direction is problematic. That being said, an accountable agency, promoting accountability throughout the microfinance field, can only contribute positively in achieving the goals of the Microcredit Summit.

There are governance features that apply to the operations of the agency itself. The model of the Compliance Advisor of the World Bank's IFAC/MIGA is a worthy example to adopt – especially the mode of recruitment of the person in charge by an external search committee. A forum comprised of several dozen practitioners, academics and government representatives, that meet once a year, to review results and future plans, is a possibility. The example is the Forum of the World Commission on Dams.

The MPA could promote accountability in governance of the microfinance activity at large. In this context, it could borrow ideas from the IMF – its Code of Good Practices on Fiscal Transparency – or from CIDA – its Compliance Standard on Gender Analysis. It could adapt the WTO's peer review process by constructively examining the policies and performance of recipients of program funds by the MPA.

There is a large inventory of good practices from which to draw. We are convinced that adopting good governance features is intrinsically worthwhile, and also will contribute positively to the reputation of the MPA, facilitating its tasks and the performance of its functions.

Annex 1: Impact Assessment Rating

Impact Assessment Rating

The twin objectives of any microfinance institution are to be financially viable, and to maximize the access of its services to the poor. While it is a difficult juggling act to be able to reach the poorest of the poor and remain financially sustainable, it is, nonetheless, the poor that make up the clientele and provide for the successes of the industry. Therefore, those MFIs that can plan for and maintain a high level of access while applying sound financial and managerial practices are likely to succeed. What is required is a means of showing how effective their operations are at raising the living standards of their customers, especially among the most impoverished.

The information required for such a task would need to take into account how well the MFI contributes to their clientele's ability to:

- Increase, stabilize and diversify their revenues;
- Ensure basic goods and services, foods and medicines among others for their households;
- Improve household living conditions, in particular those of women;
- Increase household wealth; and
- Increase participation in economic and social life as well as fostering autonomy among various population groups.

The methodology would need to be centred around a socio-economic data gathering system on households. A control group would be acknowledged, both qualitative and quantitative indicators would be drawn from the data collected from interviews and/or questionnaires, and follow-up visits/questionnaires would be established.

There are a number of important questions to be answered about the practicality and efficacy of an Impact Assessment Rating system:

Poverty impact assessments may show individual donors that their money is being spent well, but can it satisfy private investors, such as commercial banks?

It is taken as a given that an MFI must be financially viable before it can improve access to the poor. Thus, it is important that the MFI become financially sustainable; then it can offer whatever level of services it wishes to its customers. However, with the sudden proliferation of MFIs and the multitude of different business practices they employ, it is difficult to predict which ones will be ultimately successful. It is in this respect that one ought to look at what has driven the microfinance industry-the resourcefulness of the poor. The growth of the industry is based on the tapping of a resource that was previously deemed to be unprofitable. Indeed, it is the ability of MFIs to increase the living standards of the poor that is an indicator of their success. If an MFI can be acknowledged for improving the lot of its clients as a result of its level of access, it is a good indication that the MFI will be sustainable in the long term.

If individuals and households are to be seen as emerging from poverty, how do you go about defining "poverty"?

This question revolves around the issue of what standards, performance indicators, or benchmarks are most appropriate for an assessment rating. These would, as mentioned, either be formed by the MPA or decided by those organizations tapping into an MPA Rating Fund, led by certain minimum guidelines. The acceptance of such measures can be seen in how many MFIs and evaluation agencies voluntarily involve themselves in the system, and what kind of reaction it is given by donors, investors and banking institutions.

How do you know if someone has risen out of poverty due to the services offered by the MFI, or if it was due to something else?

The answer would have to be determined from the accuracy of the methodology used, but would also depend on taking a deep look into all the factors involved in poverty alleviation. MFIs will certainly be more successful if they are working in a favourable environment, and if their efforts are supplemented by different sorts of development initiatives within the community. How an MFI takes advantage of its surroundings and how it associates itself with other development organizations may be determining factors in its impact on poverty alleviation.

Assessing poverty

There are some standards of poverty assessment that are in common use that may be able to serve as a starting point for the construction of a good impact assessment. In a paper prepared for the Microcredit Summit Campaign entitled "Overcoming the Obstacles in Identifying the Poorest Families," three such examples of cost-effective methods used to identify those living in absolute poverty were presented. The first example is the *CASHPOR House Index (CHI)*, in which external housing conditions are examined as a proxy for poverty. Second, *Participatory Wealth Ranking (PWR*) uses a community's own definitions and perceptions of poverty, and employs rigorous crosschecking methods to ensure consistency and accuracy of results. Both methods aim to build on existing information, collect the minimum data necessary for reliable targeting, and follow-up targeting with a motivation process to encourage the poorest to join the program.

The third method presented is a *"check-list" approach*, which builds up a list of poverty proxies or indicators, based on a local understanding of poverty. Scores are then assigned to each indicator or a poverty-line level determined. The poverty level of a household can then be calculated from their score, or number of qualifying indicators.

The benefits of a competent poverty assessment are not only useful in evaluating the results of an MFIs current performance, but can also determine the poverty level of its clients before they start regularly using its services, providing a better indication of its rate of success. The assessment methods mentioned above may be useful for this purpose, and may provide a deeper understanding of the effects MFIs have on decreasing the poverty burden its clients face.

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