

**PLANET FINANCE**

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The Microfinance Platform

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## **Chapter 1**

### **PlaNet Finance, Presentation**



# PlaNet Finance

## Microfinance : fighting against poverty

PlaNet Finance is an International Solidarity Organisation created in 1998 and based in Paris. PlaNet Finance's mission is to take part in the fight against poverty of the microfinance sector.

The idea of PlaNet Finance was launched for the first time by Jacques Attali during a seminar of the Aspen Institute in November 1997. Professor, writer, chronicler for Express, State advisor, special counsellor to the President of the French Republic from 1981 to 1991, founder and first President of the European Bank for Reconstruction and Development in London from 1991 to 1993, Jacques Attali is now President of A&A, international consulting company and President of PlaNet Finance.

## Services

### 1. Advice and technical assistance :

- To Microfinance Institutions (NGO, Cooperatives, financial institutions)
- To the national Microfinance network
- To government (defining strategies, implementing regulations)
- To commercial banks interested in microfinance programmes

**2. Rating of MFI through PlaNet Rating, an independent subsidiary** and one of the 3 first agencies of the market, with 160 ratings.

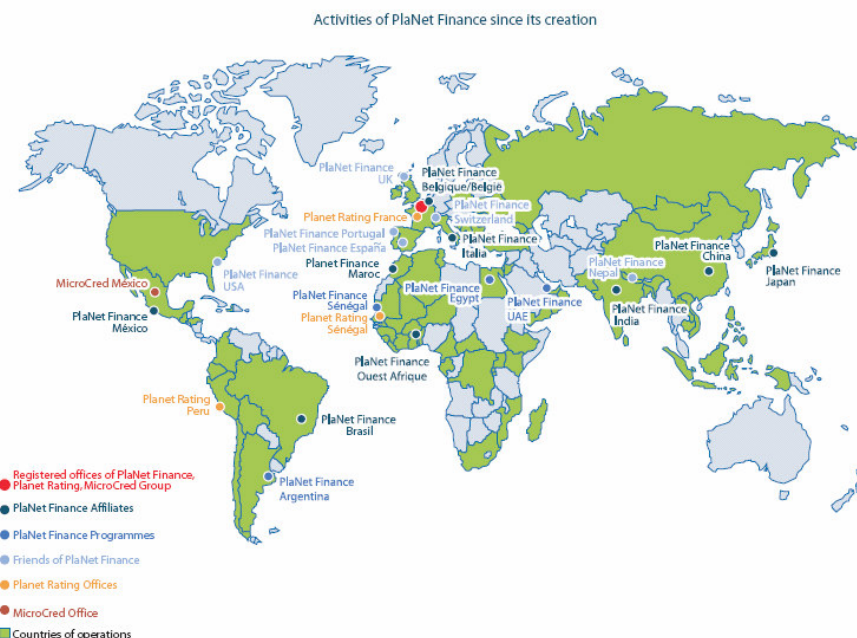
### 3. Debt financing of MFI :

- **PlaNet MicroFund**, which financed 45 young MFI (that is 15 000 microentrepreneurs)  
**PlaNet /responsAbility**: this recent partnership enabled to finance 4 mature MFI, to the amount of 1,8 million euros in 6 months.  
**Altogether, these funds have participated in financing over 107 000 microentrepreneurs' projects in 2005.**

**4. MicroCred, an investment company** created in June 2005 and aiming at creating or taking stakes in 15 MFI throughout the world in 5 years. The MicroCred MFI Mexico was officially launched in April 2006.

## International network

Thanks to 205 people present on a network of affiliated organizations in 20 countries, PlaNet Finance implements programmes of support to microfinance in more than 60 countries.



**New offices under creation:** Madagascar, Cambodia, Uganda, South Africa, Israel, Palestine, Egypt, Sri Lanka, Canada, Germany.

## Resources

On December 31st 2005, the budget of PlaNet Finance headquarters reaches around 6.8 million euros, which represents an annual progression of 34%

## Some partners

- World Bank
- European Commission
- AFD, Belgian Cooperation
- IFS (International Financial Society)
- CAF (Andean corporation)
- BID (InterAmerican Bank)
- Ernst & Young
- Sanofi-Aventis
- Orange
- Microsoft
- Altavia
- Publicis
- Société Générale
- BNP Paribas
- BMCE Bank

## **Chapter 2**

### **Brief explanation of Microfinance**



# Definitions

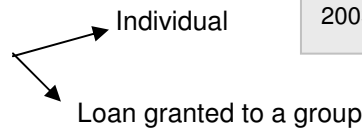
Microfinance implies the offer of financial services to poor populations, who are excluded from the banking system and do not have resources or ownership right. Often confused with microcredit, microfinance includes many other financial or non financial services. Among others: savings, microinsurance, money transfer, credit for housing, credit for education and credit for health. Microentrepreneur training, education to health and hygiene are examples of non-financial services that can also be delivered to their clients.

## Average amount for a loan in an MFI

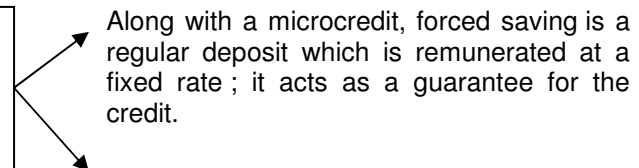
Africa : 307 euros  
Asia : 334 euros  
Latin America : 750 euros  
Eastern Europe : 1,200 euros  
France : 5,000 euros

Sources : Mixmarket, benchmarks 2003

A microcredit is a small loan granted according to specific conditions to establish income generating activities



Microloan is a means for poor people to use their own resources to escape poverty and face crisis.



## A few figures\*

- 80% of the global population does not have access to a credit. Among these people, 500 to 600 million could start an income generating activity with a microcredit, thus enhancing their family and their own living standards.
- Nowadays, an average of 100 000 million people benefit from the services provided by more than 10,000 microfinance institutions.
- 98% of microcredits are paid back in due time
- The global portfolio of microfinance applicants ranges between 15 and 25 billion euros
- The average amount of microcredit is of € 300 in developing countries and reaches € 5,000 in Western countries.
- 66,6 million applicants for a loan are the « poorest of the poor. »
- The total International Aid for Development represents 50 billion euros, out of which 1 billion is allocated for microfinance.

References: CGAP, UNDP

# History of microfinance

## An age-old and universal practice

Microfinance has been around for centuries:

Three thousand years ago, it already existed among the Hebrews, who were the only people authorised to charge interest on loans by their religious law.

It appeared again much later, in the 16th century, in Europe, when interest on loans was authorised by the Church. Pawnbroking then sprang up in the form of savings and loans associations.

During the 19th century, cooperative loans and savings banks appeared for the poorest members of the society.

In Africa, the traditional “tontine” systems allowed their members' savings to be shared.

Yet, it was only after thirty or so years that it became truly structured. In 1978, two simultaneous and independent initiatives marked the birth of a new sector to finance the business activities of the poorest members of society, without their needing to provide guarantees.

### KEY DATES

**1983** Creation of the Grameen Bank

**1997** 1st **Microcredit Global Summit**

**1998** General Meeting of UN decision to declare 2005, International year of Microcredit.

**2000** Proclamation of the **Millenium Development Goals by the UN.**

**2003** UN member States approve an action program **to promote sustainable access to microcredit.**

**2004** Declaration of the G8 on the **extension of access to microfinance for entrepreneurs**

**2005 International Year of Microcredit**

## ACCION and the Grameen Bank

In Bangladesh, a young rural economics lecturer at Chittagong University, Muhammad Yunus, came across 42 women who had to borrow from usurers to buy the straw needed to reseat the chairs, at a weekly interest rate of 10 %. When he could not find any bank ready to lend them the money to avoid them falling into the hands of the usurers, he loaned them the equivalent of \$26 that they needed.

At the very same time, on the other side of the world, an American tennis player, Joseph Blatchford, set up ACCION, an NGO aimed at helping the poorest to help themselves. It began to install electrical lines, to build schools and community centres, then decided to support microenterprises and the programmes that supported them.

In 1983, Yunus founded the Grameen Bank. His idea was simple but revolutionary: a bank dedicated to the poorest, collaborating with borrowers in an informal way \_not having to sign any formal contract

in exchange for their loan. 95% of the clients were women. Since the beginning, the recovery rate was around 99%. The same year, PRODEM, which later became Banco Sol, was set up in Bolivia and started lending small sums as working capital to groups of three people or more. Five years later, the programme had granted over 27 million dollars in loans, with an average credit of USD 273, to over 13,300 entrepreneurs, 77% of whom were women, with a repayment rate of around 100%. In 1992, PRODEM went from being a non-profit association to being a private credit and deposit bank, under the name of Banco Sol. It grants housing loans, working capital and investment capital. It receives savings deposits on sight and at term and organises an insurance service, funds transfers and credit cards.

In Africa, at the same time, Microfinance Institutions inspired by the “tontine” system were set up, which encouraged the beneficiaries to form jointly liable groups and repayment guarantees for each of their members. These initially included KRep in Kenya, PADME in Benin and other cooperatives financing cotton harvests, such as Kafo Giginew in Mali.

So far, MFIs seem to have been developed in countries benefiting from a minimum economic and political stability. They are currently to be found in 85 countries. Yet, while the needs are covered in some countries (such as Bangladesh and Bolivia), most of the most populated regions have barely any access to microfinance services.

## Operations

### Microfinance operators

**Microfinance institutions:** a certain number of organisations offer insurance, credit, savings services to populations excluded from the banking system. They are known as Microfinance Institutions (MFIs).

They exist in multiple forms: savings and loans cooperatives, international or local NGOs, programmes set up by international institutions...

**In 2005, the estimated number of MFIs is 10,000, spread out in 85 countries and reaching out 92 million people.**

Often very small and focused on their community, they can offer microcredits to several hundreds of people in a village or in a shanty town. At times more complex, they are developed on a regional or national scale and offer a range of services (savings and credit, business and consumer loans). Lastly, sometimes federated in international networks, they operate using the same methodologies in several countries and on several continents. If the smallest of them can be counted by the thousands, a dozen or so of these MFIs have become the largest banks in their countries. The largest and sometimes the most profitable banks even prove to traditional banks that a good management in the microfinance sector can be an activity that is not only socially efficient, but also provides a good financial return.

In 2005, it was estimated that there were 10 000 MFIs in 85 countries reaching out 92 million people.

**Governments and local collectives:** governments are involved in the development of microfinance, as they define the adapted legal frameworks and national strategies for sustainable development with a microfinance constituent. They also help central banks, ministers and local collectives to use microfinance as part of their actions for sustainable development.

**Banks:** commercial banks either support microfinance operations indirectly, by helping existing MFIs with financial support or by means of a stakeholding, or indirectly, by setting up an affiliate or designing a range of microfinance products and services; this is called downscaling.

## Loan methodologies:

The two most widespread loan methodologies are Group Lending and individual lending.

- **Individual contracts** are quite similar to “standard loans”: Someone has been granted a certain amount of money and usually has to repay it in a relatively short time (several weeks or several months) with the interest rate. The loan amount is usually larger than those of joint loans.
- **Group lending** are granted to a group of people that are jointly liable for repaying the loan. Individual defaults (due to illness or to a “bad week”) are thus avoided; group pressure is a strong incentive that reduces moral hazard.

## Interest rates<sup>1</sup>

The very principle of microfinance – granting access to basic financial services to those traditionally excluded from the financial system in order for them to become self-reliant– involves the application of an interest rate.

As the amounts are very low and the repayment terms very quick (often weekly), the clients can afford the amounts to be repaid when taking into account the productivity of their income generating activities: *“a study conducted in the Dominican Republic, in Colombia and in Chile has revealed, for example, that even a monthly interest rate of 6% only represents 0.4 to 3.4% of the operating costs for the microentrepreneur (...) The research work carried out in Kenya and in the Philippines has revealed that the average annual rate of return on the investment in microenterprises could range from 117 to 847 %.”<sup>2</sup> »*

### Repayments affordable by clients

- Low amount loans
- Weekly repayments
- Outputs of microentrepreneurs activity

MFIs’ interest rates are high because they grant more small loans than traditional banks, with a meticulous methodology resulting in very high processing and operating costs.

### The following elements account for the interest rates

- risk
- number of granted loans
- low amount of loan
- Operational costs and data processing

Interest rates must cover: the cost of funds, the cost linked to default in repayment, administrative expenses and processing of microcredits (time spent selecting and assisting clients, processing of financing applications, repayment collection...) The estimated operating charges represent 25% of the average loan portfolio of an MFI whereas in India, for instance, commercial banks have operating charges of 5 to 7 % of the outstanding loans.

<sup>1</sup> Source : Brigit Helms et Xavier Reille, *Le plafonnement des taux d'intérêt et la microfinance : qu'en est-il à présent ?* CGAP, Etude spéciale, septembre 2004.

<sup>2</sup> Brigit Helms et Xavier Reille, *Le plafonnement des taux d'intérêt et la microfinance : qu'en est-il à présent ?* CGAP, Etude spéciale, septembre 2004.

If a microcredit is much more expensive than a traditional credit, MFI credit agents seem to be more productive: in self-sufficient MFIs, credit agents manage about 359 microentrepreneurs, according to the Microfinance Information Exchange (MIX)

Interest rates depend on:

- local regulation on the interest rate limit
- microfinance activities expenses
- the institution's positioning (social or commercial MFI)
- Technologies or innovations enabling the MFI to increase its productivity in order to reduce its operating charges.

## **Chapter 3**

### **What is the impact of microfinance?**



# The Impact of Microfinance

Poverty leads to a worsening of living conditions: the quantity and quality of food is inadequate, children do not go to school and are forced to work in order to increase their family's income, hygiene conditions deteriorate....Access to financial services is a way for the poorest people to get access to other areas of the development process such as health care and education.

## Can Microfinance Tackle Poverty?

*"Microfinance - along with the three mainstays of development represented by democracy, education and infrastructure - is increasingly seen as a key tool for implementing effective strategies in the long-term fight against poverty."* Jacques Attali, President of PlaNet Finance.

The share of the world population living on less than \$1 per day fell from 40% to 21% during the 1980s and 1990s. In China, GDP per capita has risen fivefold since 1981 and the percentage of people who are living in absolute poverty has gone down from 64% to 17%. All in all, in ten years' time the number of people living on less than one dollar a day will have fallen from 1.3 billion to 913 million.

Despite these seemingly positive developments, the number of extremely poor people in sub-Saharan Africa shows no sign of diminishing, and is set to reach 400 million by 2015. If current trends continue, in 40 years' time, nearly half the world's population - in other words around 4 billion people - will be living on less than two dollars per day.

### The impact of microfinance

66.6 million of microfinance clients are amongst the poorest of the poor. But the impact of the loans they receive is much more widespread, covering 333 million people; a figure equivalent to the combined populations of the UK, France, Germany, Italy, Spain, the Netherlands Switzerland and Norway.

Although there is still no comprehensive worldwide research, the UN's designation of 2005 as the International Year of Microcredit (as part of the framework of the Millennium Development Goals for Poverty Reduction) was proof that the impact and activities of microfinance were being recognised and acknowledged. No less a person than former World Bank President James Wolfensohn has said that "access to financial services is a crucial condition for reaching the MDGs."

- The amount earned by the richest 1% of landowners is equivalent to the total earnings of the poorest 57%.
- 1.3 billion people live on less than \$1 a day.
- 3 billion people live on less than 2 dollars a day.
- 825 million people suffer from hunger, a figure which includes 200 million children under the age of 5.

Furthermore, specific impact studies have highlighted the poverty-reducing role of microfinance through integrating those most affected by poverty into the financial system.

For example, it was shown that 40% of the overall reduction in poverty levels in rural areas in Bangladesh was explained by microfinance activities and that 5% of microfinance clients were lifted out of poverty every year.

The impact study carried out in Morocco in 2004 by PlaNet Finance, in partnership with the country's other MFIs, showed that in macroeconomic terms, microcredit services had a positive effect on profits and investment and access to markets. At the household level, there was a positive impact on consumption expenditure. Finally, at the individual level, microcredit enabled spouses and children to achieve greater respect.

In Bangladesh the Association for Social Advancement (ASA) caters for more than 3 million clients, many of whom were extremely poor when they took out their first loan. Because of its ability to offer loans at a rate equivalent to 3.5 cents per US dollar, the ASA has been acknowledged as the world's most effective MFI.

Staying in Bangladesh, over the past 10 years, the BRAC's income-generating development programme - which is aimed at vulnerable groups in the country - has had an impact on around one million women. Through a programme costing only 135 dollars per beneficiary, two-thirds of these women have escaped from absolute poverty and no longer require support from the government.

In El Salvador, clients of the Foundation for International Community Assistance (FINCA) have seen their weekly income increase on average by 145%.

The impact of the loans made to the 66.6 million microfinance clients (who are amongst the poorest of the poor) has been felt by 333 million people, a figure equivalent the combined populations of the UK, France, Germany, Italy, Spain, the Netherlands Switzerland and Norway.

## Microfinance, A Development Tool for Women?

By the end of 2003, according to the American NGO Microcredit Summit Campaign, 84% of the 66 million of the poorest clients benefiting from microfinance services were women; in other words 55.4 million clients.

Women make up half the world's population and account for two-thirds of working time. They play a crucial role, especially in areas like nutrition and food security. However, they only earn a third of the world's income. Women are often alienated within their family and, in most developing countries, are excluded from political, economic and social power and rarely have access to education.

Between 1976 (when it was first set up) and July 2005, the Grameen Bank made 4.95 billion US dollars worth of loans to 5 million borrowers, 95% of whom were women. The Grameen Bank's case especially underlines women's better loan repayment record (almost 98% of cases). It also shows that when the family is headed by a woman, the increase in income has a greater effect, with the whole family benefiting in areas like health and education.

PlaNet Finance's recent impact study of microfinance in Morocco found that three quarters of microentrepreneurs were women and that 45% of female beneficiaries were illiterate. In tradition-based societies, where they have little or no access to education and labour markets, women often end up in insecure jobs, leading to greater social and economic vulnerability.

- Women only earn a third of the world's income and own less than 10% of its assets. They account for 2/3 of those who are illiterate and 2/3 of those who are poor
- 84% of microfinance clients are women, representing 55.4 million clients (*Source : Microcredit Summit Campaign, 2004*).

"Improving women's access to health and education, along with better employment opportunities and access to microcredit services, has widened the possibilities open to women and has given them a sense of responsibility. In spite of continuing gender disparities, women are becoming increasingly powerful catalysts for development, demanding greater independence over their fertility, the wider spacing of births, the education of their daughters and over access to services."<sup>3</sup>

A research led by the United Nations Development Programme (UNDP) the United Nations Development Fund for Women (UNIFEM) and the World Bank, among others, shows that such inequalities act as a brake on progress and economic growth in developing societies. A recent World Bank report confirmed that societies characterised by sex discrimination suffered from greater poverty, slow economic growth, weaker governments and lower living standards for their citizens.

### **Is Microfinance Social Finance?**

Microfinance programmes can be an effective means of bringing about other desirable forms of social progress. By linking financial services to health and education, the welfare of clients and their families can be increased, with a lasting effect in terms of increased productivity and reduced failure rates for microcredit programmes.<sup>4</sup>

#### **Achieving better health through the fight against poverty**

Microfinance can become a major health promotion tool via its ability to fight against poverty. By the same token, improved health levels result in higher success rates for loan repayments. This is vital if MFIs are to work effectively (as borrowers who fall ill often have to draw on monies destined for loan repayments in order to pay for increased spending on health care).

Some institutions, aware of the importance of this issue, even provide hygiene awareness programmes. A link can thus be observed between better health and access to basic financial services:

- A study showed that 53% of women benefiting from the loans and training offered by MFIs use contraceptives as against 36% of female non-beneficiaries;
- In Bangladesh, malnutrition levels among clients of the Bangladesh Rural Advancement Committee (BRAC) were lower than for other groups;
- In Uganda, 32% of the clients of the MFI "Foundation for Credit and Community Assistance" (FOCCAS) use AIDS prevention methods, a figure twice as high as that for other Ugandans.

- 53% of women benefiting from loans and training offered by MFIs use contraceptives, as against 36% of female non-beneficiaries.

- Better health results in improved loan repayments.

#### **Educational access for microentrepreneurs**

As with health, it has been shown that education benefits from the war on poverty. By the same token, MFIs should train their clients in the most effective way by setting up

- It is in MFIs' interests for their clients to have the best possible opportunities for education and training.
- In Uganda, clients of FOCCAS spend a third more than non-clients on their children's education.

<sup>3</sup>UNDP *Human Development Report 2005*

<sup>4</sup> Microfinance Summit Campaign, 2005 Report.

educational assistance programmes for the families of the beneficiaries.

Hence Freedom from Hunger, a South American microfinance support organisation, developed an approach whereby loans were combined with an education programme aimed at the poorest people. Purely finance-based services were said to be inadequate in the battle against malnutrition among rural households. Freedom from Hunger thus provides a means of spreading good health practices through the offering savings and loan services (for setting up a business and developing a regular, long-term income) alongside information sessions on nutrition, health and business.

In Bangladesh, virtually 100% of the daughters of the Grameen Bank's clients receive an education, as opposed to a figure of 60% for children of non-clients.

In Uganda, clients of FOCCAS spend a third more than non-clients on their children's education.

## Chapter 4

### 2006's major issues



# Microfinance in Europe

Microfinance is a method that originated from the developing countries and that is used to sustain growth in these countries. It takes into account and fits the economic, cultural, social, legal and administrative contexts. As a result, a large number of Western people who come from countries of the North have been convinced by microfinance.

## A promising sector <sup>5</sup>

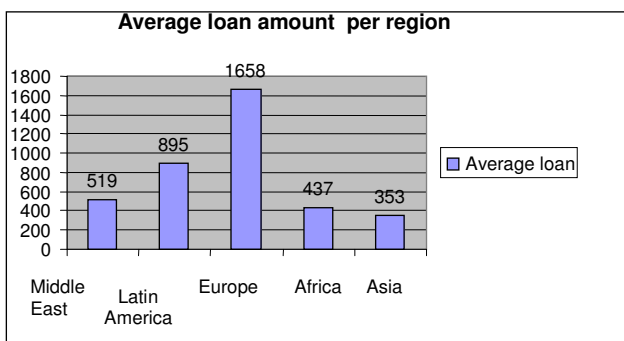
Microcredit was designed for the development of entrepreneurship with the implementation of new structures and for loan allocation to unemployed and marginal people. It contributes to the “Lisbon strategy” for the growth, employment and social cohesion prescribed by the European Union.

Europe is a booming region for the development of microfinance since 93% of 20.5 million European SMEs are, actually, microentreprises (up to 9 employees) and around 2 million of start-up companies are getting set up each year. The core of the European economic system is characterized by the significant function played by SMEs. One third of new companies are set up by unemployed people.

- 20,5 million microentreprises in Europe
- An average loan of 5 000 € in Western Europe
- An average interest rate of 8%
- An average repayment rate of 90%
- A booming sector in Eastern Europe
- Legal frameworks more complex than in developing countries

The average loan amount varies between 50 and 5,000 euros depending on the country. It is known that microloan is defined in Europe as any loan which amount is lower or equal to 25,000 euros. The average interest rate is 8% but it can change according to the legislation in force in the country. The highest rate can be found in the United Kingdom. The repayment rate obtained by dividing the total amount of loans granted by the amount still due for repayment reaches 90%, on average, in Europe.

Western and Eastern Europe know the highest average amount for group loans: **1,658** euros for each borrower<sup>6</sup>.



The progress of microfinance all over Europe is not the same due to disparate growth. Indeed, the countries that have been studied do not know the same situation; in the Netherlands and Germany, microfinance starts to develop. Banking laws and regulations as well as the predominant role of the State in tackling poverty issues can explain this situation. But in the Anglo-Saxon countries (especially in the United-States), Quebec and France, microfinance has significantly been developed: the

<sup>5</sup> Etude conjointe *nef* & *EMN* sur le secteur de la microfinance, 2004.

<sup>6</sup> Mixmarket « Global benchmark 2004 »

experience gained in the countries of the South and the high media coverage of the success met by the Grameen Bank have surely something to do with it.

Nowadays, it is in Eastern Europe that microcredit experiences a dynamic trend: it is well structured whereas in Western Europe, its growth is recent and limited. Microfinance was introduced in the former communist countries of Central and Eastern Europe after the fall of the Berlin wall. The objective was to provide a backup to people who wished to set up income generating activities in an environment where the banking sector was inappropriate and unable to match the growing needs. In just five years, MFIs established in Eastern, Central Europe and in recently independent states have provided services to more than 1,7 million borrowers and 2,3 million savers which represent an average growth of 30% per year. Besides the involvement of MFIs and NGOs in microfinance in Eastern Europe, commercial banks are increasingly interested in providing microcredit services to poor people.

Even though the sector is organized as a structure, it is small-sized and relies only on some institutions: for instance that of France and Finland provide 70% of the total loans granted in a year.

In Europe, microfinance meets with several challenges:

- An external environment where evolves a significant and competitive industry of financial services , in addition to increasing traders providing consumer credit with high interest rates leading to the rising number of families getting into heavy debts.
- A social benefit system not in favour of citizens who want to work by themselves ,
- A lack of entrepreneurial culture and the low incentive for its promotion at all levels of the society,
- A lack of equity to cover the operating costs of the MFIs since most of the funds they receive are allocated for a short term period,
- MFIs relying mainly on the public sector for the revenue and capital raising
- A legal framework that is not in accordance with the growth of the microfinance sector.

## Solidarity funding in France

Microfinance in France is mainly meant for unemployed people and the beneficiaries of the Minimum Income Guaranteed who are excluded from the banking system. The group loan and the loan on trust (allocated with 0%) being the two types of loans encouraging the funding and the setting up of companies.

Today's main characters in the landscape of Solidarity Funding in France, are mainly Solidarity Funding Institutions. At present, there are around 20 institutions and three main associative networks

- **Adie** (Association for the right to economic initiative) funds long term unemployed people who have the project of setting up a business.
- **France Active** provides people who have the project of setting up a business with the access to loan, an expertise, a financial backup (guarantee on loan, contribution in equity).
- **France Initiative Réseau**, the first associative network assisting and financing the setting up of businesses is composed of local initiative platforms.

- An average loan of 5,000€
- An average penal rate of 5,52%
- An average of 4,000 microenterprises set up per year
- A rigorous legal and administrative framework that is not beneficial for the setting up of businesses, but
- A recent consciousness-raising of the public authorities and the private/banking sectors that should lead to the growth the sector.

These 3 large associative networks have granted in all 15,000 group loans and loans on trust in 2004 which has fostered the creation of 32,000 jobs in the same year<sup>7</sup>.

Other players are involved like local venture capital societies (Autonomie et solidarité, SIFA,...) financial corporations (NEF,...), real estate corporations (Habitat et Humanisme), « boutiques de gestion » (offices giving advises on how setting up a micro entreprise) as well as local players. The financial institutions involved in a solidarity movement are also important players

Nowadays, microfinance takes part in 30,000 projects for business setting up or development. Moreover, it fosters the creation of 37,000 jobs each year<sup>8</sup>; the mean loan amount being of 5,000 euros<sup>9</sup>. After 5 years of activity the success rate of the businesses that were followed-up reaches 54% (the national average being of 50% after 3 years of activity)<sup>10</sup>.

### **Developing entrepreneurship in France**

The role of microfinance is not widely known and acknowledged. Despite the existing structures and the effort that is made, the implantation of microfinance is low in comparison with the important number of unemployed people: in 17-years, Adie has fostered the setting-up of 29,854 businesses which is little, when France has an unemployment rate of 12% exceeding 20% when affecting young people under 26. It can even reach 50% in the troubled suburbs.

Several reasons can explain why microcredit is not principally used when setting up a business in France:

- Staff in charge of the social integration are not always aware or been trained to give advice for the setting up of businesses when they should advise and give directions to those have a have idea or a project.
- Few potential entrepreneurs know that these structures exist or use them
- The groups that are most affected by unemployment are women, young people, people with no or low qualifications of troubled suburbs. However, structures are absent from these sensitive areas or difficult to approach for any person who would be willing to create a project but who has no financial nor legal support.
- The legal and financial frameworks are not are not adapted for the business setting up.

### **Evolution or revolution?**

Even though, it seems that the microfinance sector and the setting up of French business is in constant growth:

- In the framework of the Summit on Microcredit, organized on its own initiative on June, 20th 2005, President Chirac expressed the will of the government to encourage the development of microfinance to fight against poverty on a long lasting term and hopes that “the number of clients will increase from 10 million beneficiaries to hundreds of million tomorrow.” President Chirac has therefore committed himself in taking part in the development of microfinance with a reform work of the legal and fiscal framework but also with raising of private funds.

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<sup>7</sup> Activities report 2004 « Funds for loans on trust backed up by the Caisse des Dépôts »

<sup>8</sup> Source Finansol

<sup>9</sup> Source IFRAP (Institut Française pour la Recherche sur les Administrations Publiques)

<sup>10</sup> Source Finansol

- On summer 2005, the law about the SME enables the financing of businesses with the funds allocated for professional training and applied the unlimited interest rate for the setting up of a business by an individual which fostered banks to provide microcredits and cover at the same time operating costs: “What is the point of guaranteeing a low rate when we do not have access to credit?” explained Maria Nowak, President of Adie and active militant of the unlimited rate of wear and tear.
- In 2006, the Social Cohesion Funds controlling the *Caisse des Dépôts et Consignations* decided to lend support to development of social and professional microcredit in France. The funds will be allocated to PlaNet Finance (for its program called “Financités”) and Adie as well as to other associations in order to conduct 50 experimentations in 2006.

## Increasing the resources of microfinance

One of the main characteristics of the microfinance sector is its particular functioning system. It combines “private” functioning with public intervention, generally an external support strongly involved in the financing but also in the implementation and construction of structures. This situation is significant as we have witnessed, in the last few years, an increase of the government assistance sustaining the sector and an increase of the NGOs and players’ interest acting for the development (more recently of local authorities) in the framework of the fight against poverty.

If such a situation was obviously profitable for the sector, it has raised concerns about the efficiency of public actions and framing in a competitive environment. These concerns led the international government assistance to look for a consistency in its action with a well designed primary stage of description and dissemination of best practices in the sector<sup>11</sup>.

The French Development Agency (AFD) pays particular attention to local financial sectors: current volumes of granting to banking, financial and microfinance sectors has doubled between 1999-2001 and 2002-2004, representing an increase from 63 to 156 million euros.

- Present loan portfolio in microfinance: **15 to 20 Billion €**
- Annual contribution from donators < **1 billion €**
- Public development aid/year: **50 billion €**
- Global portfolio needed to reach 500 million clients : **200 Billion €**
- Annual contribution from donators needed to reach these 500 million clients: **3 billion €**

Despite these significant figures and the million of testimonies of men and women who escaped from poverty thanks to microfinance, new means provided each year are lower than one billion dollars, one third of which is collected directly from the market or from commercial banks. The remaining is provided by government assistance in technical assistance or subventions.

But if the annual amount reaches 3 billion dollars, the number of beneficiaries would increase up to 350 million, which would represent a significant impact on poverty; the international Assistance dedicated for microfinance is therefore insufficient. Only 1% of annual disbursements made by the World Bank are allocated to microfinance. This rate should increase in the coming years so that dozens of million poor people take advantage of this through MFIs<sup>12</sup>.

It is also necessary to allocate the resources more efficiently. The interventions and the strategies that are used are too disparate to be efficient. Unfortunately, microfinance is considered, most of the times, as a sub component of other programmes (rural, social, women-related programmes for instance) and not as a component of the financial sector. The funds allocated by financial backers do not follow the setting up of sustainable institutions and do not allow leverage on private resources. Moreover, these funds do not target market that has recently emerged.

Several studies have shown that microfinance is financially sustainable; it will become in 10 years time a driving force of financial services in the emerging markets. Microfinance also needs the private sector to allocate more funds and get more involved in the growth of the sector on a larger scale. The microfinance sector is a dynamic market for private investors: only 10% of the market is covered; a market that needs 100 billion euros. Besides, the sector experiences a 20% growth per year.

# Professionalizing the sector

## Microfinance: social or commercial microfinance?

Microfinance was originally dedicated to social matters. When it was first established, microfinance players were NGOs, cooperatives, humanitarian associations. Their objective was to help destitute people to have access to basic financial services in order to set up or develop an income generating activity (IGA). Commercial institutions have recently appeared on the market; but their objective is different: they aim at financial profitability.

Only 209 among 10,000 microfinance institutions are financially self-sufficient<sup>11</sup>; they deal with 60% of the 100 million microfinance clients. The rest of them will need some backing in terms of capacity building, management, profitability, etc. before thinking to be financially strong.

Even though they are recent, commercial institutions experience a rapid growth because they are financially profitable. They consequently have a larger access to international funds.

The creation of rating offices, such as Planet Rating that operates in microfinance, enables the transparency of the sector with the identification of the players and transformation of rating criteria into norms. They also encourage international shareholders to finance microfinance. This trend was initiated with the financing of commercial MFIs, considered as more secure by investors is too much inflexible; they do not consider institutions that are financially less viable but socially more efficient.

It is therefore important to sustain the growth of MFIs acting as NGOs whose mission is the seed of microfinance. They deal with the poorest and provide simple microcredit, non financial services (health and hygiene awareness for instance) but also information on savings, micro insurance, assistance for the development of income generating activities, etc.), to guarantee an access to funding. Being financially viable is not in contradiction with achieving social objectives: the Grameen Bank is one example that is financially viable and exclusively devoted to the poorest.

Moreover, commercial institutions are entering the sector in order for the world's microfinance market to become more professional, but also to foster more competition in this incipient market where little competition exists. Finally, commercial institutions' integration could largely participate in raising the attention of the international community. Even though common MFIs often deal with the less poor among the poor, they are nonetheless assisting people who do not have access to banking services. Those people, clients of non commercial MFIs, are sometimes extremely disadvantaged; they managed to escape from extreme poverty and are still in need for suitable services.

### PlaNet Finance, services adapted to the needs

- *Advice and technical assistance* to strengthen skills
- *Impact and Market Studies*, to assess the social impact of microfinance,
- *Planet Rating* to guarantee the transparency and the generalization of the fundings,
- *PlaNet MicroFund* to finance young promising MFIs,
- *PlaNet / responsAbility* to help mature MFIs and attract new investors
- *MicroCred*, to reach a higher number of clients.

<sup>11</sup> www.mixmarket.org

The ratings should therefore take into account financial figures as well as social achievements. PlaNet rating reacted accordingly by designing a new rating product; the method GIRAFE that measures financial achievements was changed into GIRAFE-S (“S” standing for “solidarity”). This new element that is actually being tested, “aims at assessing the efforts achieved by the MFIs to contribute to their clients’ standards of living, by answering the unrealized needs for credit and financial products and more broadly, to offer opportunities to improve their living conditions<sup>12</sup>”.

### **When banks are contributing to microfinance**

Commercial banks are getting increasingly involved in microfinance. Up to date, banks and commercial institutions were not interested in being fully involved in the development of the sector; since they considered microfinance as a charity action. However, some commercial banks have been convinced both by the social and financial impact of microfinance. This is how, in 2001, Citigroup’s ROE was of 19.7% while 12 MFIs in Latin America had ROEs from 20.2% to 42.9%. Consequently, more and more banks have recently implemented microfinance operations either indirectly, by assisting the existing MFIs or directly, through downscaling:

- Downscaling: PlaNet Finance has provided Bancolombia (1st Colombian bank with 600 branches across the country) with technical assistance. In 2003, they implemented the programme “Emprededor” to offer financing to Colombian microentrepreneurs. The first microcredit was granted on March 2004. At the end of April 2005, there were 3,800 clients. The number is expected to multiply by 5 by 2010.
- Established in 1998, Finadev, Financial Bank’s commercial branch was transformed in 2000 into a subsidiary dedicated to microfinance with the financial backup of the International Finance Corporation (IFC) and the Netherlands Development Finance Company (FMO). In 2004, Finadev SA had a portfolio of 6, 8 million euros and offered services ranging from solidarity loans for individual or group loans for businessmen, employees or farmers, to educational loans to around 11.100 clients.

**Banks Involvement in microfinance**

- Providing financial support to a MFI (sponsorship)
- Make infrastructures available to a MFI
- Re-financing a MFI
- Stakeholding in a MFI
- Downscaling de la banque pour proposer
- Investments funds dedicated to microfinance

There are also more banks having shares in microfinance organizations.

Lastly, banks can also create investment funds entirely dedicated to microfinance<sup>13</sup> or allocate a certain percentage of their assets to MFIs (like North/South Funds for Development of CDC Ixis AM).

Banks benefit from a serious advantage when facing competition since they have already established a network of branches which has access to financing.

<sup>12</sup> www.planetrating.com

<sup>13</sup> like Dexia MicroCredit Fund DMCF, a mutual fund created by DEXIA in Luxembourg or ResponsAbility in Luxembourg created by 4 Swiss banks and backed up by a large French banking group

# **New projects for microfinance: what needs to be done**

## **According to Jacques Attali, President of PlaNet Finance:**

There are four essential and complementary levels of actions: the opening up of trade, to enable poor states to access global markets more easily; the financing of large infrastructures, to cope with the migration of the rural population to towns; the promotion of democracy to help raise awareness of the issues; and access to financial services for the poor.

In terms of microfinance, it will have to develop in four directions: professionalization and financing of MFIs, conversion of public lending institutions into MFIs; the set-up of microfinance subsidiaries by commercial banks and the reform of regulations.

### *The professionalization and financing of MFIs:*

To improve their technical ability, it is necessary to help them to progress to financial durability, (cover costs without the help of backers), organisational durability (adapted procedures) and operational durability (access to quite a large market and a range of products enabling them to satisfy demand). Microfinance will have to be gradually balanced and not depend on external backers, and will then need to attract its clients' savings. It will also be necessary to develop new suitable products, such as microfinance services in rural areas as regards health, electronic banking or funds transfer services notably arising from migration and more complex micro-insurance services. A lot will still need to be done to enable the MFIs to implement more sophisticated information technologies, to reduce costs and particularly interest rates, which are still higher than those for commercial banks.

### *The conversion of public institutions into MFIs:*

It will be necessary to help the cooperative banks and in particular rural banks dependent on the state to gain enough autonomy to be managed as MFIs and to increase their loan repayment rates; this would then enable millions of farmers to have access to loans, in particular in India and China. PlaNet Finance has offered advice to operations of this type in Mexico and China.

### *The set-up of microfinance subsidiaries by banks:*

Commercial banking institutions will be increasingly tempted to associate themselves with microfinance. Some will be created from microfinance institutions, as in Brazil, Morocco or elsewhere. PlaNet Finance is committed to programmes of this type in Bolivia, Argentina, Morocco and China.

### *Regulation reform:*

To enable microfinance to develop, it is necessary to put in place operational control and supervision policies which ensure the principles of professionalism and independence; it is necessary to emphasise the structuring and regulation of the sector whilst maintaining its dynamism. It is also necessary to choose which institutions in each country should organise the sector's consolidation. Public resources have a major role to play in ensuring the start-up of microfinance institutions and in financing the training of officers and establishment of effective networks. Microfinance must measure its financial effectiveness and its impact on poverty on a permanent basis. We will therefore gradually see increasingly larger sums being used to finance this sector.