

# The Changing Landscape of Microfinance

BY MARILOU VAN GOLSTEIN BROUWERS, TRIODOS INVESTMENT MANAGEMENT

Much has changed since Triodos started its role as an investor in the microfinance sector in 1994 but the pace of change has increased significantly in recent times. Whether it's the environment, food or finance, profound crises have converged with far reaching consequences for individuals and industry across the world. Microfinance, and its customers, are no exception. But in 2009, the impact of these developments has been felt in very different ways across continents and regions, between countries and even between MFIs themselves. What all does this turmoil really mean for the future of microfinance, what are the challenges it throws up for the industry, and what is Triodos Bank's role in it all?

## THE IMPACT OF THE FINANCIAL CRISIS

The impact of the financial crisis has mainly been felt in Europe and the United States. Its direct influence on the emerging markets is less significant. It is important however, because it comes on top of a number of other crises, including volatile food prices during 2009 and 2008. For clients of MFIs, these combined issues can hit hard. Because foreign labour is often the first to suffer in a recession, relatives living in the United States and Europe who lose their job can no longer send money home. Decreased remittances lead to declining income, impacting directly on the lives of MFI clients as much as anyone else. For some, this means it becomes more difficult to repay loans and as a result the portfolios of the MFIs themselves are at a greater risk.

There are considerable regional differences: MFIs in Eastern Europe, Central Asia and Central America have been affected more severely than those in South America, South and South-East Asia, and Africa. Many MFIs in our portfolio reported slower growth rates in 2009 or even a contraction of their portfolios. Some saw their loan portfolio quality deteriorate resulting in high loan loss provisioning levels.

Nevertheless, well-managed MFIs continued to perform well, keeping these changes under control and focusing on the improvement of internal risk management procedures and developing better methods of assessing clients' repayment capacity.

The crisis has increased awareness of the importance of transparency and education of clients. The problem of over-indebtedness of microfinance clients has become increasingly visible, especially in more competitive and saturated markets in Central America, countries like Bosnia and Herzegovina,

and certain states in India. The importance of establishing credit bureaus has become clearer as many countries lack infrastructure to check whether clients have multiple loans from different sources. Transparency is at the heart of Triodos Bank's work. So we actively support industry-wide initiatives that advocate fair and transparent pricing, that make clients aware of their financial obligations. During 2009 *Client Protection Principles* emerged from a group of MFIs and investors – led by Accion and the Consultative Group to Assist the Poor (CGAP). We have signed and committed ourselves to these principles that re-visit what microfinance is really about, helping clients to build their assets and

**'Just as the financial crisis means the mainstream economic system needs to change so it can start to fulfill its proper role in society, so microfinance needs to focus on why it was created in the first place. The upheaval of 2009 makes the need to develop healthy, inclusive financial sectors – supported by values-driven investors – more urgent than ever.'**

improve their lives. Another global initiative that we actively support is the *Microfinance Transparency* initiative. Its goal is to provide each country with a clear and transparent overview of the effective interest rates that are charged by MFIs to their clients.

## THE INFLUX A NEW CAPITAL AND THE ROLE OF SHAREHOLDERS

Investors, and the capital they bring, can make a positive difference. They can provide large volumes of money and commit investments for a longer period of time. They also value professionalism,

forcing efficiencies that are in everyone's interests. Nevertheless, more and more capital has entered the microfinance market in recent years, and it's been a mixed blessing. 2009 was no exception. Some people see a logical progression from donors supporting microfinance in its infancy, to social investors helping it to become financially viable, before more commercial investors replace them to propel the industry further forward to bigger and better things – at a profit. We disagree. The long-term health of the industry depends on well-informed, commercially-astute social investors who understand the importance of financial strength but who are concerned with more than just financial returns.

More than ever, the role of shareholders in MFIs is important. It is important that they subscribe to the underlying mission of the sector and have a long-term vision related to it. New shareholders that are more focused on short-term profit, bring new ownership structures, and the mission is no longer always shared. An increasing number of MFIs aspire to be listed on a stock exchange or sell their shares to the highest bidder. In reality this can create a tension between short-term profits and developments that are in the long-term interests of an MFI's clients.

Profit is essential, because it enables an organisation to invest in the improvement of services and further growth and efficiency. It is also difficult to attract capital in a sustainable way if there is no solid prospect of a financial return for investors. The question is more: What is a balanced return? For example, how does the return on equity relate to the interest rates that clients have to pay for their loans? We strive for a balance between a healthy financial return and a positive impact on society and the environment. We hope to see more investors striking a similar balance. We hope that a movement of 'impact investors' offer a chance to help to make this paradigm shift happen. We're part of a new initiative, the Global Impact Investing Network, precisely so we can encourage this kind of change.

#### **A VITAL CATALYST FOR SUSTAINABLE CHANGE**

Worldwide millions of people are still unable to open a bank account, negotiate a loan or buy insurance. In that respect, we still have a long way to go to make sure that everyone, everywhere, has access to all forms of financial services. I also believe that as microfinance has matured MFIs can embrace opportunities to finance projects that have a positive impact on the environment, as well as other prospects in sectors like housing, water and sanitation, education and agriculture. Many micro-

finance clients need access to energy as well as money and MFIs could do more to help them. MFIs can promote and finance the use of biogas installations and solar energy, especially for people in remote areas who are not connected to the electricity network. During our 2009 International Workshop for our investee partners, it became clear that MFIs see this as a significant opportunity. Poverty alleviation, food security and climate change: the global challenges we face this century are numerous and highly interdependent. At the same time a number of positive trends are emerging to deal with them. There's growing awareness that we have one planet, and need to work together to build a more sustainable future for all of us who share it. We believe the microfinance banks and institutions we invest in worldwide are a vital catalyst for this sustainable change.

April 2010



#### **MARILOU VAN GOLSTEIN BROUWERS**

*is Managing Director of Triodos Investment Management, a 100% subsidiary of Triodos Bank, the leading values-driven bank in Europe. Triodos Investment Management is responsible for managing a number of internationally operating funds that invest*

*in both developing countries and Europe. These fund allow individuals and institutions to invest directly in sustainable sectors, including microfinance, sustainable trade, renewable energy, sustainable real estate, and organic agriculture. Triodos Investment Management has been one of the leading investors in the microfinance sector since making its first investments in the industry in 1994. At year-end 2009 the institution has total assets under management of EUR 1.6 billion, with EUR 236 million in microfinance investments. The microfinance portfolio includes 81 institutions in 40 countries, with equity investments in 19 different MFIs.*

#### **Contact details**

Triodos Investment Management BV  
PO Box 55  
3700 AB Zeist  
The Netherlands  
I [www.triodos.com/microfinance](http://www.triodos.com/microfinance)  
E [microfinance@triodos.nl](mailto:microfinance@triodos.nl)