

# Microfinance: Revolution or Footnote?

Microfinance Over the Next Ten Years



15 May 2018

CGAP  
MICROFINANCE  
GATEWAY

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WEBINAR

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# LOGISTICS

- 1 This is an audio broadcast. Attendee microphones will remain muted during the entire webinar session.
- 2 To ask questions during the webinar, please use the Chat box on the right-hand side of the Webex session. Please submit your question at any time during the webinar presentation.
- 3 To ensure your question is seen by the moderator, select “**All Participants**” from the drop down menu when sending your question.
- 4 The webinar recording will be emailed to all attendees and registrants.

# Speakers



**Ira Lieberman**

LIPAM International, Inc.



**Paul DiLeo**

Grassroots Capital Management PBC



Paul DiLeo

# Agenda

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- Background and Lehigh University Workshop in 2017
- Current State of Microfinance
- How We Got Here
- Key Takeaways from Microfinance
- The Challenges Ahead
- Agenda for the Next Ten Years

# Lehigh University Workshop on the Future of Microfinance

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Paul DiLeo

## WORKSHOP

- ✓ 34 leaders from the microfinance community:
  - Operators,
  - Investors,
  - Academics, and
  - Analysts and representatives of the broader impact investing and financial inclusion communities.
- ✓ Open discussion sessions
- ✓ Goal to bring varied perspectives on microfinance (MF)

# Lehigh University Workshop on the Future of Microfinance

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Paul DiLeo

## KEY QUESTIONS

- ✓ What has MF accomplished? What can it still accomplish going forward?
- ✓ Is MF in decline? Consolidating? Being absorbed? What is its future?
- ✓ What are the major issues impacting and shaping the sector globally and regionally?
- ✓ What are the successors or alternatives to traditional MF models: financial inclusion, fintech, mobile and agency banking? Can they maintain and build on the social content that inspired MF in the first place?



Ira Lieberman

# Current State of Microfinance

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## Outreach and scale far surpassed original goals:

- Microfinance Institutions (MFIs) now reach ~300 million clients
- Includes a mix of formal, regulated credit unions, cooperatives, commercial banks, non-bank financial intermediaries (NBFIs), and non-profit / NGOs



Ira Lieberman

# Current State of Microfinance

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## The MF model moved from donor dependent to commercially viable

- “Cracked” the capital markets and have dependable access to commercial funding
- Attracted \$30+ billion in cross-border investments
- 12+ MFI initial public stock offerings (IPOs) worldwide
- Approx. 80% of MFIs operate profitably





Ira Lieberman

# Current State of Microfinance

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**MFIs have redoubled efforts to keep the focus on the client while adapting to new competitors and business models**

- Continued focus on bottom of pyramid (BOP)
- Struggling to maintain continued engagement by social investors



Ira Lieberman

# Current State of Microfinance

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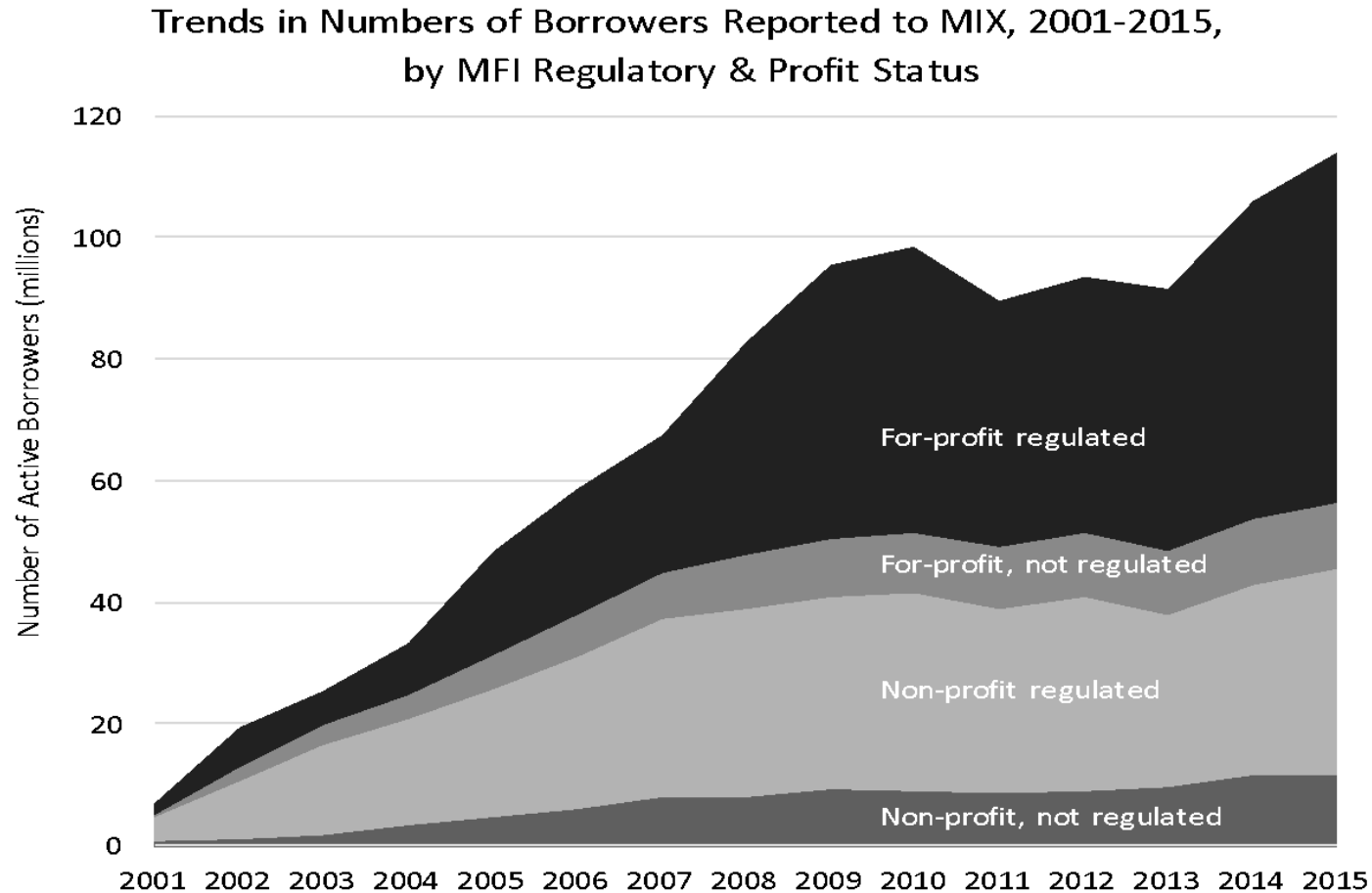
## **Largest single sector among “impact investments”**

- First and only globally scaled double bottom line (DBL) business model



Ira Lieberman

# Trend in Number of Borrowers 2001-2015





Ira Lieberman

# Importance of Institutions with 100,000+ clients

**Advantages of scale:** Increased outreach, increased sustainability and profitability, and lower prices for clients.

Measures of outreach and efficiency, by MFI scale				
<u>MFI scale</u>	<u>Small</u>	<u>Medium</u>	<u>Large</u>	<u>Very large</u>
<b>active borrowers</b>	less than 10,000	10,000 to 100,000	100,000 to 1 million	more than 1 million
<b>Share of total number of MFIs (%)</b>	41	41	16	2
<b>Share of all borrowers (%)</b>	1.3	12	38.2	48.6
<b>Share of all savers (%)</b>	2.6	20.5	48.1	28.8
<b>Median real interest rate + fees (as % of loan, inflation adjusted)</b>	22.2	20.6	17.8	13
<b>Median profit margin (% of revenues)</b>	8.8	9.4	17.1	22.8



Ira Lieberman

# Performance Metrics for Median MFI, 2009-2016

- MFI growth and performance has been healthy across most geographic regions
- Median MFI loan portfolio in all regions outperformed the 3.9% median bank PAR90 worldwide
- Average return on equity for all US banks has been hovering between 7.5% and 10% since 2010

	Africa	East Asia & the Pacific	Eastern Europe & Central Asia	Latin America & the Caribbean	Middle East & N. Africa	South Asia
<b>Active Borrowers CAGR (%)</b>	21.5	10.9	29.7	19.8	22.4	16.4
<b><u>7-year Average of Annual:</u></b>						
<b>PAR90 (%)</b>	3.8	1.4	2.7	3.4	1.5	0.9
<b>Write-off Ratio (%)</b>	1.3	0.2	0.5	1.6	0.6	0.1
<b>Return on Equity (%)</b>	4.6	10.6	8.0	7.7	10.3	11.1



Ira Lieberman

# Ten Largest Savers: Voluntary Savings Accounts, as of 2009

- Savings by regulated commercial MFIs are critical for the poor

Name	Country	Ownership	Regulated	Accounts ('000s)
<b>BRI</b>	Indonesia	Investors/Government/banks	Yes	21,229
<b>Grameen Bk</b>	Bangladesh	Members/Government/Bank	No	7,970
<b>ASA</b>	Bangladesh	NGO	No	6,613
<b>BRAC</b>	Bangladesh	NGO	No	5,447
<b>Equity Bank</b>	Kenya	Investors/Bank	Yes	4,038
<b>Caja Popular</b>	Mexico	Members	Yes	3,514
<b>Khan Bank</b>	Mongolia	Investors/Bank	Yes	2,500
<b>Capitec Bank</b>	South Africa	Investors/Bank	Yes	1,297
<b>UNACOOPEC</b>	Cote d'Ivoire	Members/Co-operative	yes	925
<b>Creditscotia</b>	Peru	Investors/Bank	Yes	808



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# How We Got Here

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- 40 year path of microfinance led to its current position of prominence and success
- Path encompassed 3 key phases and several critical components
  - Grants and concessional funding played a crucial role in successful path of microfinance across all three phases



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# Phase 1

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## **Developing the business model and demonstrating profitability and scalability**

- Bottom-up product design / intensive study of clients
- Tested multiple business models, pilots, trial and error
- Developed corporate structures, building balance sheets
- Specialized Human Resources / Social Entrepreneurs / Governance
- Management Information Systems





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# Phase 2

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## Developing a deep supporting ecosystem and institutional capacity

- Longitudinal performance data
- Benchmarking, metrics
- Emergence of supervisory and regulatory frameworks
- Financial & social “ratings”
- Training, particularly managerial talent
- Industry associations
- Codes of conduct



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# Phase 3

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## “Cracking” mainstream capital markets: international and local

- First loss capital / “Blended” finance
- Portfolio managers
- Microfinance Investment Vehicles (MIVs): > 100; \$15 Billion AUM
  - Compounded growth rate of 20% for total assets
  - Debt represents 82% of investments, equity 16%.
- Liquidity
- Investor education



Paul DiLeo

# Understanding Microfinance's Path

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- Understanding this path and these factors can help highlight:
  - the components necessary to develop a scalable pro-poor business model
  - what may be required for other aspiring impact business models to gain traction
- Newer impact sectors should be able to reduce the timeline and the subsidy requirement, but both will remain significant



Ira Lieberman

# 4 Key Takeaways from Microfinance

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1. Microfinance has exceeded expectations. Pro-poor financial products and services, developed by MFIs, have gone mainstream.

Access has increased to hundreds of millions of families through commercial MFIs and, increasingly, mainstream financial institutions



Ira Lieberman

# 4 Key Takeaways from Microfinance

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2. Traditional microfinance is a proven model, but it faces persistent challenges from new competitors and disruptive technologies.

MFIs continue to require concessional and patient capital to preserve the balance between social and financial objectives and continue their essential role in pro-poor product innovation



Ira Lieberman

# 4 Key Takeaways from Microfinance

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3. As the lines between microfinance and fully commercial financial services blur, a key caution moving forward is in maintaining adequate focus on the social agenda.

MFIs have redoubled efforts to keep the focus on the client while adapting to new competitors and business models



Ira Lieberman

# 4 Key Takeaways from Microfinance

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4. MFIs remain a unique and vital resource, with an extended trust relationship with poor clients and communities and unique potential to advance many SDGs.

Its successful four-decades-long gestation holds many lessons for the path forward.



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# The Challenges Ahead

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***What is required to build on microfinance's accomplishments to date, to preserve a balance between financial and social priorities, and to make meaningful contributions to meeting the Sustainable Development Goals (SDGs)?***





Paul DiLeo

# Poll

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Please take a moment to respond to the poll questions on the right-hand side of your screen.



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# Four Challenges Ahead for MFIs

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- 1. Product Diversification** - future growth and profitability, also improve services to clients.
  - At present product offerings beyond working capital loans and savings is sluggish, represents only ~10-15% of portfolios of major institutions
  - Significant difficulty exists scaling non-credit financial products—lack of marketing skills, need to align compensation incentives, assess the financial commitment
  - New competitors – banks, specialized lenders, MNOs – unbundle and skim off more profitable products



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# Four Challenges Ahead for MFIs

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## 2. MFIs need to adapt to Digital Financial Services (DFS)

- Varying combinations of mobile money, data mining, and algorithmic underwriting probably results in the most angst about competitive threats and new opportunities
- Threaten to undermine and cannibalize incumbent business models
- MFIs have historically taken a low-tech, high-touch approach; DFS is high tech and low touch
- The merger of the two can be a win-win for MFIs, but difficult to pull off
- MFIs need to ensure that budgets, innovation management skills, staff recruiting and training systems, and supply chains are supportive



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# Four Challenges Ahead for MFIs

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- 3. MFIs (above all rural MFIs) should evaluate non-financial services – health, ag extension, water for WASH and irrigation, solar energy**
  - Care must be taken to determine where MFIs can be directly involved and where they need to step aside and facilitate engagement by other partners
  - Offer significant value to clients, especially rural clients, but can compromise core MFI competence
  - Additional services will require time and patient risk capital for experimentation, identification of best practices, infrastructures, and staff, managerial, and board skill sets



Paul DiLeo

# Four Challenges Ahead for MFIs

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## 4. MFIs need to improve Governance

- Governance structures are a core component of effective institutions
- As MFIs grow, expand and diversify, boards need to evolve



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# The Challenges Ahead for MF Investors

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## **MF suffers from its success in capital markets**

- Seen as a commercial investment opportunity
- Fatigue and fashion drive patient capital to bright shiny impact objects



Paul DiLeo

# The Challenges Ahead for MF Investors

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## **Continued pro-poor innovation requires subsidy and patient capital**

- Skill development and training
- Institutional capacity building
- Infrastructure
- Non-financial services and digital finance integration



Paul DiLeo

# Lessons for Impact Investors

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## Impact Investor expectations

- Need to respect the double bottom line of social impact
- Everyone can't always have their cake and eat it too.





Paul DiLeo

# Lessons for Impact Investors

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**Increased commercial investment upsets the balance between commercial and social objectives**

- Key challenge for governance



Ira Lieberman

# Agenda for the Next Ten Years

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- 1. High tech – high touch:** Incorporate Digital Financial Services (DFS) in ways that protect and create value for poor clients



Ira Lieberman

# Agenda for the Next Ten Years

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- 1. High tech – high touch:** Incorporate Digital Financial Services (DFS) in ways that protect and create value for poor clients
- 2. Use infrastructure, market knowledge and relationships** to scale full range of financial products, selectively facilitate non-financial services and advance SDGs



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# Agenda for the Next Ten Years

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- 4. Cultivate and educate investors** to support continuous pro-poor innovation with patient capital and subsidy



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# Agenda for the Next Ten Years

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- 4. Cultivate and educate investors** to support continuous pro-poor innovation with patient capital and subsidy
- 5. Hardwire mission:** Incorporate features in corporate culture and structure to preserve social – financial balance

# Appendix

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## **Workshop Videos:**

Panel 1, Regional Development of Microfinance: [https://youtu.be/qabO\\_EBU8BY](https://youtu.be/qabO_EBU8BY)

Panel 2, Product Diversification: <https://youtu.be/ZC60IXIszEQ>

Panel 3, New Entrants and Competitive Challenges: <https://youtu.be/p9P9XOG0bro>

Panel 4, Financial Inclusion and Impact Investing: <https://youtu.be/tqhvr0JDSrs>

Panel 5, Successes, Vulnerabilities and the Next Ten Years: [https://youtu.be/ZmV5Ls\\_w2hE](https://youtu.be/ZmV5Ls_w2hE)

## **Post-Workshop Blog Series:**

“Microfinance Is Dead; Long Live Microfinance!”: <https://cfi-blog.org/2017/04/20/microfinance-is-dead-long-live-microfinance/>

“Time to Ditch Impact Investing’s Unproductive Self-Analysis”: <https://cfi-blog.org/2017/04/27/time-to-ditch-impact-investings-unproductive-self-analysis/>

“Can MFIs Deliver What Poor People Need?”: <https://cfi-blog.org/2017/05/04/can-mfis-deliver-what-poor-people-need/>

“FinTech in Microfinance: In Search of the High Tech–High Touch Unicorn”: <https://cfi-blog.org/2017/05/11/fintech-in-microfinance-in-search-of-the-high-tech-high-touch-unicorn/>

# Q & A

1

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# Poll

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# What's Next?

1 We will email you when the webinar recording and related materials become available on the Microfinance Gateway website.

2 Join the Microfinance Gateway's next Webinar:

- 24 May - Making the Case for Digital Learning, Gateway Academy

# Thank you

To learn more, please visit

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