

How Can MFIs Best Work in Competitive and Saturated Markets?

Written by

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Improving MFI performance in competitive and saturated environments

Introduction

The Microcredit Summit held in Washington in 1997 came up with the goal of reaching 100 million families with microfinance by the end of 2005. This figure has been attained thanks to the efforts of the entire microfinance community.

Over the last few years, several countries have integrated microfinance into **an economic and development process** that has led to improved access to funding for millions of microentrepreneurs, who are mainly women. Microcredit has facilitated their autonomy, enhanced their integration and improved their status.

The establishment of commercial, profit-making microfinance models has led to competition and to large and diversified services (which translates into reaching more people and higher savings respectively). Nevertheless, this profitability rationale, systematic in nearly all microfinance institutions has led to an increase in the number of sustainable MFIs and has often driven the same microfinance institutions towards more easily-accessible economic activities and zones in order to limit operational expenses. Rural zones in particular have been neglected for urban areas where operational expenses are lower.

This is especially true as a high concentration of competition in some geographic zones and in a number of countries has led to a gradual observation that the diversity of MFI programmes in very competitive markets yields both positive effects (low interest rates, diversification of offer, proximity, etc) and negative effects (higher risk, overindebtedness, occasional unfair competition and profit search geared towards more profitable clients).

The search for market share and profitability should not lead to losing sight of the fact that microfinance institutions have a responsibility towards their clients, the microfinance sector and, occasionally, towards their country's economic policies (typology of funded assets). The development of microcredit should not be accompanied by an increase in default cases and overindebtedness, which

could yield results that are contrary to the initial goal of microfinance which is checking financial exclusion.

Example: Market saturation problems in India

In India, joint surety sometimes discourages MFIs from getting involved in the selection of borrowers. The borrower is chosen by the group, which does not check the borrower's level of indebtedness. MFIs in India do not have organizational and financial means to address these cases on a specific basis.

MFIs establish many Self Help Groups (SHGs) every year. Competition and even conflict may prevail in zones with several MFIs – SHGs leave one MFI for another that provides better access to bank loans, a situation that results in major tension between MFIs.

Many MFIs operating in competitive markets have highlighted the financial difficulties that have resulted from the arrival of new microfinance providers in the market and have expressed concern with regard to long-term cost-recovery.

Nevertheless, microfinance institutions can create value for their clients in a structured, controlled and sustainable manner even in very saturated sectors.

A. Features of a competitive and saturated market

Definition:

A saturated and competitive environment cannot be defined in one word. However, an environment is rated as saturated and competitive according to a number of factors. These include the presence of many MFIs in one geographic zone, a range of financial services for local microentrepreneurs, MFIs difficulty in accessing new clients or retaining existing ones (high desertion rate), competition between MFIs for new clients, clients committing to multiple MFIs, etc. There are a number of indicators, but the central point is that in such an environment, the offer of financial services, especially loans, is higher than the actual microentrepreneurs' demand.

Affected geographic zones

At the first Microcredit Summit, only a few countries (and only a few zones in these countries) seemed to fall into this category, among them regions in Bolivia and Bangladesh. In 1997, it was hard to come across examples of competitive and saturated microfinance environments in Arab or African countries. Over the last nine years, the growth of microcredit in almost all countries in the world has led to an increase in the number of saturated and competitive regions. Big cities in Morocco, El Salvador, Nicaragua, Benin, Mexico, etc, are faced with a saturated, and sometimes very competitive, microcredit environment. Most countries that have well-developed microfinance sectors have some competitive geographic zones.

On a global scale, it is worth noting that saturated environments are mainly found in urban areas and the freedom to set interest rates that enables MFIs to become rapidly profitable and sustainable (thereby facilitating their development) is a tangible factor in the establishment of a competitive environment. The paradox here is that the poorest people, especially in rural areas, are not always covered and many MFIs have not made this segment their objective.

A saturated environment is therefore a difficult “work place” for MFIs (as a result of the prevailing competition) but it nevertheless offers various advantages for the microentrepreneur, among them:

- lower interest rates,
- access to a wide range of products due to the diversity of available MFIs,
- proximity of microfinance agencies.

It is noteworthy that these advantages are not always accessible in saturated zones. In general, it often takes several years of competition before a significant decrease in interest rates and a diversified product offer becomes noticeable. As long as the market is not saturated and the demand surpasses supply, MFIs could be tempted not to make “any effort” to adapt their product, either in the area of interest rates, duration or financed assets.

Although stiff competition between credit providers has some advantages for the microentrepreneur, it can also have a negative impact, notably:

- Borrowing from several institutions, leading to overindebtedness
- Competitive interest rates, leading to a decrease in support services for microentrepreneurs.

We therefore believe that the three main consequences of the presence of several MFIs in the same zone, targeting the same clientele, are: (i) competition, (ii) low interest rates and (iii) risk of cross-indebtedness.

B. Ensuring fair competition

In the first place, one of the main errors is not to avoid or limit the competition between MFIs through agreements between MFIs to share the market. Sharing the market is not a good idea: the competition between the different actors is avoided but these practices are illegal and by dividing the market the microentrepreneurs do not benefit from the competition of the MFIs (low rates, wide range of services ...). Although this principle is obvious, it is not easy to be implemented. Therefore, a small MFI settled in a rural area will see the arrival of

the largest MFI in the country as an invasion. It will think that the competitor is here to 'rob' its clients.

The competition encourages MFIs to broaden their product range which will benefit microentrepreneurs. The MFI can identify markets that are not served and therefore design new products for these markets (niche marketing) thanks to several means: the thorough analysis of the market (analysis carried out thanks to statistical market studies and 'focus group' interviews), analysis of the reasons for the clients departure (questioning the microentrepreneurs about the reasons for their departure from the institution, acute analysis of the dropout rate by product and market segmentation.)

If the MFI wants to be different from other MFIs, it should diversify its product range (specific loans, micro-insurance, money transfers ...) including loan products. It should also offer new products to microentrepreneurs.

Transparency, governance and good practices:

The development and duration of the action carried out by MFIs on the long run can be secured in any environment and especially in competitive environments with efficient governance.

Good practices imply transparency, deontology and ethics. Therefore the microcredit institutions have to share information about the cost and the loan rate that is actually charged, the rights and responsibilities of the clients and the MFI to their clients and to other MFIs. They have to take into account ethical aspects when conducting actions, funding the goods but also when dealing with the stakeholders. The implementation of communication tools between MFIs enables to set an environment of 'fair competition' focused on mutual respect. Several tools, that can be quite easily implemented, can be used before the setting up of new offices to avoid an environment of 'unfair competition': portal for data exchange, credit bureaus (to be explained later), information from the Federation or MFIs Group.

Loan officers have to use good practices, indeed:

- MFIs must explain to their loan officers that having new clients is a process that should be done without underestimating the other MFIs and without using unworthy practices (lies about the services offered by the other MFIs ...)
- MFIs must have a transparent policy about the recruitment of loan officers from the competitors. Loan officers from other MFIs should not be recruited just to gain some clients. It is also important that the loan officers be free to leave a MFI and work in another for personal reasons (salary, proximity, values corresponding more to the 'new' MFI).

Therefore, the structured network of communication tools and the implementation of good practices within an organization or a professional group gathering MFIs is definitely an important means for the implementation of an environment with good competitive practices. There are several networks of MFIs (for instance, consortium AL AFIA in Benin, FNAM in Morocco) that have set up ethical committees to ensure the respect of the principles. In several countries, MFIs share their information via websites (Senegal) and disseminate data about the setting up of new offices.

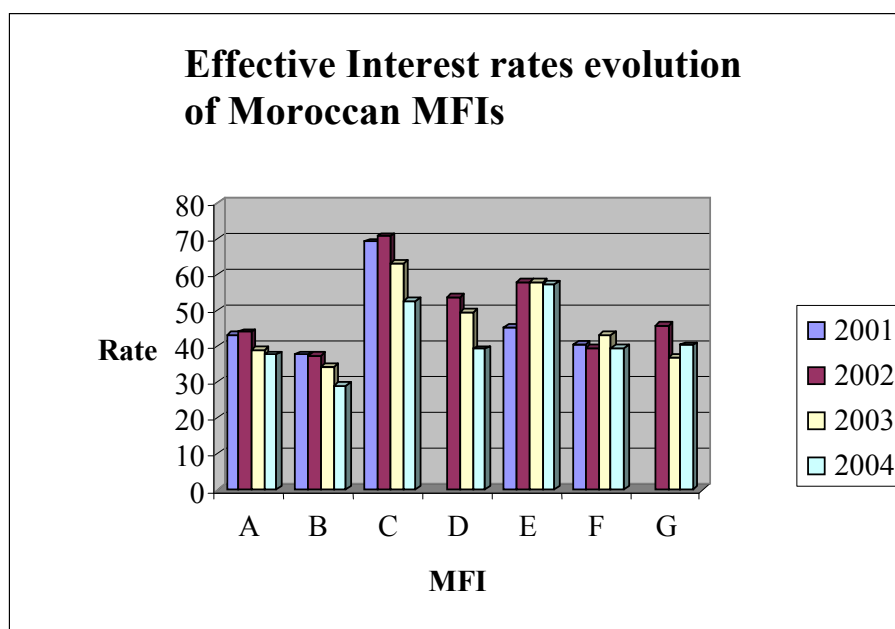
Regulatory bodies like the Central bank or Ministry of the Treasury can play a significant role: oblige financial actors to abide by the rules for good behaviour among themselves, prohibition to default loan.

C. Controlling the effects of competition on the interest rates

A few years ago, the interest rate was not considered as an issue since MFIs and the international community focused on the access to a loan which was at that time limited. The amount of the interest rate becomes an issue when access to credit is guaranteed (for instance during the last campaign for Presidency in Benin). Competition can then foster the decrease of the interest rates.

It is a means to reduce the cost of the microcredit and consequently the interest rates. In several markets where competition exists, operations have been more efficient and at the same time, interest rates have decreased.

However, we can observe that competition alone is not efficient to reduce rapidly the interest rates of every MFI. Most of the times, it is the mechanism used in the processes in addition to the will of the management to lower the interest rate that actually entails a significant reduction. For instance, I have noticed that with a competitive environment that kept increasing from 2001 to 2004, every MFI reacted differently: in some MFIs the interest rate has significantly been reduced (MFIs rated 'A', 'B' and 'C') whereas it was increasing for others ('E', 'F' and 'G').



The decrease in rates should not be avoided because it is beneficial to microentrepreneurs. However, to us, **anticipating, monitoring and compensating** the decrease in interest rates must be the main activities of MFIs and guide the intervention of international donors.

1. Anticipating decrease in rates

- The use of new technologies facilitates the realization of performances and enables the reduction of costs: computing tools, management softwares, innovative payment systems, connectivity technologies such as broad

band and VSAT connections, technologies of service delivery (cash points, network of retail outlets, mobile phone bank).

Communication technologies (mobile phones, internet) also constitute efficient tools to manage financial operations and quickly make transactions ensuring their security.

The use of new technologies facilitates the development of the offer of microfinance products and services and is a way of dealing with the lack of infrastructures and reaching less populated rural areas.

- The implementation of good analytical accounts enables the assessment of the management costs per product and thus the adaptation of its pricing by maintaining a minimum margin.
- Gain productivity: computing tools, use of infrastructures (postal networks...), scoring techniques analyzing the data enabling to foresee the clients' behaviour and providing automatic and standardized risk measures.
- Build client loyalty: by using marketing techniques practised in other sectors (decrease in interest rates, loan renewal, free training...)

The following table presents the different elements constituting the credit cost for the main Moroccan MFIs (figures of the end of 2004). By comparing the Effective Interest rates (hereafter mentioned as EIR) of these institutions with their real costs, it is possible to define the expected profit and to assess the margin between the interest rate and the optimal rate of these institutions:

	G	F	E	C	D	A	B
Outstanding loans	666	343	401	960	2 879	13 516	27 331
Number of clients	3 247	3 622	3 815	8 388	20 485	159 907	160 209
General expenses	22%	47%	39%	40%	24%	20%	19%
Irrecoverable debts	0%	0%	0%	0%	0%	0%	0%
Costs of resources	0%	5%	1%	0%	1%	2%	3%
Yields from the investments	0%	0%	0%	0%	0%	0%	0%
Total credit cost	22%	52%	40%	41%	25%	22%	22%
EIR	52%	40%	58%	64%	30%	45,2%	29,6%
Difference EIR/Credit cost	30%	-12%	18%	23%	5%	23%	8%

We can observe that the effort of industrialization of the processes varied from one MFI to another which led to significant discrepancies on the amount of the EIR.

Anticipation of competition and the decrease of interest rates should guide every MFI towards the development of their productivity with the tools mentioned above.

2. Monitoring decrease in rates

In a competitive environment, the management of a MFI should monitor the amount of the interest rates, which implies the following:

- rate determination strategy within the MFI
- follow-up of rates and costs (good analytical accounts in order to assess the production costs)
- pricing depending on the productivity of the financed activities. We can observe that the pricing applied by MFIs does not take into account the productivity of the financed activities. For instance, a shopkeeper working in an urban area who owns a high profit business will be charged the same interest rate as a farmer who makes much lower profits. In that case, even if the interest rates are identical, the burden on the income of the microenterprise is not the same at all (see example in appendix 2)

3. Compensating decrease in rates

Finally, the MFI should be able to compensate the decrease of the interest rates in order not to question its profitability. This can be achieved by implementing:

- other services: fees for assistance and training of microentrepreneurs, implementation of micro-insurance products (death, disablement, disease), savings...
- value added services, for instance money transfers

For efficient management of a MFI, the various services must be implemented while controlling the arrears.

D. Avoiding cross indebtedness: the cause of overindebtedness

The greater the level of market competition, the more noticeable the problems of cross indebtedness. This can be easily explained: the presence of many MFIs in a same region can encourage some microentrepreneurs to borrow from several MFIs or even to take a loan from one MFI to repay a loan granted by another MFI.

If borrowers are to be in a position to repay their debt, their monthly repayments should not exceed half of their income. However, given the lack of communication between MFIs operating in the same geographical area, and the high supply of microcredit, MFIs risk granting a loan to a borrower who is already a client of another MFI and exceed the limit. These problems, an inherent part of the saturated microfinance market, provide ample encouragement for overindebtedness. Overindebtedness can lead to personal problems for microentrepreneurs and the possibility of unpaid debt for the MFI. Dramatic evidence of this situation was recently seen in India, where borrowers who had taken out microcredit on several occasions from MFIs chose to take their own lives.

For MFIs, a high rate of cross indebtedness can also lead to a high increase in arrears since the clients are not able to repay. The main way of avoiding overindebtedness is the exchange of data between MFIs before the decision to award credit is taken.

Tools enabling the MFI to avoid indebtedness:

- Manual exchange of information (faxes sent between credit agents at various MFIs, listing potential new clients and asking credit agents at another MFI to confirm that the client did not have any outstanding commitments or unpaid debts to the other MFI).
- Computerised tools: credit bureaus or the exchange of information.

Once again, the aims of a credit bureau are to:

- Enable an MFI to assess better a loan requestor's ability to repay the debt, by checking whether they have outstanding loans from other MFIs.
- Provide information on unpaid debts for all microcredits which have been granted.

In regions where competition is greatest, MFIs are increasingly willing to implement credit bureaus. By sharing information on borrowers, their debt levels

and their credit history, MFIs are in a position to reduce the risk of unpaid debt and therefore minimize the chances of losses relating to non-repayment of loans. Even though interest in mutualisation information systems is decreasing, in practice, few countries have credit bureaus, or even databases including clients' economic data.

Nevertheless, advances in technology have meant that the cost of maintaining a major database can be reduced, thus making the operational cost of a credit bureau more reasonable.

Credit bureaus make it easier for financial institutions to reach a decision on whether to grant loans. By having access to a client's credit history, they can more easily assess the risk of the client concerned failing to make repayments. Borrowers who have already failed to meet their credit obligations amount to a higher risk. However, MFIs should not respond to this risk by purely turning down the loan request, but they should also work to amend contract terms to meet the client's profile.

Credit bureaus also benefit customers, since they can reduce the risk of overindebtedness: customers are often unaware of the limit of debt that they can have and the institution will take into account customers' liabilities when calculating repayment levels. Nevertheless, although several institutions are now accepting warranties, the primary objective must still be to avoid overindebtedness.

See appendix 3 for an example of a credit bureau in Bolivia.

The advantages of a credit bureau are the following:

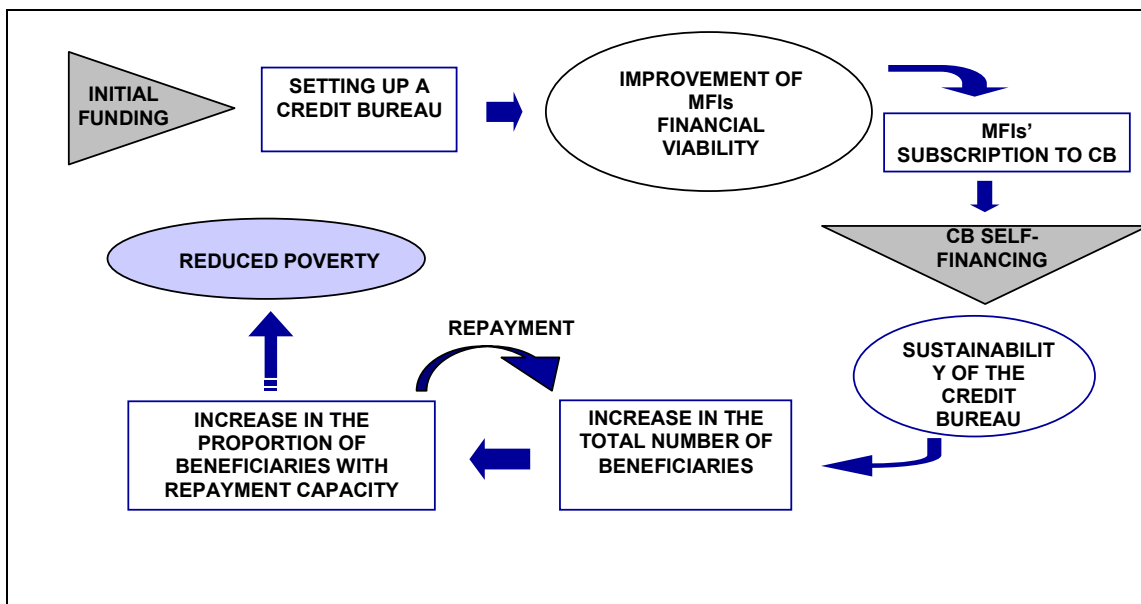
At the client's level

- Increased efficiency in the evaluation of a loan can result in **faster loan processing**
- Clients with a good record can get **preferential services**
- Default prone clients have the **desire to obtain a good report and will hence be encouraged to pay their bad debts**
- **Lower risk of over-indebtedness** by clients

At the institutional level

- **More reliable decision making**
- **Minimizing risk** because of a **better visibility** on borrowers' past and ongoing default history
- **Reducing transaction costs** as it facilitates the analysis and quantification of credit risk
- **Avoiding the aggregation of bad debt** by borrowers among a number of financial institutions
- **Increasing the number of loans granted** as potential borrowers who were before excluded become beneficiaries

Credit bureaus work thus for poverty alleviation:



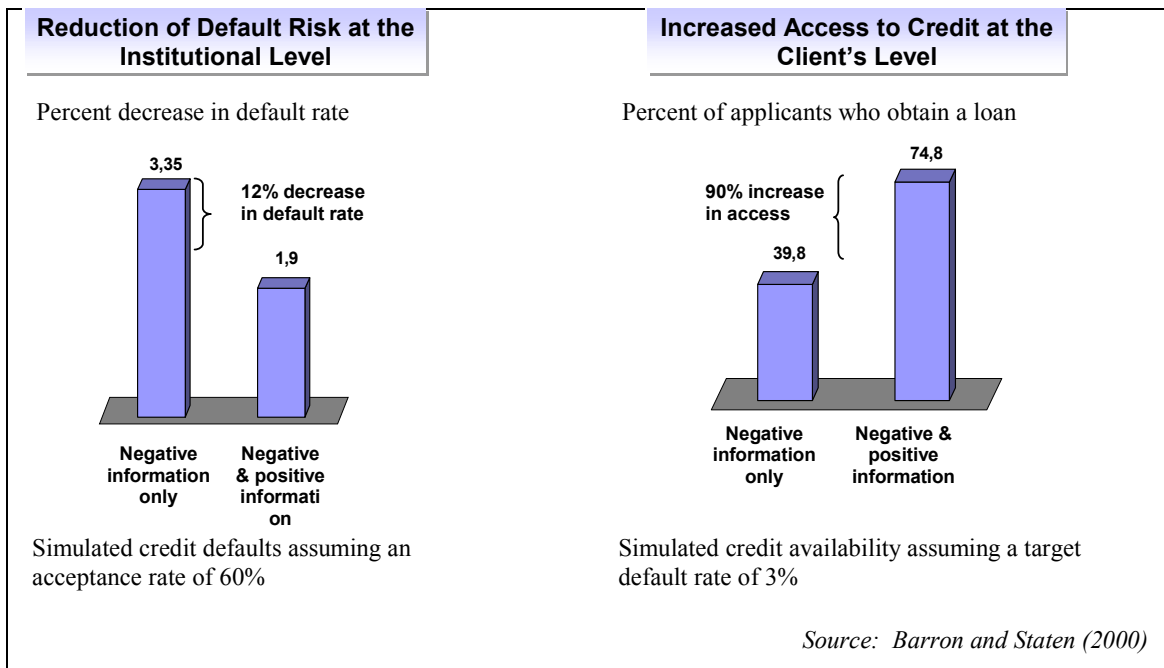
What type of information is exchanged?

The greater the amount of information exchanged, the more effectively the credit bureau can reduce the level of a financial operator's unpaid debt. MFIs can provide direct information on their activities by informing other financial institutions of the distribution of credit provided (sectors, geographical area, age range, profession, etc.)

The information exchanged on clients can be positive or negative:

- information considered as "positive" includes a variety of information on the borrower : the solvency of future clients by verifying the existence and characteristics loans already granted by other MFIs, the amount of outstanding loans, staff information, type of activities, number of loans obtained, type of outstanding loans, guarantees provided by borrowers
- information considered as "negative" only includes details on payment default, information of payment incidents.

By sharing positive and negative information, MFIs can evaluate risk more effectively, enabling them to reduce unpaid debt and increase the number of clients as presented in the following diagram by Barron and Staten:



E. The consequences of regulation: implementing a suitable legal context.

A legal framework encouraging – or even enforcing, in the case of the MFRC in South Africa –the setting up of credit and information exchange bureaus would enable the smooth running of microfinance operations.

By pursuing policies to encourage competition between credit providers and the application of well designed measures to protect consumer and to actively encourage transparency, the viability of microcredit operations could be enhanced, all the while protecting consumer interests.

The regulatory bodies may impose:

- Principles of transparency : uniform calculation and notification of interest rates
- Conflict mediation between MFIs and microentrepreneurs or between MFIs
- A grace period after the signing of the loan contract during which the latter can be cancelled.

1. Consumer protection

At present, the microfinance sector is increasingly concerned with consumer protection. Problems surrounding overindebtedness and the practice of high interest rates have fuelled the debate on the responsibility of MFIs towards consumers.

The search for profitability and the implementation of commercial models raised public awareness of consumer rights. Financial operators (sometimes less concerned than MFIs about principles of social responsibility) have been able to access the microcredit sector. Under these circumstances, the poorest borrowers are the most vulnerable.

The main areas in which consumer protection exists are: the obligation to disclose information, the prohibition of a number of loan practices, the

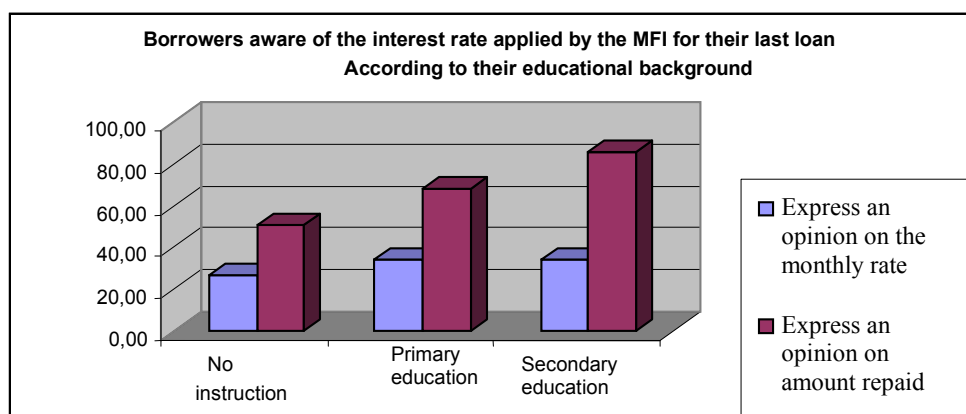
implementation of grievance procedures, conflict resolution and consumer training.

These measures can be applied in different ways throughout the loan cycle:

- Self-regulation within the microfinance sector
- Self-regulation within the MFI
- Implementation by government agencies

2. Notification of interest rates

In a competitive and saturated environment, if the microentrepreneur has access to financing from several MFIs, he should select the MFI that charges the lowest interest rate. Unfortunately, we have noticed that most microentrepreneurs do not know about the amount of the interest rate applied to their loans. During a study carried out on this subject in Morocco, I noticed that less than 30% of microentrepreneurs were aware of the amount of the interest rate for their loan (even more, the amount given was not correct in more than 60% of the cases.)



As a result, the access to several credit operators in saturated areas should lead MFIs to provide better information to clients, especially on applied rates so as to give the opportunity to the client, fully aware of the conditions, to choose the appropriate credit.

Notification of this information can take place in the form of loan contracts or through agencies. It can also be clearly provided during training sessions.

3. No limits on rates (see the examples of Nicaragua and Western Africa in Appendix 4)

At present, some 40 countries set a maximum interest rate cap. A result of this policy is that poor clients are denied access to microcredit, as it prevents financial institutions from recovering costs, the end result being that they are forced to withdraw from the market. Indeed, in order to be operational, MFIs have to achieve minimum profitability (which starts with the recovery of costs), in order to act independently of subsidies, to be able to develop their services and to provide products tailored to their clients' needs.

Moreover, limits on interest rates do not encourage credit cost transparency on the part of financial institutions. MFIs compensate for losses caused by setting interest rate cap by charging their clients in the form of not clearly defined costs and commission as part of their operational costs.

In addition, public organizations are generally unaware of the cost structure involved in microfinance when setting interest rate cap. They are generally based on the business of commercial banks who agree loan amounts that are generally higher than those offered by MFIs.

Setting interest rate cap is particularly dangerous for "high risk" economic sectors and rural areas, where it is more costly to operate. It prevents MFIs operating in rural areas from moving into more populated urban areas that are better equipped in terms of infrastructure. It also discourages financial institutions from operating in these areas. MFIs can also be tempted to make up for losses arising from the setting of interest rate cap by restricting operational budgets (by reducing staff numbers and logistical resources) or by specifically targeting richer clients at the expense of poorer ones.

In a competitive environment, the regulatory bodies do not have to set an interest rate cap since competition induces a decrease in the interest rate as we have previously seen.

Acknowledgements

I would like to thank Pascale Geslain, Jérôme Aba, and Mohammed Maarouf, all working for PlaNet Finance, for sharing their ideas.

I would also like to thank the Moroccan MFIs which provided me with significant information during the three years I spent with them (2003, 2004, 2005) and for enabling me to follow up the impact of increased competition and the actions to implement on site.

Finally, I would like to thank Peer Stein from the IFC for his very clear presentations on credit bureaus which I had the opportunity to attend on several occasions. I have reproduced some of his ideas in this paper.

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Appendix 1: Differences between credit bureaus/credit scoring and public credit registries

Credit Bureaus

A Credit bureau is a software, an institution through which creditors exchange information about their clients' repayment histories and debt profiles. Bureaus act as brokers by collecting, organizing, and disseminating this information.

Credit Scoring

Credit Scoring is a quantitative method tool used to predict risk based on the performance of past loans with characteristics similar to current loans. It therefore assumes that the performance of future loans with a given set of characteristics will be like the performance of past loans with similar characteristics.

Public Credit Registries

In addition to providing information about loans, Public Credit Registries serve additional purposes, such as enforcing bank supervision, providing economic research, and improving bank regulation.

Appendix 2: Difference in productivity in terms of activities funded and the interest rate proportion of the declared profit

Model results from a study of 200 clients from 4 Moroccan MFIs

MFI	Activity	Average loan amount	Average loan period (months)	Average declared monthly turnover	Average monthly financial costs	Average monthly declared profit	Average profit + financial costs	Actual interest rates ¹	Share of interest rate of declared profit
MFI A									
7 pers	Agriculture-rearing	3,000	6	1,000	117.5	250	367.5	47%	47 %
28 people	Craft	4,000	9	1,600	156.6	400	556.6	47%	39.2 %
14 people	Commerce	3,000	6	2,600	117.5	600	717.5	47%	19.6 %
MFI B									
8 people	Agriculture-rearing	4,000	9	1,150	221	400	621	66.3%	55.3%
28 people	Craft	3,000	8	1,600	165.8	500	665.8	66.3%	33.2 %
14 people	Commerce	3,500	9	2,800	193.4	1000	1,193.4	66.3%	19.3 %
MFI C									
16 people	Craft	5,000	4,25	4,000	123.3	1750	1,873.3	29.6	7 %
23 people	Commerce	5,000	4,25	6,000	123.3	2000	2,123.3	29.6	6.2 %
7 people	Services	5,000	8,5	10,000	123.3	2500	2,623.3	29.6	4.9 %
MFI D									
9 people	Craft	6,000	9	2,400	193.4	2000	2,193.4	37.9	9.7 %
20 people	Commerce	7,000	9	7,000	221	1350	1571	37.9	16.4 %
7 people	Services	7,500	12	3,600	236.9	1200	1,436.9	37.9	19.7 %

¹ These rates have been calculated on the basis of the average loan period for each activity within each association based on a rate per association, also calculated from the monthly rate, financial costs and by summarising the characteristics of the sample. Although all efforts have been made to calculate these as accurately as possible, they are approximate and their accuracy is dependent on the information provided by microcredit associations.

Appendix 3: Example of the Bolivian credit bureau

The Bolivian credit bureau is considered as a public asset because it helps to stabilize the financial sector, which influences the general state of the economy. The existence of the credit bureau has helped to improve repayments from institutions in liquidation, including Banco Cochabamba, BancoSur, and Banco Internacional de Desarrollo.

Clients know that they will have difficulties accessing a loan from another financial institution in the future if they don't repay their existing loan, even if the existing loan was borrowed from an institution that no longer exists. The credit bureau is a useful tool for those regulated institutions that have access to its database. Financial institutions can use the Bolivian credit bureau not only to check a client's credit history, which facilitates more informed loan decision-making, but they can also use the information to avoid client overindebtedness, a growing problem in Bolivia in the past two years.

The financial institution's process of participation in the data collection and information sharing includes the following steps:

- Collecting client information.
- Submitting data. Sharing information.
- Using the information for loan decisions.

However, many microfinance institutions are not regulated and do not have access to the superintendency's credit bureau to assess client indebtedness. Microfinance providers have sought to overcome this and other limitations of the superintendency's credit bureau by creating informal systems for information sharing and by tapping other sources of public information. In addition, the superintendency is researching the possibility of expanding its services to unregulated microfinance institutions in the near future.

Two interesting consequences resulted from the creation of the Bolivian credit bureau. First, the current credit bureau system was structured in such a way that it undermines the solidarity lending method and has added to the movement away from group lending toward individual lending in Bolivia.

Second, some financial institutions have used the client information in credit history files to steal customers from other financial institutions, which has probably fuelled the competitive environment in Bolivia.

Bolivia's credit bureau undermines the solidarity lending method by tracking only individuals who defaulted, not their associated group members. Solidarity lending works well in a strong economy to reduce credit risk resulting from moral hazard—the risk of loan loss from clients who have no intent to repay.

However, when there is an economic downturn, as in Bolivia now, financial difficulties can lead to default for some clients. The default of one member can result in a domino effect, in which others drop out of the group instead of repaying the other member's loan.

Because Bolivia's credit bureau does not track this information, a group client can refuse to cover another member's loan loss without impacting his or her ability to access a loan from another institution in the future. As the cohesion of many solidarity groups eroded during the recent economic crisis in Bolivia, Caja Los Andes took advantage of the situation by significantly increasing its client base; it offered individual loans to former group clients of other MFIs for the first time.

Limitations of the system:

- Stealing clients. Some MFIs have used information in the credit bureau to steal each other's business. For example, when a credit check reveals that the client has a loan with another financial institution, one MFI admitted that it often issues the client a loan sufficient to pay off the other loan and to meet its additional financing needs. Client stealing is a natural phenomenon of a competitive industry. With or without a credit bureau, financial institutions always attempt to steal business from their competitors.
- The superintendency does not regulate microfinance NGOs and foundations, so their loan clients are not included in the database.

Source: Client Information Sharing in Bolivia, by Anita Campion, May 22, 2006

Appendix 4: Example of interest rate cap. Nicaragua and West Africa

The example of Nicaragua (2): moving away from rural regions and charge increase

In 2001, the Parliament of Nicaragua has set an interest rate cap. According to the President of the association for Nicaraguan MFIs, the growth of the portfolio has dropped from 30% to less than 2%. Moreover, the application of an interest rate cap has led several MFIs to leave rural regions where the risks and the operational costs are higher. In order to carry on with their activities after the application of the interest rate cap, the MFIs have added some extra expenses to the costs of credit. For instance, an organization has applied compulsory administrative costs which resulted in the clients' inconvenience. Another MFI asserted that the implementation of an interest rate cap had led to the reduction of its income by 50% which forced the dismissal of 25% of its staff.

The example of Africa: increase in the outstanding amount and abandoning of poorest clients

In 2004, the Central Bank BCEAO fixed the microfinance interest rate cap at 27% in West Africa. As a result, Freedom from Hunger, an International NGO, reported that several MFIs had moved away from the poorest and most marginalized populations to concentrate on the urban areas where the expenses to cover the sector were less important. The MFIs in West Africa have increased their portfolio and may presumably offer their services to richer clients to handle the application of the interest rate cap. Unfortunately, these measures have not been efficient: 22 out of 24 Malian MFIs are not financially sustainable. Moreover, the application of the even lower interest rate cap imposed to commercial banks (18%) has discouraged people from getting involved in the sector of microcredit.

² Example from the article *Microcredit Interest Rates in Bangladesh, 'capping vs competition'*, paper produced for the Donors' local Consultative Group on Finance, David L. Wright, Dewan A.H. Alamgir, March 2004