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## Market study

## Microfinance in the Netherlands

March 2009, Willem Nolens

## Executive Summary

- This study aims to quantify the size and characteristics of the microfinance sector in the Netherlands and the feasibility of starting an independent for-profit microfinance institution (MFI). The study is based on 205 in-depth interviews with small and micro entrepreneurs.
- Of every 100 eligible entrepreneurs (fulltime, 0-4 employees, excluding advisory services), 39 have no or limited access to commercial business loans. Of these 39, only 11 express interest in receiving a loan.
- Other important characteristics of micro entrepreneurs with appetite for loans are: relatively young businesses, allochtonous entrepreneurs significantly over-represented (67%), operating from rented premises. The average equity is EUR 16K and the estimated average loan size at disbursement is EUR 7K.
- Branch of the MFI requires 400 clients to break-even. This implies that only 4 major cities in the Netherlands qualify for a branch. This is not sufficient to reach institutional break-even (14 branches).
- Banks seem most well-equipped to downscale their operations and serve micro entrepreneurs in a profitable manner. Most importantly, banks should improve their credit assessment by reducing their dependence on documentation and automation. Loan officers should expose themselves to the field and (re-)gain skills to do a sound credit assessment.
- Governments and NGOs should limit their role to facilitating the development of a sustainable market for microfinance and stimulating private actors, in particular banks, to serve the target group.

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### 1. Objectives

- a. Estimate the potential demand for microfinance in the Netherlands
- b. Assess the main characteristics of the target group
- c. Assess the feasibility of a commercial MFI in the Netherlands

### 2. Definitions

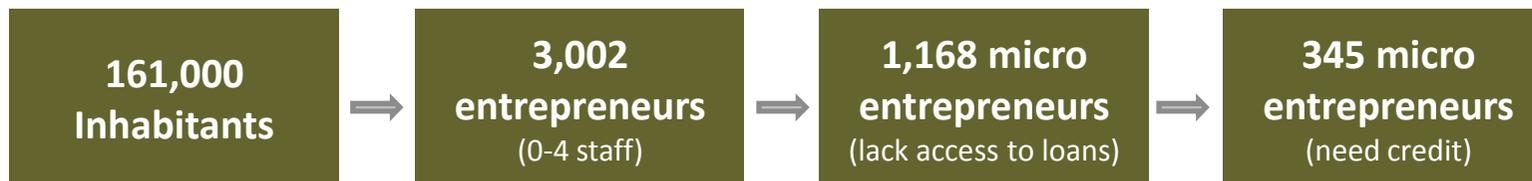
- a. Medium-sized entrepreneur: owner of a business with 5-50 employees
- b. Small entrepreneur: owner of a business with less than 5 employees who has sufficient access to business loans from banks
- c. Micro-entrepreneur: Owner of a business with less than 5 employees who has, or perceives to have, no or limited access to business loans from banks

### 3. Approach

- a. Identification of 600 entrepreneurs (0-4 employees) and selection of representative group for in-depth interviews
- b. Development of marketing tools (brochure, local newspaper coverage, website)
- c. In-depth interviews with 205 small entrepreneurs
- d. Interviews with other stakeholders – community centers, banks, governments, potential investors

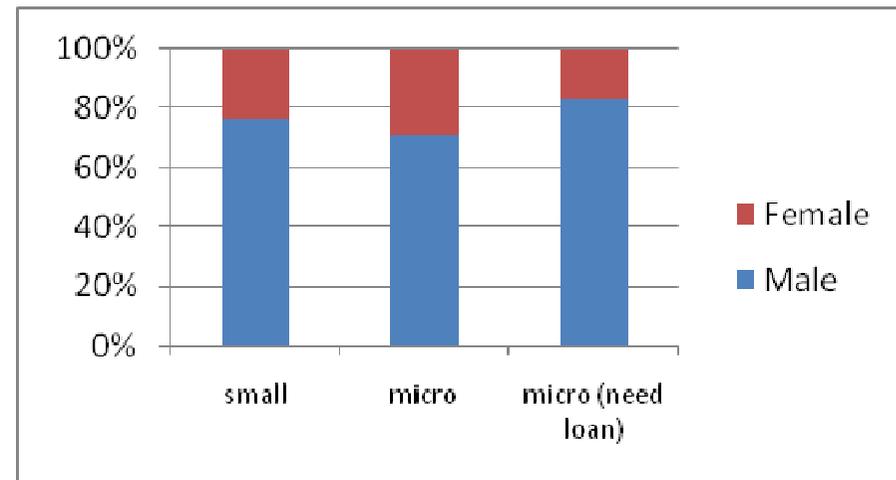
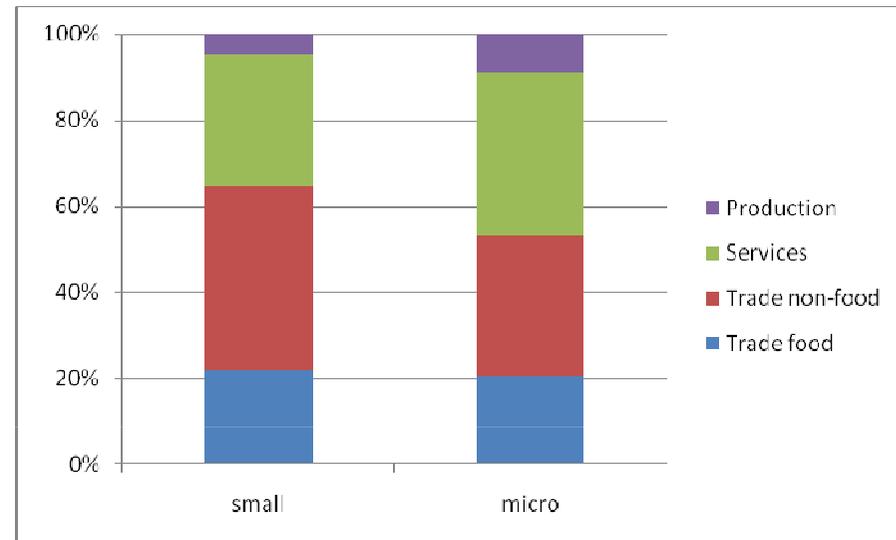
### 1. Size of target group

1. Nijmegen hosts 161,000 inhabitants (CBS, 2009)
2. Nijmegen hosts 3,002 eligible entrepreneurs (0-4 employees, fulltime business owners, advisory services excluded) (KvK, 2009)
3. MicroFin estimates that 1,168 of these entrepreneurs (38.9%) can be considered micro-entrepreneurs, as they lack or perceive to lack sufficient access to business loans
4. An estimated 29.5% of these micro-entrepreneurs is possibly desirous to apply for a business loan, if possible, during the coming 0-3 years. In other words, the total potential market is 345 micro entrepreneurs in Nijmegen



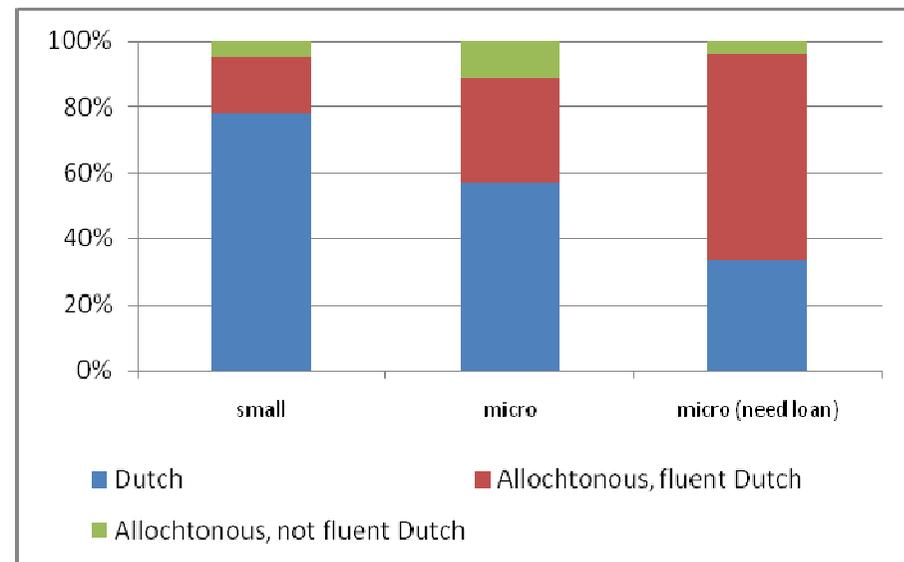
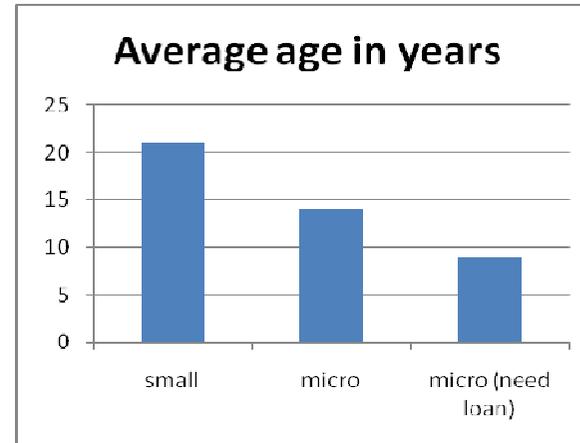
### 2. Characteristics of target group (1/3)

- 1. Activity:** micro-entrepreneurs are slightly more often involved in services and small-scale production. In particular enterprises in the hospitality sector (perceive to) lack access to credit.
- 2. Gender:** Male entrepreneurs have slightly bigger businesses than their female counterparts. Female entrepreneurs seem more risk averse and have lower appetite for loans



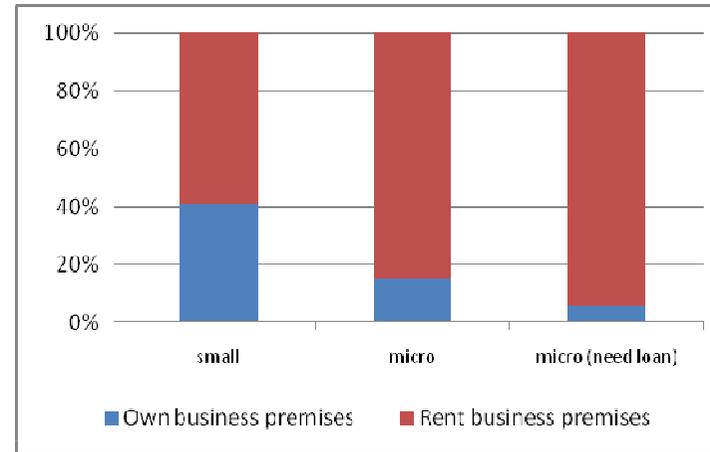
### 2. Characteristics of target group (2/3)

- 3. Age:** micro enterprises are younger, in particular those that in need of funding
- 4. Descent:** The group of micro entrepreneurs includes relatively many allochtonous entrepreneurs, and this group represents even 67% of the micro entrepreneurs with appetite for loans.

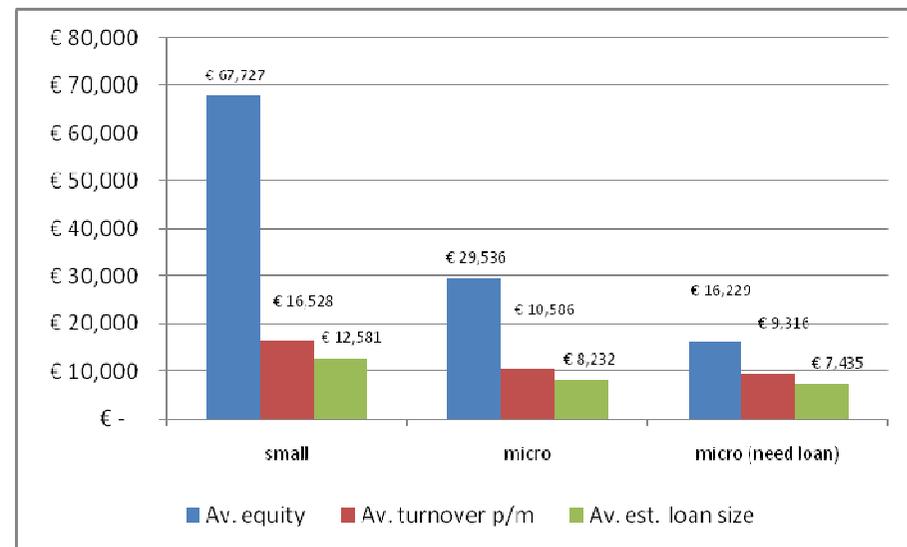


### 2. Characteristics of target group (3/3)

**5. Ownership business premises:** micro entrepreneurs hardly own their business premises; real estate owners have better access to bank credit (i.e. mortgages rather than business loans)



**6. Size:** Micro entrepreneurs, in particular those in need of a loan, are significantly smaller than small entrepreneurs. This is partly explained by the ownership of business premises (see 5.) . The average expected principal loan size is EUR 7,435.



### 3. Feasibility of a for-profit microfinance institution in the Netherlands (1/2)

#### Assumptions

1. The optimal lending model for the Netherlands is an individual lending model (“ProCredit style”) with credit assessments based on historic and present performance rather than future projections. Consequently, eligible entrepreneurs should have at least 6 months track record.
2. The MFI should optimize its efficiency by standardizing its procedures but still have a decentralized approach with local presence (its scope preferably to be limited to one city) in order to build local knowledge, client commitment and reduce the risk of default and drop-out.
3. Other assumptions include:

Average loan at disb.	EUR 7,435	Debt-equity ratio	4.0
Effective interest rate:	17.5%	Costs of debt:	5.0%
Loan officer productivity	200 disbursements p.a.	Operating Expense ratio	9.6%
Minimal staff per branch	3 FTE	Loan loss provision	3%

### 3. Feasibility of a for-profit microfinance institution in the Netherlands (2/2)

#### Conclusions

1. A branch reaches break-even (ROA 0.7%, ROE 3.3%) at 400 clients with total assets of EUR 1,487,000
2. A branch is at all times not expected to reach more than 40% market penetration (i.e. at least 1,000 micro entrepreneurs with a potential demand for credit are required for a branch to reach break-even).
3. 14 branches are required to reach institutional break-even (total assets: EUR 20.8 million)

#### Practical implications

1. Nijmegen hosts 345 micro-entrepreneurs with demand for loans. A branch with a market share of 40% would serve 138 clients. Therefore, it is not feasible to commence a branch in Nijmegen
2. Amsterdam could host 2 branches, Rotterdam, the Hague and Utrecht each 1. Assuming a market share of 40% in these cities, the MFI would serve 2,042 clients
3. Despite this, it is not likely that the MFI could establish 14 profitable branches and reach institutional break-even in the Netherlands.
4. An MFI could add services to generate income and raise client commitment. Such service could include insurances, financial planning, advisory services, etc.

## C. Recommendations

1. It seems currently not feasible to start an independent for-profit MFI in the Netherlands, mainly as the target group is too small, and the interest margin insufficient to cover the operating and financial expenses.
2. Subsidy-dependent alternatives are expected to have limited impact and may tend to crowd out commercial initiatives. Governments and NGOs should play a facilitating role and stimulate private actors, in particular banks, to develop a sustainable market.
3. Existing banks seem most well-equipped to downscale their credit operations to include non-conventional credit lines to small entrepreneurs. Banks have access to cheap funding and can offer microfinance at limited marginal costs. Finally, most micro entrepreneurs have a banking relationship for years, facilitating a smooth credit assessment and lowering the risk of default and drop-out.
4. Banks that in the end manage to serve the target group in a profitable manner, will have refrained from further standardizing and automating their credit procedures, but instead have opted to re-expose their staff to the field to re-develop their skills to do a sound credit assessment.

## D. Further information

1. This research would not have been possible without the great contribution of the following persons:
  1. Mariette van der Beek      senior researcher
  2. Walid Aga                      analyst
  3. Willemijn Verhoeven      analyst
2. IP: All data and conclusions presented herein are the sole intellectual property of MicroFin and can only be published in whatever form with the written consent of MicroFin.
3. Parties interested in obtaining a full version of the report or the data set are kindly requested to contact MicroFin. Please note that charges will apply.
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