Graduate Institute of International Development
and Applied Economics

THE POTENTIAL OF LEASING THROUGH MICROFINANCE INSTITUTIONS IN EMERGING MARKETS

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Dissertation prepared in partial fulfilment of the requirements for the Master's Degree in Development Finance

September 2010

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List of Abbreviations

HP	Hire Purchase
IFC	International Finance Corporation
ILO	International Labour Organization
MFI	Microfinance Institution
NLCL	Network Leasing Corporation Limited
SME(s)	Small and Medium Sized Enterprise(s)
$	US Dollars
$M	$Millions
$B	$Billions

Acknowledgements

I would like to acknowledge the help and assistance of Dr. Nick Beard, my supervisor. The staff, students and facilities of the University of Reading have stimulated and informed this work.

Abstract

This study uses a literature review, structured interviews and a questionnaire to demonstrate that leasing has the potential and stakeholder support to be a useful additional product for microfinance institutions (MFIs) funding the expansion of micro enterprises. The key advantages of leasing in this context are its reduced need for collateral due to retained ownership by the MFI/lessor, and the similarities in processing and customer base between leases and loans.

The sustained efforts of development agencies to encourage the development of leasing in emerging markets through traditional banks and independent leasing companies are described. MFI and funder support for leasing is demonstrated through interviews and a questionnaire. Both show broad agreement that the major constraint to leasing expansion is MFI expertise. Other potential obstacles to leasing such as funder reservations and lack of demand are not supported by the questionnaire results.

Despite the lack of MFI expertise this study concludes that large MFIs are still the best channel through which leasing can reach small and micro enterprises, in emerging markets where institutional barriers to leasing have been overcome. MFIs offer the significant advantages of a large base of potential micro enterprise customers, established funding channels and stable management. Expertise issues could be overcome with development agencies engaging with MFIs for leasing development and redirecting a proportion of lease development funding to MFIs for leasing capacity building. This would enable leasing to reach the micro enterprises that form part of the newly banked MFI customer base.

An outline of a potential field based project is presented linking the funding and capacity building expertise of development agencies with the processing capacity and customer base of a large MFI together with the distribution network of a manufacturer or distributor of green technology relevant to micro-enterprises.

Chapter 1 Leasing and Microfinance in Emerging Markets

1.1 Background

International development institutions have targeted both microfinance and leasing for direct investment and capacity building in order to broaden and deepen financial services in less developed economies. The result in microfinance has been the establishment of a substantial and growing new sector with microfinance institutions (MFIs) with social and commercial impact. For leasing the picture is less clear cut with a continuing failure to reach small and micro enterprises and no new leasing organisations emerging with the scale of the larger MFIs.

Leaving aside the question of why both financial services grew differently, it is now the case that the success of microfinance on its own has changed the conditions for the leasing. Today funders are more accustomed to supporting new financial services in emerging markets. Large scale MFIs are complex organisations that can source, process and account for large volumes of small scale financial transactions. Millions of new customers have been created that are already using financial services, and potentially available for new products. All of these factors also favour leasing. Will the future for leasing in emerging markets be different as a result?

Prior to undertaking this research the author worked as a professional manager and investor in European equipment leasing companies. He has specialist knowledge of the operations and success factors for equipment leasing companies in Western and Eastern Europe, though not, prior to this work, of the microfinance sector.

1.2 Aims and objectives

This dissertation examines whether leasing can expand as a financial service in emerging markets through MFIs. By reviewing the literature and collecting data directly from observers and stakeholders in both the microfinance and leasing sector it

- Re-examines the case for leasing in emerging markets
- Looks at the barriers to leasing in emerging markets in general, and through MFIs in particular
- Proposes next steps to take advantage of the new conditions created by MFIs and to overcome the barriers that are in place

1.3 Research Design

The work was structured in 4 parts.

1. The published literature on leasing in emerging markets was reviewed
2. A series of structured interviews with microfinance and leasing sector experts were conducted to identify a short list of key issues around leasing through MFIs in emerging markets
3. The output of the structured interviews were used to inform the design of an initial survey questionnaire delivered to a wider audience of MFI and leasing stakeholders
4. The results of steps 2 and 3 were analysed and further work is proposed to increase the availability of leasing through MFIs

In the absence of an active debate on leasing in the context of microfinance it was felt that a questionnaire with few, clear themes would engage respondents more that an open ended request for opinions. The questionnaire was structured to encourage respondents to comment on or rate particular statements, but also allowed space for comments and alternative perspectives.

1.4 Guide to the reader

The dissertation is arranged as follows:-

Chapter 1 - Introduction contains this background, aims and objectives, research design and guide.

Chapter 2 – Literature Review covers what is meant in the context of this work by microfinance and leasing, and the scope of both in the developing markets. Those markets where leasing and microfinance co-exist are identified. Given the extensive and widely available statistics and reports on MFIs this chapter focuses on the much slimmer literature on leasing in a development context, and where available, on leasing in a microfinance context. Much less successful emerging market leasing has been documented than microfinance.

Chapter 3 - Methodology lays out the design and conduct of structured interviews followed by the how the outputs of the interviews were used to design a survey questionnaire. The identification of the target stakeholder respondents is also described.

Chapter 4 - Results and analysis uses qualitative and quantitative techniques to establish the level of agreement or disagreement on the range of theoretical and practical barriers that are slowing or preventing leasing from being a significant product in MFIs.

Chapter 5 – Discussion examines the consistency of results from the literature review, the structured interviews and questionnaire. A case is made to use MFIs for the expansion of leasing together with a suggestion as to how this might be funded.

Chapter 6 – Further Work looks at how to proceed from the initial results obtained to pilot leasing projects in the field. Key issues to be addressed and a number of alternative structures are described.

Chapter 2 - Literature Review

2.1 Introduction

In this chapter the existing literature is reviewed to introduce and quantify the scope of microfinance and leasing. Because it is quickly established that microfinance arose and is strongest in emerging markets, more space is devoted to illustrating that leasing is not simply a product for developed markets. Published data will show that large scale leasing and large scale microfinance overlap in a number of developing markets. A comprehensive review of published articles on leasing further demonstrates both the amount of work done to encourage leasing in these markets and the widespread agreement that the expansion of leasing here is desirable.

2.2 Overview of Microfinance and Leasing

Microfinance. According to some microfinance is simply 'small scale financial services' (Robinson, 2001) while to others it is the provision of 'high quality financial services to everyone who needs them especially low-income and previously excluded people' (Rhyne, 2009). Both views emphasise the essential innovation of microfinance which is the miniaturisation of banking. Rhyne and others see as distinctive the social goal of targeting the poor in order to enable them to access the benefits of financial services from which they have previously been excluded. Microfinance started in developing markets and continues to expand there. According the Consultative Group to Assist the Poor (CGAP) at the World Bank by 2007 there were over 3000 MFIs reaching 133million clients (CGAP, 2010) and assets were over $44B (The Microfinance Information Exchange, 2010). Its principal product is small loans, with a small and growing amount of savings.

Leasing is a collateralised lending product that is possible under a certain set of regulatory conditions. It is widespread in the financial services' sector in the richer nations, in bank portfolios, standalone leasing companies and leasing 'captives'. Functionally it can be described as long term rental to a single client. Its attractiveness as a financial product stems from the separation of ownership and

use over the full useful life of an asset. This innovation allows different types of organisation to satisfy their particular needs more specifically which in turn creates pricing and productivity opportunities as described next.

From the end user or lessee perspective there are three principle benefits to leasing. First it is more affordable than short term leasing which typically must factor in the wear and tear of multiple users. A lease contract is between the owner and a single user and lasts for the entire productive life of an asset. Next, not having the resources to buy an asset that will benefit your business over the long term is no longer a barrier to acquiring the asset. By converting initial large capital outlay to a stream of smaller payments over time, leasing enables small business to overcome capital impediments (Higson, 2003). Thirdly if an asset can improve a business' productivity but is unaffordable from the existing cash flows of the less productive current state, the possibility exists to persuade a lender/lessor that the reliability of repayment will be *enhanced* by the increased cash flows resulting from leasing of the asset. Creditworthiness will be enhanced by leasing a productivity enhancing asset i.e. the asset 'self collateralising'. Thus the potential of the small business to increase its profitability by skilfully using new capital equipment becomes an important positive factor in the credit decision, increasing credit options.

From the owner/lessor perspective, retaining ownership of an asset mitigates the credit risk of the end user by facilitating repossession. In jurisdictions where leasing and the separation of ownership and usage are recognised, there are much fewer legal barriers to repossession than to enforcing a lien. Additionally, when done at scale, the leasing of equipment presents additional income opportunities. First, a lessor rapidly becomes a major purchaser of particular types of equipment and therefore has bargaining power to obtain lower costs and better terms. As the owner of a large portfolio of equipment the lessor becomes expert in the value of the equipment and can make the most efficient and profitable disposal decisions for equipment at the end of lease, whether through sale at a heavy discount to the lessee, or in the open market.

A third and very significant factor in the development and continuation of leasing is the fiscal and industrial policy of the government. It is common for governments to encourage capital investment by companies and enterprises by allowing owners to deduct a portion of the cost of their new equipment from profits before tax is calculated i.e. depreciation. Leasing, with its separation of ownership and usage enables this benefit to be redistributed more efficiently in an economy. Companies with a lot of capital can purchase equipment, lease it, and claim a large deduction from their profits before tax. Small companies with small profits can use leasing to transfer their depreciation to these larger companies in return for a favourably priced lease rental. Leasing therefore redistributes tax capacity while encouraging investment by small companies in more productive equipment (Higson, 2003).

There is another consequence of leasing that further enhances its role in a diverse financial services market. To the extent leasing increases the credit options of companies to invest in capital equipment it also results in more purchases of equipment. Leasing has become well established as an aid to sales for manufacturers of certain types of equipment such as technology, agricultural machinery, vehicles and industrial equipment. It is a well established strategy for companies like Dell, John Deere, IVECO and many others to offer leases to potential customers to both increase the likelihood of a sale and to access the benefits of running a profitable leasing operation.

Leasing in a development context: The aspects of leasing described above have particular relevance in the development context. The growth of MFIs is evidence for the demand for credit in emerging markets. While this demand has been met initially through loans, leasing offers both the lessor and the potential lessee additional product choice, increasing the credit available. At a macro level, while governments continue to work to attract inward investment from trans-national corporations, the domestic small and micro enterprise sector continues to be a source of employment and wealth creation. Increased productivity through the use of better technology benefits the small and medium enterprise (SME) sector and the wider economy. Leasing is a credit product for businesses

to acquire just such technology under more favourable conditions than a personal loan because the impact on productivity and cash flow is taken into account in underwriting. Finally, leasing also benefits developing markets by reducing the risk to manufacturers of equipment, and increasing their presence in the market. When deciding whether or not to enter a new market, manufacturers must decide whether or not to offer credit to customers. If they do not offer credit, they will sell less, potentially making the commercial opportunity less attractive. However, if a financial institution offers leasing for their equipment, the manufacturer can access credit customers indirectly. Equipment sold to the lessor for use by lessees will be at least partially incremental to cash sales direct to end users.

2.3 The Overlap of Leasing & Microfinance in Emerging Markets

As mentioned above, microfinance has already achieved substantial scale with 3000 MFIs active principally in emerging economies. As a sector it continues to attract investment and expand, and its principal challenges are the funding of this growth and the demand for diversification into savings and other products that accompanies this (The Microfinance Information Exchange, 2010).

Leasing on the other hand remains overwhelmingly a product of developed markets with the emerging markets of S America and Africa representing only 9% and 2% of a global market of $644B. (Table 2.1; White Clarke Group, 2010). Asia without Japan also accounts for 9% (ibid). The same report identifies 4 factors that are necessary for leasing to grow in an economy, namely a healthy global economy, growth in the domestic economy, a supportive institutional environment and favourable tax rules, including sales tax, suggesting that one or more of these has been missing in emerging markets.

A key aspect of emerging market leasing is the dominance of 'big ticket' such as real estate and infrastructure, rather than small equipment or vehicles. However, there is no inherent feature of leasing per se that makes it unsuitable for small equipment in emerging economies. Just as traditional banking was adapted to become microfinance, leasing can also be structured in smaller

amounts, and targeted specifically at equipment relevant to small and micro enterprises, both rural and urban – provided there are no specific disadvantages caused by the regulatory or tax system (Bank of Uganda, 2008).

The World Leasing Report's top 50 Economies for Leasing in 2008, and the Microfinance Information Exchange data base of 1400 established MFIs that publish data (Microfinance Information Exchange, 2010) reveal:

- 17 of the top leasing economies are also emerging economies (7 in South and Central America, 5 in Europe, 4 in Africa, plus China) *and* have MFIs that report data
- Russia, Columbia, Serbia and Peru have MFIs that report assets in excess of $1B
- All 17 emerging leasing markets except China, Nigeria, Argentina, Ukraine, Egypt and Venezuela have assets in excess of $500M.

Table 2.1 Leasing & Microfinance in Emerging Markets

Country	World Leasing Ranking	Annual Vol ($B)	Growth% '07-'08	No of MFIs (Reporting)	Total Assets $M
Brazil	4	45	46	41	678
Russia	7	25	-18	101	2,700
China	8	22	87	19	33
Romania	22	6.3	23	7	519
Columbia	25	5.7	31	31	4,200
S. Africa	27	4.8	-10	14	515
Mexico	30	3.6	-37	50	2,900
Bulgaria	31	2.8	59	24	799
Nigeria	33	2.5	38	18	104
Chile	35	2.4	-7	9	911
Serbia	38	2.0	-5	4	1,200
Morocco	40	1.7	17	10	865
Peru	43	1.4	60	65	4,800
Argentina	44	1.4	40	15	29
Ukraine	45	1.3	-40	3	438
Egypt	47	0.7	26	16	271

Country	World Leasing Ranking	Annual Vol ($B)	Growth% '07-'08	No of MFIs (Reporting)	Total Assets $M
Venezuela	49	0.6	12	2	174

(White Clarke Group, World Leasing Report 2010)

It is the view of this author, based on a review of the literature that follows, that the presence of successful MFIs has not yet been considered as a factor that might influence the growth of leasing and that leasing as a mechanism of growth for MFIs has also not been properly examined. As MFIs seek to add additional products to support growth, enhance the range of financial services available to their clients and diversify portfolio and business risk, leasing is an obvious strategy. It is a medium term, collateralised lending product that is particularly suited to capital constrained small and micro-enterprises, as illustrated by its track record in established, richer economies. From the leasing perspective, clients that have already engaged with financial services and have a credit history, and who are ready to access productivity enhancing equipment through lease can potentially now be accessed through the networks of MFIs.

2.4 Leasing and Development

I have been able to assemble 17 reports and papers that refer to leasing to small businesses in a development context. As shown in table 2.4 these works fall into a number of similar categories.

Reviews of the status of leasing in development are generally written by active promoters of the product such as the World Bank, the International Finance Corporation (IFC) both alone and in partnership with others. They offer detailed explanations of what leasing is, what institutional context is required for it to work, plus snapshots of what a particular program to support the set up of a leasing company or capability has achieved. Reviewers take the position that the conditions for leasing in a microfinance and development context exist. Their organisations have encouraged or even created these conditions and have invested in specific leasing initiatives. They do not examine whether or how these initiatives have gone on to become active and growing institutions in their own right.

These reviews contain and overlap with pieces of **Advocacy** where the suitability of leasing equipment for micro enterprises is described. There are also a number of extremely detailed and potentially useful '**How To Do Development Leasing'** manuals which contain explanations of the specific accounting, tax and organisational approaches necessary to set up a leasing entity.

6 of the 17 works are actual or variations of **Case Studies** which focus on aspects of the operations of specific leasing companies or entities. In only one of these case studies is the growth of the company considered, and none examine the growth of leasing in comparison to the growth of microfinance products in the same country or assess whether the investment by agencies is effective.

2.4.1 Reviews of Leasing in a Development Context

Both IFC and the World Bank are active and recurring promoters of leasing, with the IFC also committing debt, equity and technical assistance to leasing projects. In the most recent World Bank publication 'Managing Risk and Creating Value with Microfinance' a chapter is dedicated to micro-leasing, or the leasing of amounts comparable in size to microfinance loans. I will review the contents of this chapter in detail because i) it is the most up to date and ii) it covers much of the descriptive information restated in other publications subsequently cited. When reviewing these earlier publications I will only then mention additional pertinent findings of observations. In 'Managing Risk and Creating Value with Microfinance' (2010) Goldberg & Palladini describe leasing as particularly well suited to enable micro-entrepreneurs to make the shift to increased productivity and profitability that is key for their small business to make a contribution to overall economic growth. They point out leasing's suitability to create longer term relationships for MFIs with their clients, as it is a medium term product.

Table 2.4 Leasing Literature Summary	Leasing Explained	Conditions for Leasing	Perf.	Lease Company Mentioned?	Country	Type of Study
(Goldberg & Palladini, Managing Risk and Creating Value with Microfinance, 2010)	✓	✓	×	ANED FINARCA American	Bolivia Nicaragua Peru	Review/Advocacy
(Goldberg, Microleasing: Overcoming Equipment Financing Barriers, 2008)	✓	✓	×	FINARCA	Nicaragua	Review
(Fletcher, Freeman, Sultanov, & Umarov, 2005)	✓	✓	×	IFC/NGO Partner Uzbek Leasing	Rwanda Uzbekistan	Review/Toolkit
(Nair, Kloepinger-Todd, & Mulder, Leasing: An Underutilised Tool in Rural Finance, 2004)	✓	✓	×	John Deere DFCU AgroMash Orix	Mexico Uganda Kazakhstan Pakistan	Review
(Mutesasira & Osinde, 2001)	✓	✓	×	Multiple Multiple	Tanzania Uganda	Review
(Gallardo, 1997)	✓	✓	×	Orient Leasing Grameen Bank	Pakistan Bangladesh	Review
(Bass & Henderson, 2000)	✓	✓	×	Kenya Photovoltaic CECAM Grameen	Kenya Madagascar Bangladesh	Advocacy
(Akarakiri, 1998)	✓	✓	×	None	Nigeria	Review/Advocacy
(Deelen, Dupleich, Othieno, & Wakelin, 2003)	✓	✓	×	None	n/a	How To Guide
(Westley, 2003)	✓	✓	×		Latin America	How to Guide
(Pasco & Pinedo, 2008)	×	×	×	Banco de Commercio	Peru	Profile
(Hakobyan, 2006)	×	✓	×	ACBA	Armenia	Case Study
(Nair & Kloeppinger-Todd, Buffalo, Bakeries and Tractors: Cases in Rural Leasing from Pakistan, Uganda and Mexico, 2006)	✓	×	✓	John Deere DFCU Network	Mexico Uganda Pakistan	Case Study
(Fraslin, 2003)	×	×	×	CECAM	Madagascar	Case Study
(Campero, 2001)	✓	×	×	INDES	Chile	Case Study
(Bayes, 2001)	×	×	×	Grameen	Bangladesh	Case Study
(Dowla, 1994)	✓	×	×	Grameen	Bangladesh	Case Study

As with other authors they list the particular advantages of leasing in its ability to 'create' collateral through the continued ownership of the asset by the lessor; and the flexibility for payments to match commercial or agricultural cycles. Other characteristics noted include that fixed payment amounts are inflation friendly; the documentation is easier than loans; the client can choose the equipment for lease; and where the product is not regulated, there are no interest rate ceilings. There is a strong legal position for repossession, and it is easier to gain access due to clarity of who owns the asset established at the start. If MFIs lease standardised equipment, it can be sold more easily on repossession.

The specific risks of leasing are also described. Tax can be a burden and an additional cost if lease interest payments are not exempt from VAT. The ownership of the asset by the leasing company does raise the risks of damage during usage, liability, as well as costs in the event of repossession, though these can be offset by deposit and/or liability insurance.

While this review continues the advocacy of the World Bank for leasing, it notes but does not comment on the fact that despite the advantages of leasing described, the scale and numbers of organisations using the product remain small. The IFC and World Bank have been promoting leasing for SMEs for almost 2 decades, but there is still nothing comparable to Grameen Bank, or Compartamos, a Mexican MFI whose initial public offering in 2007 raised $450M.

Goldberg (2008) published a similar though less detailed World Bank report in 2008. In it he also points out that despite IFC support, leasing remains small in scale. In examining some of the reasons he looks at loss rates, though at 1-2% of lease costs, these are similar to MFI loan levels (at the time). He provides more details of countries where complications of taxes may be significant e.g. stamp tax in Mexico and asset tax in Romania. Regulation in certain markets may require that leasing takes place in a different legal subsidiary to where loans are held, but in the case of Bolivia, ANED still went ahead and was established. On the positive side he points out that the stronger legal claim of leasing on the asset in the event of default is known to work in Chile, El Salvador, Mexico, Honduras – all

markets where MFIs are active. He advocates strongly that leasing is a good add on product that fits with proven loan clients and that it diversifies loan portfolio. In a possible validation of this Finarca, a leasing company set up in Nicaragua, was subsequently acquired by Scotia Bank of Canada, which would imply that they perceived a commercial advantage. Beyond a comparison of loss levels however, the review does not discuss the possibility that with conditions that are on balance positive enough for companies in diverse markets to be established, there still appear to be some barriers to consistent growth and expansion similar to MFIs.

In 2005 and subsequently reprinted, the IFC prepared a leasing toolkit entitled 'Leasing in Development: Guidelines for Emerging Economies to Support SMEs as Key to Economic Growth'. The review contained a detailed guide to IFC role, as well as describing the advantages, the legal, accounting and tax context required. They mention without detail the IFC's role in 222 leasing projects, working with 130 clients in 58 countries, investing $1.4B. As a current snapshot IFC investment clients in 18 countries currently have 193000 leases for a total value $5.2B, and averages for micro leasing of $3000, small leases $20000, and medium of $207000. Focussing in on what they describe as Micro SMEs the client portfolio grew 19% in number and 47% in volume and make specific reference to a program in Rwanda in partnership with an NGO to lease $140 bikes to approximately 1400 farmers (Fletcher, Freeman, Sultanov, & Umarov, 2005).

In this 2005 review attention is focussed more on starting conditions and leasing entities initiated. It is not examined whether the programs have achieved the goals and particularly the growth levels intended. It is also notable that the IFC definition of micro lease (average $3000) would be considered at the upper end of microfinance loans, which can be less than $100.

There has been particular interest in leasing as a product to assist in the mechanisation and increasing productivity of agriculture. In 2004 the World Bank published a discussion paper entitled 'Leasing: An Underutilised Tool in Rural Finance'. While explaining leasing and its context ,of particular interest is its reference to only 10 lessors of agricultural equipment in Africa, South Asia,

Central Asia and Latin America including 3 microfinance organisations, one private company specialising in micro-leasing and one equipment manufacturer. A case study on 3 of these companies was subsequently published in 2006 (see below) and in this paper it mentions that the total lease portfolio of 3 of the companies being John Deere Mexico $25M, DCF Uganda $4M, and AgroMash Kazakhstan $1M, respectively. The small scale of two of the portfolios is noteworthy and below the minimum size necessary for sustainability in the opinion of the author. The review does add to the list of potential issues with leasing through the lack of information about leasing amongst potential clients and the operational complexity caused by its unique features. They recommend a regional approach and the utilisation of the expertise spread in the different development agencies of Europe and the US. (Nair, Kloepinger-Todd, & Mulder, 2004).

In a short report published by MicroSave in 2001 Tanzania and Uganda were identified as countries with potential for leasing. The authors set out the strategic case for creating a microleasing sector and found large unmet demand from micro-entrepreneurs requiring less than $1500, but whose needs were not being met by existing providers. The case was made that the conditions of existing leasing providers such as asking high deposits and high pricing were due to an unfavourable tax and regulatory regime. They also mention the difficulty of leasing companies finding funding that matches the terms of their leases (Mutesasira & Osinde, 2001). Tanzania subsequently passed law in 2008 and leasing in general reached $100M per year (Fletcher, Freeman, Sultanov, & Umarov, 2005). In the case studies cited below, only Uganda features. The implication is that yet again, the potential for leasing and the realisation of that potential are not matched.

Thirteen years ago the World Bank saw leasing as a way to overcome interest rate ceilings which were making loans of the emerging MFIs loss making. For the micro-entrepreneur their initial view of the advantages were in the efficient use of limited capital, and through its inherent collateral. However they believed leasing was only suitable for middle and upper strata micro and small businesses as lower strata were using loans for working capital (Gallardo, 1997). This review was a

prelude to further work. It is notable that the ambition for leasing was less and that subsequent increased enthusiasm, while driving an improvement in the leasing environment, and creating many start ups (see above) did not encourage substantial take up by the MFIs.

2.4.2 Advocacy of Leasing in Development Finance

In 2000 a promotional paper about leasing was produced as part of a 2000 conference on 'Innovations in Microfinance'. It provides a generally good overview of what leases are, and distinguishes between the 2 basic forms of leasing – finance leases and operating leases, though it does not make clear the significant expertise required to offer operation leasing (Bass & Henderson, 2000). With its target audience of microfinance institutions in mind it provides a good characterisation of what makes a good leasing client i.e. someone on a 3rd loan cycle, who knows and can use and care for the equipment. Examples are provided of leasing programs that were established, though no perspective is offered on whether they were successful over the long term: CECAM in Madagascar is a rural lender. It uses group lending, 30% down payment, 4-36 month term, annual interest up to 30%; Grameen Bank leasing in Bangladesh claims to lease anything to 2nd time borrowers from an existing program. It is flexible, including early payment and calculates price using cost of item plus 25% leasing fee. By 1997 leasing consisted of 4% of portfolio, to a value of $5.9M with average size of $623 with 98% repayment (ibid)

What is interesting about this is the additional information about actual programs. The Grameen lease size is truly microleasing, though the percentage of the product in 1997 was insignificant. In the 2007 accounts there is no mention of leasing in the top 25 products of the bank.

In a short paper entitled 'Equipment leasing: a strategy for technology acquisition in Nigeria' Akarakiri recommends leasing in general for Nigerian industry. His approach after describing leasing and its features is to demonstrate with calculations how it can be cost effective. It is notable that in the year of his writing, leasing amounted to only $30M (Akarakiri, 1998). By 2010 leasing in Nigeria

reached $2.9B, driven by the requirements for large amounts of commercial equipment by the oil sector (ProShare Nigeria, 2010). This dramatic growth would seem to prove the attractiveness of leasing in a developing country, but says little about leasing in the micro-entrepreneurial space.

2.4.3 Leasing Toolkits

In 2002 the ILO produced a guide to microleasing with detailed instructions with examples on how to set up and transact leasing. It identifies the internal conditions including right staff and systems, and the appropriate external conditions including sufficient market opportunity. Its focus on the suppliers of equipment suppliers and the need for effective maintenance and after sales service is a unique point. It does not discuss the issues surrounding funding, collection of delinquent accounts and disposal of equipment at the end of lease (Deelen, Dupleich, Othieno, & Wakelin, 2003). The issue of reliable sources of reliable equipment is likely to be extremely relevant in developing markets where the possibility of gaps in the supply chain are higher.

In the same year the Inter American Development Bank produced 'Equipment Leasing and Lending: A Guide for Microfinance'. It is clearly targeted at the sector describing how to do equipment financing from $50-2500, focussing in on what is different about lending to micro-enterprises. The report details that equipment loans and leases comprise 21% of books of 25 MFIs in Latin America with only 3 offering leases namely ANED (Bolivia), INDES (Chile) and Finamerica (Columbia). It advocates that operating leases are too risky for MFIs requiring too much expertise. Best practice recommendations are made to match fund in local currency; lend to new clients by underwriting character, cash flow, business stability and taking additional collateral; take monthly payments vs. weekly to save costs. In a similar vein to the International Labour Organization (ILO) report it also emphasises the importance of suppliers, and makes the additional point that scale can lead to dealer discount programs. (Westley, 2003)

This is a comprehensive guide all the operational aspects of getting a leasing company off the ground. Its observation that leasing occurs in only 3 of the 25 MFIs described yet again questions why MFIs are not acting on both the advice and the technical assistance of the World Bank, IFC, ILO and the IADB in greater numbers.

2.4.4 Profiles and Case Studies of Leasing Organisations in Emerging Markets

The following case studies and one profile provide additional detail about the actual experiences of leasing companies in the development context. Of all the examples only one examines the performance of the leasing company in the context of microfinance or against expectations of the investors and stakeholders.

Returning to the World Bank 2010 review of leasing, references were made to specific cases – namely Finarca of Nicaragua and American Leasing Peru. Of Finarca it was reported that prior to its acquisition by Canada's Scotia bank Finarca had a program to lease tools, machinery, and other productive assets to at least 300 micro and small enterprises, in the range $3,-8,000, with maturities from 12 to 48 months and commercial rates of interest. As of June, 2008, Finarca had a portfolio of $18.8M in leases, representing 85% of its total assets.

American Leasing Peru in 2006 had a 6.5% share of leasing market by portfolio amount, 14.1% by no of leases, 65% transport. Its focus was industrial and commercial equipment with 91% of business with companies of turnovers less than $21M. The average lease was $67,000, compared with $150,000 in the overall Peruvian market. It had a $128M portfolio with 1877 contracts. In 2007 IFC invested a $10M loan and technical assistance to strengthen its SME presence. (Goldberg & Palladini, 2010)

These cases both indicate an overlap and possible hand- off between development and commercial with agencies such as the IFO and World Bank creating the conditions, and commercial companies taking over when conditions are right. In the case of American Leasing Peru, the existing leasing activities were clearly not targeted at SMEs with average values of $67,000 but the IFC clearly

believed that the organisation had the potential to expand its operations into the SME space. It is interesting that they chose a commercial company for this diversification rather than a Peruvian MFI.

In a 2008 profile of the Peruvian Bank Banco de Commercio, the managing director describes their strategic decision to target small and micro enterprises with loans and leasing. While data as to the product mix of the portfolio for 2008 are presented, leasing does not figure despite the fact that the bank is already engaged with 900 small entrepreneurs providing training (Pasco & Pinedo, 2008).

The usefulness of this short profile is that it demonstrates a commercial interest in both the sector and the product on the part of a profitable bank. This raises the possibility that when the conditions become right, the commercial sector acts to set up its own leasing capabilities.

In 2006 US Aid published a review of the issues it faced in setting up ACBA Leasing in Armenia, to offer medium term financing for farmers and SMEs which was not available from local banks. The company was set up in partnership with the ACBA Bank, Credit Agricole and the Lebanese Leasing Company. By 2006 the company had 218 leases for 674 pieces of equipment for a value of $5.6M. It is not described whether this was in line with expectations or not (Hakobyan, 2006).

While acknowledging the usefulness of the technical assistance available to set up such a company, the report describes the particular issues that arose in this case. These were i) a lack of an asset register to track ownership, which they had to create; ii) the need to create a special position to handle the complexities of interacting with 28 foreign and 33 Armenian distributors; iii) a pervasive lack of understanding of leasing by staff, clients and government which they addressed with training, workshops, commissions, internally publically and for suppliers, as well as working one on one with government; and iv) other VAT legal and regulatory hurdles (ibid).

While this is an extremely useful insight for the next team looking to set up a leasing company from scratch it leaves open the issues of whether so much effort to build a portfolio of $6M was

considered worth it by the stakeholders and whether the organisation had become self sustaining in terms of ability to grow, manage losses and attract funding from a commercial source.

In the same year the follow up case study to the 2004 World Bank review of Leasing: an Under-utilised Tool in Agricultural Finance was published. This looked in detail at the operations and growth of three entities - Network Leasing Corporation Limited (NLCL) in Pakistan; Development Finance Company Uganda (DFCU) and Arrendadora John Deere (AJD) in Mexico

Network Leasing Corporation Limited (NLCL) in Pakistan lease portfolio in 2004 was $11.6M, 21% of which is estimated to be in rural areas. The company reported steady growth from 2000 to 2003 but had a decrease in both in 2004. It is a quoted company, reporting consistent profits, and employing 86 people. Losses have been maintained with 2% and levels of late payment are ~4%. Funding is obtained from commercial banks.

Development Finance Company Uganda (DFCU) is part of a large commercial bank, though the majority of shareholders are development agencies, who also are the principal funders. The leasing company is estimated to have a market share of 65%. The portfolio in 2004 was $25.7M, with 20% in rural areas, and growth reported over the last 5 years. The DFCU group reported a profit. No leases have been written off in 4 years and no delinquency data was reported.

Arrendadora John Deere (AJD) is the Mexican finance subsidiary of the American agricultural equipment manufacturer. In 2004 its portfolio was $74M, 85% In 'Managing Risk and Creating Value with Microfinance' (2010) Goldberg & Palladini describe leasing as particularly well suited to enable micro-entrepreneurs to make the shift to increased productivity and profitability that is key for their small business to make a contribution to overall economic growth. They point out leasing's suitability to create longer term relationships for MFIs with their clients, as it is a medium term product of which was farm equipment leases. Little or no losses are reported and tractor leases as a

proportion of tractors sold by John Deere in Mexico have increased from around 20 to 35 % over the past five years.

In the authors review and comparison of the 3 cases they note that 2 of the 3 take additional collateral; all require security deposit and all three cases required government help to jump start. They write that all 3 are now profitable but need to achieve economies of scale. (Nair & Kloeppinger-Todd, 2006)

With only NLCL operating as an independent company, with commercial funding, it is questionable whether any conclusion can be drawn as to the profitability of AJD and DFCU. Not writing off any losses in the case of DFCU puts any conclusion as to its performance in doubt. AJD exists to assist the sale of tractors of the parent company, and the potential for cross subsidy and transfer pricing again makes any conclusion as to profitability problematic. What is notable is the clear commercial interest in all three markets to commit to leasing as a financial product. While scale is still small, commercial investors will be aware of the medium term nature of lease company investing, so their continued participation could suggest that in these markets, leasing is in transition from the subsidised to the independent.

Many of the review above refer to a case study of CECAM, a Malagasy cooperative rural finance institution. CECAM does not in fact offer leasing, but does offer hire purchase (HP) which is another form of collateralised lending. The way they offer HP mirrors many of the approaches already referred to and as of 2002 HP had reached a level of 20% of a $25M portfolio (Fraslin, 2003).

In the study there is no discussion of performance beyond the fact that the HP product is growing. The author also does not discuss collectability and enforceability in the event of default, and what the level of losses are and how this is provided for. The study does indicate a good demand in yet another developing market for a collateralised lending product, and demonstrates that it can be handled effectively by a microfinance organisation.

INDES was a microfinance organisation set up in Chile by NGOs in partnership with the national development bank. This 2001 study was a strategic review incorporating review of advantages of leasing in Chile from micro-entrepreneur and INDES point of view. Between 1992 and 2000, INDES carried out approximately 980 leasing operations, for a total of $9.4M, with an average of $9,500. During the same period, they granted 3,710 loans, at an average $2,500 and a total value of $9.2M. As of October 2000, the lease portfolio was ~$2.9M with 309 clients, and the loan portfolio was $1.4M with 352 clients. However, the organisation was facing a new board and the end of funding from the development bank and this report was structured to help the incoming leadership to decide how to proceed (Campero, 2001)

Without loss performance statistics and profit information it would be difficult for the new management to assess whether this whole operation was worth continuing. The shift from development to commercial funding is difficult and requires evidence of profitability and sustainability, which in the case of leasing means scale. The lease amounts referred to are not micro leasing, though the loans are in the range of microfinance. This is another example of a multi product MFI, though lack of performance information limits its usefulness. Commercially Chile is now an active leasing market and I have been unable to find trace of INDES as an active entity. This may be another instance of the commercial market taking over from development sponsored organisations.

Grameen Bank - 2008, 2001 and 1994

The most detailed review of leasing within this most famous of MFIs was written 2 years after leasing was launched in 1992 – a period that is long enough to see demand and operation issues, but not long enough to assess performance, and in particular losses. The 1994 paper concentrates on outreach using the number and type of customers as its yardstick. By the end of year 1997, Grameen Bank had written 8,411 leases of 111 different types of asset to 96 male and 1118 female members. The portfolio was Tk. 237.67M ($5.29M) or 4% of the total bank portfolio, and the

average was Tk 28,000 ($623) per lease. The author highlights the high level of integration of leasing into the MFI via use of the existing network and infrastructure, and by allowing local managers to adapt aspects of the lease product (Dowla, 1994).

While the lease program was suspended 1998-2001, it was restarted and in particular used for the leasing of mobile village pay phones (VPPs). A 2001 study again focussing on outreach concluded that this was successful in that it benefited the poor more than non poor, made the telephone a productive asset, empowered the women involved, and enhanced communication. Nothing was presented on payment history or economic success of phones (Bayes, 2001)

Both these papers demonstrate again that leasing is useful and practical in an MFI context but leave the question of why if leasing was started as early as 1992 is it not a greater part of Grameen's portfolio today. Looking at the 2008 annual report, leasing is referred to but does not feature on the list of its top 25 products, nor are any separate statistics presented (Grameen Bank, 2008).

2.5 Conclusion and Justification for Research Direction

The literature demonstrates sustained history of support to establish leasing in developing markets to benefit both the economy generally and as an additional source of credit for SMEs and rural producers. This is manifested in a series of policy publications *and* in investments to create or enhance actual leasing capability in a series of emerging markets.

In reviewing what has been achieved against objectives, however, very little has been published. The small numbers of leasing organisations and their small scale suggest a poorer return for development funds and efforts than what has been achieved in microfinance where over 1400 publish results and the number continues to grow.

Work done to date allows a list of possible explanations for this contrast and include:

1. The requirement for a leasing friendly regulatory environment allowing leasing companies to compete on an equal basis with loan companies;

2. The requirement for specific leasing institutions such as an asset register and a legal system that allows repossession;
3. Equipment specific requirements such as a dealership or manufacturing network to ensure the equipment can be maintained for the duration of a lease;
4. Lack of knowledge of both the potential customers and within the delivering organisation.

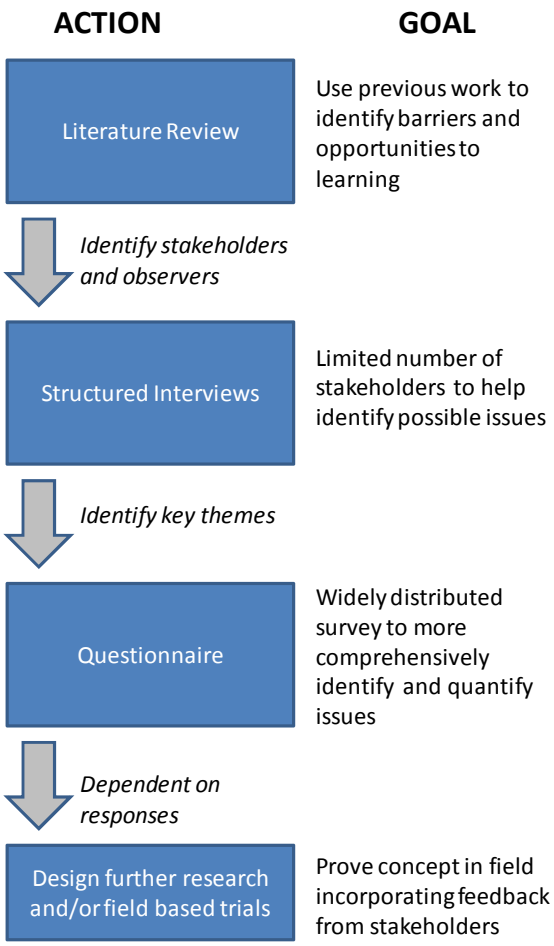
It would therefore seem useful to survey stakeholders of both leasing and microfinance to understand better why leasing has underperformed compared with microfinance. Going further, as the growth of microfinance institutions have potentially improved the conditions for leasing, a survey and questionnaire can examine whether this is the case. By understanding the barriers to leasing within potentially more favourable conditions than have existed previously, proposals can be developed to realise this enhanced potential. This is what the remainder of this dissertation attempts to achieve.

Chapter 3 –Research & Methods

3.1 Overview

As the literature review demonstrated little previous research has been done on why or whether leasing and microfinance are complimentary. To address this a stepwise approach was selected to set a scope and to proceed to steps of increasing complexity if justified by results. The dissertation goal was to make as much progress according to this plan as was feasible given constraints of time and funding, but ensuring that output would act as a firm basis for continued research. The outline structure is therefore as follows:-

Figure 1: Outline of Research Approach



In researching this topic the principal challenge lay in the fact that while microfinance is highly topical and the subject of much published research and comment, leasing is not. In this context the approach was first to narrow the scope. I started with a survey of a limited number of informed observers, practitioners and funders to develop manageable list of hypotheses as to what might be the factors relevant to leasing future as an effective micro-financing product. Then this shortened list was used to develop a detailed questionnaire for much wider distribution. The questionnaire was both to test that the initial hypotheses captured the issues, and to see which hypotheses attracted more or less agreement.

While available time and funds limited the questionnaire distribution and follow up possible, the responses received were used as a basis for discussion and for outlining subsequent, more focussed and applied research and as a guide to likely issues in setting up trials in the field.

3.2 Setting the Scope

My initial preference was to work within an existing MFI that was currently offering leasing or which was looking at leasing as a possible product. The literature review quickly established that there were very few MFIs in this state suggesting that it was neither practical or appropriate to look at field based issues when there appeared to be substantial strategic issues preventing leasing from getting off the ground in MFIs in the first place.

Once the focus of the research became strategic, the appropriate level from which to engage with these issues shifted from the field to senior management (i.e. practitioners), funders and observers of MFIs and leasing in a development context. 'Funders' are providers of capital and wholesale funds and includes Development Banks, Specialist Investment Funds and Non Governmental Organisations. 'Observers' in the context of this research is a collective term for academics, consultants and others who study, consult or comment on either sector. The research goal then became to collect and rank the opinions of these stakeholders as to what the barriers to leasing as a product for MFIs were.

Depending on the response level, the work could extend to looking at the design of future research work or projects to overcome these barriers.

Geographical scope was limited by interviews and questionnaires being prepared only in English and Spanish. The effect of this was mitigated in two ways. First a working knowledge of English is widespread in the professional and academic communitiess targeted by this study. Secondly, the responsibilities and experience of many of the respondents covered more than one jurisdiction (for instance the EBRD funding European and Central Asian MFIs) which should mean that issues from non English speaking regions could be potentially be captured.

3.3 Survey Design and Delivery

With a focus at the strategic rather than the field level, the profile of individuals who could help answer the research question changed. Not only should such a person have an informed opinion about the strategic options facing MFIs and development leasing companies, but it was likely that such a person would be difficult to access and have little time available.

To overcome this I used my professional network and some 'cold calling' to speak with 9 individuals between April and July 2010 who fitted the profile and who could help me describe the range of potential issues. Each person was called or interviewed in person for between 15-60 minutes. The format was extremely open in order to elicit new data. However, as specific topics emerged and were repeated, these were used towards the end of the interview to see if they stimulated further discussion.

The individuals interviewed came from a range of organisations and background described in the following list:

Table 3.3: Respondent Type for Structured Interviews

No of interviewees	Type of Organisation
4	Development Funder(World Bank, IFC, DFID, EBRD)

No of interviewees	Type of Organisation
2	Observers (consultants)
1	Former Practitioner
1	Observer (academic)
1	Observer (NGO)

The barriers identified by this initial group could be arranged into 3 major headings – Funding; Organisational and Demand Based. For full details see the next section. These categories in turn formed the basis for the design of the questionnaire described next.

3.4 Questionnaire Design and Implementation

Using the interview findings of the initial group a questionnaire was designed and targeted at a wider range of respondents to further test and potentially quantify the initial opinions while allowing for additional input. The process involved i) defining the aim ii) identifying the target respondents iii) deciding on the delivery mechanism iv) questions design v) pilot vi) delivery and vii) analysis (University of Leeds, 2010) with the additional step of obtaining ethical clearance from the University of Reading.

As described at the end of the literature review, the aim was to survey stakeholders of both leasing and microfinance to understand better why leasing has underperformed compared with microfinance.

The target respondents were those who, as mentioned above, would have an informed opinion about the strategic options facing MFIs and development leasing companies. Potential respondents were grouped under the headings

- Development Agency – being national and multinational organisations that deliver aid funding and advice to MFIs. *Examples: World Bank, IFC, EBRD*
- Funder – being any other non-governmental or commercial organisation that provides funding to MFIs *Examples Accion, Rabobank, Citigroup*
- Microfinance Practitioner being an organisation that delivers microfinance to end users *Examples PlaNet, Compartamos Banco, Avanaj*
- Observer such as an academic, consultant or professional adviser to the sector
- Other Financial Services such as a rating agencies, independent leasing company or captive leasing company *Examples John Deere, Scotia Bank*

Names and contact details were obtained from public sources, and from countries that appeared in the World Leasing Survey 2010 i.e. where leasing was already taking place. A deliberate emphasis was placed on practitioners in order to gather the opinions of those actually delivering micro-financial services. These practitioners were in turn selected from MFIs already publicising information about their activities on the Microfinance Information Exchange website www.themix.org. Table 3.4 shows the numbers by category of recipients who received a questionnaire:

Table 3.4: Target Respondents for Quesitonnaire Survey

Type of organisation	Number surveyed
Development Agency	9
Funder	8
Observer	20
Practitioner	110
Other Financial Service	3
Total	150

The survey questionnaire was delivered to respondents by email using a cover letter and a link to an online questionnaire service provider, www.surveymonkey.com. This provider was selected to host the questionnaire based on i) range of tools available to make questionnaire attractive and easy to use; ii) ability to present to respondents via links; and iii) data tracking and analysis tools.

Questions were designed and presented in sections to cover all of the areas identified in the initial survey as relevant. Multiple question types were used such as rankings, open questions, and multiple choices. A general section was included with 24 statements about the topic to be marked with the degree of agreement or disagreement to cross check opinions expressed in the specialised sections.

Before distribution ethical clearance was obtained from the University of Reading. Emails were sent in the last week of July 2010 and reminders on 2 & 3 August.

As only 18/150 responses were received (12%) analysis was limited to graphical presentations, ranking and discussion of results.

Chapter 4 –Results

4.1 Overview

Results were obtained from both research stages subsequent to the literature review. The initial set of structured interviews provided a list of 3 key areas where barriers might exist to the growth of leasing through MFIs. These were limitations imposed by funders, organisational barriers within MFIs themselves and potential problems of demand and distribution. A questionnaire was constructed to examine these themes further and distributed to a wider audience of 150 industry practitioners, observers and funders. It received 18 replies by the end of the research period. Replies indicated support for leasing as a product for the MFI market. Of the possible obstacles identified in the structured interviews the requirements for specialised skills and distribution received most support while those of funding and customer demand were discounted.

4.2 Structured Interviews

The opinions collected in the 9 initial interviews are summarised in table 4.2 below:

Table 4.2 - Structure Interview Responses

#	Suggested Barriers to Leasing in MFIs	Category
1	Less funder support for medium term product vs shorter term, more widely distributed loans	Strategic
2	Ignorance among prospective customers may lessen demand Difficulty for MFIs to deliver Regulatory and institutional environment may not be conducive to leasing	Demand/Distribution Organisational Institutional
3	Regulatory and institutional environment may not be conducive to leasing Management may not be incentivised within MFI to develop new products	Institutional Organisational
4	Needs strong association with a particular equipment	Demand/Distribution
5	May be complex for prospective customers More widespread in financial markets with Anglo-Saxon links	Demand/Distribution Institutional
6	Requires MFIs that are aiming to evolve into full financial service organisations Needs strong association with manufacturer – else competing with collateralised loan products	Organisational Demand/Distribution

#	Suggested Barriers to Leasing in MFIs	Category
7	Regulatory and institutional environment may not be conducive to leasing Foreign exchange risk higher on longer term funding required for leasing Leasing is a banking product – MFIs not up to the task Leasing requires more sophisticated underwriting	Institutional Strategic Organisational Organisational
8	Medium term nature may hinder outreach Needs large scale to be profitable	Strategic Organisational
9	May hinder outreach and welfare mission of MFIs Organisations may not be strong enough to handle another, different product to loans	Strategic Organisational

I grouped these initial interview responses into 4 to provide structure for a more detailed questionnaire survey. These areas were as follows:-

1. Strategic – *Funders and MFI senior management may prefer short term finance products over medium term finance products*

   If the priority of the MFI as defined by its management and supported by funders is to reach as many poor and unbanked customers as possible, strategy will favour smaller, shorter term products over medium term products. For example, one thousand loans of $100 reach more people than 100 leases of $1000, notwithstanding any additional effects of stimulating micro-enterprises, employment or industrial capacity.

2. Organisational – *Leasing may be too complex a product to be offered by MFIs in their current configuration*

   Organisational issues cover a range from the current structure of MFIs including IT systems, staff incentives, training, underwriting and equipment expertise

3. Demand and distribution – *Leasing is probably unfamiliar to customers and therefore may require active promotion through a network ofMFI branches, an equipment distributor network, or both*

Customers may not understand the difference between a lease and a loan, and therefore leasing may only sell if actively promoted by a dedicated or trained sale team or via the sales team of an intermediary such as the staff of an equipment dealership.

4. Institutional – *Leasing will only be present in jurisdictions with a favourable regulatory environment*

   Leasing requires particular legislation to codify the separation of use and ownership; to define who receives any tax benefits of ownership in a leasing scenario and to ensure that lease payments and loan repayments are treated equally by the tax system. If these are not in place and enforced, leasing is not viable. *Note: this constraint was not tested in the subsequent research by surveying MFIs only in markets where leasing was already known to be taking place as indicated by its presence in the 2008 top 50 leasing markets survey* (White Clarke Group, 2010).

The questions and summarised responses of the questionnaire survey, structured around the 3 selected areas are presented below.

4.3 Questionnaire Survey

A full copy of the questionnaire is available in Appendix 1.

150 individuals were contacted of whom 18 responded giving a response rate of 12%. By comparison a 2009 survey on the global business environment for microfinance performed by the Economist Intelligence Unit contacted 415 experts of whom 176 individuals responded – a response rate of 42% (The Economist Intelligence Unit, 2009). Clearly the scope of this work is smaller and the output less significant in comparison and analysis and conclusions are therefore more limited. The responses received span the range of alternatives presented, but attention and discussion is focussed on strong indicators where 50% or more of the respondents express the same opinion or ranking.

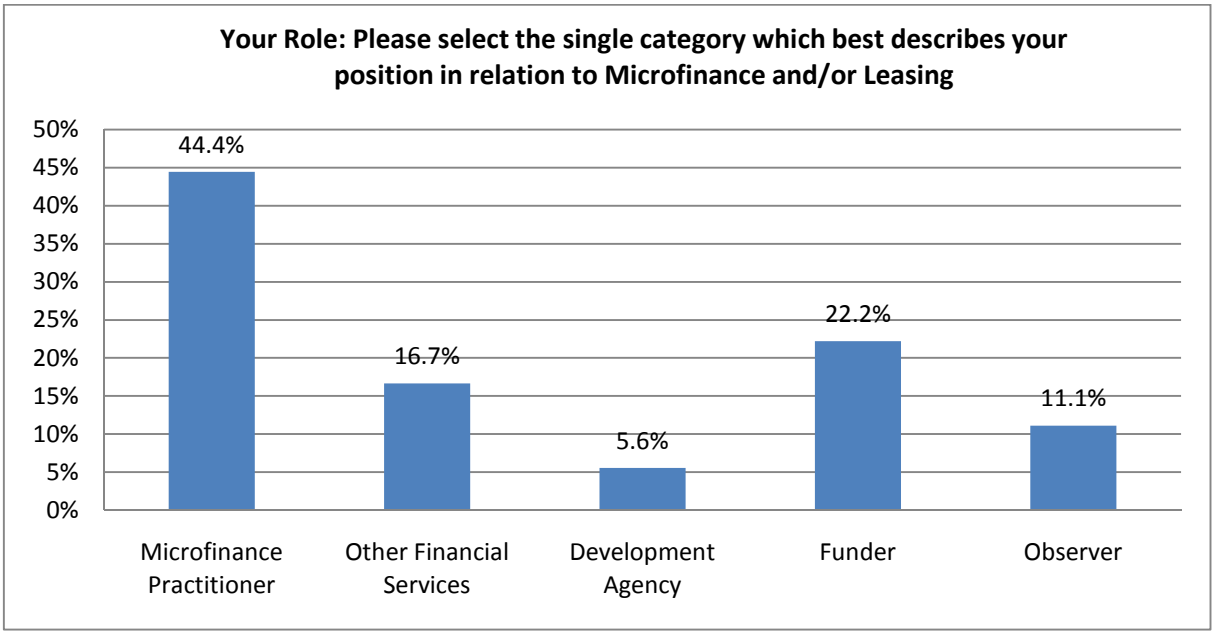
4.3.1 Profile of Respondents and the Microfinance Context

In the first section questions were designed to categorise the respondents and to give them an opportunity to describe their opinion of the key issues and priorities of the sector, before narrowing the enquiry to leasing. A good range of stakeholders responded and indicated that outreach (reaching the maximum number of poor clients) is an important but not exclusive priority for MFIs. Other concerns were over expansion of the sector, and continued funding.

4.3.1.1 Question 1 – The Respondent Profile

Responses were received from every category of respondent with 44% coming from actual MFI practitioners (see figure 4.3.1.1).

Figure 4.3.1.1: Respondent Profile



4.3.1.2 Question 2: What Is The Biggest Issue Facing Microfinance?

The responses are presented in Table 4..

There was overlap in 3 areas with 4 respondents identifying the proliferation of MFIs as a threat; 3 identifying funding and 3 commercialisation as the major issues. Funding and proliferation of many, small MFIs may be potentially linked in that funders are more likely to support large MFIs with a track record than small MFIs that have yet to prove their effectiveness.

Table 4.3.1.2: Issues Facing Microfinance

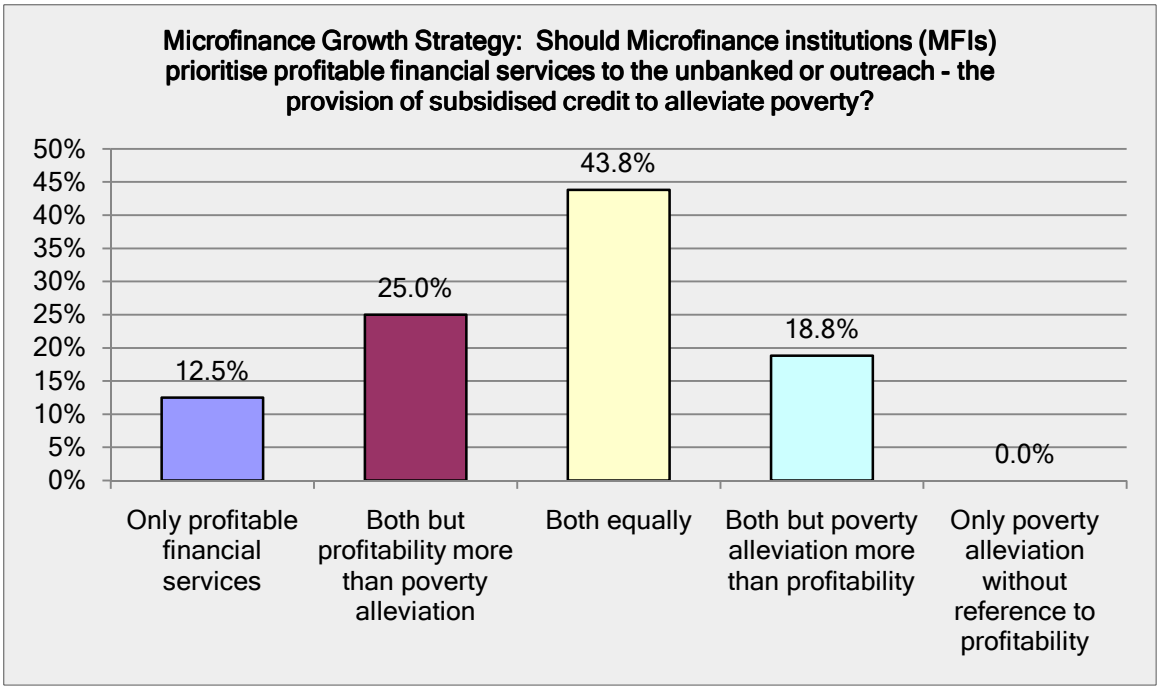
#	The Biggest issue Facing Microfinance	Category of Respondent
2	Funding	MFI Practitioner
6	Funding	Other Financial Svcs
12	Funding as credit risk deteriorates	MFI Practitioner
11	Credit risks	Other Financial Svcs
4	Commercialisation	MFI Practitioner
13	Commercialisation	Observer
14	Commercialisation and short term planning	MFI Practitioner
8	Too many MFIs in some markets, too few in others	Development Agency
15	Too rapid growth	Funder
16	Need for consolidation	Funder
18	Too many MFIs, fraud, poor reputation	MFI
7	Lack of credibility in outreach and/or sustainability mission	Funder
5	Lack of interest by wider financial svcs	Funder
3	Regulation as banks	MFI Practitioner
17	Poor data, overindebtedness, equity valuations	Observer
9	Poor understanding of why high interest rates are justified	MFI Practitioner
1	No response	Other Financial Svcs
10	No response	MFI Practitioner

4.3.1.3 Question 3: MFI Priorities

44% of respondents felt that MFIs should give equal strategic priority to outreach and profitability.

37% felt that profitability should be prioritised (see Figure 4.3.1.3).

Figure 4.3.1. 2: MFI Priorities



4.3.2 Leasing and Funding

This section examined the first of the 3 topic areas, that funding would be a possible barrier to leasing. The responses suggest that funders do support leasing, but also that they are likely to be very interested in the ability of a particular MFI to deliver leasing.

4.3.2.1 Question 4: The potential of leasing as a product for growth

This question examined whether leasing was regarded as having potential in comparison with other products currently available (loans and savings) and products being developed (insurance, Islamic finance). See Table 4.1.

Table 4.1.2.1: MFI Products

Please rank the following products according to your view of their future potential for the Microfinance sector (5 high, 1 low). For Importance						
Answer Options	5	4	3	2	1	Microleasing Survey
Leasing	18%	18%	24%	18%	24%	17
Insurance	18%	12%	53%	12%	6%	17
Savings	41%	35%	6%	6%	12%	17
Loans	53%	24%	18%	6%	0%	17
Islamic Finance	13%	6%	13%	25%	44%	16

Based on those expressing views in the 4-5 category combined, the respondents rank leasing as the product with the 3rd highest potential after loans (77%)and savings(76%), and higher than insurance (30%)

4.3.2.2 Question 5: Will funders of MFI fund leasing?

In answer to the specific question about funder support, 62.5% of respondents felt funders would encourage or even prioritise leasing (see Table 4..3.2.2).

Table 4.3.2.2: Funder Support for Leasing

To what extent do you believe that current funders of MFIs will support medium term credit such as leasing?		
Answer Options	Response Percent	Response Count
Prioritise	12.5%	2
Encourage	50.0%	8
Neither support nor discourage	31.3%	5
Discourage	0.0%	0
Refuse to fund	0.0%	0
No opinion	6.3%	1

4.3.2.3 Question 6: Ranking the concerns of funders

9/14 respondents chose high or 'very high' that lack of expertise would be a concern of funders when considering MFIS as a vehicle for leasing (see 4.3.2.3). The next highest is 6/14 for the FX implications of leasing's longer term, increasing the likelihood repayments in local currency being out of synch with funds originally borrowed in a foreign currency.

Table 4.3.2.3: Funder Concerns

Please rank the factors below as potential concerns of funders about leasing as a product for MFIs (5 high, 1 low)							
Answer Options	Very High	High	Medium	Low	Not a concern	Rating Average	Response Count
Reduced numbers of clients for same amount	2	1	2	1	5	3.55	11
Additional foreign exchange risk due to longer term of	1	5	3	4	2	3.07	15
Risk profile of leasing vs. loans	2	3	4	3	2	3.00	14
Lack of Expertise of MFIs	8	1	2	3	0	2.00	14
Lack of Expertise of Funder	1	4	3	1	3	3.08	12

4.3.3 Leasing Through MFIs

This section of the questionnaire examined the range of internal issues within MFIs that might act as barriers to the development of leasing as a viable MFI product. While respondents seem to agree that leasing is a suitable product the responses clearly favour dedicated leasing teams either within the MFI or through cooperation with the leasing equipment manufacturer or distributor.

4.3.3.1 Question 7: Is Leasing A Suitable Product For MFIs?

Before looking at the potential issues in detail this question sought an answer to the more general question of whether leasing was a suitable product for MFIs. 69% of respondents agreed or strongly agreed that it was (see 4.3.3.1).

Table 4.3.3.1: Support for Leasing through MFIs

Do you believe that small equipment leasing is a suitable product for MFIs?		
Answer Options	Response Percent	Response Count
Strongly agree	37.5%	6
Agree	31.3%	5
Neutral	25.0%	4
Disagree	6.3%	1
Strongly Disagree	0.0%	0

4.3.3.2 Question 8: Leasing As A Complimentary Or Competitive Product Within Mfis

This question revealed a strong opinion amongst respondents that leasing is a specialist activity and either should be done by experts within an MFI (53%) or in a different company (24%) (4.3.3.2)

Table 4.3.3.2: Leasing vs Loans in MFIs

Successful MFIs have a customer base, internal organisation and reporting systems to deliver loans. Leasing has similar requirements though modifications are common. In your opinion would leasing conflict with loans if offered through the same MFI?		
Answer Options	**Response Percent**	**Response Count**
Leasing is complimentary and can be done in the same company as microloans	5.9%	1
Leasing is complimentary but requires specialists to be done in the same company	52.9%	9
Leasing is competitive and should be done in a different company	23.5%	4
None of the above	11.8%	2
No opinion	5.9%	1

4.3.3.3 Question 9: Key Factors For Successful Leasing

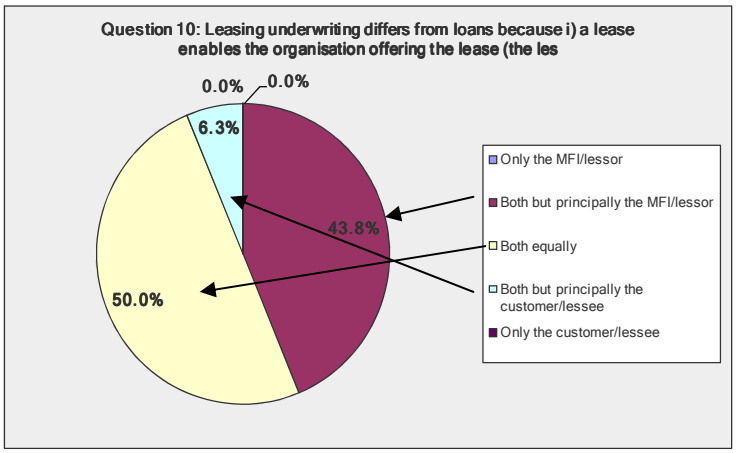
6 factors are presented in Table 4.3.3.34.3.3.3 and ranked from 6 (high) to 1(low). In looking successively at those factors ranked 6/6, 6/6 and 5/6, and 6/6, 5/6 and 4/6 a dedicated leasing team was consistently identified as the most important, with manufacturer support second or third in each case .

Table 4.3.3.3: Key factors for successful leasing

Success Factors: Score the following in terms of their importance to the successful small equipment leasing			
	6/6	6/6 and 5/6	6/6, 5/6 and 4/6
1	Dedicated lease sales team	Dedicated lease sales team	Dedicated lease sales team
2	Information systems	Manufacturer/dealer support	Manufacturer/dealer support
3	Manufacturer/dealer support	Information systems	Technical Assistance
4	Incentives for staff and management	Technical Assistance	Equipment expertise
5	Equipment expertise	Equipment expertise	Information systems
6	Technical Assistance	Incentives for staff and management	Incentives for staff and management

4.3.3.4 Question 10: Who Benefits Most From Leasing, The MFI Or The Customer?

Figure 3.3.3.4: Who benefits from leasing?



This question aimed to reveal whether stakeholders felt that leasing offered benefits to the lessor at the expense of the lessee, or vice versa. The response shows that 94% felt that it benefitted both parties with 44% of the opinion that it was more favourable to the lessor than the lessee (see Figure 4.3.3.4).

4.3.3.5 Question 11: Barriers To Establishing Leasing For MFIs

Using another question format to examine respondent views on barriers to leasing Question 11 reveals that 64% of respondents put local taxation regulations in high categories of 5-7 inclusive (see Table 4.3.3.5). The most important internal barriers was identified as organisational expertise with 73% rating this factor 5-7. The third most important issues was cooperation with the manufacturer of the leased equipment with 60% ranking this 5-7. Though the questionnaire sought to reduce taxation and regulation as a major issue by surveying only markets where commercial leasing was already taking place.

Table 4.3.3.5: Barriers to leasing

Please rank the factors below as potential barriers to establishing leasing as a product for MFIs. (7 high, 1 low)							
Answer Options	1(low)	2	3	4	5	6	7 (high)
The local taxation regulations	14%	7%	14%	0%	29%	14%	21%
Lack of funder support	14%	14%	0%	36%	21%	0%	14%
Lack of organisational expertise	0%	13%	7%	7%	20%	33%	20%
Prioritising outreach	7%	7%	20%	20%	7%	27%	13%
FXD risk of medium term funding	14%	0%	36%	43%	0%	0%	7%
Lack of demand from customers	13%	20%	20%	13%	13%	13%	7%
Absence of cooperation with mfg	27%	0%	7%	7%	33%	20%	7%

4.3.4 Demand and Distribution of Leasing

This section examines the last area identified from the structure interview, namely the potential barriers to leasing caused either by customer ignorance of the product, or by the absence of an effective distribution mechanism. Respondents preferred an independent leasing company for

distribution over MFIs as they currently exist. They indicated that they believed customers would understand the benefit to themselves based primarily on the interest cost.

4.3.4.1 Question 12: The Best Organisation Type To Offer Leasing.

This question tests opinion as to the most suitable organisation to offer leasing in a developing market.

Leasing vs Loan: Leases and loans differ in legal, accounting and regulatory aspects, and in the knowledge about the leased equipment that is required. Please rank the following organisations in emerging markets in terms of their actual or potential ability to promote and process leasing (4 high, 1 low)					
Answer Options	**4**	**3**	**2**	**1**	**Response Count**
Bank	3	3	6	2	14
MFI	2	5	3	4	14
Manufacturing Company Subsidiary	4	7	1	2	14
Independent Leasing Company	10	4	0	1	15

Table 4.3.4.1: Suitable organisations for leasing

Table 4.3.4.1 shows the respondents would appear to strongly favour that leasing should take place in an independent leasing company, rather than through an MFI. In question 8, 53% of respondents indicated support for doing leasing in an MFI but using a specialist team.

There is an alternative not tested that might resolve this conflict – leasing done through an independent subsidiary in the same group as an MFI.

4.3.4.2 Question 13: Testing Customer Demand

This question addresses opinions about whether leasing demand would be pull or push ie whether it will be taken up by customers based on an understanding of benefits to themselves (pull) or because of limited choice combined with active promotion by the lender (push).

Table 4.3.4.2: Demand for leasing

Demand from Customers: Which of the following statements do you agree most with? Tick one response only		
Answer Options	Response Percent	Response Count
MFI customers will purchase financial products based on a detailed understanding of the costs and benefits to themselves	46.7%	7
MFI customers will take up either lease or loan depending on the interest payment	26.7%	4
MFI customers will take up whatever forms of credit for which they are approved	6.7%	1
MFI customers will take up leasing only if it is associated with a particular type of equipment and offered as a means of payment by the distributor	6.7%	1
MFI customers will prefer loans for a variety of reasons	13.3%	2

A majority of respondents felt confident that customers would make an active decision to purchase a lease based on their own assessment of costs and benefits, rather than viewing it as simply a form of credit in a constrained market (see Table 4.3.4.2).

4.3.5 Validation Section

In this section a number of statements were made for the respondents to indicate agreement on a scale. The majority of the statements can be matched previous sections, checking for consistency. Statements are highlighted where 50% or more of the respondents selected options at the top or bottom two of the 7 available (see Table 4.3.5.1).

Table 4.3.5.1: Validation statements

Question 14: Validation Check								
Answer Options	**Strongly Disagree**	**2**	**3**	**Neutral**	**5**	**6**	**Strongly Agree**	**X-Ref with**
Microfinance is only possible with subsidy in the form of cheap debt or equity	7	4	1	2	0	0	2	Q1-3
Equipment leasing has already reached its potential within MFIs	5	6	2	1	0	0	1	Q1-3
Loans are preferable over any other product to the funders of MFIs because of their short term and ability to reach wide numbers of people	3	5	1	3	0	3	1	Q4-6
Customer using new loans from one MFI to repay existing loans with a different MFI is a risk for the Microfinance sector	0	0	0	1	3	5	7	Q1-3
MFIs should not seek to limit or control what their customers do with their loans	2	2	2	2	3	1	4	Q1-3
Credit is a human right	8	0	0	6	0	1	1	General
MFIs should prioritise the number of customers they have over the range of products offered	1	3	1	3	5	1	2	Q1-3
Funders of MFIs support product diversification for MFIs	1	3	0	4	2	2	3	Q4-6
Incentives provided to MFI staff are the key to the success of a new product	0	0	4	4	3	1	3	Q7-11
Leasing is a better product for MFIs than insurance	3	3	1	1	2	1	4	Q4-6
Banks are the most suitable organisation to offer leasing in emerging markets	2	3	3	1	6	1	0	Q12-13
Foreign exchange risks associated with medium term funding make offering leasing in developing markets difficult	2	3	3	3	3	1	1	Q7-11
The interest rate on microloans should be subject to a price ceiling	5	2	1	3	3	1	1	Q1-3
Small equipment leasing is practical only when offered as a financial incentive by equipment dealers or manufacturers	3	3	3	3	1	2	1	Q7-11
Leasing is an effective means of promoting green technology such as solar powered water pumps,	2	1	2	2	3	2	4	General
The difference between a loan and a lease is not important to clients of microfinance - both are credit and affordability is the key criteria	2	3	0	1	3	3	4	Q12-13
Information technology or the lack of it is a major barrier to the growth of microfinance institutions	0	2	4	3	3	2	1	Q7-11
There is no incentive for microfinance institutions or banks to offer leasing in developing markets	0	0	3	3	5	3	2	Q7-11
Development funding should be directed to expanding the role of collateralised lending through MFIs and reducing the predominance of unsecured loans	1	1	2	4	3	2	3	Q1-3
Savings and not loans should be the focus of microfinance	1	4	3	4	1	0	3	Q4-6
Tax benefits are the key to leasing and without them there is no incentive for financial institutions to promote them.	2	2	2	2	2	3	2	Q7-11
Leasing is a means for manufacturers of equipment to promote their sales and has no role in microfinance	3	8	1	1	0	1	2	Q7-11

Respondents *agreed* strongly with the 4 statements:

1. 'Customer using new loans from one MFI to repay existing loans with a different MFI is a risk for the Microfinance sector'
2. 'Leasing is an effective means of promoting green technology such as solar powered water pumps, generators, bicycles'
3. 'The difference between a loan and a lease is not important to clients of microfinance – both are credit and affordability is a key criteria'
4. 'There is no incentive for microfinance institutions or banks to offer leasing in developing markets'

Statement 1 is not checking consistency with another question directly, but does test further the strategic case for leasing. Strong agreement with the statement is potentially favourable to leasing

because the purchase of the equipment by the lessor prevents the use of cash for repayment of other loans.

Statement 2 is specifically favourable to leasing as a tool for promoting uptake of green technology.

Statement 3 is consistent with the answers to question 13 suggesting that customers will embrace leasing if affordable.

Statement 4 that there is no incentive to offer leasing in developing markets is discussed in the following chapter as the interpretation touches on multiple themes, and leads to suggestions for further work.

Respondents *disagreed* strongly with the 6 statements

1. 'Microfinance is only possible with subsidy in the form of cheap debt or equity'
2. 'Equipment leasing has already reached its potential within MFIs'
3. 'Loans are preferable over any other product to the funders of MFIs because of their short term and ability to reach wide numbers of people'
4. 'Credit is a human right'
5. 'The interest rate on microloans should be subject to a price ceiling'
6. 'Leasing is a means for manufacturers of equipment to promote their sales and has no role in microfinance'

The response to statement 1 is consistent with the responses to question 3.

The responses to statement 2 and 3 are consistent with the responses to questions 5& 7.

Statements 4 and 5 are supportive of a commercial element to microfinance and consistent with responses to question 3.

Responses to statement 6 are supportive to the potential role of leasing in microfinance.

4.4 Summary

The structured interview provided 3 areas to guide further enquiry by means of the questionnaire. These were issues of funding, organisational readiness and demand.

The sections of the questionnaire tested each of these 3 areas. With limited coverage and low response numbers, attention was focused where the majority of responses received showed strong agreement or strong disagreement. On this initial screen the indications are that respondents believe:-

- Leasing is a useful product for MFIs (Q4, Q14)
- Funders and other stakeholders support leasing (Q5 and Q7)
- The principal barrier is the expertise required within an MFI (Q6, Q8, Q9, Q11)
- The customer will engage with and benefit from leasing (Q10, Q13, Q14)
- The best way to deliver leasing is through a separated organisation (Q12)

Discussion of these results and the relation to the initial hypotheses generated from the structured interviews follows in the next chapter.

Chapter 5 – Discussion of Results

5.1 Overview

The literature review of leasing in developing markets suggests that development agencies strongly support leasing as a key financial service for emerging economies, but have not been successful in creating sustainable leasing companies that target the rural or urban micro-enterprises. Structured interviews and a questionnaire of MFI stakeholders indicate that there is support for leasing as a product for MFIs together with an acknowledgement that MFIs do not currently have the expertise to handle it within their own organisations. A case is made for investing to overcome this expertise gap in order to retain the MFI benefits of distribution, underwriting and customer service. It is also suggested that a proportion of lease development funding be re-directed to the MFI sector to enable them to develop the expertise necessary to extend leasing to the newly banked micro enterprises that are their customers. This would facilitate the achievement of strategic goals of both lease development funders and of MFIs

5.2 Limitations of Scope

The limits imposed by lack of funds and restricted time have been acknowledged throughout this dissertation. The direct result of this has been than only qualitative and low level quantitative analysis was performed on those areas where strong consistency in the views of the stakeholders was apparent. The scope for expanding the questionnaire and subsequent analysis is discussed in the next chapter.

5.3 Discussion of Literature Review

The literature review performed identified 4 possible reasons why development of leasing lags development of MFIs in new markets. These were regulatory and institutional barriers, specialist

knowledge and customer demand. These issues also emerged from the structured interviews, and were incorporated in the design of the questionnaire.

A notable feature of the literature review was that only in the most recent publications are leasing and microfinance being linked (Goldberg, Microleasing, 2008; Goldberg & Palladini, 2010). The contrast between the successes of two different strategies for developing emerging market financial services may be worth examining for potential lessons. Of more practical use is to consider that, irrespective of how we got here, microfinance has now reached such a scale that it has changed the context for leasing in the future. MFIs must now be considered alongside banks and independent leasing companies as a distribution mechanism for leasing, especially for small and micro-enterprises.

The promotion of leasing by development agencies typically focuses on either leveraging an existing customer base, or as a means for financing a particular type of equipment such as agricultural machinery. Using existing banks makes sense as it ensures wider distribution and reach. The result has been that banks sell to existing customers, which in emerging markets are not small or informal businesses. Using leasing as a means to encourage take up of new technology suffers from being tied to the productivity or outreach initiative rather than seeking to create a sustainable leasing business. Unsurprisingly, when the project funds have been used up, the leasing stops. Hence after 25 years of support, where leasing is successful, it is a product for established customers with scale who already participate in financial services. Leasing has not reached the small and informal business sector in developing markets despite its inherently attractive features of reduced collateral requirements for the lessee, and retained ownership for the lessor.

On the face of it the microfinance sector has become the natural candidate to put the option of leasing in the hands of the small and informal enterprises. With 133,000,000 customers by 2007 (CGAP, 2010) and an underwriting and customer services capability designed around individuals, groups and small and micro enterprises large MFIs would seem to have the access and the back

office required. Why this has not happened to date emerged from the survey and questionnaire discussed next.

5.4 Discussion of Structured Interview and Questionnaire Results

The interviews and questionnaire examined why leasing has not to date made significant progress as a product for MFIs. The results obtained would seem to be good grounds for believing there is a good base knowledge and support for leasing and that the barriers to its spread have been concern about the level of expertise required to create a leasing capability rather than strategic concerns about compromising outreach, or a lack of demand from customers.

The concern about expertise was most clearly manifested in question 6 where 9/14 respondents identified it as a major concern of funders; question 8 where 9/17 respondents supported the statement that it needed to be done by a specialist team within an MFI and in question 11, where 73% of respondents ranked it in the highest categories as a barriers. In question 12, 14/15 respondents felt leasing would be better done in an independent leasing company, rather than in a bank, MFI or manufacturing company subsidiary.

The conflict between the attitude expressed in question 8 supporting an internal team and question 12 supporting an independent team requires further investigation. The questionnaire did not offer an alternative of a separate subsidiary within an MFI group – an option which could resolve the matter. What is this expertise that is lacking? When asked in question 9 which function in the organisation was most important for leasing, a dedicated sales team came out on top in all categories. In developed markets leasing to small and medium sized enterprises is most often introduced at the point of sale of the asset e.g. a vehicle or office technology dealership. It is presented as a cost for usage per day or per month so that the business owner can make their own decision as to whether the benefit of increased profitability is worth the cost of the lease. This can

either be done by an expert equipment sales person or by a leasing specialist in person or subsequently at a different location or electronically.

In creating an independent leasing company one must not only secure a flow of transactions, but one must also underwrite, price, process, account, handle customer queries and collect delinquent accounts. These require the separate skills of underwriting, finance, specialist IT programming and customer services. Large MFIs, while lacking a dedicated sales team, have all of these additional functions. In particular, through their accumulation of data about customer behaviour, they are pre-eminent in financial services at predicting the risk of default of small and micro enterprises. Large MFIs have a cost structure designed around small transactions. These are substantial advantages to have over a new leasing company. Finally, as a new start an independent leasing company would also have to train a new sales team. A large MFI would be quicker to market than an independent leasing company.

5.5 The Potential for Lease Development Funding through MFIs

There would seem to be an opportunity therefore to link the appetite for new products and distribution capacity of MFIs with the technical leasing expertise and capacity building funds of development banks. This could potentially deliver a strategically important new product to MFIs and increase the reach and sustainability of the leasing development projects funded by the development banks.

The success of leasing in development is strongly associated with an existing customer base and infrastructure. To date within traditional banks, this has meant that leasing has ended up as a product for existing larger bank customers, and has missed small and micro enterprises. MFIs now offer exactly this customer base and the specialist functions and organisational design that enable sustainable financial services. If a portion of future investment in leasing development is redirected

to MFIs, the goal of expanding credit to the SME sector can be reached at the same time as supporting the growth potential and reducing the risk profile of large MFIs.

The next chapter looks at further work to validate these conclusions and to set up a project to test them in the field.

Chapter 6 - Further Work

6.1 Overview

The interest in leasing as a product for MFIs and agreement that expertise or the lack of it is the principal barrier to its spread this could be further tested in the first instance by working to obtain a greater response percentage for the questionnaire to enable more in depth quantitative analysis. Assuming validation was forthcoming, the next step could be to seek funding support for one of 3 alternative field projects designed to deliver leasing to micro-entrepreneurs, namely

1. Creating a specialist team within an MFI leasing a narrow range of equipment for which there is an existing demand amongst urban or rural micro-entrepreneurs
2. Creating a 'captive' leasing company being a partnership between and MFI and an equipment manufacturer leasing the partner's equipment.
3. Creating a separate entity, either captive or independent, in partnership with an equipment manufacturer of green technology, leasing the selected equipment.

Of these the third option would seem to be most likely to minimise risk, and fit most with the strategic priorities of all parties. For the MFI, funding would not be withdrawn from core operations; the customer base would be provided with a new product and productivity of existing operations would be maximised. For the development agency the strategic goals of extending leasing to the SME sector and reducing carbon footprints would be achieved and partnering options would be increased by working with low cost MFIs. For the manufacturer, the credit available to customers would increase the sales of their equipment and their installed base would expand.0

6.2 Extended Questionnaire and Validation of Results

The initial work of interviews and questionnaire can be seen as a pilot for further work. The ultimate goal would be a field based project, where the opportunity for leasing to micro-entrepreneurs is tested.

The next step would therefore be an extended effort to obtain a higher percentage of questionnaire responses to facilitate robust quantitative analysis. Personal follow up, incentives and better targeting based on research and networking would generate more replies which could be analysed statistically.

6.3 Proceeding to Field Work

If the additional work proposed in 6.2 validated the support for leasing and the perception that the principal barrier is current lack of MFI expertise in the product, there would seem scope to mobilise the support and overcome the barrier by designing a field trial. Such a project could both deliver specific local benefits as well acting as a template for replication through-out the sector.

Designing the project would have to take account of a number of factors such as

- Availability and interest of a local partner
- Regulatory and tax environment
- Competitive environment and potential customers
- Source of funding for the project *and* for leases
- Target equipment for leasing
- Means of distribution
- Systems and underwriting requirements
- Source and cost of capacity building expertise

The availability and interest of a local partner would determine the organisational structure of the pilot scheme. If the partner was an MFI that wished to retain complete independence – for instance in order to protect its strategic goal of outreach – a leasing team could be built within the MFI focussing on equipment that was known to be in demand with the existing MFI customer base. Funding for the pilot and for the leases would then come from existing or new MFI capital, and a likely source would be to tap into existing development funding for leasing on the basis that the scale of selected MFIs greatly increase the ability of leasing to be distributed widely and reach micro enterprises.

If one of the partners was an MFI that was willing to enter into further partnership with a large manufacturer or distributor, a leasing team could be built around the customer base and technology of the MFI, using the equipment expertise of the commercial partner and optimising the distribution of both parties. These structures are described as 'captive' leasing organisations. While funding for the project would be shared, a partnership with a purely commercially motivated company would raise issues for MFIs that priorities outreach over sustainability, thus limiting the range of MFIs willing to participate.

A third version of this which could overcome the potential conflict of interest between an MFI and a commercial partner is to design a pilot for leasing 'green' technology. The diffusion of green technology such as solar powered pumps, generators, bicycles is likely to attract support of development funders over and above existing support for microfinance as it addresses directly issues of carbon emissions. The manufacturers of the selected green technology would benefit in the same way as any manufacturer from a financing product that enhances sales through the provision of credit. This combination of partnership advantages plus funding attractiveness suggests this would be a good model with which to start.

Chapter 7 - Conclusion

Both MFIs and development agencies are in the process of transforming financial services outside of the developed markets by offering credit products to the unbanked. To date, MFIs have concentrated on loan products, and have built a large customer base of previously unbanked individuals and micro enterprises. Development agencies have broadened the availability of financial service products in many markets. In the case of leasing, agencies have worked principally with traditional financial service organisations such as banks and independent leasing companies and not with large MFIs.

Leasing can have a positive role in development by increasing the productivity of SMEs and micro-enterprises in developing markets. This is because the additional cash flow created by the leased asset is taken into account by the lessor, potentially reducing the need for collateral. Leasing can also make a positive contribution in the microfinance sector by providing additional credit to MFI customers, and by helping to diversify the risk profile of MFIs. This study suggests that the principal barrier to achieving these benefits is the lack of current leasing expertise in MFIs.

The barrier of product expertise within emerging market financial service institutions is a familiar challenge to development agencies. As some MFIs have achieved substantial scale and become a stable member of the financial service sector, this study proposes that in future they should be included as potential lessors by development agencies. In this way, the challenges of extending the benefits of leasing to micro enterprises could be overcome, at the same time as diversifying and reinforcing MFIs.

A model is proposed to test this by using leasing to promote a selected green technology asset through an established MFI, with capacity development funding from the development agency sector.

Appendix 1

Leasing in Microfinance Questionnaire

No: XXXXX

Information Sheet

This survey forms part of research aimed at understanding the actual and potential role of leasing in Microfinance Institutions (MFIs). The results of the survey will be incorporated into a Master's degree dissertation undertaken at the Graduate Institute of International Development and Advanced Economics at the University of Reading.

Participants have been selected for their expertise and/or current roles as MFI stakeholders, customers or interested parties. Your identity will not be revealed to anyone other than the project principal. You are free to withdraw from the questionnaire at any time you feel uncomfortable or unwilling to participate, and you do not have to specify a reason. Any contribution can be withdrawn at any stage and removed from the research if desired. If you wish to withdraw, please contact Kevin Kennedy (details below), quoting the reference at the top of this page. The reference will only be used to identify your questionnaire and will not reveal any other information about you.

By answering the interview questions and/or completing the questionnaire you are acknowledging that you understand the terms of participation and that you consent to these terms. This project has been subject to ethical review, according to the procedures specified by the University Research Ethics Committee, and has been allowed to proceed.

If at any stage you wish to receive further information about the questionnaire or project please do not hesitate to contact Kevin Kennedy (details below). Alternatively, this dissertation is supervised

by Dr Nick Beard of the Graduate Institute of International Development and Economics who can be contacted at the same institution or via email on n.f.beard@reading.ac.uk .

Your participation is appreciated

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Leasing and Microfinance Survey

Leasing is a form of credit where the lender buys an asset and retains ownership while the customer takes possession of and has full use of it. As a financial product leasing is considered specialist lending requiring an understanding of the type of asset leased. As a lease covers the whole of the working life of the equipment, leasing is classified as medium term credit.

For over two decades Development Banks have worked to create the right regulatory environment for leasing in emerging markets. In the same period microfinance has grown to become a major provider of financial products to the poor and unbanked. This research investigates whether leasing is a suitable product for Microfinance institutions, where the right regulatory environment exists.

Section A: The Microfinance Context

This section collects information on respondents' general views of the microfinance sector

1. Your Role: **Please select the single category which best describes your position in regard to Microfinance and/or Leasing**

   Microfinance Institution (MFI) ☐
   Commercial bank or leasing company ☐
   Development Bank ☐
   NGO ☐
   Microfinance Investment Vehicle (MIV) ☐
   Manufacturer ☐
   Consultant ☐
   Customer ☐

   Other (please specify) _____

2. State of Microfinance: **In your opinion what is the principal issue facing the Microfinance sector today?**

3. Microfinance Growth Strategy: **Should Microfinance institutions (MFIs) prioritise profitable financial services to the unbanked or outreach - the provision of subsidised credit to alleviate poverty**

- ☐ Only profitable financial services
- ☐ Principally profitable financial services to the unbanked
- ☐ Both but profitability more than poverty alleviation
- ☐ Both equally
- ☐ Both but poverty alleviation more than profitability
- ☐ Principally the provision of credit to alleviate poverty
- ☐ Only poverty alleviation without reference to profitability

4. **Please rank the following products according to your view of their future potential for the Microfinance sector** (5 high, 1 low). For instance if you view savings as the most important product to be offered by MFIs, rank it as "5"

Leasing	Choose score
Insurance	Choose score
Savings	Choose score
Microloans	Choose score
Islamic FInance	Choose score
Other (please specify)	
No opinion (tick only)	☐

Section B: Leasing and Funding

Leasing and loans both require a source of funding in order to advance the smaller credit amounts required by their customers. Sources of funds can be external from commercial markets or sources of development funds, or internal funds such as deposits and cash flow from other operations.

Small equipment leasing is typically medium term finance over 18 months or more while microloans are offered over terms of less than 1 year**.**

5. **To what extent do you believe that current funders of MFIs will support medium term credit such as leasing?**

Prioritise ☐
Encourage ☐
Neither support nor discourage ☐
Discourage ☐
Refuse to fund ☐
No opinion ☐

Comment

6. **Please rank the factors below as potential concerns of funders about leasing as a product for MFIs** (5 high, 1 low)

Reduced numbers of clients for same amount borrowed	Choose score
Additional foreign exchange risk due to longer term of funds	Choose score
Risk profile of leasing vs. loans	Choose score
Other)	Choose score
Other)	Choose score

Section C: The Organisational Challenges of Leasing

7. Lleasing has historically been offered either through banks, through the subsidiaries of manufacturing companies, or by independent specialist leasing companies. MFIs potentially represent a new way to provide leasing.

Do you believe that small equipment leasing is a suitable product for MFIs? Please explain.

Strongly agree ☐
Agree ☐
Neutral ☐
Disagree ☐
Strongly Disagree ☐

Comment

8. Successful MFIs have a customer base, internal organisation and reporting systems to deliver loans. Leasing requires many of the same ingredients though modified to take account of the product differences. **Is leasing a complimentary or competitive product in your opinion?**

   - ☐ Leasing is complimentary and can be done in the same company as microloans
   - ☐ Leasing is complimentary but requires some specialists to be done in the same company
   - ☐ Leasing is complimentary and can be done in the same company as microloans
   - ☐ Leasing is competitive and should be done in the different company as microloans
   - ☐ None of the above
   - ☐ No opinion

9. Success Factors**: Please score the following in terms of their importance to the successful offering of small equipment leasing through MFIs. (5 high, 1 low)**

Information systems	Choose score
Incentives for staff and management	Choose score
Equipment expertise	Choose score
Technical Assistance	Choose score
Manufacturer/dealer support	Choose score
Dedicated lease sales team	Choose score

Other (please specify)

10. A potential benefit of leasing is that it is self collateralising i.e because the organisation offering the lease (the lessor) retains ownership and can repossess, the equipment itself provides collateral for the credit. **Do you believe that this feature of 'self-collateral' would benefit MFIs and their customers?**

   - ☐ Only the MFI/lessor
   - ☐ Both but principally the MFI/lessor
   - ☐ Both equally
   - ☐ Both but principally the customer/lessee
   - ☐ Only the customer/lessee

11. **Please rank the factors below as potential barriers to establishing leasing as a product for MFIs**.

The local taxation regulations	Choose score
Lack of funder support for product diversification	Choose score

Lack of organisational expertise (for instance systems and training)	Choose score
Organisational strategy prioritising outreach	Choose score
Foreign exchange risk of medium term funding	Choose score
Lack of demand from customers	Choose score
Absence of cooperation with an equipment manufacturer or distributor	Choose score

Other (please specify)

Section D: Demand for Leasing

12. Leasing vs Loan: The difference between a lease and a loan lies in its legal definition and its accounting and regulatory aspects, and in the knowledge about the leased equipment that is required. Please rank the following organisations in emerging markets in terms of their actual or potential ability to promote and process leasing.

    Bank
    MFI
    Manufacturing Company Subsidiary
    Independent Leasing Company
    Other (please specify)

13. Demand from Customers: Which of the following statements do you agree most with? Tick one response only

    - ☐ MFI customers will purchase financial products based on a detailed understanding of the costs and benefits to themselves
    - ☐ MFI customers will take up either lease or loan depending on the interest payment
    - ☐ MFI customers will take up whatever forms of credit for which they are approved
    - ☐ MFI customers will take up leasing only if it is associated with a particular type of equipment and offered as a means of payment by the distributor
    - ☐ MFI customers will prefer loans for a variety of reasons
    - ☐ No opinion

Section B: General

14. After you read each of the following statements please tick the box that best shows your opinion, where 1 is strongly disagree and 7 is strongly agree

	Strongly Disagree						Strongly Agree
	1	2	3	4	5	6	7
Microfinance is only possible with subsidy in the form of cheap debt or equity							
Equipment leasing has already reached its potential within MFIs							
Loans are preferable over any other product to the funders of MFIs because of their short term and ability to reach wide numbers of people							
Customer using new loans from one MFI to repay existing loans with a different MFI is a risk for the Microfinance sector							
MFIs should not seek to limit or control what their customers do with their loans							
Credit is a human right							
MFIs should prioritise the number of customers they have over the range of products offered							
Funders of MFIs support product diversification for MFIs							
Incentives provided to MFI staff are the key to the success of a new product							
Leasing is a better product for MFIs than insurance							
Banks are the most suitable organisation to offer leasing in emerging markets							
Foreign exchange risks associated with medium term funding make offering leasing in developing markets difficult							
The interest rate on microloans should be subject to a price ceiling							
Small equipment leasing is practical only when offered as a financial incentive by equipment dealers or manufacturers							
Leasing is an effective means of promoting green technology such as solar powered water pumps, generators, bicycles etc							
The difference between a loan and a lease is not important to clients of microfinance – both are credit and affordability is the key criteria							
Information technology or the lack of it is a major barrier to the growth of microfinance institutions							
There is no incentive for microfinance institutions or banks to offer leasing in developing markets							

Development funding should be directed to expanding the role of collateralised lending through MFIs and reducing the predominance of unsecured loans							
Savings and not loans should be the focus of microfinance							
Tax benefits are the key to leasing and without them there is no incentive for financial institutions to promote them.							
Leasing is a means for manufacturers of equipment to promote their sales and has no role in microfinance							

Thank you. For further questions, information or results please contact

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