Microfinance Issues and Challenges in the Anglophone Caribbean

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ABSTRACT

This paper describes the microenterprise and microfinance sectors of seven English-speaking Caribbean states, examines main constraints on the development of a well functioning microfinance market in these countries, and highlights the amount, type, and results obtained in microenterprise projects financed by the Inter-American Bank in the last fifteen years. It suggests that English-speaking Caribbean microfinance organizations have not attained as much success in client outreach and sustainability compared to Latin American counterparts due to different legacies. Higher levels of economic and financial stability coupled with high levels of socio-economic development and strong government presence in microfinance have not created the same impetus for the rapid development of a commercially oriented style of microfinance as witnessed in Latin America in the 1980-90s. Several other factors led to a heavier and more sustained reliance on subsidies in the Anglophone Caribbean: notably, NGOs there have had less time, and less sustained external technical assistance, to experiment with commercially sustainable microfinance. This reliance on subsidies has persisted among practitioners as well as policymakers.

This differing context should be taken into account in the design of strategies promoting microfinance in the Caribbean. The paper examines the role of the Inter-American Development Bank in the sector, and draws conclusions based on the lessons learned from its Caribbean microenterprise projects of the past decade. The paper concludes with a number of potential strategic interventions: for example, educating public sector policymakers and microfinance organization (MFO) managers about appropriate interest rate policies; creating more favorable conditions for sustainable microfinance, namely by improving secured transactions frameworks and building credit bureaus; encouraging existing commercial banks and finance or trust companies to down-scale and penetrate microenterprise markets; strengthening existing institutions in order to achieve a "breakthrough model" of commercially sustainable microfinance; and, if certain conditions are met, promoting the creation of new institutions dedicated to microfinance. It concludes that the English-speaking Caribbean needs to take advantage of its relatively high level of economic and financial market development and develop new methodologies and products aimed at serving small and micro entrepreneurs.

TABLE OF CONTENTS

I. INTRODUCTION

Small and micro enterprises in the Anglophone Caribbean constitute the majority of business firms and generate significant amount of employment and economic value added.[1] A critical constraint repeatedly identified in surveys is the lack of access to formal credit. Limited access to capital stunts the growth, modernization, and expansion possibilities of many firms. While limited access to credit by small entrepreneurs is common problem in many developing countries, microfinance intermediaries in various part of the developing world have appeared and are beginning to fill some of the microentrepreneurs' latent demand for credit. Unfortunately, the microfinance industry in the Anglophone Caribbean is immature compared to other parts of the developing world, particularly South Asia and Latin America. It has suffered from substandard financial performance and has not achieved noteworthy outreach into the microenterprise sector.

The purpose of this paper is fourfold. First, it seeks to highlight the general characteristics of the microenterprise sector and the microfinance industry in the Anglophone Caribbean. Second, it will examine the main factors that help explain the differences in the development of sustainable microfinance in the Anglophone Caribbean compared to Latin America. Third, it will outline what the Inter-American Development Bank, a major donor organization, has done to support microfinance and microenterprise development in the Caribbean in the last fifteen years and what has it achieved. And fourth, it will examine the types of potential strategic interventions that can be pursued by practitioners, national governments, and donor organizations interested in accelerating the growth and consolidation of the microfinance industry in the near future.

II. OVERVIEW OF THE MICROENTERPRISE AND MICROFINANCE SECTORS IN THE CARIBBEAN

A. General Characteristics of the Microenterprise Sector

1. Definition, Characteristics, and Economic Significance

The definition of small and micro enterprises varies from country to country in the subregion. A wide array of definitions exist for the sector, some concentrating on the number of employees and assets held (as in Trinidad and Tobago, Jamaica and Guyana), others on revenues received by the company (as in Belize)[2]. Regardless of the criteria, the vast majority of microenterprises

[1] The Anglophone Caribbean member countries of the Inter-American Development are (1) The Bahamas, (2) Barbados, (3) Belize, (4) Guyana, (5) Jamaica, (6) Trinidad and Tobago, and (7) Suriname. These are the countries that will be studied in the paper, unless otherwise stated. Note: The official language of Suriname is Dutch but for Bank purposes the language used for interaction is English.

[2] For example, in Trinidad and Tobago, microenterprises are owner managed firms with less than five employees. In Guyana a small business is defined as having less that 10 employees, while in Jamaica a small or microenterprise has less than 25 employees. In Belize a small business has sale revenues less than US$250,000 per annum. In each country there are also varying levels of fixed assets that accompany the employee criteria. The range is from US$25,000 to US$121,000.

consists of "own account" operations with one owner-operator. In addition, these microenterprises have another common set of characteristics: a high degree of informality, a concentration in retail and services sectors, a tendency to be engaged in labor-intensive, home-based production; a tendency to have a significant percentage of female ownership; a tendency to serve primarily the domestic market; a small scale of operations; and a low volume of sales. In short, the majority of microenterprises are either subsistence-oriented or steady-state operations with limited potential for income and firm size growth. A small fraction, however, do have the potential to increase size, volume of sales, and wages.

Despite these characteristics, the small and microenterprise sector continues to be of vital economic importance to the economies of the subregion due to the number of jobs created and the estimated contribution to gross domestic product (See Table 1). As can be seen, small and micro enterprises account for up to 40% of total employment and up to 45% of GDP for countries with data available.

Table 1: Economic Importance of Small and Micro Enterprises in the Caribbean

Country	Estimated Number of Small and Micro Firms	Estimated Number of Employees as Share of Total Employment	Estimated Contribution to GDP	Sectors of Concentration (Rank Order)	Source
Belize	17,000	32%	45%	1. Agriculture 2. Services 3. Light Manufacture	Labor Force Survey 1993; NDF Belize op. Cit.
Guyana	22,000	40%	Min. 27.5%[1]	1. Retail 2. Agriculture 3. Services	Guyana: An Enterprise Development Diagnostic-IDB 1998
Jamaica	88,711[2]	16%		1. Trade 2. Hotels & Restaurants 3. Manufacturing 4. Services 5.	STATIN Survey 1990

1. Data are available only for small and medium-scale rice and sugar producers. These two subsectors generate 27.4% of Guyana GDP at market prices. When the contribution of urban MSME are included, the figure should be much higher.
2. Agriculture excluded. A 1999 estimate places the number of firms at 100,000. Source: Webber. 2000.
Sources: Various diagnostic studies financed by the IDB. See bibliography.

2. *Common Constraints Facing Caribbean Microentrepreneurs*

Small and micro enterprises throughout the Anglophone Caribbean tend to face common constraints. They are:

- Lack of access to resources including credit and training
- Hostile policy environments
- Lack of access to markets
- Lack of basic infrastructure

Most microenterprises are financed by own savings, transfers, and borrowings from family and friends. Formal financial institutions are reluctant to lend to small and micro enterprises because they perceive high risks and high transaction costs. Only an estimated 3-5% of microentrepreneurs in the Caribbean have access to financing.[3] Most microentrepreneurs lack real collateral to serve as a guarantee, demand small loans that have high transaction costs, and operate in unfavorable settings that may jeopardize repayment capacity. As a result, the size and growth potential of many potentially dynamic microenterprises can be constrained by lack of access to capital. Besides the problem of lack of access to credit, the generally low level of human capital in the microenterprise sector further reduces the ability to attain high levels of technical efficiency, adapt new technology, and gain access to strategic markets.

Other major constraints are poor policy and institutional environments (appreciating real effective exchange rates, inadequate legislative and regulatory frameworks, weak public sector institutions that provide legal protection and business support and training services) and inadequate physical infrastructure that reduces profitability and competitiveness.

B. General Characteristics of Caribbean Microfinance Sector

Currently, the Caribbean microfinance industry is dominated by non-governmental organizations (NGOs) and credit unions (CUs).[4] These institutions attempt to fill the gap created by the virtual absence of commercial banks in this market segment, but most are financially unsustainable and remain dependent on external donor funds. Prior to the arrival of NGOs and CUs, government-sponsored or owned specialized institutions (national development foundations (NDFs) and development banks) played a vital role. With the exception of Belize, NDFs have declined in importance. Unlike the emerging trend in Latin America, where more regulated financial entities are starting to offer microfinance products and become significant suppliers, only a few regulated institutions in the Anglophone Caribbean have been or are currently active in microfinance: Worker's Bank in Jamaica, Caribbean Microfinance Ltd. in Trinidad and Tobago, and Scotia Enterprise in Guyana (See Table 2).

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[3] See various IDB sponsored diagnostic studies

[4] There are a handful of microcredit NGOs operating, and quite a number of credit unions. Credit unions, however, despite high rates of penetration and 4 % share of total claims on private sector lending (Ratio of Coop/Bank loans for 1998), are not uniformly engaged in microfinance. Many credit unions are closed bond in the Caribbean, and small business and micro lending are relatively new product lines. Nonetheless, there is an underreporting problem—many personal and consumer loans are diverted into microenterprises. See Annex 3.

Table 2: Selected Characteristics of Caribbean Financial System and Microfinance Industry

Country	Estimated Number of Financial Institutions	Dominant Microlenders/ Type of Institution
Barbados	✍ Commercial Banks (7 total, with 3 foreign owned) ✍ Merchant Banks, Trust and Finance Companies (5) ✍ Credit Unions (38) ✍ Development Finance Institutions (3)	✍ FUND ACCESS (Governmental) ✍ Barbados Enterprise Growth Fund (Venture capital fund for micro, small and mediumscale enterprises)
Belize	✍ Commercial Banks (4) ✍ Credit Unions (10) ✍ Thrift and Finance Companies (NA) ✍ NGOs (4)	✍ National Development Foundation of Belize (NGO)
Guyana	✍ Commercial Banks (6) ✍ Development Banks (2) ✍ Credit Unions (80 est.) ✍ NGOs (3)	✍ Institute of Private Enterprise Development/IPED (NGO) ✍ Scotia Enterprise/Bank of Nova Scotia (Commercial bank) ✍ Cooperation of Development (NGO, local affiliate of parent UK NGO)
Jamaica	✍ Commercial Banks(4) ✍ Development Banks (2) ✍ Merchant Banks (20) ✍ Credit Unions (66) ✍ Building Societies (5) ✍ NGOs (3)	✍ National Development Fund of Jamaica (NGO) ✍ Worker's Bank[1] (Commercial bank) ✍ Cope (NGO)
Trinidad and Tobago	✍ Commercial Banks (5 total, with 2 foreign owned) ✍ Finance Companies and Merchant Banks (9) ✍ Credit unions (398 – but only 163 active) ✍ Development Finance Institutions (3)[2] ✍ Thrift Institutions: Post Office Saving Bank (1) and Building Societies (3)	✍ FUNDAID (NGO)

1. Worker's Bank in Jamaica was intervened in 1998/9. The microfinance portfolio has been absorbed by Union Bank, a new bank based on the acquired assets of several failed banks. Union Bank intends to sell the microfinance portfolio to a Building Society.
2. In Trinidad, FUNDAID, Agricultural Development Bank (ADB), and Small Business Development Company (SBDC) are characterized as development finance institutions. Their ownership structures are different but the mission is the same. ADB is government-owned, SBDC is mixed public-private guarantee fund, and FUNDAID is a private NGO but almost 100% dependent on national government funding.

Sources: DeMontfort University. 1997; Sobotka and Holden. 1998; Tewarie, Bhoendradatt. 1998.
Caribbean Centre for Monetary Studies. 1998. Zepirin and Russell. 1999. IDB Trinidad and Tobago: Diagnostic Study . 1999.

An efficient, productive and sustainable microfinance industry with significant outreach to the poor has not yet been built in the Caribbean. Generally speaking, existing Anglophone Caribbean microfinance organizations (MFOs) are more likely than their counterparts in Latin America to suffer from lower staff productivity, higher delinquency, less profitability and lower rates of cost recovery. For example, the average delinquency rate for the eight Caribbean MFOs examined in this paper (representing some of the larger and more established institutions in the region) is 43.4%, compared to 5.1% for a peer group of seven small but well-performing MFOs in Latin America (See table 3). Likewise, the operating expenses per loan is $450 for Caribbean MFOs compared to $91 for Latin MFOs, demonstrating the higher level of efficiency generally attained in Latin America. [5] One exception in the Caribbean is AAMM in Jamaica. In 1998, it posted a return on equity of 19.2%, had a 30-day delinquency rate of 8.7%, and its operating expenses were only $134 per loan (See Annex 1b). This institution, however, is predominately involved in consumer finance.

Table 3: Comparison of Latin and Caribbean MFOs

1998	Latin MFOs (Average)	Caribbean MFOs (Average)
CHARACTERISTICS		
Gross Loan Portfolio (US$ thousands)	$3,551	$2,127
Number of Loans	15,370	1,349
Average Loan Balance	$331	$2,805
Avg loan/GDP per capita	0.39	2.50
PROFITABILITY		
Return on Average Equity	21.0%	4.3%
ASSET QUALITY		
Loans > 30 days past due (% of Total Assets)	5.1%	43.4%
Loan Loss Reserves / Loan 30 > days past due	96.9%	27.9%
CAPITAL		
Debt/ Equity	0.7	1.1
EFFICIENCY AND PRODUCTIVITY		
Operating Expenses/Average Gross portfolio	42.8%	16.6%
Operating Expenses/# of Loans Outstanding	$91	$451
Loans per Credit Officer	273.9	202.5
GROWTH (1997-98)		
Gross Portfolio, in US Dollars	27.9%	17.4%
INTEREST RATE CHARGED BY MFO		
Weighted Average Real Interest Rate	37.5%	25.5%

*Unweighted average. Latin American peer group consists of 7 small but well-performing MFIs: Women's World Bank-Cali in Colombia, FUNADEH in Honduras, FINCA, FAMA and Chispa in Nicaragua, Compartamos in Mexico, and FED in Ecuador.
**Unweighted average. Caribbean case studies included COPE and Self Start in Jamaica, FUNDAID in Trinidad & Tobago, AAMM in Jamaica, IPED and Globe Trust in Guyana, and St. Martin's and NDF in Belize.
Source: Microrate.

[5] This figure suggests higher efficiency in Latin America once average loan size is controlled for. Because of the higher average loan size in the Caribbean, operating expenses are actually lower in the Caribbean than in Latin America when measured in relation to gross portfolio.

Furthermore, Caribbean MFOs are more likely to have slow rates of portfolio growth and depend on donor funding, and the microfinance industry in these countries is more likely to be dominated by one or two players. This lack of competition has two consequences:

It contributes to more selective lending. The average loan size for Caribbean MFOs is $2,805, compared to $331 for the Latin American peer group. Even taking into account the higher per capita GDP of the Caribbean countries[6], it is still clear that the clients of these MFOs are from a considerably wealthier stratum of society than those in Latin America.

It does not encourage MFOs to recover their delinquent loans or to compete for new customers. This is seen in the vast difference in delinquency rates between Caribbean and Latin American MFOs (described above), as well as their slower growth rates. The Latin American peer group saw average annual portfolio growth rates of 27.9% from 1997-1998, while their Caribbean counterparts averaged only 17.4% growth during the same period.

Parallelling, and perhaps helping to explain their generally lower level of performance, the Caribbean MFOs are older and perhaps more stagnant than their Latin counterparts. For example, the National Development Foundation of Jamaica, the National Development Foundation of Belize, and FUNDAID of Trinidad were founded in the late 1970s and 1980s, while Women's World Bank of Cali, FINCA Nicaragua, and Compartamos-Mexico were founded in the 1980s and early 1990s[7]. The slower growth and lower performance of the Caribbean MFOs, furthermore, seems to be due to internal factors and not external economic factors. In general, the economies of the Anglophone Caribbean in the 1980s and 1990s have performed better than the economies in which the peer group institutions operate, namely Colombia, Nicaragua, Honduras, Mexico, and Ecuador.

III. MAIN FACTORS EXPLAINING THE DIFFERENCES IN THE DEVELOPMENT OF SUSTAINABLE MICROFINANCE IN THE ANGLOPHONE CARIBBEAN COMPARED TO LATIN AMERICA

Examining why a certain industry has flourished more in one region than another always involves analyzing many variables. In the case of microfinance, the explanatory factors range from economic to regulatory to political and cultural. Nonetheless, it is possible to identify a number of factors that seem to be particularly important in explaining the major differences between Latin America and the Anglophone Caribbean. Namely, the smaller and more concentrated financial markets, the greater degree of macroeconomic stability, their lower rates of poverty and superior standard of living, as well as the prevalence of inappropriate lending technologies, are crucial factors in determining the major constraints to growth of the microfinance sector.

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[6] The average loan size per one dollar of per capita GDP is $2.50 in the Caribbean versus $0.39 in Latin America.

[7] FUNDAID was founded in 1973 while NDFJ and NDFB were both founded in 1984. In comparison, WWB-Cali was founded in 1982 while FAMA, FINCA Nicaragua and Compartamos were all founded in 1991. Source: "Review and Analysis of MicroFinance in the Caribbean" 1998 and "La Industria de Financiamiento a la Micro y Pequeña Empresa en Nicaragua¨, and IDB staff consultations.

One would expect that differences in the financial regulatory regime would be a main factor in explaining differences in density and performance of MFOs. This is not the case in the Caribbean. Many of the financial regulations that most affect the sector are less hostile than in Latin America. Like many regions of the world, the Anglophone Caribbean is marked by a regulatory system (direct business rules for small and micro entrepreneurs (SME) and financial rules for intermediaries that serve small and micro entrepreneurs) that does not always work to the benefit of the SME sector. This is a complex issue that could be the topic of a separate study; however, it is useful to include a brief summary of the financial regulatory environment and how it measures up to Latin America. Using four areas of financial regulations as guidelines (entry requirements, provisioning, documentation requirements, and interest rate restrictions) and evaluating the four countries (Belize, Barbados, Guyana and Trinidad and Tobago) for which data exist on this topic, it becomes clear that the regulatory attitude towards SMEs in Caribbean countries can be characterized as "somewhat benign neglect."

The entry barriers, specifically minimum capital requirements for the constitution of banks and finance companies, in the Caribbean are slightly lower than in Latin America. For example, Belize and Trinidad and Tobago have some of the lowest requirements in the entire Western Hemisphere. At the same time, however, innovative responses to the needs of MFOs, such as using portfolio assets as initial capital or creating new institutional forms designed specifically for microfinance, have not been seen in the Caribbean as they have in Latin America. Similarly, loan loss provision regulations in the Caribbean, which are meant to reflect the value of an MFO's portfolio at risk, are comparable to Latin America; yet unlike Paraguay, Costa Rica and Bolivia, there are no examples of Caribbean countries introducing special provisioning schedules designed for microloans. As far as interest rate ceilings are concerned, financial institutions in the Caribbean are generally more free than in Latin America to charge market interest rates, which is beneficial to MFOs since they can offset the high expenses of microlending. Some countries such as Jamaica have published interest rate ceilings, but small loans are exempted from the stricture.[8] Documentation requirements are similarly less of a hindrance in the Caribbean; but again, unlike countries such as Bolivia and Paraguay, the special needs of MSEs have not been considered, and there are no instances of more flexible rules in this regard for small borrowers in the Caribbean.[9]

Even in cases in which the standard measures of financial regulation are more liberal in the Caribbean than in Latin America, the benefits of this are only partially felt by the MSE sector because their specific needs are not being addressed. The existence of a financial regulatory framework that takes these specific needs into account is a direct function of a critical mass of well-performing MFOs that can serve as effective lobbyists for change. Thus it is not surprising that we see such tailor-made regulations in Bolivia and Peru, but not in Barbados or Trinidad and Tobago.

Even more important than specific policy reforms, however, is a change in the governmental policy of subsidized credit. In general, governments in the Caribbean view the microenterprise sector as needing and deserving of help, and so tend to rely more heavily on subsidized credit

[8] Interview with Maureen Webber, Development Options Ltd.

[9] Jansson, Tor, and Mark Wenner. Financial Regulation and its Significance for Microfinance in Latin America and the Caribbean. Inter-American Development Bank, 1997

programs. This tendency will be analyzed more fully later in this work, but it is important to mention in the context of the legal and regulatory reform. Before Caribbean governments address specific reforms of their regulatory framework, the attitude towards the sector, and the subsidized policies that accompany this attitude, should change so that commercially sustainable MFOs can charge interest rates that reflect the cost of their operations without having to face unfair competition from subsidized MFOs.

The critical factors that seem relevant in explaining the differences observed in microfinance experiences between the Caribbean and Latin America are described below.

A. Small, Concentrated Financial Markets and Greater Macroeconomic Stability

Microfinance seems to thrive in economies that have relatively large financial markets and have a history of macroeconomic and financial crises. The large size of the financial markets in Latin markets makes the appearance of banking oligopolies more difficult, and the higher degree of past volatility has contributed to the growth of large informal sectors, created stimuli for financial product innovation, and accustomed clients to high nominal interest rates. The countries of the Anglophone Caribbean do not fit this pattern, and thus they have had less impetus to experiment and innovate in microfinance.

As seen in Table 4, financial markets in the Anglophone Caribbean tend to be smaller (as seen by the nominal size of the financial markets), but deeper (as seen by the ratio of total domestic credit to GDP) and more concentrated (as seen by the greater share of total assets owned by the largest banks).

Despite the fact that financial markets in the Anglophone Caribbean tend to be relatively small in terms of total nominal assets (as would be expected given the size of their economies), the Caribbean markets have a higher average level of financial depth as measured by the domestic credit provided by the banking sector, relative to GDP: 40% vs. 30% (See Table 4). And despite their greater depth, the structure of the financial sector in many countries in the Caribbean tends to be less competitive. A few dominant banks hold a disproportionate share of assets in their respective markets, and competition tends to be based on service rather than interest rate pricing.[10] While the entry of foreign-owned banks in Latin America in the last decade has triggered banking mergers among nationally-owned banks and in some cases forced nationally owned banks to move "down market" into consumer and microfinance, this phenomenon has not occurred in the Caribbean. Foreign-owned banks have been present and dominant in the Caribbean since the early days of independence, and there are no strong market forces driving banks to seek new market niches.

[10] DeMontfort University, 1998

Table 4: Financial Depth, Breadth, and Market Concentration in Selected Caribbean and Latin American Financial Markets

Country	Domestic Credit (in millions of US$)	Domestic Credit/ GDP	Total assets of commercial banks (in millions of US$)	Percent of total assets owned by 3 largest commercial banks
Caribbean				
Bahamas	3,809.2	70.6%	21,519	39%
Barbados	1,618.95	54.8%	2,119	70%
Belize	391.215	48.1%	1,626	100%
Guyana	684.0055	19.5%	2,051	100%
Jamaica	3,025.527	28.3%	10,293	59%
Suriname	152.398	21%	4,028	91%
Trinidad & Tobago	2,647.182	38.6%	7,272	55%
Average for Caribbean	1,761	40.12%	6,987	74%
Bolivia	5,493.656	53%	24,278	65%
Colombia	33,592.65	22.9%	212,364	42%
Dominican Republic	6,339.797	19.7%	44,349	80%
El Salvador	5,427.886	41.5%	22,011	75%
Peru	13,779.2	14.1%	120,176	38%
Average for Selected Latin Countries	12,926.63	30.24%	84,635	60%

Source: International Financial Statistics July 2000 and Bankscope (financial data service produced by Bureau van Dijk).
Note: * There are four commercial banks in Guyana but data were only reported for three.

Another major difference in the structure and operation of financial markets between the two regions is the tendency towards more macroeconomic volatility and financial crises in Latin America. In the 1990s, for example, there were nine episodes of severe financial market stress or full blown crises in Latin countries, compared to one in the Caribbean.[13] Likewise, the Latin American countries have been more prone to massive currency devaluations and fiscal indiscipline (higher public deficits as a percent of GDP). These two tendencies have translated in the past into increased inflationary pressures and have resulted in tight monetary policies, which in turn have led to high real lending interest rates.

Against this backdrop of higher financial sector fragility and volatility and greater levels of bank competition, Latin American financial institutions have emerged in the last 10-15 years and sought out clients in the microenterprise sector. Some commercial banks felt obliged to search out new market niches in order to manage the intense competition. Sometimes, these commercial banks would retreat from the microfinance sector during cyclical downturns in the economy. However, the density of the microenterprise market coupled with wider availability of sustained technical assistance and the successful transfer of appropriate technologies permitted a

[11] Bankscope, 2000
[12] DeMontfort University, 1998
[13] The episodes of financial market stress occurred in Mexico (1994-95), Paraguay (1995-98), Venezuela (1994-present), Dominican Republic (1991), Ecuador (1999), El Salvador (1997), Costa Rica (1994), Argentina (1995-97), Bolivia (1995-present) and Jamaica (1997-8).

number of specialized microcredit institutions to emerge and survive despite the difficult economic circumstances. Some of the most promising institutions have been able to refine lending methodologies, and are transforming themselves into regulated financial entities so as to capture savings from the public and assure themselves of lower cost sources of funds for on-lending (See Table 5).[14]

Table 5: Selected Population and Macroeconomic Indicators

Countries	Population 1998 (millions)	GDP Per Capita 1998 (US$)	GDP Growth Rate (1990-98)	Average Annual Inflation Rate (1990-98)	Average Bank Lending Rate (1999)
Caribbean					
Bahamas	.3	12,400	.8 %	2.9%	6.38%
Barbados	.26	6,610	.7%	2.4%	9.25%
Belize	.24	2,660	3.5%	3.1%	16.27%
Guyana	.85	780	9.8%	16%	17.11%
Jamaica	2.6	1,740	1.5%	29.1%	27.01%
Suriname	.44	1,660	.8%	138%	27.75 %
Trinidad & Tobago	1.3	4,520	2.8%	6.9%	17.33%
Average for Caribbean Member Countries	.855	4,338.57	2.84%	28.34%	17.3%
Selected Latin Countries					
Bolivia	7.9	1,010	4.6%	9.9	35.37
Colombia	40.8	2,470	3.5%	21.5%	30.41
Dominican Republic	8.3	1,770	5.3%	10.6%	25.07
El Salvador	6.1	1,850	5.2%	8.9%	15.46
Nicaragua	4.8	370	3.8%	38.9%	22.15
Peru	24.8	2,440	5.8%	33.7%	30.80
Average for Selected Latin Countries	15.45	1,651	4.7%	20.58%	26.54%
Selected Asian Countries with Strong Rural Microfinance Sectors					
Bangladesh	125.6	350	4.9%	3.6%	14.13
Indonesia	203.6	640	4.1%	12.2%	27.66
Thailand	61.2	2,160	4.6%	4.8%	8.98
Average Asian Countries	130.13	1,050	4.5%	6.86%	16.92

Sources: IMF's International Financial Statistics, July 2000, United Nation's Human Development Report 2000. Inter-American Development Bank's Economic and Social Progress in Latin America: Facing Up to Inequality. 1998-99.

[14] Some of the "upgraded" or transformed NGOs in Latin America include: ADEMI-BancoAdemi in Dominican Republic, AMPES-Financiera Calpia in El Salvador; Prodem-BancoSol in Bolivia; Bangente in Venezuela, Caja Los Andes in Bolivia, and FIE in Bolivia. Some of the NGOs in process of transformation include Agrocapital in Bolivia, ADRI in Costa Rica, and Compartamos in Mexico. Some of these institutions however, have been multi-year recipients of high quality, intensive, external technical assistance: Financiera Calpiá and Caja Los Andes from IPC; Prodem and Compartamos from Accion Internacional; Agrocapital from ACDI/VOCA. In the Anglophone Caribbean there are few if any such examples.

It should be noted, however, that present macroeconomic stability is not a constraint on the development of an efficient microfinance sector; on the contrary, stability should provide a strong foundation for microfinance to flourish, while volatility tends to negatively affect both microenterprises and the institutions that serve them. Yet the *past* instability seen in Latin America, coupled with other factors such as a low rate of overall domestic credit, played a role in creating a favorable backdrop by increasing informal sector activity and creating the expectations of high and fluctuating interest rates.

B. Lower Rates of Poverty and Higher Savings Rates

Microfinance tends to thrive in countries with high rates of unemployment/underemployment, high rates of poverty, and high degrees of inequality in access to basic services and government transfer programs. The inability of the formal economy to generate a sufficient number of jobs to gainfully employ the economically active population at a living wage, creates long spells of unemployment for some and underemployment for many. In the absence of adequate social safety nets (unemployment compensation, welfare assistance, training programs, etc.), many of the unemployed have no choice but to pursue self-employment or wage employment in the informal economy. Countries that do not have extensive social safety nets, high expenditures on social services (health, education, and infrastructure), and solid macroeconomic management, tend to be poorer and more unequal. High rates of unemployment coupled with high rates of poverty create the conditions for a large and thriving microenterprise sector. The larger and more dense the microenterprise sector, the more likely it is that viable microfinance institutions will appear. The Caribbean does not fit this pattern, as can be seen in Tables 5 and 6. For example, El Salvador reports 397,500 active microenterprises, or 6725 microenterprises per 100,000 inhabitants, Nicaragua reports between 400,000 and 500,000, or approximately 11,494 microenterprises per 100,000 inhabitants, and Honduras reports 200,000 microenterprises, or 3,257 microenterprises per 100,000. In comparison, Guyana reports 22,000 or 2,588 microenterprises per 100,000 and Jamaica 100,000 microenterprises, or 3921 microenterprises per 100,000.[15]

The Anglophone Caribbean has much higher levels of socio-economic development compared to the Latin American comparator countries (all known for having strong microfinance industries). As can be seen in Table 6, the Caribbean has higher rates of open unemployment but lower poverty rates than selected Latin American countries with strong microfinance institutions.[16]

[15] Findley, Andrea. Katalysis Partnership, DEVFINANCE Posting September 19, 2000

[16] In developing countries, it is quite common for persons educated at the secondary and tertiary level to experience higher relative rates of unemployment than persons with primary education. Thus, countries with relatively highly educated populations tend to record higher rates of open unemployment. Also at work is the definition of employment and how employment/unemployment statistics are captured. In higher income countries more frequent surveys and higher degrees of coverage in social security systems tends to yield more reliable statistics. Poorer countries may report lower open unemployment figures but tend to have much higher rates of discouraged workers, persons who have stopped actively seeking work, and higher rates of underemployment, persons who are employed but desire longer hours or more productive, challenging jobs. Thus, lower-income countries may report lower open rates of unemployment due to unreliable measurement and the urgency to be employed in some fashion. Source: World Development Indicators 2000, pp. 54-57.

As can be seen on the right hand side of Table 6, the Anglophone Caribbean scores higher on United Nations compiled indices for Human Development (HDI) and Human Poverty (HPI) than the Latin America comparator countries. On the HDI, a composite measure of life expectancy at birth, adult literacy rate, combined school enrollment at primary, secondary, and tertiary levels, and GDP per capita in purchasing power parity, only two of the six Latin countries with strong microfinance sectors rank above the lowest two Anglophone Caribbean countries. On the HPI, which incorporates measures of economic deprivation and exclusion, (for example, share of income of the richest 20 percent in relation to the poorest 20 percent), percentage of underweight children less than five years old, level of access to health services, and level of access to safe drinking water, all the Caribbean countries for which complete data exist outrank the countries in Latin America and Asia with strong microfinance institutions.

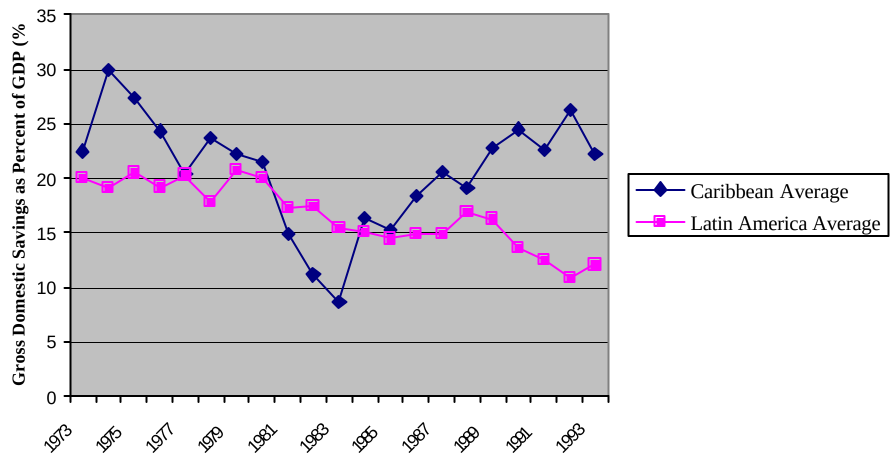
Table 6: Unemployment and Poverty Rates, and Socioeconomic Indicators of Development

Countries	Unemploy-ment Rate % (1993-1998 Average)[a]	Population Below the National Poverty Line % 1987-1997	Human Development Index (HDI) 1998 Rank[b]	Human Poverty Index (HPI-1) 1998 Rank[c]
Caribbean				
Bahamas	11.72	NA	33	NA
Barbados	18.11	NA	30	NA
Belize	10.45	NA	58	NA
Guyana	NA	NA	96	10
Jamaica	15.91	34.2	83	16
Suriname	11.7	NA	67	NA
Trinidad & Tobago	16.81	21	50	5
Average for Caribbean Member Countries	14.12	27.6	59.6	10
Selected Latin Countries				
Bolivia	4.3	NA	114	27
Colombia	8.03	17.7	68	NA
Dominican Republic	16.88	20.6	87	20
El Salvador	8.2	48.3	104	34
Nicaragua	14.6	50.3	116	41
Peru	8.05	49.0	80	25
Average for Selected Latin Countries	10.01	37.18	81.29	29.4
Selected Asian Countries with Strong Rural Microfinance Sectors				
Bangladesh	NA	NA	NA	70
Indonesia	NA	NA	NA	46
Thailand	NA	NA	NA	29
Average Asian Countries	NA	NA	NA	48.3

a Most recent years available used.
b A ranking of 1 on the HDI scale signifies the highest level of human development
c A ranking of 1 on the HPI scale signifies the lowest level of human poverty
Note: Anglophone states have more reliable sources of capturing employment/unemployment status. This may help explain the higher levels of reported open unemployment. Another factor are varying definitions of employment and unemployment used.
Source: International Financial Statistics, July 2000, and Human Development Report 2000.

In summary, while the Anglophone Caribbean may have a large self-employed and micro-enterprise sector, the lesser degree of poverty does not create the same sense of urgency to access credit at all costs that may exist in the comparator countries. The Caribbean microfinance clientele has more options. Given the generally higher levels of income and wealth, there are more opportunities for self-financing through savings, and informal financing from family and friends. For example, the higher penetration of credit unions, and the larger relative number of thrift institutions (Building Societies, Postal Savings systems, and trust companies) in the English speaking Caribbean compared to Latin America can be used as a proxy to indicate that low and moderate income persons tend to hold more saving accounts. As can be seen in Figure 1, the seven Anglophone Caribbean states have on average a higher level of domestic savings compared to five selected Latin American countries with strong microfinance sectors (20% vs 16%) - (See figure 1).

Figure 1: Gross Domestic Savings Rates for Latin America and the Caribbean



C. Inappropriate Credit Technologies and Interest Rate Policies

Caribbean MFOs, as a rule, tend to use traditional asset-based lending methodologies and charge low interest rates.[17] In comparison, Latin American MFOs tend to use character-based lending methodologies and charge high interest rates. These two characteristics help to explain slow growth in MFO portfolios and the paucity of financially sustainable MFOs in the Caribbean.

Inappropriate Credit Technologies: Caribbean MFOs tend to manage credit risk through the threat of foreclosure on fixed collateral rather than through a careful analysis of the client's character, quality of management, financial strength, and willingness and ability to build and maintain a long-term lending relationship. As a result, the loan evaluation process in Caribbean MFOs tends to generate high levels of transaction costs due to the need to have "proper legal

[17] Some exceptions to the rule are the Caribbean Microfinance Ltd. in Trinidad and Tobago, Scotia Enterprises in Guyana, and the groups affiliated to Development Options in Jamaica, an apex for the Government of the Netherlands/Government of Jamaica Microfinance Line of Credit operation.

documentation," in the belief that a well documented loan is a sound one. While "character-based" lending methodologies are not prohibited under most existing regulatory regimes in the Caribbean, the larger the financial institution, the greater the tendency to follow prevailing guidelines concerning collateralization and documentation for small and micro business loans. The exception is consumer lending, which is targeted largely to salaried workers.

In contrast, many Latin American MFOs have less stringent fixed collateral requirements – or none at all - and depend more on alternative collateral (moveable) and repayment incentives (graduated lending or interest rate rebates for prompt payment). Clients tend to "prove" themselves creditworthy through a series of ever-increasing small loans. As the loan size increases, more collateral may be required; but if the client uses the initial loan productively, then a rise in income will permit the use of more collateral. In essence, credit risk in Latin America is managed through a "termination threat": given the difficulty small and micro entrepreneurs have in accessing formal credit in most developing countries, Latin MFOs in effect threaten to close access to credit to clients who default, and project a tough image simply by monitoring delinquency closely. Caribbean MFOs' heavy reliance on asset-based lending or "threat to foreclose" technology is inappropriate because low-income, small and micro entrepreneurs by definition have limited amounts of fixed collateral. As can be seen in Annex I, the ratio of average loan size to per capita GDP for seven of the eight Caribbean MFOs studied (excluding Globe Trust of Guyana, which has an extremely high average loan size) was 0.63, compared to 0.39 for Latin MFOs, suggesting that Caribbean MFOs are not reaching the poor to the same degree as their Latin counterparts. If Globe Trust is included, the mean for the Caribbean MFOs is skewed up to 2.5.

Low Interest Rate Policies: Caribbean financial systems have been characterized by historically stable and low interest rates (See Table 5). Because of this fact, Caribbean MFOs feel socially obliged to charge rates that are not perceived as "usurious". Both the nominal and real interest rates charged to clients are much lower than the averages in Latin American comparator institutions, often at the expense of sustainable operations or cost recovery (See Table 3 and Annex 1). While this results in cheaper funds for microentrepreneurs, it has many negative side effects: namely, a reduced ability to expand and offer more credit to more microentrepreneurs; and, related to this, a rationing of credit. Without the growth that comes with more complete cost recovery, these MFOs continue to maintain a small client base, and the credit tends to gravitate towards a relatively wealthy group of individuals with superior collateral, information, and connections.

The reasons for this tendency to charge low interest rates are twofold: first, it is due in part to a historical view of the microenterprise sector as needing and deserving of help in the form of subsidized credit; and second, it is due to the competition from government-sponsored credit schemes which subsidize their interest rates in the name of correcting market imperfections.
Second-tier institutions and national development banks have been the favored vehicle for channeling small and micro business loans in the Caribbean. Yet these institutions have been characterized by inefficiency, poor outreach (loaning a small amount – in terms of gross portfolio size - to a mostly non-poor client base), difficulty in recovering loans, and a tendency to undercut the microfinance industry by fixing loans at below-market rates. Several case studies in the region illustrate these points:

In Jamaica, the National Development Bank initiated the Interest Rebate Programme, by which the NDF subsidized loans to retail organizations and fixed the interest rate to the final borrower at 17%, as opposed to the normal market rate of approximately 26%. This subsidized program failed to attract borrowers despite the low interest rates, largely because of the extremely large size of loans offered (the average loan size in 1996 was $74,000) and the stringent criteria that included maximum debt/equity levels, finance and marketing plans, and regulatory requirements. In addition to these issues, the approval process was reported to be overly prolonged, requiring two separate approval processes. The result was that "the NDB [had] a client focus on the small to medium firm and that the micro sector would . . . have to find alternative sources." [18] MIDA, an APEX institution established for microlending, had a similar experience.

In Trinidad and Tobago, a number of governmental programs, notably the Small Business Development Company Limited (SBDC) and the Agricultural Development Bank (ADB) have had serious institutional difficulties ranging from large operating losses to high delinquency. The IDB judged in 1997 that in the case of the SBDC, "because of the under-pricing of risk and a high default rate, the program is financially unsustainable" and "judged the impact of the program to be minor."[20] In sum, these programs were inefficient and unprofitable, and at the same time undercut any attempts at market pricing of microcredit, thereby precluding the growth of a sustainable microcredit industry.

In Barbados, the Barbados Development Bank, which had been involved in micro and small lending, was forced to cease lending in 1995 "as a result of insolvency."[21]

Paradoxically, the same pattern can be detected in several middle-income Latin American countries (Brazil, Mexico, Venezuela, Argentina, Uruguay, Costa Rica, and Chile). In these countries, many policymakers still adhere to the notion that subsidized interest rates are necessary to help the poor, and these governments have more fiscal capacity to continue to fund these types of microcredit programs. The presence of subsidized programs and large state-owned development banks hinders the development of sustainable, commercially oriented programs. Many aspiring microcredit NGOs, short of loanable funds, align themselves with government programs and become dependent on external funds

The presence of widespread subsidized interest rate programs, and the corresponding lack of consensus between donor agencies and national governments, is probably the single most important reason why commercial microfinance in the Anglophone Caribbean has developed at such a different pace than many Latin American countries.

[18] IDB, "Diagnostic of the Micro and Small/Medium Sized Enterprises in Jamaica," 1997: p. 78
[19] IDB, "Barbados: A Diagnostic of the Financial System, p. vi
[20] IDB, "Trinidad & Tobago: A Diagnostic of the Financial System, p. 29-31
[21] IDB, "Barbados: A Diagnostic of the Financial System, p. vi

IV. BANK SUPPORT FOR MICROENTERPRISES AND MICROFINANCE IN THE CARIBBEAN

A. Level and Nature of Bank Support

In the last fifteen years the Inter-American Development Bank (IDB) has approved 21 microenterprise projects with a total value of US$9.9 million for the Anglophone Caribbean (See Table 7 and Annex 2). As of February 2001, three projects are pending approval with a value of US$6.6 million. The value of approved Anglophone Caribbean projects to date is approximately 1.3% of the total value of microenterprise projects approved for the period 1985-1999 ($787.8 million).

The Microenterprise Strategy approved by the Bank management in 1997 calls for concerted action to "promote the conditions necessary for the growth and development of the microenterprise sector in the region: a favorable policy and regulatory environment; strong, sustainable institutions providing financial and nonfinancial services to meet the demand of microenterprises; and expanded, continuous and permanent flows of resources for investment in microenterprise." In the case of the Caribbean, although the provision of non-financial services is equally important in the development of a thriving microenterprise sector, the majority of Bank resources has supported the provision of financial services for small and microentrepreneurs.

Table 7: Summary of IDB Support for Microenterprise in the Anglophone Caribbean

	Small Project or Social Entrepreneur-ship Program	Multilateral Investment Fund	Technical Cooperations	Total
1985-1989				
Number of Projects	6	0	0	6
Amount (US$)	2,200,000			2,200,000
1990-1994				
Number of Projects	3	1	0	4
Amount (US$)	1,500,000	1,900,000		3,400,000
1995-1999				
Number of Projects	2	4	2	8
Amount (US$)	100,000	3,652,396	180,000	3,932,396
2000*				
Number of Projects	0	1	2	3
Amount (US$)		300,000	100,000	400,000
Total Number of Projects	**11**	**6**	**4**	**21**
Total (US$)	**3,800,000**	**5,852,396**	**280,000**	**9,932,396**

Up to September 2000.
Source: IDB's Microenterprise Unit and Regional Operational Department 3 Databases.

The two most commonly approved types of projects were Small Projects (SP), low-interest loans aimed at establishing revolving credit funds, and non-reimbursable Technical Cooperation (TC) programs, or grants for technical assistance. Small Projects usually involved the establishment of revolving credit funds, and Technical Cooperations usually involved assistance in improving management and service delivery capacity in a beneficiary institution. In terms of geographical distribution of resources, the larger Anglophone Caribbean member states, Jamaica, Guyana, and Trinidad and Tobago, tended to receive more financing for microenterprise development than the smaller Caribbean member countries. The least common type of operation, but the largest in terms of total funds commited, were Multilateral Investment Fund operations involving non-reimbursable funds for institutional strengthening and reform.

The relatively low amount of approvals is due to a combination of factors: (1) a smaller microenterprise sector compared to most Latin American countries; (2) a paucity of able, market-oriented intermediaries; and (3) unfruitful dialogues with member governments about improving the policy environment for microenterprise development, and with practitioners concerning interest rate policies. As a result of the unattractive prospects to develop viable microenterprise projects, the Bank has tended to allocate much more staff resources to the design and preparation of projects in Latin American countries than in the Caribbean.

B. Common Project Results Obtained

In reviewing the types of projects approved, the interventions can be categorized in three groups. First, three projects were aimed at strengthening and modernizing credit union federations; these included three large projects (in The Bahamas, Jamaica, and Trinidad and Tobago) that used the resources of the Multilateral Investment Fund, as well as two projects (in Guyana and Suriname) that used Trust Funds for technical assistance grants. Second, a number of Small Projects sought to establish revolving credit funds and to subsequently extend the supply of credit for a target group. The notable examples are FUNDAID in Trinidad and Tobago, National Development Foundation in Belize, BEST in Belize, and National Development Foundation of Jamaica. The last type of intervention involved capacity building and the introduction or promotion of non-financial services. The examples are the National Centre for Persons with Disabilities in Trinidad and Tobago, the Black Belly Sheep project in Barbados, specifically improving feedlot operations and livestock marketing, and the introduction of a pilot voucher program for business development services in Guyana.

1. Lessons: Credit Union Projects

The five credit union projects have had a very mixed record. The larger projects in Jamaica, the Bahamas, and Trinidad and Tobago experienced severe start-up problems. Some of the problems stemmed from delays in the contracting of consultants (as in the Bahamas); other problems were due to resistance from Credit Union League officials fearing loss of power (as in Jamaica); still other problems stemmed from a dispute between the Central Bank and the Ministries of Finance and Labor (in the case of Trinidad and Tobago) over ownership and supervision of the project. In all three cases, the delays robbed the projects of their momentum. In contrast, the two small credit projects in Guyana and Suriname, which had better execution records and work plans to improve accounting systems and train staff, proceeded without major problems.

Below are some highlights of the progress and challenges faced in the credit union projects:

- Despite early execution problems in the larger credit union strengthening projects in Jamaica and Trinidad and Tobago, important progress has been made of late in training, reformulating bylaws and operating procedures, and improving financial management.
- In the Bahamas, the project has started training Boards of Directors and undertaking market studies with the aim of designing new products.
- Likewise, the smaller projects in Guyana and Suriname have succeeded in improving the internal functioning of three individual credit unions. The credit unions in Suriname improved accounting and management information systems, trained staff, conducted marketing studies, and developed business plans that have resulted in increases in membership, savings mobilization, and a decrease in delinquency. Microenterprise lending, however, is still a small part of the portfolio of the two Surinamese credit unions, and has decreased over time due to a high-risk external environment (high inflation).
- No impact information is available for the New Amsterdam Credit Union project in Guyana.

The main lesson to be learned is that it is better to work with individual credit unions that are open to reform than with federations. Engineering institutional change is very time-consuming and labor-intensive, even in the best of circumstances. Significant investments over a long period of time will be needed to reform credit union federations, because “buy-in” is needed at three levels: the general membership, the board of directors, and the management team. Because of the larger number of stakeholders in federation credit union projects, it is often difficult to arrive at consensus and obtain positive financial results in the typical 3-4 year execution period. One of the main obstacles to institutional reengineering, whether in an individual credit union or a federation, is the dominance by persons with social charity perspectives and non-financial backgrounds on the boards of directors. Leadership with “traditional” views of credit unions tends to slow and undermine many of the proposed changes. Unless the leadership can become fully convinced, many of the reform efforts tend to be frustrated. With time and when the above conditions regarding “buy-in” are met, such reform can have important effects. For example, after six years in execution, some of the individual Jamaican credit unions are beginning to report improved financial performance.

A second main lesson is that a consensus is needed as to how and when to regulate credit unions. Self-regulation schemes have tended not to work worldwide. The alternative proposition to place credit unions under the Superintendent of Banking is often resisted by the superintendencies on cost-benefit grounds. Many superintendents believe that because credit unions represent such a small share of total assets in the financial system, it is not efficient to use scarce resources to supervise numerous, small institutions that do not represent a systemic risk to the entire financial system. Others, nonetheless, argue that superintendents have the responsibility of protecting all public deposits and that many savers, especially middle- and low-income ones, hold deposits in credit unions. Supporters of credit union supervision recommend that the full cost of supervision should be charged to small deposit-taking financial institutions in order to protect depositors. Still others argue that even will full pricing of supervision, the desired level of supervision quality and effectiveness may remain elusive. Many believe that the supervision of commercial banks has improved in recent years in Latin America and the Caribbean but still more improvement is needed. The added task of supervising small institutions may strain abilities to apply uniformly high standards, especially given that some modifications in supervisory techniques would be needed for non-banks. Though the debate continues, it is quite clear that without an appropriate legal framework and clear benchmarks towards which to strive, self-motivated credit unions may languish. The role of the IDB and other donors is not so much to spur credit union reform, but rather to help accelerate and consolidate such reform once strong leaders have emerged and governments are amenable to changing the legal framework.

Looking forward, the utility of pursuing a credit union-dependent strategy in the Caribbean may be questionable for two reasons. First, many of the dominant and well-performing credit unions in the Anglophone Caribbean are closed-bond and wage employee-based (Teachers, Hotel Workers, Police Force, Petroleum Workers etc.), unlike Latin America, where many strong credit unions are open and community based. These strong Caribbean credit unions are not likely to aggressively adopt microfinance technologies because the majority of their members are salaried employees and their "core business segments" — consumer and mortgage lending — are performing exceedingly well. Moreover, representatives of these strong credit unions dominate island-wide leagues and federations. When projects are structured to work through Credit Union Leagues to economize on transaction costs and improve scale of impact, these leaders tend to be the most resistant to change.

From the experience of other donors in other countries, namely in Guatemala and Ecuador, it is possible to have successful credit union rehabilitation projects; these successful projects, however, worked parallel to national federations with groups of individual credit unions committed to reform. Once success was demonstrated, the national federations became supportive.

Second, the majority of deposits in the Caribbean are captured by large commercial banks, especially foreign-owned ones, which are perceived to be extremely safe and sound. In the absence of deposit insurance schemes, albeit with their high costs and moral hazard issues, the amount of savings captured by the credit unions, even if they are convinced to adopt microcredit lending technologies, may not be sufficient to sustain a massive expansion of operations.[22]

[22] One exception is the Jamaican Credit Union League, which offers deposit insurance. The credit union movement in Jamaica mobilizes significant amounts of savings from low-income and moderate-income people compared to credit union movement in Trinidad &Tobago, The Bahamas, and Suriname.

2. Lessons: Revolving Credit Fund Projects

The four small projects allowed the beneficiary microfinance institutions to increase portfolio size.[23] However, the interventions, were not catalytic. Despite many years of existence, the institutions do not compare well with Latin American microfinance peers (see Annex I). Small projects can indeed help an institution; however, management ability, policy settings, and market conditions are the key factors in determining whether an increase in supply of credit will help the move towards sustainability and scale, or if it will simply lead to a temporary portfolio expansion. Furthermore, the lack of performance-based disbursement or repayment demands (the funds were non-reimbursable) may have contributed to the less stringent nature of these projects. As a result, these small credit operations do not seem to have played a catalytic role in building sustainable institutions. Two of the beneficiary organizations of the small projects, both NGOs, are either currently applying for additional IDB assistance or were recently granted additional assistance with the justification that the current leadership is now committed to adopting the “new style, commercially-oriented microfinance technology.”

3. Lessons: Non-Financial Services Projects

The most successful non-financial services project in the entire Caribbean, and one of the most noteworthy in both Latin America and the Caribbean, was a Small Project to the National Centre for Persons with Disabilities (NCPD) in Trinidad and Tobago. The NCPD is a private non-profit organization that provides rehabilitative and training services to disabled persons with the aim of better integrating them into the economic mainstream. NCPD received a Small Project in 1989 for a pilot small business development program. The program consisted of training disabled persons to run and operate businesses and to prepare for gainful employment. The goal of the training program is to permit the disabled persons to meet or surpass expectations of quality, skill or output demanded by open market competition. The program has been enormously successful in placing trainees/graduates and in increasing income-earning ability. The program has been recognized nationally and internationally, and has received several awards, including the IDB’s Award for Social Entrepreneurship in 1999. International organizations such as the International Labour Organization (ILO), the United Nations Development Program (UNDP), and the Organization of American States (OAS) have modeled programs in other English-speaking Caribbean after NCPD. The major achievement of NCPD has been to transform the view of disabled persons in Trinidadian society: rather than inconveniences that need to be removed from public view, the disabled are now seen as capable contributors to society. Originally, the pilot program included a credit component, but that component was discontinued due to repayment problems and high administrative cost issues. Since the mid-1990s, NCPD has focused solely on providing technical assistance and training services. The main challenge facing the institution is how to meet increased demand for services while maintaining quality in service provision and continuing to strive for financial sustainability. The maximum training capacity for NCPD has reached 150 trainees each six-month cycle.

[23] Impact information on Small Projects benefiting small farmer groups is generally not available. The reports that do exist for Magenta Ploder in Suriname, indicated that severe inflationary shocks undermined the project, that farmers switched from rice to vegetable production, and that the credit component was never implemented.

The two other non-financial projects are fairly new and in early phases of execution. Therefore, there is insufficient information to make an evaluation. The Guyana voucher program is in the process of contracting consultants, and the Black Belly Sheep project is in the process of drafting legal papers for the leasing of land upon which to build the feedlot. Overall, the emphasis of the IDB has been heavily skewed toward credit projects and the number of business development or non-financial services is not significant. In the future, the IDB may want to invest more heavily in this sector, given the more developed state of financial markets, higher levels of education, and the possibility of linking to vibrant tourism industries in some islands.

C. Strategic Interventions for Building Financial Retail Capacity

The interventions to pursue in the Anglophone Caribbean should be sequenced and focused largely on creating more favorable conditions for the development of efficient, competitive, and sustainable microfinance intermediaries. They are:

1. Lobby public sector policymakers, banking superintendents, and microfinance practitioners, with the goal of convincing them that liberalized and cost covering interest rate policies are feasible and represent the fundamental building block in creating viable and permanent microfinance institutions. This change of attitude is the first and most important step in improving microfinance retail capacity.
2. Improve the secured transactions framework so that more types of moveable collateral can be easily pledged as guarantees, and the cost of enforcing claims on such guarantees will be lowered.
3. Build and promote credit bureaus that have wider coverage, so that a demonstrated willingness to repay loans can be used as a justification for further credit. Improving the information available to lenders and creditors will in the end benefit responsible borrowers.
4. Promote relevant new financial products-- leasing, credit cards, and back-to-back letters of credit (subcontracting relationships)-- to take advantage of the more developed and stable formal financial markets in the subregion.
5. Initiate research on commercial bank and finance company downscaling in the subregion in order to better understand the process, as well as the steps that are needed to convince or entice such entities to enter this market during economic downturns..
6. Provide sustained and long-term technical assistance to the most promising existing microfinance institutions.
7. Where necessary and when a number of well-performing microfinance institutions exists, work with policymakers and banking superintendents to analyze the feasibility of allowing specialized but regulated microfinance organizations, probably with lower capital minimum requirements, such as has occurred in Bolivia and Peru.

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The pros and cons of each of the options are briefly discussed below.

1. *Lobby Policymakers, Banking Regulatory Authorities, and the Financial Community to Reform Interest Rate Policies*

The prevailing notion that low-income persons cannot and should not pay high rates of interest leads many of the region's governments to create and support subsidized interest rate programs that undermine efforts to create sustainable, efficient, and well-managed microfinance institutions. The education process will have to be undertaken at two levels: (1) directly communicating microfinance best practices via seminars, presentations by respected experts in the field, exchange visits to leading microfinance institutions in Latin America, and dissemination of technical reports and project evaluations; and (2) indirectly through better donor coordination. At present, the other leading donor agencies in the subregion are the European Union, United States Agency for International Development, the Government of the Netherlands, United Nations Development Programme, and the Prince of Wales Trust. Many of these donors have different approaches to microfinance, and the result is that mixed signals are sent to the governments and financial intermediaries in the subregion. The negative side of this proposal is that it may be difficult to secure interagency donor coordination; thus, governments in the subregion may choose to work with certain donors and not others.

2. *Secured Transactions Framework*

The ability to pledge moveable assets as surety, and to enforce such claims in a cost effective manner, needs careful review in many of the states in the subregion. Since, by definition, the poor do not have large amounts of high value fixed assets (especially titled land), substitutes must be found in order to reduce the exposure to default risk for prospective lenders. Two substitutes are moveable assets and improved information about the creditworthiness of prospective clients. In the Anglophone Caribbean, the English common law tradition favors the creditor in many respects, but the cost of enforcing claims, especially small valued transactions, can nonetheless be prohibitive. The establishment of Alternative Dispute Resolution (ADR) mechanisms or the establishment of special courts that can expedite small credit claims would represent an advance in lowering risk for financial intermediaries interested in or involved in microfinance.

3. *Credit Bureaus*

The promotion, strengthening, and creation of credit bureaus promises to help improve the flow of information regarding the capacity and willingness to repay on the part of prospective moderate and low-income clients. In order to start the process, actions by the state may be necessary to help standardize reporting norms, compel banks to report loan data, remove legal obstacles to the transfer of data to private credit bureaus, and give consumers an avenue to dispute alleged errors in credit reports. However, the initiative should be largely a private sector one and be run on a sustainable basis.

4. *New Financial Products*

Several of the countries in the Anglophone Caribbean, namely Trinidad and Tobago, Barbados, and the Bahamas, have stable financial markets, well-developed telecommunications infrastructure, and good macroeconomic management. In these countries, it may be advisable to promote the introduction of several financial products that have great potential for extending and deepening the microfinance market. For example, leasing can facilitate the purchase of capital goods that can be amortized over several years, and serve as a substitute for medium-term bank credit. Since the capital good will remain in the name of the financial intermediary (lessor), recovery of the good in the event of default is greatly facilitated, thereby greatly reducing risks to the creditor. The challenge will be clarifying tax issues and improving the functioning of insurance markets. Similarly, the promotion of credit and debit cards can reduce the transaction costs for both lenders and end users. The challenge will be to teach lenders how to evaluate self-employed clients who have variable cash flows. Lastly, back-to-back letters of credit can be promoted in subcontracting relationships in which a larger firm involved in export can issue a letter of credit to a small-sized supplier who can then use this instrument to access credit from a commercial bank. As assembly type manufacturing (*maquiladoras*) spreads throughout the region, this is one alternative that can be used to improve small firm access to financing.

5. *Initiate Research on Downscaling, and Engage in a Dialogue with Regulated Institutions*

Given the existing banking structure of the reviewed English-speaking economies, a spontaneous move towards microfinance is unlikely. No strong market forces exist that will force the management of commercial banks to penetrate the microfinance sector. Lack of familiarity, perceptions of high risk, regulatory norms, and acceptable rates of return in traditional markets will tend to impede a strong down-market move. Nonetheless, two exceptions exist.

First, one noteworthy experiment that should continue to be monitored and more widely publicized is the experience of Scotia Bank Enterprise in Guyana. If the leadership of Bank of Nova Scotia (BNS) can be convinced to expand this operation in Guyana, and replicate it in other countries as a profitable line of business (as opposed to pure public relations), then it may be possible to entice other commercial banks to follow suit. The appropriate role for the IDB and other donor organizations may be limited to providing consultancy services, disseminating knowledge, and moral suasion, rather than large lines of credit or guarantees. Second, finance or trust companies exist in several islands that are well performing and may be inclined to diversify from consumer to small and micro business lending. These financial entities may need to be more closely examined. The appropriate role for donor organizations may be to facilitate the transfer of appropriate technology and to emphasize small business lending first, followed by promotion of microlending technologies. Mandates and program guidelines that emphasize micro as opposed to small business lending, however, may have to be modified. Two promising examples of finance companies that may be persuaded to enter – or are already entering on their own - are Globe Trust in Guyana and Caribbean Microfinance Ltd., which is a subsidiary of Development Finance Ltd. in Trinidad and Tobago.

Another area of promise is research on how "downscalers" in Latin America and the Caribbean have penetrated this market, and what has been their record of financial performance. The emphasis should be on strategic motivations, the role of leadership, detailed cost accounting analysis of the microfinance product(s), and coping mechanisms in the event of economic downturns and other operational risks. The results should then be disseminated widely to the regulated entities, with the aim of convincing them that "downscaling" is a profitable proposition given committed leadership and appropriate technology.

6. Provide Sustained Technical Assistance to Promising Microfinance Institutions

A fundamental need in the Anglophone Caribbean is to highlight a "breakthrough case", an organization that demonstrates to other microfinance practitioners and to policymakers that commercially-oriented microfinance is feasible. In order to achieve this in Latin America, donor organizations cultivated long-lasting relationships with well-performing institutions in Latin America (such as Prodem in Bolivia, Compartamos in Mexico, or AMPES/Calpia in El Salvador). The first characteristic necessary to transform an MFO into a fully sustainable operation is an open, competent, dynamic leadership. The second characteristic is a board of directors committed to transforming the institution into a sustainable entity in the shortest period of time possible. Many of the microfinance projects in the Caribbean have involved sporadic assistance over time, or generalized access to a rediscount line of credit. The approach outlined above, in contrast, would involve "picking a winner" and investing heavily and effectively over a sustained period of time.

7. Upgrading Existing Microfinance Institutions to Regulated Institutions

Once a number of non-regulated, commercially-oriented microfinance institutions are performing well in the subregion, it may be advisable to analyze banking levels to see whether a space exists within the existing legal framework for the creation of a regulated, specialized microfinance entity. In many cases, this may require lowering the minimum capital requirement, restricting the number of products that can be offered, and exacting compliance with stricter capital adequacy ratios. The call to create yet more financial institutions, especially ones dedicated to high-risk microfinance, in the context of financial systems that are already quite deep, may seem counterintuitive. Yet it may be more feasible to build a sustainable microfinance institution from the bottom up than to try to reform existing state-sponsored institutions that are burdened with long histories of non-professional leadership, political interference, social charity perspectives, and excessive dependency on external subsidies. It may also be more feasible than enticing private commercial banks to "downscale". The "new regulated institutions" approach, however, would have to be conditioned on a number of requirements: the adequacy of the regulatory framework; the existence of talented people with strong backgrounds in finance and banking but also with a strong commitment to the small and microenterprise sector; and sufficient private investment to capitalize these institutions. In order to achieve economies of scale in relatively small financial markets, a regional MFO could also be considered.

V. CONCLUSIONS

Building a well functioning and sustainable microfinance industry in the Anglophone Caribbean will not be an easy task. Some institutions are beginning to adopt the new paradigm of commercially-oriented microfinance with cost covering interest rates and strict attention to delinquency control. However, there is much that still needs to be done. The immediate challenge is fourfold: how to improve knowledge of best practices in commercial microfinance; how to formulate and implement policy reform; how to obtain a break-through demonstration model; and how to introduce new financial products.

First, donors have to raise the level of understanding of what constitutes commercially-oriented microfinance: interest rates sufficiently high to cover operating expenses; design of appropriate loan and savings products; appropriate and effective loan evaluation procedures; reliance on character and moveable collateral; appropriate loan loss reserves; and strict delinquency control.

Second, national governments have to create favorable conditions for the emergence of private, commercially-oriented institutions. Donor organizations can play a vital role in better coordinating efforts, combating subsidized interest rate policies, and reforming the legal and regulatory frameworks that govern microfinance intermediation. National governments, in turn, need to strengthen credit bureaus and reform secured transaction frameworks as a means to help lenders rely less on fixed collateral as guarantees.

Third, donors and national governments have to convince managers of Caribbean microfinance institutions that commercial microfinance is feasible. Donors can help by supporting a handful of retail institutions that are committed to new-style commercial microfinance, and use these institutions as demonstration models. Exchange visits to successful Latin institutions can help to share knowledge and establish contacts, but are insufficient given the very different circumstances in the Anglophone Caribbean described earlier this paper. Caribbean practitioners may not be convinced until a few of their own institutions deliver first-rate outreach and financial results. In order to get such results, sustained performance-based support should be provided. This would imply greater emphasis on marketing studies to develop better products, larger investments in staff training, and greater monitoring and supervision on the part of donor organizations.

Fourth, the Anglophone Caribbean has a number of stable and well developed financial markets that can initiate pilot projects using new financial instruments aimed at small and microentrepreneurs. (for example, leasing, electronic cards, and back-to-back letters of credit in the context of subcontracting relationships). The challenge is to find the leadership and the vision in the financial sector to explore new niches. . Traditional microfinance was born and developed in poor and crisis-prone countries; modifications may be needed in middle-income subregions such as the Anglophone Caribbean.

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Annex 1a: Financial Indicators of Select Latin American MFOs

1998	L A 1	L A 2	L A 3	L A 4	L A 5	L A 6	L A 7	Latin MFOs
CHARACTERISTICS	**Colombia**	**Honduras**	**Nicaragua**	**Nicaragua**	**Nicaragua**	**Mexico**	**Ecuador**	**(Average)**
Gross Loan Portfolio (US$ thousands)	$8,640	$4,354	$935	$2,646	$1,869	$2,930	$3,481	$3,551
Number of Loans	18,812	10,268	11,864	5,036	6,610	43,401	11,596	15,370
Average Loan Balance	$459	$424	$79	$705	$283	$68	$300	$331
GDP per capita	$2,470	$730	$600	$600	$600	$3,970	$1,530	$1,500
Avg loan/GDP per capita	0.19	0.58	0.13	1.17	0.47	0.02	0.20	0.39
PROFITABILITY								
Return on Average Equity	17.5%	5.2%	17.9%	4.3%	15.8%	29.7%	56.8%	21.0%
ASSET QUALITY								
Loans > 30 days past due (% of Total Assets)	1.2%	13.0%	0.8%	2.7%	5.4%	6.0%	6.4%	5.1%
Loan Loss Reserves / Loan 30 > days past due	100.0%	51.3%	188.6%	72.1%	51.5%	103.6%	111.1%	96.9%
CAPITAL								
Debt/ Equity	1.5	0.1	0.9	0.5	0.8	0.1	0.8	0.7
EFFICIENCY AND PRODUCTIVITY								
Operating Expenses/Average Gross portfolio	15.2%	31.1%	51.0%	47.3%	46.0%	73.3%	36.0%	42.8%
Operating Expenses/# of Loans Outstanding	$70	$133	$37	$143	$116	$45	$90	$91
Loans per Credit Officer	537.5	197.5	312.2	83.9	227.9	374.1	184.1	273.9
GROWTH (1997-98)								
Gross Portfolio, in US Dollars	46.0%	48.6%	43.9%	-29.4%	61.8%	$0	-12.2%	27.9%
INTEREST RATE CHARGED BY MFI								
Weighted Average Real Interest Rate	30.8%	17.4%	46.3%	29.7%	22.3%	88.9%	27.0%	37.5%

* The institutions evaluated here are all small but well-performing MFOs.
Source: Microrate, 2000

Annex 1b: Financial Indicators of Select Caribbean MFOs

1998	Carib 1	Carib 2	Carib 3	Carib 4	Carib 5	Carib 6	Carib 7	Carib 8	Caribbean MFOs (Average)**
CHARACTERISTICS	**Belize**	**Jamaica**	**Belize**	**Jamaica**	**T&T**	**Jamaica**	**Guyana**	**Guyana**	
Gross Loan Portfolio (US$ thousands)	$5,174	$200	$928	$230	$2,117	$2,753	$1,307	$4,306	$2,127
Number of Loans	1,581	726		624	1,331	2,070	2,753	355	1,349
Average Loan Balance	$3,273	$275	$3,000	$369	$1,591	$1,330	$475	$12,130	$2,805
GDP per capita	$2,660	$1,740	$2,660	$1,740	$4,520	$1,740	$780	$780	$2,078
Avg loan/GDP per capita	1.23	0.16	1.13	0.21	0.35	0.76	0.61	15.55	2.50
PROFITABILITY									
Return on Average Equity	2.4%	-29.8%	3.4%	7.3%	n/a	19.2%	11.6%	16.3%	4.3%
ASSET QUALITY									
Loans > 30 days past due (% of Total Assets)	12.4%	58.6%	100.0%	19.6%	34.7%	8.7%	28.9%	84.3%	43.4%
Loan Loss Reserves / Loan 30 > days past due	18.6%	46.5%	n/a	58.6%	0.0%	35.8%	25.6%	9.9%	27.9%
CAPITAL									
Debt/ Equity	0.7	0.8	0.4	0.4	n/a	0.1	1.1	4.0	1.1
EFFICIENCY AND PRODUCTIVITY									
Operating Expenses/Average Gross portfolio	15.2%	26.6%	7.3%	52.3%	0.0%	10.1%	6.7%	14.6%	16.6%
Operating Expenses/# of Loans Outstanding	$498	$73		$193		$134	$32	$1,776	$451
Loans per Credit Officer	225.9	72.6	-	208.0	102.4	690.0	n/a	118.3	202.5
GROWTH (1997-98)									
Gross Portfolio, in US Dollars	92.1%	0.0%	-13.0%	-1.2%	17.4%	42.2%	-3.3%	4.8%	17.4%
INTEREST RATE CHARGED BY MFI									
Weighted Average Real Interest Rate	12.0%	38.0%	12.0%	46.8%	20.4%	30.0%		19.0%	25.5%

** The institutions evaluated here are 8 of the best performing MFOs in the Caribbean region.
Source: Microrate 2000

Annex 2a: Approved Microenterprise Projects: 1985-2000

Country	Project Title	Amount Approved (US$)	Year Approved	Type Of Project	Beneficiary or Executing Agency	Description
Bahamas	Credit Union Strengthening	660,000	1998	Multilateral Investment Fund	League of Credit Unions	Institutional Strengthening
Barbados	Barbados Business Youth Trust	70,000	2000	Technical Cooperation	Youth Group	Institutional Strengthening
	Black Belly Sheep	60,000	1998	Small Project	Sheep Growers Association	Improve Marketing of Sheep
	Support to Producers of Cut Flowers	500,000	1988	Small Project	Horticultural Association	Credit Fund and Technical Assistance
	Support to National Development Foundation	250,000	1987	Small Project	NGO	Credit Fund
Belize	Assessment of Microcredit Institutions	30,000	2000	Technical Cooperation	Three MFOs (BEST, National Development Foundation of Belize, Help for Progress	Diagnostic assessments
	Trade Promotion and Business Development	1,146,786	1996	Multilateral Investment Fund-Technical Cooperation(TC)	Institute of Business and Chamber of Commerce	Technical and marketing assistance to small farm producers
	Support for Belize Enterprise for Sustainable Technology	500,000	1994	Small Project	BEST (NGO)	Credit Fund
	Support to National Development Foundation of Belize (NDFB)	500,000	1994	Small Project	NDFB (NGO)	Credit Fund
Guyana	Institutional Strengthening of IPED	300,000	2000	Multilateral Investment Fund-(TC)	Institute for Private Enterprise Development	Institutional Strengthening
	Microenterprise Training Services	900,000	1999	Multilateral Investment Fund-(TC)	Private Sector Commission	Voucher Program for BDS
	Institutional Strengthening of New Amsterdam Credit Union	60,000	1995	Technical Cooperation	New Amsterdam Credit Union	Institutional Strengthening
	Support to Institute for Private Sector Enterprise	250,000	1987	Small Project	IPED (NGO)	Credit Revolving Fund
Jamaica	Institutional Strengthening of Credit	1,900,000	1994	Multilateral	League of Credit	Institutional Strengthening

	Unions			Investment Fund(TC)	Unions	
	National Development Foundation of Jamaica (NDFJ)	200,000	1986	Small Project	NDFJ	Revolving Credit Fund
Suriname	Support to Microentrepreneurs in Magenta	40,000	1997	Small Project	Micro-entrepreneur Association	Institutional Strengthening
	Credit Union Strengthening-(Godo and De Schakel)	120,000	1995	Technical Cooperation	2 Large Credit Unions	Institutional Strengthening
Trinidad and Tobago	Institutional Strengthening of Credit Union League	945,610	1995	Multilateral Investment Fund-(TC)	Credit Union League	Institutional Strengthening
	Microentrepreneur Credit	500,000	1990	Small Project	FUNDAID	Revolving Credit Fund
	Small Business Pilot Project	500,000	1989	Small Project	National Centre for Persons with Disabilities	Pilot Vocational and Business Training Program
	Rural Credit and Marketing Support	500,000	1988	Small Project	Farm Association	Credit Fund and Technical Assistance
TOTAL		**9,932,396**				

Source: IDB Databases of Microenterprise Unit and Regional Department 3.

Annex 2b: IDB Pending Microenterprise Projects (As of September 2000)

Country	Title of Project	Amount	Type	Beneficiary	Description
Belize	Support Toledo Institute for Development	270,000	Social Entrepreneurship Program and parallel TC*	Toledo Institute for Development (NGO)	Ecotourism Development
Trinidad and Tobago	Support to FUNDAID	300,000	MIF Line of Activity	FUNDAID (credit granting NGO)	Institutional Strengthening
	Support to Caribbean Microfinance Ltd.	6,000,000	MIF	Caribbean Microfinance (Finance Co.)	Institutional Strengthening and Equity
TOTAL		**6,570,000**			

Small Project Program renamed Social Entrepreneurship Program in December 1998.

Annex 3: Credit Union Movements Compared:

Caribbean	Number of Coops	Penetration Rate	Coop. Loans (US$)	Bank Loans (US$)	Ratio (Coop/Bank Loans)
Bahamas	14	20.75%	43,000,791	2,256,653,061	1.9%
Barbados	38	16.16%	12,997,712	1,069,050,000	1.2%
Belize	10	29.73%	1,443,018	305,360,000	0.5%
Guyana	28	6.89%	1,443,018	325,615,578	0.4%
Jamaica	66	30.58%	147,812,219	2,017,782,455	7.3%
Suriname	21	10.32%	256,000	197,264,339	0.1%
Trinidad & Tobago	96	61.20%	279,278,760	2,133,624,524	13.0%
Averages	**39**	**25.09%**	**69,461,645**	**1,186,478,565**	**4.0%**
Latin America					
Bolivia	20	8.67%	177,192,418	4,661,250,000	3.8%
Colombia	NA	28.80%	1,326,000,000	33,135,193,794	4.0%
El Salvador	30	2.51%	76,984,580	4,887,863,248	1.6%
Peru	130	3.83%	121,826,065	14,833,333,333	0.8%
Averages	**60**	**10.95%**	**425,500,766**	**14,379,410,094**	**3.0%**

Source: World Council of Credit Unions, 1998 Statistical Report

International Financial Statistics, July 2000

Note: Penetration Rate = Number of Members/Economically Active Population