

Dynamics of Commercial Microcredit - Sustainable Growth

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Inner Mongolia Autonomous Regional (IMAR) Workshop on
Sustainable Development of Microcredit Institutions
12-13 October 2006

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Outline

- Introduction: The Context
- Commercial Microcredit: The Concept
- Two Basic Growth Strategies
- Four Ways to Organic Growth
- Four Keys to Sustainable Organic Growth
- Broader Conditions for Sustainable Growth
- Concluding Remarks

Introduction: The Context

- a set of new microcredit institutions
- What approaches and strategies they can adopt to grow?
- What issues on their growth path?
- What challenges?
- Empirical evidence from other countries

Purpose: to stimulate a thorough discussion;
not to be prescriptive.

Commercial Microcredit: The Concept

“Microcredit operations carried out with application of market-based principles”

“profit-driven microcredit operations”

Simple concept.

But profoundly impact on operations.

Rationale for Commercial Approach

- Need for Institutional sustainability and growth
- Need to expand outreach
- Clients want permanent services
- Clients want quality services at reasonable prices

[Compare with social welfare approach to credit.]

Growth Strategies and Empirical Evidence

- Institutions adopt different strategies.
- They affect growth differently: quantity and quality
- What are these strategies?
- How they affect growth?

Two Basic Strategies

Intensive Strategy (in a given area)	Extensive Strategy (across areas)
Limited Product Menu (Market Penetration)	Limited Product Menu (Penetration across areas)
Broader Product Menu (Market Broadening)	Broader Product Menu (Market Broadening)

Intensive Growth Strategy

- Grow in a given sub-geographic area [given locality in a county]
- Two options:
 - Intensive growth with limited product menu
 - Intensive growth with broader product menu

In both cases, stay within the same sub-area.

Extensive Growth Strategy

- Extend branch network to many areas [say within a county]
- Two sub-options:
 - Extensive growth with a limited product menu
 - Extensive growth with a broader product menu

Key to sound choices

- Choices must be made based on sound business principles.
 - resource (human/financial) position
 - market potential
- Limit the number of variables you have to manage

Empirical Evidence

- **Prodem's (Bolivia) Growth Strategy**
 - Early years [1987-1989]
 - ◆ Adopted an intensive growth strategy
 - ◆ Chose to build economies of scale within two branches
 - ◆ Focused on credit
 - ◆ Efficiency improved (cost per dollar lent decreased rapidly)
 - ◆ Credit officer productivity increased
 - ◆ Able to pay more attention to delinquency

ACLEDA's (Cambodia) Growth Strategy

- Early years [1993-1995]
 - ◆ Relied on Extensive Growth Strategy
 - ◆ Branches in a number of provinces
(donor financing and pressure)

Impact of ACLEDA's Early Strategy

- Increased fixed investments
- Increased staff training costs
- Increased monitoring costs
- Dispersed management attention
- Low staff productivity
- High cost per dollar lent; high PAR

Four Ways to Organic Growth

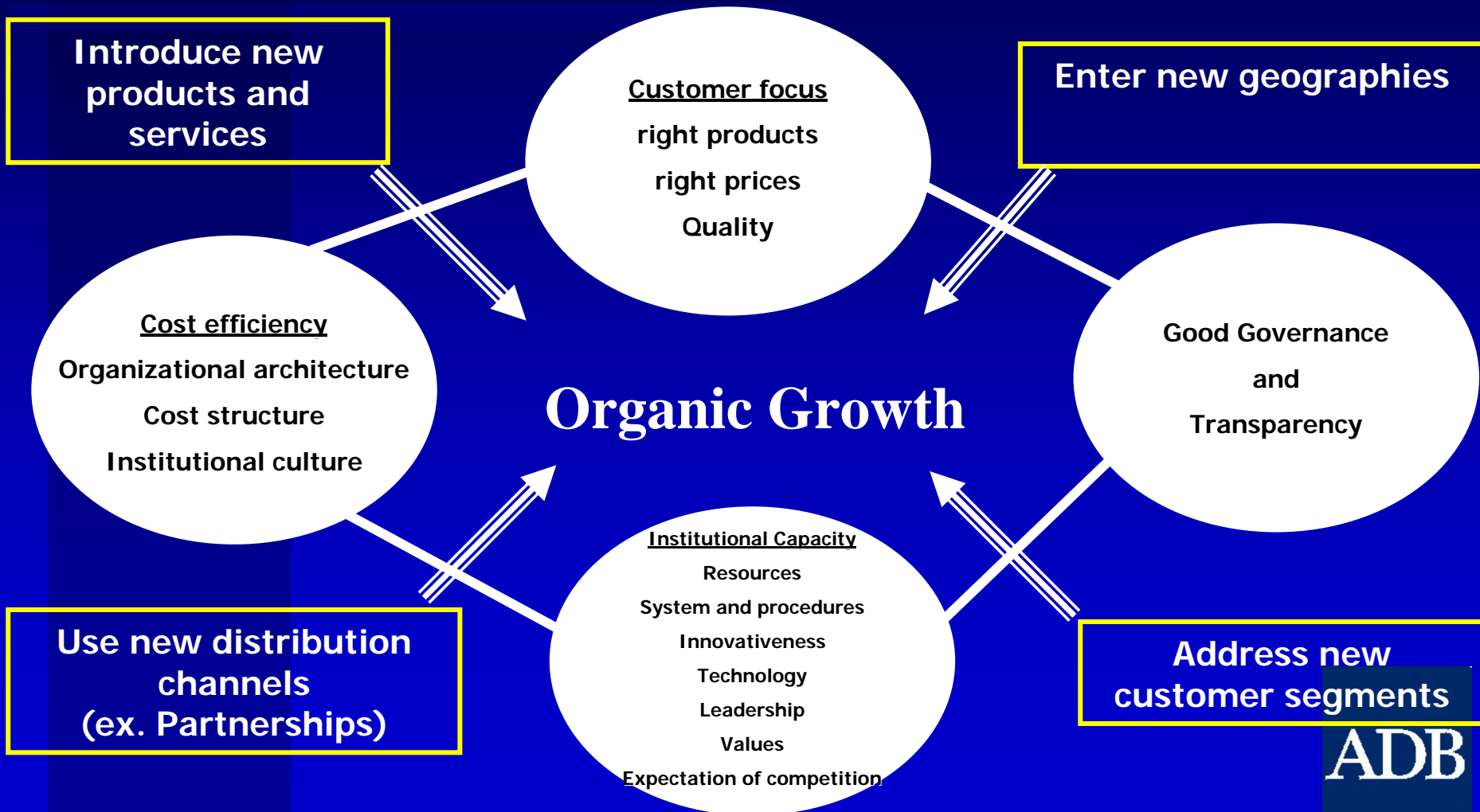
**Introduce new
products and
services**

**Enter new
geographies**

**Use new distribution
channels
(ex. Partnerships)**

**Address new
customer segments**

Four Keys to Sustainable Organic Growth



First Key: Customer Focus

- Seems basic and simple.
- Products / Prices / Quality.
- Many MFIs pay inadequate attention to these.
- Example: borrower transaction costs.

Borrower Transaction Costs (BTCs)

- A critical factor
- Lots of attention needed to keep them low
- High BTCs reduce demand
- Low BTCs allow lenders to charge higher interest rates

ALCEDA's Example (1996)

- Wanted to increase interest rate on small business loans
- When clients were polled about the increase, they agreed
- But on one condition: decrease training
- In 1996, ACLEDA removed compulsory savings, too.

Second Key: Cost Efficiency

- Attention to Organizational architecture
- Organizational architecture affects cost structure
- Costs influence growth in many ways
- Lean/Mean Organization
- Cost efficiency related to institutional culture
 - The case of ASA (Bangladesh)

Third Key: Institutional Capacity

- Human resources
- Systems and procedures
- Innovativeness
- Technology
- Specialization
- Leadership
- Values
- Expectation of competition

Fourth Key: Good Governance and Transparency

- Organizational mechanisms that ensure commitments to stakeholders (investors, customers, employees, regulators, and others)

Broader Conditions for Sustainable Growth

- Macroeconomic stability
- Enabling policy environment
- Supportive regulatory framework
- Profitable economic opportunities

Concluding Remarks

- Different ways to grow
- Customer focus is the most fundamental for growth
- Sustainable growth requires financial viability.
- Growth should be seen as a marathon; not a sprint.

Thank you for listening.

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