

**MICROFINANCE APEX MECHANISMS:
REVIEW OF THE EVIDENCE AND POLICY RECOMMENDATIONS**

by

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CONTENTS

I.	Organization of the Paper and Primary Conclusion	1
II.	Methodology and Limitations	3
	A. Theoretical Exercises and Empirical Verification	3
	B. Objectives of the Research Agenda	3
	C. Obstacles and Limitations	4
III.	Definitions and Assumptions	5
	A. Apex Organizations	5
	B. Microfinance	7
	C. Difficulties and Success of Microfinance	8
	D. Sustainability	9
IV.	Summary of General Results	11
	A. Two Roles of an Apex Organization	11
	B. Value Added as Success	11
	C. The Apex as Financial Intermediary	12
	C.1 An established microfinance sector	12
	C.2 Large market size	12
	C.3 Opportunities for diversification	13
	C.4 Sustainable microfinance organizations	14
	C.5 Comparative advantages as intermediary	15
	C.6 Monitoring and compatible incentives	16
	C.7 Leveraging	17
	C.8 Incentives for upgrading	17
	C.9 Sustainability of the apex organization	18
	D. The Apex as Developer of the Market	19
	D.1 Funds as the binding constraint	20
	D.2 Lack of technology, mission, and organization as the constraints	20
	D.3 Market size	21
	D.4 Generation of new lending technologies	21
	D.5 Transfer of existing lending technologies	24
	D.6 Leadership	25

D.7	Redesigning and upgrading organizational structures	26
D.8	Compatibility between technology and organization	26
D.9	Joint learning-by-doing	27
D.10	Technical assistance as ownership	27
D.11	Competition	28
D.12	Scarce human capital	28
E.	Two Roles in Conflict	29
E.1	Disbursement pressures	29
E.2	Ownership and sustainability	29
E.3	Economies of scope	31
E.4	Diseconomies of scope	31
E.5	Incompatible incentives	32
E.6	Competitive pressures	33
E.7	Upgrading and downscaling	33
V.	Lessons from the Case Studies	36
A.	Methodology	36
B.	Bangladesh: PKSf as a Role Model	37
C.	India: Friends of Women's World Banking and Competing Apex Organizations	41
D.	Benin: The PADME/Financial Bank/AFRICARE Connection	45
E.	Mexico: A Country in Search of a Microfinance Sector	48
F.	Bolivia: Apex Organizations in Search of a Role	49
G.	The Small Country Syndrome: Apex Organizations in Search of a Market	54
G.1	Honduras: Fundación Covelo	54
G.2	Costa Rica: ACORDE	56
G.3	Dominican Republic: FondoMicro	58
H.	Paraguay: Technical Assistance for Downscaling	59
VI.	Policy Recommendations	62
	References	64
	Annex A.	68
	Annex B.	69

MICROFINANCE APEX MECHANISMS: REVIEW OF THE EVIDENCE AND POLICY RECOMMENDATIONS¹

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I

Organization of the Paper and Primary Conclusion

This occasional paper summarizes key overall results from the comprehensive research project on *Microfinance Apex Mechanisms* undertaken by investigators of the Rural Finance Program at The Ohio State University (OSU) in collaboration with the Consultative Group to Assist the Poorest (CGAP). The purposes of this research project have been to examine the rationale for the creation of domestic apex organizations established in developing countries to promote the advancement of microfinance and to learn lessons from their actual performance.

Based on serious examination of the theoretical rationale and detailed evaluation of the available empirical evidence, the researchers would like to caution donors and policymakers that **"current enthusiasm about the potential contributions of domestic apex mechanisms to progress in microfinance is not warranted."** Given several distinct shortcomings identified by the research, the creation of domestic apex organizations should in general not be recommended, except in those cases where a number of critical preconditions are met.

To arrive at this conclusion has not been an easy task. On the one hand, the researchers have recognized the political urgency of finding effective mechanisms to expand the outreach of microfinance. Moreover, the researchers believe that in many circumstances sustainable microfinance does improve the welfare of the poor and other target clientele. In principle they share the goals of the proponents of apex mechanisms, but they do not share their naive enthusiasm.

¹ This *CGAP Occasional Paper* was written for the research project on *Microfinance Apex Mechanisms* undertaken by the Rural Finance Program at The Ohio State University (OSU) and the Consultative Group to Assist the Poorest (CGAP). For additional papers produced by the project and for papers in preparation, see the list of references.

² Claudio Gonzalez-Vega is Professor of Agricultural, Environmental, and Development Economics and Director of the Rural Finance Program at The Ohio State University. The contributions of members of the OSU research team on microfinance apex mechanisms (Mayada M. Baydas, Geetha Nagarajan, Sergio Navajas, Korotoumou Ouattara, Rodolfo Quiros, and Mario Villalpando-Benitez) and comments and recommendations from Douglas H. Graham, Richard L. Meyer, and Mark Schreiner are gratefully acknowledged. The team is grateful for the support of Mohini Malhotra and for the detailed guidance and observations of Richard Rosenberg. The researchers are particularly grateful with representatives of the apex organizations observed, who were helpful and gracious hosts even when the findings were threatening to them. The opinions expressed here are those of the author and not necessarily those of the sponsoring organizations.

On the other hand, the conceptual framework specifically built for the analysis of this problem has revealed that there is not a theoretical first-best justification for the establishment of a domestic apex organization to promote the emergence of the missing microfinance market. Creation of domestic apex mechanisms might only be justified, therefore, on weak second-best grounds (Gonzalez-Vega, 1998). As second-best interventions, however, the likelihood of success of these apex mechanisms depends on a number of demanding empirical (case-by-case) circumstances. Most of the cases observed by the OSU researchers did not meet the necessary conditions for this outcome.

To assess these circumstances, the research has examined strengths and weaknesses typical of domestic apex organizations in developing countries. As a result, this paper describes those prior conditions, organizational designs, and policies and procedures most conducive to the successful promotion of sustainable *microfinance organizations* (MFOs) through the operation of apex mechanisms. The analysis identifies elements of the institutional design of apex organizations that work better than others. This review of their distinctive strengths and weaknesses leads to recommendations about when and where to create and when and where not to create domestic apex organizations.

This exercise has focused its efforts on a search for a justification for the creation of *new* domestic apex organizations or, if one is not found, on the verification of the lack of a strong rationale for this type of intervention. The paper, therefore, does not make specific recommendations about *existing* apex organizations. Given that the high costs of creating them are already sunk, a few of these organizations offer socially-valuable services now, even when, at the time of their creation, an alternative intervention might have been a better use of the donor and government funds targeted for the promotion of microfinance (Schreiner, 1997). Special circumstances, examined in this paper, explain their current success. Despite its focus on the creation of new organizations, results of this investigation may still suggest some guidelines for improving the performance of the few existing apex organizations that may have a promising future.

Finally, to further clarify the role of domestic apex mechanisms in expanding the supply of sustainable microfinance, the paper includes some reflections on key conditions that lead to the successful development of microfinance in general. These considerations make it possible to evaluate if apex organizations have a comparative advantage in delivering these key ingredients for success.

In addition to this introduction, the paper has five more sections. Section II describes the methodology used in the investigation and discusses the limitations of the results. Section III defines key concepts and spells out the basic assumptions underlying the approach. This section defines the problem to be addressed by the apex organization. Section IV summarizes the central conclusions of the research project. Section V discusses some salient results from the case studies that support the conclusions of the investigation, and it reviews other sources of information that reinforce these results. Section VI outlines the main policy recommendations. Annexes describe

elements of the research effort, and a list of references invites the reader to further consider the evidence.

II

Methodology and Limitations

A. Theoretical Exercises and Empirical Verification

Serious and detailed analysis has preceded the recommendations offered in this occasional paper. First, this analysis has included the development of a conceptual framework for the exploration of the theoretical justification for the creation of apex mechanisms and of the sources of their potential comparative advantages in the promotion of microfinance (Gonzalez-Vega, 1998).

Second, the researchers have also observed a number of apex organizations around the world, in an effort to derive lessons from their actual experiences about the costs and benefits of their operation. Special case studies have been undertaken on apex organizations in Bangladesh, Benin, Bolivia, Costa Rica, Honduras, India, Mexico, and Paraguay.³

Third, a questionnaire was mailed to 24 organizations in 18 countries, and the responses from 16 of them were recorded. The data from this survey reinforce the results from the case studies.⁴

Fourth, additional information has been gathered from the existing documentation on apex mechanisms, from discussions in the electronic list *devfinance*, and from informal contacts with experts in the field and with several donor agencies. Specific results from this information-gathering efforts have been presented in several papers generated by the project (Baydas and Gonzalez-Vega, 1997). Some of these results are discussed here, but only as they help to clarify a particular general argument or conclusion.

B. Objectives of the Research Agenda

The conclusions reported in this paper respond to the goals of a clearly-bounded research agenda. The specific objectives of these research activities have been:

- (a) to understand the *necessary* and *sufficient* conditions under which domestic apex mechanisms for the promotion of microfinance can be successful in increasing the outreach and sustainability of MFOs,

³ Consult the list of references for the individual case studies and other papers written for the project. See Annex A for a list of the organizations included in the case studies.

⁴ See Annex B for a list of the organizations included in the survey.

- (b) to identify advantages and disadvantages of domestic apex mechanisms over alternative instruments available to increase the access of MFOs to loanable funds and/or organizations equipped with the knowledge and experience needed to strengthen the institutional viability of MFOs, and
- (c) to examine elements of the organizational design, policies, and procedures of domestic apex organizations that contribute to their successful performance, in the hope that this knowledge will be relevant in decisions about creating new or restructuring existing apex organizations.

In addressing this well-delineated set of questions, the researchers encountered severe obstacles. These obstacles are described in the paper, and some of the limitations of the conclusions are discussed below. The set of materials from this research project reflect, however, the most rigorous and complete attempt to understand this topic to date.

C. Obstacles and Limitations

Given the small number of existing apex organizations whose funding and institution-building operations are attempting to promote an expansion of microfinance supply and given the recent creation of most of these mechanisms, any generalizations from inductive exercises that have observed a few actual experiences are difficult to make. The OSU researchers have recognized this limitation. To address it, they have also taken into account, among several other inputs, the experience of apex mechanisms created earlier, not for the promotion of microfinance, but for the advancement of other goals, such as agricultural development (Villalpando-Benitez and Gonzalez-Vega, 1998). Lessons from these other experiences shed light on the prospects for success or failure of these interventions.

Moreover, given a broad range of domestic apex organizations and significant differences across their various types, specific results reviewed here may apply to some but not to other types of apex organizations. A discriminating reading, which would keep these distinctions in mind, is therefore advised. Each type of apex organization has its own strengths and weaknesses. Each type of apex organization caters to different categories of MFOs. While the concerns conveyed in this paper apply more strongly to some types of apex organizations than to others, the more general results apply, however, to most of them.

Despite the difficulties encountered, the conclusions reported here are robust. The recommendations presented in this occasional paper have emerged from a coherent combination of rigorous deductive reasoning, from basic principles and common sense, and a detailed understanding of the lessons learned (inductively) from the specific case studies and other empirical evidence. The researchers feel confident, therefore, that their recommendations are the most sensible possible, given the available information set. They hope that these recommendations will be taken seriously and will be useful for those in charge of deciding about the use of public funds for microfinance.

III

Definitions and Assumptions

A. Apex Organizations

For the purposes of this research project, *apex organizations* have been defined as mechanisms created to operate as *wholesaling*, second-tier organizations to facilitate the disbursement of funds to *retailing*, first-tier microfinance organizations and/or umbrella mechanisms created to develop the sustainable capacity of retailing MFOs. The research efforts have focused on *domestic* apex organizations and, therefore, they have ignored issues concerning similar organizations that offer these services on an international scale.

Microfinance apex organizations are defined by their operations with retailing organizations and by the provision of one or more of the following services to MFOs:

- (a) the wholesaling of loanable funds,
- (b) the disbursement of grants and subsidies on behalf of donors and government,
- (c) the screening and certification of MFOs that fulfill certain eligibility criteria,
- (d) the operation of loan-guarantee facilities,
- (e) the supply of guarantees for MFOs raising funds in capital markets,
- (f) institution-building support in the form of technical assistance and/or training of the staff of the MFOs,
- (g) the provision, through direct production or purchase, of cost-effective services and inputs for MFOs,
- (h) the generation of public goods (*e.g.*, lobbying for appropriate policies and regulations, creating a forum for the exchange of information across the industry) useful for the expansion of the microfinance sector, and
- (i) the prudential regulation and supervision of MFOs.

The purpose of the research project has been to evaluate the validity of arguments for the adoption of these functions by an apex organization. The rationale for the provision varies with the different types of services offered, as follows:

- (a) The *wholesaling* of funds and disbursement of grants and subsidies by the apex organization has been usually justified in terms of economies of scale and other cost savings for donors not well-prepared to deal with a large set of very small and frequently semi-formal MFOs.
- (b) The *screening* and *certification* functions of the apex organization have been usually justified by the information advantages that a local agency may have in selecting participants according to eligibility criteria, in order to make sure that the funds and other assistance reach the target organizations.

- (c) *Loan guarantees* have been usually justified as mechanisms to encourage financial intermediaries to expand their lending activities to marginal and risky clienteles, such as micro-entrepreneurs.
- (d) Guarantees (*avales*) offered in capital markets on behalf of MFOs may reduce the existing reluctance of private investors to channel funds to these organizations due to imperfect information.
- (e) *Institution-building* support has been usually considered necessary to allow the retailing MFOs to become viable clients of the wholesaling apex organization. That is, through these services, the apex organization invests in creating its own market.
- (f) A more cost-effective provision of some inputs by the apex organization (*e.g.*, accounting systems, software) may result from *economies of scale* or from discounts on bulk purchases.
- (g) Similarly, the use of donor and government funds may allow the apex organization to effectively supply *public goods* that otherwise would be undersupplied, because threats of free-riding would discourage private initiatives in the provision of these goods.
- (h) The *prudential regulation and supervision* of MFOs by an apex organization have been usually justified as a substitute mechanism in the absence of a formal regulatory framework that would contribute to the sustainability of MFOs and that would promote the confidence of potential depositors in these organizations.

This is an impressive list of tasks and of potential contributions of apex organizations. It is not surprising, therefore, that these apparent opportunities for intervention have caught the attention of policymakers. Moreover, this allure has made it difficult in practice to persuade policymakers to recognize that the instrument has severe limitations, particularly as a tool for the promotion of microfinance, and to dissuade them from converting apex organizations into their intervention of choice. The shortcomings identified by this research effort should result in a cautious attitude and in the recognition that in the microfinance field, as in other policy arenas, there are no panaceas (Gonzalez-Vega, 1994).

To facilitate the discussion, this paper focuses on the *wholesaling* of loan and grant funds and on *institution building* efforts as well as on the interactions between these two central functions of apex organizations. The reasons for this focus are clear. Loan guarantees have been discussed elsewhere (Meyer and Nagarajan, 1996, Llisteri and Levitsky, 1996). The production of public goods and economies of scale in input supplies are marginal activities compared to the former two. Associations of MFOs that merely produce these collective services are not investigated here. Moreover, although apex organizations may perform important *monitoring* functions with respect to MFOs, they are not ideal frameworks for prudential regulation and supervision (Chaves and Gonzalez-Vega, 1994).

By definition, the MFOs that are clients of the apex organizations operate at the *retailing* or first-tier level and disburse their loans directly to the ultimate borrowers (e.g., microenterprises). In contrast, the apex organizations operate as wholesalers and disburse their loans and/or grants to MFOs for on-lending to the final borrowers. Some apex organizations also have, however, operations with final borrowers, thereby combining first-tier and second-tier activities. Potential conflicts emerge from these dual functions, which are discussed below. The research project has highlighted, however, the second-tier activities of the apex organizations and the effect of these operations on strengthening the retailing capacity of their MFO clients.

From an organizational perspective, there are several types of apex facilities, ranging from mere rediscount windows (sometimes at central banks) to full-fledged independent organizations with multiple functions. To different degrees, the recommendations of this paper apply to all of them, although concerns about organizational design vary from one type to another of apex organization. They are all described here as *mechanisms*, in recognition of the fact that they are devices introduced by donors and governments in order to address problems that may not be resolved by markets or to pursue goals that may not be entirely achieved by market forces alone.

B. Microfinance

Microfinance refers to the provision of various types of financial services (loans, deposit facilities, instruments for the transfer of funds) to marginal clientele (typically the poor). Despite the value of all of these services for the target clientele, most of the efforts of apex organizations have been directed at the promotion of *microcredit*. Not only has this bias ignored the importance of other financial services for the target clientele, but it may also have been counterproductive. Indeed, the operations of apex organizations may discourage deposit mobilization by MFOs. This, in turn, may conspire against the sustainability of MFOs.

Microfinance attracts public attention because it is very difficult to supply financial services to the target population. The challenges of microfinance emerge from a number of factors:

- (a) The characteristics of the *transaction* (e.g., a very small loan amount, a short term to maturity, the absence of legally-enforceable collateral, and the need to program frequent repayments to facilitate the monitoring of borrowers) are such that the supply of these services is expensive (high costs per dollar of the transaction).
- (b) The characteristics of the *client* (e.g., low level of income --poverty-- and informality of the business, remote location, unstable occupation, high mobility) are such that the risks involved in lending are high and the costs involved in lowering these risks are also high.
- (c) The characteristics of the *project* being financed (e.g., incomplete information to evaluate its risk profile, uncertainty about the determinants of its success, difficulties in monitoring the efforts of the borrower, high variance of expected returns, high covariance with the outcome of other local projects) also increase the risk of losses from default.

For numerous combinations of these transaction-client-project features, the supply of financial services based on standard (traditional) *banking technologies* is not profitable and, as a result, potentially creditworthy clients are left without access to formal loans and to other financial services. Microfinance offers an alternative, but so far it usually does not spring from market forces alone. Because an expansion of the supply of financial services is potentially welfare-enhancing, there is a public interest in promoting the growth of microfinance. The OSU researchers accept this as a valid goal of public policy (Schreiner, 1997).

The recent development of microfinance, based mostly on innovations in lending technologies, has made it possible to expand the frontier of formal financial services to reach larger segments of the target population. The challenge here is to assess to what extent these successful developments have actually relied on the support of domestic apex mechanisms and what role, if any, might new apex mechanisms play in the replication of these positive developments.

Answers to these questions require a good understanding of the actual nature of the microfinance problem. A full examination of this question is a task that cannot be accomplished here. It may be useful, however, to recognize a few basic facts about the nature of the challenge and make some key assumptions explicit. This recognition is a necessary condition for an assessment of the comparative advantages of domestic apex organizations as a tool to address the microfinance problem (Gonzalez-Vega, 1998).

Moreover, this paper assumes that the objective of the policymaker is to promote the development of *sustainable* MFOs. Again, an analysis of the debate on sustainability is a task that cannot be accomplished here.⁵ The paper does not evaluate, moreover, the role of apex organizations as tools to disburse *welfare* transfers to target clientele for political reasons. Rather, the paper evaluates the role of domestic apex organizations in promoting the development of a market of sustainable MFOs that supply valuable financial services to the target clientele.

C. Difficulties and Success of Microfinance

For the successful provision of financial services to marginal clientele, MFOs must usually overcome several severe difficulties. These difficulties sharply reduce the profitability of providing these services when standard banking technologies are used. A basic assumption adopted in this paper is, however, that, at least after a reasonable gestation period, when appropriate technologies are used and when these technologies are implemented by organizations that can guarantee their own permanency, it is *possible* to supply these services on a profitable basis. This assumption is based on empirical observation, but it may be restricted to special cases where favorable conditions are present. The key assumption of this paper is that the role of public policy is to create conditions for the emergence of sustainable, profitable MFOs.

⁵ The reader can consult, among others, Yaron (1994), Gonzalez-Vega (1994), Morduch (1998), Schreiner (1997), Conning (1998), Rhyne (1998), and Navajas *et al.* (1998).

Indeed, particularly during the past decade, a number of comparatively successful MFOs have made important gains in outreach and sustainability (Christen *et al.*, 1995; Chaves and Gonzalez-Vega, 1996; Gonzalez-Vega *et al.*, 1997). This progress has resulted from organizations that have valued sustainability, have adopted adequate pricing (interest-rate) and product-design policies, and have implemented appropriate lending technologies.

Successful microfinance organizations have been able and willing to charge interest rates that cover their costs, have designed products that match the demand from the clients in the market niches where they operate, and have adopted lending procedures that lower borrower transaction costs. These organizations have frequently pursued altruistic goals by implementing a business plan that incorporates both a mission to reach the target clientele (outreach goals) and a vocation for permanence of the MFO (sustainability goals).

To accomplish their mission, these MFOs have adopted appropriate *lending technologies* that have incorporated incentives to repay responsible for very low losses from arrears and default and that can be implemented at reasonable costs. These technologies have shifted the *structure of incentives to repay* from the role of collateral to an emphasis on the development of a valuable long-term relationship with the client. The success of the MFO depends on the value of this relationship for both the MFO and the client and this, in turn, depends on the sustainability of the organization.

These new lending technologies offer cost-effective means for overcoming the uncertainties about the ability and willingness to repay of micro-borrowers and reduce expected losses from default to a minimum. Given well-recognized obstacles to accomplish this, associated with imperfect information, opportunistic behavior (moral hazard), and ineffective mechanisms for contract enforcement, these innovative lending technologies have allowed successful MFOs to expand the frontier of formal finance (Von Pischke, 1991, Gonzalez-Vega, 1997).

D. Sustainability

These days, the performance of MFOs is frequently evaluated in terms of outreach and sustainability (Yaron, 1994). Modified versions of these criteria have been adopted for this research project as well. Several dimensions of *outreach* have been considered. *Depth* refers to the social value of supplying microfinance services to particular clienteles (e.g., the poor). *Quality* reflects the value of a given microfinance product to the client, to be compared to the *cost* of the product to the client. *Breadth* refers to the number of clients of a given depth reached with a product of a given quality and cost. *Variety* refers to the range of products supplied by the MFO. *Length* defines the time frame over which this happens (Navajas *et al.*, 1998).

Among these dimensions of outreach, length is related to sustainability. In the simplest words, *sustainability* means the ability to reach goals in the short term without harm to the ability to meet goals in the long term. A central assumption of this investigation has been that the pur-

pose of the apex organizations whose justification is being studied is "**an expansion of sustainable outreach in microfinance.**"

There is much inconclusive debate about the measurement and importance of sustainability in microfinance (Schreiner, 1997). This debate cannot be resolved here. Many authors describe sustainability as the ability to maintain the real value of equity with all public support replaced by private funds and all resources bought in markets. This is a stringent but realistic long-term criterion: MFOs that need public support to survive will not generate outreach for very long, as public support for microfinance fades and the dependent MFOs lack incentives to be permanent. Few MFOs are sustainable in this sense, however, and many experts use less stringent definitions.

Some refer to industry standards in terms of cost recovery. According to these criteria, *operational self-sufficiency* measures the degree to which cash operating income covers cash expenses. *Financial self-sufficiency*, in turn, compares total operating income to total expenses, including the cost of maintaining the real value of equity and after adjustments to fully take into account subsidies received as well as write-offs for non-collectable loans (*The Microbanking Bulletin*, 1998).

For the purposes of the survey of apex organizations conducted under this study, *sustainability* was defined broadly as "the ability to pursue the mission of the institution (e.g., lending to the poor) in a permanent fashion, while covering all financial and operational costs from revenues from operations, excluding grants and subsidies." Although this statement may be interpreted differently by different people, what matters for current purposes is the general idea that the goal of the domestic apex organization must be to promote some degree of sustainability of its MFO clients.

The debate about the importance of sustainability is also intense (Morduch, 1998; Conning, 1998, Rhyne, 1998). This research activity has assumed that sustainability matters a lot. The most important reason why the sustainability of the MFO matters is that it elicits appropriate, *compatible incentives* from all the participants in the microfinance market (Gonzalez-Vega, 1994). Without these incentives, microfinance cannot be successful.

Thus, an image of MFO sustainability is necessary to promote loan repayment when there is no physical collateral to guarantee repayment. Borrowers will have less incentives to repay when the MFO is unsustainable, because a good repayment record has little value with a lender that will not last long. An image of sustainability is necessary to create depositor confidence and to attract commercial funds to the MFO. Sustainability is necessary for managers and staff to be diligent, because they value their career within the organization, and for them not to take their knowledge and experience elsewhere when the first opportunity arises (Gonzalez-Vega, 1994). In almost all cases in practice, improvements in outreach require improvements in sustainability (Navajas *et al.*, 1998).

IV

Summary of General Results

A. Two Roles of an Apex Organization

While domestic apex organizations may engage in the provision of a number of diverse services to promote the development of microfinance in their respective countries, the CGAP-OSU project has focused its research on two central roles: financial intermediation and market development. These functions of an apex organization are defined as follows:

- (a) An apex organization may intermediate, as does any other *wholesaling* financial institution, funds from government and donors, in the form of loans and equity grants, to *retailing* MFOs. This is its (pure) **intermediation** role. The apex organization receives funds from donors and government and, after a number of transformations of risk perceptions, loan size, terms to maturity, timing of disbursement, and other contract conditions, it delivers the funds to MFOs for on-lending to the target clientele. At a more advanced stage, the apex organization may intermediate funds between the private capital market and credit-worthy MFOs (*e.g.*, through the *securitization* of microfinance portfolios).
- (b) An apex organization may help develop the supply side of the microfinance market, by offering *institution-building* support to newly-created and to existing-but-unsustainable MFOs and by producing *public goods* for the microfinance sector. To develop the market, the apex organization transforms funds from government and donors into structures of incentives for the upgrading or downscaling of MFOs, transfers of technology, technical assistance services, training of the staff of MFOs, and other non-financial services valuable as inputs for specific MFOs or for all actors in the market. This is its **market-development** role. The objectives of these efforts may be to develop or to strengthen specific *sustainable* MFOs that could become *clients* of the apex organization in its pure intermediation role and/or the promotion of the microfinance sector *per se*.

B. Value Added as Success

Success of an apex organization is defined here in not very demanding terms. Any apex organization that *adds value* through the performance of either one of the two roles described above and thereby expands the *sustainable outreach* of the microfinance sector is considered successful for the purposes of this paper. In particular, the paper focuses on apex organizations that increase the number of sustainable MFOs in a given country at a reasonable opportunity cost.

Typically, a successful apex organization reduces transaction costs for government and donors willing to fund *already sustainable* MFOs (in its pure intermediation role) and/or enhances microfinance retailing capacity by helping to *transform* unsustainable into sustainable MFOs (in

its market-development role). This latter role differentiates *microfinance* apex organizations from other types of apex mechanisms created in the past for similar purposes.

The OSU researchers have found very few microfinance apex organizations that are successful in this broad sense. This has not been surprising. *Conditions for success* appear to be quite exacting regarding the performance of each one of the two possible roles of an apex organization *per se*. Attempts to combine these two roles by one single organization face additional complications. Those conditions for success and these complications are discussed below.

This section first examines the challenges faced and the conditions for success of an apex organization in its pure intermediation role. The section next examines the difficulties faced in the performance of the market-development role of an apex organization. Finally, the section addresses some serious questions that emerge when both functions are performed by the same apex organization.

C. The Apex as Financial Intermediary

The conceptual framework as well as the empirical observations suggest the following essential conditions for success in the *intermediation* role of a domestic apex organization. Although they may be present in a few cases, these conditions for success are not easily replicable. These conditions are:

C.1 An established microfinance sector

Domestic apex organizations might play a value-adding financial *intermediation* role **only** when a sufficiently large and well-established microfinance sector already exists. This is the case in two different sets of circumstances:

- (a) If its task is to lend (grant) donor and government funds to MFOs, an apex organization needs a *minimum mass* of creditworthy (eligible) MFO clients to justify its efforts.
- (b) If its task is to intermediate across the members of a *deposit-based* network, such as a federation of credit unions or an association of village banks, a minimum mass of sustainable retailing, deposit-taking organizations is needed for success. This type of network has been evaluated elsewhere and will not be discussed here further (Poyo, 1990; Ouattara, Gonzalez-Vega, and Graham, 1998). Their main strength springs from their emphasis on deposit mobilization, while their main weakness stems from the client-owner structure of the governance of the apex organization and of the participating MFOs.

C.2 Large market size

For a justification, therefore, of the intermediation role of an apex organization, both the numbers and the sustainability of the existing MFOs matter. Numbers matter for these reasons:

- (a) The *number* of potential clients among the MFOs in the country determines the extent to which the apex organization can take advantage of *economies of scale*. If the market is too small, the costs of the apex mechanism may exceed its benefits. It seems hardly justifiable, given its high opportunity costs, to create the bureaucratic and technocratic structures of a domestic apex organization to cater only to a market where at best four to eight MFOs are or will ever have a chance to become sustainable. This unfavorable cost-benefit ratio is present even when the role of the apex organization is not to lend but to serve as a mechanism for the transfer of grants.

This appeared, however, to be the case in several countries where some apex organizations studied had only been reaching about half-a-dozen MFOs over several years. Although some of these organizations are well-run, the thinness of their market hardly justifies their operations. Aware of this limitation, several of these apex organizations have been looking for additional functions, including first-tier direct operations with final borrowers. This has been the case, for example, of ACORDE in Costa Rica, FondoMicro in the Dominican Republic, and Fundación Coveló in Honduras.

C.3 Opportunities for diversification

A small number of potential clients usually leads to the concentration of the portfolio of the apex organization in one or two larger MFOs. Portfolio *concentration* may create two types of problems:

- (b) One problem is the increased risk of a portfolio highly dependent on the performance of a few specific MFOs. Failure of one or more of these MFOs can place the apex organization in serious financial difficulties and can jeopardize its ability to perform its intermediation functions.

This is a serious problem. Domestic apex organizations usually not only confront a market that is too thin, but they also confront a high *covariance* in the performance of their MFO clients. Problems in the environment in which they operate (*systemic risk*) can simultaneously cause problems for most of the clients of an apex organization. This reduces its opportunities for using *portfolio diversification* as a tool to manage risk.

If, in addition, its portfolio is highly concentrated on a few MFOs, losses associated with *idiosyncratic risk* concerning one or a few large clients can also have devastating consequences on the apex organization. In these circumstances, risk is too high for the apex organization to perform well as a financial intermediary. In contrast, an apex organization that simply disburses grants does not face this problem, but it may still encounter serious difficulties from concentration of its activities in a few large clients.

- (c) Indeed, another problem is the implicit *power* gained in their relationship with the apex organization by a few large, strategic MFOs among its borrowers or grantees. A large

grantee, frequently associated with a powerful patron, may request special treatment because it realizes its own role in justifying the existence of the apex organization. In its earlier years, for example, ACORDE in Costa Rica had to (successfully) rebuff MFOs linked to American NGOs in their claims for grants despite their lack of sustainability.

Even when the strategic large borrower is a good client, there is the threat that the MFO will consider ending the relationship with the apex organization. This uncomfortable situation was confronted in the Dominican Republic by FondoMicro, where its loans to ADEMI represented over four-fifths of the portfolio of this apex organization (Schreiner and Gonzalez-Vega, 1996). This gave ADEMI enough power to attempt to influence policy decisions at FondoMicro, including FondoMicro's consideration of the opportunity to engage in first-tier lending operations, which ADEMI opposed. To escape the trap associated with a small market and to use its formidable microfinance resources, FondoMicro decided to start its own operations at the retailing level, but in the process lost ADEMI as a client. This has likely been a good business decision by FondoMicro, given its binding constraints from market size, but it has been a severe blow to its role as an apex organization, a role that in any case had limited opportunities in this small market.

C.4 Sustainable microfinance organizations

In addition to their number, the *sustainability* of the potential MFO clients determines their creditworthiness or eligibility for grants and thereby the success of the apex organization in its *intermediation* role (disbursement of funds). Indeed, lack of MFO sustainability may limit the value added by the intermediation role of an apex organization in several ways:

- (a) When the MFOs are not sustainable, simply adding to their pool of funds for on-lending usually destroys rather than enhances their capacity to sustain outreach at the retailing level. Unable to manage their current level of loanable funds in a sustainable fashion, the flood of funds from the apex organization further brings out and accentuates the weaknesses of these MFOs. In these cases, the value added by the apex organization is negative, and the survival of the apex organization itself is in jeopardy. Numerous examples of apex organizations from the past illustrate the credibility of this threat. The Mexican experience in the 1990s is a good recent example of this danger (Villalpando-Benitez and Gonzalez-Vega, 1998).

If the existing MFOs are few, the apex organization might attempt to aid in the creation of additional MFOs before it fully engages in its intermediation role. If the existing MFOs are not sustainable, the apex organization might attempt to develop a market of sustainable MFOs by investing in their improvement.

- (b) This *market-development* role, which is not easy, may in any case be also constrained by country size and by other environmental features as well as by the long time it takes to develop strong MFOs. As discussed below, the conditions for success in market-develop-

ment tasks are even more demanding than the conditions for successful intermediation of funds, and the apex organization may not be well-equipped to undertake these efforts. If the apex organization does not have the capacity to engage in market development, in the absence of sustainable MFOs it cannot be a successful intermediary. If the apex organization has the capacity to develop a market, it still needs to confront the challenges of delivering both types of services through the same organizational structure.

- (c) Moreover, the central problem in many countries is that a large number of the existing MFOs currently are not and will never be sustainable. Those who created these MFOs did not have sustainability in mind, and their current quasi-owners are not interested in sustainability. These MFOs are too small, have not developed cost-effective lending technologies, charge interest rates that will never cover even a significant portion of their costs, and possess governance structures that will not lead to sustainability.

Incentives and broadly-offered technical assistance are not powerful tools to address the sources of their poor prospects. These unsustainable MFOs are candidates neither for the intermediation nor for the market-development role of the apex organization. Several well-run apex organizations, such as ACORDE in Costa Rica and Fundación Covelo in Honduras, initially attempted to improve the performance of many unsustainable MFOs, to eventually give up on this unrewarding task and focus on a few promising MFOs.

C.5 Comparative advantages as intermediary

Even when a market of numerous and sustainable MFOs already exists, justification for the creation of a domestic apex organization requires demonstration that this mechanism possesses *comparative advantages* as a financial intermediary. There are several reasons for this:

- (a) If the existing MFOs are already sustainable and creditworthy, they may already have access to *commercial* sources of funds. In this case, the apex organization would be redundant; it would generally add little value. An extreme example of this situation is the case of Bolivia, where several advanced MFOs already have access to commercial sources of funds as well as to a non-specialized development apex (NAFIBO) and where a competent non-government microfinance apex (FUNDA-PRO) has seen its role recently evaporate due to the presence of these market actors (Navajas and Schreiner, 1998).

The paradox is that an apex organization needs a developed microfinance market to be successful in its *intermediation* role, but that when a microfinance market is sufficiently developed, its services may be redundant and it may not possess comparative advantages to compete with other financial intermediaries in lending to advanced MFOs. This may be the case even when the terms of contracts with the apex organization are softer than commercial terms, because advanced MFOs prefer the flexible and timely service of commercial lenders to the conditioned and bureaucratic procedures of the apex organization.

In many developing countries, however, given problems of risk, information, and contract enforcement similar to those faced by the MFOs in their lending activities, commercial lenders and private investors may not be ready to channel their funds to sustainable MFOs **despite** their genuine creditworthiness or profitability. At least in theory, therefore, by using its *information advantages*, an apex organization might compensate for these shortcomings of undeveloped financial markets, and this may bring the availability of funds for microfinance closer to a social optimum.

Similarly, sustainable MFOs may be prevented from mobilizing deposits from the public by their inability (sometimes due to high minimum capital requirements) to obtain a *charter* with authorization for deposit-taking activities. In other cases, deposit mobilization may not be profitable in narrow market niches (Schmidt and Zeitinger, 1996). At least in theory, therefore, an apex organization might compensate for some of these regulatory restrictions and other constraints by making government and donor funds available to MFOs that cannot mobilize deposits.

- (b) In an actual *dynamic* context, however, creation of a domestic apex mechanism may not be (even in theory) the optimum way to deal with these market distortions and regulatory constraints on funds mobilization. As examined next, the main reason for this is the effects that the operations of the apex organization may have on the structure of incentives of the MFO clients.

C.6 Monitoring and compatible incentives

One key reason why the creation of a domestic apex organization may not be optimum is that sustainability itself is generally enhanced by the pursuit of funds on the market.

- (a) The accomplishment of efficient and sustainable microfinance retailing capacity is usually promoted when private investors, commercial lenders, and/or depositors become holders of the MFO's liabilities. This positive effect is obtained because *market-based funds* are usually accompanied by structures of *compatible incentives* and by outside *monitoring* that further the sustainability of the organization. This positive effect may be dampened by access to funds from an apex organization in terms softer than those of commercial funds and that are sufficient for the desired level of operations of the MFO.

In effect, the pursuit of market funds contributes to sustainability in two complementary ways. On the one hand, it creates incentives for the MFO to become sustainable, so that it will be able to attract these funds. That is, it constrains the MFO and induces appropriate managerial decisions that contribute to sustainability. On the other hand, the use of market funds creates incentives for private lenders, depositors, or investors to sufficiently monitor the MFO, so that their funds will not be at excessive risk. *Monitoring* on the part of depositors, accompanied by the threat of withdrawal of funds, and on the part of commercial lenders, accompanied by the threat of calling or not renewing loans, also induces responsible MFO behavior. Private investors, particularly when they are owners or quasi-owners, also contribute with their advice to the

management of the MFO. In this sense, the sustainability of the MFO and the interests of the holders of its liabilities are made compatible.

- (b) Domestic apex organizations are rarely good substitutes of these monitoring agents, in part because their threats tend to be less credible and in part because their expertise may be limited. Their threats are less *credible* because it is widely known that they use public funds in their operations, and the assumption is that donors encourage disbursements even when the sustainability of the MFO is questionable. Public officials are rarely expected to withdraw support from the clients of any apex organization.
- (c) In order to compete with other lenders, when the MFOs already have access to commercial sources of funds, domestic apex organizations may be inclined to soften the terms and conditions of their own loan contracts. These easier terms have ambiguous effects on the sustainability of the MFOs. On the one hand, they lower the costs of funds and make it possible for the MFO to concentrate on lowering its operational costs. On the other hand, the easier terms may make the MFO management complacent and uninterested in deposit mobilization.

C.7 Leveraging

A second reason why the creation of a domestic apex organization may not be optimum when there is market or regulatory failure is that government and donor funds are inevitably limited and, thus, the rapid expansion of microfinance will require the leveraging of these funds with market funds (Rosenberg, 1994).

- (d) The creation of a domestic apex mechanism is not an optimum intervention, therefore, because the positive effect that it is expected to generate (the expansion, through donor contributions, of loanable funds available for microfinance) is weak in the absence of sufficient commercially-based *leverage*, while the negative effects that it infuses (wrong incentives) discourage efforts to achieve use leverage and attain the sustainability of MFOs. The negative effects appear to dominate the positive effects in many cases. In several countries, MFO lobbying for regulation has actually reflected, not a desire to mobilize funds from the market, but the desire to access a less-demanding apex organization.

C.8 Incentives for upgrading

Easy access to funds from a domestic apex organization may remove the incentives that an MFO may have to seek funds on the market. It may also lessen the interest of the MFO in *upgrading* and thereby gaining access to market-based funds.

Discouragement of these efforts is directly related to the extent of the interest-rate *subsidy* transferred with the funds. The more subsidized the funds from the apex organization, the less the MFO will want to seek funds on the market. These negative incentives to upgrade and to

pursue market-based funds may thus retard development of competent and sustainable retailing capacity, the reason for the creation of the apex organization in the first place. Indeed, little progress toward MFO sustainability was made during earlier periods when the funds from apex organizations were heavily subsidized, as compared to recent progress, when some apex organizations (e.g., ACORDE in Costa Rica) have become more strict in their pricing of loans and in their creditworthiness criteria (Quiros and Gonzalez-Vega, 1998).

This dilemma (growth of loanable funds versus sustainability) is one of several ways in which the intermediation and the market-development roles of the apex organization may not be compatible. Thus, depending on circumstances of the environment, when an apex organization is created in a given country, a delicate balance between these two functions must be found.

C.9 Sustainability of the apex organization

When the role of the apex organization is (pure) financial intermediation, its success also depends critically on its own *organizational design* and *modus operandi*. In particular, an apex organization that emphasizes its *intermediation* role and that hopes to develop long-term relationships with its client MFOs must attempt to become *sustainable* itself. This may not be necessary if the apex organization is designed as a transitory mechanism for the disbursement of grants, while there is much controversy about the desirability that an apex organization devoted to institution building be sustainable itself. This issue will be discussed further below.

It appears that the sustainability of a domestic apex organization devoted to financial intermediation matters for several reasons:

- (a) The OSU researchers found much variation across apex organizations in their pursuit of their own sustainability. The researchers noticed, however, that weak property rights arrangements and governance structures have typically not resulted in the structures of compatible incentives needed for sustainability, efficient performance, and outreach achievements.
- (b) Internal controls in domestic apex organizations without well-defined owners or with weak governance structures tend to be poor, while limited owner monitoring frequently leads to managerial and financial problems at the apex organization itself. These problems reduce, in turn, the effectiveness of the apex organization in expanding loanable capacity at the retailing level and reduce the authority of the apex organization in demanding sustainability from its MFO clients.
- (c) Similarly, operational modalities that lead to steady losses jeopardize the sustainability of the apex organization and thereby its ability to achieve its own objectives. The case studies show that apex organizations concerned with their own sustainability adopt better policies and procedures and thereby have greater probabilities of success. Unfortunately,

most domestic apex organizations lack robust *organizational designs* and many adopt unsustainable policies and practices.

- (d) While the pursuit of sustainability by the apex organization is important, particularly when it engages in lending rather than disbursing grants or developing the market, many apex organizations encounter difficulties in realizing this goal due to the small size of the domestic market where they operate. When they still have the desire for sustainability (frequently because its managers and staff want to protect their jobs), these organizations tend to search for other tasks (including retailing operations) that would allow them to achieve sustainability. The paradox is that, while this behavior may boost the sustainability of the apex organization, these direct operations with first-tier clients may not necessarily be what the donors had in mind at the time they promoted the creation of the apex organization and they may create conflicts with its MFO clients. In this cases, it is better to promote the creation of a *retailing* MFO from the beginning.

D. The Apex as Developer of the Market

Where a sufficiently large market of sustainable MFOs is missing, a domestic apex organization faces even more acute challenges. To confront this situation, the apex organization might consider to (or may be mandated to) develop the market. That is, the apex organization might attempt to facilitate the establishment of new MFOs, improve the sustainability of existing-but-weak MFOs, or assist in the upgrading of promising-but-still-unsustainable MFOs. These *market-development* tasks differentiate microfinance apex mechanisms from other apex arrangements.

These tasks are, in general, among the central tasks of any effort to expand sustainable outreach in microfinance. *Institution-building* is a key input in these tasks. Indeed, many consider support for institution-building as the most important (direct or indirect) contribution of a donor to an expansion of the frontier of microfinance (Khranen and Schmidt, 1994).

Institution-building relies mostly on organizational engineering and mechanism design, transfers of technology, technical assistance, and staff training. Although subsidized institution-building increases the equity of any MFO as much as grants do, it is different from cash grants and subsidized loans for on-lending (Schreiner, 1997). Indeed, large and premature disbursements of funds to the MFO typically reduce the effectiveness of any institution-building effort.

Institution-building services, moreover, can be delivered by different institutional mechanisms, including but not restricted to domestic apex organizations. The main question to be addressed here is (not the importance of institution-building *per se* but) the extent to which domestic apex organizations possess comparative advantages for the delivery of institution-building services. Are they good providers of these services?

The conceptual framework developed by the OSU researchers suggests that a domestic apex organization is not an optimum response to this challenge. Moreover, based on the limited

empirical information available, the researchers have found very little evidence, if any, of success (value added) of a domestic apex organization in this important market-development role.

Delivery of these services by a domestic apex organization appears to be neither a *necessary* nor a *sufficient* condition for successful development of the microfinance sector:

- (a) Most of the successful MFOs (*e.g.*, in Bangladesh, Bolivia, El Salvador, Indonesia) have been developed without the assistance (or with only marginal assistance) from domestic apex organizations, and
- (b) in most countries where domestic apex organizations have been created, their ability to develop a microfinance market has been limited, as shown by the case studies.

Thus, creation of a domestic apex organization has been neither necessary nor sufficient for the expansion of sustainable outreach in microfinance. There are several reasons for this.

D.1 Funds as the binding constraint

To understand the potential effectiveness of a domestic apex organization in developing the microfinance market of a given country, it is necessary to understand the nature of the challenges faced in this task. What obstacles must be overcome? For success, the intervention must respond to the specific nature of these obstacles (Gonzalez-Vega, 1998). Moreover, there are important differences from country to country with respect to the obstacles to be overcome. These differences suggest that even when a domestic apex organization might be useful in one country, it may not be useful in another. *Replication* of apex organizations is difficult at best.

In the same way as market size matters for the success of an apex organization in its pure intermediation role, market size and other country characteristics matter for the success of an apex organization in its market-development role. Different *binding constraints* limit the expansion of sustainable microfinance in different countries and call for different types of interventions.

- (a) Insufficient funds, however, appear not to be the binding constraint to the expansion of microfinance in most developing countries. Instead, most experts (including representatives of the apex organizations surveyed) agree that the major bottleneck is a shortage of *retailing capacity*, *i.e.*, a shortage of well-designed and sustainable organizations, with competent staff who can implement a cost-effective microfinance technology.

For this reason, institution-building for market development is critical for the future of microfinance in these countries. Moreover, most experts agree that unless donors and government support them (but do not deliver them directly), these institution-building efforts will be insufficient to achieve the desired expansion of the frontier of microfinance. Nevertheless, the creation of domestic apex organizations to deliver these services is not necessarily the best possible channel for this market-development assistance.

- (b) In contrast, in those few countries where lack of funds has actually become **the** binding constraint, a domestic apex organization with a pure *intermediation* role may be a reasonable response of government and donors, but it will be successful **only** when guided by the strict conditions discussed above.

D.2 Lack of technology, vision, and organization as the constraints

Lack of funds is not the only possible constrain to the expansion of sustainable microfinance. As discussed earlier, in different countries a number of diverse constraints inhibits the growth of sustainable outreach in microfinance market niches. These constraints include but are not limited to the following:

- (a) Existing *lending technologies* may not allow cost-effective responses to the information and contract-enforcement barriers that curb financial transactions at the frontier. Implementation may be as difficult as the development of a new lending technology.
- (b) Poorly-constructed *ownership and governance structures* and other shortcomings of *organizational design* conspire against the sustainability of MFOs.
- (c) Typically, unsustainable MFOs cannot attract *competent staff* to support expanded outreach over time.
- (d) Frequently, the individuals who created the MFO and those who manage it lack the *vision* (vocation) to seek sustainability and lack the competence to achieve it.
- (e) Some environments are less hospitable to the development of microfinance than others. Repressive *regulatory frameworks* as well as the small size of the potential market at the retailing level and severe restrictions on *portfolio diversification* and other risk-management strategies (*e.g.*, highly covariant incomes) hinder the expansion of a sustainable microfinance sector.

Overcoming these other constraints, where possible, requires intensive market-development efforts. Both theory and the empirical observation suggest that, in general, domestic apex organizations do not possess comparative advantages in the provision of the institution-building inputs required to accomplish this market-development goal successfully. The shortcomings include the following limitations.

D.3 Market size

When the microfinance market at the retailing level is too narrow, there are few reasons to create a domestic apex organization to develop the market. The obstacles raised by small market size have already been discussed. In thin microfinance markets there is room, at best, for a few sustainable MFOs. In these circumstances, donors and government would be better advised

to focus their efforts on directly strengthening a few MFOs, rather than spending these efforts in creating the costly structure of an apex organization that would hardly justify its own existence. This would be frequently the case in small African countries.

D.4 Generation of new lending technologies

The successful evolution of MFOs requires the adoption of a cost-effective lending technology. Domestic apex organizations are not good tools to promote this adoption.

When the binding constraint is the absence of an *appropriate lending technology*, the correct intervention is to facilitate the generation, transfer, and adoption by the country's MFOs of lending procedures that are more cost-effective than those already in practice. The adaptation of new lending technologies to the features of specific market niches is not a trivial task. Domestic apex organizations are not the best possible mechanism for this finely-tuned task and, if asked to undertake it, they can provide only a partial substitute for other types of intervention. Insufficient support of these alternative mechanisms is one of the *opportunity costs* of creating domestic apex organizations.

- (a) Domestic apex organizations have usually encountered important limitations in the generation and transfer of new lending technologies. The OSU researchers could not find any domestic apex organization that had been the source of an important *innovation* in micro-finance technology. Other institutional mechanisms appeared to have been more effective in the performance of this critical task. Moreover, the apex organizations studied had difficulties even in effectively delivering more than one, already-known lending technology to their MFO clients. This is not surprising, given the lack of proximity of the apex organizations to the actual market niches where the MFOs operate.
- (b) The generation and development of cost-effective lending technologies requires a flexible framework for *experimentation*. Alternative approaches must be tested with an open mind, while the costs and risks of investments in research and development (R&D) are inevitably high. Indeed, it has been their vast *flexibility* in exploring alternative solutions for the typical information and contract-enforcement problems that plague financial markets at the frontier which has allowed some *non-government organizations* (NGOs) to develop several notable innovations in financial technologies over the past couple of decades. MFO-specific donor assistance, frequently delivered through mechanisms that possess comparative advantages in institution-building, have supported these innovative NGO efforts, not domestic apex organizations.
- (c) Moreover, it is unlikely that any particular domestic apex organization would be willing to undertake several experiments in the development of new lending and deposit-taking technologies at the same time. Such *multiplicity* of experiments is still needed, however, because nobody knows before hand which one will be the best solution to a particular problem, because unexpected second-generation problems continue to emerge, and because

solutions to similar problems may still differ in different environments. Strong reliance on domestic apex organizations to develop new microfinance technologies, in contrast to alternative institutional mechanisms, would narrow the range of innovation. Market failure with respect to innovation represents, however, the most important justification for government intervention in microfinance.

- (d) The OSU researchers have observed this situation in Bolivia, where several MFOs have pursued different strategies to address the problems of microfinance. Some of these organizations (PRODEM and BancoSol) have emphasized, for instance, the development of group-lending technologies, while other organizations (Caja Los Andes and FIE) have focused on the development of individual-lending technologies (Gonzalez-Vega *et al.*, 1997). Both strands of microfinance practice have made significant contributions to the defeat of obstacles to microfinancial transactions, each one of these organizations has learned from the other, and a healthy debate continues about the superiority of one lending technology over the other. **None** of these achievements has involved any of the numerous domestic apex organizations that have attempted to operate in Bolivia. Moreover, the multiple development of lending technologies has promoted not only a broader but also a stronger market. Faced with a demand for individual loans, for instance, BancoSol has quickly learned about individual lending technologies from its competitors.
- (e) Domestic apex organizations, particularly when they are in charge of developing the market rather than just intermediating funds, tend, instead, to be quite *rigid* in their support and understanding of lending technologies. After all, *lending technologies* are complex and delicate structures; innovators typically concentrate on the development of only one particular lending technology. Thus, the varied and prominent Bolivian contributions to the development of new lending practices would not have happened if a domestic apex organization had been in charge of exploring, if a domestic apex organization had attempted to promote, or if a domestic apex organization had required the adoption of a particular lending technology in the operations with its MFO clients. It is not surprising, therefore, that several existing domestic apex organizations have played a minimal role, at best, in the celebrated development of microfinance in Bolivia (Navajas and Schreiner, 1998).
- (f) Moreover, particularly if they also lend to MFOs, apex organizations are too *risk-averse* to promote risky experimentation. Indeed, in their intermediation role they cannot afford to encourage multiple experiments with uncertain outcomes, because the associated risks may jeopardize repayment. In their intermediation role, domestic apex organizations should only lend to MFOs that already possess sufficient mastery of their lending technology. When they do not, lack of funds is not the binding constraint. When MFOs are in the early stages of adoption of a new lending technology, they should not be funded so they can prematurely expand their lending capacity.
- (g) Furthermore, while domestic apex organizations may contribute to the internalization of some of the *externalities* that result from the production of new knowledge about lending

technologies by different MFOs, they find it difficult to promote competition among their clients. Intense *competition*, however, usually leads to the adoption of innovations by rival MFOs. This result has also been observed in Bolivia, where increasing market-niche saturation and the emergence of new competitors has induced leading MFOs to accelerate their rate of technological transformation and to adapt elements of the lending technologies of their competitors.

In conclusion, the OSU researchers know of no examples of domestic apex organizations that have been major sources of new financial technologies. Indeed, in recognition of these limitations, hardly anyone expects domestic apex organizations to engage in technological development. The issue here, however, and the reason why this matters, is not that domestic apex organizations are usually not good mechanisms for innovation in lending technologies but, as will be argued below, that the best instruments for the delivery of institution-building services tend to be those organizations that have actually been engaged in the development of new lending technologies and that best can assist the MFOs in the adoption of these technologies.

Too much emphasis on the creation of domestic apex organizations as the panacea would take the attention of government and donors away from these central questions. Public support for the development of new microfinance technologies may still be needed, however. Moreover, a feasible role for a domestic apex organization in these circumstances is still missing.

D.5 Transfer of existing lending technologies

Domestic apex organizations, nevertheless, tend to exhibit less comparative disadvantages in the *transfer* of lending technologies that have already been developed and tested. The apex organization's possible role in this respect assumes that:

- (a) cost-effective technologies already exist,
- (b) the apex organization has easy access to best-practice technologies and can disseminate them, and
- (c) the apex organization can effectively assist domestic NGOs in the *adoption* of these technologies.

These are not trivial tasks, and most domestic apex organizations do not appear to have comparative advantages even in these areas, but there are exceptions. In these special cases, a domestic apex organization may play a useful market-development role.

- (a) Where successful lending and deposit-taking technologies have been developed by *leading MFOs* in the country and where there is a *second echelon* of MFOs that may adopt technological practices that have already been adapted to the characteristics of the country and to the features of the market niches where the target MFOs operate, by disseminating these technologies a domestic apex organization may have a greater probability of success in expanding the microfinance market than otherwise.

- (b) This seems to be the case in Bangladesh, where most prominently the Grameen Bank, but also other leading MFOs such as ASA and BRAC, have over many years developed lending technologies adapted to the circumstances of this country. In this environment, PKSF appears to be successfully attempting to extend existing, well-adapted technologies to a fringe of smaller rural NGOs (Nagarajan and Gonzalez-Vega, 1998). Even in this instance, however, the range of lending technologies that has been accommodated by PKSF is narrow and the challenges faced by remote rural NGOs may require new solutions that depart from the existing technologies. Moreover, this environment of a *mature* microfinance market with well-developed technologies will not be easily replicable elsewhere.
- (c) Where, in contrast, there are no sources of local innovation in the country where the apex organization operates, the task involves the transfer of knowledge about microfinance technologies from abroad, the adaptation of the technological blue prints to the specific circumstances of the country, and the adoption of the new technologies by the local MFOs. *Domestic* apex organizations have few comparative advantages in implementing these tasks, in part because they are removed from the target clientele and in part because they cannot focus specific attention on a given MFO. Several features of microfinance, which is an activity extremely intensive in *local information* and in learning processes with long gestation periods, explain these difficulties. These tasks are, in any case, quite difficult, and domestic apex organizations have few advantages to overcome these difficulties.
- (d) Domestic apex organizations can actually gain access to a pool of international knowledge about microfinance best practice. At this accessible level, however, what this pool offers is a number of important but fairly *general principles*. A clear understanding of these principles is indeed critical as a starting point in the construction or upgrading of a successful MFO, but it is not sufficient for the adoption of specific lending technologies.
- (e) In these institution-building efforts, therefore, *domestic* apex organizations cannot compete with *international networks* (e.g., ACCION International) or *consulting firms* (e.g., Internationale Projekt Consult) with substantial field experience both in the development and extension of specific lending technologies. Although these mechanisms operate, *de facto*, as international apex organizations, the broad scope of their experience across many countries and many MFOs raises the quality of their advice and of their technical assistance services. Continuous monitoring of their affiliates allows them to enrich the information set from which they operate, beyond the possibilities of any domestic apex organization, particularly in small countries.
- (f) Moreover, these international entities tend to protect their information capital. While they disseminate some information about best practices to the public, most of their knowledge and the experience of their staff is *private information*, which cannot be easily transmitted to others. Unless the domestic apex organization hires their services, the apex organization, with less field experience, will not be able to replicate the results of these international mechanisms. If to accomplish their market-development goals, the domestic

apex organizations needed to seek the services of these international actors, then it might be more cost-effective for the donors to hire the international entities directly.

- (g) Sometimes, however, political constraints may bar this possibility for the donors and the government. In these cases, the domestic apex organization may play the role of broker of institution-building services. The infrastructure needed for this would be very minimal. Furthermore, their international status usually shields the foreign organizations from domestic *political pressures* that otherwise may weaken the performance of the domestic apex organization.

D.6 Leadership

Some of the most successful MFOs around the world have originated from the extraordinarily creative efforts of outstanding individuals (*e.g.*, Grameen Bank in Bangladesh). These situations, by definition, are not replicable, and a domestic apex organization cannot induce them. In contrast, most MFOs have emerged from a mixture of the sound local efforts of quasi-owners with vision and ample access to vigorous international providers of technical assistance. Such have been the cases of Bank Rakyat Indonesia (Patten and Rosengard, 1994), of PRODEM-cum-BancoSol in Bolivia (Glosser, 1994), and of Caja Los Andes in Bolivia and Financiera Calpiá in El Salvador (Gonzalez-Vega, 1996), among many others. Domestic apex organizations have rarely provided this vision and the complementary technical assistance.

D.7 Redesigning and upgrading organizational structures

The successful evolution of MFOs requires the adoption of an effective organizational design that privileges sustainability. Domestic apex organizations are not good tools for this task.

- (a) Domestic apex organizations are typically deterred by their own legal status and market position from engaging in the ambitious *redesigning* of the organizational structures of specific MFO clients. Instead, their technical assistance is frequently restricted to demonstrating specific procedures of general interest and to monitoring the evolution of its MFO clients and then offering advice when problems emerge.

Moreover, the effective redesigning of the organizational structure of a MFO may require upgrading the organization to become a regulated financial intermediary. Domestic apex organizations are not good tools for this task either.

- (b) The operations of any apex organization usually create positive and negative incentives for organizational transformation and MFO *upgrading*. While concern about the effects of these incentives should always be one of their important preoccupations, apex organizations do not have comparative advantages in the actual institution-building tasks of redesigning MFOs in response to these incentives to upgrade.

D.8 Compatibility between technology and organization

Moreover, successful implementation of cost-effective lending technologies requires a compatible organizational design. Because domestic apex organizations face severe limitations in drastically influencing the organizational structure of their MFO clients, this also influences their ability to promote the adoption of new lending technologies.

- (a) The testing and adaptation of a new lending technology in a particular market niche takes time. This, in turn, requires a *long-term commitment* by the provider of the institution-building assistance. Donors are unlikely to offer a long-term commitment of any direct presence, but they may be willing to contribute the funds needed for this long-term process. For this purpose, they may be inclined to fund an apex organization, but only a sustainable apex organization will be able to commit to this long-term task. In any case, it more effective to make long-term commitments to particular MFOs rather than to offer long-term assistance to any and all MFOs that may potentially request it.
- (b) Because of political constraints, however, domestic apex organizations usually have difficulties in picking a few *potential winners* and in committing to them over the long term. Instead, they tend to offer non-organization-specific, short-term technical assistance. This may lead to an emphasis on reaching numbers of MFOs rather than on the quality of the organizations. The development of high-quality organizations requires a strong commitment.

D.9 Joint learning-by-doing

Success in the implementation of any lending technology typically results from efficient *learning-by-doing* processes. Domestic apex organizations face severe constraints in this task.

- (a) Microfinance is essentially about the evaluation of risks, the management of information, and the creation of lender-borrower relationships that carry incentives to stay in the relationship. The exact nature of these risks and the precise structures of incentives that sustain these relationships vary from country to country and from market niche to market niche. Accumulation of information on these characteristics by a given MFO occurs gradually, as it learns about its clients, about the markets where they operate, and about potential threats of default. *Canned how-to recipes* are not sufficient, therefore, to learn about how to lend in this market niche. The success of prominent MFOs around the world has ensued only after long processes of learning-by-doing accompanied by interactions with international providers of technical assistance. This interaction requires institutional mechanisms that may not be accessible to domestic apex organizations.
- (b) While useful, the *formal training* on general principles and procedures that most apex organizations can provide can do only part of the institution-building job. Instead, success requires a *continuing* supply of technical assistance and training services offered *in situ*,

through a process of *joint learning-by-doing*, which involves both the provider and the MFO in close relationship. Most of the relevant training takes the form of *apprenticeships* within the MFO itself or at another MFO with a similar organizational structure (*e.g.*, another affiliate of the same network). This is the case even when a domestic apex organization, such as PKSF in Bangladesh, sponsors the training of the staff of smaller NGOs as apprentices at some of the major MFOs in the country (Nagarajan and Gonzalez-Vega, 1998).

D.10 Technical assistance as ownership

Such an intense joint effort requires a strong commitment on the part of both the MFO and the provider of the institution-building services, whose reputation is at risk. Frequently, therefore, the provider of technical assistance becomes a *quasi-owner*, heavily involved in decisions about organizational structure and policies. This heavy involvement is important, because success always relies on a *combination* of consistent and mutually-reinforcing technological, organizational, and policy elements. Moreover, because of its status as quasi-owner, with *reputation capital* at risk, the provider of the technical assistance has strong incentives to perform well.

- (a) The adoption of any one of these combinations of elements (*systems*) frequently implies a *one-on-one* relationship between the provider and the MFO (*e.g.*, Financiera Calpiá and IPC) or the affiliation of the MFO to a network characterized by a strong identity (*e.g.*, Acción Comunitaria del Perú and ACCION International or the Kafo Jiginew in Mali and Freedom from Hunger). Domestic apex organizations cannot easily become quasi-owners.
- (b) Because it must operate as an *umbrella* for the whole sector, it is almost impossible for a domestic apex organization to develop these one-on-one relationships. If, however, the domestic apex organization attempts to promote the expansion of a single, specific microfinance system, then this behavior may stunt innovation in the particular country and the depth of outreach of the chosen system will be narrowly concentrated on a particular clientele.

D.11 Competition

As its market niche becomes saturated, an important dimension of the MFO's strategy is the adoption of policies to keep the preference and loyalty of its clients and to preserve *market share*.

- (a) Market penetration, client retention, and the encouragement of repeat loans become important tasks in the competitive game, and MFOs need to learn how to respond to these competitive threats (Chu, 1998). An apex organization that serves as an umbrella for competing MFOs would find it difficult to advise them in these areas.
- (b) Similarly, the client MFOs may be reluctant to share too much of their private information with the apex organization, for fear that this knowledge will be shared with their com-

petitors. For these reasons, international networks usually cultivate only one affiliate per country. This option is not open to domestic apex organizations.

D.12 Scarce human capital

In small developing countries, where the endowment of *human capital* for the microfinance sector is very limited, employment of the best experts in the market-development tasks of a domestic apex organization comes at the expense of not staffing the retailing MFOs with the best human resources available. This is an important trade-off, since in the end what matters is the development of competent and sustainable capacity at the retailing level. While these competent professionals use their expertise in assisting a number of MFOs on behalf of the apex organization, their efforts would be easily diluted among a large number of clients, as each one of them receives only an insufficient amount of attention. The secret for the success of many provider of technical assistance-MFO connections seems to have been a strong concentration of attention.

In conclusion, in general a *market-development* role involves the generation and extension of microfinance technologies, the redesigning and upgrading of organizational structures, the training of MFO staff, and recommendations on business plans and policies to compete in the target market niche. Successful intervention typically requires that these tasks be undertaken by a provider of institution-building services willing to commit over the long term, as a quasi-owner, to a one-on-one relationship with the MFO for the joint learning-by-doing of the business in the particular environment. Domestic apex organizations are ill-prepared for these tasks.

E. Two Roles in Conflict

Not only are domestic apex organizations usually not well-suited for the requirements of a critical institution-building role, but their financial intermediation role may actually be in **conflict** with their market-development role.

E.1 Disbursement pressures

The simultaneous undertaking of these two roles may create structures of *incompatible incentives* between, on the one hand, the apex organization and government and donors and, on the other hand, the apex organization and its MFO clients. The first source of incompatibility springs from disbursement pressures.

- (a) The main objective of government and donors is usually the rapid disbursement of funds in response to policy (political) goals. To accomplish this objective, government and donors pressure domestic apex organizations to disburse the funds according to a predetermined schedule. To respond to these *disbursement pressures*, apex organizations frequently lower their standards of creditworthiness. This behavior reduces incentives for

MFO improvement, and it conspires against the market-development role of the apex organization.

- (b) The OSU researchers observed that domestic apex organizations that are interested in their own sustainability tend to fight these disbursement pressures. This has been the case, for example, of PKSF in Bangladesh and of ACORDE in Costa Rica (Nagarajan and Gonzalez-Vega, 1998; Quiros and Gonzalez-Vega, 1998). In many cases, however, the incentives to respond to the *short-term* interests of government and donors frequently appear to be stronger than the aspirations of *long-term* sustainability of the apex organization, particularly when replenishment of its funds depends on keeping the donors pleased. When, in contrast, interest in sustainability has resulted in resistance to disbursement pressures, this has reflected, as in the cases above, the leadership of strong personalities with a clear vision about the role of the apex organization.
- (c) Moreover, if, to begin, the number of sustainable MFOs in the country is small, the apex organization typically finds additional reasons to lower its standards of creditworthiness in order to "create" a clientele. This behavior is incompatible with the market-development role of the apex organization.

E.2 Ownership and sustainability

To avoid these conflicts, the apex organization must be strongly *independent* and must be concerned with its own sustainability. Both the (formal and informal) *ownership structure* of the apex organization and the rules for its budget determine its behavior and its choices between rapid disbursement of funds and the pursuit of sustainability.

- (a) Dominant *government ownership* of the apex organization increases political intrusion and disbursement pressures. In this case, the managers of the apex organization are civil servants, and their decisions are supposed to respond to government policies. This has been the case, for example, of the Social Development Fund in Egypt (Baydas and Gonzalez-Vega, 1997) and of several Mexican development banking interventions (Villalpando-Benitez and Gonzalez-Vega, 1998).
- (b) *Per se*, non-government ownership, however, is not sufficient to reduce these pressures. In particular, when the apex organization is dominated by its own clients, these *client-owners* also advocate rapid disbursement and lower standards of creditworthiness.
- (c) The OSU researchers observed disbursement pressures from client-owners in several of the case studies. This threat to sustainability was also documented earlier for the history of credit union federations (Poyo, 1990). Easy access to donor funds through these federations was responsible for the demise of many cooperative systems in Latin America.
- (d) In deposit-taking, client-owned organizations, a strong presence of depositors tends to abate the threat from these conflicts of interests and from insufficient *internal control*.

This was observed by OSU researchers in depositor-oriented credit unions in the Dominican Republic (Poyo, Gonzalez-Vega, and Aguilera, 1993). This potential check is usually not present in most types of domestic apex organizations, which obtain most of their funds from government and donors, rather than from *strategic depositors* or from private investors in capital markets.

- (e) When the apex organizations are NGOs, *property rights* are similarly attenuated, and lack of sufficient *internal control* from a board of directors of non-owners leads to the pursuit of the objective function of the managers, which may or may not include sustainability. In the absence of strong owner control, the preferences of the managers determine the performance of the organization. When the managers earn *efficiency wages* (a more attractive remuneration than in alternative occupations), they tend to favor sustainability, as was observed from Bangladesh to Bolivia.
- (f) Moreover, managers are more interested in sustainability when they face a *fixed budget rule*, as in the case of FUNDA-PRO in Bolivia (Navajas and Schreiner, 1998). Apex organizations that confront a fixed budget rule have in general more reasons to demand disciplined, sustainable performance from their MFO clients than organizations flooded with funds, particularly if the funds are available independently of the performance of the portfolio of the apex organization. The managers of an organization are also interested in sustainability when there is a profit-sharing rule and there are few alternative opportunities for employment as attractive as the current one (Chaves and Gonzalez-Vega, 1996). Even in these cases, however, the solution to the conflict between rapid disbursement and sustainability is not easy.
- (g) Some apex organizations are successful despite their poorly-designed formal ownership structures. These organizations tend to be characterized by strong *informal* ownership. In these cases, the informal quasi-owners are frequently strong leaders interested in sustainability. These unique instances of leadership are not replicable. This is the case, for example, of PKSF in Bangladesh, which is a government-owned apex organization with a strong board of independent personalities and of Friends of Women's World Banking in India, a non-government apex organization with outstanding leaders.

E.3 Economies of scope

This potential conflict between the two roles of an apex organization is paradoxical, because there may be potential advantages (*economies of scope*) from the simultaneous delivery of funds for on-lending and of non-financial services for institution-building:

- (a) First, the apex organization may incur in lower *monitoring costs* as a lender, through the acquisition of information about the borrowing MFOs in the implementation of its technical assistance role. This has been the case, for example, of FondoMicro in the Dominican Republic (Schreiner and Gonzalez-Vega, 1995).

- (b) Second, the threat of loss of the *relationship*, which severs ties both with the lending arm of the apex organization and with its technical assistance services, may increase the incentives that the MFOs have to upgrade their organizational structures and to repay their loans.
- (c) Third, the apex organization may use its own expertise in screening and in monitoring its client MFOs in support of its technical assistance and training services. After all, the apex organization and the MFOs are engaged in the same line of business and both need to overcome similar information and contract enforcement problems in their lending activities.

E.4 Diseconomies of scope

While important, however, these potential advantages of combining the intermediation and the market-development roles of the apex organization may not be sufficient to compensate for some strong disadvantages. The OSU researchers observed that, in practice, the disadvantages tend to dominate the advantages. The disadvantages of combining the two roles of the apex organization are discussed next.

- (a) Experts have almost unanimously recommended the complete *specialization* of MFOs in the supply of financial services (Rhyne and Otero, 1994). The reason for this recommendation has been that the simultaneous provision of financial and non-financial services distracts the MFO's management and staff from the efficient undertaking of what is already a difficult endeavor: producing financial services.
- (b) This recommendation may apply to apex organizations as well, but in some cases it may apply with less grounds for justification than for MFOs generally. One reason is that apex organizations have a small number of clients and lots of unused installed capacity. Problems may emerge, however, from the *structures of incentives* to repay and to collect loans associated with this joint production of financial and non-financial services.

E.5 Incompatible incentives

Thus, the most important drawback in combining the two functions is the potential for conflicts of incentives.

- (a) As described earlier, the most effective forms of institution-building are similar to *partnerships* built on the joint accumulation of a stock of *information capital* by the provider of technical assistance and the MFO. The provider transfers new technologies and organizational designs and at the same time learns about their adaptation to a particular environment. Apex organizations usually find it difficult to engage in this type of arrangements.

- (b) These partnerships imply structures of *risk-sharing* that are not compatible with the terms of loan contracts, which are not *state-contingent contracts*. Loans are supposed to be repaid, independently of the outcome of the borrower's activities: high profits or low profits. Partnerships are based on sharing both profits and losses.
- (c) If the apex organization is seen as a partner, rather than as a pure lender, the repayment behavior of the MFO will be influenced by this perception, and the likelihood of *moral hazard* will increase. In particular, the MFO may find it attractive to behave less prudently, a behavior that may lead to default. Lack of repayment hurts the apex organization, and it teaches the wrong lesson to the borrowing MFOs.
- (d) The *opportunistic behavior* of the MFO is further encouraged if the MFO is asked to take large amounts of loans from the apex organization. When large amounts of credit are used to *persuade* the MFO to accept the technical recommendations of the apex organization, the MFO may find that "it is not really obliged to repay the loans if failure of its own lending activities can be attributed to poor technical advice from its dominant implicit partner." This attitude is also present when the MFOs see the apex organization as a political tool to dispense patronage. Disbursement pressures tend to be a signal of this situation.
- (e) Moreover, anticipation of this less strict obligation to repay lessens diligence and caution on the part of the MFO managers and increases the probability of default.
- (f) Furthermore, a *sine qua non* for institution-building to be effective is the willingness of the MFO to accept the advice of the provider of technical assistance. When the technical assistance is tied to borrowing, it is hard to tell if the MFO wants the advice.
- (g) Similarly, when the apex organization has invested its time and resources in institution-building inputs and when the performance of the apex organization is evaluated by the success of these upgrading tasks, it finds it difficult to strictly insist on repayment when the MFOs fail in their endeavors and when they are in danger of not repaying their loans. *Disclosing* default by the MFOs that it has upgraded would reveal the failure of its own market-development efforts. The apex organization would be inclined, instead, to find excuses and rationales for the inability of the MFOs to service their debt regularly, and it will *reschedule* the loans in arrears or find another way to postpone the day of reckoning. That is, when the two functions are combined, not only do the MFOs have less incentives to repay, but the apex organization also has less incentives to collect. This behavior does not contribute to the market-development role of the apex organization.

E.6 Competitive pressures

In its task of developing the microfinance market, the apex organization must encourage *competition* among the existing MFOs. Competition spurs technological innovation, and it forces

MFOs to supply better quality of services at lower prices. Competition also creates threats for the apex organization.

- (a) Increased competition encourages efficiency but it also increases risks, and it may force some MFOs out of the market. The apex organization faces a dilemma between vigorously encouraging competition and the potential failure of some MFOs due to increased competition. Some of these MFOs may be among its own clients, which cannot survive these competitive pressures. The apex organization possesses few tools to assist in this market-development task.
- (b) The implicit partnership between the domestic apex organization and the MFOs that receive its technical assistance services is not compatible with the need to confront competitors and to develop strategies to defend or increase market shares at the expense of competing financial intermediaries. This *conflict of interests* becomes more acute as the microfinance market matures and the MFOs find themselves competing for the same clients in a particular market niche. Institution-building at this stage requires a *one-on-one* relationship with a provider of technical assistance that can participate in strategic decisions about competing in the market. Competition is difficult but, as the recent Bolivian and Indonesian experiences suggest, competition is also a strong inducement for innovation.

E.7. Upgrading and downscaling

One key assumption of the CGAP-OSU research project has been that there are large unmet demands for financial services (loans and deposit facilities) among poor household-firms in developing countries. Another key assumption has been that the route toward market saturation requires *sustainable retailing capacity* in the supply of microfinance. There is much debate, however, among experts in the field about the best way to achieve sustainable retailing capacity.

Many experts remark that the NGO experiments will have little chance of becoming sustainable, given major shortcomings in their property rights and *governance* structures. Asymmetric information about their creditworthiness and the value of their loan portfolios may reduce their ability to borrow on commercial terms. Lack of owner control may, in turn, keep private investors away from contributing to the capitalization of MFOs. Increasing numbers of experts foresee the future of microfinance in the hands of regular financial intermediaries. The potential *commercialization* of microfinance will have major consequences on the role of domestic apex organizations and their prospects for success.

There are, therefore, two alternative routes toward building sustainable retailing capacity for microfinance. One is a process of *upgrading* existing MFOs. Several NGOs have been appropriate mechanisms for flexible, albeit subsidized, experimentation in lending technologies. They have earned their subsidy by creating the public good of the new microlending technologies. Several have evolved to the point where they can follow the steps of BancoSol and Financiera Calpiá, among others, to become regulated financial intermediaries. Most of the discussion so

far in this paper has focused on the role of domestic apex organizations in this process of upgrading MFOs. Many of the challenges faced by these organizations emerge, nevertheless, from the weaknesses of this type of clientele.

A multitude of subsidy-dependent, unsustainable MFOs will never have the opportunity to upgrade. They lack the vision and the commitment needed for sustainability and, given their ownership structures, better-qualified quasi-owners will not be interested or will not be able to take over the organization. In fact, by not operating on market terms, they tend to become a *barrier* to the *entry* of commercial providers and thereby help stunt private innovation.

The alternative route is a process of *downscaling* the operations of regulated financial intermediaries to the target market niche. The challenge here is the adoption of an appropriate lending technology by a banking institution. This is not a trivial task (Baydas, Graham, and Valenzuela, 1997). On the one hand, the regulated intermediary possess a well-defined property rights and governance structure, internal control mechanisms are in place, and the fixed costs of organizational development are sunk. Moreover, financial intermediaries are subject to a well-defined prudential regulation and supervision framework, and they engage in active deposit mobilization. On the other hand, features of the new lending technologies are not easily compatible with the corporate culture of banks and there is, in general, less commitment to the mission of reaching the target market niche.

A domestic apex organization faces a very different challenge in a downscaling exercise. Once the regulated financial intermediary declares its intention to serve this market niche, the apex organization does not have to worry about sustainability *per se*. There are generally accepted criteria for the evaluation of the sustainability of regulated financial intermediaries and the required data are available from the prudential supervisor. All the apex organization has to do is to verify some eligibility criteria that demand sustainability. The apex organization can then focus on the transfer of microlending technologies and on monitoring its lines of credit for the client.

It is not surprising, therefore, that when the *willingness* to serve the microfinance market niche exists, the operations of a domestic apex organization that facilitates this process are frequently successful. This has been the experience with a few Micro Global Loans of the Inter-American Development Bank.

A domestic apex organization may face, however, two types of problems in these downscaling interventions. First, commercial banks and other regulated financial intermediaries may still be reluctant to operate in this market niche because of limited profitability, given their own banking technologies. Bankers need to be persuaded that adoption of the new lending technologies will increase the profitability of these operations sufficiently. If they are not, the resources of the domestic apex organization will remain untouched, as illustrated by several other Micro Global loans from the InterAmerican Development Bank (Taborga and Wenner, 1997).

Second, the apex organization may have a more serious screening and monitoring task when the eligible regulated financial intermediaries are not banks but *financieras*, credit unions, *fondos financieros privados* and other non-bank intermediaries. In this case, the *certification* implicit in their regulated status is not sufficient guarantee that these MFOs are sustainable. The apex organization faces, in this case, challenges similar to those faced in an upgrading exercise.

V

Lessons from the Case Studies

A. Methodology

The CGAP-OSU research project has attempted to derive lessons about conditions favorable to the promotion of sustainable microfinance from the experience of a few domestic apex organizations in several countries. These experiences have been recorded through a review of the literature, a survey, and several case studies. This section reports some results from nine case studies prepared after a brief visit by an OSU researcher to the apex organization.⁶

The challenge has been to generate robust lessons from a very small sample, characterized by tremendous diversity. Not only is the number of existing apex organizations small and their institutional design diverse, but the performance of specific apex organizations seems to be highly dependent on local *sui generis* circumstances. This makes both any generalizations from the empirical observations difficult and any recommendations about replication of a single success story unwise. While this section attempts, therefore, to identify elements of success or of failure that appear frequently or that are consistent with the conceptual framework, it also attempts to highlight the special circumstances that may explain success in each particular case.

The challenge is great, given the possibility of self-selection. A *self-selection bias* would emerge if the organizations that were willing to participate in the study are perceived as success stories, while those that are already encountering problems were not willing to participate. The danger is that the researchers would then observe exceptions, where special factors have allowed the organizations to overcome the weaknesses of a generally unsatisfactory approach or where consequences of their shortcomings are not yet evident.

The apex organizations visited are characterized, in general, by competent and highly-motivated staff, who are making their best effort to pursue the goals of the organization, frequently within fairly unfavorable environments. Sometimes their efforts are not sufficiently rewarded, however, because the institutional design imposed by the specific donor is weak or because the market is too small. In several notable cases, the sad feeling is that the outstanding human resources employed by the apex organization would have the capacity to make even more substantial contributions to the development of their country.

Thus, the *cost-benefit* outcome of many of these observations tends not to be favorable, even in these special cases, particularly when costs and benefits are measured from the creation of the organization. Because the high costs associated with that creation are already sunk, today some of them represent valuable social interventions, but this is not even the case where the market for their operations is too small or where they are politically vulnerable.

⁶ The short duration of the visits limits the scope of the observation. The case studies should not be seen as thorough evaluations of these organizations, but only as opportunities to derive lessons of general interest from the experiences of these organizations.

B. Bangladesh: PKSF as a Role Model

The *Palli Karma Sahayak Foundation* (PKSF), a domestic apex organization owned by the Government of Bangladesh, is one of the best of its kind in the world (Nagarajan and Gonzalez-Vega, 1998). It operates in an environment dominated by the Grameen Bank and other prominent MFOs, including BRAC, ASA, and Proshika. It is, therefore, an example of a domestic apex organization that functions in a large, quite advanced microfinance market, with sustainable industry leaders and a fringe of smaller MFOs that represent its target clientele. This is indeed one of the conditions for success identified by the CGAP-OSU study.

The huge size of the microfinance market in densely populated Bangladesh, where legitimate excess demands for financial services among the population below the poverty line still prevail, should be underscored. In this market, the Grameen Bank is the only significant formal source of microcredit, but large numbers of NGOs engage in microfinance. Among more than 4,000 NGOs with some financial activities, about 450 are specialized in microfinance and about 300-350 are potentially sustainable. About 1,300 new NGOs applied to PKSF for loans, about 500 were appraised, and 162 have received PKSF loans over the past seven years.

In contrast to the large, well-known NGOs, most of these MFOs are very small. Based on local initiatives, they operate in an environment characterized by a large pool of young, educated, strongly motivated people who are willing to be recruited at comparatively low pay as the staff of these NGOs. This deep stock of human capital separates Bangladesh from many developing countries where, in the absence of these conditions, replication would be difficult.

Many of these small NGOs disburse loans quickly and collect on them effectively. Despite these favorable conditions, however, not all of them have the willingness and the ability to manage sustainable microfinance. Most depend on external funds for their growth and on heavy technical support from the donors. In contrast, the large NGOs are much older, have professional management, possess abundant internal funds, and enjoy direct access to external funds.

Although PKSF is the only apex organization of its kind in Bangladesh, several large NGOs (ASA, BRAC, Proshika) function as *mini-apex mechanisms* and nurture small MFOs that emulate their lending technologies. The large NGOs wholesale funds and assist in the institution-building of small MFOs that are not typically candidates for PKSF funding, but that the large NGOs may be able to monitor well. Although apparently successful replications of Grameen Bank and ASA have been observed, other experiences suggest that replication is not always easy.

The role of large NGOs as mini-apex mechanisms has been a reaction to the high costs and risks of further expanding their vast networks. They have pulled out of risky areas, in response to failures there, and the medium and small NGOs are expected to cover the areas that they do not want to penetrate. It is in this environment that PKSF is expected to play a role in building up the *sustainable* retailing capacity of the medium and small MFOs, with technical assistance (market-development function) and loanable funds (intermediation function). PKSF is expected to promote a more competitive market niche and assist in increasing the depth of outreach of the microfinance sector. The vision of taking advantage of existing economic opportunities for the poor rather than on welfare-oriented relief contributes to its sustainability.

PKSF was created in 1990, after the fall of the military government, in an effort to develop a local capacity (talent and funds) for implementation of microfinance programs which would, in turn, serve to attract foreign donor funds. This strategy has been successful. Funding for PKSF has come from the Government, USAID, and a highly concessionary loan from IDA.

As IDA conditionality, PKSF was asked to earmark one-half of the loan funds for the large NGOs. On the one hand, because these NGOs have been successful in attracting donor funds based on their own performance and status, the *additionality* of this new task is questionable. Also, the new role may shift the focus of PKSF away from promoting greater depth of outreach. On the other hand, it may generate economies of scale for PKSF, and contact with the large MFOs has been a source of knowledge on best practices and market features for the apex organization. This *demonstration effect* could spill over, in turn, to the small NGOs.

PKSF is an example, therefore, of a domestic apex organization working in a very large market, where *economies of scale* may be important, and where lending technologies already adapted to the environment can be disseminated by the apex organization with the assistance of the same MFOs responsible for the innovations. Indeed, PKSF has successfully sought the collaboration of the Grameen Bank and other large NGOs for its training activities.

Moreover, neither the government nor the donors were heavily involved in the initial efforts to create a microfinance sector in Bangladesh. The initiatives leading to the creation of the Grameen Bank, ASA, BRAC, and Proshika were genuinely local, and the role of bilateral donors was eventually limited to funding their activities, without the assistance of a domestic apex organization. Over the years, financed by these liberal donor funds, the local organizations engaged in systematic *learning processes*, which have resulted in the development of new lending technologies. While no domestic apex organization played any role in the learning stages of microfinance in Bangladesh, however, now that a well-developed market exists, one may still play a useful role in the dissemination and adoption of these tested lending technologies.⁷

Although owned by the Government, PKSF is fairly *autonomous* and, so far, it has been able to fend off the political intrusions that are a threat to many domestic apex organizations. Several features incorporated in the *governance* structure of PKSF to minimize its vulnerability to political influences would not be sufficient *per se* to avoid this threat. Rather, while control is in the hands of government and microfinance-sector representatives, in practice the independence of PKSF has reflected the personal standing of its board members. Prominent board members, including Dr. Mohammed Yunus, have been a remarkable safeguard against the implicit weaknesses of the governance and ownership structures of PKSF. Domestic apex organizations in other developing countries may not be able to recruit such capable, honest and dedicated leaders. This clearly represents one among several major obstacles to replication of this experience.

⁷ Although it is also a domestic initiative, PKSF emerged after recommendations from The World Bank. Thus, it is not clear if it emerged to respond to the demands of existing MFOs or to respond to operating constraints on World Bank interventions in Bangladesh.

PKSF employs 98 people, of whom 49 work in credit activities. *Compatible incentives* appear to motivate the staff of the organization. The professional staff must have a Master's degree with first-class grades and are recruited through a rigorous selection process. They are typically at the start of their professional careers and are trained within PKSF, the Grameen Bank and other NGOs. Their salaries are higher than those paid to regular government employees and the staff of large NGOs. These high salaries encourage the staff to value sustainability.

PKSF uses the microfinance technology developed by the Grameen Bank to screen applicants for *partner organization* status. Selection criteria assess the MFO's organizational structure, reputation of the organizer, management quality, staff capacity and efficiency, area of operation (landless and assetless clients), past performance, and management information system (MIS). The MFO must have at least 400 clients, organized in groups, who practice regular savings for at least six months. All the time, the MFO must maintain a minimum recovery rate of 98 percent of amounts due (95 percent after three years of operation).⁸ Assessment takes about three months. These requirements reflect PKSF's mission to work with sustainable MFOs.

Only a small proportion of applicants are accepted for partnership. Between 1990 and mid-1997, the *acceptance rate* was only 13 percent of all applications. Up to mid-1996, 1,005 MFOs had applied for loans; of these, 438 had been rejected *ad portas*, 567 had been accepted for preliminary appraisal, and 399 had been actually appraised. Of these, 168 had been asked to provide further information, and 126 had been accepted for loans. During the following year, 245 new MFOs applied for loans and 36 received them. A low ratio of loans to assets and a low acceptance rate reflect the conservative approach of PKSF, unusual for a domestic apex organization. The low acceptance rate also suggests that there are large numbers of unsustainable MFOs in Bangladesh. This increases screening costs and the risk of mistakes, but understanding how difficult access is creates incentives for partners to protect their relationship with PKSF.

The interest rate charged increases, from 3 to 5 percent per year, with the size of the MFO, and it thus ignores the higher costs and risks of lending to the smaller NGOs. The initial loan is Tk. 100,000 in all cases, even for the large NGOs. Repeat loans depend on both demand and the performance of the MFO. The partner organizations are made aware that PKSF is a government agency and that default will provoke legal action leading to the closing of the MFO. The success of PKSF must be associated, however, with an image that goes beyond the government's stamp, because government affiliation usually weakens the enforcement of contracts, as is the case with the development banks of Bangladesh. What matters is a signal, reinforced by actual experience, of the intention to enforce contracts coupled with the expectation of continued access to quality services.

The intensive training services of PKSF seem to have been valuable and relevant for the partner organizations. As elsewhere, the microfinance sector of Bangladesh has evolved through learning-by-doing rather than formal training. *Apprenticeships* and continuing mentoring by the larger MFOs are found by the new MFOs to be more helpful than formal training modules.

⁸ Despite the emphasis placed by PKSF on management information systems, the available quantitative information about its operations is thin.

The number of MFOs reached by PKSF increased from 23 in 1990 to 162 in 1997. Because 10 MFOs were dropped in 1997 due to non-performance, the current clientele amounts to 152 MFOs. This is a substantial market. The Board, however, intends to reach 200 MFOs in five years, and then hold this number constant to ensure good quality of service. This conservative attitude reveals an interest in protecting the sustainability of the apex organization.

In turn, the volume of loans disbursed by PKSF increased from Tk. 3 million in 1990 to Tk. 1,620 million in 1997. While the share of PKSF's small partner organizations in the total number of borrowers served by MFOs in Bangladesh was 6.2 percent in 1995, their share in the total volume of funds was 3.2 percent. Thus, PKSF's outreach was important but not dominant.

Recently, operations with the large NGOs have increased the share of PKSF's partner organizations in the microfinance sector of Bangladesh, but their outreach can be hardly attributed to PKSF, and the burden of dealing with the large NGOs may in part explain the desire to set the 200 MFOs ceiling. Moreover, these operations have increased the concentration of PKSF's portfolio and the risk of its operations. Thus, risk-taking was shifted from IDA to PKSF, which is assumed to have a comparative advantage in monitoring the large NGOs.

In summary, while the *additionality* of PKSF funds in expanding the microfinance sector of Bangladesh has been important but not decisive, given the prominence of the already-existing players in the market, it seems to be quite substantial in the case of the small MFOs. Among the partner organizations, 132 reach less than 5,000 clients each. The majority of these clients are women. If these small MFOs reach poorer segments of the population, in remote areas, the most important contribution of PKSF would be a greater *depth* of potentially sustainable outreach.

From an accounting perspective, PKSF has recorded positive net profits since inception. This has resulted primarily from interest earnings from investments, not from the loan portfolio. This has been made possible by holding a high proportion of assets as investments rather than as loans. This is a luxury that few apex organizations can afford, but it does reflect PKSF's ability to avoid *disbursement pressures*. The bias in asset holdings is large: the share of loans in total assets increased only from 29 percent in 1993 to 59 percent in 1996.

Interest income from loans, however, has not been sufficient to cover operating expenses except in 1997. *Operational sustainability* has been improving with the larger volume of loans, nevertheless, as income from loans as a proportion of total operating expenditures increased from 4 percent in 1992 to 118 percent in 1997. It took seven years to reach this status. Among the sources of this improvement, the addition of the large NGOs as partner organizations has bolstered interest earnings.

Furthermore, the inability to service its debt at commercial interest rates has reduced the capability of PKSF to raise funds from the public, perpetuating its dependency on subsidized donor funds. To be able to raise funds, PKSF would have to charge 8-9 percent rather than 3-5 percent per year to its partner organizations. At present, however, it has been predicted that PKSF will be able to raise funds from commercial sources by the year 2006. The leaders of the apex organization claim to be committed to achieving the economic sustainability needed for this.

PKSF is a comparatively successful domestic apex organization. It has been recommended as a role model for apex organizations in Bangladesh and in other developing countries. Several specially favorable conditions explain this success, however, which may not be replicable elsewhere:

- (a) First, PKSF operates in a large, advanced microfinance market, where several leading MFOs have developed and adapted effective lending technologies and are directly involved in disseminating them.
- (b) Second, because PKSF has had access to abundant funds, it can keep most of them as investments rather than as loans to MFOs. This asset structure curbs disbursement pressures and generates income to cover costs.
- (c) Third, PKSF has had access to a large pool of cheap, well-educated human resources appropriate for its labor-intensive operations.
- (d) Fourth, PKSF has operated in an environment characterized by a supportive but not interventionist government. This, combined with the exceptional standing of its board members, has guaranteed independence from political pressures despite government ownership.
- (e) The leaders of the organization have been primarily concerned with its own sustainability and, in consequence, with the sustainability of the MFO clients.

C. India: Friends of Women's World Banking and Competing Apex Organizations

The apex mechanism *Friends of Women's World Banking* (FWWB) has been operating as a non-government organization (NGO) in India since 1989 (Nagarajan, 1998). This is also a large market, where competing apex organizations offer wholesaling and training services to a multitude of unsustainable MFOs. It is a less favorable environment for success.

On the demand side, it is a huge, under-serviced market. On the supply side, this is an environment characterized by numerous MFOs and by vast networks of financial cooperatives and commercial banks. Thus, FWWB's clientele of 69 NGOs, cooperatives, and self-help groups (SHGs) is a minuscule drop in this ample ocean of financial organizations. Moreover, for more than four decades, the Government of India has been active in supplying credit to the poor at subsidized interest rates through 36 nationalized commercial banks and regional rural banks. This active role of the Government is in contrast with Bangladesh, where the Government has been supportive but not as interventionist in microfinance activities as in India. The National Bank for Agriculture and Rural Development (NABARD) and the Reserve Bank of India offer, in turn, (apex) refinancing facilities to the commercial banks that reach MFOs and SHGs.

Anecdotal evidence suggests that there are more than 100,000 NGOs in India, of which about 10,000 provide financial services. Only 20 to 30 NGOs can be considered, however, as potentially sustainable and their outreach is minimal. Among these, the Self-Employed Women's Association (SEWA) was created in 1972 as a trade union by 4,000 poor women in Ahmedabad, in an effort to improve their access to formal financial services. The association became a bank managed by its members in 1974, and by 1996 the bank had 14,000 women shareholders, 30,000 depositors, and an outstanding repayment rate of 98 percent of amounts due. This experience has been successfully replicated in urban areas of Gujarat, but replication has encountered severe difficulties elsewhere. Once again, the challenges to *replication* have been evident.

Several apex organizations offer their services to banks, NGOs, and SHGs. NABARD, created in 1979 as a wholesaler for banks and regional rural banks that lend for agriculture and rural development, has recently redirected its efforts to microfinance. NABARD launched a project for linking SHGs to banks in 1992. By 1996, 5,850 SHGs had been linked to 28 commercial banks, 60 regional rural banks, and 7 cooperative banks through 130 NGOs. Of the Rs. 78 million disbursed, Rs. 70 million had been refinanced by NABARD. In Gujarat, where FWWB headquarters are located, the linkage program had reached 337 SHGs. NABARD even finances FWWB for on-lending to NGOs and SHGs and with training grants. Its outreach and sustainability accomplishments are modest at best.

Rashtriya Mahila Kosh (National Trust Fund for Women) is a government-owned apex organization created in 1992 under the Ministry of Women and Child Welfare and with initial funding from The World Bank. It wholesales funds for NGOs active in microfinance. There are claims that, after obtaining the guidelines for client selection and lists of FWWB clients, it began lending to FWWB clients at subsidized interest rates. This is an example of the conflicts that can emerge from *competition* among several apex organizations that do not operate on market terms. FWWB has been eager to increase its interest rates from 12 to 15 percent per year to cover its costs, but it finds it difficult to compete with NABARD, the financing of cooperatives by the Small Industries Development Bank of India, and the *Rashtriya Mahila Kosh*, all of which charge lower interest rates. On the balance, the Government's own microfinance apex may be doing more harm than good.

In addition, some prominent NGOs, such as PRADHAN, MYRADA, SEWA, and ASA have been promoting federations of SHGs that access and manage external funds and supply loans to members of the SHGs. They pool the resources of several SHGs, guarantee bank loans to SHGs, lobby on behalf of their members, and engage in institution-building activities. Although these are typical functions of apex organizations, their outreach is limited. They typically reach about 1,000 to 3,000 members. They are highly dependent of the parent NGO and are not sustainable.

Despite the multiplicity and variegation of suppliers of microfinance in India, therefore, most efforts are not sustainable and their outreach has been modest at best. It is in this environment that FWWB was created in 1982, as an affiliate of Women's World Banking (WWB), primarily to operate as a credit guarantee fund. Despite the guarantees, FWWB was able to convince only one bank to open a special window for poor women. Few guarantees were issued and the fund was inactive for several years. In 1989, the guarantee fund was transformed into an apex organization.

FWWB was patterned after the success of the SEWA Bank. While the SEWA Bank, as an urban cooperative bank, was restricted in its area of operations by the Banking Law, FWWB could operate on a national scale. Ms. Ela Bhatt, founding member of WWB and Managing Director of SEWA, was instrumental in these efforts. She is another example of the role of strong *leadership* in explaining the success of specific organizations. In contrast to other Indian organizations that lacked access to knowledge on best practices, Ms. Bhatt offered SEWA and FWWB a link to the ample network of WWB and the rest of the world. One outcome of her leadership has been a concern with sustainability.

Moreover, this non-government apex organization is controlled by a Board of Trustees appointed by invitation. Trustees include representatives of SEWA and of other prominent NGOs working with women (MYRADA, SAMAKHYA, ASTHA, ASSEFA, Gram Vikas) as well as microfinance experts, all with long experience. Deficiencies of organizational design are then compensated by the personal attributes of the trustees. This raises questions, however, about successful replication.

The mission of FWWB is the empowerment of poor, assetless, unskilled, rural women by improving their participation in income-generating activities through access to financial services. The majority of the funds are mobilized from local Indian sources, including NABARD and other government programs. Early experiments in channeling funds to SHGs in Bihar and Orissa, the poorest states in India, failed due to the weak retailing capacity of the local MFOs. After these failures, FWWB decided to channel institution-building services only where existing retailing capacity is weak. FWWB also learnt that, despite the huge demand for credit, NGOs and SHGs require a lot of institution-building efforts before the supply of credit can be expanded. In 1992, FWWB adopted a systematic training program designed by World Education to strengthen NGOs and SHGs. In contrast to the training activities sponsored by PKSF, this training curriculum consists of modules on organization and management rather than the *on-the-job learning* adopted by the former organization.

The gender orientation is clear. FWWB wholesales funds (intermediation function) and training services (market development function) to women's organizations that offer microfinance services to poor women. A staff of 12 people are responsible for credit, training, and research activities. The mandate of FWWB limits the appointment to key staff positions to only women. These staff are well-qualified with college (BA or MA) degrees and must be able and willing to deal with culturally and linguistically diverse clients. Loans go to women only. Beyond gender, however, there is no other form of targeting, and the partner MFOs are allowed to operate on their own terms and conditions. A strong emphasis is placed, however, on member savings. This flexibility has responded to the heterogeneity of the environment where FWWB operate.

The clients of this apex organization are diverse, ranging from SHGs (58) and NGOs (1) to cooperatives (10) and federations of SHGs. Fairly elaborate loan applications are evaluated by loan officers and considered by a credit committee that includes the Chief Executive Officer of FWWB, the general manager of the local NABARD office, some trustees, and loan officers. Screening and monitoring of these MFOs is extremely difficult. Few of them have access to electricity and, thereby, computers. Frequent staff turnover reflects salaries well-below market rates. Accounting systems are diverse and SHG heterogeneity enormous. The acceptance rate has increased from 10 to 60 percent of applicants. The process takes from 3 to 5 months.

At present, FWWB has 69 MFO clients from a total of some 110 reached at some point during the past eight years. The number of new loans to MFOs increased from 4 in 1989 to 31 by 1997, while the volume of loans increased from Rs.150,000 to Rs. 13.6 million in the same period.⁹

⁹ A less-than-adequate MIS is in place, and available information is shallow.

Of the 164 loans made since 1989, 86 are still outstanding. The portfolio outstanding is Rs. 35 million (about one million dollars). On average, terms to maturity are three years. The MFO clients are located in 8 of the 23 Indian states. The costs of these attempts to gain national outreach are not trivial. These MFOs are small and work, on average, with 260 borrowers. The SHGs, in particular, are small groups of 20 to 50 women, mostly in rural areas. Many are not sustainable.

The cumulative number of ultimate borrowers reached by FWFB clients is 50,576, of which 17,985 were being reached by these MFOs in 1997. Compared to the outreach of major MFOs such as SEWA, MYRADA, and PRADHAN (around 20,000 each), the indirect outreach of FWFB is not inconsequential. Compared to the size of the Indian market, it is insignificant. Therefore, while its operations are clearly important for its clients, as a mechanism to promote the development of microfinance all over India, FWFB is not successful.

Since 1989, FWFB conducted 6 to 8 training programs per year and reached about 1,500 women leaders of SHGs (group management, record, portfolio management) and 300 NGOs (financial management, group organization, strategic planning). In 1996, 15 training programs reached 355 participants. No fees are charged.

Total accounting income exceeded total accounting expenses for the first time in 1997.¹⁰ The income to expenses ratio increased from 91 percent in 1996 to 103 percent in 1997. Interest earnings on loans accounted for two-thirds of total income. These earnings were equivalent to 67 percent of total expenses in 1997 and they were equivalent to 380 percent of monitoring and training costs, staff salaries, and bad-debt losses. These earnings were used, however, to build up the core fund, since operating expenses are fully met by donor grants. FWFB claims that it could become *subsidy-independent* if it increased its interest rates from 12 to 15 percent per year, but in claiming this it may be ignoring important subsidies.

Repayment rates have been modestly successful and many loans will not become due until 1999. MFO payments of interest and principal are made before 30 days after due dates about 85 percent of the time. FWFB has never written a loan off, however, but it has rescheduled a few loans. The apex organization does not have a clear provisioning rule for losses, and it considers that, in the distressed areas where it operates, an 85-percent recovery is reasonable. While this may be the case, its interest rates do not reflect this fact. Moreover, of the six unpaid loans outstanding by 1997, five were in Gujarat (out of a total of 25 in this state), where presumably FWFB has information advantages. In four cases, no single payment had been made. This may reflect pressures to disburse in Gujarat, but it also signals potential difficulties as loans granted in remote locations become due.

The Indian landscape is dominated by numerous government interventions to supply financial services to the poor through competing apex organizations. Among them, FWFB has been more concerned with sustainability than the others, and its record of success is modest.

¹⁰ These figures have not been properly verified and adjusted and are presented here for illustration purposes only.

D. Benin: The PADME/Financial Bank/AFRICARE Connections

The *Projet d'Appui au Développement des Micro Entreprises* (PADME) in Benin is an example of a comparatively successful retailing microfinance organization pushed by donors to undertake domestic apex responsibilities without being prepared for this task (Ouattara and Gonzalez-Vega, 1998). Moreover, the case study illustrates the difficulties of promoting microfinance in countries with dispersed, low-income, rural populations vulnerable to major exogenous shocks.

This is not a unique situation.¹¹ Several comparatively successful MFOs have been asked by donors to play the role of apex mechanisms, in recognition both of their relative strengths and of the difficulties of creating new institutions in many developing countries. The outcome has seldom been successful. The new responsibilities tend to overload the organization and the *dual role* creates a tension between the wholesaling and the retailing functions. In some cases, such as K-REP in Kenya, the apex activities of the organization are eventually abandoned.

Although per capita income in Benin is slightly higher than in Bangladesh, Benin is still one of the poorest countries in the world, and population density is very low. Moreover, a poorly-educated population shrinks the pool of human resources available to staff MFOs, while a limited physical and institutional infrastructure constrains productive opportunities for their clients. In this environment, demands for financial services emerge mostly from the trading and service sectors. To respond to these demands, financial markets are rudimentary and fragmented. Microfinance in Benin remains the domain of credit unions, specific donor programs, and NGOs, while the informal finance of *tontines*, moneylenders and moneykeepers thrives.

About 20 local NGOs have provided financial services to the poor in Benin, mostly as a complement to their non-financial services. Most exhibit a crucial lack of capacity to engage in financial intermediation. Fewer than five specialize in microfinance; the market for any domestic apex organization is thus very thin.

PADME is a special donor program, created in 1993 by a World Bank initiative within a structural adjustment package, to mitigate the social costs of laying off government employees. In general, credit programs created for specific clienteles to compensate them for the negative effects of policy reforms or other exogenous events encounter great difficulties in enforcing contracts, cannot focus on the evaluation of creditworthiness (rather than the entitlement), and experience high arrears rates. PADME escaped this fate by rapidly expanding to include all types of microentrepreneurs.

PADME has gone through several phases. During a pilot phase, until 1995, PADME was managed with technical assistance from VITA, an American NGO. After a consolidation phase, in mid-1996 an institutionalization phase followed, which was completed at the end of 1997, when PADME became a private, voluntary, not-for-profit organization under the name of *Association pour la Promotion et l'Appui aux Micro Entreprises*.

¹¹ This evolution from retailing to wholesaling functions is in contrast, however, with the more frequent evolution from wholesaling to retailing functions examined below.

Prior to this transformation, PADME had been part of a government program (*Project d'Assistance aux Entreprises*) under the direct supervision of the Ministry of Planning, Economic Restructuring, and Employment. Except for the oversight of the Ministry, PADME was free in hiring its staff and carrying out its mission. Although the *transformation* into NGO is expected to take away much of the threat of political intrusion, inadequate *internal control* still may follow from the attenuated property rights characteristic of any NGO.

PADME started with five employees, and it received technical assistance from VITA until August 1995, when it was handed over to a Beninese staff. By December 1997, it had 32 employees. As an *incentive* for diligently screening and monitoring clients, 13 loan officers receive a yearly bonus equal to 5 percent of the amount of loans granted and recovered by the officer.

To be eligible for its first-tier loans, clients must have an enterprise in operation, located in the urban and peri-urban areas where PADME operates. The enterprise's loan demand should not exceed CFAF 2 million (US\$ 4,000), while minimum loan amount is CFAF 2,000 (US\$ 40). Borrowers are required to attend a four-hour workshop on microenterprise management every time they get a loan. The maximum term to maturity of the loans is one year, to be paid in monthly installments. A 10-percent forced savings requirement is used for a guarantee fund.

By 1997, PADME had a portfolio of CFAF 2.8 billion (US\$ 5.6 million) and had granted an accumulated 7,145 loans to 4,599 clients since inception. This represents about 3 percent of the estimated microenterprise clientele of Cotonou and Porto Novo, places where PADME faces little competition. Breadth and depth of outreach are not impressive. This suggests, however, that there is scope for expansion of PADME's first-tier activities before it tackles the apex level.

All loan transactions are handled by the Financial Bank, PADME's long-time commercial bank partner. The bank has offered PADME special windows at its branches, and transactions with PADME's clients account for one-third of the bank's cash transactions. The partnership with PADME allows the bank to become familiar with microentrepreneurs who are potential clients, whom may eventually graduate to the bank's own operations. This is thus a cost-minimizing *downscaling* exercise for the bank. In the meantime, PADME offers better service to its clients but, because it also bears all credit risk, the screening and monitoring of clients are undertaken by its own loan officers. This partnership, however, allows PADME to economize on the costs of setting up branches, and the connection is reassuring for its clients.

In general, *partnerships* with formal financial institutions represent alternatives to access to domestic apex organizations. The PADME-Financial Bank partnership seems to be cost-effective, and the potential synergies are many. It will be worthwhile to observe the evolution of this partnership as an alternative model to domestic apex organizations, particularly if deposit mobilization is brought into the arrangement.

PADME's original mission to supply loans and technical assistance in Cotonou, where laid-off government employees reside, was rapidly expanded to all urban microentrepreneurs. The combination of credit and technical assistance services offered at the retail level already stretched the limited managerial resources of this MFO. The addition of apex functions through the relationship with AFRICARE stretched them further.

AFRICARE is an American NGO that works in 28 African countries. In Benin, its mission was to help local NGOs develop more effective, accountable, and participatory structures. In 1994 it was awarded USAID's *Benin NGO Strengthening Program* (BINGOS). The goal of this project was to improve the capacity of local NGOs to become effective development tools. A grant to VITA allowed PADME to initiate its apex activities by providing technical assistance in credit technology and by wholesaling loans to local NGOs.

Potential conflicts between PADME and its NGO clients were resolved by a division of labor that reserved the urban clients for PADME and left the rural clients to be reached by the NGOs alone. Because very few NGOs offered financial services only and most did not have much experience in credit delivery, PADME was pushed into dealing with unsustainable NGOs. In some cases, the NGO's only knowledge about microlending came from attending PADME's courses. In 1996, the only year when PADME made loans to NGOs, seven organizations received loans ranging from CFAF 600,000 to CFAF 3 million. These loans reached over 500 borrowers in the rural areas. While this increased the depth of outreach of PADME, which had not entered the rural areas, it affected its breadth of outreach minimally. Once VITA turned over the PADME operation to local management, the apex functions were put on hold.

In summary, growth of PADME's retailing operations has been substantial, and the organization has built a solid reputation. With only one percent of its loans in arrears, operating expenses at 20 percent of its loan portfolio, and a ratio of revenues to operating expenses of 174 percent, PADME's future as a *retailing* MFO seems promising. Its short-lived experience as an apex organization, in contrast, contributed little to building sustainable retailing capacity in Benin.

The PADME experience suggests the *lesson* that in low-income countries with limited human capital and institutional structures, most donor and government efforts should focus on improving a few promising retailing MFOs, such as PADME, and not on the creation of domestic apex organizations that draw scarce resources away from the first-tier of retailing operations in order to serve a thin MFO market.

In Benin, the CGAP-OSU research project also examined the operations of the *Fédération des Caisses d'Épargne et de Crédit Mutuel* (FECECAM), an apex organization created in 1993 for the largest credit union network in West Africa. Credit unions dominate microfinance in Benin as a result of a rehabilitation program started in 1990, after the collapse of the banking sector and of the former apex organization, the *Caisse Nationale de Crédit Agricole* (CNCA). By 1997, FECECAM oversaw a network of seven *Unions Régionales* and 82 *Caisses Locales de Crédit Agricole Mutuel*, with a membership of 210,651 shareholders, US\$ 35.4 million in deposits, and \$ 24.2 million in outstanding loans to 69,359 borrowers (Fruman, 1997).

This type of apex organizations has been examined elsewhere. FECECAM shows the typical strengths of savings-led interventions and the weaknesses of client-owned organizations. The latter are reflected at FECECAM in power struggles between paid staff and elected board members. Despite these problems, the network has grown rapidly, to reach 15 percent of the working rural population of Benin. The network was second only to the largest bank of Benin in terms of deposit mobilization.

E. Mexico: A Country in Search of a Microfinance Sector

The Mexican case has been rich in experiences about the effects of government intervention in financial markets (Villalpando-Benitez and Gonzalez-Vega, 1998). In this sense, Mexico is similar to India. Domestic apex organizations have been among a number of policy instruments used to promote the supply of targeted and subsidized credit for priority activities. The microfinance sector, however, is less advanced in Mexico than in other Latin American countries, in part as a consequence of misguided government intervention in financial markets. A few promising MFOs, nevertheless, have grown without the assistance of any of the numerous apex organizations that have recently attempted to promote credit for the poor in Mexico.

Among a number of apex organizations established to promote loans for particular sectors of the economy through the rediscount of private bank loans, known as *Fondos*, for 30 years the *Fondo de Garantía para la Pequeña y Mediana Industria* (FOGAIN) directed some credit toward small and microenterprises. The effects of this intervention were marginal; emphasis was placed on employment-creation and available funds were directed to medium-size and large firms.

With the policy reforms initiated in the mid-1980s, apex organizations have been chosen as the main instruments of public action in financial markets, while the *retailing* role of the state-owned banks has been minimized. In this sense, apex organizations have been an intermediate step in the withdrawal of the Mexican government from direct intervention in financial markets. Because this strategy has allowed the Government to move away from its even more problematic retailing activities, it is a step in the right direction. It is not a lesson, however, about the success of apex organizations.

Numerous semiformal experiments to reach microenterprises with financial services, with and without government support, have been a failure. These have included credit cooperatives (*cajas or cooperativas de ahorro y crédito*), savings and loan societies (*sociedades de ahorro y préstamo -SAPs*), credit unions (*uniones de crédito*), solidarity credit cooperatives (*Solidaridad*), and some NGOs.

There are at least 300 credit cooperatives in Mexico. The confederation *Caja Popular Mexicana* associates over 300,000 members from 120 cooperatives. These cooperatives have been characterized by instability in membership and high levels of non-performing loans. Fraud has been frequent. In response to the failure of these cooperatives, savings and loan societies (SAPs) were added to the set of regulated financial institutions in 1993. The first SAP to be authorized, *Caja Mexicana de Fomento* (CANAF0), reached a membership of 70,000 members at 98 branches in two years. Not many have been able, however, to obtain the coveted charter.

Credit unions are usually short-lived. They are frequently syndicates created to reap the benefits of subsidized credit; their members used to request long-term loans from the state-owned banks and then disbanded. The 1990-94 period was the golden age of the credit union movement, when NAFIN increased over 60 times the amount of funds disbursed to credit unions. Fraud and non-performing portfolios, however, have required intervention of the National Banking Commission and the movement has become a headache for the financial authorities. This is an example of the dangers of pressures to disburse.

Only some members of the Mexican Association of Credit Unions (AMUCCS) can be considered as MFOs, as many credit unions are rent-seeking vehicles for wealthy producers. They obtain their funds from the apex organizations NAFIN and FIRA and from BANRURAL, and their financial health is poor (Mansell, 1995). Their non-performing portfolio ranges between 11 and 87 percent of the total portfolio. Average arrears are 19 percent of amounts due.

The anti-poverty *Programa Nacional de Solidaridad* also promoted the creation of credit cooperatives. Their initial capital came from repayments of loans from *Crédito a la Palabra* (credit on one's word), a program designed to offer loans to the poorest peasants without collateral. The Solidarity Enterprises National Fund serves as an apex organization for these cooperatives. Their portfolio in arrears had increased from 4.4 percent in 1994 to 17.4 percent in 1996. These are threatening signs but not unexpected results, given the political origins of the system.

In contrast to these weak government-sponsored interventions, some commercial banks and retail chain stores have recently entered the microfinance business. Examples are the banks BITAL and BANCRECER, a pioneer in the strategy of setting up numerous small branches, with only one or two tellers, many of them inside markets. BITAL has adapted the *tanda*, a traditional savings scheme, for its deposit mobilization services and it has created a small loan product. All of these innovations have emerged without the intervention of any apex organization.

NGOs emerged in Mexico after the 1985 earthquake. Among them, Compartamos, Emprendedores, and CAME are examples of promising MFOs. The outreach and sustainability outcomes of *Compartamos* are impressive. The number of members of the *Compartamos* village banks grew from 17,500 in 1995 to 32,254 women in 1997, many of them in some of the poorest rural areas of the country. Loan size ranges between 400 and 5,000 pesos (US\$ 47 to 580). Non-performing loans were only 2.6 percent of the portfolio in 1997, when the rate of return on assets was 10.2 percent. CAME and Emprendedores show more modest indicators of outreach and sustainability, but their operations are promising. The number of CAME members increased from 470 in 1993 to 3,182 in 1997 and non-performing loans are practically nonexistent. These NGOs have been the result of private initiatives where no domestic apex organization has played any role.

In early 1998, NAFIN began implementation of the *Programa Global para el Desarrollo de la Microempresa*. Under this program, NAFIN will assume both first- and second-tier responsibilities in microfinance. Similarly, with support from The World Bank, the authorities are implementing a Rural Bank Branches Program to subsidize the establishment of rural branches by private commercial banks. The success of these efforts is yet to be seen.

F. Bolivia: Apex Organizations in Search of a Role

Bolivian MFOs have had uncommon success (Gonzalez-Vega *et al.*, 1997). Bolivia had the first NGO (PRODEM) to grow to become a chartered commercial bank and take small deposits (BancoSol). Bolivia has some of the few MFOs that use individual loans to reach people as poor as those reached by group loans (Caja Los Andes and FIE FFP) and that experiment in rural microfinance (PRODEM and Caja Los Andes). Bolivia has developed prudential regulation tailored to MFOs (Trigo, 1996).

In terms of outreach, financial performance, cost-effectiveness, and sustainability, the best MFOs in Bolivia are also among the best of the world. These MFOs have received different degrees of donor support. Little of this support has been channeled, however, through domestic apex organizations (Navajas and Schreiner, 1998). Rather, Bolivia is an interesting case of the success of *alternative mechanisms* for the delivery of donor support.

Like Mexico, Bolivia has had its share of government-sponsored domestic apex organizations. Some of them, such as the *Fondo Nacional de Vivienda Social*, a housing fund for the poor now defunct, *Financiera de Desarrollo Santa Cruz*, and the *Fondo Nacional de Desarrollo Regional*, a regional development fund, do not deal with MFOs. The *Fondo de Desarrollo Campesino*, a rural development fund, and the *Nacional Financiera Boliviana* (NAFIBO) deal with supervised MFOs. The *Programa de Microcrédito Popular* (PMP) did support unsupervised MFOs, but it crashed quickly. The *Programa de Apoyo a las Microfinanzas* (PAM), also meant to support unsupervised MFOs, never got off the ground. The *Fondo de Microcrédito* is the most recent government initiative in microfinance, and it is supposed to replace the PMP and PAM. The development of the microfinance sector in Bolivia owes nothing to these apex organizations.

The *Fondo de Desarrollo Campesino* (FDC) is a parastatal organization created in 1989. Its attempts to lend for agriculture failed; by 1993 more than 90 percent of its portfolio was in arrears. In 1992, the GTZ convinced the Government to get FDC out of retail lending and become an apex organization for supervised MFOs in the rural areas. Because FDC also makes numerous grants for infrastructure development, its role as a lender has not been credible. This lack of *credibility* encourages default. Thus, the FDC has done little to strengthen microfinance in the rural areas. With few supervised MFOs in the rural areas, it has been completely unimportant as a microfinance apex organization. It has not lent much funds to MFOs, and it has not strengthened MFOs (Navajas and Schreiner, 1998).

NAFIBO is a second-tier bank that makes long-term loans to all kinds of regulated financial intermediaries, including banks and *fondos financieros privados* (FFPs), the special charter created for regulated MFOs. NAFIBO emerged in 1996 from the conversion of the Development Office of the Central Bank. It has lots of funds, but it does not have experience in microfinance. The combination of low interest rates, no collateral requirements, and long terms to maturity of the NAFIBO loans may explain, however, why so many MFOs want to convert to the status of *fondo financiero privado*. These MFOs do not necessarily want to conform to the discipline and supervision of the Superintendency of Banks and Financial Institutions in order to earn the right to mobilize deposits from the public. Rather, they may accept regulation because they covet the access to the soft funds from NAFIBO.

NAFIBO does not seem to address any major constraint faced by the microfinance sector of Bolivia. For NAFIBO, the restriction to operate with regulated intermediaries allows the apex organization to lend only to the best MFOs (pure *intermediation* function). This means only three MFOs: BancoSol, Caja Los Andes, and FIE FFP, and eventually PRODEM and Ecofuturo. NAFIBO has nothing to offer these MFOs except cheap, long-term funds. These funds are a double-edged sword: they facilitate growth at low financial costs, but they discourage *market-based* liabilities, including deposits. For other MFOs, it creates perverse reasons to seek supervision and to avoid seeking funds from the market (Navajas and Schreiner, 1998).

The constraint may help sustainability by rewarding those MFOs that upgrade themselves enough to qualify for the FFP charter. It may thus strengthen the market for microcredit. It may also wither the market for microdeposits. The link between supervision and access to the apex organization removes much of the incentives to mobilize deposits, as it gives precisely the MFOs that could take deposits a new source of large amounts of cheap funds. Moreover, the lure of cheap funds may allow the apex organization to break good habits developed by MFOs over the years when such cheap funds were not as easy to get.

The *Programa de Microcrédito Popular* (PMP) started in 1995 with Swiss funding as an effort to extend the outreach of MFOs to the rural areas and unattended urban areas. That year, it disbursed US\$ 1.5 million to four cooperatives and six NGOs. Since then, it has fallen into disuse. A main reason for this was that the board of trustees in charge of selecting the MFOs eligible to bid for the equity grants to open rural branches was composed of representatives of the Government and of the networks of rural and urban MFOs, namely, the potential bidders. This conflict of interests, typical of client-owned apex organizations, led to failure. It is an example of failure due to poor *institutional design*. The main purpose of PMP was to inject funds, not to strengthen sustainable capacity. The high costs of setting up this whole structure, however, were not justified by the mere disbursement of US\$ 1.5 million.

The *Programa de Apoyo a las Microfinanzas* (PAM) was designed as a systematic attempt by the Government of Bolivia to play a more important role in the allocation of donor funds earmarked for microfinance. It was going to be housed in the *Fondo de Desarrollo del Sistema Financiero y Apoyo al Sector Productivo* (FONDESIF), a government office specialized in the support of supervised financial intermediaries. In the past, FONDESIF was essentially a clinic that administered bail-outs for sick financial institutions. It is unclear that it has the experience needed to provide innovative technical assistance to MFOs. Among the target clientele of PAM were going to be the cooperatives, which are already supervised and have access to other apex organizations (Navajas and Schreiner, 1998).

Another serious danger is political intrusion in PAM or its successors. Microfinance has attracted the gaze of the Government because of the large flows of foreign aid associated with it and the success of microfinance in Bolivia. Moreover, MFOs reach a multitude of households; the Government may see the apex mechanism as a way to divert microfinance to its own ends. From the perspective of the donor, an apex organization like PAM is a risk. Donors would no longer wield direct control over the funds, and the apex organization may make choices that do not necessarily match the preferences of the donors. Donor skepticism about these questions may have led to the abandonment of this project. With the announcement of the creation of the *Fondo de Microcrédito*, however, the Government has signalled its continued intent to control the sector. Donors may have to follow the Government in this initiative to create another domestic apex organization. Rather than a welcome innovation, this is a threat to microfinance in Bolivia.

This experience has demonstrated, moreover, the high costs incurred in building an apex organization. Government, donors, and MFOs have been engaged in lobbying and multiple and distracting negotiations. These transaction costs may never pay off with future cost-savings. While donors and Government haggle over PAM and its successors, however, microfinance in Bolivia goes on, as it did in the past without the assistance of domestic apex organizations.

Instead, the development of microfinance in Bolivia has been the result of strong private local initiatives coupled with proficient foreign technical assistance. One extreme case of this model has been the close partnership between *Internationale Projekt Consult* (IPC), a German consulting firm that has operated in Bolivia mostly with GTZ funding, and the local NGO PRO-CREDITO, which led to the upgrading of this NGO into Caja Los Andes.

This relationship has been the archetype for the concept of an implicit *partnership* in the development of information capital and organizational design that was highlighted as central to the successful development of microfinance in Section III of this paper. This experience is a replication of an equivalent relationship between IPC and the *Asociación de Medianos y Pequeños Empresarios* (AMPES) which, with GTZ support, led to the creation of *Financiera Calpiá* in El Salvador, another outstanding MFO by world standards developed without the assistance of a domestic apex organization. The irony is that much of the support to the creation of PAM in Bolivia had come from the GTZ, as the German technical assistance organization shifted its support toward a broader, system-wide intervention through an apex mechanism.

The evolution of the partnerships between PRODEM and BancoSol with ACCION International, with USAID support, and with the Calmedow Foundation has been similar. These relationships have been a source of two-way transfers of technology and of elements of ownership in the MFOs that have contributed to their success, without the assistance of any domestic apex organization. Moreover, the successful development of other MFOs in Bolivia, such as FIE FFP, Sartawi, and Ecofuturo, has resulted from their own autonomous efforts and from the demonstration effects from the leaders in the industry, with some donor support but, again, without any technical assistance from a domestic apex organization. Some of these newer regulated MFOs have received, however, funding from Funda-Pro.

Funda-Pro is a sustainable non-government microfinance apex organization created in 1992 with USAID support. As the FOCAS program (*Formación de Capital en Areas Secundarias*), designed to promote capital formation in market towns, was coming to an end, USAID and the Government of Bolivia started to look for another use of the funds. Funda-Pro was created as an "ad hoc response to give continuity to the FOCAS project" and to place the funds with the private sector in order to free them from political pressures (Davalos, 1996). Since then, Funda-Pro has been searching for a permanent function.

Eventually, among other functions, Funda-Pro assumed the role of a microfinance apex organization. Funda-Pro has assembled a highly competent and motivated staff of professionals. To date, however, it has found few opportunities to offer technical assistance to develop sustainable microfinance at the retailing level. Rather, FundaPro has made loans to (and deposits in) BancoSol, several NGOs such as PRODEM and Procrédito, the predecessor of Caja Los Andes, FIE, Sartawi, Agrocapital, and IDEPRO, that is, to the most successful MFOs in Bolivia. Recently, it has started to lend to financial cooperatives. For these MFOs, the financial assistance of FundaPro has been useful as a source of quick liquidity. These MFOs get most of their funds from other sources, but value the timeliness and promptness of FundaPro disbursements. The true impact of this apex organization, therefore, has been to relax some *temporary liquidity constraints* for the biggest and best MFOs in Bolivia and its clients claim that this has been a valuable service.

Moreover, Funda-Pro is a sustainable organization. It charges interest rates on its loans that cover both inflation and its operational costs. The impact of FundaPro on the size of the Bolivian microfinance market, however, has been slight at best. In 1996 and 1997, it funded 10 percent of the total portfolio of those MFOs. It is likely that these MFOs could have obtained most, if not all, of these funds from other sources. Nor has FundaPro had an important role in the improvement of the strong MFOs that it reaches. For the most part, these MFOs were already well-established by the time Funda-Pro started to lend.

FundaPro has offered, nevertheless, valuable *public goods* to the microfinance sector of Bolivia. It has sponsored the training of the staff of MFOs through the PRE program at the *Instituto Boliviano de Estudios Empresariales*. It has run a *microfinance forum* that has funded research and provided a neutral place for the exchange of ideas. It has served as a focal point for policy dialogue concerning the sector. Despite the exceptional talent found among its staff, it has played a small role in the development of microfinance in Bolivia.

This has not happened without costs. Since 1992, Funda-Pro has sought a charter as a second-tier bank but its application has been rejected by the Superintendency of Banks and Financial Institutions. All the maneuvers required by these process have been expensive and have occupied valuable human capital. As in the case of PMP and PAM, high start up costs have been essentially wasted, as these domestic apex organizations could not contribute to the development of microfinance in Bolivia.

In conclusion, the varied pool of successful MFOs in Bolivia have received valuable donor support through a number of channels: international networks (*e.g.*, ACCION), consulting firms with worldwide experience (*e.g.*, IPC), the USAID-sponsored FundaPro, and directly from the donors. Several have attracted equity contributions from donors and international NGOs. Success has been achieved with only minimal inputs from any domestic apex organization, while those channels represent tested alternatives to domestic apex organizations. Moreover, some of the key contributions could not have been delivered by a domestic apex organization.

The multiplicity of government initiatives for the operation of apex organizations in Bolivia has reflected the absence of a conceptual framework for the promotion of microfinance. At this point in time, the process of market development is almost complete, and the best MFOs are capable of obtaining their funds in the market. Is there a role for a domestic apex organization to consolidate these gains? While this is a valid question, the actual government proposals to address the consolidation of microfinance in Bolivia through a domestic apex organization illustrate more the dangers than the potential contributions of this mechanism.¹²

¹² Perhaps, a reasonable solution would have been to allow Funda-Pro to become the domestic apex organization for microfinance. This effort would have made valuable use of the competent resources housed in Funda-Pro, and it would have prevented the political intrusion associated with the government-owned apex organizations. Understanding the political economy of the creation of apex organizations is important, however, to appreciate why this second-best solution was not chosen in Bolivia.

G. The Small Country Syndrome: Apex Organizations in Search of a Market

The problem for Funda-Pro in Bolivia has been that the share of the market that it can capture in competition with several government-owned and government-sponsored apex organizations is too small to justify its operations. In smaller countries, even when there is a need to promote sustainable microfinance outreach, the market is so small that it cannot support even one domestic apex organization. This predicament has been the case, among others, of the *Fundación José María Covelo* in Honduras, the *Asociación Costarricense para Asociaciones de Desarrollo* (ACORDE) in Costa Rica, and *FondoMicro* in the Dominican Republic.

G.1 Honduras: Fundación Covelo

Microfinance is supplied by several organizations in Honduras. There are close to 100 credit unions, with 250,000 members and a loan portfolio of more than US\$ 70 million as well as numerous NGOs that provide financial services. Of the 300 NGOs that exist in Honduras, 76 have credit operations. Alvarado and Daly (1995) found, however, that only three NGOs had a chance to become sustainable. The typical NGO is not concerned with the client's credit history and repayment capacity and will not increase interest rates to reduce its strong dependence on donor funds.

The *Fundación José María Covelo* was created in Honduras in 1984 with support from USAID and the *Asociación Nacional de Industriales* (ANDI), a producers' association. It began as a mechanism to support small and microenterprises and it eventually evolved into a microfinance apex organization. Its evolution has reflected a series of adjustments driven by external advisors and prompted by the constraints faced in its operations (Quiros, 1998).

In its earliest stage, known as *Programa de Pequeña y Microempresa* (PYME), its goal was to provide training and technical assistance to the borrowers of the *Financiera Agroindustrial y Agropecuaria* (FIA), an organization created by five commercial banks. This arrangement was short-lived; while FIA insisted on collateral, ANDI was committed to microentrepreneurs. As a result, ANDI began to support NGOs, whose number grew to 20 by 1987.

PYME II began in 1988, with the goal to strengthen NGOs involved in microenterprise development. Nathan Associates became the technical unit for the project. Under its leadership, the project focused on NGOs with credit activities, but some of the ANDI directors opposed the more strict eligibility requirements suggested by Nathan. José María Covelo, in particular, argued against limiting the number of eligible NGOs. These arguments are a good example of the problems that emerge when *property rights* are not well-defined. The project was, at the same time, a tool for a donor (USAID) and for a producers' organization (ANDI) to pursue their own goals, while the technical unit (Nathan) was also becoming a *de facto* quasi-owner.

Nathan Associates won the argument, and eligible NGOs were required to have sufficient capacity to manage a minimum microfinance portfolio. It was not easy to persuade them about the new criteria, and complaints reached the American ambassador. By 1990, only 8 NGOs had

been left in the program. This *cycle* of initial expansion in the number of NGOs, followed by shrinkage when the apex organization discovers that they were not sustainable, is typical.

After a mid-term evaluation in 1993, a fund was established at the newly-created Fundación Covelo for on-lending to NGOs. Thus, the apex organization acquired an intermediation role in addition to its original market-development role. Credit operations were expected to provide a source of income for the apex organization, while the funds would allow an expansion of the portfolio of the NGOs. Covelo concentrated its efforts on helping five NGOs become sustainable.

The *trade-off* between numbers and sustainability in a small country became evident. If Covelo wanted to lend to sustainable MFOs, it would never find more than half-a-dozen clients. If it wanted to expand its clientele, to justify its existence, it would risk lending to unsustainable MFOs. A related issue were the low revenues of Covelo, given its small clientele, which did not promote sustainability. In response to this problem, Covelo began looking for new sources of income.

By 1996, Covelo began charging for the sale of non-financial services and it established, as a pilot experiment, a *first-tier* microfinance program. The ostensible goal was to introduce and demonstrate new microfinance lending technologies in Honduras. The implicit goal was to guarantee the sustainability of the apex organization for a new group of *quasi-owners*: its own technical staff. The first experiment has been a solidarity group credit program. A second experiment has been an incentive program, whereby MFOs that fulfill several outreach and financial performance indicators gain access to funds at subsidized interest rates.

The regular credit program is available to any MFO that is part of the Covelo network. Membership is achieved after a thorough evaluation of the MFO. Three products are offered: regular loans, overdrafts, and lines of credit. By 1997, all MFOs were using the line of credit at 29.5 percent rate of interest. The financial incentives plan offers a credit line at no interest and a 9-percent commission fee. This program was adopted so Covelo could be competitive compared to other subsidized donor programs accessible by the MFOs. Only four of the six clients of Covelo have access to this program. Non-financial services to microenterprises are no longer offered, but Covelo offers technical assistance to MFOs for sustainability.

As a response to a slow disbursement of funds at the second-tier, a first-tier operation was created in late 1995. The solidarity group lending technology observed at GENESIS in Guatemala was chosen for this activity. Loans are offered at 10 branches, some of them located in markets. Loan size ranges between US\$ 35 and US\$ 2,330. Covelo officers claim that they are not in competition with their second-tier clients, as they operate in other regions, but the implicit *conflict* is evident. Representatives of the MFOs justly claimed that Covelo's first-tier program competes both for funds and for clients.

The outreach of the Covelo network has been important. The number of clients increased from 6,990 in 1992 to 42,894 in 1997. Of these, 38,324 were women. The number of village banks and solidarity groups reached increased from 193 to 1,612 during the same period. The credit portfolio grew from Lps. 8.3 million to Lps. 62.4 million. It took, however, US\$ 19

million to develop a portfolio of US\$ 5 million for the Covelo network of six MFOs. This is not a positive cost-benefit ratio.

G.2 Costa Rica: ACORDE

The evolution in Costa Rica of the *Asociación Costarricense para Asociaciones de Desarrollo* (ACORDE) is also a reflection of the constraints imposed by a small market size (Quiros and Gonzalez-Vega, 1998). Created in 1982, with USAID support, ACORDE also evolved from a sponsor of small projects to become a microfinance apex organization.

The Costa Rican is a small economy, with a small financial system, and a small micro-enterprise sector.¹³ There are only 180,000 self-employed persons in the working force, one-third of whom are farmers. The informal sector is very small. For decades, the state-owned Banco Nacional de Costa Rica has been the most important source of small loans. Credit unions are also important. The InterAmerican Development Bank's Micro Global Program, for US\$ 10 million, has not been successful in getting private commercial banks interested in microfinance (Taborga and Wenner, 1997). The workers' bank (Banco Popular) and the Mexican-owned BANCRECEN as well as a number of *financieras* also operate in this market niche. The largest NGO in Costa Rica is FINCA, an adaptation of the rural village banking technology (Gonzalez-Vega, Jimenez, and Quiros, 1996). The larger urban NGO, AVANCE Microempresarial, failed in 1997.

In 1982, USAID sponsored the creation of the *Coalición Costarricense de Iniciativas de Desarrollo* (CINDE), for export-oriented training and export and investment promotion. The CINDE-PVO component was added soon afterwards, to support private voluntary organizations. USAID had considered creating the program within one of the American NGOs already operating in Costa Rica, but rivalry among them made this option impossible. Creating a new NGO was also discarded as a costly and lengthy process. A channel to disburse was needed soon.

CINDE-PVO became a vehicle for disbursing grants to NGOs, but CINDE was allowed to keep interest earned on undisbursed funds. USAID still determined which NGOs and for what amounts were to be funded. CINDE-PVO, in turn, was expected to develop "productive projects" for the clients of the NGOs, a task for which it did not have any experience. In practice, the mechanism was simply a tool to disburse USAID funds to American-based NGOs, which had a close relationship with the Mission and were influential in Washington. Disagreements between ACORDE and some NGOs even led to the intervention of U.S. senators. The goal was to disburse funds as rapidly as possible regardless of their expected uses. ACORDE was then the clearest example of the *disbursement pressures* that can plague an apex mechanism.

CINDE did not support the PVO program as much as USAID wanted. In 1986, USAID created ACORDE to take over the program. Well-known politicians and businessmen (70) were asked to join the association. Although apparently a contradiction, the *grant ideology* of the lead-

¹³ At least 19 individual Latin American banks have larger loan portfolios than the entire Costa Rican financial system.

ing businessmen of the first board of directors is not uncommon among apex organizations. Not much changed, except that ACORDE was asked by USAID to keep track of the numbers of projects and final beneficiaries.

Another relevant, frequently negative, role in the history of ACORDE was played by the *external advisors*. They had an implicit seat in the board of directors. In the early days, given its lack of experience, the organization was highly dependent on these advisors. The first one, from the Panamerican Development Foundation, was extremely helpful in the development of procedures and manuals. Later on, the external advisor became the strongest voice against the transformation of ACORDE. Private Agencies Collaborating Together (PACT), which acted as an intermediary between the USAID Mission and ACORDE, defended the interests of the U.S. NGOs against the sustainability of the apex organization.

The transformation of USAID in the early 1990s and the prospect of ending its operations in Costa Rica changed this philanthropy-cum-rent-seeking vision for ACORDE. The *Financial Services Project*, implemented by The Ohio State University and Academia de Centroamérica, questioned the performance of ACORDE. This project alerted on the lack of sustainability of the apex organization. USAID mandated a change of approach, from the disbursement of grants to lending to MFOs on market terms. New members of the board of directors, which has a lot of power, adopted the fresh approach and influenced the management of ACORDE.

Once sustainability became an issue, the constraint posed by the small size of the market became evident. ACORDE stopped disbursing grants and started to lend to creditworthy MFOs at market interest rates. The number of MFOs reached declined drastically. In particular, the American-based NGOs, which had been a source of conflict and abuse, no longer wanted to deal with ACORDE. The resulting contraction of the loan portfolio forced ACORDE to seek credit unions as clients. Eventually, to justify its existence, ACORDE decided to initiate first-tier lending operations for medium and small enterprises.

An evaluation in 1992 by ACORDE demonstrated that most MFOs had few chances for survival, as a result of their weak organizational design and lack of human resources. The credit unions that replaced the NGOs as clients had, in contrast, ample experience with credit. These credit unions typically lend for small agricultural projects. By 1997, ACORDE was lending to 14 NGOs and 10 credit unions. The maximum loan size for the microenterprises reached in this way was US\$ 7,500; for small enterprises the maximum loan size was US\$ 15,000.

In 1993, ACORDE decided to implement its own first-tier credit program for medium and small producers. Its large equity base allowed this expansion of its portfolio, and ACORDE had found a profitable, unattended market niche. In engaging in these transactions, ACORDE expected not to compete with its MFO clients, whose activities were either rural or with microenterprises. ACORDE successfully sought a US\$ 500,000 loan from the Central American Bank for Economic Integration to expand this activity. These were the first non-USAID funds used in the history of ACORDE. Under this program, loan size can reach up to US\$ 100,000. Plans to transform ACORDE into a regulated financial institution, however, have been postponed.

There is a common thread in the history of Fundación Covelo in Honduras and ACORDE in Costa Rica. They were both created for the convenience of the donor, as a tool for the disbursement funds. As donor perceptions changed over time, the role of the apex organization also changed. Eventually, strong managerial teams took control of the organization. These teams reinforced the theme of sustainability and took the organizations in unexpected directions.

At present, a small but highly qualified managerial team at Covelo considers ambitious plans for the apex organization. With the support of USAID, they have been lobbying for legislation that would allow organizations like Covelo to mobilize deposits from the public. This would be an alternative to a process of *transformation* into a regulated financial intermediary, according to existing charter types, a route discouraged by USAID at this time. New regulation would also allow Covelo to enter the market for leasing, factoring, and credit cards. Covelo has also considered selling its services to commercial banks interested in downscaling.

ACORDE's strong managerial team has chosen, instead, the route of competing in the market for small (rather than micro) loans. The possibility of becoming a regulated financial intermediary has been explored, but the strong board of directors, wisely, has discouraged this idea for the time being. As ACORDE gains further experience in the market for small loans, however, it will position itself at least for a profitable strategic alliance in the Costa Rican financial market.

G.3 Dominican Republic: FondoMicro

The experience of FondoMicro in the Dominican Republic is a similar illustration of the constraints experienced by a domestic apex organization in charge of supplying second-tier services in a thin market (Malhotra, 1994). FondoMicro, moreover, developed outstanding expertise in providing technical assistance to its MFO clients (Schreiner and Gonzalez-Vega, 1995). The quality of these services was not sufficient, however, to create a sufficiently large market to justify the existence of the apex organization. In addition, FondoMicro had over three-quarters of its portfolio concentrated in one client (ADEMI). The only way out of this trap was for FondoMicro to *downscale* to retailing operations. It has accomplished this purpose by creating a formal financial intermediary.

FondoMicro, as a private non-profit organization created with USAID support, was entrusted with implementation of the Micro and Small Business Project in 1990. USAID envisioned that FondoMicro would become a permanent structure in the Dominican financial landscape, serving as a bridge between the formal financial sector and the microfinance sector. The project was designed in response to perceived market demand: several MFOs were interested in streamlining their operations and gaining access to funds to address an increasing demand for microfinance in the Dominican Republic.

Project design assumed the existence of "scores of NGOs" with the capacity to absorb the predetermined volume of funds within a specific time frame, after the provision of some technical assistance. In fact, there were only eight NGOs with a credit program. Only three, however, fulfilled USAID's requirement of at least one year of experience and a minimum of 200 clients. ADEMI was the only potentially sustainable MFO at that time. The minimum *critical mass* for

success of a domestic apex organization was not there. Moreover, the sustainability of the potential clients had been overestimated, and their shortcomings in managerial, financial, and lending know-how were systemic. They required ongoing technical assistance, on an on-call basis, in almost every aspect of institution building (Maholtra, 1994).

FondoMicro responded to these challenges efficiently and earned a reputation of competence and integrity. It opened credit lines for five NGOs and two of the credit cooperatives developed by an earlier Ohio State University project. Its services, however, were not vitally important for ADEMI, an outstanding program in its own right and the most important client in its portfolio. In fact, ADEMI already had and at any time could have had access to sufficient funds on a commercial basis from its banking connections.

FondoMicro also provided technical assistance to about a dozen MFOs. Its technical assistance services have been highly valued by its clients. The scope for developing a sufficiently large portfolio was limited, nevertheless, by the lack of vision and commitment among most MFOs in the country, which no amount of outside technical assistance can provide. As a sustainable apex organization, the role of FondoMicro was seriously constrained by small market size. Its investment in a highly professional management team was too large for the volume of operations allowed by the market. The management team began to look for alternative functions. Eventually, Banco de la Pequeña Empresa was created in 1997.

H. Paraguay: Technical Assistance for Downscaling

The involvement of a domestic apex organization in the *downscaling* of the operations of an established financial intermediary is a less demanding task than the upgrading of MFOs. The apex organization still faces, however, significant challenges in the transfer of the new lending technologies and in the adjustments of the organizational design required to efficiently *match* technology and organization. This task requires competent technical assistance.

The *Global Microenterprise Program* sponsored by the InterAmerican Development Bank in Paraguay is one of the most successful examples of involvement of a domestic apex organization in a downscaling exercise (Navajas, 1998). Success has resulted at least from two factors. First, the greater proximity of the financial intermediaries selected for the experiment (*financieras*) to the target clientele and their experience in lending to low-income people. Second, the quality of the technical assistance input provided by the German consulting firm IPC.

Before the development of the Global Microenterprise Program, in Paraguay the supply of microfinance was shallow. Private banks were not interested in this market niche, while state-owned development banks focused on agricultural lending. *Financieras* emphasized consumer credit in the urban areas. They had actually emerged from the credit departments of large retail stores and, in becoming regulated financial intermediaries, had been influenced by the Chilean experience. Their clientele was concentrated in salaried employees. Only Financiera Visión, created in 1992, had started to seek business in the microenterprise market niche.

The *Consejo Nacional de Entidades de Beneficiencia Financieras* (CONEB) and the *Fundación Paraguaya de Cooperación y Desarrollo* (FUPACODE) were the only promising MFOs. By 1989, CONEB had about 600 clients. FUPACODE, which had been created in 1985 by local business leaders with technical assistance from ACCION International, by 1989 had about 4,700 clients (Gonzalez-Vega and Chaves, 1991). FUPACODE's clientele has remained stagnant, and by 1997 this MFO had 4,580 clients. In contrast, at the end of 1997, the *financieras* associated with the Global Microenterprise Program had 18,000 clients in their microfinance portfolio.

The Global Microenterprise Program began in 1992 as an effort to expand the supply of microfinance through formal financial institutions. It has been implemented by an office at the Central Bank of Paraguay (*Unidad Técnica Ejecutora del Programa -UTEP*), with technical assistance from IPC. The Program has two components. Under the financial intermediation component, the apex mechanism screens MFOs and disburses, monitors, and collects loans to eligible MFOs. Under the market-development component, the apex mechanism, with the collaboration of the foreign provider of technical assistance, transfers appropriate technologies to the participating MFOs. The UTEP has been responsible, in addition, of lobbying and policy dialogue in order to promote appropriate government policies, and it has administered an innovative mechanism to deliver technical assistance to microenterprises, through the use of training vouchers, which has been extremely successful but that is not examined further here.

The UTEP is a small unit in charge only of managing the Program. It consists of eight Central Bank employees and eight consultants. Its costs are covered either by the Program or by the Central Bank. Its authority and independence are linked to the authority and independence of the Central Bank itself.

The IPC contribution has strengthened the ability of UTEP to manage the program, has assisted in the assessment of the eligible MFOs and in the transfer of appropriate technology, in an effort to demonstrate that the new technology is sufficiently profitable, and has designed and managed the voucher program. The vouchers are redeemable at eligible private training organizations for partial payment of the costs of training. It has been assisted, in this last task, by the Uruguayan consulting firm GAMA.

The eligibility of regulated financial intermediaries is based on minimum levels of financial soundness and on their willingness to work in the target market niche. The private banks showed little interest, as the cost of funds from the Program is similar to their own cost of funds. The *financieras*, in contrast, were successfully attracted by the Program. They were familiar with what they believed was a similar product: consumer credit characterized by small amounts, no collateral, and high interest rates. Moreover, the pool of *financieras* is large in Paraguay. By 1997 there were 52 *financieras* in this country and *competition* is intense. Their smaller size allowed them to innovate more easily than banks could. The predicted size of the microfinance portfolio did not seem to interest the banks. Four large *financieras* (Familiar, Visión, Interfisa, and Fincresa) have received the lion's share of the Program funds.

The core of the technical assistance provided to the participating MFOs has been the transfer of appropriate and profitable lending technologies. In this case, the technology transferred has been the individual-loan approach developed by IPC in other parts of the world. Individual lending was compatible with the experience of the *financieras*, while the technical assistance in-

roduced the concept of *performance-based* remunerations for the loan officers. IPC has been involved in the training of loan officers (the program lasts seven months) and in the practical on-the-job adaptation of the technology within the MFO. Direct technical assistance has also been provided to select *financieras*, depending on their willingness to transform their organizational structures. IPC firmly believed that it was better to *concentrate* on a few potential winners rather than attempting to help everyone. Three *financieras* (Familiar, Visión, and Interfisa) have been the beneficiaries of this institution-building input.

As in other places, the intervention of IPC has been intense. An individual consultant, with extensive experience elsewhere, is placed inside each *financiera*. Each consultant faces different challenges and each MFO has embraced the new lending technology to different degrees, depending on their organizational structures and preferences. Financiera Familiar, the largest, has expanded its microfinance portfolio to 16 percent of the total, while Financiera Visión has expanded its microfinance portfolio to 23 percent of the total. Moreover, these two MFOs have been using their own funds, and not just Program funds, for this expansion. In the case of Financiera Familiar, program funds have accounted only for 53 percent of the microfinance portfolio, while the proportion was 52 percent for Visión. According to representatives of these MFOs, the key component of their interest and success has been the quality of the (subsidized) technical assistance that they have received.

VI

Policy Recommendations

Given the enormous diversity of experiences with domestic apex organizations, it is not easy to arrive at too many generalizations. The primary conclusion of this research effort is, however, that:

"the creation of domestic apex organizations should in general not be recommended."

Under very special circumstances, however, domestic apex organizations have a modest probability of success. Consideration of these circumstances suggests that the probabilities of success are higher when:

- (a) a sufficiently large and well-established microfinance market already exists,
- (b) a sufficiently large number of sustainable or potentially sustainable microfinance organizations exists,
- (c) the existing microfinance organizations do not already have access to commercial sources of funds, and the domestic apex organization has a comparative advantage as a financial intermediary,
- (d) the domestic apex organization has the will and the credibility needed to enforce financial contracts,
- (e) the degree of interest-rate subsidy incorporated in loans from the domestic apex organization is not excessive, and the apex organization encourages the mobilization of deposits and other funds from the market,
- (f) the apex organization seeks its own sustainability or is forced to operate according to a constraining budget rule,
- (g) the ownership structure protects the apex organization from political intrusion or from the rent-seeking efforts of client-owners,
- (h) the apex organization has access to internationally available best-practice lending technologies, business policies, and organizational designs,
- (i) existing lending technologies have been developed by local leaders of the microfinance industry, and there is a second echelon of microfinance organizations that can adopt those technologies with assistance both from the apex organization and the innovative leaders in the industry,
- (j) the apex organization is willing and capable of selecting a few potential winners and concentrates its attention on strengthening these organizations,

- (k) the apex organization makes a long-term commitment to institution-building of the client organizations,
- (l) the apex organization provides opportunities for on-the-job learning for the staff of its client organizations,
- (m) the apex organization does not crowd out the retailing organizations in the competition for scarce human resources with expertise in microfinance,
- (n) there is a clear distinction between the intermediation function and the market-development function of the apex organization; ideally, the two functions are performed by separate organizations,
- (o) the apex organization is able to withstand disbursement pressures from government and donors,
- (p) government ownership of the apex organization is avoided,
- (q) the apex organization is engaged in a downscaling exercise for existing, sustainable, regulated financial intermediaries rather than in the upgrading of non-regulated microfinance organizations.

The most important consideration is that the funds granted to a domestic apex organization can reach the target microfinance organizations through a number of *alternative*, frequently superior channels, and that the funds used to promote microfinance through the operations of a domestic apex organization have other valuable alternative uses.

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ANNEX A

LIST OF CASE STUDIES

Africa

1. Benin *Fédération des Caisses d'Épargne et de Crédit Mutuel (FECECAM)*, visited by Dr. Korotoumou Ouattara.
2. Benin *Projet d'Appui au Développement des Microentreprises (PADME)*, visited by Dr. Korotoumou Ouattara.
3. Benin BINGO Program, AFRICARE, visited by Dr. Korotoumou Ouattara.

ASIA

4. Bangladesh Palli Karma-Sahayak Foundation (PKSF), visited by Dr. Geetha Nagarajan.
5. India Friends of Women's World Banking (FWWB), visited by Dr. Geetha Nagarajan.

Latin America

6. Bolivia Funda-Pro, visited by Sergio Navajas.
7. Costa Rica *Asociación Costarricense de Iniciativas de Desarrollo (ACORDE)*, visited by Rodolfo E. Quiros.
8. Honduras Fundación José María Covelo, visited by Rodolfo E. Quiros.
9. Mexico Prepared by Mario Villalpando-Benitez.
10. Paraguay Micro Global, visited by Sergio Navajas.

ANNEX B

SURVEY OF APEX ORGANIZATIONS

A worldwide survey of domestic apex organizations was implemented by sending a questionnaire to the organizations listed below and receiving their answers by mail. The researchers are grateful with the organizations that took the time to answer the questionnaire. In addition, this Annex includes a copy of the questionnaire used for the survey.

Africa

1. Benin *Fédération des Caisses d'Epargne et de Crédit Mutuel (FECECAM)*
2. Benin *Projet d'Appui au Développement des Microentreprises (PADME)*
3. Benin BINGO Program, AFRICARE
4. Cameroon
5. Egypt Social Fund for Development
6. Kenya Kenya Rural Enterprise Programme (K-REP)
7. Senegal Programme d'Appui aux Mutuelles d'Epargne et de Crédit au Senegal
8. Senegal Programme d'Appui SMEC de l'UEMOA (PA-SMEC)
9. South Africa Khula Enterprise Finance Ltd.
10. Togo FUCEC

ASIA

11. Bangladesh Palli Karma-Sahayak Foundation (PKSF)
12. India Friends of Women's World Banking (FWWB)
13. Philippines PCFC
14. Philippines TSPI Development Corporation
15. Sri Lanka SANASA, Federation of Thrift and Credit Co-operative Societies
16. Thailand Catholic Relief Services, USCC

Latin America

17. Bolivia Funda-Pro
18. Colombia Cooperative Emprender
19. Costa Rica ACORDE
20. Dominican Republic FondoMicro
21. Ecuador Corporación de Garantía Crediticia para el Fomento de la Microempresa (CorpoMicro)
22. Honduras Fundación José María Covelo
23. Peru Consorcio de ONGs que Apoyan a la Pequeña y Microempresa (COPEME)
24. Peru Corporación Financiera de Desarrollo S.A. (COFIDE)