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International Herald Tribune – Up to \$500 million pledged for microloan institutions

05.02.2009, By Carter Dougherty

FRANKFURT: The World Bank and the German government said Thursday that they would inject as much as \$500 million into microcredit banks, fledgling institutions in the developing world that are being starved of funding as financial markets in rich nations constrict.

The effort highlights how even small banks in poor countries are getting caught in the global financial riptide - and it offers them a chance as well as public money to replace a rapidly diminishing supply of private capital.

"You have some viable projects here where the financing has simply dried up," the World Bank president, Robert Zoellick, said by telephone from Berlin, where he and the heads of other leading economic organizations met with Chancellor Angela Merkel.

The microcredit investment fund is part of a broader effort by the bank and other development agencies to mobilize rich-country cash for poorer countries during the credit crisis, Zoellick said. Other funds are focused on infrastructure projects, bank recapitalization and trade finance.

Microcredit institutions, which generally make tiny loans of \$100 or less to individuals or small businesses, gained attention in the 1990s as a way to foster private enterprise in poor countries. In 2006, Mohammed Yunus, the founder of the Grameen Bank in Bangladesh, one of the first microbanks, won the Nobel Peace Prize for his work..

Though many banks were seeded with money from western aid agencies, a long process of drawing more investment from private sources was well under way - until the credit crisis began in August 2007.

"In general, there was a lot of momentum from the private sector," said Jack Lowe, president of BlueOrchard Finance, one of the firms that have been selected to manage the new fund. "But when you have the wind at your back and financial markets are heady, it is easier to raise money."

Under the plan, the World Bank would initially provide \$150 million alongside another \$130 million from the German government. Zoellick said the bank was soliciting contributions from other countries and agencies, and hopes to mobilize up to \$600 million. That would be enough to help 150-200 microfinance banks based in 40 developing countries, he said.

The money would be managed by three private companies that specialize in microfinance: BlueOrchard and ResponsAbility Social Investments, both based in Switzerland, and Cyrano Management, which operates out of Lima, Peru.

The firms have seen business grow over the last decade by attracting private capital into funds which was invested with individual microcredit banks. Now they will do that with public money.

Like many large commercial banks, many microcredit institutions take deposits from individuals or businesses and lend the cash out. The main difference is that they parcel out tiny loans to finance small businesses.

But other microcredit banks function like investment banks, drawing money from wholesale financial markets at one rate of interest and lending it out at a slightly higher rate.

Patrik Huber, a managing director at ResponsAbility, said that wholesale rates averaged three to six percentage points above Libor, a benchmark in lending, before the credit crisis. Now, depending on country or region, the rate can be five to seven percen-

tage points above Libor, effectively extinguishing the margin microcredit banks depended on to make a profit and expand future lending.

"They cannot work as they once did," Huber said. "So the amount being funded by the international organizations and microfinance funds has to increase."

To avoid crowding out the private sector over the long term, Zoellick said, money from the new lending facility would be lent for between 6 and 24 months on the theory that, as credit markets normalize, the World Bank can withdraw its money.

Zoellick emphasized that the cash being offered was not a recapitalization of microcredit banks after heavy losses.

Microfinance banks are generally solvent, have a strong record of making sensible loans, and did not speculate in the complex mortgage-linked securities that have caused so much woe among western banks. Only 2 to 3 percent of their loans tend to go bad, Zoellick said.

"It always depends on the institution," he said. "But what we finance in general in the microfinance industry is that their problem loan percentage is quite low."

Japan has pledged \$2 billion to a separate facility run by the International Finance Corporation, a part of the World Bank, to recapitalize banks in poorer countries.

Along with Zoellick in Berlin were the heads of the International Monetary Fund, World Trade Organization, Organization for Economic Cooperation and Development and the International Labor Organization. In a statement, they called for new global economic rules to prevent future crises and said all countries had a duty to resist protectionism.