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FINANCIAL INSTITUTIONS WITH A "DOUBLE BOTTOM LINE": IMPLICATIONS FOR THE FUTURE OF MICROFINANCE



CGAP, the Consultative Group to Assist the Poor, is a consortium of 28 development agencies that support microfinance. More information is available on the CGAP website: www.cgap.org.

Please contact CGAP with comments, contributions, and requests to receive other notes in the series.

1818 H Street, NW
Washington DC 20433

Tel: 202 473 9594
Fax: 202 522 3744

E-mail:
cgap@worldbank.org

Web:
www.cgap.org

IMPORTANT CLARIFICATION: "This paper reports a surprisingly large number of savings and loan accounts—probably well over 750 million—in financial institutions that focus on a clientele that is generally below the level served by commercial banks. Even before publication, it has become clear that repetition of this finding invites serious misinterpretation when the nuances of the data are not understood and explained. The large numbers being reported can lead to a facile impression that the task of reaching lower-income clients, especially poor clients, has been accomplished because so many people are already being served. No such conclusion is justified by the data reported in this paper. The institutions studied here serve many clients who are not poor or near-poor, probably including some people who could also use a commercial bank. (There is usually no information available on the socio-economic distribution of these institutions' clients.) Further, four-fifths of the accounts reported are savings accounts, and access-to-service problems may be greater for loans than for savings.

"A correct statement of this paper's main conclusion is that there are over 750 million accounts in various classes of financial institutions that are generally aimed at markets below the level of commercial banks, and that some substantial fraction of these institutions' clients are probably poor or near-poor. The message is not that the task is nearly done (anyone with field experience knows this to be untrue), but rather that these institutions represent an important potential opportunity.

"CGAP requests that this paper and its data not be cited without clarification of this essential point."

Summary

Most participants in the microfinance movement of recent decades see their goal as improving the availability and quality of financial services for poor and near-poor clients.¹ Thus far, much of the movement's attention has been focused on a relatively new breed of specialized microfinance institutions (MFIs) that focus directly on this clientele. Most but not all of these MFIs have been not-for-profit non-governmental organizations (NGOs) that concentrate on providing loans.

¹ While this study focused only on savings and loans, other financial services—including remittances and insurance—are also important for lower-income customers.

CGAP recently surveyed the global outreach of a broader set of institutions, all of which focus to some degree on extending financial services downward from the economic level of the traditional clients of commercial banks. Thus, these institutions have a “double bottom line”: in addition to a financial objective, they also have a developmental or social objective. If their managers were asked which of the objectives is primary, most of them would say that the non-financial objective—extending outreach to people not normally served by banks—is the crucial one, and that solid financial performance is a means to that end rather than an end in and of itself. This paper will refer to these institutions as “alternative financial institutions” (AFIs).

The CGAP research has identified a surprising number—**well over 750 million savings and loan accounts in AFIs**—in developing and transition countries.² AFIs include state-owned agricultural, development, and postal banks; member-owned savings and loan institutions; other savings banks; low-capital local and/or rural banks; and specialized microfinance institutions and programs (MFIs) of varying types.³ Historically, almost all of these institutions were set up with an explicit objective of reaching clients who did not have access to services from commercial banks and finance companies.

All types of AFIs, including MFIs, share certain common characteristics. They are generally aimed at lower-income clients and are not profit-maximizers. **The data needed to quantify the split between poor and non-poor clients in these institutions is almost never available.** Specialized MFIs differ from the other types of AFIs in that MFIs tend to be more specifically focused on the poor and near-poor, not just the unbanked.⁴ But even for MFIs, data on the percentages of poor and non-poor clients is sketchy. Because of the specific poverty orientation of many MFIs, it is probably true that **MFI clients tend to be poorer on average than clients of other AFIs in the same country.** At the same time, it is clear that **these other AFIs also have very large numbers of poor clients.** Average

account sizes are not uniformly smaller in MFIs than in the other AFIs.

Given their age and size, MFIs account for an impressive share (about 33 percent) of loan accounts identified, but the MFI share of total accounts is 18 percent.

When viewed from the conventional perspective of total financial system assets, AFIs are not significant players in most countries. But the picture is much different when one counts citizens rather than money. **AFIs probably account for a significant share—sometimes the majority—of financial system clients in most developing and transition countries. As such, they deserve more attention than they sometimes receive from government policy makers and external donors.**

The research reported in this paper suggests that specialized MFIs account for a relatively small proportion of the total savings and loan services delivered by AFIs. **While governments, donors, and others interested in the outreach of microfinance should continue to foster the growth of high-performing MFIs, these stakeholders also need to think about the opportunities and challenges presented by the other AFIs.**

In CGAP’s view, the goal of microfinance is a world in which as many poor and near-poor households as possible have permanent access to an appropriate

² As will be discussed later, the total number of active clients is probably considerably less than the total number of accounts. “Transition” is used to designate countries in the process of moving from socialism to a more open-market economy. The countries included in this study are listed in annex 1.

³ This paper uses “microfinance institution” and “MFI” narrowly, referring to NGOs, non-bank financial institutions (NBFIs), and commercial banks that specialize in microfinance, as well as separate microfinance programs in full-service banks. “Microfinance” as used in this definition refers to financial services designed for lower-income clients using the new delivery methodologies developed during the last twenty-five years.

⁴ No attempt is made to prove any quantitative definition of the terms “poor,” “near-poor,” and “unbanked.” These terms are used simply in order to recognize two realities: 1) the clientele of MFIs includes some customers who are above national or international poverty lines; and 2) in many countries, commercial banks serve a small minority at the upper end of the income distribution, and leave unserved large numbers of potential customers who could not reasonably be characterized as “poor” or “near-poor.”

range of high-quality financial services, including not just credit but also savings, insurance, and fund transfers. Viewed from this perspective, AFIs come up short. Despite their vast outreach, **AFIs probably serve only a minority of the unbanked clientele they were created for, and many suffer significant limitations**, including financial services unfriendly to clients, weak loan collection, continuing reliance on large subsidies, political domination, and lack of aggressive focus on poor clients.

At the same time, non-MFI AFIs often have outreach and infrastructure that may offer great opportunities for expanding the extent and quality of microfinance. The most obvious of these is the opportunity to transplant into the other AFIs the highly successful microlending techniques developed by MFIs over the past two decades.

This paper reports the results of the CGAP survey of the global outreach of AFIs, then discusses in more detail the characteristics of the types of institutions that were surveyed, and finally suggests some strategic implications for those who want to help develop financial systems that work for poor people. An annex discusses methodology, including some serious limitations of the data reported here.

The Data

This section analyzes the number of loan and savings accounts reported by over 3,000 AFIs,⁵ broken down by region:

- *East Asia and the Pacific* (EAP)
- *Eastern Europe and Central Asia* (ECA)
- *Latin America and the Caribbean* (LAC)
- *Middle East and North Africa* (MENA)
- *South Asia* (SA)
- *Sub-Saharan Africa* (AFR)

and institutional type:

- *MFIs* (including NGOs and licensed non-bank financial institutions [NBFIs], commercial banks

specializing in microfinance, plus microfinance programs in full-service commercial banks)

- *Financial cooperatives/mutuals* (including credit unions and municipal savings and loan institutions)
- *Low-capital rural and/or local banks*
- *State agricultural and development banks*
- *Postal savings banks* (Non-postal savings banks are discussed separately at the end of this section.)

Institutional types are described in more detail in the next section, which discusses how MFIs compare with the other types of AFIs.

Methodology and Limitations

It is difficult to obtain reliable information on numbers of borrowers and savers in AFIs. Many AFIs do not report to any central organization, so the authors collected information from hundreds of sources. Much of the information came from databases maintained by institutions such as the World Bank, United States Agency for International Development, World Council of Credit Unions, Microcredit Summit, and other networks. This information was updated and supplemented with data provided directly by many individual institutions, especially where the authors knew of large institutions that were not included in existing databases.

Data is reported for the most recent year available. In some cases, the information is as old as 1997, but most of the data cited is from 2000 or later.

The reliability and completeness of the information reported here are subject to a range of limitations detailed in the annex. Two of those limitations are especially important:

- The mapping was not exhaustive. No doubt many institutions escaped the net.

⁵ When this paper is posted to the CGAP web site (www.cgap.org), a listing of countries and institutions will be provided there.

Some institutions reported number of clients or number of members rather than accounts. Fund transfer and insurance services for lower-income clients were not included in the research because information on these topics proved too difficult to obtain.

- Generally, numbers of accounts, rather than numbers of clients, are reported.⁶ Many institutions could not provide client numbers. The distinction between *accounts* and *clients* is an important one. The number of active clients is less than the number of accounts because clients have multiple accounts in one or several institutions, and many savings accounts are inactive.

In view of these limitations, and the above-mentioned fact that the data include both poor and non-poor clients in unknown proportions, it is crucial to stress that this survey has not identified 750-plus million microfinance clients (i.e., poor and near-poor) receiving savings and loan services from AFIs. The exaggerated emphasis given to this point stems from the experience of pre-publication discussions of the data: there was an almost irresistible tendency to oversimplify, and thus overstate, the conclusion of the survey.

At the same time, it is clear that AFIs, including those not usually thought of as microfinance providers, serve a very large number of poor or near-poor clients, even though there is no basis for estimating what percentage of their clients fit this description. The infrastructure and mission of the non-MFI AFIs

present significant opportunities for further improvement of poor people's access to financial services.

Finally, the survey dealt only with numbers and volumes of savings and loan accounts. Other observations about the nature and limitations of the various kinds of AFIs are based on the anecdotal experience of the authors and their colleagues, not on this research exercise.

Numbers of Loans and Savings Accounts

Figures 1 and 2 present numbers of loans and savings accounts, respectively, by type of AFI and geographical region. Figure 3 combines both loans and savings, but not by simple addition. For institutions reporting both loans and savings accounts, only one or the other, whichever was larger, has been included in the combined data.⁷ This adjustment avoids double counting clients who have both a savings and a loan account with one institution, and thus probably brings one somewhat closer to a picture of client numbers rather than account numbers. It does not, however, compensate for clients

⁶ Most specialized MFIs reported numbers of clients. Credit unions generally reported number of members.

⁷ Globally, over 70 percent of AFIs reported both savings accounts and loans.

Figure 1 Active* Loans in AFIs (in thousands)

Region	MFIs**	Co-ops and credit unions	Rural banks	State/agricultural/development banks	Postal banks	Total	Percent of total
AFR	3,956	857	33	348	-	5,193	3%
EAP (incl. China)	18,292	1,069	3,147	65,624	-	88,133	58%
<i>China only</i>	<i>153</i>	<i>18</i>	<i>0</i>	<i>46,570</i>	-	<i>46,741</i>	<i>31%</i>
ECA	430	90	-	28	-	548	0%
LAC	4,464	655	162	51	-	5,332	4%
MENA	909	11	-	5,912	-	6,832	4%
SA (incl. India)	22,366	355	1,467	22,030	-	46,217	30%
<i>India only</i>	<i>3,961</i>	<i>51</i>	-	<i>19,748</i>	-	<i>23,760</i>	<i>16%</i>
TOTAL	50,415	3,037	4,809	93,994	-	152,255	100%
%	33%	2%	3%	62%	-	100%	

Key: **AFR** Africa (sub-Saharan) **EAP** East Asia and the Pacific **ECA** Europe and Central Asia
LAC Latin America and the Caribbean **MENA** Middle East and North Africa **SA** South Asia

*Typically includes loan amounts that have been disbursed, but not repaid or written off.

**Includes NGOs, banks, and non-bank financial institutions that specialize in microfinance, as well as microfinance programs in full-service commercial banks.

worldwide pattern that does not vary much by region.

In its first two decades, the microfinance “movement” focused more heavily on loans than on savings, for three main reasons:

- The movement’s aim was to help the poor, who were not thought of as having much money to save.
- In most countries, new credit techniques, not new savings techniques, launched the movement.
- Most of the institutions involved were NGOs, which were not legally licensed to collect savings.

However, in recent years there has been an increasing recognition that most poor families do save, and that this saving is usually in non-financial form (for instance, stockpiling goods). This is not because the poor prefer non-financial savings, but because they often lack access to good formal savings facilities.

Anecdotal evidence suggests that the worldwide predominance of savings over loans in AFIs also seems to apply in many individual institutions focused more narrowly on poorer clients. Where such institutions offer both good loan services and good voluntary savings services, there is usually more demand for savings than for loans, not least of all because when a poor household needs a relatively large amount of money for some purpose, saving is a less risky way to get it than taking on a debt with a fixed repayment obligation.

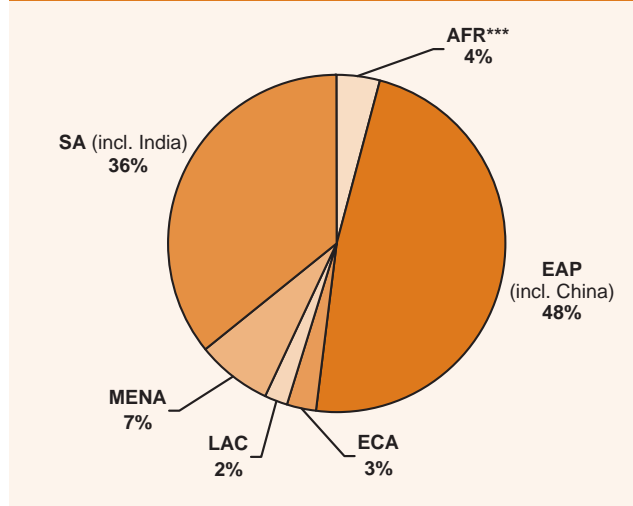
Geographical Distribution

The worldwide numbers are dominated by Asia, which has about five-sixths of all AFI accounts, both savings and loans.

The Asian numbers, in turn, are dominated by China and India, where there has been a heavy, if not always efficient, government commitment to extension of financial services. These two countries alone have 65 percent of AFI accounts in Asia and more than half of all such accounts worldwide.

In comparison with their respective regional populations, the number of AFI accounts is high in Asia,

Figure 4 Total Accounts by Region



and low in Africa, Latin America, and Eastern Europe/Central Asia.

Distribution by Institutional Type

Most discussions of microfinance—and databases reporting microfinance performance—focus on NGOs, NBFIs, and commercial banks that specialize in microfinance, as well as microfinance programs in full-service commercial banks. As a group, these “MFIs” account for approximately 18 percent of the total combined accounts identified in this exercise. (Within the MFI group, NGOs hold about 6 percent of total accounts.) Financial cooperatives add another 6 percent. **Government-owned AFIs, including postal savings banks, dominate the scene**, with about three-quarters of the combined accounts.

It may not be surprising that MFIs constitute only a small portion of total accounts, since most are savings accounts and many MFIs are credit-only institutions. When one looks only at credit services, **MFIs account for about 33 percent of the loans** (25 percent of the loans are from NGOs). The MFI share rises to 57 percent if China and India are excluded. This is an impressive accomplishment, given that MFIs as a group are younger and smaller than the other AFIs. At the

Figure 5 AFI Accounts per Capita by Region

Region	Population	Total accounts	Accounts per hundred
AFR	666	27,000,000	4
EAP (incl. China)	1,866	319,000,000	17
<i>China only</i>	<i>1,280,975,000</i>	<i>157,000,000</i>	<i>12</i>
ECA	385,369,332	18,000,000	5
LAC	515,988,980	14,000,000	3
MENA	377,797,840	49,000,000	13
SA (incl. India)	1,372,806,710	238,000,000	17
<i>India only</i>	<i>1,048,279,000</i>	<i>188,000,000</i>	<i>18</i>
TOTAL	5,183,731,692	665,000,000	13

Key: **AFR** Africa (sub-Saharan) **EAP** East Asia and the Pacific **ECA** Europe and Central Asia
 LAC Latin America and the Caribbean **MENA** Middle East and North Africa **SA** South Asia

Figure 6 Total Accounts by Institutional Type

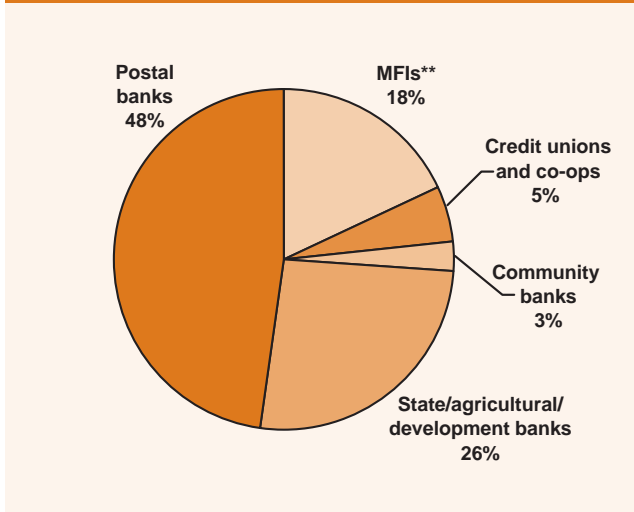
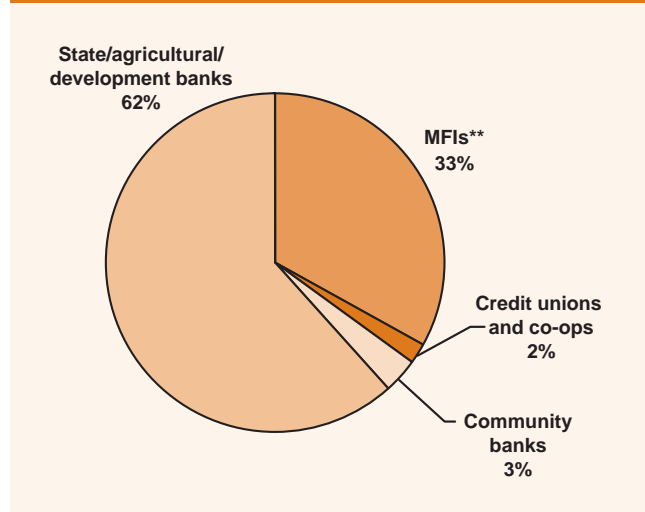


Figure 7 Loan Accounts by Institutional Type



same time, it is clear that there is a great deal of credit being delivered to poor and near-poor clients by non-MFI institutions. (Poverty levels of AFI clients are discussed below.)

Account Size and Client Poverty Levels

Microfinance is usually understood as financial services for poor or near-poor clients. For most of the AFIs reviewed, there is no meaningful way to estimate the percentage of their clients who fit this description. At the same time, **it is very probable that poor or near-poor clients make up a significant portion of**

the clientele of the AFIs—even the non-MFI AFIs. This proposition is supported, not only by anecdotal experience with AFI clients and branch locations in a number of countries, but also by average account size data developed in this study.

There is a meaningful, albeit quite rough, correlation between account size and the level of client assets and income. Average account size was calculated for the subset of institutions (about 80 percent) that provided both total loan or savings balance and the number of loan or savings accounts. The average savings balances shown in figure 8 are very low in some

institutions. The loan balances in figure 9 are usually lower for MFIs than for the other AFIs, but not always: in Africa and Eastern Europe, credit unions have lower loan balances than MFIs.⁸

Savings Banks

Non-postal savings banks generally qualify as AFIs under the definition used in this paper: most were set up with a mission to reach down to clients who were not being served by commercial banks. Typically they are not profit-maximizers. But even though these savings banks

serve important numbers of lower-income clients, they have not been included in the data reported so far

⁸ The institutions included in the figures shown in figures 8 and 9 do not constitute a random sample of the institutions in the data set: the only selection criterion was availability of average account size information.

The average balance of *active* savings accounts would be somewhat higher than that shown in figure 8 because the data set contains an indeterminate number of inactive savings accounts whose average balances are presumably much lower than the average for active accounts.

Outstanding loan balances include disbursed amounts that have not yet been repaid or written off. Outstanding balances on loans average out at a little more than half of the originally disbursed amount.

Figure 8 Average AFI Savings Account Balances as Percent of per Capita Gross National Income

Region	MFIs**	Co-ops and credit unions	Community banks	State/agricultural/development banks	Postal banks
AFR	29%	27%	11%	-	8%
EAP (incl. China)	9%	64%	6%	-	42%
<i>China only</i>	-	-	-	-	41%
ECA	25%	7%	-	-	318%
LAC	15%	16%	2%	-	-
MENA	-	-	-	-	13%
SA (incl. India)	10%	2%	4%	37%	18%
<i>India only</i>	2%	0%	0%	37%	18%

Key: **AFR** Africa (sub-Saharan) **EAP** East Asia and the Pacific **ECA** Europe and Central Asia
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** Includes NGOs, banks, and non-bank financial institutions that specialize in microfinance, as well as microfinance programs in full-service commercial banks.

Figure 9 Average AFI Loan Balances as Percent of per Capita Gross National Income

Region	MFIs**	Co-ops and credit unions	Community banks	State/agricultural/development banks
AFR	137%	55%	34%	143%
EAP (incl. China)	14%	74%	58%	23%
<i>China only</i>	8%	13%	-	22%
ECA	68%	15%	-	-
LAC	43%	57%	39%	69%
MENA	131%	-	-	1%
SA (incl. India)	17%	12%	18%	66%
<i>India only</i>	13%	9%	-	66%

Key: **AFR** Africa (sub-Saharan) **EAP** East Asia and the Pacific **ECA** Europe and Central Asia
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** Includes NGOs, banks, and non-bank financial institutions that specialize in microfinance, as well as microfinance programs in full-service commercial banks.

Figure 10 Total Assets of Savings Banks Compared to Total Banking Assets by Region (US \$ millions)

Region	Total savings banks assets	Total banking assets [§]	Percent of total banking assets
EAP	\$649,338	\$2,217,064	29.3%
SA	\$65,039	\$302,184	21.5%
LAC	\$47,689	\$985,179	4.8%
AFR	\$821	\$152,055	0.5%
ECA	\$100,275	\$367,099	27.3%
MENA	\$15,279	\$484,673	3.2%
Total	\$878,441	\$4,508,255	19.5%

Key: **AFR** Africa (sub-Saharan) **EAP** East Asia and the Pacific **ECA** Europe and Central Asia
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[§]Source: World Savings Banks Institute, data from 2000-2003, depending on country.

because information on the number of accounts in these institutions was seldom available. Figure 10 shows asset size for savings banks in the countries included in this study. It is based on information from the World Savings Banks Institute (WSBI). The few WSBI members whose data was captured under one of the other institutional types were omitted from this figure.

If these non-postal savings banks are not included in the total figures, AFI assets are generally tiny in comparison with total banking system assets. For the countries surveyed, they represent on average only about 2.5 percent of banking system assets. However, figure 10 shows that the savings banks are significant financial players in most regions: in the countries surveyed, savings banks represent almost a fifth of banking assets.

Despite the absence of data on the number of accounts in non-postal savings banks, they probably reach a very large number of “AFI-like” clients—i.e., clients not typically served by commercial banks. The only way to reach an order-of-magnitude “guesstimate” of this number is to indulge in some speculative assumptions without much empirical support. The assumptions indicated below feel conservative to the authors; readers are invited to substitute any assumptions that seem more plausible to them. The authors make no claim to having produced a reliable estimate.

First, it might be assumed that as much as 90 percent of savings bank assets correspond to their equity capital and large deposit accounts that are more typical of commercial banks than of AFIs. The remaining 10 percent of assets, corresponding to smaller accounts, would be about US \$90 billion. One might then assume an average account size of US \$600, which is near the top of the distribution of average account sizes found in the study. Based on these speculative—but probably conservative—assumptions, non-postal savings banks would add another 150 million accounts, bringing the total number of all AFI accounts to well above 750 million.

Remittances

Because of limited availability of data, the study did not include international remittances and in-country fund transfers. Such services are, however, very large in volume and very important for poor clients. Many poor families survive on remittances from family members working in other countries. In 2002, remittances to developing countries were estimated at US \$80 billion, which is double the amount of aid provided by rich countries.⁹ Actual inward remittances are probably

⁹ World Bank, *Global Development Finance 2003* (Washington, D.C.: World Bank, 2003), p. 198.

considerably higher because the above figure does not include funds transferred through couriers and other informal mechanisms. In-country transfer services are also important, especially for rural families supported by a member working in the city.

Institutional Characteristics: MFIs and the Other AFIs

Grouping the AFIs

Specialized microfinance institutions are the latest in a centuries-old series of alternative financial institutions that have been established by philanthropists, other social entrepreneurs, governments, and communities to serve households that do not have access to appropriate services from commercial banks and finance companies. The categories employed in this paper are neither exhaustive nor free from overlap and ambiguity, but they have proved useful in organizing the research reported here.

- **Specialized MFIs.** These MFIs are organized as non-governmental organizations or officially licensed non-bank financial institutions. Most of these institutions have grown out of the “micro-finance revolution” that began to gather momentum in the 1980s. They are usually credit-focused, using strikingly successful, new techniques for making and recovering tiny uncollateralized loans. Deposits are often limited to obligatory cash collateral for loans. Some MFIs have become licensed and supervised by governmental financial authorities, in order to provide voluntary deposit services to their target clienteles and to fund themselves either with deposits captured from the public or from commercial funding.
- **Commercial bank MFIs.** As a group, commercial banks do not share the social objectives that characterize most of the AFIs. Nevertheless, a number of specialized MFIs are organized as commercial banks. In addition, a number of commercial banks have created specialized microcredit programs or

departments in addition to their more conventional operations. These institutions and programs are included here because they aim at a clientele below the level normally served by commercial banks. The motivation for these programs usually, though not always, includes a significant social element.

- **Financial cooperatives (including credit unions).** This category embraces a wide range of member-owned savings and loan institutions. Because membership is usually based on some “common bond” (e.g., employment at a company or residence in a village), financial cooperatives tend to be relatively small. Healthy ones tend to focus more strongly on savings than on credit. Governance is usually based on a one-person, one-vote principle. Some municipally owned savings and loan organizations (e.g., Peru’s Cajas Municipales) have also been included in this category.
- **Low-capital rural and/or local banks.** Several countries offer a special license for small, locally owned, non-cooperative financial intermediaries (e.g., Philippine Rural Banks, Indonesian BPRs, Nigerian Community Banks, Ghanaian Rural Banks, and Chinese Rural Credit Cooperatives). Some of these institutions are owned by individuals, others by a combination of local and regional governments. They may normally be licensed with a paid-in capital of a few ten thousands of dollars. Although some may grow substantially, these banks remain small-scale in comparison with other regulated financial intermediaries in a given country. With the exception of their governance structure, which is normally concentrated in a few owners, they look somewhat like credit unions in scale and scope of services.
- **State development and agricultural banks.** In order to reach sectors that commercial banks do not serve, many governments have established state-owned banks to promote agriculture or other perceived development priorities. These banks are

often large. Many focus more on credit than on savings, making them particularly susceptible to political interference. Governments have often been willing to subsidize continuing losses in these institutions, a policy that tends to weaken management discipline. Getting information on these institutions was particularly challenging, so a significant number are not represented in the database for this analysis.

- **Postal savings banks.** Delivering mail requires a wide network of post offices that includes rural areas, and a functioning system for moving documents and information among the offices. In some post offices, staff time is not fully occupied by handling mail. Many countries take advantage of their postal infrastructure to provide financial services. Postal banks usually do not make loans: their services are limited to savings and payments/transfers. Account and transaction sizes tend to be quite small.
- **Non-postal savings banks.** This category includes both private and public institutions. The latter are often very large. As the name suggests, they are heavily savings-focused. Some have loan portfolios, but most of their loan assets are in large investment loans rather than small retail loans. Because global data on the number of accounts in savings banks was too difficult to obtain, this category has been discussed separately from the rest of the AFIs.

What Do AFIs Have in Common?

All of these institutional types (including MFIs) were originally established with an express objective of reaching a clientele that was not adequately served by commercial banks and finance companies. The vast majority of AFIs have a “double bottom line”: in addition to their financial objective, they also have some kind of social or public-purpose objective. Thus, they are not profit-maximizers. Speaking in broad averages, their clients tend to have lower incomes and

assets than clients who have access to commercial banks. Average account and transaction sizes tend to be smaller in AFIs than in commercial banks. All types of AFIs probably reach substantial numbers of poor clients, but the proportion of such clients can seldom be determined from available information.

When AFIs are licensed to take deposits, they are usually not supervised by the same unit that supervises commercial banks. Typically they are supervised by a separate non-bank unit in the government agency that supervises banks, or by a separate agency altogether. Regulators and supervisors often think of AFIs as lying outside of the country’s financial mainstream. Actual supervision of AFIs is often not only less rigorous but also qualitatively inferior to the supervision applied to commercial banks.

How Different Are MFIs from the Other AFIs?

The most important distinction is that the mission of MFIs usually includes a strong focus on the poor, or the poor and the near-poor, not just lower-income clients or the unbanked. While most MFIs do not provide data on the poverty level of their clients, it is likely that these clients as a group are poorer on the average, probably considerably poorer, than the clients of other AFIs (although there may be regional exceptions).

The Microcredit Summit maintains the largest database of MFIs. Its data on the outreach of these institutions is mainly self-reported, and the degree of independent confirmation is somewhat unclear. According to the Summit, as of year-end 2002, over 60 percent of MFI borrowers were “very poor” when they began receiving loans from the MFI. “Very poor” includes people in the lower half of those living below their country’s poverty line, or with individual incomes below US \$1 per day.¹⁰

¹⁰ Sam Daley-Harris, *State of the Microcredit Summit Campaign Report 2003* (City: Publisher, 2003), p. 3, 16-17. [http://www.microcreditsummit.org/pubs/reports/socr/2003/SOCR03-E \[txt\].pdf](http://www.microcreditsummit.org/pubs/reports/socr/2003/SOCR03-E [txt].pdf).

Unlike some of the other AFIs, most MFIs began with a heavy focus on credit. This is not surprising because the proliferation and outreach of MFIs was driven by the development of new technologies that proved strikingly successful in making and collecting very small loans to borrowers who could provide no conventional collateral.¹¹ Their core insight was that a good loan facility is so valuable to poor clients that those clients would repay their loans faithfully, even though no collateral had been pledged, in order to keep their access to the loan facility (as long as the MFI was disciplined in conditioning new loans on good repayment of earlier loans).

The MFIs surprised the world, not only by showing that the poor would repay tiny loans, but also by proving that such lending, when done right, could be made into a profitable business that covered all its costs and achieved massive outreach without the need of continuing infusions of undependable government or donor subsidies. While most MFIs are not financially sustainable, those that are tend to become much larger, with the result that profitable MFIs now account for a substantial and growing percentage of all MFI clients worldwide.

Because of their initial focus on lending, as well as legal constraints, MFIs as a group have been much better to date at providing credit than providing good voluntary deposit services. However, the MFI “industry” is increasingly aware of client needs for services other than credit, including savings, insurance, and fund transfer facilities. Certain other AFIs have more experience and outreach in these areas than do MFIs. This suggests an opportunity for MFIs, who may be able to tap other AFIs as sources of business knowledge or potential partners.

Unlike some of the other AFIs that make loans, most MFIs originally saw their mission as (very) small business lending: they wanted to finance tiny micro-enterprises that would lift their clients out of poverty, or at least shield them from some of the vulnerability associated with poverty. More recently, it has been

recognized that even when loans are explicitly made for business purposes, many—and in some cases, most—clients actually use the liquidity generated by such loans for non-business purposes in the household economy. This is probably as it should be, on the highly plausible assumption that borrowers are usually better than a lending institution at determining which uses of funds will most increase their household welfare.

AFIs and the Goals of Microfinance

In CGAP’s view, the challenge of microfinance is to build a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high-quality financial services. This vision involves four dimensions:

- **Breadth of outreach:** Providing access to as many people as possible
- **Depth of outreach:** Reaching as far down the income scale as practical
- **Service quality:** Offering a suitable variety of financial products (savings, loans, remittances, and insurance) that are well-matched with the real needs of clients
- **Financial sustainability:** Pricing financial services so that their costs are covered and they do not disappear when donors or governments are no longer willing or able to subsidize them

How Well Do AFIs Meet These Goals?

Breadth of Outreach (Market Coverage)

If AFIs supply over 750 million accounts worldwide, how well do they cover the market of potential clients—that is, customers below the level normally served by commercial banks and finance companies? It has not been possible, at least within the bounds of the present

¹¹ Characterizing MFI lending techniques as “new” does not imply that these techniques are without precedent.

Figure 11 Estimating AFI market coverage

Demand	
1. World population	6 billion
2. Minus rich countries and commercial bank clients in other countries	(1 billion)
3. Minus people below or above working age	(2 billion)
4. Equals AFI target market	3 billion
Supply	
5. Combined savings/loan accounts in AFIs including savings banks (from table 2), plus estimate for non-postal savings banks	750 million
6. Minus inactive savings accounts	(100 million)
7. Equals active savings and loan accounts	650 million
8. Minus allowance for multiple accounts per client [one-fifth of line 7]	(130 million)
9. Equals active AFI clients	~ 500 million
Market Coverage	
10. Active clients as % of target market [line 9 / line 4]	17%
11. Individuals with access as % of target market [line 10 x 2]	~ 33%

research exercise, to form any reliable estimate of global demand for AFI services. Correspondingly, no reliable estimate can be produced for the percentage of that market presently served by AFIs.

A rough order-of-magnitude guess about market coverage can be constructed only by indulging in highly speculative assumptions with little empirical support. Figure 11 contains a calculation based on one set of assumptions, every single one of which raises questions that the authors are unable to answer at present. Readers are encouraged to substitute any other assumptions that they find more plausible.

On the demand side, one might start with a world population of about 6 billion and then deduct an estimated 1 billion people who live in rich countries or who are commercial bank clients in other countries. The remaining 5 billion might be further reduced by an estimated 2 billion people who are younger than 15 or too old to work,¹² leaving an AFI market of perhaps 3 billion working-age people—individuals who are not served by the commercial banking system.

On the supply side, one might begin with the extreme assumption that the more than 750 million existing AFI accounts are all held by clients who do not have access to commercial banks.¹³ Of 700 million savings accounts

(550 million from table 2, plus an estimated 150 million savings bank accounts), it is assumed that one-seventh, or 100 million, are inactive. Deducting these 100 million inactive accounts from the 750 million total accounts (table 3, plus 150 million accounts in savings banks), one is left with 650 million active accounts. Finally, if it is assumed that one-fifth of this number reflects multiple savings accounts held in one institution by a single client, or accounts held by a single client in multiple institutions, then what remains is an estimate of about 500 million active clients at any point in time, compared to a target market of 3 billion potential clients.

On these assumptions, AFIs would be actively serving only about one of every six potential clients. But active usage is not the same thing as access: financial services are available to many people who may not choose to use them at a particular point in time. If one assumes that active AFI clients represent only half of the people who have access to AFI services if and when they want them,

¹² People above or below working age sometimes have loans or, especially, savings accounts. However, it was assumed that they use these services considerably less than the working-age population.

¹³ Note that the estimate of savings bank clients in the previous section tried to exclude large account holders.

then the estimate rises to 1 billion people with access to AFI services, or one-third of the target market.

These admittedly speculative assumptions would suggest that AFIs may still fail to reach two-thirds of the unbanked population they were created to serve. Some people included in this demand estimate are too destitute to use financial services. Others live in areas so remote or thinly populated that it is not practical to provide formal financial services. But even making allowances for such people and, more generally, for the high margin of error in the assumptions behind this estimate, it is clear that the battle to bring financial access to as many people as possible is a very long way from being won.

Depth of Outreach: Getting to the Poor

The highly speculative estimate developed in the previous section is that two-thirds of the unbanked population have no access to formal financial services. One would expect that the unserved proportion of the poor and near-poor to be considerably higher. MFIs as a group tend to focus very specifically on poor and near-poor clients, but most AFIs in the other categories do not, even though their average account sizes suggest that they serve many such clients.

Uncollateralized loans and fully liquid deposits are two financial products that are particularly important to poor people. Most of the state-owned AFIs, which account for a heavy majority of the infrastructure and service delivery, either do no uncollateralized lending at all or do it badly. Public AFIs tend to do a better job with savings mobilization, but many of them do not offer savings products that are sufficiently liquid and convenient to match the needs of poor people, who want immediate access to their money to deal with the unpredictable ups and downs of their vulnerable existence.

Service Quality

The CGAP study casts no new light on this issue. However, anecdotal experience strongly suggests that

service in many AFIs—especially state-owned ones—can be inferior. Common problems include high transaction costs for customers (including, especially, the time required to access services); unnecessarily rigid, one-size-fits-all savings and loan products; inaccessible and unreliable account information; and disrespectful personal treatment. In addition, there are issues with the range of products available: for instance, AFIs fall short of what they could be doing in terms of remittances and insurance.

Financial Sustainability

Many AFIs do not generate enough revenue from clients to cover the costs of delivering their financial services. Some people consider this acceptable because of the social mission of these institutions. This point of view might be less problematic if one assumed that there are enough subsidies available from governments and donors to provide financial access to all poor and near-poor households, and that long-term continuance of these subsidies is assured. But these assumptions do not match very well with the real world.

Obviously, institutions that do not cover their costs will decapitalize themselves and disappear unless governments or donors continue to pump in subsidies. But even where such subsidies are available, they are almost never large enough to meet more than a fraction of demand, so service has to be rationed (for instance, by political allocation or imposition of high transaction costs on customers). There is no reason to expect government and donor subsidies for poor people's finance to increase dramatically in the future—if anything, the trend seems to be downward.

By contrast, financial institutions that do cover their costs, including the projected cost of commercial funding, can continue their services and expand them, by attracting unsubsidized funding on market terms. For practical purposes, market funding is unlimited. There is a huge gap between the present supply of poor people's finance and the demand for it. This gap will

never be filled by financial intermediaries that consistently lose money, as many of the AFIs do.

One of the biggest challenges to financial sustainability lies in the fact that most government-owned AFIs, and some private institutions as well, do not know how to make and collect small, uncollateralized loans well enough to avoid unsustainable levels of default. In more than a few cases, the problem goes beyond simple ignorance of proper lending techniques: blanket forgiveness of loans made by government AFIs is sometimes used for political purposes.

More generally, politics can distort many dimensions of operation in a state-owned AFI, including selection of managers, location of branches, and labor relations.

Strategic Implications for Microfinance

The information collected in this study suggests that AFIs deserve more attention than they receive, both from microfinance proponents and from central banks and finance ministries.

During the first two decades of the modern microfinance movement, people working in this area have tended to focus heavily on new credit techniques and the private “microfinance institutions”—mainly NGOs—that led to the development of these techniques. Now there is a growing tendency to broaden the focus to other financial services—especially savings—and to other institutions. In particular, government-owned institutions provide three-quarters of total AFI accounts, and two-thirds of AFI loan accounts. Even if the focus is limited to poor and near-poor clients or, even more narrowly, to loans to such clients, institutions other than MFIs may be providing the most of services.

As a general rule, government financial authorities do not think of AFIs as part of the mainstream financial system, and thus may treat them with a kind of “benign neglect.” In particular, AFIs are often left with inferior supervision. This attitude is understandable, given that

AFIs (aside from savings banks) account for such a tiny percentage of financial system assets. But asset size is not the only way to measure a financial system. If one counts people instead of money, then AFIs loom large: they probably account for a significant share—sometimes the majority—of financial system customers in many of the countries included in this study. From this perspective, **AFIs ought to be front and center in financial sector reform and modernization programs.**

For most countries in the survey, the research team was unable to locate information on numbers of accounts in commercial banks or the banking system as a whole. As a result, no worldwide comparison of AFI account numbers with commercial bank account numbers was possible. However, the examples shown in figure 12 illustrate how important AFIs can be, even when one excludes savings banks from the comparison due to the lack of account information.

The outreach information reported in this paper for MFIs is not particularly surprising: much of it comes from the database of the Microcredit Summit, summaries of which are published annually. Rather more surprising (to the authors, at least) was how wide a net the other AFIs cast.

MFIs, which focus more aggressively on poor clients than do most other AFIs, deserve continued promotion and support. At present, however, the other AFIs have most of the outreach, as well as most of the infrastructure. (Even though many of their clients are not poor, these AFIs are more likely than commercial banks to have branches in areas where poor people live.) In view of this situation, **donors, governments, and other stakeholders interested in fostering financial services for poor and near-poor clients should be looking closely at the opportunities and challenges presented by all AFIs.**

Many of the limitations of AFIs are also opportunities: there is room for major improvements in terms of financial sustainability, attention to poor clients, and product quality (especially loan collection).

Figure 12 AFI Accounts vs. Banking Accounts

Country	AFI accounts	Bank accounts (non-AFI)	AFI accounts as percent of total accounts
Bolivia	686,716	601,565	53%
Burkina Faso	1,099,883	328,994	77%
Colombia	1,769,425	29,065,495	6%
Côte d'Ivoire	1,243,917	659,642	65%
Nicaragua	248,725	495,526	33%
Niger	1,527,363	29,057	98%
Poland	713,812	8,951,100	7%

Sources: Bolivian, Nicaraguan, and Colombian bank superintendencies; Banque Centrale des États de l'Afrique de l'Ouest; Microfinance Centre (Warsaw).

There are also important possibilities for cross-fertilization among AFIs. MFIs have developed a very successful delivery model for uncollateralized loans to poor borrowers. Grafting this model onto the infrastructure of the other AFIs could produce a great expansion of loan services. On the other hand, most MFIs are newcomers when it comes to deposit services, and may benefit by learning from—and partnering with—competent savings-based AFIs.

Reform of state-owned institutions will raise governance problems. State-owned financial retailers are notoriously difficult to reform, especially in the area of sound lending practices, because their masters and managers face political and other incentives that do not always push in the direction of quality financial services for poor people. But many state banks already provide quite respectable savings services, so many of the others should be able to improve their savings performance.

With respect to lending, the picture is more challenging. Very few state-owned AFIs do lending well at present, despite many attempts at reform. One can find occasional cases where state-owned AFIs have been able to develop sound lending practices in a large branch network, with spectacular results. But such cases are rare; it is realistic to recognize that only a small minority of state-owned AFIs have the conditions necessary for the introduction of good microlending.

The predicament is that on the one hand, state-owned institutions seem to present a great

opportunity—they account for a large majority of the clients and infrastructure—while on the other hand these institutions will rarely do a good job of microlending. Recognition of this pattern might suggest that governments and donors ought to focus more seriously on improving savings services at state-owned AFIs, especially savings services tailored for the particular needs of poorer clients. In some state-owned intermediaries, there is plenty of room for improvement in these services. Upgrading deposit service is usually feasible because it tends not to conflict with political incentives. And we know that poor clients, including the very poor, value good formal savings opportunities very highly.

State banks that are being privatized may present interesting possibilities. Buyers would often prefer to close down unprofitable rural branches, while governments are anxious to see financial services maintained in these areas. The introduction of good microlending in such branches could drastically reduce loan losses and increase branch income without requiring much increase in payroll and administrative costs, all of which could substantially improve branch profitability.

One issue with credit unions and other customer-owned financial cooperatives is that their common-bond structure tends to result in the proliferation of relatively small institutions. Although federations and

government regulators exercise some supervision over credit unions, it remains generally true that reform of weak credit unions happens one institution at a time, and thus depends on decisions of many sets of directors and management. Branches subject to central control may be easier to change than a series of autonomous institutions. But this obstacle should not be overstated. One can find some very successful initiatives to strengthen credit unions, probably

more so today than in the past. In particular, increasing numbers of credit unions are adopting microlending techniques to reach poorer clients.

The core conclusion that emerges from this survey is that **making finance work for the poor will involve a wide range of institutional types delivering a variety of financial services**. Contributing to this process calls for a broad perspective and creative approaches.



Annex: Methodology and Data Limitations

Reliable information on numbers of borrowers and savers in AFIs is hard to find. Many of these institutions do not report to any central authority, so the authors have collected information from hundreds of sources. Much of the information came from databases maintained by institutions such as the World Bank, United States Agency for International Development, World Council of Credit Unions, Microcredit Summit, and other networks. This information was updated and supplemented with data provided directly by many individual institutions, especially where the researchers knew of large institutions that were not included in existing databases.

Data is reported for the most recent year available. In some cases the information is as old as 1997, but most of the data is from 2000 or later.

The reliability and completeness of the information reported in this paper is subject to a range of limitations. To begin with, the mapping was not exhaustive. No doubt many institutions escaped the net. The survey was concluded at a point where the additional information being collected did not seem to be affecting the overall shape of the mapping.

More efforts were made to get numbers from larger countries than from smaller countries, and from larger systems of institutions than from smaller ones. The survey has certainly missed thousands of very small NGOs that do not report to any central network. However, while there are many of these small institutions, their numbers probably do not alter the general picture very much.

As in many other areas of economic activity, it seems that a relatively small number of large institutions account for most of the activity. In the CGAP data set of over 3,000 AFIs, two-thirds of the accounts were concentrated in the top five organizations, and four-fifths of the accounts in the top eleven. In Latin America, where the inventory was most thorough because it was built on an earlier stock-taking exercise, it was estimated that the small NGOs left out of the study accounted for 75–80 percent of all institutions, but only about 25 percent of all actual clients. An inventory of MFIs in Bangladesh included data for over 573 MFIs, but the largest 20 of these institutions accounted for 80 percent of all clients.¹⁴

¹⁴ Includes clients of Grameen Bank (December 2002) and 572 NGOs (June 2000), all of which are reported in *CDF Statistics*, vol. 11 (November 2000), Credit and Development Forum.

Data collection for this study ended in September 2003. The information used was the most recent available for each institution. For 78 percent of the institutions, the data cited is from 2000 or later.

The study was conducted as a one-time inventory. CGAP has made no decision about future updates or iterations.

Most AFIs were set up to reach clients who were generally below the level of clients being reached by commercial banks at the time. However, there is obviously a certain amount of overlap between AFI and commercial bank clienteles. In particular, some commercial banks have responded to financial liberalization by reaching further down into small-transaction retail finance. However, commercial bank clients were included in this study only where they have specialized in microfinance (using the narrow definition of “microfinance” employed elsewhere in this paper) or report separately on their microcredit clients.

Generally, numbers of *accounts*, rather than numbers of *clients*, are reported in this paper.¹⁵ Many institutions could not provide client numbers. **The distinction between accounts and clients is an important one. The number of clients is less than the number of accounts, to the extent that clients have multiple accounts.** A client may have both a savings account and a loan with the same institution, or multiple deposit

accounts, or occasionally more than one loan at a time. Finally, some clients have accounts in more than one institution.

Savings accounts outnumber loan accounts by more than four to one. The existence of a savings account on an institution’s books does not necessarily mean that a client is actively using the institution’s services at the time of measurement. Most savings institutions have a significant proportion of inactive accounts whose small balance may reflect nothing more than a minimum requirement for membership or a desire to keep the account open for possible use in the indefinite future.

Very little information was available on the socioeconomic level of clients of various institutions.

Finally, the information collected in this study consisted of indicators of outreach (usually numbers of accounts) and of portfolio or asset size. Observations about the nature and limitations of the various kinds of AFIs are based not on the research exercise, but on the experience of the authors and their colleagues.

A list of countries and institutions in the database is included with this paper on the CGAP web site: www.cgap.org

¹⁵ The most specialized MFIs reported numbers of clients, whereas credit unions generally reported numbers of members.

Notes

Occasional Paper No. 8

The authors of this Occasional Paper are Robert Peck Christen, Senior Advisor, Richard Rosenberg, Senior Advisor, and Veena Jayadeva, Research Assistant, all of CGAP.

Gautam Ivatury and Rani Deshpande made major contributions to this paper.

Marguerite Robinson, Frank DeGiovanni, Brigit Helms, Elizabeth Littlefield, and Ousa Sananikone provided useful suggestions.

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