



**BREAKING TRADITIONAL STRUCTURES:  
CAPITAL MARKETS AND MICROFINANCE IN LATIN AMERICA**

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*The selected panel, “The Opportunities of Microfinance in Latin America,” moderated by Jonathan Mordoch, associate professor of public policy and economics at New York University Wagner School of Public Service and author of the book The Economics of Microfinance, began with a review of the history of microfinance institutions and developments in the last several decades. The discussion then led to the ways in which microfinance institutions can serve entrepreneurs and how the role of microfinance has changed at global multinational banks like Citigroup. The panelists were*

- Kurt Koenigsfest, Sr., CEO and General Manager of BancoSol S.A.
- Bob Annibale, Global Director of Microfinance at Citigroup

Microfinance institutions originally sprouted up in developing countries as small banks with the mission of serving those untouched by the traditional capital markets as much as the bottom line. Over time, the sophistication of microfinance institutions has changed dramatically. Taking the Bolivian microfinance institution BancoSol as a prime example, we find that microfinance has stepped out of the shadow of the world’s capital markets and has now become a player within them. Furthermore, in looking at the activities of large, traditional global banks like Citigroup, we see that microfinance institutions serve a key role—that of a partner institution—in some of the world’s developing countries. This role extends not only Citigroup’s global reach but also that of their underserved clients.

**Pushing the Poverty and Commercial Frontiers**

Jonathan Mordoch began the panel with a simple introduction of what microfinance is and where it has come from. “The origins of microfinance rest as justifiably in Latin America as they do in Bangladesh. What we learn from microfinance in Latin America are the frontiers

of this area—what we have learned, what we need to learn and the questions going forward. What we've learned is that this can be about more than alleviating poverty. It can be about pushing the frontier in terms of how technology can be used to make small business better." He elaborated that the area in which microfinance institutions are still pushing the frontiers of banking and fighting poverty is in the creation of integrated models of microfinance. "The integrated model of microfinance is not the right model for every program. They're more managerially complicated and can sink a credit institution. However, we're beginning to see how they impact several layers in society and institutions." But it was within these integrated models that Mordoch noted the future of microfinance lies. "It's within these institutions that there's some interesting work being done to push the poverty frontier, as well as the commercial frontier."

Kurt Koenigsfest described how the social and the profit mission were the dual focus of his microfinance institution in Bolivia, BancoSol. "What we are trying to do is have a business with both high economic and social returns. And what we are asking in our firm is, 'Is that possible?'" After years working to serve the financial and banking needs of the poorest level of the population in Bolivia, BancoSol and Koenigsfest have in many ways answered their own question with a resounding "Yes." As evidence of that success, Koenigsfest could point to market recognition. "BancoSol was named one of the top two banks in Bolivia last year. So, we're doing our business part as well as our social part."

Bob Annibale described Citigroup's mission in the microfinance sector as having a two-pronged approach. "I think that we have a double bottom line—that we believe in doing this and that this is the right thing to do." He admitted that large banks like Citigroup had largely stayed out of the microfinance sector until recently because it was not perceived as a profitable business segment for them; however, he also stressed that now large institutions are entering the sector because it can be both profitable and "the right thing to do." He summed up Citigroup's entry into the microfinance sector for both missions: "I've spent a lot of time looking at why large banks didn't enter into markets like Bangladesh and Bolivia, where microfinance has really taken off and been a source of innovation. I've also spent time looking at other countries, like Brazil and Mexico, in which traditional banks are quite strong and microfinance did not take off. My role was to find or figure out how we at Citi work with microfinance institutions to help them achieve scale—to allow them to provide services to poor people."

### **Microfinance Reaching the Capital Markets**

The origins of microfinance are ironic, given where these institutions are moving toward today. "Microfinance started simply as very small loans to entrepreneurs who had been

squeezed out of the very large, formal capital markets,” commented Mordoch, as he explained the history of the institutions. Yet, as microfinance has evolved—as their institutions have grown in their size, services, and complexity, and as their clients’ businesses have grown from small, single entities to more robust enterprises—microfinance institutions have begun to interact with the larger capital markets and more traditional banking structures that they previously had needed to supplement for the poorest segment of the economy. “BancoSol has even seen an IPO as of last year in New York City, and this was the first time that microfinance reached the world’s capital markets,” boasted Koenigsfest.

But with the new foray into the world’s capital markets come new requirements for microfinance institutions. Koenigsfest commented on one new requirement that BancoSol has tackled effectively. “Of course, if you want to reach the capital markets, you have to have ratings—and we have them, and they’re not too bad.” He then outlined the ratings system that BancoSol had created and how it has helped his clients reach the capital markets and helped BancoSol better structure how it evaluates new clients.

#### **Microfinance Attracting New Clients and Institutions**

But in many ways, Koenigsfest believes that BancoSol—and microfinance institutions in general—reaches its social mission by just focusing on a different segment within the population. “We believe that the bottom of the pyramid is a legitimate business segment. But targeting this sector does not mean that we’re not going to give them a high-quality, complete line of products. We have everything that you might find in a commercial bank—the difference is the market that we’re reaching.”

Large, traditional banks often did not serve this part of the population, because the banks did not have the capabilities, product lines and services to do so effectively and efficiently. Annibale elaborated on this point with regard to remittances programs for immigrants that traditional banks hadn’t been able to effectively manage. “The thing about remittances is that the traditional banks haven’t done a good job of providing the right set of products and services for how immigrants want to bank. We’ve finally brought the cost down from 40 dollars a transfer to 5 dollars a transfer. But we hadn’t done that for quite some time.”

For BancoSol, first-mover advantages had provided superior returns. “We have lines out of our doors because we were the first to give loans to people who would have otherwise had to get money from loan sharks or their families.”

By focusing on an underserved segment, microfinance institutions not only helped an underserved part of the population but also avoided any competition from traditional banks. This aspect of the market is now changing, and for good reason. Koenigsfest summed up the current competitive landscape: “Some of the ROEs of our initial successes were around 76 percent, and last year they were close to 100 percent. However, our returns have attracted competition.” In Bolivia, this competition has come from a state-run bank now offering similar products and services to the poorest in the economy. But other entrants—partners for microfinance institutions—have also entered the market.

Annibale commented on why Citigroup is now partnering with microfinance institutions, “Not all clients of microfinance are entrepreneurs. They’re also cooperatives. They’re also postal savings banks. That’s very important to us because it’s very unlikely that we’ll be able to replicate our traditional institutional structures in other countries. We need to leverage the institutions that are already there. And what we’ve always really wanted was for someone else to partner with to ‘bank’ the family on the other side. With microfinance partner institutions, we’re finally getting that.” In many ways, these new partnerships are an appropriate step in the evolution of microfinance institutions, as they augment the financial institutions and leverage available to the “bottom of the pyramid.” Annibale described the new entrants into the market as helping to further the social mission of microfinance. “Ultimately, the diversification of who’s reaching and who’s banking the underserved is going to serve them.”

### **The Challenges Ahead**

But even with all the successes that today’s microfinance institutions can boast—IPOs, ATMs, lower rates for lenders, credit rating systems—there are still many key challenges ahead for the microfinance sector. Koenigsfest outlined several of these challenges:

- Continuing to fight against poverty in a country and economy where it is still widespread
- Advancing in rural areas where poverty rates remain quite high
- Hedging against political risk
- Continuing to reduce costs of a microfinance operation in order to then reduce rates charged to borrowers
- Introducing new products and services, like healthcare, that the bank’s segment needs
- Generating more entrepreneurs to serve and grow in the country

When reflecting further on the many daily challenges he faces, Koenigsfest focused on borrowing rates for lenders as being top of mind. “A lot of people talk about the interest

rates. Twenty years ago, rates were at 70 percent, whereas the rates today are around 21 percent. We're still in the process of reducing rates for borrowers." But he stressed that with time, experience and scale even those rates would decline and a larger set of borrowers could be served. And, in many ways, traditional banks like Citigroup may play the most important role in tackling the challenges that lie ahead. Annibale remarked, "Today, microfinance clients and institutions are truly paying for the services they get. And there's room for a large financial institution to provide them with services that will allow them to achieve scale." With the help of larger, traditional financial institutions, microfinance institutions will continue to evolve, in both their social mission and their profit mission.

Mordoch concluded, thinking optimistically about the sector, "Not only have microfinance institutions rethought the banking model once, but in the past couple of years they've rethought the model again in response to the new challenges in the microfinance market." While the future will likely bring great challenges, the flexibility and drive of microfinance institutions is likely to meet those challenges.

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